

REMARKS OF
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Recently I read the papers and talks presented at the Seaview Symposium covering the topic "Corporate Financial Reporting: Conflicts and Challenges." One of the contributors at the Symposium predicted the Commission would usurp the authority of the Accounting Principles Board. It seems the profession has lived with this fear since 1936. The genesis of that fear is described in Jack Carey's recent book published by the Institute. Jack, in the section entitled "Honeymoon Ends," commented that after the Commission was established, several conciliatory speeches were made to the profession, until December 4, 1936, when in a speech made to the Investment Bankers Association, Chairman Landis said:

The impact of almost daily tilts with accountants, some of them called leaders in their profession, often leaves little doubt that their loyalties to management are stronger than their sense of responsibility to the investor.

How well has the relationship fared since that indictment was expressed? Jack continues by saying the relationship between the profession and the Commission has ranged from praise to criticism. Sometimes seemingly unduly harsh; and, sometimes mingled with the thinly veiled threat the Commission might exercise its latent powers to prescribe accounting principles and methods.

The relationship was further discussed at the annual meeting of the American Institute of Certified Public Accountants in 1966, in a speech in which Chairman Cohen stated:

... Congress gave us the final responsibility for insuring that adequate standards of disclosure are maintained and it is a responsibility that we take very seriously. However, we prefer -- and I anticipate that the Commission will always prefer -- to accomplish these objectives through cooperation as long as we are persuaded that it is an effective and expeditious way to achieve them.

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The relationship between the SEC and the profession, Jack Carey concluded,

... prodded the profession to make improvements both in accounting and auditing that otherwise might have taken longer to achieve.

Personally, I see little possibility the relationship between the profession and the Commission will change materially; and while the "honeymoon" has ended, I trust the two groups can maintain some marital bliss. Like other groups which have their own personality and which must work continually in close proximity, some friction will develop; but, the beneficial results so far have made the relationship one to be envied by other professionals.

Mr. Landis's speech also raised the issue of independence. The term has reached its present definition in an evolutionary process like many of the other concepts in accounting. No one here needs to be reminded under existing Commission regulations an accountant is not considered to be independent if he has any direct financial interest or any material indirect financial interest in his client.

The members of the profession have no problem with this aspect of independence; but, independence has a broader meaning and imposes a positive duty upon the accountant about which Maurice Stans, now Secretary of Commerce, had this to say:

With the addition of the qualifying adjective "public," to define an area of service and also a profession, there are added to accounting two connotations -- one of service to a general clientele, the other of responsibility to the public interest. It is the second of these that is least understood.

I believe the obligation imposed upon the accountant within this meaning of independence is that he should use accounting to convey to the public the clearest picture of the financial condition and results of a business.

The real test of the accountant's independence often comes when he must make a decision with respect to an accounting treatment of a matter not covered by a specific APB Opinion. Too many times the accountant rationalizes or justifies his decision by pointing to the fact that his problem has not been specifically dealt with in accounting literature. This is the most specious form of reasoning.

I believe that too many times when confronted with close questions some accountants ignore one of the fundamentals of accounting -- namely that substance shall triumph over form. This means that despite complicated legal instruments and whatever other documentation presented by a client, the accountant is charged, in the first instance, with the responsibility of seeing to it that the business impact of the transaction in question is reported rather than a literal reflection of a legal document.

Furthermore, structuring a "business deal" in an attempt to exploit unsettled accounting principles is unfair to everyone and at times can come perilously close to commercial fraud. Management, as well as accountants, has a responsibility to see to it that the real significance of financial transactions is set forth properly in financial statements.

Truly independent accountants are well aware of their responsibilities in this area. As a matter of fact, the vast majority discharge those responsibilities in keeping with their code of professional ethics. Nevertheless, too often the valuable time of the Commission and its staff is consumed in discussions with issuers and their professional advisers who are not motivated towards full and fair disclosure but more towards the reporting of improved earnings.

This practice is of real concern to the professional staff of the Commission. I urge the business community and its professional advisers to have this matter foremost in their minds.

In conclusion, I must confess the Securities and Exchange Commission has often been characterized in unflattering terms; but, on balance, I believe our reputation is best described by a recent writer who said:

The Securities and Exchange Commission is known as a considerate agency of government, the guardian angel of widows and orphans and the polite policeman of those in the securities business. It is happily endowed with a competent staff which has traditionally displayed a benign understanding of the difficulties of compliance with all the niceties of federal securities regulation.

In all fairness, I must also tell you the writer then went on for three pages to expose our weaknesses.

Sadly, no government agency can expect to be loved by all of the people, all of the time -- particularly an agency such as ours, which has such broad responsibilities. However, it is much more important that people, such as yourselves, understand the reason for our being and something of the problems we face.

I hope my remarks have contributed toward that end.