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Ethics of Accountancy

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THE subject of ethics for the accountant is one which has engaged the attention of the members of that profession for quite a number of years. In fact, the subject was one of those presented before the Congress of Accountants, meeting at St. Louis in September, 1904. Prior to that time, however, definite rules of professional conduct had been formulated by the accounting societies of England for their members. In this connection it is interesting to note that in the latter part of 1905 a bill was introduced into Parliament by the Government of Tasmania for the regulation of the profession of accountancy in that colony. This bill made mention specifically of certain actions on the part of accountants which were to be regarded as unprofessional, and the practice of which should render them liable to fine, suspension or expulsion.

At the Convention of the American Association of Public Accountants, held at St. Paul, Minnesota, in October, 1907, Mr. J. E. Sterrett, C.P.A., presented a paper on "Professional Ethics" which is the standard treatise on that subject today. This paper was characterized at that time by Mr. Robert H. Montgomery, C.P.A., as one "which bids fair to become a classic," and this prophecy has indeed been amply fulfilled. Mr. Sterrett called attention to the fact that the older professions of law and medicine had even at that time (1907) made considerable progress in the development of systems of professional ethics, and called attention also to the work being accomplished along that line by the American Institute of Electrical

Engineers. In measuring the distinction between the accountant as a member of one of the newer professions, as contrasted with the lawyer or physician, Mr. Sterrett stated:

A lawyer's real opinion of another lawyer, or that of one physician concerning another, is usually a much more accurate judgment of the man's character and ability than is indicated by the reputation which he bears in the community at large. It may be that the opinion of the public and that of those who know the man from the inside, as it were, will coincide. This is likely to be the case with men of good ability and fine character, but the sham and the trickster are likely to be weighed and labeled by their professional brethren long before their real character is discovered by outsiders.

Under ordinary circumstances regard for the good name of his profession seals the lips of the professional man about matters concerning others in his own profession. The physician considers it quite unethical to pass harsh judgment upon his brother physician, except under the most urgent conditions. As accountants endeavoring to build up professional ideals, we should feel that the good name of our profession requires us to avoid all needless reference to the weaknesses or imperfections of other accountants.

While since that time there have been more or less serious infringements of the rules of ethics as laid down for the guidance of accountants, yet these have been dealt with fairly and impartially by committees on professional conduct of the American Association of Public Accountants and of its successor, the American Institute of Accountants. The work of these committees has always tended to-

wards the improvement and development of the profession, to the end that there shall be a recognition on the part of its practitioners as well as on the part of the general public, that all who are its members not only are those of high professional attainment, but those in whom the moral ideal exists in more than name only.

Mr. John Alexander Cooper, C.P.A., also presented, at this same convention, an excellent paper on the same subject, in which he divided his remarks under the following headings:

First—the elemental reasons that justify the claim that accountancy is a profession and all that the word implies.

Second—the aims and ultimate goal for those engaged in the practice of accountancy.

Third—a statement of a few classified and tersely expressed rules, that may form a proper basis for the guidance of accountants in practice.

In defining a profession, Mr. Cooper called attention to the dictionary definition of the term: "The calling or occupation which one professes to understand or follow; a vocation in which a professed knowledge of some department of science or learning is used by its practical application to the affairs of others, either in advising, guiding or teaching them, or in serving their interests or welfare in the practice of an art founded on it": or, to give the same thought more concisely, "Professed attainments in special knowledge, as distinguished from mere skill." He sees the services performed by the accountant as falling within the scope of the above definitions, and concludes that those who engage in this practice should "promulgate and maintain at all times, and that inflexibly, those rules of conduct which are known to all professional men of lofty instincts as the keystone that upholds the arch of public confidence." He further continues:

There is no profession, not excepting that of the ministry or of the law, in which it is more imperative that the practitioner be governed by the highest code of morality, than that of public accounting. Great as may be the influence which our profession can and does exercise upon business affairs, it is only by strict observance of ethical rules and right conduct that we can hope to pay the debt we all owe to such profession by uplifting and maintaining the highest standard, thereby bequeathing to our successors a calling placed upon a higher plane than when we first embraced it. It rests largely with this generation of the guild, who can, many of them, recall the inception of public auditing and accounting as it is now recognized, to lay the foundation of a noble profession that may justly be called the right hand of the law, or on the other hand, so bear themselves that this proud opportunity will be lost and our term of stewardship wasted.

The rules of conduct as he summarizes them are expressed as follows under the several headings indicated:

Service

1. To certify to statements, exhibits, schedules or other form of accountancy work, the auditing or preparation of which was not carried on entirely under the supervision of himself, a member of his firm, or one of the staff, is wrong.
2. The use of a practitioner's name in professional work by others than partners or employees is wrong in that it implies deception.
3. To perform accountancy work payment for which is by arrangement upon the contingency of the result of litigation or other form of adjustment is unprofessional.
4. The payment of a commission, brokerage or other form of inducement to the laity from professional fees is wrong.
5. The acceptance of any part of the fees of a lawyer or any commercial brokerage, bonus or commission as an

incident arising out of a practitioner's service is wrong.

6. Active interest in a commercial enterprise while practicing as a public accountant is to be avoided as incompatible with strict ethical principle.

7. The practitioner should, wherever possible, avoid acting as a trustee of special funds or pools as an incident of his calling.

8. A practitioner should avoid serving as a director in corporations in which he is professionally employed.

Clients

1. Upon engagement a practitioner is in duty bound to tell his client of all foreknowledge he may have had touching the matter under consideration.

2. Personal responsibility is a fundamental rule of the profession. A practitioner cannot screen himself from the specific acts or laches of his employes; the responsibilities are his and those of his firm.

3. Information acquired in the course of service is privileged and inviolable. Abuse thereof to the detriment of a former client renders a member subject to the severest discipline.

4. Efforts that tend to invite or encourage legal contest, or foster further employment by neglect, manipulation or unfinished service, should be severely dealt with; it is, in fact, barratry.

5. To recommend or advise clients to a measure or course of procedure that may even indirectly give the practitioner a personal advantage must be considered as flagrant professional infidelity and misconduct. It is "maintenance," and is punishable as such at common law.

Inter-Professional

1. Depreciation of opponents in contested matters is unprofessional and ethically wrong.

2. Acceptance of an appointment from which a colleague has withdrawn from conscientious motives, without previously making direct inquiry of such colleague as to the conditions, is professional discourtesy.

3. Canvassing the clients of a colleague for business is unprofessional.

4. To recognize or affiliate with a society that in its charter title assumes the words "Certified Public Accountant," without warrant of law as to its membership, is wrong, and gives countenance to an implied fraud.

Publicity

1. No professional accountant should advertise or display his talents as a merchant does his wares.

2. Professional cards should show in plain inconspicuous type the name, occupation, and office address. No strained effect is consistent or dignified.

3. The same form of card may be used in publications of a recognized standard, such as technical magazines, law periodicals, etc.

4. It is not good professional form to solicit business through trade journals, flashy publications, programs, or the daily press, especially under a pseudonym or publisher's index mark.

5. The use of the public press in discussions or essays on matters of technical or general interest is legitimate.

6. The use of initials or other insignia as an affix to a practitioner's name in his business advertisements other than such as is recognized by statutory enactment in the United States or is authoritatively recognized in other countries is unprofessional.

Corporations

1. No member should conceal his personality under a corporate name, either actual or fictitious.

2. The skill and knowledge of the

profession is individual, and cannot be transferred to a corporation, the accruing goodwill is otherwise lost.

3. Success in any professional career is a matter of personality.

4. A corporation *per se* cannot make an audit which in the full intent of the service is a judicial function.

5. A corporation is without honor, which is the keystone of the profession.

6. Directors cannot direct in a profession of which they are not members. It is a prostitution of the financial standing of the directors and stockholders, leading to unfair competition and prejudiced decisions.

7. The ultimate profit to the lay stockholder or director, whether expressed tangibly or otherwise, is an illegitimate gain or advantage which the profession cannot countenance.

8. In the case of legal liability as the result of negligence or criminal perversion of logical facts the ultimate responsibility rests with the practitioner, notwithstanding the financial support and control of outsiders.

9. Assurance of secrecy in affairs of clients of such corporations cannot be taken seriously.

10. The profession needs no control or regulation from the laity; it is not an industry.

The work of the Convention of 1907, in which the subject of professional ethics was crystallized, is set forth in Articles VII and VIII of the by-laws of the Association which were amended to read as follows:

ARTICLE VII

SUSPENSION AND EXPULSION

Section 1. A state or district society, or any member-at-large failing to pay the annual dues, or any subscription, assessment, or other sum owing by them to the association, within five months after such debt has become due

shall automatically cease to be a member of this association.

Sec. 2. A state or district society renders itself liable to be expelled from the association or to be suspended for a term not exceeding two years by resolution of the board of trustees sitting as a trial board, if, after election to membership, it (a) lowers its standards of admission to membership; (b) fails to maintain its organization; or (c) refuses or neglects to give effect to any decision of this association, of the board of trustees or of the committee on arbitration.

Sec. 3. A member renders himself liable to be expelled from the association or to be suspended for a term not exceeding two years by resolution of the board of trustees sitting as a trial board, if (a) he infringes any part of the rules of conduct of the association; (b) is convicted of felony or misdemeanor; (c) is finally declared by a court of competent jurisdiction to have committed any fraud, (d) is held by the board of trustees on the written complaint of any person aggrieved, whether a member or not, to have been guilty of any act or default discreditable to the profession, or (e) is declared by any competent court or commission to be insane or otherwise incompetent.

ARTICLE VIII

TRIAL BOARD

Section 1. For the purpose of adjudicating complaints or charges against members of the association as provided in Article VII the board of trustees shall convene as a trial board.

Sec. 2. Due notice shall be mailed to the parties to the cause by the secretary at least thirty days prior to the proposed session.

Sec. 3. A three-fourths vote of those trustees present shall be necessary to a decision.

Sec. 4. The Board of Trustees (sitting as a trial board) may in the exercise of its discretion recall, rescind, or modify any resolution for expulsion or suspension at a meeting similarly called and convened by a like majority vote as required in Section 3 of this article, provided that not less than three-fourths of the members constituting such board shall have been of the board that issued the decree then being reconsidered

Sec. 5. Written notice of any resolution for expulsion or suspension shall forthwith be sent to the member affected thereby and to the secretary or secretaries of the state or district society or societies with which such member is affiliated or in which state he has his domicile or place of business.

These articles continued until the year 1916 substantially without change with the addition only of Section 6, which reads:

Sec. 6. No member shall take part in any effort to secure the enactment, alteration or amendment of any state or federal law affecting the profession without giving immediate notice thereof to the secretary of this association, who in turn shall at once advise the secretary of the state or district society concerned.

THE PRESENT CODE OF ETHICS FOR ACCOUNTANTS

In 1916 the American Association of Public Accountants was reorganized under the present title of the American Institute of Accountants. The Institute while not incorporating a code of ethics or rules of conduct in its constitution and by-laws, nevertheless formally adopted a set of rules of professional conduct, which in its present form is as follows:

(1) A firm or partnership, all the individual members of which are members of the Institute (or in part

members and in part associates, provided all the members of the firm are either members or associates), may describe itself as "Members of the American Institute of Accountants," but a firm or partnership, all the individual members of which are not members of the Institute (or in part members and in part associates), or an individual practising under a style denoting a partnership when in fact there be no partner or partners, or a corporation or an individual or individuals practising under a style denoting a corporate organization, shall not use the designation "Members (or Associates) of the American Institute of Accountants."

(2) The preparation and certification of exhibits, statements, schedules or other forms of accountancy work, containing an essential misstatement of fact or omission therefrom of such a fact as would amount to an essential misstatement or a failure to put prospective investors on notice in respect of an essential or material fact not specifically shown in the balance-sheet itself, shall be, *ipso facto*, cause for expulsion or for such other discipline as the Council may impose upon proper presentation of proof that such misstatement was either wilful or the result of such gross negligence as to be inexcusable.

(3) No member shall allow any person to practise in his name as a public accountant who is not a member of the Institute or in partnership with him or in his employ on a salary.

(4) No member shall directly or indirectly allow or agree to allow a commission, brokerage or other participation by the laity in the fees or profits of his professional work; nor shall he accept directly or indirectly from the laity any commission, brokerage or other participation for professional or commercial business turned over to

others as an incident of his services to clients.

(5) No member shall engage in any business or occupation conjointly with that of a public accountant, which in the opinion of the Executive Committee or of the Council is incompatible or inconsistent therewith.

(6) No member shall certify to any accounts, exhibits, statements, schedules or other forms of accountancy work which have not been verified entirely under the supervision of himself, a member of his firm, one of his staff, a member of this institute or a member of a similar association of good standing in foreign countries which has been approved by the Council.

(7) No member shall take part in any effort to secure the enactment or amendment of any state or federal law or of any regulation of any governmental or civic body, affecting the practice of the profession, without giving immediate notice thereof to the secretary of the institute, who in turn shall at once advise the Executive Committee or the Council.

(8) No member shall directly or indirectly solicit the clients or encroach upon the business of another member, but it is the right of any member to give proper service and advice to those asking such service or advice.

(9) For a period not exceeding two years after notice by the Committee on Ethical Publicity no member or associate shall be permitted to distribute circulars or other instruments of publicity without the consent and approval of said committee.

(10) No member shall directly or indirectly offer employment to an employe of a fellow member without first informing said fellow member of his intent. This rule shall not be construed so as to inhibit negotiations with any one who of his own initiative

or in response to public advertisement shall apply to a member for employment.

(11) No member shall render professional service, the anticipated fee for which shall be contingent upon his findings and results thereof.

A comparison of these rules with those appearing as part of the by-laws of the American Association of Public Accountants discloses a number of points of similarity. This is especially marked in the comparison of the third, fourth, fifth, sixth and seventh rules of professional conduct with rules one, two, three, four and six of those of professional ethics of the Association.

In the accountancy profession, as in the case of the older professions of law and medicine, there are those who do not adhere strictly to the rules of conduct laid down for their guidance. Mr. Robert H. Montgomery in the latest revision of his book, *Auditing Theory and Practice* after calling attention to the rules of the American Institute as above set forth, states that "the student of accounting and the young practitioner should familiarize themselves with these recommendations and keep informed regarding the development of rules of ethics of the profession." At the Convention of the American Institute of Accountants, held in Washington in September, 1921, considerable discussion was had on the subject of professional publicity through means which were characterized as unprofessional. Mr. Montgomery on this point, while he does not condone the violations of those rules which are intended to discourage advertising or other forms of solicitation, yet speaks of them as violations of good taste only, and in no wise to be compared with the infractions of the more important rules dealing with the relationship of the accountant to his

client and to the public. He suggests as a preventative of such infractions, the necessity of emphasizing and of developing to the highest degree the feeling of moral responsibility on the

part of accountants which in the certificates granted by many of the states to the qualified candidate, is placed above the fact that such an one has passed a satisfactory examination.