TOWARDS AN UNDERSTANDING OF ACCOUNTING AND SOCIETY: SOME EPISODES IN THE FORMULATION AND DEVELOPMENT OF THE GOING CONCERN CONCEPT

by

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Vol I

A Thesis submitted to the University of Sheffield
in partial fulfilment of the requirements
for the degree of

DOCTOR OF PHILOSOPHY

in

ACCOUNTING

Sheffield University Management School
University of Sheffield
April 1991

DECLARATION

No portion of the work referred to in this thesis has been submitted in support of an application for another degree or qualification of this or any other University or other Institute of Learning.

DEDICATION

This thesis is dedicated to the memory
of my mother Shakuntala Devi Sikka
and my father Amar Nath Sikka who
gave me their blessings for this
work but alas did not live long
enough to see me complete it.

.... Until we meet again ....

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ACKNOWLEDGEMENTS

Writing a thesis is a very long and an illuminating journey. This journey would be very lonely, tiresome and impossible, if it were not for the help of my family, friends and colleagues.

I am particularly grateful to Tony Lowe for his constant support and encouragement not only in his capacity as my first supervisor, but also as a colleague and a friend. Without his help this thesis would not have been completed. My thanks also go to Richard Laughlin for his valuable support and contribution in helping me to develop this thesis.

Thanks are also due to Tony Puxty and Hugh Willmott for their valuable comments and insights. I am indebted to Colin Horner, Murray Glickman and Philip Arestis, not only for commenting on earlier drafts, but for giving me support during times of personal tragedies. Further, my thanks are also extended to Harry Haywood for his support and encouragement.

I am also grateful to the staff of the Library of the Institute of Chartered Accountants in England and Wales for their help and co-ordinating access to archival material. The financial support provided by the Polytechnic of East London is gratefully acknowledged.

I wish to thank my wife Joan, for providing the home, care and support which enabled me to carry out the research. Thanks are also due to Karen and Neil for playing their games quietly and reminding me that there are other things in life.

ABSTRACT

Accounting is a social process, yet little is known about the manner in which its various meanings and interpretations are shaped. Within a sociopolitical framework, this thesis examines the complicated relationship between accounting and society by focusing upon the changing meanings and interpretations of the going concern concept from the late nineteenth century to 1985. It is found that the changing meanings of the concept are shaped by a residue of historical influences and a variety of events and interests. In view of the conflict, tension and unequal distribution of power in a society, various developments enabled and constrained some to play a particular part in shaping the meanings of the concept. The changing meanings and interpretations of the concept are particularly shaped by auditing elites, the State, interests of finance capital and the material interests of practitioners themselves. The evidence suggests that the meanings of the concept preferred by the profession and auditing firms are particularly shaped by the economic interests of practitioners.

CHAPTER 1

INTRODUCTION

1.1: The Nature of the Research

Accounting and auditing practices are implicated in numerous social and political processes. Accounting functions as an instrument of social control (Zeff, 1978), social change (Burchell et al, 1980), medium of accountability (Flint, 1971), justification of monopoly rents (Adams, 1984) and promoter of particular interests (Hopper et al, 1986). It has come to be seen as a "means for resolving social conflict, a device for appraising the terms of exchange between social constituencies, and an institutional mechanism for arbitrating, evaluating and adjudicating social choices" (Tinker 1985, page 81).

Accounting promotes particular interests by privileging certain types of social reality (Tinker et al, 1982). The State has used audited financial information for the regulation of wages, competition, labour relations, prices, economic strategy and promotion of particular interests and relations of power (Rorem, 1928; Scott, 1931; Tricker, 1979; Flint, 1982). This reliance is frequently legitimised by referring to the apparent neutrality[1] of accounting principles and by promoting the same. For example, Scott (1931) notes that

> "the extent to which this independent standing of accounts has developed is indicated by the fact of an increasing readiness of the courts of law to give heed to accounting principles and to adjust legal rules. .... Instead of depending upon the market or upon the law, regulatory

commissions turned to accounts and accounting principles for guidance and support .... because commissions have been dependent upon accounting principles to guide their decisions, accounting has been the major source of new law developed by regulation" (page 235-236).

Thus seen, the ability to officially define the meaning of accounting becomes a source of power and a shaper of public awareness and opinion (Berry et al, 1985). Much of accounting information is frequently legitimised by appealing to concepts and principles[2] . Such principles are part of social relations of power and are actively implicated in the construction of social reality, legitimacy of the State, and promotion of particular interests in a society. In this context, the meaning of accounting concepts becomes a terrain for ideological contestation and struggle, where each party invokes a particular grid of meaning to justify a particular view of the world. The meaning attached becomes a source of power, influence and conflict not only for the assumed experts, but also for the 'significant others' and thus becomes a subject of negotiation, contention, manipulation, dispute, speculation and outright denial.

Whenever the privileges of the accountancy profession are challenged, it defends its interests by mobilising accounting concepts and principles (Hines, 1989). The times of crisis are often accompanied by calls for the creation of a conceptual framework (for example see, Peasnell 1982; Stamp 1985; Dearing 1988; Hines, 1989). Eminent scholars (e.g. Solomons, 1983) expect such frameworks to be underpinned by accounting concepts often described as 'fundamental' and/or 'generally accepted'. The meanings of such accounting concepts are also cited in negligence lawsuits by auditors to defend themselves[3] .

One such accounting concept is the 'going concern concept'. It is the main focus of this thesis. Its meanings and interpretations provide a means of exploring the complicated relationship between accounting and society. This concept is deeply embedded in accounting tradition and practice. All aspiring accountants are required to study it and it is considered to be a vital part of a conceptual framework[4] . It is regarded as 'fundamental' by the accountancy profession (ASC, 1971) and is enshrined in legislation (Schedule 4, para 10, Companies Act 1985). It has been defined as:

> "the enterprise will continue in operational existence for the forseeable future. This means in particular that the profit and loss account and balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operations" (ASC, 1971).

At the institutional level, the meanings and implications of the concepts are not considered to be problematic because, "they have such general acceptance that they call for no explanation in published accounts and their observance is presumed unless stated otherwise" (ASC, 1971, para 2). The legitimacy of the going-concern concept is enhanced by support from powerful international organisations (IASC, 1975; Choi, 1979). Commenting on the concept, Chambers (1966) argued,

> "....... it is an easy step, but a mistaken one, to suppose that the expectation that a firm shall have an indefinite life ......" (page 203).

For Paton (1922),

> "the going-concern assumption is entirely reasonable. ...... The accountant accordingly has the right to take it for granted that the specific concern in which he is interested will continue to operate for some time" (chapter 20).

Whilst Paton and Littleton (1940, page 9) thought that the going-concern concept ruled out the use of liquidation values and justified amortization of fixed assets at cost, Storey (1959) argued that

> " .... no general agreement exists regarding the meaning of the term going-concern value" (page 232).

Sterling (1968) felt that in a changing and dynamic economy the static accounting model underpinned by the going concern concept is "difficult to justify" (page 501), especially as corporate survival depends on successful adoption to technological change and an orderly liquidation of existing assets and liabilities. Whilst the Accountants International Study Group (1975) insisted that "there is a substantial degree of unanimity as to the meaning of the going concern concept" (para 2), Sterling argued that he has "only the vaguest idea of what they mean by going concern" (Sterling, 1985). From his literature review, Carmichael (1972) came to the conclusion that,

> "While accounting literature differs on the appropriate term to describe the going-concern idea-postulate, concept, assumption etc. - there is substantial agreement on the meaning of the term. In accordance with the going-concern concept, an entity is presumed to continue in existence indefinitely, although not necessarily in perpetuity, contrary evidence may negate this assumption" (page 91).

May (1943) described the concept as "essential" (page 49) . However, Arthur Anderson & Co. (1972) state that the going concern concept "should no longer be regarded as fundamental" ....." (page 126). Having described the going-concern concept as 'generally accepted' and 'fundamental', the Institute of Chartered Accountants in England and Wales (ICAEW) declared that

> "various bases of valuation are in common use .... some like 'going concern are regarded as unsuitable for use in relation to property assets of a company" (ICAEW, 1974, para 3).

For the ICAEW, a 'true and fair view' implies "the consistent application of generally accepted accounting principles" (ICAEW, 1958, para 4). In this context, the meaning and interpretations of the going concern concept have considerable impact on auditor responsibilities and the auditor's assessment of a true and fair view (Mautz and Sharaf, 1961; Carmichael, 1972). Indeed, the implications of the concept have been described as

> "one of the most serious problems facing the auditor" (Lee 1982, page 140; 1986, page 142).

Major accountancy firms claim that an

> "auditor should consider the appropriateness of the going concern concept" (Coopers & Lybrand, 1984, page 479).

The going-concern concept has been mentioned in accounting literature for nearly 100 years (see Dicksee, 1892 for one of the earliest discussions), enshrined in legislation and appealed to by the accountancy profession (ASC, 1971); for Mathew Patient, a partner in Deloitte Haskins and Sells (now Coopers Lybrand Deloitte) and a former Chairman (from March 1986 to December 1988) of the Auditing Practices Committee (APC),

> "...... there is no clear accounting definition of what 'going concern' actually means .... [and] .... There are dangers when auditors pronounce on accounting matters which have not been fully explored" (Patient, 1983).

Despite such views, the UK accountancy profession has issued an auditing guideline on 'going concern' (APC, 1985a). Such professional pronouncements themselves are also steeped in contradictions. Whilst SSAP 2 regards the concept as 'fundamental', the APC in its auditing standards (APC, 1980a) treats the matter as an uncertainty inherent in financial statements and for audit report purposes regards it as "material but not fundamental" (paragraph 8). Whilst the auditor's operational standard (APC, 1980b) states that "The auditor should obtain relevant and reliable audit evidence sufficient to enable him to draw reasonable conclusions therefrom" (para 4), the view taken by the auditing guideline on going-concern (APC, 1985a) is that an auditor need not 'actively' collect evidence to support the going-concern assumption.

In 1976, the APC advised auditors,

> "...... so don't assume the going-concern basis is appropriate for all your clients - confirm that it is! .... if you cannot satisfy yourself that the client will remain in business in the forseeable future, then reconsider the going concern" (APC, 1976).

But by 1985, the position had shifted and "the APC ...... decided in favour of the passive approach" (Charlesworth, 1985) even though the implications of a going-concern qualification are said to carry important messages for the share prices and the workings of financial and capital markets (Firth, 1978; 1979; 1980).

The continuing tensions and contradictions of the concept may conceal the contested nature of the concept. The concept may be periodically invoked to promote particular interests. It should be noted that SSAP 2 identifies four fundamental accounting concepts (prudence, consistency, accruals and going concern) which are all enshrined in the Companies Acts, yet only one of these (going concern) has merited an auditing guideline. Why? The privileging of going concern and the meanings assigned to the concept may be indicative of the influence of some sociopolitical factors. Accordingly, the institutionalised invocation of the going concern concept in an auditing context is a major focus of this thesis. Why has the going concern concept been singled out for particular attention and why in 1985 and not earlier? This thesis will provide an answer to such questions.

At the outset, it should be noted that the main aim of this thesis is not to suggest that the 'going concern concept' ought to have a particular definitive and technical meaning or to indicate that some scholars/authorities have arrived at an incorrect technical definition. On the contrary, this thesis recognises that all concepts are multi-accented and have numerous meanings, with each meaning struggling for ascendancy. Rather, in this thesis, the going concern concept is more of a means of illuminating a complicated interplay between accounting and society. This relationship is examined by referring to 'common sense', structural, material, ideological and historical factors. In doing so, an approach substantially different from that employed by much of the current accounting research is adopted.

Traditionally accounting is seen as being factual. This, however, overlooks that not only are the facts theory dependent, the collection of facts themselves is dependent upon the 'interests' of those who seek to collect and present them. The facts may be produced by socially organised practices to privilege the interests of an elite. The embedded interests are historically formulated and manifest themselves through technical meanings and definitions. Much of the traditional accounting writings on history continue to be preoccupied with techniques and procedures (a good example of this is Nobes and Parker, 1979) and consequently little attention has been paid to the relationship of the development of accounting concepts and auditing practices to wider social aspects. Much of the previous research into the going-concern concept is influenced by the methods of neo-classical economics and natural sciences (for example see, Taffler and Tisshaw, 1977; Taffler and Tseung, 1984) and pays little attention to the historical, social, political and ideological factors which shape accounting (Tinker, 1984).

The research undertaken here is of a different kind in that it locates accounting within a sociopolitical framework which recognises conflict and uneven distribution of power in a society (Cooper and Sherer, 1984). It does not assume a basic harmony of interests and thus does not view the interpretation and meanings of accounting concepts in an unproblematic way. Such an approach, whilst noting the contribution of individuals and professional bodies, pays particular attention to the social structures which enable as well as constrain the development and discussion of ideas. The view taken is that there is nothing natural or inevitable about accounting practices or the meaning attached to accounting concepts such as the going concern concept. The principles are the result of interaction between social, economic and political influences (Zeff, 1972). Accounting statements and concepts, just like other social practices are socially constructed and are the result of ideological struggles and influences. It is the social structure[5] and culture[6] which shapes the grids of meaning and the going-concern concept is no exception.

In this thesis, the development of the theory and practice described as the 'going-concern' concept is explored in the context of a complicated relationship between accounting and society at a number of levels.

Firstly, the major theme of the research is to focus on the explicit invocation of the going concern concept in an auditing context. Unlike any other 'fundamental' concept, the going concern concept was the subject of an auditing guideline in 1985. Its formulation provides an opportunity for studying the social, political and economic influences which shape the meanings of accounting concepts. Just why did the accountancy profession find it necessary to refer to the concept at that point in time and why in the manner as explained in the auditing guideline? Were there any particular dangers for the profession? Were particular interests threatened? Which dominant parties are implicated in shaping the meaning of the going concern concept in an auditing context? An answer to such questions will be provided by this thesis. The issuance of the auditing guideline may be indicative of the much deeper ideological and material influence of the auditing wing on the accountancy profession.

Secondly, attention is paid to periods prior to 1985. The meanings assigned to the concept in the auditing context may differ from the earlier ones. In this context, it was decided to look at the meanings from the late nineteenth century onwards. In view of the relative absence of any research into accounting concepts, it was unclear whether the going concern guideline marked some discontinuity in the traditional meanings of the concept, or whether it was referring to the sedimented residue of some earlier periods. As the research progressed, it was found that the going concern concept only became recognised as 'generally accepted' by the UK profession in the 1970s. In contrast, the American State and profession gave institutional support to the concept in the 1930s. Why such differences? What social, economic and political developments enabled or constrained the institutional recognition of the concept? An explanation of the events would provide further insights into the complicated relationship between accounting and society. The explanations provided do not assume that the past is somehow marching towards some pre-destined future. Instead, history is seen as an unending process where the social forces have enabled (and constrained) some groups to either open up and/or limit the possibilities for change. The struggles around the meaning and interpretations of the concept are also seen as part of the ideological struggles, contestations involving the State, institutions, groups, elites and privileged individuals. Rather than attending to the myth of steady progress, the historical analysis will attend to an "interplay of meaningful actions and structural contexts to make sense of the unfolding of unintended as well as the intended outcomes" (Skocpol, 1984, page 1). Whilst the accountancy profession may claim accountancy concepts/principles as its own intellectual property, an historical analysis may reveal that such ideas are actually negotiated within the constraints of social structures to promote particular interests.

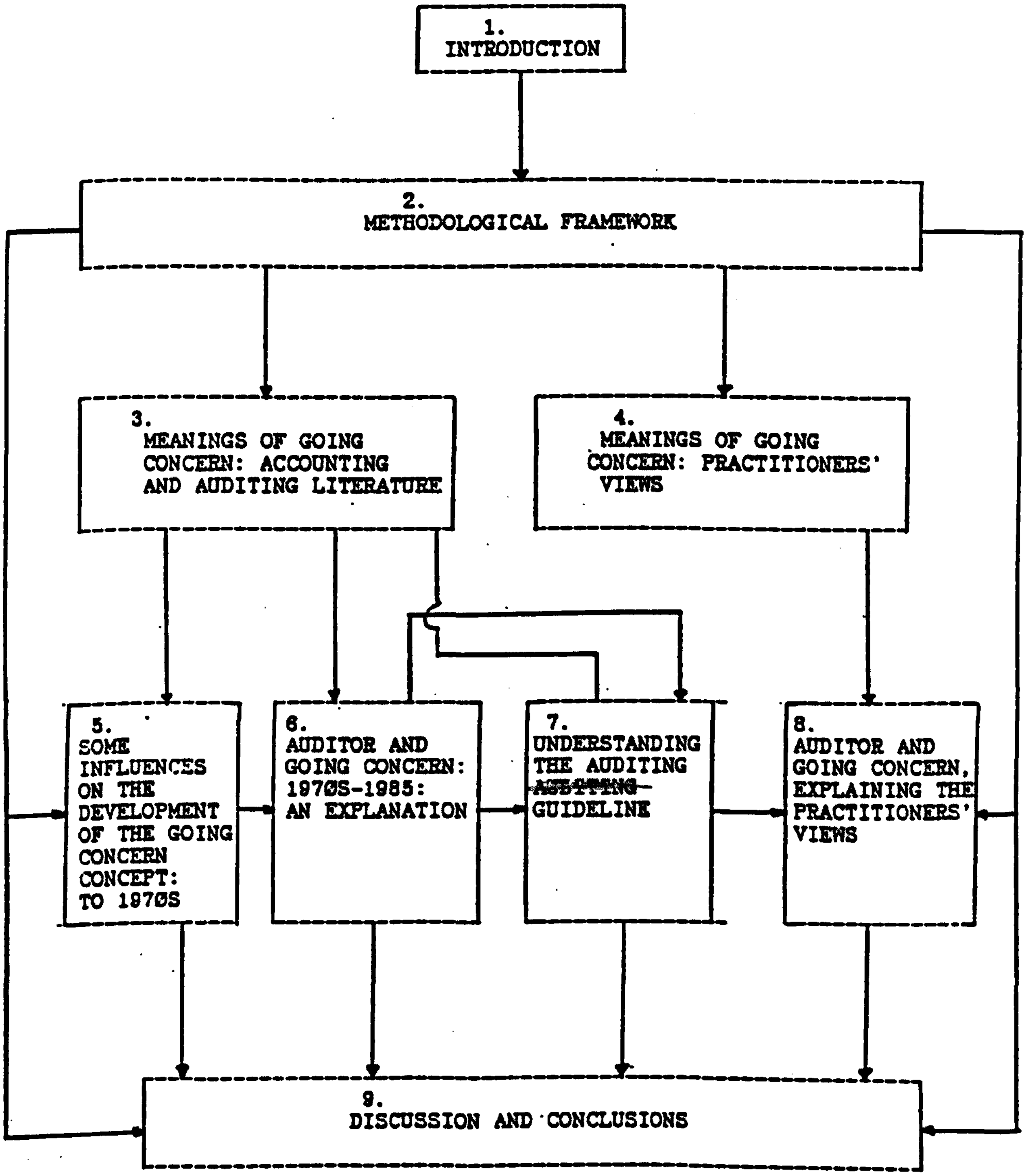
The third major strand of the study investigates the contemporary meanings and interpretations of the going-concern concept (or what is assigned to the phrase 'going-concern') by present day auditors. At the outset it should be noted that whilst seeking the views of auditors and auditing firms, this thesis is not concerned with any large-scale, mass or group behaviour conceived as the behaviour of a large number of auditing partners, accountancy firms, or individual auditors. The behaviour of individuals, or groups of auditors, is an interesting psychological phenomena and a worthy topic for research, but it is not the subject of this thesis. Instead, within the context of the methodological framework, this thesis is concerned with persistent relations between individuals and social structures, groups and social structures and with the relations between these relations. Such social relations are general and are relatively enduring and do not necessarily involve any conscious collective or mass behaviour. In order to present the various arguments, analyses and evidence, the thesis is organised as follows:

1.2: Organisation of the Thesis

This thesis is organised into eight further interconnected chapters as shown in figure 1.1. Frequent references to this figure will assist the reader in seeing the connections between various chapters and arguments. As figure 1.1 shows, the thesis should be seen as consisting of two broad layers. The first layer, consisting of chapters 3 and 4, refers to the meanings which the accounting literature, institutions and practitioners have attached to the going concern concept. In this layer, little attempt is made to provide any sociopolitical explanations of the concept or to explore the complicated relationship between accounting and society. Such tasks are undertaken in the second layer, which consists of chapters 5, 6, 7 and 8.

FIGURE 1.1

STRUCTURE OF THE THESIS



Details of each of the eight succeeding chapters are as follows:

Chapter 2 explains the methodological framework used in this thesis. In line with the view that the development of and the meanings assigned to the going concern concept are socially constructed, humanly determined and hence subject to change, this thesis refers to theories which provide a framework for examining the going concern concept in a structural, material, ideological and historical context. Such theories focus on ideological contestation, struggles and 'interests' and thus regard conflict and tension as a central feature of a capitalist society rather than consensus and harmony. The major benefit of such a approach is that accounting is not seen as an unproblematic, narrow, neutral technique, but as political and the result of power, influence and ideology.

Chapter 3 focuses on the history of the going concern concept. The period covered from the late nineteenth century to 1985, being the date of the issuance of the auditing guideline (APC, 1985a). Such a coverage is necessary as any understanding of present is dependent upon the past. The changing meanings of the concept may well carry stratified deposits of an earlier era. There is a wide spread belief (for example, see Yamey 1956; 1979) that most accounting principles and concepts were developed in the late 19th century, but the literature is found to include little specific reference to the going concern concept in an auditing context. Indeed, the going concern concept only came to be labelled as 'generally accepted' in the 1930s. In the UK, discussions of the concept in an auditing context only began to emerge in the 1970s.

Chapter 4 continues with the first layer by focusing upon the interpretations and meanings assigned to the concept by auditors. This chapter describes the results of empirical researches by referring to the views of auditors from large and small firms.

Chapter 5 marks the beginning of the second layer of the thesis (see figure 1.1), which provides explanations of the invocations, meanings and interpretations of the concept. Within the scope and space of this thesis, an encyclopaedic analysis of everything associated with the going concern concept from the late nineteenth century onwards is neither possible nor attempted. Chapter 5 has a rather modest aim. It focuses on selected episodes and flows from the contents of chapter 3. In this chapter, it is shown that despite the contradictory meanings assigned to the concept, it came to be regarded as 'generally accepted' in the USA in 1930s even though the earlier (and possibly first) discussions of the concept were to be found in the UK literature. By contrast, there were no moves by the professional bodies or regulators to recognise the concept as 'generally accepted' in the UK. This recognition was not received until the 1970s. However, the institutional recognition of the concept was frequently accompanied by traditional meanings. Chapter 5 explores the early influences which shaped the meanings and interpretations of the concept and the factors which led to the institutional recognition of the concept, both in the USA and the UK.

Chapters 6 and 7 also follow on from the contents of chapter 3 (see figure 1.1), where it is noted that the going concern concept in an auditing context began to be elaborated in considerable detail from the 1970s onwards. The explanations contained in chapter 6 suggest that the rise of the going concern concept in auditing is very closely associated with the economic, political and social developments of the time. This period is marked by considerable economic turbulence resulting in a restructuring of the British industry, secondary banking collapse and a decline in the property markets. Such turbulence helped to focus critical attention on the role of auditing and accounting practices in the legitimation of corporate disclosures and the workings of financial and capital markets. Contrary to popular beliefs and 'common sense' views, auditors were not seen to be effective in performing their 'watchdog' functions. Upon such a realisation, 'significant others' including the State crticised auditors and launched massive negligence law-suits. The argument of chapter 6 is that it is the concern with auditor liability and professional legitimacy which made the implications of the going concern concept a major issue for the accountancy profession, eventually resulting in an auditing guideline in 1985.

Chapter 7 provides further sociopolitical explanations of the interpretations of the concept. This chapter examines the way the UK profession came to interpret the going concern concept in an auditing context. It will be shown that the particular interpretations are meant to promote the 'economic interests' of major firms by narrowing auditor responsibility. The main intention of the profession was to protect major firms from law-suits without any meaningful increase in audit work. In order to understand the institutional invocation of the concept, this chapter also focuses upon the Auditing Practices Committee, which formulated the auditing guideline. Upon investigation, it is found that the APC is the result of particular pressures from the State and press criticisms. This Committee is dominated by the very firms who were being sued, mostly after one of their clients ceased to be a going concern. It is argued that the APC, in common with some of its other activities, interpreted the going concern concept to promote the major firm's interests.

Chapter 8 follows from chapter 4 and concludes the second layer of the thesis (see figure 1.1). Chapter 4 referred to the interpretations of the concept by practising auditors. Within the context of the methodological framework, chapter 8 will explain the material, ideological and historical factors which have shaped the auditors' interpretations of the concept.

Chapter 9 finally concludes the thesis with a discussion, summary and review of the evidence presented.

1.3: Chapter Summary

The main focus of this thesis to provide insights into the complicated relationship between accounting and society, as seen through the various meanings assigned to the going concern concept. The main thrust of the thesis is on the meanings of the concept in an auditing context. Such meanings and interpretations are contained in the auditing guideline issued in 1985. This thesis will examine the manner in which the profession came to interpret the concept. This will be accompanied by an analysis of the institution (APC) which was primarily responsible for formulating the privilged meanings. The thesis does not neglect the earlier periods. It explores the late nineteenth century and early twentieth century developments which came to influence the interpretations of the concept and gave it 'common sense' meanings. In addition, it also examines the factors which led to the concept receiving institutional recognition in the UK and the USA. Finally, the thesis examines the factors which shape the meanings which the practitioners assign to the going concern concept as part of their practice. Unlike much of the recent accounting research, this thesis will focus on the ideological, historical amd material factors which shape the implications of the concept. Throughout this thesis, no attempt will be made to argue that the going concern concept should have any particular technical or definitive meaning. Rather the main thrust is to show that the meanings assigned depend on particular social relations of power.

Chapter 1 Footnotes

1) Neutrality (interpreteted as freedom from bias) and representational faithfulness are regarded as essential qualitative characteristics of accounting information by the FASB (1980).

2) The accounting literature also refers to these as postulates, assumptions, conventions etc.

3) For example, Lloyd Cheyham & Co. v Littlejohn & Co. (1985) Q.B., as reported in Accountancy, February 1986 and Accountancy Age, 16th January 1986. In this case the auditors cited SSAP 2 and the matching principle in favour of their audit approach and were exonerated by the courts.

4) The accounting concepts mentioned in SSAP 2 are often in conflict with each other. Many of the UK accounting standards do not attach equal importance to such concepts, mainly relying on prudence, yet these concepts are thought to provide a framework for what is called a conceptual framework.

5) Theories of social structure are mostly associated with various strands of Marxism. This thesis will place considerable reliance on such a research programme (see chapter 2 for further details).

6) This thesis recognises the contribution of various individual authors, but only in a social and cultural context. It is reasonable to assume that culture gives identity to man. This is so because the condition of man requires that the individual, while he exists and acts as an autonomous being, does so only because he can first identify himself as something greater, as a member of a society, group, class or something similar. He may refuse to attach a name to it, but he instinctively recognises it as 'his'.

CHAPTER 2

METHODOLOGICAL FRAMEWORK

2.Ø: Introduction

As an introduction to the problematic, chapter 1 noted that the going concern concept has been assigned numerous meanings and interpretations (often conflicting and contradictory). In view of a variety of meanings and interpretations, the question then is what kind of methodological framework will help to understand and explain the changing meanings of the concept? Methodology consists of "interrelations of substantive problems, sources of evidence, and of larger assumptions about society, history, and the purposes of scholarship" (Skocpol, 1984, page x). The choice is important because it guides the manner in which researchers investigate a phenomena, understand complex processes, generate knowledge and demystify (or mystify) social processes (Morgan, 1983).

In selecting the methodological frameworks, one could seek guidance from the frameworks currently popular in much of the accounting research. However, much of the traditional accounting research is often silent about the ontological and epistemological assumptions which sanction a particular investigation (for a review see, Chua et al 1981; Christenson 1983). Much of the accounting research has also tended to be located in positivist frameworks (Christenson, 1983) which tend to produce quantifiable facts, without necessarily inquiring into the social conditions of their existence (Bernstein, 1976; Tinker, Merino and Neimark, 1982). In such approaches, the historical grounding of a problematic is neither studied nor acknowledged (Held, 1980). Little effort is made to explain how social practices have come to be in their present state (Giddens, 1977). Matters such as class, society, power, subjectivity, ideology, etc. are regarded as "messy" (Morgan, 1983, page 398) and are thus ignored. Such methodologies often make individuals or groups the loci of inquiry and fail to pay adequate attention to social structures, patterns of relationships and institutions within which individuals exist and construct competing meanings of concepts, such as the going concern concept. In view of the criticisms of such methodologies and calls for alternative approaches (for example, Lowe and Tinker, 1977; Tomkins and Groves, 1983; Hopwood, 1983; Cooper and Sherer, 1984; Laughlin 1987), this thesis adopts an alternative framework. This views accounting principles, such as the going concern concept and its various meanings emerging from the dynamics of social structures, power, ideology, change, continuity, discontinuity, privilege, institutions and a constant human struggle to define and redefine them.

The methodological approach developed here borrows from a number of different traditions to construct a rich framework for understanding the relationship between accounting and society. Throughout the thesis particular attention is paid to social formations, institutions and the distribution of power within them. It is argued that in a capitalist society, discourses relating to the 'economic' are prioritised and that the State (Althusser, 1971; Gramsci, 1971; O'Connor, 1973; Habermas, 1976; Jessop, 1982; Offe, 1984) and 'ideological state apparatuses' (Althusser, 1971; Laclau,

1977) are a privileged site of power. Such institutions hold a key to understanding the various meanings of the going concern concept.

In order to present the various arguments, this chapter is organised into four sections. Following the insistence that all social practices and concepts exist within a social context, it is not too unreasonable to assume that any theoretical framework used to explore the changing meanings of the going concern concept must take account of society and the position of individuals within such structures. Therefore, section 2.1 provides a basis for understanding enduring social relationships. In this context, section 2.1.1 develops a model which provides an understanding of the society/individual relations. Section 2.1.2 explains the processes by which a society is reproduced and transformed. However, there are competing theoretical schools which strongly challenge the focusing of research on such structures. Therefore, section 2.1.3, in addition to summarising the section, also answers some of the criticisms. Following the argument that the economy and the State are major influences in reproducing and transforming society, section 2.2.1 in Marxist traditions, discusses those aspects of the economy which are relevant to understanding the changing meanings of the going concern concept. The State is seen as actively involved in reproducing and transforming the meanings of accounting concepts. Therefore, section 2.2.2, examines the role of the State in a capitalist society. After a discussion and summary (section 2.2.3) of the arguments so far presented, section 2.3 locates the accountancy profession and practices in the framework developed in the previous section and highlights the relationship between accounting and the 'economic' and the State. Section 2.4 concludes the chapter with a summary and its implications for the remaining chapters.

2.1. UNDERSTANDING ENDURING SOCIAL RELATIONSHIPS

All concepts, knowledge, conventions, discourses and practices are located in particular social formations and structures. The changing meanings and interpretations of the going concern concept, whilst elaborated by individuals, are unlikely to be exempt from such influences. So a framework is needed which will help to conceptualise society/individual relations.

Before moving on to the details of the framework, it would be helpful to make a few preliminary remarks. Broadly speaking, the framework is 'realist' (Bhaskar, 1979, 1989). It views human subjectivity as constituted by enduring social structures and practices. Here society is assumed to be differentiated and changing. However, it rejects the over-determinist tendencies of classical Marxism. It does not regard ideology as purely false or illusory, but does recognise that in view of constant ideological contestation and struggle, worldviews are always distorted. In this framework social structures are 'real' and have material existence in the sense that the individual practitioners have to take them seriously and act upon them. Following Gramsci (1971), it is argued that meanings and interpretations of the going concern concept are changed through ideological struggle and contestation. The framework recognises the influence of society in shaping subjectivity, but is not sympathetic to Durkeheimian (1964, 1978) conceptions in which society may be seen as being too rigid and functionalist. The chapter is sympathetic to Weberian (1976) thought and recognises the role of the individual in shaping social practices, but believes that this can only happen within the constraints of social structure. It acknowledges the Althusserian (1971) notion of interpellation, but following Foucault (1977, 1979), recognises that individuals may resist some discourses. Though acknowledging the Foucauldian connections between knowledge and power, this thesis does not share his belief that power is amorphous and that there are no pivotal centres which secrete power and give direction to discourses.

2.1.1: Conceptualising Society/Individual Relationship

Critical realism assumes that a society consists of enduring structures and generative mechanisms which produce observable events and phenomena. It insists that all social phenomena are the product of a plurality of influences. It does not assume that social structures are spontaneously apparent in the observable events, rather the view is that they can be identified through theoretical perspectives. Any empirically controlled investigation needs to take account of such factors.

In Marxist thinking, society is viewed as a system of relationships and positions, not as a collection of individuals (Bhaskar, 1989). As most (but not all) important groups are constituted by modes of production, Marxist theories focus on class and class relations. Though Durkheim (1978) contested some of Marx's ideas, he did acknowledge the importance of society in forming individual consciousness and thus creating conditions for reproduction of societies. In opposition to utilitarianism, which advocated empiricist philosophy and focused upon individuals, Durkheim (1978), instead advocated a collectivist perspective on society with a positivist[1] methodology. He wrote,

> "There exists a social consciousness of which individual consciousness are, at least in part, only an emanation. How many ideas or sentiments are there which we obtain completely on our own? Very few? Each of us speaks a language which he has not himself created: we find it ready made" (Durkheim, 1978, page 102).

It is important to appreciate that Durkheimian and realist conceptions of society are not the same. By the commitment to positivism, it is only possible to construct enduring relationships from collective phenomena, whereas under realism the collective phenomena themselves are the result of enduring relationships. Durkheim felt that an individual is constructed by society, but the society had its realities which were not the outcome of motivations and actions of individuals. Society is reproduced because social norms are internalised by individuals which then become regulative mechanisms and construct individuals. Society seems to be beyond human control and acquires a fixed and immutable quality. This view is depicted in figure 2.1.

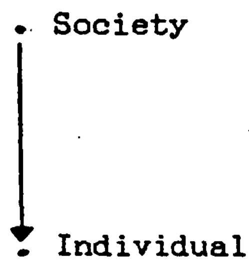


Figure 2.1
Durkheimian Model of Society and Individual
Source: Bhaskar, 1989, page 74.

The Durkheimian conception of society commits the error of reification and is too restrictive. Levi-Strauss (1964), one of the inheritors of the Durkheimian traditions, used the analogy of a card game to illustrate the effect of social structures. In a card game, each deal results in an arbitrary distribution of cards and each player, depending on the cards (resources), can use different tactics within the overall rules of the game. Regardless of the tactics and strategies, the end result is dependent upon the rules. Indeed, Durkheim went as far as to suggest that in social explanations, the characteristics of individuals could be ignored and that 'social facts' could be understood independently of the individual whose actions they determine.

Figure 2.1 does not recognise the ability of some individuals or groups to resist a certain kind of subjectivity being imposed upon them. The society is seen as external to the individual, who is thought to be unable to elaborate any discourse of resistance, ideological contestation, or struggle to transform the meanings of accounting concepts such as the going concern concept. In contrast, critical realism does not see society as a closed system (card game), but rather as an open system, or a system which can be modified through struggle and contestation.

Another approach is by Weber (1968), who as figure 2.2 shows adopted an essentially individualistic[2] conception of society.

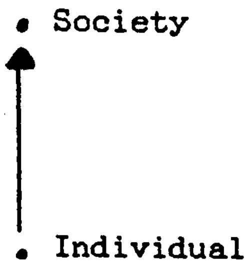


Figure 2.2
Weberian Model of Society and Individual
Source: Bhaskar, 1989, page 74.

Like Durkheim, Weber seeks to identify causes of social relationships and actions. However, in his model, almost all social facts are seen to be the result of intentional or meaningful human activity. The individual's intentions, motives and actions are assumed to be 'voluntary' rather than being 'determined' by the social relations. The obvious problem is the relative neglect of the influence of social structure and social relations of power. As Westergaard and Resler (1975) put it,

> "In any society, the pattern of people's lives, and their living conditions take the form which they do, not so much because somebody somewhere makes a decision to that effect; but in large part because certain social mechanisms, principles, assumptions - call them what you will - are taken for granted" (page 142).

In contrast, realism is opposed to methodological individualism, which seems to assert that social practices can be explained solely in terms of facts and information about some individuals or groups. This is not too helpful, as in talking about an individual one presupposes a social existence and context. Any discussion of a tribesman presupposes the existence of a tribe. The need for financial statements presupposes some social arrangements of accountability. The existence of a professional auditor presupposes the existence of a profession. It is the society which shapes individual's subjectivity.

Such thoughts suggest that the consideration of any social practice or concept requires the consideration of both the individual and society. The model suggested by Berger and Luckman (1967) is a compromise on the Durkheimian and Weberian conceptualisations. In this model, as shown in figure 2.3, the individual creates society who produces the individual, who produces society in a continuous dialectic.

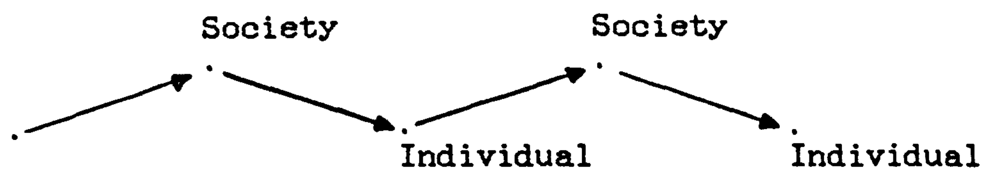
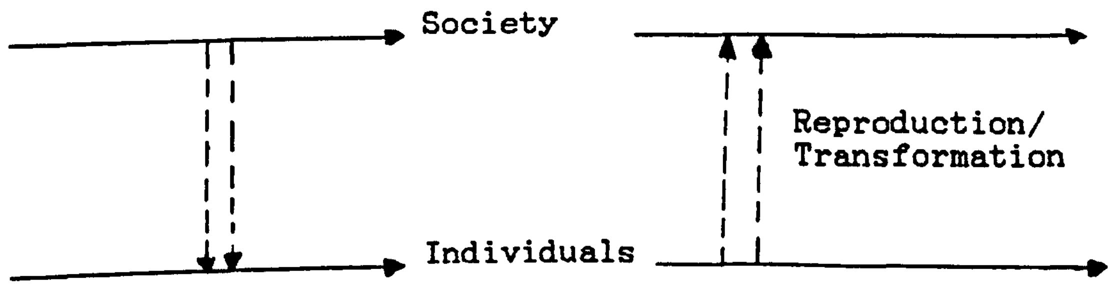


Figure 2.3
Berger and Luckman Model of Society and Individual
Source: Bhaskar, 1989, page 75.

This model tries to avoid the voluntaristic implications of Weberian and reification of Durkheimian traditions. It assumes that shared meanings and interpretations become institutionalised and are then experienced as social 'facts' by the later generations. It recognises the subjective and intentional actions of individuals, as well as the coerciveness of social facts. However, there are difficulties with this schema. Society and individuals are not related dialectically. The model encourages a rather mechanistic determination of the individual by the society. On the part of the individual, it appears to encourage belief in voluntaristic idealism. Under this model, social structure is not characterised as being able to stand on its own, irrespective of the actions of an individual. Figure 2.3 can be improved by recognising that

> "people do not create society: for it always pre-exists them and is a necessary condition of their activity" (Bhaskar, 1979, page 47).

A newly born infant will find beliefs, rituals, language, etc., always already made and will experience these as 'real'. If individuals encounter an already made social world then there is no question of them creating it. It is more appropriate to say that through struggle and practice they reproduce and/or transform society. Marx (1986) argued that the activity of human beings is two-fold: social reproduction and producing society anew. Individuals reproduce society and society reproduces them. The individual exists in society and the society exists in the individual. This position is synthesised in figure 2.4.



<u>Figure 2.4</u>
<u>A Transformational Model of Society</u>
<u>Source:</u> Bhaskar, 1989, page 77.

The model gives full recognition to the argument that,

> "Men make their own history, but they do not make it just as they please; they do not make it under circumstances chosen by themselves, but rather under circumstances directly encountered, given and transmitted by the past" (Marx, 1986, page 277).

The tranformational model sees society as the ensemble of structures, positioned practices, conventions and network of relationships which individuals do not intentionally create in their activity, but in such activity they always presuppose their existence. Bhaskar (1979) argues that it is mistaken to reduce society to groups because, a

> "society does not consist of individuals but expresses the sum of the relations within which individuals stand" (page 32).

Society provides rules, conditions, opportunities, resources, constraints and necessary conditions for intentional human activity. The model recognises that society does not exist independently of conscious human activity, but is not its product. The dotted vertical lines show that society provides the necessary conditions for intentional human activity. All social practices and structures, for example, the family, economy, State and professional institutions depend upon or presuppose social relations. Through their conscious human activity, people unconsciously produce the structures that govern their activities of production. For example, people do not have children with a view to providing labour for capitalist enterprises. Society is the unmotivated condition of all human motivated productions, but can not be seen to exist independently of human agency.

Realism insists that social structure and relations are a necessary condition for any human activity. The structures which agents produce or transform in their activity are also structures of power which may involve alienation, domination, coercion, oppression and opportunities for democracy and liberation. Realism avoids the errors of reification and voluntarism and insists that through resistance, struggle and contestation individuals can transform society. Compared to the ideologies of positivism, the social world is not assumed to be made up of some random events and sequences, rather it is assumed to be structured, differentiated and changing. The manner in which the social world is differentiated and structured is ultimately a matter for theoretical and empirical investigation. In this context, it is appropriate to conceive of Marxism as an ongoing research programme, an empirical thesis, which provides an understanding of the way the social world is structured and how it can be changed (Bhaskar, 1989). Indeed, the remainder of the chapter borrows freely from this research programme to enable this thesis to explain the various meanings of the going concern concept.

2.1.2: Conceptualising Reproduction and Transformation

Whether the meanings of the going concern concept are reproduced or transformed, is to a considerable degree a question of ideologies and human subjectivity (Gramsci, 1971). Human subjectivity is shaped by competing discourses (taken to mean an organised set of meanings) and ideologies which form a tradition, mutually define each other and hang together by defining a discursive chain of meaning to form what Foucault (1977, 1979) calls the 'regimes of truth'. Contrary to the tenets of classical Marxism, ideologies are not 'false' and 'illusory'. The 'false consciousness' thesis (Marx and Engels, 1970) assumes that a great mass of people are unable to perceive their real social situation. It assumes that some interests and classes reside outside society and whose 'true' knowledge is already pregiven. Such an explanation is vulnerable to the charge of class essentialism as it assumes that classes are unified and do not have to come to terms with contradictory and conflicting ideas.

Following Gramsci (1971), Althusser (1969, 1971) and Laclau (1977), it is argued that ideologies are social forces in their own right. They affect social practices and change our conceptions of the world. The fact that some ideologies may be regarded by some as partially correct, false, illogical, incoherent or unsound, may be of little consequence. Whilst on moral, ethical or epistemological grounds, one may object to some ideologies, the point remains that all ideas, no matter how illogical or unsound, shape people's motivation and commitment. They represent their interests and thus persuade them to follow course A rather than course B and so on. People experience the social world through competing ideological categories and images, but such images will only help to see partial truths.

Ideologies for Althusser (1969) are not a consciously held set of beliefs, but structures which "act functionally on men via a process that escapes them" (page 233). Ideologies have a material existence. They are not some vague ideas, but are inscribed in or 'inserted into practices' through language, institutions and social relations. Therefore, there is no question of having something beyond ideology. No social practice or institution resides outside ideology. These practices are governed by, symbols, rituals and modes of operations within institutions.

If any society or social practice is to continue, it must be reproduced and/or transformed. Ideological and social positions are not taken up by magic. They are strongly shaped by discourses which are articulated by powerful groups. These include the State and what Gramsci (1971) calls 'civil society'. 'Civil society' connotes organisations which may not be directly funded by the State or be part of the material production in an economy, but are nevertheless long-lasting. Althusser (1971) called them 'Ideological State Apparatuses' (ISAs). Examples of which are the Church, schools, press, professional bodies, etc. Such organisations may be relatively autonomous and thus capable of having a dominant role in some discourses. There is a plurality of ISAs both in the public and private domain and they function massively and predominantly by ideology, but depend on certain economic and political conditions for their existence. Thus there is always a connection between ideology, economic and the civil society (Gramsci, 1971).

In the processes of reproduction, the ISAs have a particular role to play by transmitting dominant ideologies (which cut across class, gender, race etc). Whilst there is no guarantee that the subjectivity transmitted and appropriated will be identical, the ISAs aim to perform a dual role of reproducing and transforming a society by the process of interpellation (Althusser, 1971; Laclau, 1977).

Interpellation (or hailing) involves recruitment of the subjects by addressing them in such a way that the subject recognises himself both as the author and the receiver of the symbols and beliefs of an ideology. In taking up a position within ideology, a subject is at once dominated and empowered by the categories and associations of the discourse. For example, in religious ideologies such as Christianity, individuals are given a certain relationship in relation to God and other human beings. By being described as a christian or a sinner, an individual is inserted in social practices and structures and is given a concrete identity. Once an individual recognises himself as a christian or sinner, this then invokes a cluster of other relationships and positions which then places them in the social order.

Interpellations operate on an exclusion principle, in that some elements are marginalised or excluded. This means that ideologies work by overlooking some elements and thus present a particular picture of the world. The criteria of including or excluding something is not given by the word 'christian', but rather depends on the contexts. It is appropriate to recognise that individuals are never in any simple sense recruited to one ideological system. The ideological elements themselves have multiple meanings and certain kinds of interpellations can be wrested away from a discourse (Laclau, 1977). Thus subjectivity is never fixed and is changing. Individuals do and can resist certain interpellations, otherwise it is difficult to transform society.

All social practices and concepts are subject to continuous ruptures and transformation through contestation and struggle (Gramsci, 1971). Contrary to classical Marxism, Gramsci argued that ideologies cannot become organised simply by appealing to economic factors alone. To become dominant, they need to become embedded in everyday experiences and become 'common sense' ideas. 'Common sense' constitutes the already formed and taken for granted ground on which more coherent ideologies compete for dominance. Whilst acknowledging that social structures are differentiated, Gramsci (1971) argued that,

> "Every social stratum has its own 'common sense' and its 'good sense' which are basically the most widespread conception of life and man. Every philosophical current leaves behind a sedimentation of 'common sense' .... Common sense is not something rigid and immobile, but is continually transforming itself, enriching itself with scientific ideas and with philosophical opinions which have entered ordinary life" (page 326).

The 'common sense' itself does not start anew and has no history. Rather, it is a sedimented residue of historical traces containing myths, diluted concepts, prejudices, inherited wisdoms, folklore, etc. It is episodic and fragmentary and will thus contain contradictions. The 'subject' itself is the site and terrain of struggle and need not be logically coherent. This is why when interpellated, people swing back and forth from conservatism, liberalism, laissez-faire, welfarism and so on, seemingly at times without hesitation. Gramsci argues that to understand the dynamics of a society, greater attention needs to be paid to those ideologies which have influenced a great mass of people, organise their everyday thinking about society, form mass consciousness and provide the basis for spontaneous thought. It is these ideologies which have become 'organic' and are the prime movers of human consciousness. Such ideologies

> "...... organise human masses, and create the terrain on which men move, acquire consciousness of their position, struggle etc. ......" (Gramsci, 1971, page 377).

To become effective, ideas need to be organised. This is dependent upon politics and institutions which disseminate and circulate ideologies. People are comforted by the fact that some social ideas and practices are sanctioned by eminent institutions. Ideologies are always related to class or group interests. Whilst Foucault may be more interested in micro politics of power and less in a theory of truth/power, Gramsci (1971) argues that the State and institutions of civil society (what Althusser calls 'ideological state apparatuses') have a crucial role to play in the constitution of subjects by reproducing their sense of identity within the existing power relations. The truth/power of class interests or hegemony[3] is pursued not through coercion, but through consent. This consent is not based on illusions, but is founded on a material base (e.g. the need to earn wages exerts pressure on subjects) in which the State and 'Ideological State Apparatuses' (ISAs) play a particular part. In addition, business organisations also influence the lives of the masses to produce a set of beliefs, values and practices which form the 'common sense' and even philosophies (Gramsci, 1971, pages 279-318).

Hegemony requires the successful mobilisation and reproduction of the active consent of dominated groups. A major question then is how is the consent produced, especially in a society which on one hand is committed to democracy yet on the other is marked by inequalities in the distribution of wealth and political power. Gramsci argues that this is done by taking systematic account of popular demands and interests. Such demands and interests themselves are selectively defined and are presented as 'real'. The active consent is not limited to some simple show of preferences as some pluralists will have us believe, but rather it is produced by controlling the agenda, mobilising bias in a system, determining which issues are key issues, excluding some threatening issues and by shaping the needs and desires of the subordinate groups by a variety of ideological and institutional means (Lukes, 1974)[4]. Hegemony

> "occurs when the intellectual, moral and philosophical leadership provided by the class or alliance of class fractions, which is ruling, successfully achieves its objective of providing the fundamental outlook of the whole society" (Bocock, 1986, page 63).

The ruling groups may have the support of the State. They may also dominate some economic areas. In order to pursue their interests, the dominant classes will build alliances and make compromises, but usually only on the secondary issues. They may grant rights of equality, such as citizenship and access to the judicial system, but may not eliminate the economic inequalities which enable some to use the same structures more effectively. Concessions and compromises help to reduce the severity of any class conflict, maintain general support and secure legitimacy of the power bloc in an inherently unstable political system. When a current of ideas becomes a faith, then it becomes capable of preserving the ideological unity of a block and serves to cement and unify it. Hegemonic processes are concentrated in certain organisations, such as the school, mass media, the State, professional institutions, etc. Through 'traditional'[5] and 'organic'[6] intellectuals, the dominant group provides moral, political and intellectual leadership in order to reproduce or form a collective will and pursue its interests. In this respect, the education system has a major role to play in producing assent for dominant ideas (Gramsci, 1988, chapter X). The intellectuals play an important role in organising the dominant class into an historic bloc. Indeed, Gramsci insists that any understanding of reproduction and transformation of societies must be accompanied by an analysis of the ISAs which elaborate ideology - its 'organic intellectuals', for these are the key means of production and dissemination of ideas.

The hegemony is unlikely ever to be complete as competing discourses are always present. As Foucault argues, 'where there is power, there is resistance'. All organisations, including the State, are involved in determining which philosophy is to be widespread. These organisations may have conflicting interests. Some may be dependent upon the State for their existence whilst others may be relatively free from the direct influence of the State and may become important and effective sources of independent philosophy and political criticism. The times of upheavals are marked not by the introduction of new scientific forms of thought, but by providing and making 'critical', through struggle and contestation what is already an exisiting activity. Such struggles seek to alter the meanings of practices.

The above paragraphs have referred to the notion of dominant ideologies (Marx and Engels, 1970), therefore, it is appropriate to say a few words about ruling class/ideas, or the dominant ideology thesis. Such a thesis has attracted considerable criticism (for example, Abercrombie, Turner and Hill, 1980). Contrary to populist conceptions, Marx was less reductionist than is commonly assumed. For example, he wrote,

> "...... one must not form the narrow-minded notion that the petty bourgeoisie, on principle, wishes to enforce an egoistic class interest. Rather, it believes that the special conditions of its emancipation are the general conditions within which alone modern society can be saved and the class struggle avoided" (Marx, 1986, page 307).

The dominant ideologies may unify some groups, but their ideas can be contested by other groups and that is one of the reasons for struggle and contestation through which social practices are transformed. However, there is another aspect. The notion of 'dominance' is essential to any empirical test of pluralism. By abandoning the notion of ruling ideas or ruling classes, there is a danger that one may abandon the very idea of 'dominance' in social formations and discourses and end up with a rather weak pluralistic concept of power. Rather than simply conceiving it as the imposition of a framework, whether by force or through ideological compulsion on a subordinate group or class, there is an alternative. This 'dominance' can be both through the level of the conscious and the unconscious. It can be seen as a property of the system or social relations involved, rather than an intentional bias. Auditors and standard setting bodies would rarely acknowledge the intentional bias in their decisions, but due to social relations of power, mode of production, etc., their decisions may systematically favour a particular group or class. This is why Gramsci refers to hegemony through cultural and moral leadership, where a group moulds or fashions a way of life in such a way that conditions are created for the furtherance of its interests. Gramsci rejects the simple economism of vulgar Marxism and any simple link between the economic and ideas. Like Habermas (1976), Gramsci too emphasises the importance of institutions and politics in transforming and/or reproducing society. In the final analysis, according to Gramsci, politics is about the articulation of meanings, which are only partially fixed. It is this articulation of the meaning which is the real terrain of struggle, contestation and hegemony.

As has already been commented, in a highly differentiated society, concepts such as the going concern concept change through ideological struggle and contestation. Social practices and concepts do not have any fixed meanings as there are always competing discourses which seek space (Laclau, 1977). Such competing meanings can be integrated into different discourses. For example, the concept of 'democracy' can enter different discourses (say of socialism, conservatism, fascism, communism, liberalism) and carry a different meaning in each discourse. The feminist movement has struggled to shape the meaning of 'personal'; the gay movement has struggled to define 'sexual' politics; the word 'pig' need not just mean an animal but can be used to denote an aggressive policeman or to describe male attitudes; black movements have sought to disarticulate the historical meanings of 'black' from 'despised' and 'backward' to 'beautiful'. This is because, as Volsinov (1973) explains, almost all concepts and words are multi-accented. The problematisation of meaning is not the result of some functional reproduction in the world of language, but of a social struggle in which particular elements are brought together to achieve a mastery in discourse. The struggle is not over the word itself, but over the meaning which it connotes. The struggle is also about the way a meaning is put together, terms of the debate, the institutions, their control and the agenda. Each meaning is the result of particular power relations in which economic, political and social antagonisms play their full part (Mouffe, 1979). Each accent has further consequences as it invokes a different chain of connotations, ideological associations and clusters of other meanings which affect specific classes and social forces. Each meaning has to be constructed and articulated in the language reflecting the social organization of the participants involved and by their position in any social formation. The meaning can never be finally fixed because the hegemony of the ruling bloc is never complete and because it is relational and thus cannot be stabilised (Laclau and Mouffe, 1985).

In times of relative social stability, a dominant bloc tends to reproduce its relations through traditional channels and because of its dominance succeeds in neutralising its contradictions by displacing them, or making them relatively less visible (Laclau, 1977). However, in times of acute crisis, the Janus-like character of social practices and concepts becomes more visible. Periods of rapid historical change exacerbate the ever present ideological contradictions and a dissolution of the unity of the dominant ideological discourses follows. Depending on the strength of the competing groups, old ideas may be forcibly broken. At such times, the existing power bloc is weakened and may resecure its hegemony by adopting a competing meaning, which was previously perhaps secondary or subordinate (Gramsci, 1971). As ideology constitutes individuals and provides 'identity', the ideological crisis also creates an identity-crisis for social agents. During such times, there is the possibility of the deployment of radically new discursive formations and the elaboration of new philosophies. As part of this, various competing sectors will try to create a new ideological unity by disarticulating the ideological discourses of their opponents. Laclau (1977) argues that an ideological unity does not depend on logical consistency, but rather on the ability of one interpellation to persuasively evoke or connote other interpellations. Following this, for the dominant bloc, one possible way of resolving the crisis is to accept one interpellation, explore its logical implications and use it as a critique of the existing system and at the same time as a vehicle for reconstructing its ideological domain. The ideological struggle takes place not by substituting one meaning for another, but by shifting the accent which a particular concept carries in a discourse. The struggle makes full use of symbols of authority, historical heritages, rituals, flags, myths, the ISAs and the State. Laclau (1977) suggests that the more central the role of a particular sector is in the particular social formation, the more central will be its role at the ideological level, at least in the resolution of the crisis or that part of the crisis which relates to its domain. How this struggle will be resolved depends on the historical contexts and the nexus of relationships involving various centres of power.

2.1.3: A Connective Summary and Discussion

So far, this section has provided the foundations of the methodological framework for this thesis. A 'realist' framework which avoids the errors of reification and voluntarism has been advocated for understanding the changing meanings of the going concern concept. Individuals are not seen to be determined by society and society is not seen to be created by individuals. Full recognition is given to the actions of individuals, but within a social context. Throughout, it has been argued that social structure and practices are changed through contestation and struggle. The extent of this struggle is dependent on human subjectivity which is shaped by competing ideologies. The classical 'false consciousness' thesis advanced by Marx and Engels has been rejected. Instead, ideologies are seen as 'real'. It has been argued that there is a connection between the 'economic' and subjectivity in which particular roles are played by the State and the 'Ideological State Apparatuses'. Such structures help to form the 'common sense' of the masses and provide a basis of reproducing and/or transforming society. Along classical Marxist lines, a society is seen as 'relational' which provides the basis for advancing competing discourses and ideologies. Such struggles occur around the meanings of words and concepts whose meanings define social relations, power and the means of making sense of social existence. The accent of concepts is not changed without political and ideological resources.

Critical realism is committed to explaining the way the social world is structured and changing and that this ultimately is a matter of theoretical and empirical investigation. In this context, it is clearly stated that this thesis will borrow heavily from the ongoing Marxist research programme. In accordance with such traditions, it is clearly assumed that there are centres of power and that discourses do have a strong economic content. In addition, this chapter has given considerable weight to the role of ideologies (which have a material existence), the State and 'Ideological State Apparatuses' in reproducing and transforming society. Such connections are, however, denied by Foucault (1977, 1979, 1980, 1982) and others. Therefore, before considering further aspects of this chapter, it is appropriate to answer such critics.

Many scholars criticise much of the economic reductionism of Marxist thought. However, in escaping economic reductionism, they have emptied society of all economic contents and have given little specific consideration to the mode of production or class. In distancing themselves from Marxist thought, some critics have abandoned all concern with ideology and its role in the political struggles and transformation of society. Instead of the problematic notion of class ideologies we have now moved in the opposite direction where the image of,

> "great, immovable class battalions heaving their ascribed ideological luggage about the field of struggle ...... is replaced ..... by an infinity of subtle variations through which the elements of a discourse appear spontaneously to combine and recombine with each other, without material constraints of any kind other than provided by the discursive formations themselves" (Hall, 1983, page 79).

Foucault is reluctant to attribute a social source to discourses and power. In Foucauldian texts, power is dispersed because of the theoretical perspectives adopted. As Hall (1980) puts it,

> "His 'power' is dispersed precisely so that it cannot, theoretically, be traced back to any single organizing instance, such as the 'state'. It voids the question of the economic precisely because it cannot, in his view, be crystallized into any set of global relations - e.g. class relations" (page 67).

The generalised assertion that "power is everywhere, not because it englobes everything, but because it comes from everywhere" (Foucault, 1979, page 93), amounts to an almost pluralistic concept of power and leaves no space for understanding or analysing any new source or formation of power. Who or what does one critique in order to transform social practices? Which sources of power does one challenge to transform social structures? Indeed, in Foucauldian analysis, it is not possible to move outside discourses to locate any source of power. If 'power is everywhere' then again a question arises what kind of social formations are driving it? Indeed, if this question is pursued in any detail, then one is forced back to consider the more familiar concepts of class, the State and other social antagonisms. Even if one agrees with the Foucauldian insistence that these features are the outcomes and not the origins of a vast number of competing discourses, it does not necessarily follow that they have not been, cannot, or have not become, the sites and centres for the exercise of power and thus perform the functions which Marx, Gramsci, Althusser, Habermas, and others associate with the State and Ideological State Apparatuses. It is hard to believe that discourses can be disarticulated and re-articulated at will without being anchored in some powerful and enduring mode of social formation.

Foucault's work does not offer the emancipatory framework which critical theorists and realists alike seek. Through discourse and criticism all that can be done is to change the balance of power in the present 'regime of truth' and then wait to move from one regime to another. There is no hope of transforming society or removing oppressive structures. The Foucauldian discourses on sexuality, madness, medicine, etc., examine the micro politics of disciplinary regimes, but do not necessarily see any prioritised concern with the economic or ideologies of capitalism, seemingly at times content with ethnocentric and behaviourist rather than relational explanations. However, there is another aspect. Marx and Engels, rather polemically, put forward the dominant ideology thesis and critics do acknowledge the existence of numerous (rather than a single) dominant ideologies, at least for the dominant classes (Abercrombie, Hill and Turner, 1980), each seeking converts for its worlview. In the case of competing discourses, one also wonders whether there is a tacit acknowledgement of dominant ideologies. Are the discourses not trying to shift some dominant meaning of say 'gay', 'black', 'feminism', etc.? If the discourses do succeed then they become dominant ways of normalising social relations. Indeed, this thesis is not the place to analyse Foucauldian texts, but a view remains that Foucault does assume the existence of dominant ideologies.

2.2: THE ECONOMIC AND THE STATE

This thesis, whilst not subscribing to economic reductionism, shares the views expressed by Marx and Engels that in the final analysis, 'the economic matters'. This conception is also supported by critical theorists (for example, Habermas, 1976) and others (for example, Offe, 1984). Following such views, this section focuses on aspects of the economy and the State which are likely to be relevant to appreciating the changing meanings of the going concern concept. Section 2.2.1 focuses upon the role of the 'economy' in creating a terrain of struggle and contestation. The State is actively involved in the reproduction and transformation of society. Its involvement is heavily influenced by the need to manage the inherent contradictions of capitalist economies. Such an involvement further exacerbates the contradictions in a capitalist society and thus creates space for changing the meaning of social practices. Therefore, section (2.2.2) focuses upon the State.

2.2.1: The Economy

In Marxist thought, a capitalist society is seen as 'relational'. As figure 2.5 shows, such a society is marked by the presence of two mutually dependent yet antagonistic classes, namely capital and labour. Capital and labour have a common interest in maximising productivity, increasing efficiency, successfully competing in domestic and international markets and maintaining social stability. But labour, unlike capital cannot be stored and is also more dependent upon capital. Labour is only employed if it serves the interests of capital. Replacing labour with machines or working labour harder and longer are seen as legitimate tactics. A capitalist society is full of tension and conflict as the prime aim is the creation of profits rather than the satisfaction of human needs. It is the "appropriation of surplus value which is the defining feature: the basis of the exploitative relations of production and the condition for the emergence of antagonistic social classes (Johnson, 1980 page 344). In a capitalist system, the owners of capital have an interest in creating economic surpluses for private gain and thus organise production, administrative and legitimising processes (e.g. auditing) to maximise surpluses.

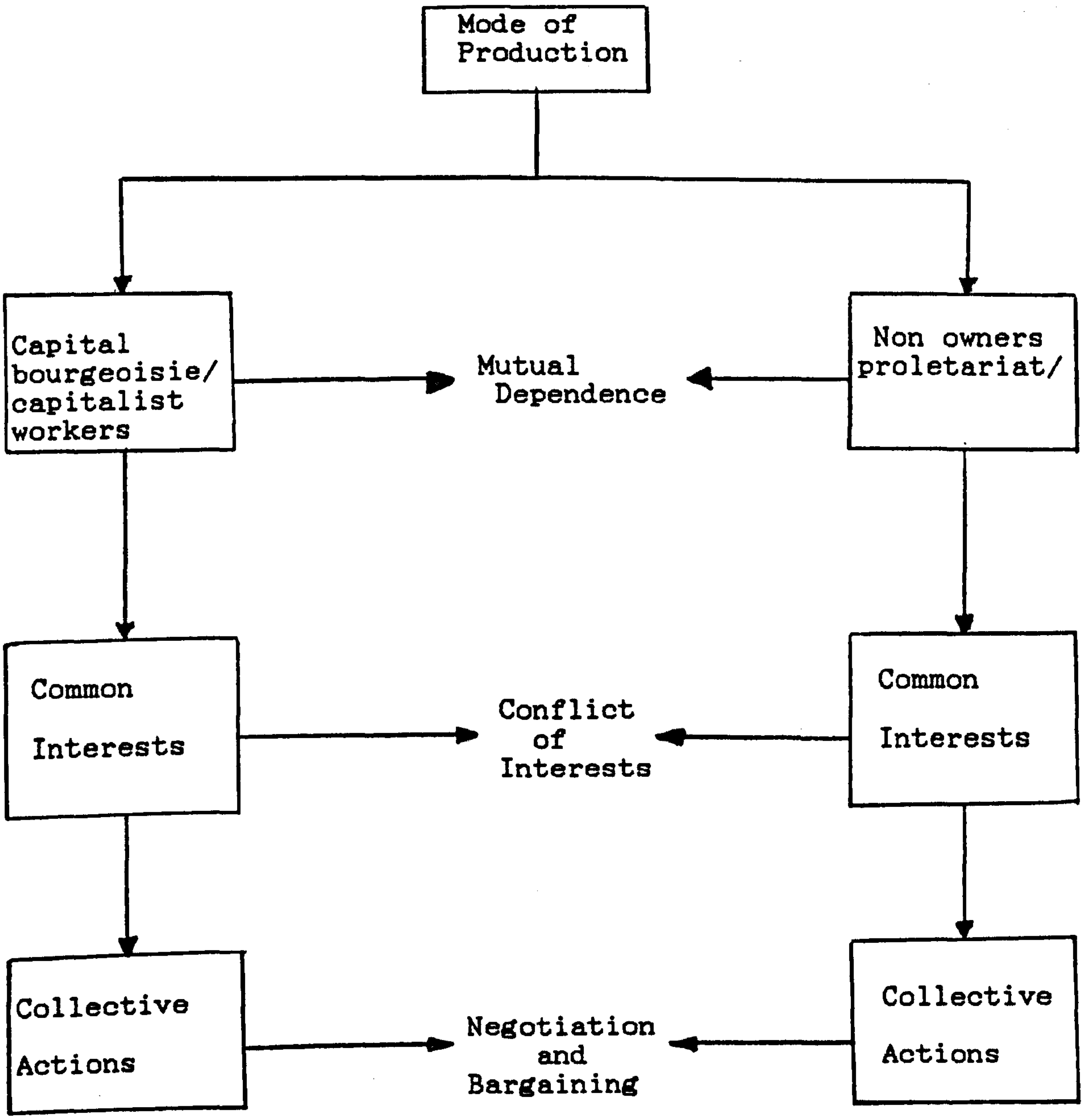


Figure 2.5
A Generalised Description of a Capitalist Society

The capitalist classes may have common interests in maintaining certain arrangements, laws and rules which are conducive to the accumulation and legitimation of economic surpluses. In pursuance of this, they may take collective action to form organisations (e.g. CBI) to protect or promote their interests and negotiate and bargain with the opposing forces. However, capital like other classes is not homogeneous and is made up of numerous 'fractions' such as 'large capital', 'small capital', 'state capital', 'production capital', 'finance capital' and so on (Giddens and Held, 1982). In this context, it is also appropriate to regard accountancy firms as a fraction of capital.

The dynamics of capitalism require each fraction of capital to compete (on unequal terms) with each other for profits, resources, influence, control and markets. The petit-bourgeoisie must either become full scale capitalists i.e. 'large', or risk being driven out. The capitalist competition (pursuit of private rather than common interests) may threaten some 'fractions of capital', yet open up opportunities for others. For this reason, one will find conflicts, localised or global, betwen various fractions of capital.

In view of the inherent tensions, the capitalist economies do not function smoothly and are expected (unlike the Keynesian and monetarist analysis) to be in a continuous state of crisis. This crisis is induced by the disorganised and contradictory nature of capitalism which prevents one economic cycle from necessarily smoothly leading to another (Fine, 1975). Under capitalism, economic growth cannot be sustained in a co-ordinated way. The desire for profitability attracts competitors and drives the profits down. In order to maintain profits firms, as part of their cost cutting drive, push wages down. Such actions result in over exploitation of labour and a reduction in the consuming power of society accompanied by an increase in social conflict. The very success of tactics and strategies of capital ensures that consumers are unable to purchase the goods and services produced with their labour. Higher productivity also causes capital to overproduce. Eventually firms find difficulties in selling all their output. This results in a realization crisis, as happened in the 1930s, which was managed by direct State intervention through the adoption of Keynesian policies. On the other hand, higher wages for labour lead to increased purchasing power, larger markets and a stronger working class. During such times, labour cannot easily be persuaded to accept low wages or increase productivity without additional rewards. This then squeezes profitability and leads, as it did in the 1970s, to an 'accumulation crisis'. An important aspect of the crisis resolution is that such policies create space for the restructuring of capital and restore the balance of class and social relations in such a way that capital can continue its growth. The competition process results in the elimination of some organisations and also leads to monopolies and oligopolies. Crisis management techniques lead to the introduction of new production methods, takeovers, mergers, hunt for economies of scale, efficiency, reorganisation of labour processes and so on. In the need to create economic surpluses, technical solutions are sought and the possessors of appropriate technical skills (e.g. accountants) are handsomely rewarded. Thus capital prepares itself for a new wave of accumulation and crisis. Crises are indeed the mechanisms by which capitalism reasserts itself (O'Connor, 1987).

Capital also needs to replenish and replace itself. In this context, profits are reinvested in larger and newer machinery, thus squeezing the working classes and their purchasing power. As long as profits remain high investment may continue. However, there are contradictions in that once capital becomes fixed, it needs time to recoup the value embodied in it. Any premature retirement due to technological or organisational change robs capital of surplus generating potential and hurls it towards new dangers associated with restructuring and the adoption of new technologies. In addition, as Marx noted, there is also a tendency for the rate of profit to fall. When profits fall, new outlets for capital are found in the lesser developed economies. Capitalists must also innovate in the field of technology, transport, communications, etc., to stay ahead of other fractions and increase the rate of profit. At such times, the various cost-cutting approaches may increase the rate of profit, but they also alter the balance in social relations of power. This affects not only the relations between capital and labour, but also amongst various fractions of capital.

The falling rate of profit to some extent may be countered by the creation of a 'reserve army of labour', something which helps to discipline the rest of the workforce. The existence of a 'reserve army of labour', whilst increasing class antagonisms, creates space for restructuring industrial relations and a competition for wages amongst the working classes for employment, thus enabling wage costs to be pushed down and profits to be increased. The existence of a 'reserve army' also enables many organisations to expand at the time of economic booms without doing injury to the scale of production in other spheres. Capital restructuring essentially results in the premature phasing out of inefficient businesses and hence a loss of value embodied. The above, accompanied by the processes of bankruptcy ensures that the weaker capital is cannibalised by the stronger ones. This sharpens conflict, but results in the distribution of economic surpluses to fewer capitals, thus increasing the average profitability in an economy (Fine and Harris, 1976). In the process of restructuration, industry shifts geographically seeking favourable conditions. Further divisions in social labour to form new administrative and organisational structures occur. Related unemployment and other symptoms of economic crisis may threaten legitimacy of the social system. In the face of a continuous crisis, a need for a considerable variety of institutions, (e.g. the State and the ISAs) which institute counter tendencies exists.

The overproduction of capital and insufficient demand for goods and services also requires a credit system. Indeed, inadequate supply of money, inappropriate financial structure and tight monetary policy can become a barrier to the expansion of commodity production. In a modern complex economy, the credit system has become a major source for organisational and technical change, coming to the aid of the accumulation process (Harvey, 1984, chapters 9 and 10). The use of credit tends to make matters worse in the long run because it can deal only with problems that arise in the exchange and never with those in production. Amongst other things, credit generates erroneous price signals to producers.

The overextension of credit also becomes a source of 'liquidity crisis' (O'Connor, 1987) and causes periodic business failures, leading to centralisation and concentration of capital in large and more productive, but fewer capitals. During such crisis, financial institutions are usually willing to lend money to large firms only and smaller businesses are starved of finance (Wilson Committee, 1978). Such policies inhibit accumulation and further speed the centralisation and concentration of capital.

The credit system also confers power to financiers who are independent of the production processes. The financiers act as intermediaries for the 'moneyed class' and the 'industry capital' must approach them for finance. This centralisation gives them great power and enables them to cannibalise some 'fractions of capital' for quick gains and interfere in the operations of other capitals. In order to protect the interests of its class, 'finance capital' indulges in speculation, either of good fortune or disaster. Such actions are also the basis of the conflict between the interests of 'finance' and 'production' capital. As a leading industrialist (quoted in Grant and Marsh 1978, page 69) puts it, "There is a false assumption that all businessmen have common interests. Yet to me it is patently obvious that the interests of manufacturing business and City are sometimes not coincident". Despite the interlocking and interdependent nature of capitalist organisations, historically, 'finance capital' has held a privileged position in Britain (Ingham, 1984). Its privileged position has enabled it to protect and promote its interests at the expense of industry and agriculture (O'Connor, 1987, page 22), thus further speeding the creation of monopolies and concentration of capital. In addition, as the monetarists notice (Friedman, 1962), excessive increase in credit money is also a prime source of inflation. Inflation may initially be welcomed by capital in that it assures a continued profitability, but eventually it devalues capital and makes accumulation difficult.

The monopolies and oligopolies caused by the dynamics of the capitalist system take away incentives to be efficient and result in misallocation of resources. Monopoly control enables capital to be a price-maker rather than a price-taker and thus undermine the allocative efficiency of markets. Monopolies acquire a powerful position in an economy because numerous customers and suppliers rely upon them. Managers of large corporations can easily switch capital from one country to another in order to generate a stable rate of profit, but their actions may have a negative impact on other businesses. The managers of such corporations are seen as pursuing their interests rather than pursuing the interests of capital in general and may thus give rise to demands for regulation of monopolies.

In view of the appropriation of surpluses by a select class, a capitalist society is marked by an unequal distribution of wealth and power. "Such inequalities are sustained by processes that are created in the normal operations of the economy. Cycles of economic activity, systematically, though not mechanically, affect political strengths and personal fortunes of the major class groupings" (Clegg, Boreham and

Dow, 1986, page 388). The inequalities in wealth and power put relatively few groups and individuals in a powerful position (McCarthy, 1984). The elite groups have become institutionalised and effectively plan the economy and national affairs (Miliband, 1969). Such groups pursue their interests by operating an effective system of domination and coercion which enables them to dominate critics and opponents (Giddens and Stanworth, 1974).

To sum up, this section has referred to a model of society in which economy is the epicentre of crises. The capitalist economic system is full of tensions between capital and labour. Furthermore, the capital class itself is not harmonious as it is engaged in a continuous pursuit of profits. The capitalist mode of production ensures that conflict and tension, rather than peace and harmony are the norm and provides a platform for struggle and contestation for the reproduction and transformation of social practices.

The next section shows that the State agencies try to manage the crisis tendencies of capitalism, but in so doing they themselves become enmeshed in contradictions of capitalism. Consequently, the crisis tendencies are dispersed into the social and political spheres as well, creating space for reproduction and transformation of social practices.

2.2.2: The State

The concept of the State[7] is difficult to define and has continued to be highly problematic for scholars (Althusser, 1969; McLennan, Held and Hall, 1984; Dunleavy and O'Leary, 1987). Most scholars recognise that the State is not a monolithic and unified entity. It is more than the government, civil services, Parliament, the judiciary, police, army and other obvious organisations. A capitalist state is best seen as a series of part-bureaucracies which try to maintain particular social relations. One thing that many scholars (for example, Poulantzas, 1975; Habermas 1976; Offe 1984) agree on is that the State cannot be considered apart from the economy. It is part of a particular social formation - capitalism - and is implicated in the transformation and survival of the capitalist mode of production.

The State needs revenues to survive and perpetuate itself, but the dominant ideologies of capitalism make it uncomfortable for the State to be directly and openly involved in the processes of production. In such circumstances, the State has to rely on the revenues from taxation on the capitalist mode of production, which is mainly in the private hands. Because of its dependence on the capitalist mode of production, the State cannot and does not permit the market system to operate unhindered. It will intervene, plan and organise capitalism to manage the crisis tendencies in a variety of ways (Poulantzas, 1975). It indeed has been a sponsor of modern corporations (Lindblom, 1977) and has encouraged accumulation by granting legal status and privileges to capitalist entities through Royal Charters and limited liability statutes.

The need for State intervention arises because the capitalists are assumed to be 'myopic' and more concerned with short-term rather than the long-term goals. In pursuing short-term goals, they may overlook the common interests of their class and may not pay adequate attention to the long-term factors relevant to their survival and prosperity. They may overexploit labour and cause harm to long-term productivity or fail to make adequate concessions to the working class in order to instil long-term environmental stability. This myopic view and the crisis tendencies of capitalism not only threaten the State, but also the social stability necessary for capitalism to flourish (Offe, 1984). The State finds it necessary to institute counter-tendencies and maintain social cohesion by intervention and has to manage or displace the crisis through material as well as ideological processes (Habermas, 1976). It can best promote the long-term interests of capital not by being at the beck and call of capital, but by being 'relatively autonomous' (Miliband, 1983).

The State promotes the long-term interests of capital through selective intervention (O'Connor, 1973), adjusting government spending to stimulate demand, welfare programmes, pursuing appropriate taxation and fiscal policies to prevent financial collapse, aiding industry, tinkering with statistics (e.g. unemployment rates), passing legislation such as fixing minimum working hours, concealing information from Parliament, promoting likeminded regulatory agencies and co-opting professions (including accountancy profession) and assumed technical experts into decision-making (Gilb, 1966). If the circumstances permit, the State will also redistribute wealth to create conditions conducive to accumulation. In order to encourage accumulation the State may fill gaps in the market by providing collective commodities and by bearing the costs of education, health, infrastructure etc (Gough, 1978). The State's aid is effectively based on using future tax revenues today. Such revenues may, or may not be received in the future, but their utilisation today can cause capital to both over and underproduce. The State cannot win favour with all fractions of capital simultaneously. Following the 'New Right' philosophies, it may promote efficiency, productivity, competitiveness and the alleged superiority of private regulation (Green, 1987). It may promote research in areas, where the private sector is reluctant to become involved. The State has become a guarantor of capitalism by providing finance, grants, export aid and sponsoring merger waves and legitimacy. Thus the State is seen as a promoter of the long-term interests of capital (Offe, 1984).

If the working class strength prevents capital from accumulating surpluses, the State acts as a 'safety valve' and will even legislate to reduce the working class resistance. Against the wishes of the employers, the State reduced the length of the working day (Muller and Neususs, 1978). In 1974, the British State managed a crisis by granting concessions to the striking miners. However, since the mid-1970s the rate of profit of the British industry had been declining and any further concessions to the miners did not appear to be in the long-term interests of capital. In 1984 when the energy supplies were plentiful and dispersed and the working class strength much less, due to the existence of a huge 'reserve army of labour', the State did not make any concessions (Wilsher, MacIntyre and Jones, 1985). It appears that concessions are only made if they are conducive to the long-term interests of capital.

The State also forms a particularly special relationship with 'large capital' since it represents a publicly visible image of social stability, wealth and economic growth. Because of its dependence on the capitalist mode of production, the State cannot allow the major enterprises to be liquidated since that will threaten the social cohesion and order. As Held (1980) quotes,

> "Today, many enterprises in industry and banking have grown so gigantically, that no state power, no matter how liberally it behaves [that is within the terms of reference of laissez-faire economics], can stand by and witness their downfall. Above a certain size of capital, the enterprise may continue to claim profit(s) for itself, but the risk is unrolled [passed on] to the mass of tax-payers, since its collapse would bring about the most severe consequences - both for the body economic and political situation" (page 57)".

The 'bailing out' of businesses also helps to postpone the crisis in the economic by relocating it in the 'social' and 'political' (Habermas, 1976). The State intervention allows inefficient capital to survive and reduces the average rate of profitability as well as sending incorrect pricing signals to the markets. This, however, also creates space for capital to restructure and once again begin accumulation by a variety of mechanisms. A consequence of State intervention has meant that it has given more and more legal backing to restricted competition and monopoly control of the markets (Friedman, 1962). Such monopolies are also part of the ideological apparatuses in that they seek to tell others of what is good, right and possible (McKinlay, 1973; Dingwall, 1983).

The State's actions may affect different 'fractions of capital' in different ways and may thus result in conflict between the State and some groups. For example, through regulatory agencies, the State may pursue actions designed to enhance public confidence in capitalist enterprises, yet some capitalist enterprises may resent the reduction in their revenues caused by the State's actions. In order to increase the capital's chances of raising finance, the State may compel it to regularly publish audited accounts (e.g. under the Companies Acts), yet some fractions may complain on the grounds of cost and revealing information to competing interests.

The State becomes implicated in the reproduction of social relations conducive to accumulation. It has to perform functions which cannot effectively be carried out by individual capitals. It reconstitutes individuals through education, media and ideology to make them more compliant. As Johnson (1980) notes, "The state, in centralising and formalizing processes of reproduction, such as education, creates a labour force less tied to local and particularistic cultures; sharing in a common (yet hierarchially organised) formal socialization process" (page 362). The recessions engineered by the State's monetary and fiscal policies promote capitalist ideologies of competition and work and a compliant and uncritical workforce (Armstrong, Glyn and

Harrison, 1984).

The co-ordination of a huge bureaucracy also creates administrative problems. Some times it is not clear which symptom of the 'crisis' needs to be tackled first. Should the priority be to tackle unemployment, inflation, exchange rate, manufacturing output, job training, burden of taxation or something else? The Departments of the State may themselves be adopting contradictory positions. Due to the contradictions of capitalism, rationally consistent policies cannot be adopted. The State itself is clearly not monolithic. It is staffed by elites (Miliband, 1969) who operate a filter system, favouring the interests of particular groups (Offe, 1984) and find various financial, institutional and ideological means for promoting particular interests. Due to its increased involvement, the State also becomes more bureaucratised. Its officials (e.g. civil servants) have career ambitions and consequently want to appear in the right light. Such individuals develop various rules, 'risk avoidance' strategies which persuade them to build alliances with the assumed experts (Benveniste, 1977).

To be effective, the State apparatus must give the appearance of being knowledgeable. In doing so a complex bureacratic structure is created which then favours a few 'insider groups' who acquire a consultative status with the aim of promoting particular interests. The State also comes to rely on organised business interests for policy-making options. As Miliband (1969) puts it, "Large scale business enjoys an advantage inside the state system, by virtue of the composition and the ideological inclination of the state elite" (page 23). Even if the dominant groups have no legal status, their definitions of matters such as education, auditing, accounting, health, justice, deviancy, financial soundness, etc., come to dominate policy-making (Johnson, 1982). For example, the report on the collapse of the Vehicle and General Insurance Company (House of Commons Report, 1972) shows that even though the company's poor financial health had been noted by civil servants some years before the collapse, this was concealed from the general public. What eventually mattered was whether or not the representatives of finance capital would agree with the conclusions reached. Indeed, Ingham (1984) argues that in view of finance capital's ability to finance wars, trade, booms and government deficits, its interests have received a more privileged treatment. Finance capital has developed ways of protecting interests in such a way that the State can not easily interfere with it for the fear of precipitating panic and a massive financial crisis.

Capitalism has come to rely on the support of the economically powerful organisations and individuals. Indeed, it creates a kind of dependence on the powerful who could hold back, discipline, punish and reward as and when necessary. In order to survive the State has to win and renew social legitimacy. In order to appear legitimate it must promote itself as being a neutral arbiter (Dahl, 1982) and a weathervane of public opinion. In order to manage the crisis, the State seeks popular support, e.g. through elections, but actually grants monopolies to minority groups. As the elite theorists argue, the State favours a few powerful groups and consequently relatively few citizens are able to influence policy choices (Giddens and Stanworth, 1974). This privileged treatment of a group (e.g. a profession), initially resulting from the manner in which production is organised, leads to an unequal distribution of wealth, influence, power and control and becomes another site for the social struggle. The reliance on assumed experts and the related privileges tilt the power positions in favour of social and political elites who end up exercising significant influence on society and form unelected mini private governments (Gilb, 1966).

The State's actions, designed to help capital, can cause an oversupply of money whose value is then devalued and leads to inflation. The devaluation erodes the value embodied in capital. Increasingly, the State itself has become a site for social struggle and for the promotion of various interests (Poulantzas, 1978). The very success in managing or displacing crises becomes a source of crisis for the State (Habermas, 1976). The State's success creates an expectation that it can deliver almost anything and the State gets sucked into issues of accountability (Berry et al, 1984), industrial relations (Hopper at al, 1986) and other areas previously outside its influence. As King (1976) commenting on the 1974 sugar shortage in the UK notes,

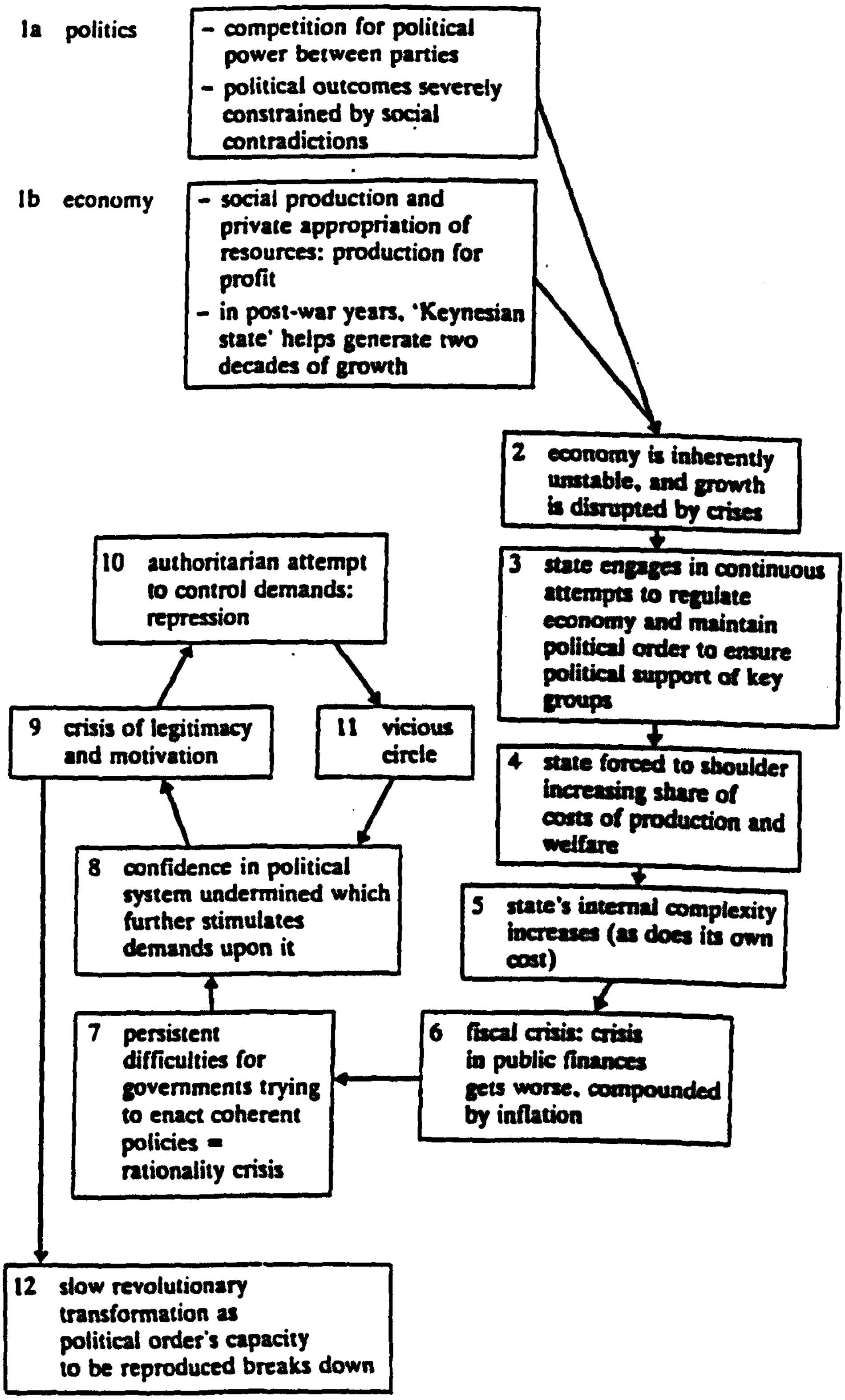
> "The growing of sugar is in private hands; the refining of sugar is largely in private hands; the distribution and selling of it is wholly in private hands. Yet, when there is not enough of it in the shops, we look not to growers, refiners or distributors to solve our problem but to Mr. Fred Peart i.e. to government. During the Irish potato famine, thousands of United Kingdom citizens could

not count on government to give them life; today we expect government to provide us with sugar for our tea" (page 15).

In view of the greater expectations, the government becomes 'overloaded' (King, 1976; Habermas, 1976) and cannot effectively support capitalism and the ideologies necessary for its expansion. The economic crises exacerbate the conflicts of interests between various classes and create uncertainties about the State's claim to legitimate power, especially as the State claims to speak on behalf of the whole society. The economic crises make the State's claims vulnerable by revealing that it acts for particular classes or interests rather than society as a whole. It is seen as failing to deal with the internal chaos and disorder which results from unequal distribution of resources, wealth and power. A 'legitimation crisis' results from the inherent contradictions of capitalism (Habermas, 1976) and creates space for transformation of societies (see figure 2.6). There is no escape, doing less as well as doing more causes problems for capitalism. The State needs to actively intervene in the process of capital restructuring, however inefficiently it does so. Even the 'New Right' wishes to promote the State as an environment smoother, but rather wishes to limit its activities to those arenas which promote the interests of capital (Green, 1987). Caught in a web, the State manages the legitimacy crisis by drastically altering the public sphere. In this context, the public sphere becomes a field of competing interests in which "Large organisations strive for a kind of political compromise with the state and with one another, excluding the public whenever possible" (Habermas quoted in McCarthy, 1984, page 382).

Figure 2.6

Legitimation Crisis of the Capitalist State



Source: McLennan, Held and Hall, 1984, page 326.

In sum, the actions of the State are determined by the particular nature of economy and social structure in which it is located. Its actions can best be understood within the logic of capitalism which requires it to regulate and manage conflict not only between capital and labour but also between their various fractions. The State is not 'neutral' as it promotes a particular kind of social order, a capitalist order. The crises are also key periods of social change in that they cause the balance of power to alter.

2.2.3: Section Summary and Discussion

After the initial argument that all discourses have a strong 'economic' content and that in the Marxist traditions, the State is a particular centre of power, this section focused on those parts of the economy and the State which are likely to be particularly relevant to appreciating the changing meanings and interpretations of the going concern concept. It is argued that due to the mode of production, a capitalist society is not a harmonious society. It is marked by competing and antagonistic groups which have common and conflicting interests. Capital itself is further fractionated into numerous fractions which have common and competing interests. Due to the contradictions of capitalism, the economy is in a permanent state of crisis. The availability of credit further distorts the market mechanisms. The unequal distribution of wealth, accompanied by capitalist ideologies gives some groups greater opportunity of influencing policy-making. The relentless pressures to increase profitability, production and efficiency always pit one fraction of capital against another with the result that many businesses attach greater weight to short-term goals. This is where the State can act in the long-term interests of capital by providing collective commodities and by arbitrating in social disputes, thus creating conditions for the reproduction and transformation of capitalism. In view of its 'relative autonomy', the State may make concessions to some groups, or exert pressure on others to modify their policies for the long-term interests of capital. The State's involvement creates social expectations and thus the crisis emanating from the 'economic' also engulfs the political and social arenas, creating a legitimation crisis. In order to manage the crisis, numerous crisis management tendencies are instituted which create reliance on assumed experts and results in alliances with unelected groups. Such groups become 'insiders' and a major influence on State policies. This means that power also resides in numerous private interest governments, each of which seeks to legitimise a particular meaning of social practices.

2.3: LOCATING ACCOUNTANCY PRACTICES AND PROFESSION

The purpose of this section is to locate the accountancy profession and practices in the framework developed in section 2.2. Within the framework of this chapter, accounting and auditing practices are seen to exist in social contexts which shape their developments and meanings. Overall they cannot escape their shaping by the dominant modes of thought and influences of major centres of power. These were identified as the 'economic' and the State.

Until recently, in the functionalist traditions, much of the literature on professionalism continued to focus on what many scholars regarded as the characteristics or 'traits' of a profession (Greenwood, 1957; Elliott, 1972; Millerson, 1964; Montagna, 1974; Previts, 1985). These included attributes such as command of knowledge, codification of practices, independence, ethics, autonomy, discipline and many other items. Based upon the self-images of a profession, each scholar produced a list of whatever constituted a desirable characteristic of profession and then the debate proceeded to decide which profession fitted this idealised list. The self-images, as part of an ideological armoury, may help professions to maintain their cohesiveness as a distinct entity. However, such an approach lacked connections between professions and modes of production, social formations and the centres of power (Saks, 1983). The new critical approaches borrowed from the Weberian and Marxist traditions to problematise and question the very processes by which professions attained their status and maintained it. Now the professions were seen as collective movements controlling markets and securing niches through monopoly control, social closure and technical division of labour (Larson, 1977). The professional institutions came to be seen as reflecting the inequalities of society and relying upon patronage from the economically powerful for continuation of their privileges (Friedson, 1970). In this movement, scholars also made use of the ongoing Marxist research programme and came to analyse professions in terms of their links with the capitalist mode of production. Professionalism was no longer the consequence of some idealised characteristics but a consequence of "social power" (Johnson, 1980, page 345). Within the themes pursued in this chapter, it is this connection with modes of production and centres of power which forms the context for locating accountancy practices and profession in a social setting.

The social concern with accounting arises because it helps to reproduce ideological and political relations in a society. More specifically, within the dynamics of capitalism, accounting is "viewed as functioning in relation to a specific and determining historical process: the appropriation of value and the accumulation and concentration of capital" (Johnson, 1980, page 359). In a capitalist society, with the emphasis on profit, competition, market share and efficiency, the process of appropriation requires that all surplus value be accounted, allocated and distributed. In this context, accounting performs the function of "watching over capital, of checking and controlling the process of its enlargement" (Johnson, 1980, page 355).

In advanced capitalism with large scale organisations, capital tends to become centralised and concentrated. In this context, three functions assume particular significance for the survival of capital: that is the appropriation, realisation and reproduction. Taken together these constitute 'global functions of capital' and are essential for the perpetuation and survival of capital (Johnson, 1977). Such processes require significant input from accounting and auditing in key decision-making aspects and also give accountants a position of power in organizations and society (Armstrong, 1985). The performance of the 'global functions of capital' is considered to be a major reason for the privileges, monopolies and status of accountants in society (MacDonald, 1984). Through accounting, organisational processes, decisions, allocations and distributions are made visible. In view of the separation between control and ownership, the financial calculus is also of interest to absent owners, since it has an impact on the measurement of their wealth. The accountancy practices and profession is closely identified with internal controls, surveillance, accounting to risk bearers and legitimation of disclosure of absent owners and other providers of finance. Thus accounting methods and disclosures assume political significance and become implicated in conflicting discourses and struggles.

Accounting has a continuous role to play in capitalist economies. For example, it is used to restructure capital, encourage accumulation and create a 'reserve army of labour' (Bryer and Brignall, 1986). Accounting is used not only to construct poverty and prosperity of capitalism, but also to encourage belief in efficiency, private profits, property rights, competition and other capitalist ideologies (Hines, 1988). Accounting has played a part in restructuration and stagnation of capital in times of peace and war (Loft, 1986). Accountancy indeed functions as a medium of social control and change (Burchell et al, 1985). In order to reproduce social power relations, accounting is promoted as neutral, factual and objective rather than subjective and socially constructed and a promoter of particular interests and classes (Roberts and Scapens, 1985).

The previous sections also argued that a capitalist society is a fractionated society in which each class competes with other classes. Such competition creates antagonisms and conflicts which then become the basis for transformation of practices. The accountancy profession cannot be immune from such influences. The position of accountancy firms is no different from that of 'capital' in general, in that, in accordance with the capitalist ethos, they need to reduce costs, increase labour productivity and increase profits. Therefore, various accountancy firms have common interests in finding ways of achieving such obectives. They may prefer certain technologies and social arrangements which make pursuit of accumulations possible. However, large firms also have advantages in terms of economies of scale, finance and clientele which threaten the small and medium firms and are thus capable of driving them out of business. The partners in smaller firms can either compete with large firms in the hope of becoming full-scale capitalists, or be driven out by the larger firms. The competing interests of various firms give rise to conflict and tension. Such a conflict may result in each 'fraction' preferring different policies. For example, small and medium sized accountancy firms would like to retain small company audits, especially as this opens the door to lucrative non-auditing services. On the other hand, large firms are unable to perform small audits economically, but would like to win a greater share of the non-audit services market. Therefore, they advocate abolition of small company audits. Small firms provide book-keeping services to their clients and large firm partners claim that such services compromise auditor independence; whereas large firms provide management consultancy to large companies and small firm partners claim that such services compromise auditor independence (Firth, 1980). The common and competing interests of firms need not just be confined to such issues, but may also extend to other areas. For example, the various meanings of the going concern concept may have different implications for firm clientele and profitability and thus force firms to articulate different positions.

In section 2.2, the State and the ISAs were identified as important and pivotal centres of power for numerous discourses. The accountancy profession and the State are best seen as interdependent. In this relationship, each is seen as enabling and constraining the other (Johnson, 1982). Indeed, at times the accountancy profession, through its authority to set accounting and auditing standards, acts as though it is part of the State apparatus and adjudicates amongst the various fractions of capital (Puxty et al, 1987). The State has to rely upon the revenues from the capitalist mode of production for its survival and perpetuation. In order to do so it has to manage the contradictions of capitalism by instituting crisis management mechanisms and build alliances with various organisations which would help to promote the long-term interests of capitalism. The accountancy practices, amongst other things, enable the State to regulate, monitor, legitimise and support capitalist enterprises. The provision of independent and reliable audited information helps the State with the collection and forecast of tax revenues. It may also help the capital markets in allocating scarce resources yet avoids the scrutiny of the mode of production. The profession is seen as an ally of the State in helping it to smooth the path of accumulation by providing independently attested information (Jones, 1981) which not only reduces the costs of providing information, but also encourages and reinforces beliefs about the fairness of information disclosure policies by capitalist enterprises.

In view of the economic and ideological functions performed by accountancy practices and the profession, the State has nurtured the accountancy profession through Bankruptcy Acts, statutes (Brown, 1905; Stacey, 1954) and by granting monopolies (Larson, 1977). Much of the early corporate legislation was particularly in the interests of finance capital and this provided a vehicle for the accountancy profession (Johnson, 1982; Macdonald, 1984). In the event of bankruptcy, accountancy practices help to salvage capital and make it mobile again, thus affecting the rate of profit. Conventional financial statements are designed to emphasise the rights of providers of finance. Indeed, a balance sheet is best conceptualised as a statement of property rights. In much of the modern literature, investors and creditors are thought to be the main and legitimate users of financial statements (FASB, 1978). The auditing processes legitimise corporate disclosures in financial statements and help companies to raise capital enabling them to reproduce and transform themselves. This connection is still particularly strong and dominant in that the focus of accounting regulation continues to be finance, banks and big corporations (Montagna, 1986). In view of the functions performed by it, the accountancy profession has also managed to win important 'insider' status within the government departments and is in a position to influence legislation and State policies. Such influence also enables it to protect the interests of its members and articulate solutions beneficial to accountancy firms.

The State is clearly a guarantor of markets for the profession, but at the same time there are tensions between the profession and State. The reason is that each has to appeal to different constituencies; the profession to its members and the State to wider society. For its legitimacy, the State may pursue policies which may be considered to be detrimental to the interests of the profession. The conflict can be illustrated through recent episodes. For example, the State in 1975 wished to promote a particular kind of inflation accounting (Sandilands, 1975), which conflicted with the variety being suggested by the professional bodies. The professional bodies were willing to promote the version preferred by the State, but the accountancy profession's membership was not willing to support it (Westwick, 1980). However, in the final analysis, the accountancy profession derives its power from the State and had to compromise its interests (Loft, 1986). On the question of inflation accounting, it had to compromise and support 'current cost accounting'. On the one hand the profession wishes to guard its autonomy, whilst on the other it is dependent upon the

State and cannot enhance its legitimacy by completely opposing key policies of the State.

In order to promote its interests, the profession mobilises bias by appealing to the immemorial past and invoking what it claims to be the true inheritance of the profession - the right to self-regulate. In pursuance of such aims, self-regulation is used as a rallying cry and the State is portrayed as a demon (Accountancy, January 1987) in order to mobilise the membership to support the interests of accountancy firms and their clients. The representatives of the State are even derided on the grounds of lack of knowledge (The Accountant, October 1980, page 611). Such mobilisation of bias creates conditions for bargaining with the State and promotion and protection of particular interests (Portwood and Fielding, 1981).

The policies of the State have been the silent shapers of accounting thought and practice. In its quest for legitimacy, the State may raise taxation, give grants, etc., to alleviate unemployment, provide social services and manage balance of payments crises. In its advanced stage, capitalism has to increasingly rely on State support in order to look for new markets and become global. In order to operate beyond international boundaries, capital finds new and exotic ways of reproducing and transforming itself. Such actions pose fresh challenges to accounting thought. To finance investment, capital finds new ways of raising finance through leasing and other methods of off-balance sheet financing. As a result, the accountancy profession has to find a solution to the problem of accounting for leases (SSAP 21) and 'off-balance sheet financing'. The State aids industry by giving grants and capital allowances and altering the effective rate of taxation. As a result, the accountancy methods are needed to find ways of dealing with government grants (SSAP 4) and deferred taxation (SSAP 15). In pursuit of profit, capitalist organisations become large through mergers and acquisitions. Capital seeks out new markets and becomes global. As a result, the accountancy profession has to find solutions for dealing with consolidation of accounts (SSAP 14), mergers and acquisitions (SSAP 23), foreign currency translations (SSAP 2Ø) and goodwill (SSAP 22) amongst others. In pursuit of profits, capital may replace labour by machine and the accountancy profession as a 'gatekeeper of capitalist ideology' has to reveal whether such actions are ordinary or extraordinary (SSAP 6 suggests that they are extraordinary!). In order to manage the crisis tendencies, the State initiates price controls, wage controls, output controls and exchange controls, all with the aid of accounting. The crisis tendencies and the State intervention causes class antagonisms and sets up one capital against another. The accountancy profession and practices reflect such shifts. It transforms and is transformed by the crisis (Hopper et al, 1986). The various meanings and interpretations of the going concern concept are unlikely to escape the influence of the State.

The accountancy profession, practices and concepts are also implicated in class conflict in a society. Production capital may well like to disclose the minimum possible information to investors, whereas 'finance capital', in order to pursue its profits, may like greater and more frequent information. The disclosures may be detrimental to the interests of 'production capital' yet be beneficial to 'finance capital'. The State may have to arbitrate, but the eventual interpretation of policies and disclosure requirements is still down to the auditors who become implicated in this conflict. In view of its reliance on economically and politically powerful groups and corporations for its status and privileges, the profession cannot afford to antagonise such groups (Johnson, 1977). Accountancy firms are thus forced to make compromises with their clients and accomodate the demands of their clientele and expect reciprocal favours in return. The accountants may also sympathise with the interests of capital because of the material rewards and working conditions enjoyed by them. Most accountants enjoy a high status and levels of income from promoting capitalism (Aranya, Pollock and Amernic, 1981) and may, therefore, have little reason to oppose the development of novel techniques supporting the accumulation process. Most accountants have also spent a large part of their working lives in capitalist organisations (this also includes accountancy firms) and are thus not only habituated in capitalist ideologies, but have also learnt to sympathise with the interests of the appropriate 'fraction of capital'. Commenting on the relationship between accountants and business organisations, Montagna (1986) notes that there is "a market dependency of corporations on the accountant/auditor for good advice and a clean bill of health on their financial statements, and a reverse dependency of the auditor for comfortable fees and support against excessive state regulation". Professional pronouncements may well be reflective of such economic arrangements and compromises. In folklore, auditors are set up as adversaries to the management and protectors of shareholder and public interest, but Barber (1978) has argued that the "accounting firms have aided corporations in deceiving the public and government" (page 610). Public awareness of this can damage legitimacy of the State and may force the State to take steps (formal and informal) to modify accounting and auditing practices. Thus, the extent to which firms may be willing to promote and protect the interests of their clients is dependent upon the extent to which such actions are consistent with the interests of the firms themselves. Any compromises reached also have implications for auditor responsibilities and liabilities. Thus the profession may prefer certain accounting and auditing choices. At one level, the conflict between various fractions of capital (Laughlin and Puxty, 1983, 1984) influences accounting discourses, yet at another, in view of their reliance upon corporate patronage, auditing firms may be willing to make compromises, as long as this is consistent with their own long-term interests. Rather than revealing its sectional interests, the accountancy profession mobilises consent by arguing that it promotes and serves the 'public interest'.

Throughout this chapter, it has been argued that the social world is differentiated and relational. The accountants and the professional bodies themselves exist in a structured world and reflect different social constituencies and interests. Accountants work in the public, private and non-profit making sectors. Some are partners in large firms, whilst others are partners in small and medium sized and small firms. Some hold managerial positions in industry and commerce, whilst others (possibly a majority) perform routine tasks in accountancy firms and industry. Each is subjected to different economic clientele and thus different pressures from their employers. Such pressures create antagonisms and opportunities for transformation of practices. Through their membership of major regulatory agencies, some accountants may be seen to be acting on behalf of the State (Puxty et al, 1987). Such positions may give some accountants a privileged access to the policy-making apparatuses and an ability to pursue private interests, something which may be resented by other accountants. In view of the social inequalities, the policy-making committees may not reflect the broader interests of accountants, or the general mass of public, who the profession claims to serve. Such conflicts become a source of tension and may affect the shape of accounting discourses and with it the meanings of concepts such as the going concern concept. The various fractions, represented on the regulatory agencies and important Committees, may come to operate a negotiated order under which they make concessions to each other. The conflict may be reflected through the conflicting meanings of the going concern concept.

This section has located the accountancy profession and accountancy practices within the nexus of the capitalist economy and the State. The accountancy profession and its practices exist in a society which is marked by inequalities in distribution of income, wealth and power. These are constructed and sustained through the aid of accounting processes and techniques. The State is implicated in such inequalities. It maintains a particular social order by using accounting practices and by relying upon the profession to assist it in smoothing the environment for accumulation. Following the discussions of section 2.1, this section argued that neither the profession nor the accountancy firms ought to be seen as harmonious entities. Instead, it is argued that there is conflict and tension between firms, which is likely to influence a particular interpretation of accounting principles and practices.

2.4: Chapter Summary and Discussion

This chapter has provided the framework within which the changing meanings and interpretations of the going concern concept will be explored. Within the context of the arguments of this chapter accounting and auditing are seen as a social practice and thus cannot escape the wider social, political and economic developments. The meanings of the going concern concept are elaborated by individuals, but they all presuppose certain social relations of power, modes of production and structures.

Concepts such as the going concern are unlikely to arise spontaneously. Each meaning is unlikely to be new. In talking about the concept, various institutions and writers are likely to indulge in a two fold activity, namely reproducing and transforming the meaning. In explaining the various meanings of the concept, particular attention needs to be paid to historical processes which shape accounting thought and practice. The meaning which various writers assign to the concept will reflect various developments and antagonisms in a society. There is no neutral position which any author can adopt in any discussion of the concept. Each meaning of the concept is likely to be a modification of the existing and previous meanings. The meaning assigned will depend upon the extent of ideological contestation and struggle in society.

It is quite likely that some meanings of the concept may have become deeply embedded in accounting thought and thus form the 'common sense' view. Such meanings are likely to be contradictory, conflicting and episodic, frequently reflecting a residue of historical processes, folklore and myth. Such conflicting meanings are likely to help some groups to make sense of their existence and for them they would be 'real'. Although on epistemological grounds, one may challenge some meanings, the point remains that such preferred meanings may be serving the interests of some dominant group. It was argued that in view of struggle and contestation, the hegemony of a dominant group is unlikely to be complete. Therefore, some competing meanings will always seek space, either by displacing the older ones, or by making a subordinate meaning the dominant meaning. The changing meanings and interpretations may be articulated by the State, various institutions and intellectuals. In the world of accounting, institutions are the prime means of transmitting meanings and are promoters of sectional interests. They produce, perpetuate and popularise meanings of the going concern concept through education policies and professional magazines. Each meaning, whilst appearing to be logical, will invoke a cluster of other meanings and may overall contain contradictory elements.

Due to ideological contestation and struggle, the social structure is differentiated and changing. Various fractions of capital and accountancy firms of differing sizes have economic incentives to shape the meaning of accounting and auditing practices. Therefore, the concept cannot have any fixed or unambiguous meaning. The going concern concept, like all other social concepts, is likely to be multi-accented. The meaning of the concept will depend on the discourses into which it has been inserted by powerful groups. Such meanings require mobilisation of bias and the shaping of beliefs. The accent invoked will depend upon the resources of the competing groups and their ability to invoke particular interpellations and connotations. The very struggle over the meaning will be rooted in the historical contexts.

The chapter argued that there is a connection between ideas and class interests. Therefore, particular attention will be given to the class(es) which are shaping and influencing the meanings of the concept. It is possible that the meanings assigned may promote and protect some class interests. Such classes are unlikely to be homogeneous and thus conflict and tension will be the norm amongst them. This conflict and tension is a major motor for transforming the meanings of the going concern concept.

Following Marxist insights, it has been argued that in a capitalist society there is always a connection between discourses and the 'economic'. The various interpretations of the going concern concept are unlikley to be an exception to this, that is not to say that the other elements are ignored, rather that the 'economic' is prioritised. Accounting is seen as aligned with the interests of capital. Therefore, as and when the economy goes through various stages of acute crisis, the technologies which sustain the economic calculus are also likely to be scrutinised to ascertain whether they are delivering the required amount of legitimacy. In this sense, one would expect greater concern with accounting and auditing processes during times of acute economic crisis.

It is significant that much of the accounting literature also prioritises the 'economic'. Historically, accounting developed under the influence of economics and remained highly focused on the questions of 'economic well-offness' (for example, Edwards and Bell, 1963; Chambers, 1966). The very definitions of accounting show prioritised concern with the 'economic'. For example, accounting has been defined as "the process of identifying, measuring and communicating economic information to permit informed judgements and decisions ...." (American Accounting Association, 1966, page 1). The same organisation then went on to define it in 1975 as "information which is potentially useful for making economic decisions ......" (American Accounting Association, 1975). FASB (1978) argues that financial reports "should provide information about the economic resources of an enterprise ......". Intellectuals (for example, Solomons, 1978; Zeff, 1978) also see accounting as the financial expression of 'real economic phenomena' which has 'economic consequences'. Such images of accounting are to be found in numerous books and are promoted as being 'real' through the education processes (for example, Hendriksen, 1982; Underdown and Taylor, 1985). Such approaches to accounting are reflective of social structure and relations of power in which the 'economic' is prioritised. They form the 'common sense' way of thinking about accounting and thus constrain and enable the possibilities for change. The going concern concept is part of the broader thinking about accounting and is unlikely to escape such influences.

Due to the crisis of capitalism, the State itself has become enmeshed in contradictions of capitalism and places considerable reliance on accounting processes to enable it to support capitalist accumulation. The State cannot be neutral in discussions of accounting and auditing. It is likely to take an active part in shaping developments to support the long-term interests of capital.

The above discussions provide the framework within which this thesis will investigate the changing meanings and interpretations of the going concern concept. Towards this end, within a theoretical context, the empirical evidence is provided by analysis of literature covering a period of more than one hundred years; interviews with twenty one auditors, three directors, two liquidators, five current and past government ministers[7] and senior civil servants and the interpretations of replies to an eight page questionnaire.
The remainder of the thesis now operationalises the framework elaborated in this chapter.

Chapter 2 Footnotes

1) This is a broad generalisation. In his publication 'The Elementary Forms of Religious Life', Durkeheim (1965) does display anti-positivist tendencies.

2) This is a broad generalisation. There are non- and even anti-individualist tendencies in Weber's work (see the volume by Gerth and Mills, 1948).

3) In Gramscian thought, hegemony relates to the way one class successfully achieves its objective of providing the fundamental outlook for the whole society. It is not imposed, but is achieved by a combination of intellectual, moral and philosophical leadership.

4) Lukes' (1974) 'third dimensional' view of power comes close to the 'realist' and Gramscian view of dominance and power, though there are some tensions. These are discussed in Clegg (1989).

5) Traditional intellectuals are those

> "whose position in the interstices of society has a certain inter-class aura about it but derives ultimately from past and present class relations and conceals an attachment to various historical class formations" (Gramsci, 1971, page 1).

6) The 'organic' intellectuals are

> "the thinking and organising elements of a particular fundamental social class. The organic intellectuals are distinguished less by their profession ...... than by their function in directing ideas and aspirations of the class to which they organically belong" (Gramsci, 1971, page 1).

7) In analysing the State, much of the attention is frequently directed on government, but this need not ignore other support agencies. For a review of the various theories of the State, see Dunleavy and O'Leary, (1987).

8) Held (1980, page 57), quotes from F. Pollock 'Die gegenwartige Lage des Kapitalimus und die Aussichten einer planwirtschaftlichen Neuordnung' [The present situation of capitalism and the prospects of a new planned order], Zfs, vol. 1 (1932), and 'Bemerkungen zur Wirtschaftskrise [Observations on the economic crisis] Zfs, vol. 2 (1933). Both essays are reprinted in his Stadien des Kapitalismus.

9) These were:

Tony Benn, the Secretary of State for Industry 1974-75.

Peter Shore, Secretary of State for Trade 1974-76.

Edmund Dell, Secretary of State for Trade 1976-78.

Stanley Clinton-Davis (now Lord), the Parliamentary Under Secretary of State for the Department of Trade 1974-79. He was directly responsible for regulating accounting and auditing for all of those years.

John Redwood, Minister for Corporate and Consumer Affairs (September 1989 to the time of writing). Throughout the discussions, John Redwood was accompanied by his three senior Department of Trade and Industry (DTI) civil servants, one of whom has been the DTI's representative on the Auditing Practices Committee.

Separate discussions were also held with three other senior civil servants who had particular connections with the accountancy profession and have also been responsible for drafting many of the DTI's consultative papers on regulation of auditors.

PART I

Chapter 1 noted that this thesis consists of two broad layers. The first layer consisting of chapters 3 and 4 examines the various meanings and interpretations of the going concern concept. Chapter 3 focuses upon the meanings which various authors and institutions have assigned to the concept from the late nineteenth century to 1985. Chapter 4 focuses upon the meanings which the practitioners have attached to the going concern concept. In this layer, little attempt will be made to explain the particular meanings and interpretations of the concept in any institutional, structural, political, ideological or sociopolitical context. Such tasks will be undertaken in the second layer of the thesis and covered in chapters 5,6,7 and 8. Such explanations cannot begin until the meanings of the concept are investigated.

CHAPTER 3

HISTORY OF GOING-CONCERN

3.Ø.: Introduction

This chapter begins the first layer of the thesis which is concerned with the meanings and interpretations assigned to the going concern concept. The primary emphasis is upon the implications of the concept for auditors. However, in doing so, the interdependence of accounting and auditing is recognised. Therefore, both the accounting and auditing literature will be examined. An immediate problem is where to begin the analysis. Chapter 2 noted the timelessness of ideas and historians (for example, Thompson, 1963; Hobsbawm, 1968) have correctly noted that each period is rooted in a previous period. An understanding of the past meanings and practices is esential in order to appreciate the multi-accentuality and various inflections of the concept, especially as most 'common sense' ideas of the present day are made up of the historical residues.

In one sense the search for a starting point is assisted by social developments. One could begin from the period when writings on accounting and auditing became widely available and began to elaborate a particular kind of discourse. However, early accountants were few in number (Cooper, 1886) and tended to receive their training in offices rather than through any organised professional education system (Macdonald, 1984). This aspect restricts the number of early published works which any researcher can examine. As social conditions altered and accountants embarked on their professionalisation project (Larson, 1977), the number of accountants increased, resulting in the launch of 'The Accountant'[1] in 1874 and the creation of a new platform for debate. Its early contents and the extant books provide a starting point for the analysis.

Accounting[2] and auditing[3] are ancient crafts, but prior to the nineteenth century, most English accounting text-books tended to refer to the mechanics of book-keeping or accounting techniques and contained little discussion of accounting principles (for an elaboration of this point, see Chatfield, 1977; Yamey, 1979). Yamey (1956) claims that towards the end of the nineteenth century, accounting literature began to mention accounting principles and conventions. If this is the case, then the late nineteenth century would also be a reasonable place to commence the search for the meanings of the 'going concern concept' in an auditing context.

With the above in mind, this chapter begins (section 3.1) by tracing the early discussions relating to the going concern concept up to the 1930s. This is a suitable point of departure as the period around the 1930s is marked by considerable economic turbulence. This separation may also provide an opportunity to consider (in subsequent chapters) whether economic crisis led to any greater scrutiny of accounting and concern with accounting concepts, such as the going concern concept, or perhaps accounting has a technical logic of its own and develops independently of social, economic and political pressures. After a summary (section 3.1.1), section 3.2. covers the period up to the 1970s. A period which ended with the emergence of standard setting bodies such as the Accounting Standards Committee (ASC). It is also a period in which the going concern concept is formally recognised as 'a fundamental accounting concept' (ASC, 1971; IASC, 1975) and a 'basic feature of accounting' (AICPA, 1970). This period also marks the end of what many economists call the 'greatest economic boom ever' (Harris, 1988) and the start of the biggest capital restructuring in British history. How did this affect the meanings of going concern, especially in an auditing context? After a connective summary (section 3.2.1), the third section (section 3.3) looks at the meanings assigned to the concept between the early 1970s and 1985. This period also includes the formation of a new regulatory body in the UK accountancy profession (the Auditing Practices Committee) and ended with the first formal auditing guidance on the going concern concept. Section 3.3.1 summarises the going concern guideline issued to auditors by the profession, followed by a section summary (3.3.2). Finally, section 3.4 summarises the chapter and refers to its impact on the subsequent chapters.

3.1: GOING CONCERN TO THE 1930s

The nineteenth century witnessed the formal establishment of the accountancy profession in the UK. The Scottish accountants obtained a Royal Charter in 1854 and their English counterparts obtained their Charter in 1880. By 1879 audits had been made compulsory for all banks, but there were no accounting books with any mention of going concern. By 1880, the ICAEW obtained a Royal Charter for excellence, amongst other things in auditing, but still no auditing books appeared on the market. In the wake of increasing interest in auditing, the first English book on auditing, 'Auditors: Their Duties and Responsibilities' written by Francis William Pixley [4] was published in 1881. Pixley's book was written at a time when "the bulk of the legal profession ..... looked upon accountants with ill-concealed dislike and jealousy" (The Accountant, 28th July 1877, page 2) and is almost totally confined to a paraphrasing of the legal aspects of accounting and auditing. Pixley (1881) did not make any direct reference to the going-concern concept, but some of his contemporaries did.

In a lecture given on 2nd April 1883, published in The Accountant on 21st April 1883 and entitled 'Depreciation and Sinking Funds', Edwin Guthrie[5] referred to 'going concern' in the context of depreciation and valuation. The main aim of the paper was to discuss interim valuation (i.e. for interim or annual accounts as distinct from valuation when businesses are bought and sold) of assets and depreciation without any actual conversion into cash. Guthrie (1883) was adamant that realisable values were not appropriate for any interim valuation of assets and businesses. He argued that

> "Manufacturers and traders do not construct business premises or lay down special plant in the intent of a short period. ....A large, irrecoverable outlay is expended in the preparation of a factory, and unless speedy destruction overtakes any certain business, the method of treatment for annual accounting is as of a "going concern." Manifestly the career of the business contemplated must have

an assured term, and the cost of the consumption of machinery and other erections must be attributed to the whole term assumed.

For fuller occasional satisfaction, prudent manufacturers will periodically call in professional valuers .... Every valuation so taken for the purpose of the proprietor's account should be made with regard to normal cost rather than to the value on the day of valuation. Matters and things fixed in a permanent working position must not be treated in account as following the fluctuations of the market, for it is not a trading item ...... which can be sold any day without interruption to the works. Such a valuation is for purpose of check" (Guthrie, 1883, page 7).

The whole tone of Guthrie's paper makes it clear that he is concerned with values for balance sheets. He considered original cost less depreciation to be a good proxy for what he regarded as current value or a 'going concern value' and that periodic valuation could provide a check on this figure.

Harris (1883) in a follow up to Guthrie's paper noted that there are two methods of carrying out an interim valuation of a business. Assets could be valued on the basis of a 'going concern' or on the basis of 'break-up' values. These meant knowing whether the valuation was to be based on "what the property would be worth if purchased with the intention of working it exactly as it stood without interruption or displacement; or is it to be valued on the basis of what it would fetch if offered for sale in the ordinary way" (page 9). Taking his cue from Guthrie, Harris wrote,

"I think that the valuation should be on the basis of a going concern without reference in the least to the normal cost, which ought to have no influence on the figures whatever. If it happens that the normal cost, and the amount of subsequent valuation, show, after allowing for wear and tear, no material

> differences, then it is very satisfactory as a kind of test of the accuracy of the re-valuation, but this should, I think be looked at merely as an accident, a coincidence. The value obtained on the day of valuation for going concerns is, I think, the only sound and safe way of determining the amount" (Harris, 1883, page 9).

Harris also referred to a paper by Mather (1876). Mather's paper was entitled "Depreciation in relation to the Audit of Accounts" and did not contain any direct reference to 'going concern'. However, in view of the reference by Harris (1883), it is reasonable to assume that Mather's paper, in Harris' mind at least, had implications for 'going concerns'. Mather (1876) thought that an audit certificate implied that "nothing charged to capital was valued above its cost; ..... no ordinary repairs had been charged to plant; ..... when the item of depreciation was omitted or seemed insufficient, he [auditor] had received explanations which would satisfy him ...... whatever be the explanation, the omission or apparent undercharge [of depreciation] should be specifically reported, if it was proposed to pay a dividend on the basis of accounts in question" (page 6). On the principle of valuation, he stated that the "simplest and broadest principle for regulating the value and depreciation of plant might be said to be its known capacity under normal circumstances to produce profit, subject, however, to its cost being fixed as the maximum value" (Mather, 1876, page 6). The adherence to costs was also supported by Bogle (1889), who believed that all fluctuations in value should be ignored and excluded from the balance sheet.

One of the earliest and perhaps the most detailed discussions of 'going concern' can be found in Lawrence Dicksee's[6] book 'Auditing: a practical manual for auditors', published in 1892. Dicksee, is credited with establishing "more than any other man ...... the continuity assumption as a meaningful accounting concept" (Chatfield, 1977, page 235). Dicksee wrote about the phrase 'going concern' under the heading 'Principles in Valuation of Assets'. He believed that the "primary object of most ordinary undertakings was to continue to carry on operations, it is but fair that the assets enumerated in a Balance Sheet be valued with that end in view" (Dicksee, 1892, pages 117-118). Dicksee differentiated between three kinds of entities; Parliamentary Companies, private traders or businesses that were inseparable from their proprietors and companies with perpetual succession established under the Companies Act 1862. The Parliamentary Companies were required to operate a double account system (see Kitchen, 1974; Edwards 1985, for a discussion), maintain their assets perpetually and show them at cost. Therefore, the question of fluctuating values was not thought to be relevant for their financial statements. In the case of private traders, Dicksee argued,

> "It is true that the business may, and frequently does, live longer than its founder; but to do so, involves a change of proprietorship, and what is this?-a <u>revaluation of assets</u> (emphasised in the original). It will thus be seen that there is no necessity to consider the contingency of liquidation (at what are expressively known as "knock down" prices) not merely the contingency must be faced, but the eventual certainty of a re-valuation. The basis of such a valuation will be that currently known "as a going concern" (page 119-120).

On the meaning of the phrase 'going concern', he wrote,

> "So far as it possesses any definite meaning-for, of necessity, the term is an elastic one-the qualification implies "at such a value as they [the assets] would stand in the books if proper depreciation had been provided for"-the term depreciation being taken to represent the amount by which the value of an asset has become reduced by effluxion of time or wear. A fluctuation in value caused by external circumstances will also require to be taken into consideration when property changes hands." (Dicksee, 1892, page 120).

Dicksee appears to have thought that the 'registered companies' having a perpetual succession are entitled to be considered theoretically permanent and that the principles of double account might be applied. His principles of valuation were that assets should be valued on the assumption that the business intended to continue in operation - remaining a going concern and, by considering the legal requirement on distribution of dividends. Fluctuations in the value of 'permanent assets', unlike the 'floating assets' were not to be shown in the profit and loss account (page 121).

In 1904, in the 6th edition of his 'Auditing', Dicksee insisted that the "primary object of most undertakings is to continue to carry on operations' .... the assets enumerated in the balance sheet should be valued with that end in view" (Dicksee, 1904, page 208) and that 'going concern' implies at such a value as they [assets] would stand in the books if proper depreciation had been provided for" (page 210). But an additional paragraph relating to secret reserves and distribution of dividends appeared to support valuations. He wrote, "if ..... a profit has been made which is not available for distribution, it is often considered unnecessary to modify the accounts so as to disclose the circumstance. .... As a rule, the amount at which all assets are stated in the Balance Sheet, except where a special statutory provision to the contrary obtain, should be regulated-at all events to some extent-by the value of such assets" (Dicksee, 1904, page 211).

By 1907, in the 7th edition of his book, the same paragraph read that "...... As a rule, the amount at which all assets are stated in the Balance Sheet, except where a special statutory provision to the contrary obtain, should be regulated by the <u>realisable value</u> (my emphasis) of such assets on the basis of a going concern" (Dicksee, 1907, page 201). In the same book, he now explained 'going concern' as

> "at such a price as a willing purchaser would be prepared to give ......[but] the asset should be written down from time to time to provide effectively for depreciation" (Dicksee, 1907, page 199).

In the 9th edition of his book published in 1912, Dicksee repeated the earlier text and argued that a balance sheet was not prepared to show the debenture holders and mortgagees the minimum value of their security upon being wound up. In relation to fixed assets he noted that,

> "so far as these assets are concerned, so long as it is reasonable to assume the continuity of the business, the correct thing is <u>not to attempt to show the realisable value</u> [my emphasis] ......" (Dicksee, 1912, page 194).

These conflicting paragraphs[8] continued to appear until the final edition of his book in 1928. Dicksee and his contemporaries were writing at a time when the courts also had an opportunity to consider the meaning of the phrase 'going concern. In one of the earliest legal references to 'going-concern' in the case of the County of Gloucester Bank v Rudry Merthyr Steam and House Coal Colliery Company (1895), Lindley L.J. interpreted it in a literal and 'common sense' manner, i.e. a business which was still thriving and going: in this case in accordance with the terms of a lease and reasonably expected to keep going for the whole duration.

Costs were regarded as the main basis of valuation by other writers as well. Reid (1897) rejected the use of market values by arguing that "Market value is not a fair test ...... in the case of assets not intended to be realised .... A going-concern valuation would afford a fair test; but valuation unless taken with a deliberate regard to cost, and of course actual condition and usefulness, may also mislead" (page 158).

The Accountant also joined in the debate. An editorial comment associated 'going concern' with the recovery of outstanding debts and prevention of losses. The same editorial argued that:

> "In the first place, it [the balance sheet] may be regarded as a summarised list of balances .... in the second place, assuming that the books have been properly and fairly kept, it will automatically follow that the Balance Sheet will give a fair and reasonable account of the financial position of the undertaking as a going concern" (The Accountant, 21st April 1900, pages 361-365).

Dawson (1900) equated 'going concern' with adequacy of capital, solvency and valuation of assets by reference to historical costs. The debate on 'going concern also had implications for auditors. Without invoking the concept of going concern, Dickinson (1902) noted that the most important features of an independent audit were the "verification of assets and liabilities in the Balance Sheet, the determination of proper and adequate rates of depreciation".

The Accountant (4th December, 1909, pages 676-677) argued that "liquid assets are necessarily valued for balance sheet purposes having regard to their realisable values, because their realisation in the near future has, naturally, to be contemplated. Fixed assets, on the other hand, are not for realisation in the ordinary course of business, but to be used in their existing form. So regarded, they represent - for balance sheet purposes at least - not so much tangible property capable of being sold for a stated sum, as expenditure, which for the time being at least, may properly be capitalised instead of being charged at once against profits". It concluded that the valuation of fixed assets at cost less depreciation "........ provides a quite intelligible reason for disregarding fluctuations in realisable values at intermediate periods". In such a debate, Pixley in a letter (The Accountant, 4th December 1909) commented that the balance sheet is

> ".......... nothing but a collection of the debit and credit balances of the ledgers. .... the debit balances of the ledgers are supposed to be reduced, where necessary by what is known as "depreciation", before such balances are taken out, leaving them at an amount which is considered to be their value, having regard to the fact that the company is a going concern" (pages 699-700).

The topic of 'going concern' had not clearly excited all of the contemporary authors. Books by Cutforth[7] (1908 and 1910) were also examined for this study but contained no discussion of 'going concern' or its association with asset valuation and depreciation. Some authors also opposed the use of historical costs for valuing assets. In a letter to The Accountant (1st January 1910) a Mr. E.M. Carter insisted that,

> "........ the correct basis of value for assets is their market value. Apart from plant, machinery and goodwill, there are comparatively few important exceptions to the general rule that assets should be stated in the Balance Sheet at their market value" (pages 12-13).

In a subsequent letter (The Accountant, 22nd January 1910, pages 126-127) Carter clarified his ideas by arguing that a business must maintain its original capital, but insisted that from the investor's viewpoint valuation based on market value is justified. Dickinson (1913, pages 80-81) argued that asset valuation based on original cost is misleading and recommended periodic valuations, with the

> "....... resulting increase (or possible decrease) being taken up as a special credit or debit to profit and loss account (or surplus) and shown as entirely distinct from operating results" (pages 80-81).

Dickinson may have been echoing the thoughts of Garcke and Fells (1893, page 103) who had already recommended that assets should be revalued and that appreciation be credited to a capital reserve. It appears that in subsequent years Dicksee (1915, 185-186) also had some sympathy with the suggestions of Garcke and Fells.

P.D. Leake (1912) thought that "if all the assets and liabilities are stated at their true going concern values, the balance sheet will show the nearest possible approximations both to the appropriate value of the capital, and to the amount of the profit or loss arising within the year" (page 3). But, the contemporary views on valuations were not necessarily shared by other groups. For example, Bauer (1913), an economist, criticised accountants for holding a "pretty rigid cost theory of value" and described this position as "extreme". He advised the accountants to use replacement costs. However, despite such criticisms, orthodox views continued to dominate. F.R.M. de Paula[10] (1912) wrote,

> "The particular plant is held as a fixed asset, and is not with a view to re-sale, but with a view to earning income by the use thereof during its working life. Therefore, as a going concern all that is necessary and all that is essential is that the net cost should be written off over the working life" (pages 905/906).

Writing in his 1914 book, de Paula wrote,

> "......fixed assets ...... are not held for the purpose of re-sale .... the valuation of such assets is a matter of estimate and personal opinion .... [but] there is no true profit unless the original capital ..... is intact" (de Paula, 1914 pages 68-69).

> "Fixed assets are valued upon the basis of cost, and if such assets are of a wasting nature, the original cost price in most cases is written off to revenue, by means of depreciation over the period of the estimated working life .... this represents the present value of such assets to the particular undertaking as a going concern, or in other words, the value of such assets to the proprietors of the particular business. Current market value and break-up value are

disregarded, as these do not affect the working lives of particular assets at all. Fixed assets are not valued upon their saleable value, but upon their value to the proprietor of the business ...." (de Paula 1914, page 70).

He recommended (page 71) that floating assets should be valued upon the basis of cost or market price, whichever is the lower. He advised that "On no account should floating assets be valued above cost price" (page 72), but argued that stock should be valued at the 'lower of cost and market value' rule. The auditor's task, he stated, is "to ascertain as far as possible that such valuations appear to be fair and reasonable, and that they are based on correct principles" (page 73). On page 94 he notes "Plant and machinery is not valued upon the basis of its realisable value" and recommends its valuation based on cost less deductions for depreciation.

In the 11th edition of his book on Auditing, published in 1918 and many years after the 1900 Companies Act introduced audits for limited companies, Pixley wrote:

"when the word "value" is used in connection with the amounts placed ...... on the ..... Balance sheet it must not be understood to represent what that item would realize if offered for sale in an open market. It represents what that item is believed to be worth to the concern or individual owning it, having regard to the fact that the owner is what is technically known as a 'going concern' " (Pixley, 1918, Page 501).

In an attempt to make sure that the reader was left in no doubt, he added

"...... 'going concern' ...... has no relation whatever to current or market values" (page 502).

He also repeated these views in the 12th edition published in 1922. From the views expressed in his books it also appears that secret reserves for continuing businesses were justified as they prevented outsiders from learning about the company's affairs. In his view

> "Many companies have passed away which would probably at the present moment be in existence had they been provided with a Secret Reserve.
>
> ...... the Directors have not to consider the interests of individual shareholders or even a group of shareholders, their business is to preserve the capital of the Company and keep it in existence as a going concern, and if a Secret Reserve is created to this end they are, undoubtedly - from a financial and commercial point of view - jusitified in so creating it" (Pixley, 1918, pages 518-520; 1922, pages 537-539).

Elsewhere, Pixley (1922) wrote that it was the directors duty to keep the capital of a company intact and ensure that it becomes a permanent institution (page 413). But Paton (1922) equated going cocern with the use of market values.

Reflecting perhaps, the conventional wisdom, Spicer and Pegler (1925) wrote that

> "if all the assets were valued at the moment they are expected to realize if the business is expected to close down, a heavy loss would necessarily be shown. This method therefore is not adopted, but the valuation is made on the basis of the going concern ...... Floating assets should not be valued above cost, ... the proper basis being cost, market or realizable value, ... which is the lower (page 343-344).

Littleton (1929) criticised the 'lower of the cost and market value rule', but Cutforth (1926) noted that "the assets will, of course, require to be valued on the footing that they form part of "going concern" and not at the amount which they would be expected to realise on being sold piecemeal" (page 28).

Whilst accounting writers were discussing the meaning and implications of going concern, a 1921 banking dictionary explained the meanings which bankers assigned to the concept. Here the meaning was a 'common sense' one and indicated

> "an undertaking which is in full working order. The value of, say, an ironworks as a going concern is usually far removed from the value of the same property when working operations have ceased. In the latter case the value is often not much more than that for old material. When taking any such security, a banker is therefore careful to remember that its value as a going concern may disappear entirely at the very time when it may be necessary to look to the security for repayments" (quoted in Strachan, 1985, page 65).

Indeed, Roy Kester (1924) argued that bankers were concerned with market values and this should be the basis of balance sheet values. However, Leake in his 1923 book 'Depreciation and Wasting Assets', continued to reflect traditional views. He wrote,

> "The common commercial view of the economic value to a going concern of plant in use is based upon the unexpired capital outlay on that plant, computed by deducting an equal annual instalment from the cost, less the estimated residual value, in respect of each year of the estimated efficient life which has expired ...." (Leake, 1923, page 171).

Couchman (1924) advocated the use of original costs fearing that depreciation based on a figure in excess of cost would reduce profits and increase product costs. The recording of values was considered to be cumbersome (page 42) and realization values had "no place in the ordinary balance-sheet" (page 43). After suggesting, three balance sheet valuation bases, he concluded that "of the three bases ...... only one is capable of accurate determination and that is the amount which the assets have cost the organization" (Couchman, 1924, page 45).

Rorem (1928) in a chapter headed 'The common rules of accounting valuation' explained that the going concern concept justified the use of cost less depreciation for fixed assets, lower of cost or market for current assets, maximum value for liabilities, non-recognition of unrealised gains and conservatism in accounting. For Rorem the going concern concept meant that the assets

> "of an enterprise will all be used in the manner intended; for example, that merchandise will be sold within the usual period of time, that supplies will be consumed in normal operations, and that plant and equipment will be depreciated gradually through continuous service. The going concern assumption is consistent with the facts of modern life, for most enterprises do continue their normal operations for a reasonable period of time and most assets are used in the manner intended by the management" (page 289).

Like his British counterparts, Rorem also acknowledged the existence of two kinds of accounting principles; one set relating to going or continuing concerns and the other relating to non-going concerns. He stated, that "when unusual conditions appear, such as when an enterprise faces the discontinuing of operations, the going concern assumption must be brushed aside to make room for the existing facts" (Rorem, 1928, page 290).

Hatfield (1927) supported the conventional views on going concern by arguing that

> "it is legitimate to continue fixed assets at their cost despite a subsequent decline in their value. But in valuing circulating assets, regard must be had to current values, although there is some question as to whether the market value, even of circulating assets, can be accepted where that exceeds the original cost. This is clearly an application of the principle of the going concern. ....consensus of opinion is against recognizing changes in the value of fixed assets in accounts ..... accountants are, in general strongly opposed to marking up the value of fixed assets, and do not insist that they must be marked down to correspond to current value" (pages 76-77).

However, elsewhere in his book Hatfield also suggested the possible merits of replacement cost accounting. Canning (1929), one of his contemporaries, criticised the accountants' concept of 'cost' and 'valuation' and felt that unlike an economist they had no theory of valuation. He noted that "Accountants have never been given to expressing systematically the hypothesis upon which they proceed" (page 186). However, the traditional views continued to be expressed. In his book 'Balance Sheet Values', published in 1929, P.D. Leake argued that

> "[Going concern value is] the unexpired original outlay on plant computed by deducting from historical cost, less estimated scrap value, an equal annual instalment in respect of each year of the estimated efficient life which has expired (page 11). ...... going-concern values do not often coincide with present selling prices" (pages 11-12).

> The going concern values ...... are not affected in any way by consideration as to the probable cost of replacement, or as to whether the undertaking happens to be earning a small or a large percentage of profit on the real capital employed or by any considerations whatever based on the estimated amount of future earnings" (page 60).

Leake distinguished three methods of valuation which he claimed are in common use (page 14). These were: 1) Going-concern cost-basis, based on the unexpired original capital outlay on plant less a deduction. 2) The then-value, which is to be computed on the sale of business and 3) The going-concern profit basis value, which involved consideration of the degree of success enjoyed and likely to be enjoyed by a business and required consideration of future prospects. Leake regarded alternative 1) as suitable for financial reporting.

The monograph by Kettle (1928) suggested that the auditors qualified the accounts if they were unable to verify the value of properties, debtors and investments, etc., but his specimen audit reports did not contain any direct references to 'going concern'.

3.1.1: Summary of the Early Views on Going concern

So far this chapter has examined the meanings associated with 'going concern' up to the 1930s, in many ways a formative period for the UK accountancy profession. During this period, the professional bodies such as the Institute of Chartered Accountants of Scotland (ICAS) and Institute of Chartered Accountants in England & Wales (ICAEW) obtained

Royal Charters. They were granted mainly for excellence in bankruptcy work, but increasingly auditing was also becoming a major function. As a part of the professionalization project, professional accountants began to discuss the technical aspects of their craft. In this context, references to 'going concern' began to be widespread. The main meanings of the concept are shown in figure 3.1

Figure 3.1

Meanings of Going Concern to the 1930s

IN AUDITING CONTEXT

No explicit discussion.

IN ACCOUNTING CONTEXT

Primary Meanings

Prospect of a long/permanent life
It influences valuation
Justifies the use of historical costs
Cost is the maximum value of an asset
Underpins the need for depreciation
Cost less depreciation = going concern value
Concerned with adequacy and maintenance of capital
Focus on solvency
Floating assets to be valued at 'lower of cost and market value rule'
Stock to be valued at 'lower of cost and market value rule'
Rejects the use of realizable values for fixed assets
Rejects the use of market values
Justifies the use of 'secret reserves'
It had implications for dividends

Secondary Meanings

Market values are appropriate
Justifies periodic valuation of assets
Realisable values are appropriate for assets
Justifies the use of replacement costs

The literature shows that in the early life of the UK accountancy profession, depreciation and questions of asset valuation were firmly linked to the meanings of the 'going concern'. The concept had acquired a 'common sense' meaning. Within the prevailing social environment, it was frequently interpreted to mean a business which had adequate capital, solvency, liquidity, collected its debts, prevented losses and kept 'going'. Such interpretations were put not only by intellectuals but also by the courts and bankers.

Intellectuals such as Guthrie, Pixley, Dicksee, Cutforth and de Paula regarded as 'pioneers' by Kitchen and Parker (1980) and thought to have 'influenced accounting thought more than anyone alive today' (Chatfield, 1977) were all expressing views on the meaning of the going concern concept. Whilst differing in minor ways, they associated going concern values with original cost less depreciation. The resulting figure appears to have been regarded as a good proxy for market values. Most of the authors seemed to reject the use of realisable values in balance sheets and equated going concern with an almost permanent existence. However, it is not clear whether some authors were discussing 'going concern value' or 'value to a going concern'. In the period covered, the going concern concept had also been invoked to justify maintaining capital, use of market values, opposition to market values, use of historical costs, opposition to historical costs, maintaining secret reserves, valuing stock at lower of cost and market value, and valuing most liquid (current) assets at realisable values.

Most of the authors, despite writing books on 'Auditing' had very little to say about the audit implications of the concept. This strongly suggests that either the going concern was not regarded as important for auditors, or perhaps the auditors' duties were inferred from the various accounting interpretations of the concept. In addition, no reference has been found to suggest that 'going concern' was described as 'fundamental' or 'generally accepted'.

Having noted the early meanings of the concept, the next section focuses upon the literature from the 1930s to the 1970s, a period ending with the emergence of the standard setting bodies.

3.2: GOING CONCERN: FROM THE 1930s TO THE 1970s

This section continues to examine the various published works for the meanings assigned to the going concern concept.

In Britain, the period began with references to what by now appear to have become 'common sense' and traditional meanings and interpretations of the going concern concept. For example, de Paula (1933) in the sixth edition of his book, 'Principles of Auditing' continued to refer to the meanings which he had mentioned in his 1914 book. He still used 'going concern' to reject the use of market and realisable values for fixed assets and continued to support their value at a figure of original cost less depreciation (page 75). He also used the going concern concept to justify valuing current assets at realisable values or at the 'lower of cost and market value' rule (page 77) and argued that "...... there can be no true profit unless the original capital, together with any additions thereto, is intact ...." (page 75). The auditors were thought to be mainly concerned with verification of assets and application of correct principles of valuation (pages 77-79).

The same period also saw the publication of books by Pickles (1934) and Rowland and Magee (1934 and 1936). The Rowland and Magee preface stated that the aim was to give the readers "a proper understanding of the principles of accounts", but contained no reference to the going concern concept.

In the USA, by 1932, the American Institute of Accountants (AIA) began to refer to a "body of conventions, based partly on theoretical and partly on practical considerations ...... [and] there is a fairly general agreement on certain broad principles to be followed in the formulation of conventional accounting methods ...... (Zeff and Moonitz, 1984, page 78). In 1936, the AIA declared that the external financial statements were mainly "for credit purposes". It acknowledged "increased emphasis on accounting principles and consistency in their application ....". It referred to "generally accepted accounting principles and conventions" (AIA, 1936, page 1) and added that

> "One of the most important accounting conventions is that the balance sheet of a going concern shall be prepared on the assumption that the concern will continue in business. Plant assets, permanent investments and intangibles are usually stated at cost or on some other historical basis without regard to present realizable or replacement value.

> Consideration of the accounts of a business enterprise must start from the premise that an annual valuation of all the assets is neither practicable nor desirable for a going concern" (American Institute of Accountants, 1936, page 2).

In Britain, 'Standard Practice in Auditing' approved by the Society of Incorporated Accountants and Auditors was published in 1937 (Bace, 1937), but contained no reference to 'going concern'. F.R.M de Paula (1937), in discussing the valuation of stock, once again invoked going concern to justify the 'lower of cost and market value rule'. Some accountants such as Greenwood (1937), whilst acknowledging that "the ordinary balance sheet is a document relating to a going concern, and not a statement of possible realisation values", nevertheless advocated reform and the adoption of economic values. Such suggestions were considered to be impractical by The Accountant (22nd May 1937, pages 718-719).

The role of accounting and the implications of the going concern concept by now started to attract criticisms. For example, R.G.H. Smails, a Canadian economist, writing in The Accountant on 6th November 1937 (pages 626-629) observed that accounting had "traditions and conventions but not principles ...." and that many accountants had been looking towards economics for a way of developing accounting principles. He also felt that the "balance sheet does not bear a relation to any capital concept .... the accountant has no capital concept as that term is understood by economists". In his 1938 review of the contemporary accounting theory and practice, Sir Ronald Edwards, an economist, noted,

> "There is wide acceptance of the view that

fixed assets are brought into the balance sheet at their <u>going concern</u> (emphasised in the original) value. So far as this writer is concerned, this expression has never received at the hand of an accountant a formulation which could be regarded as logically satisfactory (page 115).

The expression "going concern" is unfortunate in that it is misleading. Accountants, when valuing fixed assets, do not look at the value of the asset to the going concern. This, however, does not make it any easier to say what they do look at ....

.... going concern value is not the value of the equipment to its owner or to any alternative user-it is merely original cost expenditure adjusted in an arbitrary manner" (Edwards, 1938, page 116).

From what Edwards could deduce, he noted that according to the contemporary thinking, "fixed assets must not be valued at a figure exceeding original cost, but depreciation must be written off. No generalisation of the principles of writing off is possible owing to the confusion of views" (Edwards 1938, page 125).

In their book 'The Technique and Principles of Auditing', Binnie and Manning (1938) made no reference to the going concern principle. But Leake now noted that "the question of going-concern must depend on trading results" (Leake, 1938, page 63). He clung on to his earlier views, but now only mentioned two valuation methods. A position which he repeated in the 1943 and 1947 editions of his book. In his 1947 book he noted that "......... the term 'going concern values' i.e. accounting values has a very definite meaning .... Balance sheet values should be strictly confined to true going concern values ...." (Leake, 1947, page 1). On methods of valuation, Leake wrote ~~wrote~~ that

> "...... there are at present, two distinct methods in common use for valuing industrial plant - one being based on historical cost, the other having some regard to expected future benefits. the first method is the true 'going-concern value'. This is the value at which industrial plant should always be carried in the accounts of a going-concern. The second method of valuation may be defined as the 'going-concern profits basis value' .... This is not the value at which industrial plant should be carried in the accounts of a going-concern" (Leake 1947, page 11).

Another instance of sustained criticism of the going concern concept came from Kenneth MacNeal (1939). He attacked what he regarded as a misuse of the theory of 'value to a going-concern'. In his view asset valuations based on original cost had "become a defense for misrepresentation" (page 46). Such valuations mislead creditors, bankers and stockholders and "hopelessly deceived, not only as to the value of the assets .... but also as to the earnings of their company" (MacNeal, 1939, page 48).

He went on to call for changes[11] in accounting practice and advocated the use of economic values in the shape of market values. Commenting on the going concern concept, Paton and Littleton (1940) felt that businesses have a continuous chain of transactions. As a result, they continue for very long periods of time. Thus "liquidation is not the normal expectation; continuity is. The concept of continuity is also important in that it complements and strengthens the earning power. ....." (pages 9-10).

May (1943) described 'going concern' or 'continuity' as an almost essential postulate of accounting (page 49) and stated that for "current accounting purposes depreciation must be based on cost. ...... The historical character of accounting cannot be too strongly emphasised; and attempts to divorce the present from the past in one respect, even when it may be practicable - as, for instance, by substituting a valuation for cost - are often objectionable because they are at best partial adjustments and because they tend to obscure the true nature of accounting" (May, 1943, pages 49-5Ø).

The institutional concern with accounting principles also arose in the UK. In July 1942, the ICAEW created it's Taxation and Financial Relations Committee (TFRC) and began issuing recommendations (non-mandatory) on accounting principles and practices (it issued 29 recommendations between 1942 and 1969). On 19th May 1944, de Paula[12], by then the Chairman of the the TFRC and responsible for developing 'Recommendations on Accounting Principles', gave evidence to the Cohen Committee on the reform of UK company law. His dialogue with the Committee went thus,

> "Would you ...... agree that the balance sheet is a historical document which shows what expenditure a company has made, what provisions it has made, and that it does not attempt in any way to show the realizable value, or in fact the going concern value of assets?
>
> -No, I say it does show the going concern value.
>
> I thought you agreed with the suggestion that the going concern value of the assets is dependent on the earning capacity?
>
> -The going concern value is represented by the cost of acquisition less a proper allowance for wear and tear. As to whether directors have invested capital wisely or unwisely will be shown by the earnings of those assets.

So you are not suggesting that in giving the certificate as to fair value the directors should make any computation based on profits?

-None whatever; simply on what they spend, less a provision for reasonable depreciation of those assets that are wearing out. That is a fair going concern value which, I suggest the directors should confirm.

My difficulty is in the use of the words 'fair value', because a fair value means a different thing, I suggest, to the shareholders than the interpretation you are seeking to put upon it.

-I have said, 'upon the basis of the undertaking continuing as a going concern'; I pin it to that".[13]

The ICAEW's, recommendations avoided any direct mention of 'going concern', but nevertheless contained shadows of what by now had become 'common sense' views. In its statement N9 'Depreciation of fixed assets' (issued 12th January 1945), it noted,

"Fixed assets .... are held with the object of earning revenue and not for the purpose of sale in the ordinary course of business. The amount at which they are shown in the balance sheet does not purport to be their realisable value or their replacement value, but is normally a historical record" (ICAEW, 1945, para 1).

Meanwhile, books such as Rowland[14] and Magee (1946), aimed at giving the students "A proper understanding of the principles of accounts" still contained no reference to going concern. May (1948) argued that going concern underpinned the allocation of costs and thus provided support for practices such as depreciation. However, the 1948 publication 'Balance Sheets: How to read them and understand them' (Tovey, 1948) contained no mention of going concern, but 'Practical Auditing' by Irish, published in 1948 noted that the

> "values expressed in a balance sheet are ...... book values on a going concern basis. They have no relationship necessarily to market values or economic values ....
>
> .... book values are assessed according to accepted accounting principles which rest fundamentally on the concept of a going concern ..... original cost is a basic feature of valuation .....
>
> [The auditor's duty] is to satisfy himself beyond any doubt as to the existence, ownership and correct valuation of all items in the balance sheet ..... Tangible fixed assets are valued at original cost less due provision for depreciation ...." (Irish, 1948, pages 77-79).

The ICAEW in its 'Recommendations on Accounting Principles' still made no direct references to going concern, but its statement N12 'Rising price levels in relation to accounts' (issued 14th January 1949) recommended that "For balance sheet purposes fixed assets should not, in general, be written-up on the basis of estimated replacement costs ......" (ICAEW, 1949, para 20). By 1952, the view expressed in N15 'Accounting in relation to changes in the purchasing power of money' (issued 30th May 1952) was that "Unless and until a practicable and generally acceptable alternative is available, ... historical cost should continue to be the basis on which annual accounts should be prepared" [15] (ICAEW, 1952). Around the same time, an editorial comment in Accountancy (June 1952) noted that "The breakup value of a concern is a purely artificial notion, for it cannot have any practical meaning if the concern is to continue in being" (page 190). "Experience over the years has shown quite clearly that businesses were founded with the underlying idea of being continuing enterprises and most have succeeded in that objective. Even complete or partial changes in proprietorship have failed to disturb this inherent principle of continuity" (page 192).

'Auditing Practice' (Coomber, 1951) and 'Principles of Auditing' by Taylor and Perry (1956) included the procedures for verification of assets and liabilities, but made no explicit reference to going concern.

In contrast to the British profession, the American Institute of Certified Public Accountants (AICPA), singled out three postulates for special attention (AICPA, 1953). One of these was labelled, 'the permanence postulate' and defined as

> "In the absence of actual evidence to the contrary, the perspective life of the enterprise may be deemed to be indefinitely long" (AICPA, 1953, page 19).

By 1957, the American Accounting Association (AAA), stated that:

> "The "going-concern" concept assumes the continuance of the general enterprise situation. In the absence of evidence to the contrary, the entity is viewed as remaining in operation indefinitely. Although it is recognised that the business activities and economic conditions are changing constantly, the concept assumes that controlling environmental circumstances will persist sufficiently far into the future to permit existing plans and programs to be carried to completion. Thus the assets of the enterprise are expected to have continuing usefulness for the general purpose for which they were acquired, and its liabilities are expected to be paid at maturity.
>
> ...... the assumption provides a reasonable basis for presenting enterprise status and performance" (page 2).

In this debate, Storey (1959) argued that the going concern convention is neutral as regards valuation. It merely rules out the liquidation values and requires that the assets be valued according to their intended use. He pointed out that "it is the 'realization convention' which requires valuation of all unrealized assets at cost, whether they be fixed or unsold inventories" (page 237). Goldberg (1960) argued that the concept of continuity depends on successful operations, adequate profitability and return on capital employed.

In 1957 the ICAEW argued that the 'post balance sheet events' (Statement N17) ought to be taken into consideration in the financial statements (ICAEW, 1957), but it still made no explicit reference to the going concern concept. The 12th edition of de Paula's 'The Principles of Auditing', now written by his son, excluded much of the previous discussion on going concern and devoted more space to ICAEW's recommendations on accounting principles. It identified four bases of valuation and one of these was explained as "the amount that an asset cost, when purchased or acquired, less provisions for depreciation since acquisition (known as the "written down" or "going concern value")" (de Paula, 1957, page 77).

Biggs and Davies (1959) advised the auditors to look at the solicitors' correspondence to establish the cost of fixed assets "acquired as a going concern" (pages 9), but contained no discussion of going concern in an auditing context. Whilst accounting books by Pickles and Dunkerley (1960) and Rowland and Magee (1961) aimed at giving the students "A proper understanding of the principles of accounts" (as per the preface) still contained no reference to going concern, a study by Moonitz (1961) disagreed with the definition provided by the AICPA (1953). Moonitz argued that "Going Concern should not be identified with "permanence" .... Permanence means, fundamentally that economic activity of some sort or other will be carried on as long as human beings inhabit this planet. It is, therefore, much too sweeping a concept to serve as a guide to action" (Moonitz, 1961, page 39). Instead, in what the Accounting Princples Board (APB) chairman (Powell, 1961) claimed to be "an authoritative written expression of what constitutes generally accepted accounting principles" (page 28), Moonitz (1961) suggested that

> "Going concern implies indefinite continuance of the accounting entity under scrutiny. Indefinite continuance means that the business will not be liquidated within a time span necessary to carry out present contractual commitments or to use up assets according to the plans and expectations presently held. This view makes the concept a tentative judgement, subject to revision in the future as contractual agreements are changed and plans and expectations with respect to operations shift. ...... the concept has been useful in broadening the scope of accounting beyond the limitations of liquidation value and of strictly construed legal rights and obligations" (page 39).

In his view the concept justified the use of cost for inventories, receivables, buildings, intangibles, etc. Sprouse and Moonitz (1962) further supported the views expressed by Moonitz (1961). In the continuing debate about the interpretations of the going concern principle, Spiller (1964) argued that the principle justified ‘matching’, allocation of costs and added

"...... if evidence exists that an entity will not remain in operation indefinitely, then a different assumption should be selected and different accounting procedures developed from that assumption. Thus we need special accounting procedures developed for concerns in liquidation or bankruptcy contrasted to concerns that are expected to remain in operation" (page 854).

In another research study, Grady (1965) acknowledged that "a large part of accounting practice as well as theory is based on the presumption that the accounting entity will continue in operation and not be liquidated in the forseeable future" (page 27). In common with Moonitz (1961), Grady argued that the going concern concept justified valuation of accounts receivable at anticipated future cash receipts less provision for doubtful debts, use of cost in valuation of inventories, use of cost less depreciation for fixed assets, carry forward of prepaid expenses and intangibles (e.g. goodwill) at cost and recognition of liabilities at cost. In his view,

"Corporate management must view their operations as a continuing process. No enterprise of any consequence could operate from day to day under the cloud of expected liquidation.

...... Indefinite continuance means that the business will not be liquidated within a span of time necessary to carry out present contractual commitments or to use up assets according to the plans and expectations presently held" (Grady, 1965, pages 27-30).

In such a debate, Vatter (1963) argued that "to view going concern as a postulate is to make accounting stand on quicksand" (page 187), but following the traditions established by the AICPA, Metcalf (1964) continued to regard the going concern principle as 'generally accepted'. Helfert (1966) advocated the use of present values and felt that going concern values are dependent on earnings and these consist of "judgements about the quality of its operating management, the age and condition of its physical plant, and the ingenuity and calibre of its technical and marketing personnel" (page 75). Gordon and Shillinglaw (1969) also equated the use of present values with 'going concern values' for the purpose of balance sheet and income determination.

In 1961, the ICAEW started issuing 'Statements on Auditing' ('U' Statements) and by 1977, twenty three had been issued, but none of these contained any direct references to the going concern concept. However, in the same year, a book published by Mautz and Sharaf (1961) argued that 'going concern' is a vital postulate, whose absence would make auditing 'impossible'. The postulate implied that "In the absence of clear evidence to the contrary, what has held true in the past for the enterprise under examination will hold true in the future" (page 42). For Mautz and Sharaf, the "acceptance of this postulate placed important limits on the extent of an auditor's responsibilities and provides a basis for reducing the extent of his obligation to forecast the future and to have his work judged on the basis of hindsight" (page 49).

Around the same time, Edwards and Bell (1961) continued to further the 'economic' associations of the concept by suggesting that for "going concerns current cost data may be more meaningful" (page 109). They, however, added that "other types of cost data, as they may relate both to the possible sale of existing assets and to the purchase of new (presumably improved) assets may provide important and useful subsidiary information for the making of new decisions" (page 275). Despite such views, the Jenkins Committee, established to reform the UK company law, endorsed historical costs as a basis for valuing fixed assets (Edey, 1963).

Hendriksen (1963) contributed to the contemporary debate on price level accounting by invoking the going concern (or continuity) concept. In his view, the

> "continuity of life does not mean that the firm must replace specific assets. But it does mean that the firm should maintain its purchasing power to acquire investment goods. ..... With an assumption of continuity, the relevant purchasing power is the power to purchase investment goods" (page 486).

Contrary to Hendriksen's views, Gynther (1966) invoked the 'going concern concept' to argue that companies need to be concerned with their current costs [16]. In his view, corporate survival was dependent upon awareness of costs which are real and specific to each company (pages 46-49). Chambers (1966) criticised the conventional meanings of going concern and its association with historical costs and suggested that the concept implies the use of exit values [17]. Fremgen (1968) also pointed out the inconsistencies in the meanings attached to going concern and thought that it was not helpful in guiding accounting. Sterling (1968) argued that an orderly liquidation of existing assets and liabilities is the distinguishing feature of companies rather than the static view portrayed by the traditional definition. Sterling did not regard continuity as a desirable postulate because he regarded this as a status-quo assumption and falsifiable and misleading. Lowe (1970) also pointed out that a firm's value is dependent on the plans which its management has for the utilisation of its assets and argued that businesses 'going' anywhere ought to publish details of management plans and controls as a way of highlighting the asset and income store of a company.

Despite the various criticisms, the AICPA (1970) described the 'going concern concept' as a "basic feature" (page 10) of external financial reporting and supported it by adding that

> "The framework of law, custom, and traditional patterns of action provides a significant degree of stability to many aspects of the economic environment. In a society in which property rights are protected, contracts fulfilled, debts paid, and credit banking and transfer operations efficiently performed the degree of uncertainty is reduced and the predictability of the outcome of many types of economic activities is correspondingly increased" (pages 22-23).

Hendriksen (1970, pages 100-101) criticised the association of 'going concern' with historical costs. Yu (1971) argued that the concept is deficient and static in depicting the socio-economic activities of specific entities. In his view going concern as a concept can only apply to the whole firm and not to each individual asset.

In this environment, the UK accountancy profession began to issue accounting standards. Prior to 1971, the UK professional bodies had not jointly issued any accounting standards. However, following the creation of the Accounting Standards Steering Committee (ASSC) in December 1969 and the launch of the accounting standards programme, the profession set about creating what an editorial in Accountancy (February 1971) described as the "whole new terminology [which] may prove to be the beginning of a UK accounting theory - an area in which Britain seems to have lagged well behind the United States" (page 54). As part of this project, the going concern concept came to be defined as a 'fundamental accounting concept' in SSAP 2 (ASC, 1971). The 'fundamental accounting concepts' are those which have "such general acceptance that they call for no explanation in published accounts and their observance is presumed unless stated otherwise. They are practical rules rather than theoretical ideals ...." (ASC, 1971, paragraph 2). In this context, going concern came to be defined as:

> "the enterprise will continue in operational existence for the forseeable future. This means in particular that the profit and loss account and balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operation" (ASC, 1971, para 14).

Having issued SSAP 2 (ASC 1971) and described 'going concern' as 'fundamental', in February 1974, the ICAEW issued a statement S2Ø which argued that there are

> "various bases of valuation in common use such as, 'current open market', 'existing use', 'alternative use', 'depreciated replacement cost', 'going concern' etc. Some of these are suitable for use when valuation is to be incorporated in the accounts of a company, others when merely disclosure is made in the directors' report or chairman's statement. Some like 'going concern', are regarded as unsuitable for use in relation to property assets of a company" (ICAEW, 1974, para 3).

A guidance note issued by the Royal Institution of Chartered Surveyors (RICS) to compliment the ICAEW (1974) statement also argued that "the expression 'going concern valuation' in relation to company property should not be used" (RICS, 1974, para 2). At the same time, the profession continued to invoke the concept to resolve contentious issues. When faced with finding a solution to the growing use of sale of goods 'subject to reservation of title', the ICAEW (see the guideline reproduced in Accountancy, November 1976, pages 81-182) once again invoked the going concern concept (para 13) to justify disclosure.

By the early 1970s, the concept had institutional support in Britain, the USA and other countries[18], but its traditional meanings [19] continued to be challenged. Arthur Anderson & Co (1972) felt that the concept was preventing recognition of changing economic values and recognition of losses and was thus responsible for misleading investors and creditors (pages 40-41). The firm concluded that the going concern concept needs "to be reassessed and should no longer be regarded as fundamental ...." (page 126).

Meanwhile, the 13th edition of Cutforth's 'Audits' (Palmer and Crawford, 1971) did not contain any discussion of 'going concern'. McKinneley (1972) invoked the going concern concept to justify maintenance of real capital and use of replacement costs, but Vickery (1973) contained no mention of the concept.

3.2.1: Going Concern to the 1970s: A Connective Summary and Discussion

In its search for discussion of the going concern concept in an auditing context, this section reviewed the literature for the period from the 1930s to the early 1970s. The concept continued to receive numerous meanings to reflect its Janus-like character. Various authors clung on to the traditional, which by now were the dominant and 'common sense' views. At the same time, some competing meanings were also seeking space. The common and competing meanings of the concept are shown in figure 3.2.

The period began with a re-iteration of the conventional views by established writers such as Leake, de Paula, Dicksee and others. Such views associated going concern with original costs, depreciation, lower of cost and market value rule, solvency, capital maintenance and so on. In the same period, a number of critiques of the concept by economists (for example, Edwards and Smails) and accounting academics (such as MacNeal, Sterling, Storey, Fremgen, Chambers and Yu) began to appear. Within an economic framework, such critiques challenged the traditional views and associated the going concern concept with the use of market values, replacement costs and present values.

By the early 1930s, the going concern concept received institutional support in the USA and began to be acknowledged as a 'generally accepted concept'. This support continued to grow and by 1953, 'going concern' was thought of as one of the three most important postulates of accounting. This recognition continued until the 1970s and if anything has strengthened in the UK by formal recognition of the concept in accounting standards (SSAP 2), in law (Companies Act 1981, 1985) and internationally (IASC, 1975).

Figure 3.2
Meanings of Going Concern to the 1970s

IN AUDITING CONTEXT

Little explicit discussion though Mautz and Sharaf referred to it to justify a 'passive' approach.

IN ACCOUNTING CONTEXT

Became 'generally accepted' in the USA in the 1930s, but not in Britain until the 1970s.

Primary Meanings

Prospect of a long/permanent life
Contractual obligations will be carried out
It influences valuation
Justifies the use of historical costs
Cost is the maximum value of an asset
Underpins the need for depreciation
Cost less depreciation = going concern value
Concerned with adequacy and maintenance of capital
Makes earnings the main focus of accounting.
Concerned with matching costs and justifies allocations.
Advises on valuation of receivables, intangibles and goodwill.
Justifies carry forward of prepaid expenses
Focus on solvency
Floating assets to be valued at 'lower of cost and market value rule'
Stock to be valued at 'lower of cost and market value rule'
Rejects the use of realizable/replacement values for fixed assets
Rejects the use of market values for fixed assets
'Secret reserves' only justified for 'finance capital'.

Competing Meanings

The concept is not very important.

Present values are important
Economic values are appropriate.
Market values are appropriate
Realisable values are appropriate for assets
Justifies cash flow accounting
Justifies the use of replacement costs
Underpins current cost accounting
Underpins constant purchasing power accounting
Management plans should be revealed

Much of the literature covered in the period 1930s-1970s is primarily by American institutions and authors. By contrast, in Britain, the older traditional definitions lingered on and the ICAEW's 'Recommendations on Accounting Principles' made no direct reference to the concept. F.R.M. de Paula in his books and in his evidence to the Cohen Committee held on to his previous views and his lieutenant Stanley Rowland, despite writing books on 'accounting principles', did not make any explicit references to the concept.

By the 1970s, the going concern concept appears to have been firmly rooted in accounting thinking. Various authors invoked different accents and meanings of the concept and inserted them in competing discourses. The meanings were invoked to justify or oppose almost any accounting development, ranging from historical cost accounting, constant puchasing power accounting, varieties of current cost accounting, cash flow accounting, exit values, replacement costs, capital maintenance, inventories, treatment of prepaid expenses, intangibles, stock valuations, write-off of losses, etc. It is notable how the critics of conventional accounting, such as Hendriksen, Sterling, Chambers, Gynther, Edwards and Bell and Lee amongst others, all had to appeal to the Janus-like character of the going cocern concept to justify their preferred alternatives. It is as though anyone proposing any reform of accounting had to appease the concept or the authorities supporting the traditional views on going concern.

Having been accepted as 'fundamental', much of the accounting literature continues to reflect the traditional meanings of the going concern concept (for example, Beckett, 1980; Bedford and Perry, 1973; Blake, 1985; Cameron, Woelfel and Pattilo, 1979; Carrington and Howitt, 1983; Davidson and Weil, 1977; Farmer, 1980, 1983; Fess and Warren, 1984; Finney and Miller, 1968; Gee, 1985; Harvey and Keer, 1983, 1984; Hawkins, 1977; Istavan and Avery, 1979; Kieso and Weygandt, 1977; Lewis and Firth, 1985; Lewis, Pendrill and Simon, 1982; Limmack, 1985; Stilling, Wyld and Guida, 1982). Some authors within the economic frameworks continue to pursue the revised meanings of the concept to justify the use of current costs, cash flow, constant purchasing power and other varieties of price level accounting (for example, Edwards, Bell and Johnson, 1979; Egginton, 1977; Hendriksen, 1982; Lee, 1984; Meyer, 1980; Most, 1982; Whittington, 1983). On the other hand, some books still make no mention of the going concern concept (for example Lafferty, 1982)

There is, however, another major feature of the literature so far examined and which is highly relevant to the overall objective of this thesis. One of the purposes of this chapter was to search for interpretations of the going concern concept in an <u>auditing</u> context, but up to the 1970s such discussions were relatively scarce. With the exception of Mautz and Sharaf (1961), it was difficult to find any writings which explained the possible interpretations by auditors or the manner in which an auditor might approach the work ensuing from this concept. The 'going concern' concept was originally referred to in 'Auditing' books by Dicksee (1892), de Paula (1915, 1934), Pixley (1918, 1922) and Cutforth (1926, 1928), but since then its implications have been confined to accounting books. Indeed, even Dicksee, de

Paula, Pixley and Cutforth framed their discussion in the context of valuations and balance sheet treatment rather than the auditing aspects, even though audits had been compulsory for banks and insurance companies since 1879 and became the domain of professionally qualified accountants from 1948 onwards. This seems to suggest that the auditing aspects were implied from accounting discussions.

In 1958, the ICAEW (statement N18) argued that 'true and fair' implies "the consistent application of generally accepted accounting principles" (ICAEW, 1958) and in 1968 its guidance on 'Auditors' reports: forms and qualification' made no reference to going concern qualification or the concept. The paper by Kettle (1928) indicated the possibility of going concern audit qualifications, but the Auditing Statements (prefixed with the letter 'U' in the ICAEW handbook) issued since 1961 made no explicit reference to going concern. Auditing books such as Bace (1937), Binnie and Manning (1938), Irish (1948), Coomber (1951), Biggs and Davies (1959), Coopers and Lybrand (1966), Waldron (1969), Palmer and Crawford (1971), just to mention a few, contained no mention of the auditing aspects of going concern. The absence of the topic may suggest that perhaps the matter was either not on the professional, political agenda or was perhaps a low visibility issue. Alternatively, the ambiguous relationship between accounting and auditing may have hampered discussion of the auditing aspects. For example, Mautz and Sharaf (1961) note that "Auditing is concerned with accounting .... but [accounting] is not part of auditing .... Auditing must consider business events and conditions too, but it does not have the task of measuring or communicating them. .... [Auditing] is concerned with the basis for accounting measurements and assertions" (Mautz and Sharaf, 1961, page 11).

With the relative scarcity of any discussions of the concept in an auditing context, at least from the late nineteenth century to the 1970s, how then might one go about exploring the auditing aspects of going concern? Such a task becomes more challenging, especially, as in the period up to 1970s, research papers relating to the auditing aspects have been relatively scarce. Are there any publications which might be indicative of the extant auditing practices? A partner from a major international accountancy firm has claimed that auditing standards and procedures used by auditors can be found in "certain recognized textbooks on auditing, e.g. Practical Auditing (emphasised in original) by Spicer and Pegler ......" (Stamp and Moonitz, 1979, page 67). Following such suggestions, the extant auditing textbooks were examined for discussions of the implication of the going concern concept in auditing. The books by Spicer and Pegler (Waldron, 1979) Coopers & Lybrand (Cooper, 1971 and 1979), de Paula and Attwood (1976, 1982), Howard (1972, 1974, 1976, 1981, 1982), Lee (1972), Millichamp (1978, 1981), Thornton Baker (1981) and Stoy Hayward (1983) were examined and found to contain little or no explicit discussion of the auditing aspects of the going concern concept, though most bu now repeated the going concern definition from SSAP 2 (ASC, 1971). This is despite the ambiguities in the meaning and interpretations of the concept mentioned in this chapter. Perhaps, going concern in an auditing context was not as yet considered to be important.

The next section now focuses on the period from the early 1970s to 1985, a period which started with recognition of the concept as 'fundamental' in accounting and ends with the first formal auditing guidance in the UK on the going concern concept.

3.3: GOING CONCERN IN AUDITING - TO 1985

As has already been mentioned, one of the earliest references to going concern in an auditing context is by Mautz and Sharaf (1961), who in their seminal work 'The Philosophy of Auditing' considered the going concern concept to be vital for auditors. It provided the basis for verifying inventories, receivables, fixed assets and internal controls. It influenced the collection and evaluation and audit evidence and enabled the auditor to make predictions about the future of a business by assuming that "In the absence of clear evidence to the contrary, what has held true in the past for the enterprise under examination will hold true in the future" (page 42). The acceptance of the concept placed limits on auditor responsibility (page 49). After Mautz and Sharaf, whose work is regarded as 'the extant theory of auditing' (Robertson, 1984), little reference was made to going concern in auditing, even though the implications of the concept were described as "one of the most serious problems facing the auditor" (Lee, 1982, page 140).

By the late 1960s and early 1970s, it appears that the auditors were issuing going concern qualifications. For example, Price Waterhouse had issued a going concern qualification on the 1968 accounts of Lawes Chemical and the 1969 accounts of Harland and Wolff, a shipbuilder which had been making losses and whose future survival was dependent upon continued government support (The Accountant, 22nd April 1971, page 525). Deloittes qualified the 1973 accounts of Kearney and Trecker Marwin on the basis of a need for additional finance. Coopers & Lybrand gave a going concern qualification to the 1973 accounts of Pennine Motor Group as the company was trading at a loss and was dependent on the bankers for continued financial support (Accountancy, November 1974). By 1974, even major multinational and household companies, such as British Leyland began to attract going concern qualifications[20] on the grounds of continuous financial support being available from the State. The 1975 accounts of John Stephen of London Limited carried a going concern qualification dependent upon continued support from the group's bankers (Accountancy, August 1976, page 8).

The press reports and a highly visible concern with going concern by auditors may have been connected to some changes in environmental factors. As an editorial in Accountancy[21] noted, "In the difficult days that undoubtedly lie ahead, auditors will be forced increasingly to think in each individual case whether the going concern concept is satisfied - something which it has rarely been necessary to consider in the past" (Accountancy, November 1974, page 5). In such an environment, prominent accountants, such as Tom

Watts (at the time an ICAEW Council member), argued that from an auditing viewpoint, ascertaining the applicability of the going-concern concept required,

> "preparation of forecasts by companies and adequate checking of these - particularly cash forecasts - by auditors" (Financial Times, 13th December 1974).

The first major institutional advice on the audit implications of the concept came from the Institute of Chartered Accountants of Scotland (ICAS) in February 1975, when it commissioned F.A. Strachan (a Peat Marwick Mitchell partner) to write an article. Under the title of "This 'Going Concern' Business", Strachan (1975) re-iterated the traditional interpretations and views on 'going concern'. To Strachan, going concern meant valuing the fixed assets at cost (or at valuation) less depreciation. Current assets had to be valued at net realisable values. However, no provisions were to be made for any additional liabilities which may arise on closure of business. If closure was anticipated then assets had to be valued on estimated realisable values or on a break-up basis. In addition, Strachan added that "every accountant and businessman in the United Kingdom must now consider whether the "going concern" concept still applies to the financial accounts of the business with which he is involved" (page 65). Strachan gave 'going concern' a literal meaning, i.e. a thriving and on-going business and suggested that auditors ought to look for symptoms of going concern problems. He gave some examples of ratios [22] and trends which could assist with this task. These included matters such as, an excess of current liabilities over current assets, an excess of total liabilities over total assets, a long record of losses, a default in connection with debt agreements and so on. Strachan suggested that the auditors ought to examine a company's profit and cash flow forecasts to satisfy themselves that a company will have the resources to survive. He argued that the absence of a cashflow forecast may even be a ground for qualifying the accounts. He also advised the auditors to make use of bankruptcy prediction models developed by researchers such as Altman and McGough (1974).

Following the Strachan article, the ICAS issued guidance to auditors (ICAS, 1975). It highlighted a major change in the auditing environment by adding, "In the past it has usually been clear whether or not the going concern concept was appropriate, but the present economic climate is causing the position to be less obvious" (page 141). It recommended that the auditors ought to concentrate on certain key variables to identify going concern problems. It called on auditors to examine and evaluate profit forecasts covering the next twelve months, paying particular attention to the likely cash shortages and the steps taken by the management to correct them. In addition, the ICAS highlighted the importance of post balance sheet events by stating that,

> "doubts on the going concern status sometimes arise by the date of the annual balance sheet but could also become apparent during the period between that date and the date when the accounts are adopted by the directors. It is clear that under existing economic conditions post balance sheet events can be of such a nature as to challenge the justification of the going concern status. The legal requirement is that the annual accounts show a true and fair view at the date of the balance sheet, but the view at that date is dependent upon the concept of going concern, which embraces the subsequent period. This means that both management and

> auditors must give weight to the post balance sheet events of which they have, or might reasonably be expected to have, knowledge" (ICAS, 1975, pages 141-142).

Increasing interest in the audit implications of the concept also resulted in the publication of a paper by the Accountants International Study Group (AISG)[23] in October 1975 (AISG, 1975). The purpose of this report was to "examine the problems which arise in the application of the going concern concept, particularly in the current volatile economic environment [and] difficulties which confront the auditor" (para 5). It compared auditing practices in the UK, USA and Canada and stated that

> "The circumstances which indicate that an enterprise is not a going concern are relatively clear cut: the liquidation of assets, or insolvency of the enterprise.
> ......
>
> A company with a liquidity problem will not necessarily have a going concern problem since the needed funds may be derived from incurring further debt, obtaining advances ..... issuing shares, or other sources. However, such a situation cannot continue indefinitely" (AISG, 1975, paras 12-14).

The AISG provided an extensive checklist of circumstances indicative of going concern problems. It referred to the importance of 'post balance sheet events'; noted the British practice of qualifying accounts for doubts about the ability of an enterprise to remain a going concern and advised auditors to review the client's budgets and cash forecasts and third party evidence (e.g. from financiers). The study noted that the auditor only refers to going concern if he has specific reservations. In such circumstances, full details of the reservations need to be given, but the auditor needs to be alert to the 'self-fulfilling prophecy'. The AISG (1975) did not directly say too much about auditor responsibility, but it favourably quoted a monograph by Carmichael (1972), which, despite its American origins, was thought to be "equally applicable to the UK" (para 11). It noted "there is substantial agreement on its [going concern concept's] meaning and role in financial statement preparation" (page 91). Carmichael's monograph eventually went on to influence the development of the going concern auditing standard (SAS 34) in the USA. Carmichael (1972) felt that the auditors were expected to give warning of exceptions to the going concern, however, he drew his insights from Mautz and Sharaf and argued that

> "An unqualified audit opinion means that either no evidence has come to the auditor's attention to contradict the going-concern concept, or that the auditor has evaluated known contrary evidence and concluded that it does not indicate that liquidation is imminent.
>
> ...... the auditor is entitled to assume that future operations will continue unless contrary evidence comes to his attention. In the course of his examination the auditor does not actively seek to validate the going-concern status of the entity, but remains aware of the possibility that the entity is not a going concern.
>
> Naturally, the going-concern assumption is not always valid. Nevertheless, in the absence of evidence to the contrary, the auditor should assume that the entity is a going concern. If successful operations are predictable, there would be no risk in economic activity. However, the auditor does not assume that liquidation is impossible. Although he plans his examination as if the assumption were true, his mind is not closed to the possibility that in a given examination the going-concern assumption may be false. He remains alert to any indication in the present examination that liquidation may be imminent" (Page 92-93).

Thus, the idea of what would subsequently be known as a 'passive approach' was firmly laid down by Mautz and Sharaf (1961), Carmichael (1972) and AISG (1975).

The fifteenth edition of 'Auditing: Principles and Practice' by de Paula and Attwood (1976) and reflecting the practice of the auditing firm Robson Rhodes, made no reference to going concern. It noted a number of valuation concepts, one of which was described as 'written down' or 'going concern value' defined as "the amount that an asset cost, when purchased or acquired, less the provisions made for depreciation since acquisition" (page 122). It added, fixed assets "are not held for the purpose of resale" and are stated in the balance sheet upon the basis of historical cost less depreciation. "Current replacement value, realizable value, and break-up value are disregarded, as these do not affect the working lives of the particular assets at all [but] current assets should be valued .... upon the basis of their realizable value" (page 124). The same points are also repeated in the 16th edition of de Paula and Attwood (1982, pages 208-212).

In May 1976, Dunlop and Land (1976) published an ICAEW backed research study on 'Post balance sheet events', and it included a section on the going concern concept. It noted that "the going concern concept may cease to be applicable on the happening of a particular event, e.g. voluntary or compulsory liquidation, appointment of a receiver or sale of the business, but it may also be inapplicable if liquidity or other problems (e.g. history or forecast of serious operating losses, loss of major customers, legislation or litigation) raise doubts as to the continuity of business" (page 22). In the Summer of 1976, the ICAEW published 'Accountants Digest No. 31' (Blackwood, 1976). Two pages of this drew attention to the implication of going concern for auditors. The auditors were urged to "assess the financial factors leading to liquidation or curtailment" (page 3) and examine company forecasts.

March 1976 also saw the formation of the Auditing Practices Committee (APC) with a specific mandate to develop auditing standards and guidelines. Percy and Logie (1976) immediately urged the profession to issue an auditing standard on going concern. This was not yet forthcoming, but the very first edition (Autumn, 1976) of the APC's quarterly bulletin drew attention to 'going concern' problems and advised

> "......... so don't assume the going concern basis is appropriate for all your clients - confirm that it is! ...... if you cannot satisfy yourself that the client will remain in business for the forseeable future, then reconsider the "going concern"" (APC, 1976, page 5).

It then listed and asked the auditors to consider what it regarded as symptoms of going concern problems (almost identical to AISG, 1975) and added,

> "If the answer is 'yes' to any of the above questions then you must take further steps to confirm that the client is a going concern - and not on the way out. At the very least -
>
> 1. compare the client's cash flow forecast with the overdraft or other loan facilities available for up to twelve months from the accounting date.
>
> 2. obtain written confirmation from the holding company that it intends its

subsidiary to continue in business and will not withdraw loan facilities.

3. enquire into or obtain written evidence of any steps the client is taking to correct its decline in fortunes.

If you cannot satisfy yourself that the client will remain in business in the forseeable future, then reconsider the going concern basis" (page 5).

In Autumn 1978, the APC recommended that "the auditor may need to .... carry out a specific post balance sheet events review [and consider] whether the company can continue as a going concern" (APC, 1978b, page 68). This advice was not all that different from that contained in previous publications (Strachan, 1975; ICAS, 1975, AISG, 1975; Blackwood, 1976). It also advised auditors to begin their diagnosis of going concern problems by paying attention to what it regarded as 'symptoms' of problems; these included, high gearing, deferment of purchases, reduction in profitability, increasing dependence on short-term finance, etc. To Woolf (1980, page 60), this seemed to suggest that the profession was urging auditors to adopt an 'active' approach.

Though Waldron (1979), Millichamp (1978 and 1981) and Cooper (1979) made no reference to any audit implications of the going concern concept, Woolf (1979, pages 477-479) advocated a review of the post balance sheet events by the auditor to identify symptoms of going concern problems. Whilst Helfert (1966), Gordon and Shillinglaw (1969) and Lowe (1970), amongst others, argued that going concern meant consideration of managerial plans and skills. Shaw (1980), a past president of the ICAS, argued that the auditor does not directly express an opinion on the quality of management. Such judgements were to be formed by the users of accounts. For Shaw, the going concern assumption meant that

> "the business will continue in existence and there will be no dramatic change in its economic circumstances; it excludes the possibility of short-term break-up, forced sale or liquidation. Figures based on the going concern assumption are not related to realisation values ...... To the extent to which the going concern assumption is fundamental to the form and content of the accounts, therefore, the auditor indicates by inference his belief that it is the appropriate basis. He does not "guarantee" that the business is a going concern in the long term, but he does confirm that the assumption that it is a going concern is a valid basis for the financial statements" (Shaw, 1980, pages 16-17).

In 1980, the APC published its long awaited auditing standards. These did not include any guidance on going concern aspects, but referred to the concept in a specimen audit report[24]. This associated going concern qualification with the lack of finance. Whilst the concept was thought of as 'fundamental' in accounting (ASC, 1971), the auditing standards advised auditors to regard going concern reservations as 'material but not fundamental' and consequently a 'subject to' audit opinion was recommended, though a 'disclaimer of opinion' was not ruled out.

Millichamp (1981) still made no reference to going concern, but some books began to advise the auditors on tools and techniques for making going concern predictions. For example, Westwick (1981) in an ICAEW sponsored book, advised auditors to use accounting ratios, perform analytical reviews and study trends to spot "danger signals" (page 44). Westwick identified seven ratios[25] considered to be useful predictors of potential liquidity and solvency problems. If the auditor's doubts persisted, then he was advised to examine a company's cashflow projections. Following the publication of an article by Taffler and Tisshaw (1977), highlighting the usefulness of Z-scores for going concern predictions, Westwick also emphasised the usefulness of Z scores[26] to auditors. In a subsequent work, Westwick (1987) stated, "It is up to the reader to decide whether that view [true and fair view] encourages him to believe in the company's continuing existence or to have doubts about its viability. If the auditor concludes that there is a strong evidence that a company will not remain a going concern, either in any event, or unless certain major uncertainties are favourably resolved (e.g. the continuing support of the company's bank is assured) then he should qualify his report" (page 319).

Whilst there was no known plan for the UK professional bodies to issue an auditing guideline on the subject matter, the Canadian profession dealt with going concern in August 1980 by treating it as a contingency for auditing purposes (Canadian Institute of Chartered Accountants, 1980). It ruled out the use of a 'subject to' audit report for going concern matters. In March 1981, the Statement on Auditing Standards (SAS) 34 codifying the auditing practices on going-concern matters was issued in the USA. It recommended a 'passive' approach by stating that "the auditor does not search for evidential matter relating to the entity's continued existence because, in the absence of information to the contrary, an entity's continued existence is assumed in financial accounting" (AICPA, 1981, para 3). SAS 34 included indicators of going concern problems with recommendations to examine budgets and cash forecasts, if necessary. The Australian guidance (AUP 7) issued in June 1981 recommended that "when a question arises regarding the going concern basis, certain of these [normal] auditing procedures may take on additional significance or it may be necessary to employ additional auditing procedures" (Australian Accounting Research Foundation, 1981, para 10). It suggested that the auditor should focus on indicators of going concern problems to identify key areas requiring special attention. However, the auditor needs to be alert to the possibility that such indications may be mitigated by other factors, for example, the company's ability to maintain cashflows, disposal of assets to generate cash, rescheduling of loan repayments or obtaining additional capital, availability of alternative sources of supply, etc.

An auditing manual published by Thornton Baker (1981, page 228) noted that events subsequent to the year-end may prejudice the application of the going concern concept. Innes, Lee and Mitchell (1981a) published a series of auditing case studies contributed by various firms and sponsored by the ICAEW. The back cover of the book noted that "these case studies reflect the auditing practices of .... firms". One of these case studies was contributed by Arthur Anderson and related to "Assessment of Going Concern". The going concern case study consisted of three pages and included a conventional balance sheet and extracts from the profit and loss account. It invited the reader to calculate some accounting ratios from the past data and to judge whether the business was likely to remain a going concern. The outline solution (Innes, Lee and Mitchell, 1981b) suggested that factors such as overdue creditors, unproven track record, cost overruns, lack of finance and undercapitalisation could jeopardise the application of the going concern concept. The authors also invoked the traditional meanings of the concept by noting that

> "fixed assets are being accounted for on a historical cost basis ...... They are so accounted for and presented in an operating company because of the utilisation of the 'going concern concept'. Under this concept day-to-day or even year end changes in the market values of the fixed assets do not affect the accounting for such assets.
>
> It would be misleading to use the 'going concern concept' for a company in a development stage without any qualification, if only because the company is not yet a going concern" (page 88).

Whilst de Paula and Attwood (1982) and Howard (1982) made no explicit references to going concern in their auditing books, some authors argued that auditors need to look beyond the traditional areas of audit evidence to make going concern judgements. Hatherly (1980) argued that "As an alternative to the auditor developing predictions, the auditor may use predictions made by the enterprise itself in the form of budgets or other forecasts. Where the auditor considers the enterprise's predictions to be made on a satisfactory basis ..... its predictions for the future time periods may form the basis of an assessment of the 'going concern exposure' of the enterprise" (page 38). In a similar vein Lee (1982) argued that the auditor needs to pay attention to

> "the company's operations and finance - not just in terms of these matters in the present but also in the indefinite future. He must therefore become concerned with the forecasting function .... He is attempting to search for signs of potential liquidation of parts or the whole of the company at some future date. ...... The use of formal forecasting models for potential bankruptcy may be of some use to the auditor in this respect; constant vigilance and commonsense are also important attributes of auditing in this area" (page 140).

Following the issue of SSAP 17 (ASC, 1980), the APC issued the auditing guideline 'Events after the Balance Sheet date' (APC, 1982) which asked the auditors to take account of events "which may affect the company as a going concern" (Pratt, 1983, page 274). In forming his judgement, the auditor was advised to examine management accounts, profit forecasts, cash flow projections and evidence from third parties. However, the same guideline, despite the legal requirement (section 384, Companies Act 1985) that an auditor remains in office from one AGM to the next, emphasised that the auditor had no 'active' responsibility to search for 'post balance sheet events' falling between the date of the audit report and the AGM (APC, 1982, para 7).

Whilst the auditing manual of Stoy Hayward (1983) did not explain the firm's going concern practices, a glimpse of the auditing practices was also given by the 1983 publication of the DTI's interim report into Bryanston Finance Limited (later known as Ramor Investments). The investigation had originally been commissioned in 1974. The report included a section, 'Was Bryanston a going concern' and gave an indication of the auditing procedures used by auditors Price

Waterhouse. The report noted that "The illiquidity and the reduction of the loan facilities available caused Price Waterhouse to examine whether the group could be considered as a going concern for the purposes of 1973 accounts. A cash flow forecast and letters from the bankers were requested by Price Waterhouse" (DTI, 1983, page 243). The report also noted that the loan and financing facilities were reviewed and pressures from bankers to reduce loans were also relevant factors (page 271).

On 28th September 1983, an exposure draft 'The auditor's considerations in respect of going concern' was issued. This was accompanied by the following commmentary in the Autumn 1983 edition of 'True & Fair'.

> "The essence of the exposure draft is simple: the auditor should be watchful for indications of potential going concern problems; if he identifies such indications he should look for mitigating circumstances; if he eventually concludes that there is reasonable doubt as to an enterprise's going concern status, he should qualify his report" (APC, 1983a, page 1).

Whereas the American auditing standard (AICPA, 1981) on the subject matter was based upon a 'passive approach', Ray Hinton, the chairman of the APC working party stressed that the British auditing guideline was different. He wrote that

> "In light of the widely held perceptions in the UK that the auditors' report is some form of seal on continuing existence, it seems that going concern should be given specific rather than merely tacit consideration.
> This is in contrast to the position taken in the SAS 34 (the equivalent US Standard) which provides that the auditor does not search for evidential matter relating to the entity's continued existence because, in the absence of information to the contrary, an entity's

> continuation is assumed. Clearly, the user of financial statements is entitled to assume that a company will continue in existence for a forseeable future ...." (Hinton, 1983, page 14).

Martyn Jones of Touche Ross, another member of the going concern working party (also APC Secretary from April 1983 to September 1984) supported this differentiation with the American pronouncement (Jones, 1985). However, Woolf (1983b) felt that the UK exposure draft (in line with the American standard) was based on a 'passive approach'. His own preference was for an 'active approach'.

The auditing guideline ('The auditor's considerations in respect of going concern') was formerly issued on 28th August 1985. It's issue was accompanied by a commentary that "In view of the accusing fingers which have recently been pointed at auditors in connection with certain well-publicised company failures, this guideline is a significant addition to the framework of auditing guidance" (APC, 1985b, page 2). This time, Robert Charlesworth, the APC Secretary stated that the auditing guideline is based on a 'passive approach' (Charlesworth, 1985).

The going concern concept is almost always accompanied by some notion of a 'foreseeable future'. SSAP 2 does not define its meaning even though some meanings are mentioned in the literature (see figues 3.3). These include periods such as 'twelve months from the balance sheet date', 'twelve months from the audit report date' and others.

Figure 3.3
Some Definitions of the Foreseeable Future

Definition	Sources
Twelve months from the balance sheet date	Coopers & Lybrand (1985) Millichamp (1984), Pratt (1983)
Twelve months from the date of the audit report	Stilling, Wyld and Guida (1982) Thomson McLintock (1983) Thornton Baker (1983)
Long enough to realize its projects, commitments, and ongoing activities.	Belkaoui (1981)
At least twelve months ahead	Strachan (1975)
Long enough to carry out its existing commitments.	Hendriksen (1970)
A period long enough to enable the cost of fixed assets to be written-off to revenue over their useful lives and any other costs which have been deferred to be written-off over the period of time during which revenues are expected to benefit.	ICAS (1975)
A time span necessary to carry out present contractual commitments or to use up assets according to plans and expectations presently held.	Moonitz (1961)

The definition in the going concern auditing guideline was not supported by any of the previous literature. The APC stated that

> "..... the foreseeable future must be judged in relation to specific circumstances, it

should normally extend to a minimum of six months following the date of the audit report or one year after the balance sheet date whichever period ends on the later date. It will also be necessary to take account of significant events which will or are likely to occur later" (APC, 1985a, para 8).

The source of this formulation was neither explained in the guideline nor in any accompanying commentary.

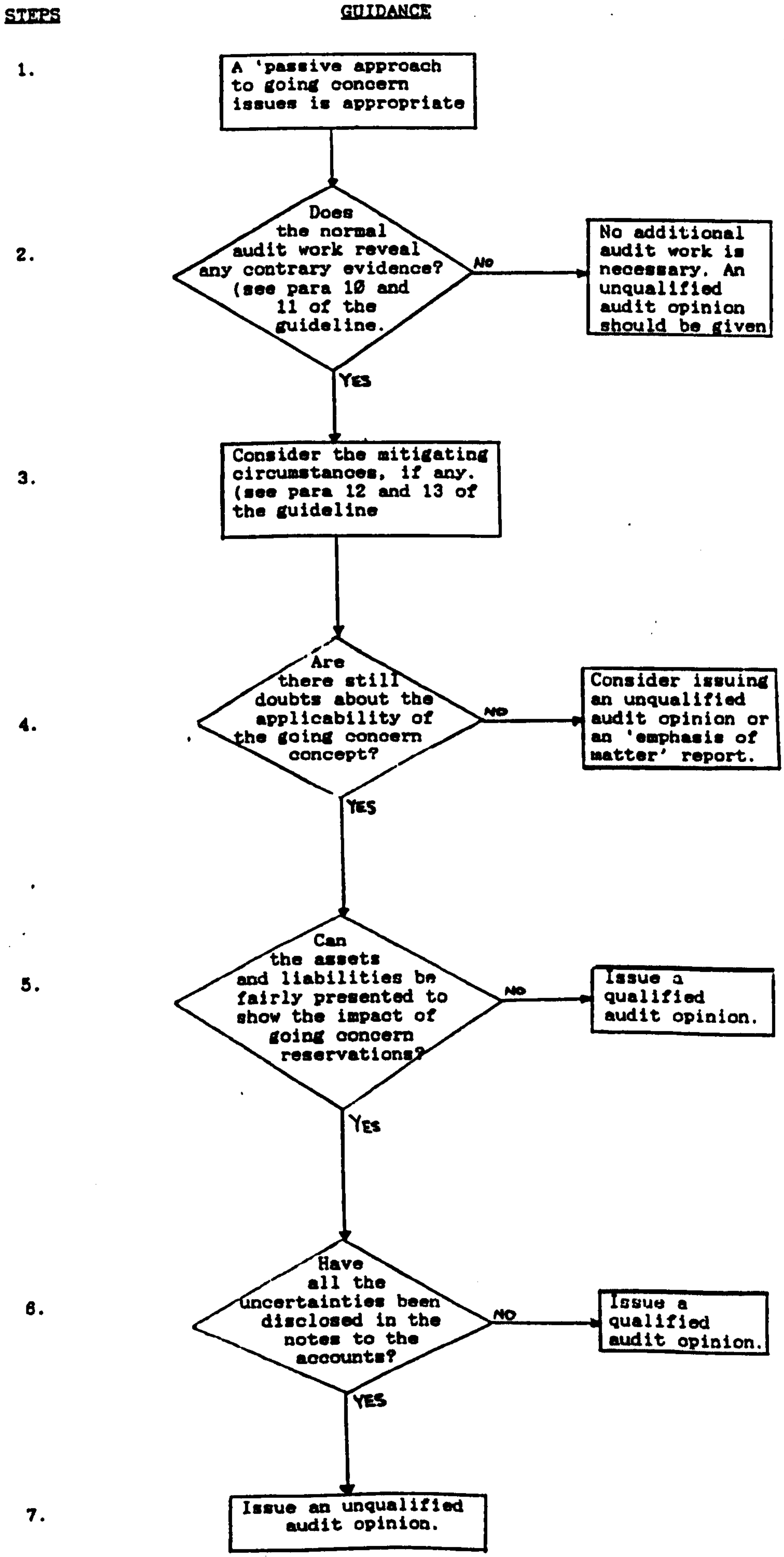
Having noted the relatively recent development of the implications of the going concern concept for auditors, the next sub-section provides a summary of the main features of the auditing guideline issued by the APC.

3.3.1: 'The Auditor's Considerations in Respect of Going Concern', The Auditing Guideline

The auditing guideline ('The auditor's considerations in respect of going concern') was developed by a working party set up in the Spring of 1982 under the Chairmanship of Ray Hinton, an Arthur Andersen partner. This working party is thought to have had its final meeting in July 1984 and formally stood down in September 1985[27]. The membership of this working party, its deliberations and voting patterns, if any, are not widely known (Sikka, Willmott and Lowe, 1989). The work of the working party resulted in the publication of an exposure draft on 28th September 1983. After consideration of the comments[28] from various interested parties and approval from the governing bodies of the CCAB, a revised version, in the form of the auditing guideline, was issued on 28th August 1985. The main contents of the auditing guideline are shown in figure 3.4.

FIGURE 3.4

FLOWCHART SUMMARY OF THE AUDITING GUIDELINE: THE AUDITOR'S CONSIDERATIONS IN RESPECT OF GOING CONCERN



The following are the main features of the guideline.

1) The guideline begins by firmly stating that the primary responsibility for preparation and publication of financial statements rests with the directors. On auditor responsibility, the chairman of the working party stated that "going concern should be given specific rather than merely tacit consideration on all engagements" (Hinton, 1985, page 15). An 'active approach' to making going concern evaluations was rejected because this would

> "involve carrying out specific audit procedures designed to obtain positive audit evidence that substantiate the applicability of the going-concern concept. This would be an onerous responsibility .... and presents many practical problems .... it would probably prove an impossible task in many cases. At the vey least it would require substantial audit time - and cost to the clients - to obtain such positive assurance. ..... an unqualified audit report might be interpreted as a form of guarantee of the company's viability. ...... So, in practice, it is likely that the active approach would result in a plethora of audit qualifications" (Charlesworth, 1985).

The auditing guideline went on to adopt a 'passive approach' because "its presumption in favour of the going-concern basis, is clearly more economical of audit effort and cost" (Charlesworth, 1985).

2) The guideline argues that in the course of the normal work audit, an auditor is likely to be alerted to symptoms of going concern problems or 'contrary evidence'. This would "raise questions about the continuation of a business" (APC, 1985a, para 9) and ought to put the auditor 'upon enquiry'. Paragraphs 1Ø and 11 of the guideline contain comprehensive

(but not exhaustive) examples of such evidence. These include matters such as recurring operating losses, overdue creditors, working capital deficiencies, low liquidity ratios, over-gearing, undue influence of a market dominant competitor, technical developments and so on. If the auditor does not come across any contrary evidence then he is advised to issue an unqualified opinion. Charlesworth (1985) clarified such an approach by arguing that the

> "going concern basis is appropriate unless indication to the contrary comes to his [auditor's] attention as a result of the other audit procedures. Only when such problems have been identified does he need to apply audit procedures specifically directed towards the going concern basis" (Charlesworth, 1985).

Further light on the 'audit procedures' is also shed by the guideline.

3) If by following his normal auditing procedures, "evidence comes to the auditor's attention that suggests that the company may be unable to continue in business, he should review any factors that may counterbalance that evidence" (para 17). These are the mitigating factors. Paragraphs 12 and 13 of the guideline include a comprehensive list. Examples are matters such as discussions with the management, review of corporate plans, possibility of raising new finance, restructuring debts, reviewing guarantees, obligations and collecting third party evidence in support thereof. In particular, the auditor is asked to consider future oriented information, because "it is implicit in assessing the foreseeable future that a judgement must be made about uncertain future events" (para 7). Examples of

this include consideration of company forecasts, plans and budgets.

4) If after consideration of the mitigating circumstances and examining the relevant audit evidence, an auditor concludes that the application of the concept is appropriate then an unqualified audit opinion should be given. The guideline also suggests that an 'emphasis of matter' audit report may be issued where such a report might give the reader "a better understanding of the financial statements" (para 24). If the auditor's doubts remain then further tests are to be applied.

5) Much of the accounting literature argues that some different accounting principles are applicable to a non-going concern, in accordance with which assets need to be stated at a liquidation (or some equivalent) value. As Lewis and Pendrill (1982) put it, "if ...... continuation is not expected, then the going concern concept must not be applied. So if, for example, liquidation seems likely then the valuation of assets on the basis of net realizable value would be appropriate" (pages 20-21). Such views are typical of most of the literature (for example, see books by Davidson and Weil (1977) Belkaoui (1981), Anthony (1983), Carrington and Howitt (1983), Farmer (1983) and Harvey and Keer (1984), amongst others).

Neither the draft (APC, 1983a) nor the guideline proper (APC, 1985a) gets into any discussions of valuation concepts, but the auditor is reminded that if he has material reservations about the going concern basis, then the balance sheet figures for assets and liabilities may have to be adjusted. In particular, "the auditor should consider the recoverability and classification of assets, the classification of liabilities and the possibility of new liabilities were the company to cease to be a going concern." (para 26).

6) If details of all material uncertainties cannot reasonably be estimated and disclosed then a qualified opinion is appropriate. The guideline prefers a 'subject to'[29] type of qualified audit report (i.e. regarding the matter as material but not fundamental) for going concern matters. In principle, this is consistent with the specimen audit report included in the auditing standard (APC, 1980a), but there are differences[30]. Whereas the auditing standard related going concern to financial arrangements only, the guideline identifies loss making operations, adverse working capital ratio and a reliance for finance on external parties as a reason for issuing a going concern qualification.

A 'Disclaimer of Opinion' may also be appropriate where the uncertainties are considered to be 'fundamental' to appreciating the financial statements.

7) Where all uncertainties have been fairly estimated and disclosed, or all the assets and liabilities have been reclassified, then an auditor may give an unqualified audit opinion. As mentioned earlier, he may also give an unqualified opinion where his normal audit work does not reveal any 'contrary evidence', or where an evaluation of the

'mitigating factors' suggests that the going concern assumption is appropriate.

3.3.2: Summary of Going Concern from the 1970s to 1985

This section began by looking for explanations of the going concern concept in an auditing context, something which had been virtually absent from the literature for the period up to 1970. The main interpretations of the concept are shown in figure 3.5.

Figure 3.5
Meanings of going concern to 1985

IN ACCOUNTING CONTEXT

The concept remained 'fundamental' and 'generally accepted' in the UK.

Numerous competing and contradictory meanings continued to exist side by side. These are shown in figure 3.2.

IN AUDITING CONTEXT

The traditional accounting meanings accepted in an auditing context.
A struggle between the 'passive' and 'active' approaches.
The auditing guideline favoured the 'passive' approach, but this was not always supported by others.
The concept was regarded as 'material but not fundamental'.
Going concern means a concern with the survival, profitability, liquidity and solvency of a business.
It requires particular emphasis on financing aspects.
Auditor advised to focus on future oriented aspects by examining corporate plans, budgets and forecasts.
Post balance sheet events must be examined.
Going concern problems can be diagnosed from accounting ratios.
It is not concerned with the quality of management.
The applicability of the concept is ultimately a matter of judgement.
Unlike SSAP 2, the term 'forseeable future' is defined in the auditing guideline.
The debate did not directly address questions of asset or business valuation but acknowledges the existence of separate accounting methods for non-going concerns.

It appears that the references to going concern in an auditing context began to emerge in the 1970s. The reasons for this will be investigated in chapters 6 and 7. Whereas SSAP 2 regarded the concept as 'fundamental', auditing pronouncements regarded it as 'material but not fundamental'. In an earlier period, the concept had been frequently associated with accounting discussions about valuations and depreciation, but such discussions were not widespread in the auditing literature. Interestingly, in an auditing context 'going concern' was interpreted in a literal sense, i.e. will the business being audited be still 'going' after the immediate short period. It is as though the auditors are expected to give an informed opinion on the survival of a business in the face of uncertainty.

The professional advice to auditors had been changing throughout the period. Having recognised the going concern concept as 'fundamental', the ICAEW then said that 'going concern valuations' are not appropriate. The auditors, it was argued, were not concerned with the quality of management, but were advised to examine forecasts, budgets, post balance sheet events and pay particular attention to the availability of finance. In the mid 1970s, the profession appeared to be urging auditors to be adopt an 'active approach', but subsequently in the auditing guideline, it advocated a 'passive approach' which is considered to be less onerous on auditors. Such an approach to an audit may also beg some questions of the nature of an audit. To what extent are audits carried out for the benefit of shareholders, creditors, society, or the auditors themselves?

Throughout the literature, the auditors have been advised to adopt the traditional tools of accounting, such as ratios from the past data, and then make predictions about the future. It is also noted that the professional guidance in the UK appeared at a time different from that in other countries, for example the USA, Canada, Australia; suggesting that there must have been some specific UK factors giving rise to the guideline.

3.4: CHAPTER SUMMARY AND DISCUSSION

This chapter began with a search for the meanings which various writers and institutions have attached to the going concern concept. The main emphasis of the chapter is to focus on the auditing meanings, but it was recognised that accounting and auditing are interdependent. Therefore, both accounting and auditing literature have been examined, starting from the late 19th century.

The going concern concept is multi-accented. It has numerous meanings, which various authors and institutions have inserted into numerous discourses. Possibly reflecting the flavour of the times, the earlier writings tended to say little about the auditing implications. In the late nineteenth/early twentieth century, the concept was mainly invoked in the context of balance sheet and interim valuations. The prominent authors firmly associated going concern values with the use of original cost less a due provision for depreciation. They also expected businesses to have an almost permanent life. Here their 'common sense' view of accounting may have been formed by the almost perpetual life granted to Parliamentary companies and chartered companies such as the East India Company, Russia Company and Hudson Bay Company. In view of the prevailing legislation and social relations of power, such entities were expected to have perpetual succession. Such images may have been further reinforced by the advent of limited liability and the accompanied rise of capital and financial markets in which shares were traded. Consequently, operations did not have to be liquidated to recoup any investments. Such images of permanence and perpetual succession became synonymous with any discussion of going concern.

The multi-accented nature of the concept continued to be evident in the period from the 1930s t0 the 1970s. This period is also notable for a number of extensive critiques of the concept by scholars such as Edwards, MacNeal, Storey, Fremgen, Chambers Sterling and Yu. Whereas up to the 1930s, the British books were regarded as leading in the USA (for example, Dicksee's Auditing was published as 'Montgomery's Auditing' in the USA), the position changed during the period 1930-1970. In the 1930s, phrases such as 'generally accepted' accounting conventions or principles began to appear. Indeed, the going concern concept itself began to be described as such in the USA. In this period, with the formal recognition of 'going concern' as a postulate, convention, concept, principle and assumption in the USA, many American books discussed accounting principles. But, this did not appear to be the case in Britain where the concept did not receive the same institutional support. The ICAEW's 'Recommendations on Accounting Principles' and 'Statements on Auditing' made no explicit reference to the going concern concept. Whenever the books by authors such as de Paula, Leake and Cutforth were published they tended to re-iterate the traditional meanings. It is as though something which was driving accounting in the USA was absent in the UK.

Right up to the 1970s (and possibly beyond) there appeared to be some confusion with 'going concern values' and 'values to a going concern'. However, 'going concern' remained a powerful influence on accounting thought and its meanings continued to be inserted into debates relating to adoption of historical costs, price level accounting, cash flow reporting, inventory valuation, deferring of expenditure, depreciation, goodwill, doubtful debts provision, etc. The literature also seems to point towards the existence of two kinds of accounting principles and practices. One set relating to 'going concerns' and the second set relating to 'non-going' concerns, or those in liquidation, though hardly anyone explained how the second set of principles worked.

This chapter has noted that until 1970, the auditing implications of the going concern concept hardly appeared in British literature. Perhaps, prior to this the auditing aspects were not considered to be problematic. Perhaps, the auditing discourses were not too voluminous. It should also be noted that almost all of the writings on the concept in an auditing context are by audit partners who tended to be concerned with their technical interests in auditing. Though the professional bodies had been issuing auditing pronouncements since 1961, they did not explicitly address going concern. However, from the mid 1970s onwards, they began to directly address the concept. Compared to accounting, the audit interpretations of the concept appear to have some specific characteristics. For example, in an auditing context, the concept is interpreted literally, i.e. there is a need to know whether the business will still be 'going' after a reasonably short period of time. To make this prediction, an auditor is expected to exercise his rights (for example under the Companies Act) to obtain and examine the future oriented information such as profit and cash flow forecasts. This is in marked contrast to the earlier literature where the auditors were simply expected to verify assets and liabilities etc. However, there are throwbacks to past tools and ideologies where the auditors are asked to use ratios and make predictions. Overall, despite the early articulations, the profession appeared to be advocating a 'passive' role for auditors. Such a change of direction may be indicative of some wider struggles. This would be investigated in the subsequent chapters.

The literature reviewed here covers a large time span and provides a rich analysis of the themes pursued in the name of the going concern concept. In offering explanations of the meanings and interpretations of the concept in an auditing context, within the methodological framework, one will have to take account of numerous interconnecting social, political and economic events. Such goals, within the constraints of this thesis, as chapter 1 noted, are not possible. Instead, the aim is to offer a sociopolitical explanation of a narrow range of questions. One puzzling question is why the going concern concept became 'generally accepted' and received institutional support in the USA in the 1930s, but failed to receive the same support in Britain until the 1970s? An answer to this will be provided in chapter 5 together with an indication of the early influences which shaped the meanings being invoked.

Prior to the 1970s, the UK literature made very little reference to the going concern in an auditing context, even though the profession had been issuing audit guidance since 1961. However, from the early 1970s onwards a considerable institutional interest began to be expressed in the concept. Why should the profession suddenly find a need to focus on the going concern concept in an auditing context? An explanation of this aspect would be provided in chapter 6 by examining the extensive capital restructuring and State intervention in Britain and its impact on the accountancy firms (themselves a significant fraction of capital) and profession.

This chapter noted a major development in the UK, that is the publication of an auditing guideline on going concern in 1985. Despite recognising four accounting concepts as 'fundamental', no other concept has been the subject of an auditing guideline. The auditing guideline itself marks a break from previous meanings of the concept (see this chapter). How did the professional bodies come to formulate this guideline? What kind of interests and pressures persuaded the profession to issue the guideline? In pursuance of such questions, chapter 7 explains the formulation of the auditing guideline. In order to focus upon 'interests', it is also important to study the organizations which have a particular role in formulating the meanings and shaping the discourses. Indeed, it is impossible to understand the meaning and implications of the going concern concept without an awareness of the agencies which formulate and issue such guidelines. Therefore, chapter 7 also examines the formation and development of the Auditing Practices Committee (responsible for formulating the auditing guideline) in a sociopolitical context.

Chapter 3 Footnotes:

1) The Accountant is the oldest English language accounting periodical. Its weekly publication began in 1874.

2) For example, see the essays in Littleton and Yamey (1956).

3) For example, Cooper (1886) noted the mention of auditors in a 1285 statute.

4) Francis William Pixley was a founder member of the ICAEW and its President for 1903-1904. He was also called to the Bar in 1894 (Kitchen and Parker 1980).

5) Edwin Guthrie was a founder member of the Institute of Chartered Accountants in England and Wales and a signatory to the Royal Charter in 1880 (Kitchen and Parker, 1980, page 8).

6) Lawrence Robert Dicksee was appointed to the first Chair of Accounting at the University of Birmingham in 1902 and subsequently became the first teacher of accounting at the London School of Economics (LSE). Dicksee's 'Auditing' was edited by Colonel Robert H. Mongomery to accommodate the legal differences and was also published in America in 1905 and 1909 (Kitchen and Parker, 1980, page 60).

7) Hatfield (1909) supported Dicksee's views.

8) Kitchen (1979) thinks that the paragraphs may be compatible if "Dicksee saw an 'original - cost - less - depreciation' value as being (and likely to continue to be) closely representative of likely 'current' values such as would meet his understanding of going concern value ......".

9) Arthur Edwin Cutforth (later Sir Arthur) became President of the ICAEW in 1935-36 and was very much concerned with the education of accountants (Kitchen and Parker, 1980).

10) Frederick Rudolph Mackley de Paula gave part-time classes at the LSE. He was the first non-practicing accountant to be admitted to the ICAEW Council in 1943 and was the Chairman of the ICAEW's Taxation and Financial Relations Committee (TFRC) which from 1942 began to issue Recommendations on Accounting Principles.

11) Kenneth MacNeal's reward for pointing out the weaknesses of the contemporary accounting theory and practice was academic annonymity and ridicule (Zeff, 1982).

12) F.R.M. de Paula was appointed the Vice-Chairman of the TFRC in July 1942. On 18th November 1943, he was appointed Chairman of the TFRC and retired from that position in 1945 (Kitchen and Parker, 1980).

13) As quoted in Kitchen (1979).

14) Stanley W. Rowland was appointed a Secretary of the ICAEW's TFRC in July 1942. Rowland was a partner in Dicksee's firm and for many years also lectured on accounting at the LSE (Kitchen and Parker, 1980).

15) Statement N15 was enthusiastically supported by the eminent American academic Eric Kohler (1963).

16) Egginton (1977) thought that the profit calculations implied by current cost accounting are consistent with the continuity assumption (page 144).

17) By building upon the suggestions of Chambers (1966) and Sterling (1970), Lee (1984) has developed a system of cash flow reporting (CFR) which makes use of exit values (or selling prices). Lee argued, "Despite the use of sale prices, CFR does not breach this [going concern] convention - the use of sale prices does not signal a realization of the assets nor a liquidation of the entity. Instead, it conveys the message that assets should be transformed, as and when required, into alternative forms by means of sale and subsequent acquisition. The entity, under these circumstances of gradual adaptation to change, is the permanent feature (the going concern)" (page 92).

18) The first international accounting standard (published in 1975) published by the International Accounting Standards Committee (IASC), itself established on 29th June 1973, labelled 'going-concern' as a 'fundamental accounting assumption' and explained it thus: "The enterprise is normally viewed as going concern, that is, a continuing operation for the forseeable future. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing materially the scale of its operations" (IASC, 1975, para 7).

In 1981, following the implementation of the EEC Fourth Directive, the going concern concept also came to be recognised as a fundamental concept by Companies Act 1981.

19) The Traditional meanings and approaches to the going concern concept have continued to appear in much of the literature. For example,

Bedford, Perry and Wyatt (1973) state that "Since a substantial number of the transactions of the enterprise are in a somewhat indeterminate status at any reporting date, accounting needs to make some assumptions as to the future of the enterprise...." (page 7).

Hawkins (1977) invokes the concept to justify the valuation of receivables and inventories at net realisable value. The going concern concept underpins accruals and allocations (Istavan and Avery, 1979), the use of double entry book-keeping (Lee, 1982), the inclusion of non-cash assets in the balance sheet (Meyer, 1980), writinmg off and/or deferring expenditure (Fess and Warren, 1984), rules out realizable values (Lewis and Pendrill, 1982; rules out liquidation values Anthony, 1983; Carrington and Howitt, 1983; Davidson and Weil, 1977; Farmer, 1983; Wood, 1984; Blake, 1985).

20) The following audit report was issued on the accounts of the British Leyland Motor Corporation Limited.

Report of the Auditors to the Members of

British Leyland Motor Corporation Limited

We report on the accounts together with the notes set out on pages 18 to 31. Our report is based on our examination and the reports of certain subsidiaries not audited by us.

These accounts have been prepared on the normal going concern basis which assumes that the Corporation will obtain further finance as referred to in the paragraph headed 'Finance' set out in the directors' report on page 14.

On this basis, in our opinion the accounts together give a true and fair view of the state of affairs at 30th September 1974, and of the results for the year ended on that date and comply with the Comapnies Act 1948 and 1967.

Coopers & Lybrand

Chartered Accountants

London

18 December 1974

21) According to the editor, "As the Journal of the Institute of Chartered Accountants in England and Wales, it clearly has a duty to present the 'official view' (Accountancy, October 1973, page 3).

22) Accounting ratios are deeply embedded in accounting thought and have a long history which suggest that selected ratios have an ability to make predictions (see for example, Horrigan, 1968; Dev, 1974; Beaver 1966).

23) Some aspects of the origins of the Accountants International Study Group are discussed in Benson (1976).

24) <u>Specimen Audit Report</u> (from the Auditing Standard)

AUDITORS' REPORT TO THE MEMBERS OF ....

We have audited the financial statements on pages ..... to ..... in accordance with approved auditing standards.

As stated in note ...... the company is currently negotiating for long-term facilities to replace the loan of £...... which becomes repayable on (a date early in the next financial year); continuation of the company's activities is dependent upon a successful outcome of these negotiations. The financial statements have been drawn up on a going concern basis which assumes that adequate facilities will be obtained.

Subject to a satisfactory outcome of the negotiations referred to above, in our opinion the financial statements, which have been prepared under the historical cost convention, give a true and fair view of the state of affairs of the company and the group at 31 December 19.... and of the profit and source and application of funds of the group for the year then ended and comply with the Companies Acts 1948 and 1967.

SOURCE: APC (1980a)

25) A large number of accounting ratios are thought to be in continuous use by auditors (Graham, 1981; Holder, 1983; Biggs and Wild, 1984; Herskovitz 1984; Darcoa and Holder, 1985).

26) For an explanation of Z-scores, see the seminal work of Altman (1968). Z-scores and its variants have also been applied to auditing in the going concern context by Altman and McGough (1974); Blum (1974); Altman, Halderman and Narayanan (1977); Taffler and Tseung (1984). Eventually Altman (1982) came to conclude that "failure classification models of the Z-Score and Zeta type should not be used as a failure prediction tool to determine going concern problems" (page 5).

Whilst proponents of Z-scores have argued that their mathematical models could outperform the auditor's predictive abilities, Kida (1980) disagreed by noting that the auditors frequently correctly (i.e. in line with the models) identified going concern problems but then were reluctant for various reasons to qualify the accounts. Mutchler (1984) also reported similar research findings.

27) As per a letter from the APC, dated 10th December 1986.

28) Chapter 7 will examine the submissions, comments and the 'interests' which were being pursued in the development of the auditing guideline.

29) The 'subject to' type of audit reports are of American origins (see Carmichael, 1972). Their use has been criticised by the Commission on Auditor Responsibility (Cohen Commiision) in the USA. It argued that "the meaning and significance of a "subject to" qualification are difficult to understand. The "subject to" phrase is ambiguous to users because there is no way to tell whether the auditor's intention is only to highlight information more fully disclosed elsewhere or to indicate a deficieny in the financial statements. .... the "subject to" qualification may cause the financial statement user to believe the financial statements will be restated when the uncertainty is resolved, but this will probably not be the case. In fact, the general practice of using "subject to" qualification may confuse financial statement users" (AICPA, 1978, page 25).

30) <u>Specimen Audit Report (from the Auditing Guideline)</u>

AUDITORS' REPORT TO THE MEMBERS OF ....

We have audited the financial statements on pages.....to .....in accordance with approved Auditing Standards.

The financial statements have been prepared on a going concern basis. This may not be appropriate because the company incurred a loss after taxation of £.......during the year ended 31 December 19....and at that its current liabilities exceeded its current assets by £.......Further , the company is currently negotiating for long-term facilities to replace the loan of £.........which is repayable on .... These factors, which are explained in note ...., indicate that the company may be unable to continue trading.

Should the company be unable to continue trading, adjustments would have to be made to reduce the value of assets to their recoverable amount, to provide for any further liabilities which may arise, and to reclassify fixed assets and long-term liabilities as current assets and liabilities.

Subject to the company being able to continue trading, in our opinion the financial statements, which have been prepared under the historical cost convention, give a true and fair view of the state of affairs of the company at 31 December 19...... and of its loss and source and application of funds for the year then ended and comply with the Companies Act 1985.

<u>SOURCE: APC (1985a), para 28.</u>

CHAPTER 4

MEANINGS OF GOING CONCERN: THE PRACTITIONERS' VIEWS

4.Ø: Introduction

This chapter continues to provide evidence about the meanings associated with the going concern concept. Whereas chapter 3 concentrated on the literature in a search for meanings attached to the going concern concept in an auditing context, this chapter is concerned with the meanings and interpretations which auditors place upon the concept. Under the influence of law, professional and institutional discourses, auditors play a powerful role in external financial reporting and have a significant impact on the meanings and interpretations of the concept. At this juncture little attempt will be made to explain the reasons for the practitioners' views and beliefs. Such explanations form part of the second layer of the thesis and will be offered in chapter 8. In order to highlight the meanings which the auditors attach to the going concern concept, this chapter is divided into four parts.

The first part (section 4.1.) explains the research methods used to obtain the meanings of 'going concern' as seen by auditors. Such research methods eventually led to the development of a questionnaire which was mailed to 3ØØ participants. The second part (section 4.2) describes the selection of the participants. The third part (section 4.3.) refers to the replies obtained from the respondents, highlighting the manner in which they interpret the going concern concept. The chapter concludes with a summary and discussion (section 4.4.)

4.1: RESEARCH METHODS

After a detailed study of the appropriate literature (see chapter 3), semi-structured interviews with 15 experienced audit partners from large, medium and small firms were conducted. The purpose of such interviews was to obtain an undertanding of the social world inhabited by auditors. Such interviews, within the methodological framework are assumed to display realities which extend beyond merely the conversational practices. Such encounters display artful accounts and cultural particulars of professional practices (Silverman, 1985). The accounts of 'going concern' offered by the participants were assumed to be neither naive nor apologetic, but were treated as an informed statement of the social world inhabited by them.

The interviewees included two members of the APC working party responsible for developing the auditing guideline ('The auditor's considerations in respect of going concern') and former as well as current members of the APC. Initially, contact was established with each partner on the telephone and a brief description of the project was given. Upon securing an interview, all partners were sent a letter, which courteously reminded the individuals of the time and venue for the meeting. The discussions with each party lasted a minimum of about 1-1.5 hours and in some cases up to 3 hours. With the participant's permission wherever appropriate, the interviews were taped. Where this was not possible detailed notes were taken of the discussions. In order to deepen the understanding of the relationship between accounting and society, it was considered appropriate to interview directors and liquidators. Such interviews were also considered to be desirable as some participants were making contradictory claims and comments. Therefore, five additional individuals were interviewed. These included three finance directors, one from Europe's largest quoted property company, one from a meat company on the Unlisted Securities Market (USM) and one from an unquoted timber company. Both of the liquidators were well known specialists in their area and partners in a major multinational accountancy firm. In total, 20 individuals were interviewed prior to the designing of the questionnaire.

Subsequently, in order to solicit views on a larger scale, a postal questionnaire was developed. In accordance with the social science literature suggestions (for example see, Fowler, 1984), the questionnaire went through a development stage and eventually 13 individuals were asked to pretest it. These included a member of APC working party responsible for developing the auditing guideline, members of the APC, a recent president of a professional body and others. They were in particular asked to note the time taken to complete the questionnaire, question clarity, persuasiveness of the covering letter and the comprehensiveness of the questionnaire in light of their own views and experiences. One of the pretesters, a recent President of a professional accountancy body and a member of the APC wrote,

"questions were clear but whether

practitioners would answer them is another point".

In order to increase the appeal of the questions, particular attention was paid to the relevance and acceptability of the questionnaire. The pretesters felt that the questions should not take more than an average of 30 minutes to answer and the resulting design was devised with this in mind. The final version (Appendix 1) of the questionnaire was eight pages long[1] and consisted of broadly three parts. Part A consisted of statements inviting auditors to indicate their attitude towards various meanings, interpretations and consequences of the going concern concept on a five point Likert scale. Part B related to the manner in which the auditors may assess the applicability of the going concern concept to businesses. This part also included open-ended questions on matters such as the meaning of 'forseeable future', 'going concern qualifications', reservations on professional pronouncements as well as some functional aspects of auditing such as the data the auditors use to assess going concern strengths or weaknesses. Part C solicited biographical data from the respondents.

The next section explains the manner in which the participants for the postal survey were selected.

4.2: THE PARTICIPANTS

In order to obtain the views of a reasonable cross-section of practitioners, it was decided that the questionnaire would be mailed to 300 individuals. In light of the literature and interviews, it was thought that auditors from the major accountancy firms would have a considerable experience of interpreting and assessing meanings of going concern. The large firms were also of particular interest as between them they train nearly 70% of all potential chartered accountants (Accountancy, June 1987, page 63). The audit manuals of such firms are required reading for students and are thought to be influential in shaping perceptions of audit work (Stamp and Moonitz, 1979). Large firms with extensive turnover (Accountancy Age, 18th June 1987, page 17) also dominate the auditing market[2] and are thus thought to be significant interpreters of the going concern concept in an auditing context.

In view of the dominant position of the major firms, the UK's top 60 firms (as indicated by The Accountant, 26th June 1986, page 15) were included in the sample of 300 firms. The same publication also identified 31 other 'significant firms' which it was assumed would also be major interpreters of the meanings of the going concern concept. In addition, the Audit Report (a monthly publication relating to the wording of the audit reports) was scrutinised from 1984 (its first edition) onwards and nine other firms, associated with going-concern qualifications were identified. This made a total of 100 firms. A further 200 firms were selected at random from the ICAEW handbook. A personalised letter accompanied by the questionnaire was sent to a partner of the firms selected (Appendix 2). This letter was designed with the help of pretesters and contained a promise to send a summary of the research findings, if the respondents so wished. The questionnaires accompanied by a 'Freepost' envelope were mailed in November 1986. The first wave of replies resulted in 89 responses. In accordance with the suggestions of Kanuk and Berenson (1975), a reminder accompanied by a fresh copy of the questionnaire was mailed to non-respondents during January 1987. This yielded 33 further responses. Subsequent telephone calls (as suggested by Sheth and Roscoe, 1975) managed to obtain 9 more responses, making a total of 131. For various reasons as table 4.1 shows, the effective sample was reduced to 281. Overall, the effective response rate of 47%. Interestingly, 7 questionnaires were returned by firms claiming 'not to have adequate experience of the subject matter' but nevertheless were designated as 'training offices' by the ICAEW. The respondents included not only the Big-Eight, but also all of Britain's top twenty firms which between them account for 42.4% of Britain's top 40,000 public and private companies (The Accountant, July 1989, page 7). 44 of the respondents came from the top 60 firms whilst 87 came from other firms. The responses received were analysed by using the SPSSx computer routines. A chi-square test revealed that there was no non-response bias between the first and second wave respondents at 0.05 level.

Though the questionnaire was addressed to a partner and most of the responses came from partners (not necessarily the addressee), some responses also came from individuals holding other posts. In total 107 responses were from partners, 10 from technical directors, 7 from audit managers, 1 each from a group manager, training manager and an audit clerk; four respondents did not identify their job titles. 123 of the respondents had identified going concern problems as part of their work and only 7 had no direct experience of such matters, with one respondent not giving a reply. A chi-square test revealed that there was no significant difference between the replies provided by the two groups at Ø.Ø5 level. 112 of the respondents had been responsible for issuing going concern qualifications whilst 18 had not made any such decision, with one respondent not giving a reply. Once again, a chi-square test revealed that there was no significant difference between the replies provided by the two groups at Ø.Ø5 level. The respondents had auditing experience of 17.91 years on average, and thus were in a position to provide informed insights. Following the receipt of a completed questionnaire, six respondents from large, medium and small firms were interviewed to verify their responses to the questionnaire, taking the total of interviewees to twenty six.

The next section refers to the interpretations and meanings of the going concern concept as indicated by the auditor's responses to the eight page questionnaire.

4.3: PRACTITIONERS' VIEWS

In the first part of the questionnaire, the practitioners were asked to indicate their attitude towards 38 different statements. Each statement related to the meanings, implications and interpretations of the going concern concept in an auditing context. The replies received are shown in table 4.2.

The responses to statements 1, 2 and 3 suggest that the auditors clearly believe that going concern qualifications have important implications for finance and capital markets. Such qualifications contained messages and were seen to be carrying information about the prosperity and well being of a company. 80.9% of the respondents felt that a going concern qualification would cause a negative share price reaction i.e. going concern qualifications were characterised as bringing bad news. 87.8% and 65.6% respectively felt that the going concern qualifications alert institutional and individual investors of uncertainties inherent in financial statements. 65.6% also felt that going concern qualification would alert creditors (statement 4). The auditors clearly believe that the going concern qualification is important. Only 3.8% indicated an agreement to the statement that a 'going concern qualification is of no consequence' (statement 5).

A recurring issue in the literature (see chapter 3) and during interviews was the specific impact of a going concern qualification on client companies. 73.3% of the respondents felt that a going concern qualification reveals risks previously hidden and this revelation will increase the client's financial problems (statement 6). The interviewees identified these as problems in securing bank overdrafts, loan, credit terms and credit rating. Such perceived messages could not only threaten company survival but could also very quickly alter the validity of the audit opinion given. If the client is experiencing going concern problems then the uncertainties are at the forefront of an auditor's mind. In such circumstances, would the auditors try to complete the audit quickly or try to delay completing the audit in order to see resolution of some of the uncertainties and also enable the client to secure aditional financial resources? Statement 7 addressed such matters and in response, 35.9% of the respondents felt that a client experiencing going concern problems should be given more time by the auditor, whilst 45.1% disagreed with the suggestion. If the going concern qualification is indicative of new and negative information then can it precipitate the client company's failure (statement 8)? Here 36.6% of the respondents disagreed arguing that audit qualifications do not cause company failures whilst 40.5% agreed arguing that the audit report must be instrumental in precipitating a company failure. Many of the interviewees felt that one consequence of a going concern qualification is to increase the client's cost of obtaining finance (statement 9) and eventually increase the cost of capital and affect investment opportunities. 62.6% of the respondents agreed with this scenario whilst 20.5% disagreed.

By issuing a going concern qualification, an auditing firm may attract publicity which may be damaging to its profitability. Statement 10 asked whether the resulting publicity is bad? According to the respondents, the reverse appears to be true here. 74% felt that going concern qualifications do not provide adverse publicity to their firms whilst only 13% felt that they did. By issuing a going concern qualification, is the auditor commenting on the management's abilities (statement 11)? Here the respondents were almost equally divided. 36.7% felt that such qualifications are not a reflection on the manner in which the management handle a company's affairs, whilst 34.4% felt that going concern qualifications are a reflection on the personal skills of the management. The views expressed may be indicative of possible behind the scene pressures, perceptions and conflict over the auditor's ability and desire to issue a going concern qualification. Does a decision to issue a going concern qualification enhance a firm's credibility (statement 12)? 35.1% disagreed with the proposition whilst 36.6% felt that such qualifications give the public a reminder of the firm's independence, objectivity, honesty and professional skills, 28.2% on the other hand were unsure.

What is the difference between an unqualified audit opinion and an opinion expressing a going concern qualification? Many users of financial statements believe (see Purewal and Sikka, 1987 for a survey) that an unqualified audit reports suggests that in the auditor's opinion a business is financially viable (statement 13). 40.5% disagreed with the suggestion whilst 50.2% agreed. Almost every auditor argued that he/she had the professional skills and ability to correctly diagnose going concern problems, but due to various pressures, potential law-suits and other reasons they were unable or unwilling to subsequently issue a going concern qualification. Some interviewees actually cited instances where due to the resulting pressure, they actually lost the client or were unable to secure additional business from the client. In response to statement 14, 39.7% of the respondents felt that a going concern qualification increases the likelihood of their firm losing the client, whilst 42% felt that it made no difference. Does the firm's reputation for issuing going concern qualification scare off any potential clients (statement 15)? 71% felt that the potential clients are not lost by the firm's decisions to issue going concern qualifications and only 7.6% felt that the potential clients would be lost. Does a going concern qualification increase the likelihood of a law-suit against a firm (statement 16)? In fact, the reverse seems to be true. 71% felt that it does not and only 10.7% agreed with the suggestion. To some (see chapter 3), going concern means alerting the users of financial statements of the likelihood of insolvency (statement 17). On this issue, the accountancy firms appear to be divided: 32.1% agreed with the suggestion that auditors should be required to alert investors on the likelihood of company insolvency whilst 54.2% disagreed with this.

Chapter 3 noted that there has been a tendency to interpret 'going concern' in a literal sense i.e. a business which will survive and continue for the forseeable future. In order to survive in a capitalist economy, a business needs to remain competitive for the forseeable future. Therefore, a question arises about the auditor's role in satisfying himself about the business's competitiveness (statement 18). 73.3% disagreed with any role for the auditor in becoming involved with reporting on competitiveness whilst 21.4% agreed. Survival, prosperity and ability to remain in continuing existence is also dependent on at least retaining, if not increasing the market share (statement 19). Here a massive 87% felt that such matters are the directors' domain and did not see any role for the auditor, whilst 4.6% felt that the auditor should take active steps to satisfy himself that a business will retain its market share. Much of the auditing literature (for example, Lee, 1984), including the auditing guideline (APC, 1985a) suggests that 'going concern' implies auditor's involvement with future oriented data. However, many interviewees were uneasy with such a suggestion, as in their mind through his/her involvement with plans etc., the auditor may give the impression that he has authenticated the company's financial plans. The respondents were asked to consider whether they should be required to analyse the company's financial plans (statement 20). 48.1% felt that the auditors should, but 32.1% contrary to the exhortations by Strachan (1975) felt that they should not be involved with such an analysis.

Chapter 3 noted that in the going concern auditing guideline (APC, 1985a), the professional bodies advocated a 'passive approach'[3] (Charlesworth, 1985) for auditor's and rejected the alternative 'active approach'. Some commentators (e.g. Woolf 1983b) advocated the 'active approach', whilst others (Hinton, 1983 and 1985; Jones, 1985) gave a somewhat confusing account altogether. The passive v active conflict was considered to be central to discussions about going concern and was raised by almost all the interviewees, even when not prompted. Therefore, the respondents were asked to consider whether 'the auditor should take active steps to satisfy himself/herself that an enterprise is a going concern' (statement 21). No respondent indicated strong disagreement with the statement and only 8.4% indicated disagreement. A massive 88.5%, contrary to the official line (APC, 1985a), supported the adoption of an 'active approach'.

The auditor's have statutory rights (for example, under the Companies Act 1985) of information and explanations from the management and inside information which is not available to external users of the financial statements. The superior information, professional education and privileged position may mean that the auditors are in a better position to predict resolution of uncertainties. However, following the views of the Cohen Commission (AICPA, 1978, page 27), statement number 22 of the questionnaire was expressed in the negative, i.e. the "auditor is no better position than the financial statement user to predict resolution of uncertainties". 64.1% of the respondents disagreed with the statement, thus suggesting that the auditor is in a better position to predict resolution of uncertainties whilst 25.9% agreed with the statement. During the interviews, auditors, directors and liquidators strongly expressed the view that the auditors should consider ways of increasing the value of audit reports and financial statements by explaining how they arrived at their conclusions relating to going concern matters (statement 23). 42.7% of the respondents disagreed with the suggestion that the auditor should explain how he/she made going concern decision whilst 48.7% agreed with the suggestion. Lack of cashflow has frequently been cited (Lee, 1984; Kharabanda and Stallworthy, 1985) as a major reason for insolvency and the professional literature (for example, APC, 1985a) asks auditors to pay attention to cash forecasts. The interviewees agreed that cash forecasts provide useful indicators of likely going concern problems and that the companies should even consider publishing such statements. But would the auditors be willing to report on such statements if they were to be published (statement 24)? 47.3% of the respondents felt that the auditor should not report on cash flow forecasts whilst 40.4% felt that if such statements became a part of the financial statements, then they ought to report on them.

The audit reports are a medium of communication, but did the respondents feel that the existing going concern qualifications (see APC, 1980a and 1985a) are very informative (statement 25)? 42.8% felt that they are not very informative whilst 45.1% were satisfied. The Canadian practice is that the financial statements should disclose the uncertainties (see chapter 3 for a summary) and if the auditor is satisfied that the disclosure is adequate then no going concern (or other) qualification is warranted. By contrast, the British position has been that the auditor should comment on going concern uncertainties either by qualifying or by issuing an 'emphasis of matter' report. During interviews, some respondents felt that the value of 'going concern' audit reports was being eroded by a proliferation of audit qualifications and this tendency ought to be curbed by adopting the Canadian approach (statement 26). However, 74.8% disagreed with this suggestion whilst 15.3% supported it.

Currently, the going concern auditing guideline (APC, 1985a) appears to recommend a 'subject to' type of audit report by treating going concern as a material but not fundamental (contrary to SSAP 2) uncertainty. The guideline does not rule out the issues of a 'disclaimer of opinion', but the specimen audit reports refer to a 'subject to' audit opinion. The respondents had to decide whether a 'disclaimer' was the most appropriate audit opinion (statement 27). 74.1% rejected the use of 'disclaimer of opinion' for going concern qualification whilst only 7.7% preferred it. As responses to statement 28 show, 73.3% of the respondents felt that the status-quo ought to be maintained and 'subject to' type of opinions should be continued. The 'subject to' type of opinion is of American origin and was crtiticised by the Cohen Commission as being "difficult to understand" and "ambiguous" (AICPA, 1978, page 25)[4]. It is not clear whether the users understand the significance of a going concen qualification (statement 29). 39% of the auditors felt that they did. 28.2% felt that they did not and 32.8% were undecided.

A related question is, what in the auditors' view is the purpose of a going concern qualification? This question was posed in part c) of the questionnaire and the auditors were invited to indicate the meanings they attached to a going concern qualification. As table 4.3 indicates, a considerable variety of meanings are attached to a going concern qualification by auditors. Whilst much of the professional literature argues that auditors cannot be expected to warn external users of impending solvency and liquidity problems, many respondents felt that the purpose of a going concern qualification is to 'alert shareholders and other investors and creditors of impending solvency and liquidity problems', 'inform shareholders that the company has possible financial problems'. Whilst the professional literature (for example, see Lee, 1986) argues that an auditor has no responsibility for reporting on efficiency or effectiveness of a company, many respondents felt that the purpose of a going concern qualification is to 'alert the reader of the risks surrounding investments in or dealings with the client company', 'warning of possible liquidation unless steps are taken to deal with the situation'. Whilst the legislation (for example, Companies Act 1985), auditing standards and case law may restrict auditor obligations to shareholders only, some respondents felt that the purpose of a going concern qualification is to alert 'management, members and third parties on future viability of the business'. Some auditors saw the qualification purely as an insurance policy which would protect them in a lawsuit, in that they had already highlighted material uncertainties and thus a litigant could not accuse them of being a party to misleading financial statements.

Much of the accounting literature (see chapter 3) states that in the event of the going concern assumption being invalid, the financial statements need to be drawn up on a non-going concern basis by the directors. Such financial statements need to show assets at their recoverable values. However, in order to audit such financial statements effectively the auditors also need to be familiar with the various valuation bases. Statement 30 sought views on the auditors' ability to do this. 59.5% felt that they did not have sufficient ability to ascertain or attest recoverable values of assets whilst 29.8% felt that they did. It should also be noted that the traditional literature (see chapter 3) associated going concern with choice of valuation bases. Following this, attempts were made to enagage every interviewee in some discussion of valuation bases but none of them were willing to discuss the matter in any detail. Further aspects of this issue will be discussed in chapter 8.

Following the arguments of chapter 2, it would be appreciated that the going concern auditing guideline is unlikely to be neutral. It may have consequences for auditors and auditees. During the interviews, many participants indicated that the auditing guideline was unsatisfactory (also see chapter 7) as it failed to consider the points they regarded as relevant. Prime amongst their objections was the feeling that the guideline gave the impression that that the 'auditor is required to give assurances on the financial viability of the company audited' (statement 31). 42.7% felt that the guideline indeed gave this impression whilst 38.2% felt that it did not. On the other hand, the guideline was also welcomed as it appeared to redress the balance of power between auditors and management (statement 32). 64.1% felt that the auditing guideline has 'strengthened the auditor's ability to withstand pressure from management' whilst 20.7% disagreed with the statement. The going concern auditing guideline attempts to deal with auditor responsibility in an area which has been the subject of considerable litigation[5].

The guideline, by giving publicity to an area, may increase auditor awareness yet at the same time it may mark out an arena for further dispute. The respondents were asked to consider whether the guideline 'has increased the possibility of a law-suit against your firm' (statement 33). 45.8% disagreed with the suggestion whilst 24.5% felt that on balance the guideline has increased the likelihood of a lawsuit against their firm by making issues of auditor responsibility highly visible. The auditing standards and the going concern guideline contain examples of going concern qualifications. Such examples, in appropriate circumstances may have persuaded auditors to issue qualified reports, where previously they might not have. The respondents were asked to consider whether 'the auditing guideline has increased the likelihood of you issuing a going-concern qualification' (statement 34). In response, 46.5% of the respondents felt that the auditing guideline has increased the likelihood of them issuing a going-concern qualification whilst 32% felt that it did not. Some interviewees regarded going concern qualifications of recent origin and felt that in view of the changing economic and litigious environment, they may issue more going concern qualifications now than ever before. Statement 35 expanded on this and discovered that 38.2% felt that they are more likely to issue going concern qualifications now whilst 39.7% felt that the current developments would not have any impact on their decisions.

Has the going concern guideline been of any use to the accountancy firms (statement 36)? 21.4% felt that the auditing guideline was of little use to them but 65.6% found it to be useful. This is despite the point (from the answers to open-ended questions in part b) of the questionnaire) that 101 (77%) respondents felt that the guideline did not change any of their auditing procedures and 47 (36%) expressed reservations concerning the contents of the guideline. In response to statement 37, 62.6% wanted the APC to give some guidance on the 'techniques useful for making going-concern decisions', but 21.4% were opposed to this. 36.7% of the respondents felt that the auditing guideline increased the audit costs whilst 41.9% felt that it did not (statement 38).

The auditors believed that going concern problems could be identified with the aid of selected statistics and data. A number of items and approaches were considered to be helpful. These included accounting ratios; forecasts; Z-scores; computer graphs depicting trends, averages, etc., and a variety of other approaches. The various approaches and combinations considered to be helpful by the auditors are shown in table 4.4.

The table shows that considerable use of accounting ratios is made by 118 firms, but rarely on their own and frequently in conjunction with other approaches. Accounting ratios have been traditionally used to make financial predictions. Much of the recent literature, often relying upon discriminat models has further suggested that the auditors can use some ratios to make going concern predictions (see Appendix 3 for a summary). The interviewees were asked to indicate the ratios they considered to be useful in making going concern evaluations. In addition, they were asked to consider and choose the ratios which various researchers have suggested would be useful to auditors. The resulting list of ratios was included in section c) of the questionnaire and the respondents were asked to indicate the importance they attach to each of the them. The responses (table 4.5) show that ratios such as creditor turnover, gross profit margin and the current ratio are considered to be very important by the practitioners. Ratios such as debtor turnover, stock turnover, current assets/total liabilities, net income/net sales, total debt/total assets, interest cover and cash flow/total debt were also considered to be important. Other ratios attracted low to moderate ranking. Table 4.4 also shows that 114 firms made some use of company forecasts to identify going concern problems. Once again, these were frequently used in conjunction with other approaches. But do the auditors require their client companies to prepare financial plans for the forseeable future? 27 respondents stated (section (b) of the questionnaire) that they did whilst 102 did not. In the absence of a financial plan, the auditors stated that they adopt a number of alternative strategies (table 4.6). These included discussions with the management, the auditor himself preparing the forecast, encouraging the client to prepare one, review of post balance sheet events etc. Contrary to the advice by AISG (1975), Strachan (1975), Blackwood (1976), APC (1976) and others, 16 respondents felt that the forecasts were nothing to do with audit work and would therefore not examine such items. Z scores have been considered to be useful for auditors (Altman and McGough, 1974; Taffler and Tisshaw, 1977; Taffler and Tseung, 1984) and table 4.4 shows that 20 firms were using them. 10 firms used graphs produced by modern desk top computers to discern patterns and identify going concern problems.

As the auditors claimed to be looking at patterns, what kind of a period did they examine? A wide range of beliefs existed amongst the respondents (table 4.7) with three years (including past and future) being the most popular period for discerning a pattern for the identification of going concern problems. The interviewees believed that they needed to look at the trends in order to make judgements and predictions. Is there any minimum information which the auditors look at to identify going concern problems? As table 4.8 shows, 43 auditors believed that as a minimum they needed to look at forecasts, profit and cash position to identify going concern problems. 31 auditors referred to current draft accounts only to make going concern decisions, whilst 23 focused on key accounting ratios. 24 respondents felt that the answer would depend on each case and thus did not specify the minimum information needed.

The identification of going concern problems was considered to be a task primarily for senior and experienced personnel (see table 4.9), reflecting the power of the organisational hierarchical work relationships. In 56 firms, the audit partners were responsible for such tasks and in 44 cases the task was done jointly by partner and manager. The ultimate decision to issue a going concern qualification, as table 4.10 shows, is made by partners. In 99 cases the audit partner on his own decided, but in 23 cases the firms had a panel of partners which advised. In all cases, the going concern judgements depended on the perceptions of the individuals involved. 18 respondents had formal written policies for issuing going concern qualifications (see part b) of the questionnaire) whilst 112 firms had no written firm-wide policy, as the matter was thought to be dependent on judgements which could not be codified. The identification of going concern problems and the decision to issue a qualified opinion is also influenced by a consideration of the meaning of the phrase 'forseeable future' - something which is inherent in discussions of going concern (see chapter 3). SSAP 2 (ASC, 1971) does not define the term, but the going concern guideline (APC, 1985a) stated that it "should normally extend to a minimum of six months following the date of the audit report or one year after the balance sheet date whichever period ends on the later date" (APC, 1985, para 8). Table 4.11 shows that a considerable variety of meanings are attached to the term 'forseeable future'. This included a support from 37 firms for the traditional 12 months from the balance sheet date and 31 firms supporting the 12 months from the audit report date. The definition preferred by the Auditing Practices Committee in the going concern guideline, only had the support of 19 firms out of a total of the 129 responding firms.

4.4: SUMMARY AND DISCUSSION

Chapter 3 noted a particularly widespread concern with the going concern concept in an auditing context starting from the 1970s and eventually leading to the issuance of an auditing guideline in August 1985. This chapter added to this layer by noting the views of the practitioners. The auditors' views were solicited through a postal survey of 300 firms, resulting in 131 useable responses. The questionnaire was devised after an extensive literature review and a large number of interviews. The responses in this chapter show a considerable diversity of interpretations and meanings of the concept. These are highlighted in figure 4.1

Figure 4.1

Some Meanings and Implications of Going Concern

Auditor should 'actively' satisfy himself that a business is a going concern.
Auditors should not be required to alert investors on the likelihood of insolvency.
The auditing guideline gives the impression that the auditor is giving assurances on the financial viability of a company.
Auditor should not focus on company competitiveness and market share.
Auditor should analyse company plans but not be required to report on cashflow forecasts.
Forseeable future has many meanings.
Going concern evaluations may be related to management ability.
A going concern qualification has many meanings.
Going concern qualifications are important and have consequences for share prices, investors and creditors.
A going concern qualification could lead to the loss of a client.
Going concern qualifications increase a client's financial problems and increase cost of finance.
Going concern qualifications do not give bad publicity to auditing firms and do not damage their credibility.
Unqualified audit opinion indicated that a business is a going concern.
Auditor should issue a going concern qualification even if all material uncertainties are disclosed.
Auditors do not have the know-how to ascertain the recoverable value of assets.
The auditing guideline has strengthened the auditor's ability to withstand pressure from management.
The auditing guideline has increased the incidence of firms issuing a going concern qualification.
The guideline may be helpful in combating law-suits against the firms.
Going concern problems can be diagnosed by focusing upon trends with the aid of ratios, forecasts and other approaches.
The profession should develop techniques useful for making going-concern decisions.

Much of the accounting literature relates the concept to questions of valuation bases. It is the frequently invoked to justify the use of replacement costs, realizable values, cash flow accounting etc., but no interviewee was willing or able to discuss such bases. Much of the literature argues that a different set of principles is applicable to non-going concerns and that in such cases the assets and liabilities need to be stated at their realisable values. This advice is also contained in the auditing guideline. However, the auditors argued that they did not have the know-how to ascertain such values. The auditing guideline states that for going concern issues, the auditor should adopt a 'passive approach', whereas a large number of respondents supported the 'active approach'. The going concern concept is almost always linked to the notion of a 'forseeable future'. Very few of the respondents supported the profession's preferred definition of 'six months from the audit report date or twelve months from the balance sheet date, whichever is the longer'. It is as though many of the respondents were refusing to be interpellated by some aspects of the auditing guideline. It is possible that the guideline may be directly addressing the 'interests' of some practitioners and not others. These aspects will be pursued in chapter 8.

The auditors believe that the going concern qualifications have consequences for share prices, institutional investors, private investors and creditors. The implications for finance were uppermost in the practitioner's minds. The respondents argued that a going concern qualification adds to a client's financial problems, cost of capital and could precipitate company failures with possible implications for auditor liability. The traditional literature freqently presents the auditor as an umpire or an unbiased arbiter who will present the 'truth' and put the interests of users of financial statements above his own. However, as chapter 8 will explain, this may only be possible, as long as the interests of the users' are constructed to being synonymous with those of the auditors.

In much of the literature (see chapter 3), the concept is associated with survival and continuity of the business in some shape, but the auditors showed little enthusiasm for becoming involved with reporting on a company's market share and competitiveness. Indeed, many auditors felt unhappy with the auditing guideline because they felt that it sought to discuss an area of responsibility which is best not articulated. They would have preferred the auditing guideline to concentrate on techniques for making going concern evaluations.

Accounting ratios have been in use for the best part of the twentieth century where bankers calculated simple statistics to make assessments about the recoverability of loans (Horrigan, 1968). The auditors confirmed using accounting ratios to make predictions about corporate survival, but such ratios were very rarely used on their own. They were very frequently supplemented by forecast and narrative data. However, there is another aspect. Due to the lack of any published future oriented information, the use of ratios derived from the past published accounting data by external users may be understandable. But, by virtue of their statutory rights, the auditors have access to information about forecasts, budgets and plans, yet auditors use ratios from the past data to make going concern predictions. Why? The professional literature argues that an unqualified audit report should not be associated with financial viability, yet some 50% of the respondents felt that a clean audit report indeed implies 'financial viability'. Many respondents also welcomed the auditing guideline as it was seen to be helpful in resisting pressures from the management. Some saw it as a useful device for protecting auditors from lawsuits. The guideline was also seen as a political tool which would be helpful in informing media and 'significant others' of auditor responsibilties.

The multi-accented nature of going concern is once again visible. Many of the contradictions, similarities and diversity of meanings may be due to the dynamics of capitalism, power and control of regulatory bodies, the existence of some elites and the auditors' need to accomodate some prior interests. Any theory which sees social world and accountancy profession as flat, harmonious and homogeneous is unlikely to get very far in explaining the diversity of practices. On the other hand, theories which assume the existence of ideological contestation, multi-accentuated nature of concepts, a fractionated profession and tension between various large and small firms are more likely to be able to offer insights into the changing meanings and interpretations of the concept. The shifting of the meanings may well be indicative of some bases of power and some organising ideologies at work. The methodological framework advanced in chapter 2 is indeed of this kind. Chapter 8 will use such theories to provide an explanation of the various meanings and interpretations of the concept by auditors.

Chapter 4 Footnotes

1) The questionnaire length is always problematic. The researcher has to strike a balance between what he would like to know, what the subjects would like to know, what the subjects would like him to know, and the free time the participants are willing to offer. According to the survey literature, reasonable length is not necessarily a barrier to responses. For example, Champion and Sear (1969) sent three, six and nine page questionnaires and noted that the nine page questionnaire obtained a higher response rate as it managed to engage the subjects' imagination and therefore became more interesting. The eventual eight page questionnaire for the research described in this chapter was considered to be interesting by the relevants and did not receive any adverse comments from any of the pretesters.

2) Of the UK's top 250 companies 230 are audited by the top eight accountancy firms (The Accountant, 27th May 1987).

3) Chapter 7 will examine some of the reasons behind the Auditing Practices Committee's preferences for the 'passive approach'.

4) In the USA, the going concern auditing standard SAS 34 has now been replaced by SAS 59. It does not advocate the use of 'subject to' audit opinion for going concern qualifications.

5) See chapter 6 for more details.

Table 4.1

Analysis of Responses Received from Accounting Firms

Questionnaires Issued		300
Less		
Firms no longer in existence due to mergers:-		
Spiro & Co. merged with Casson Beckman (32)	1	
Hodgson Impey merged with Chalmers Impey (20)	1	2
		298
Returned marked 'gone away'	5	
Questionnaire returned as the firms did not have adequate experience of the subject matter	7	
Firms not wishing to participate in any research	3	
Too busy	1	
Wanted money to complete the questionnaire	1	
		17
Net Sample		281
Responses Received		131
Response Rate		47%

Sample Split

	Top 60 Firms	Other Firms	Total
Sample	60	221	281
Responses	44	87	131
Response Rate	73%	39%	47%

Table 4.2
Responses to the Auditor and Going Concern Decisions Questionnaire

The respondents were asked to indicate their attitude towards each of the following statements.

	% RESPONDING				
	STRONGLY DISAGREE	DISAGREE	UNSURE	AGREE	STRONGLY AGREE
1) Going-concern qualifications cause a negative share price reaction in the client company's share price.	1.5	5.3	12.2	49.6	31.3
2) Going-concern qualifications alert institutional investors to uncertainties inherent in the financial statements.	0.8	6.1	5.3	48.9	38.9
3) Going-concern qualifications alert individual investors to uncertainties inherent in the financial statements.	-	9.2	25.2	51.9	13.7
4) Going-concern qualifications alert creditors to uncertainties inherent in the financial statements.	0.8	9.9	23.7	42.7	22.9
5) Going-concern qualification is of no consequence.	66.4	26.7	3.1	1.5	2.3
6) A going-concern qualification is likely to increase the client's financial problems.	1.5	11.5	13.7	61.1	12.2
7) A client experiencing going concern problems should be given more time by the auditor.	13	32.1	19.1	26.7	9.2
8) Going-concern qualification is likely to precipitate the client company's failure.	7.6	29.0	22.9	31.3	9.2
9) A Going-concern qualification is very likely to increase the client's cost of obtaining finance.	2.3	18.3	16.8	44.3	18.3
10) Going-concern qualifications give bad publicity to your firm	42.7	31.3	13	12.2	0.8
11) Going concern qualifications are a reflection on the management's abilities.	4.6	32.1	29	31.3	3.1
12) A decision to issue a going concern qualification enhances your firm's credibility.	7.6	27.5	28.2	35.1	1.5

	% RESPONDING				
	STRONGLY DISAGREE	DISAGREE	UNSURE	AGREE	STRONGLY AGREE
13) An unqualified audit report indicates that in the auditor's opinion the business is financially viable.	11.5	29.0	8.4	48.9	2.3
14) A decision to issue a going-concern qualification increases the likelihood of your firm losing that client.	3.1	38.9	18.3	37.4	2.3
15) A decision to issue going-concern qualification increases the likelihood of your firm losing potential clients.	16.8	54.2	21.4	5.3	2.3
16) A going-concern qualification will increase the likelihood of a law-suit against your firm.	23.7	47.3	18.3	7.6	3.1
17) Auditors should be required to alert the investors on the likelihood of company insolvency.	16.8	37.4	13.7	26	6.1
18) Auditors should take active steps to satisfy themselves that the business remains competitive in the forseeable future.	26.7	46.6	5.3	19.1	2.3
19) Auditors should take active steps to satisfy themselves that the business retains its market share.	35.1	51.9	8.4	3.1	1.5
20) Auditors should not be required to analyse the company's financial plans.	6.9	41.2	19.8	29	3.1
21) The auditor should take active steps to satisfy himself /herself that an enterprise is a going-concern.	-	8.4	3.1	61.8	26.7
22) The auditor is in no better position than the financial statement user to predict the resolution of uncertainties.	12.2	51.9	9.9	20.6	5.3
23) The auditor should explain to the users how he/she made his/her going concern decisions.	12.2	30.5	8.4	42.7	6.1
24) If the companies publish cashflow forecasts then the auditors should be required to report on them.	9.9	37.4	12.2	35.1	5.3
25) Going-concern qualifications are not very informative.	9.2	35.9	12.2	42.8	Nil

	% RESPONDING				
	STRONGLY DIS AGREE	DIS AGREE	UN SURE	AGREE	STRONGLY AGREE
26) If financial statements disclose all material uncertainties, then the auditor should not issue a going-concern qualification.	18.3	56.5	9.9	12.2	3.1
27) 'Disclaimer of opinion' should be the most appropriate form of audit qualification for going concern problems	13	61.1	18.3	4.6	3.1
28) 'Subject to' audit reports are the most appropriate for going-concern qualification.	3.1	9.2	14.5	67.2	6.1
29) Users do not understand the significance of a going-concern qualification.	6.9	32.1	32.8	26.7	1.5
30) For a non-going concern, auditors do not have the know how to ascertain the recoverable value of assets.	4.6	25.2	10.7	51.1	8.4
31) The auditing guideline gives the impression that the auditor is giving assurances on the financial viability of the company audited.	3.1	35.1	19.1	37.4	5.3
32) The auditing guideline has strengthened the auditor's ability to withstand pressure from management.	3.1	17.6	15.3	62.6	1.5
33) The auditing guideline has increased the possibility of a law-suit against your firm.	6.9	38.9	29.8	23.7	0.8
34) The auditing guideline has increased the likelihood of you issuing a going-concern qualification.	5.3	26.7	21.4	45	1.5
35) We are likely to issue more going-concern qualifications now.	9.2	30.5	22.1	37.4	0.8
36) The APC guideline is of little use to my firm.	13.7	51.9	13	15.3	6.1
37) The APC should develop an auditing guideline indicating the techniques useful for making going-concern decisions.	2.3	19.1	16	57.3	5.3
38) The APC guideline has increased the audit costs.	5.3	36.6	21.4	32.1	4.6

Table 4.3

The Purpose of a Going Concern Qualification

Purpose	No. of times Mentioned
To alert shareholders and other investors and creditors of impending solvency and liquidity problems	36
To inform the shareholders that the company has possible financial problems.	14
Alert the reader of the risks surrounding investments in or dealings with the client company.	13
Warning of possible liquidation unless steps are taken to deal with the situation.	13
Alert users that the accounting policies may not be appropriate	9
Alert users of the need for 3rd party financial support which if withdrawn may lead to corporate collapse	7
Alerting management, members and 3rd parties on future viability of the business.	7
Protects the auditor's position	4
To highlight what in our opininon is a deviation from the accounting convention which may have a material impact on the values in the financial statements.	4
To highlight impairment of 'truth and fairness'.	3
Indicates that the accounts are not misleading	2
Alerting shareholders and other users to material uncertainties	2
It is a comment on the viability of a business.	2
To draw attention to inadequacies in the system and our doubts as to the efficient running of the business.	1

Cont'd

Alert users of the possibility that the concern may not be able to trade at expected levels	1
To better inform the shareholders thus allowing them to make better judgements about directors' performance.	1
Warning that assets might be overvalued	1
To warn the reader that the accounts may be suspect	1
Removes the impression that the auditor is giving assurances on financial viability.	1
In small companies it serves no purpose	1
Warn the users that the balance sheet values are not necessarily net realisable values.	1
Expresses doubts about disclosure of assets and liabilities	1

Table 4.4

The Approaches Used for Identification of Going Concern Problems

Approach	No. of Firms using it
Accounting Ratios	118
Company Forecasts	114
Z Scores	20
Graphs etc	10
Variety of Other approaches	67

Under the heading 'Other' following items were mentioned.

Item	No. of Mentions
Discussions with management	19
Support from bankers	14
Judgement	10
Post balance sheet events	9
Knowledge of client's business	9
Financial agreements	8
Pressure from creditors	8
Industrial relations problems	2
Independent economic forecasts	1
Dishonoured cheques	1
Debenture trust deed covenants	1
Net realisable value of assets	1

The combination of the approaches used was as follows:

Approaches	No. of Firms
Accounting ratios	5
Company forecasts	2
Other	1
Accounting Ratios and Forecasts	37
Accounting Ratios and Other	4
Forecasts and Other	4
Accounting Ratios, Forecasts and Other	48
Accounting Ratios, Forecasts and Z Scores	14
Ratios, Forecasts, Graphs and Other	4
Ratios, Z Scores, Graphs and Other	1
Ratios, Forecasts, Z Scores, Graphs and Other	5
Depends on each case/ Not answered	6
Total	131

Table 4.5

The Importance Attached to Accounting Ratios Considered to be Useful for Detecting Going Concern Problems

RATIOS	MEAN SCORE
Creditor Turnover	4.75
Gross Profit Margin	4.57
Current assets/current liabilities	4.42
Current assets minus stock /current liabilities	4.26
Debtor Turnover	3.97
Stock Turnover	3.85
Current assets/total liabilities	3.45
Net income/ net sales	3.4
Total debt/total assets	3.28
Operating profit before interest and taxes/interest expense	3.14
Cash flow/total debt	3.12
Current liabilities/total assets	2.92
Working capital/total assets	2.91
Current assets/total assets	2.89
Net income/total assets	2.87
Earnings before interest and taxes/ total assets	2.77
Total liabilities/shareholders' funds	2.76
Working capital/net sales	2.6
Operating profit/shareholders' funds	2.52
Operating profit before taxes/total tangible assets	2.45
Common equity/ total debt	2.44
Profit before tax/current liabilities	2.42

Cash/total assets	2.4
Sales/total assets	2.36
Current assets/net sales	2.31
Retained earnings/total assets	2.31
Shareholders' funds/ fixed assets	2.17
Market value of equity/book value of total debt	1.98

Other Accounting Ratios mentioned	No. of Mentions
Cashflow from Normal Operations/ Immediate Liabilities	1
Working Capital Operating Cycle	1
No Credit Interval	1
Turnover/ No. of Employees	1
Margin of Safety	1

Note: The responses were on a scale of 1 to 5, where 1 = of no importance, 2 = of very little importance, 3 = of moderate importance, 4 = important, 5 = Very important.

Table 4.6

Action Taken if the Client Company does not have a Cash Forecast

Action	No. of Mentions
Hold discussions with the management	27
We would prepare a rough and ready forecast	25
Encourage and help the client to prepare one	17
Do Nothing/ Matter does not concern the auditor	16
Look at post balance sheet events	7
Depends on my judgement	7
Thoroughly review financial statements	6
Insist on its preparation	5
Examine bank correspondence	4
Pay attention to the company's liquidity position	4
Reluctantly accept the position	3
Cash Forecasts are of no interest to an auditor	1

Table 4.7

The Length of the Period(s) for which Data is examined to Identify Going Concern Problems

The respondents indicated that where appropriate they would consider management plans and forecasts. Including this, the diagnostic data would relate to the following:

Period	No. of Firms
1-2 years	1
2 years	15
2-3 years	12
3 years	51
2-5 years	1
4 years	8
3-5 years	5
5 years	15
Depends on Judgement	16
No Answer	7
Total	131

Table 4.8

The Minimum Information Needed to Identify Going Concern Problems

Minimum Information	No. of Mentions
Review of Forecasts, current profits and the cash position	43
Position per Current Draft Accounts	31
Key Accounting Ratios	23
Evidence of Financial Support	17
Subsequent Management Accounts	12
Evidence of Pressure from Creditors	10
Liquidity position	9
Management Representations	9
Economic Climate Relevant to the Industry	7
Last two years balance sheet	5
Focus on net current liabilities	3
Current Income Statement	3
Discussions with Financiers	3
Factors per the APC Guideline	3
Current Value of Assets	1
Market Trends	1
Intuition	1
Depends on Judgement	24

Table 4.9

Responsibility for Identifying Going Concern Problems

Audit Partners	56
Audit Managers	13
Partner + Manager	44
Panel of Partners	2
Audit Partners + Technical Dept	2
Other Staff	6
No Reply	1
Total	131

Table 4.10

Responsibility for Issuing Going Concern Qualifications

Partners	99
Partner + Audit Manager	6
Panel of Partners	23
Partners + Technical Dept	2
No Reply	1
Total	131

Table 4.11

Meaning of 'Forseeable Future'

Meaning	No. of Firms
12 months from the balance sheet date	37
12 months from the audit report date	31
Varies according to the clients' business	22
Per the APC guideline	19
2 years from the balance sheet date	5
2-3 years from the balance sheet date	4
3 months from the audit report date or the balance sheet date whichever is the later	2
6-12 months from the balance sheet date	2
6 months from the audit report date	1
1-2 years from the audit report date	1
1-3 years from the balance sheet date	2
3-5 years from the balance sheet date	2
2-4 years from the balance sheet date	1
No Answer	2
Total	131

PART II

The second layer of this thesis consists of four chapters, i.e. chapters 5, 6, 7 and 8. The first layer (covered in chapters 3 and 4) was concerned with the meanings which various scholars, institutions and practitioners attached to the going concern concept. In that layer little effort was made to explain the sociopolitical influences which have shaped the meanings and interpretations of the concept. Now, within the methodological framework of chapter 2, the second layer will provide an explanation of the various meanings of the going concern concept to illuminate the relationship between accounting and society. The broad relationship between the first and second layer of this thesis is shown in figure II.I. Each subsequent chapter is devoted to the following specific tasks.

Chapter 5 traces some of the early influences on the development of the concept from the late 19th century to the 1970s. This is meant to be an exploratory rather than an exhaustive analysis.

Chapter 6 explains the rise of the going concern concept in auditing. In the UK, prior to the 1970s, the concept was rarely mentioned in an auditing context. However, as chapter 3 noted, such references became plentiful from the 1970s onwards culminating in the issue of an auditing guideline. This chapter explains the social, political and economic developments which led to the invocation of going concern in an auditing context.

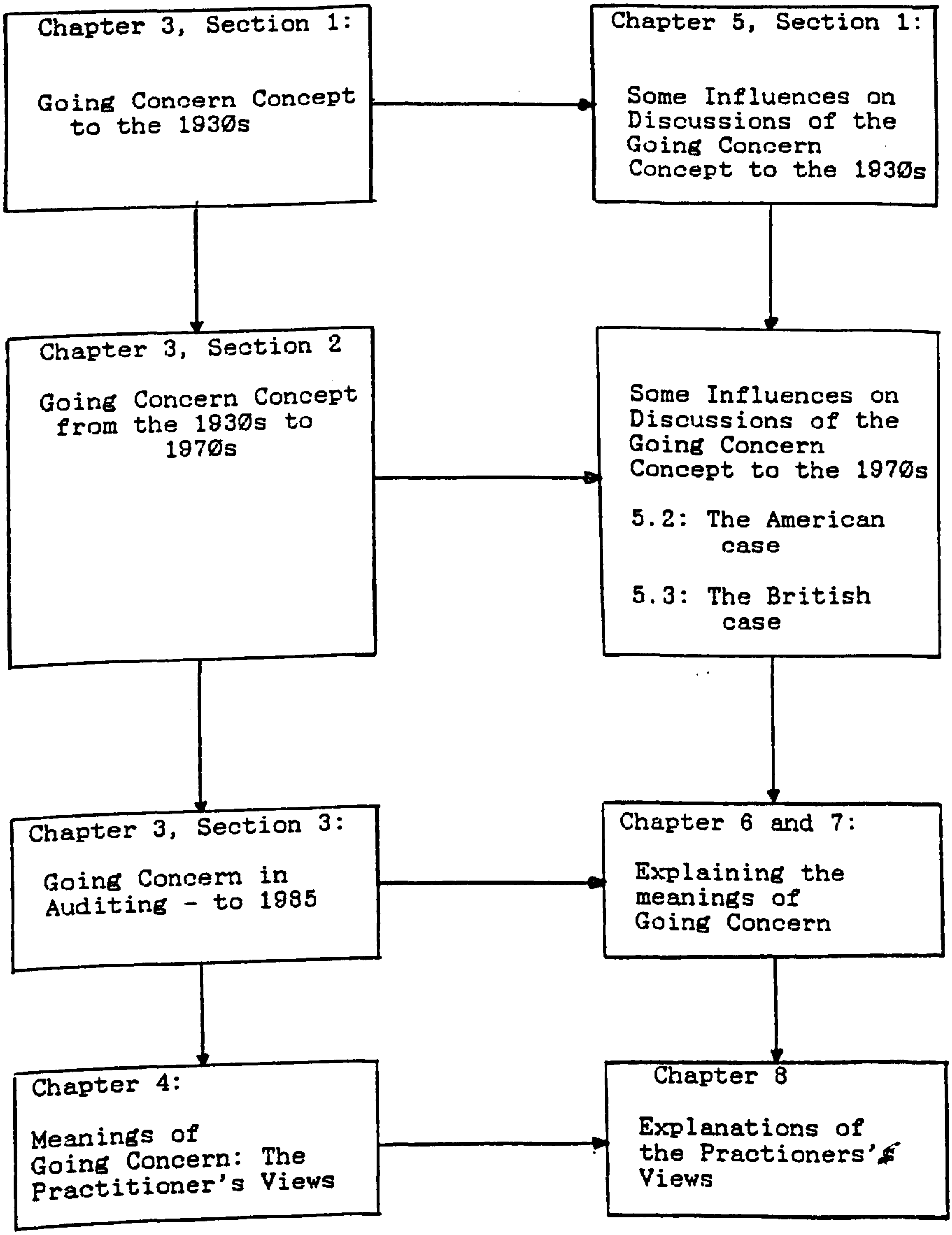


Figure II.I
Relationship between the First and Second Layer

In the UK, the going concern concept received formal institutional recognition through SSAP 2 in 1971. SSAP 2 also mentions three other fundamental accounting concepts, but to date only the going concern concept has been subjected to an auditing guideline. As chapter 3 noted, the meanings attached to the going concern concept in an auditing context are very different from those traditionally associated with it. Chapter 7 will examine the way in which the UK profession came to formulate the auditing guideline. However, as chapter 2 argued, no understanding of any meaning can be complete without an awareness of the major institutions which disseminate meanings and interpretations. In pursuance of such views, chapter 7 also focuses upon the relevant aspects of the formation and development of the Auditing Practices Committee (APC). The APC was responsible for formulating the auditing guideline issued in August 1985.

Chapter 8 identifies some of the structural and ideological factors which influence the meanings and interpretations which the practitioners assign to the going concern concept.

Chapter 5

SOME INFLUENCES ON THE GOING CONCERN CONCEPT: TO THE 1970S

5.0.: Introduction

This chapter traces some of the major influences on the development and interpretations of the going concern concept. It directly follows on from chapter 3 which noted that it became a widely quoted concept during the period up to the 1930s. Until the 1930s, the concept was not explicitly supported by the accountancy profession or the state agencies. However, from the 1930s, the concept began to be described as a 'generally accepted accounting principle' by the American accountancy profession and was approved by state agencies such as the Securities Exchange Commission (SEC). Such institutions frequently legitimised the meanings previously associated with the concept. In contrast, explicit institutional support was absent in Britain during the 1930s. This is so despite the fact that the concept was first discussed by British writers such as Dicksee, de Paula, Leake and others. It only received institutional support in the 1970s when SSAP 2 described it as 'generally accepted' and 'fundamental' (ASC, 1971). Such episodes in the formulation and development of the concept pose a number of questions. What factors shaped the early meanings of the concept? Why did the concept receive support from the American profession and the State in the 1930s, but similar support was not forthcoming in Britain until the 1970s? This chapter will provide an answer to such questions. However, it should be noted that in view of the vast time span covered, an encyclopaedic explanation of the various factors influencing the formulation of the concept is not possible within the space of this thesis. Instead, within the methodological framework of chapter 2, this chapter focuses on some selected episodes to highlight the manner in which the meanings of the concept have been shaped by the wider social contexts.

The explanations of this chapter explicitly assume that accounting is linked with social, economic and political developments. This means that the interpretations and meanings of accounting concepts cannot remain fixed, but are changed through practice and contestation. This chapter will argue that the meanings and invocations of the going concern concept are particularly shaped by the early accounting and accountants' association with bankruptcy practices, interests of finance capital, economic crises, general interests of capital, profession and the State. It is further argued that the concept has played a part in legitimising a particular social order and has enabled the accountancy profession to manage its crisis of legitimacy.

In order to present the various arguments, as figure 5.1 shows, this chapter is divided into three sections. The first section (5.1) explores some of the influences on the formulations of the going concern concept to the 1930s, in many ways, the formative years of the concept and the accountancy profession. Much of the intertwining of accounting and the sociopolitical is yet to be investigated. Therefore, considerable difficulties remain in identifying the manner in which accounting became implicated in various developments of this period.

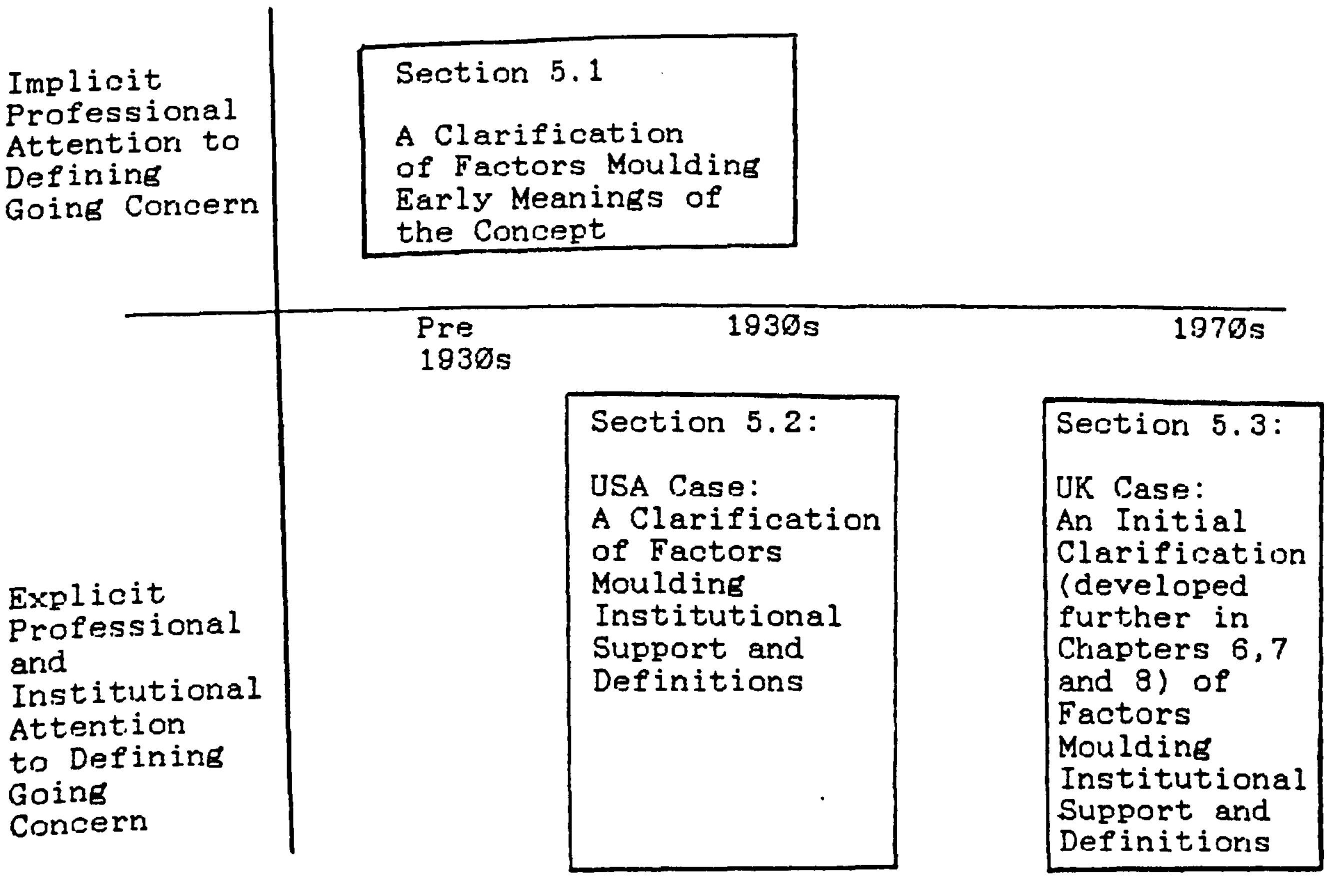


Figure 5.1
An Overview of Chapter 5

In view of such difficulties, this section makes a limited attempt to examine only some of the influences shaping the early interpretations of going concern. The evidence and arguments show that the early meanings of the concept are best seen as a sedimented residue of inherited wisdoms and practices representing 'common sense' views shaped by the role of accountants in bankruptcy work, safeguarding the interests of finance capital and promoting reproduction and transformation of capital. The early meanings were also shaped by changes in the economic environment and concern with managing conflict between directors and investors. The meanings of the concept developed in an environment particularly shaped by the State and Ideological State

Apparatuses (ISAs), such as the courts. Therefore, the section also pays attention to legal requirements and the decisions of the courts.

The second section (5.2) focuses on the period from the 1930s onwards. It examines the factors which led the American profession and the state agencies to give institutional support to the concept by describing it as 'generally accepted'. Rather than focusing on a whole range of episodes, this section focuses on a few selective events to explain the reasons for the institutional support for the concept. It is found that the concept received institutional support at a time when the legitimacy of the American State and the profession was being threatened by a major economic crisis. This crisis was managed by enhancing confidence in financial institutions and corporate financial reports by appealing to the going concern (and other) concepts.

In contrast to the American position, the concept did not receive any explicit institutional support in the UK in the 1930s. It came with the issue of SSAP 2 in the 1970s. The third section (5.3) examines the factors leading to such institutional support. It is argued that the profession appealed to the going concern concept to manage a threat to its legitimacy. Such a threat emerged with the expansion of financial markets and merger waves which particularly scrutinised the role of accounting in constructing the social/economic affairs of a company and found it to be deficient. Under such circumstances, the UK profession appealed to the going concern and other concepts describing them as 'generally accepted' and 'fundamental'. Section 5.4 concludes the chapter with a summary and discussion.

5.1: GOING CONCERN TO THE 1930s: SOME INFLUENCES

This section argues that the meanings of going concern were shaped by a number of influences. The early accountants could not start thinking about accounting with a clean slate. They had to come to terms with the views, already in existence, on whatever constituted good or normal accounting. In such a context, meanings of going concern were frequently derived from the contemporary dominant ideologies and practices. As many of the early accountants were engaged in practices associated with bankruptcy, it is reasonable to assume that such an involvement must have shaped their views. As much of the bankruptcy work is concerned with making capital mobile and privileging the interests of 'finance capital', the early accountants through practice came to sympathise with such interests. The bankruptcy work required accountants to pay particular attention to recoverability of loans and valuation of assets. Their connection with financiers and bankers persuaded them to regard highly conservative asset values as virtuous. Such an approach to valuation helped 'finance capital' to protect its interests and became synoymous with going concerns. Through practice the early views on going concern became part of a tradition and shaped the 'common sense' views on the meaning of the concept.

With the emergence of capitalism, accounting also played a particular role in 'watching over capital' and performing 'global functions of capital'. In this context, accounting processes were closely aligned with the interests of capital and were concerned with the reproduction and transformation of capital. The meanings of going concern could not escape such influences. It appears that any major threats to the ability of capital to accumulate economic surpluses also create pressures to modify accounting techniques. In this context, this section shows that in the face of the late nineteenth century depression, the meanings of the going concern concept were transformed. Instead of insisting that going concern justified valuing all assets at original costs, some influential writers now accepted that the concept required current assets, such as stocks, to be valued at the 'lower of cost and market value rule'.

The concept should not just be viewed as a technique. It will be shown that the going concern was used to promote a particular social order. The maintenance of 'secret reserves' and the associated director discretion was justified by invoking the going concern concept. Thus the meanings of the concept were shaped by its role in adjudicating conflicts between directors and investors.

The meanings of the concept did not occur in a vacuum. They were particularly shaped by the actions of the State and related ISAs. In view of its reliance upon taxation revenues from profits generated by busineses, the State had to create an environment to enable businesses to continue in existence for very long periods. Towards this end, the State and the ISAs required companies to make depreciation provisions and generally maintain capital. Under the influence of the State and the ISAs, such views became synonymous with going concern.

The above arguments and their interconnections are shown in figure 5.2.

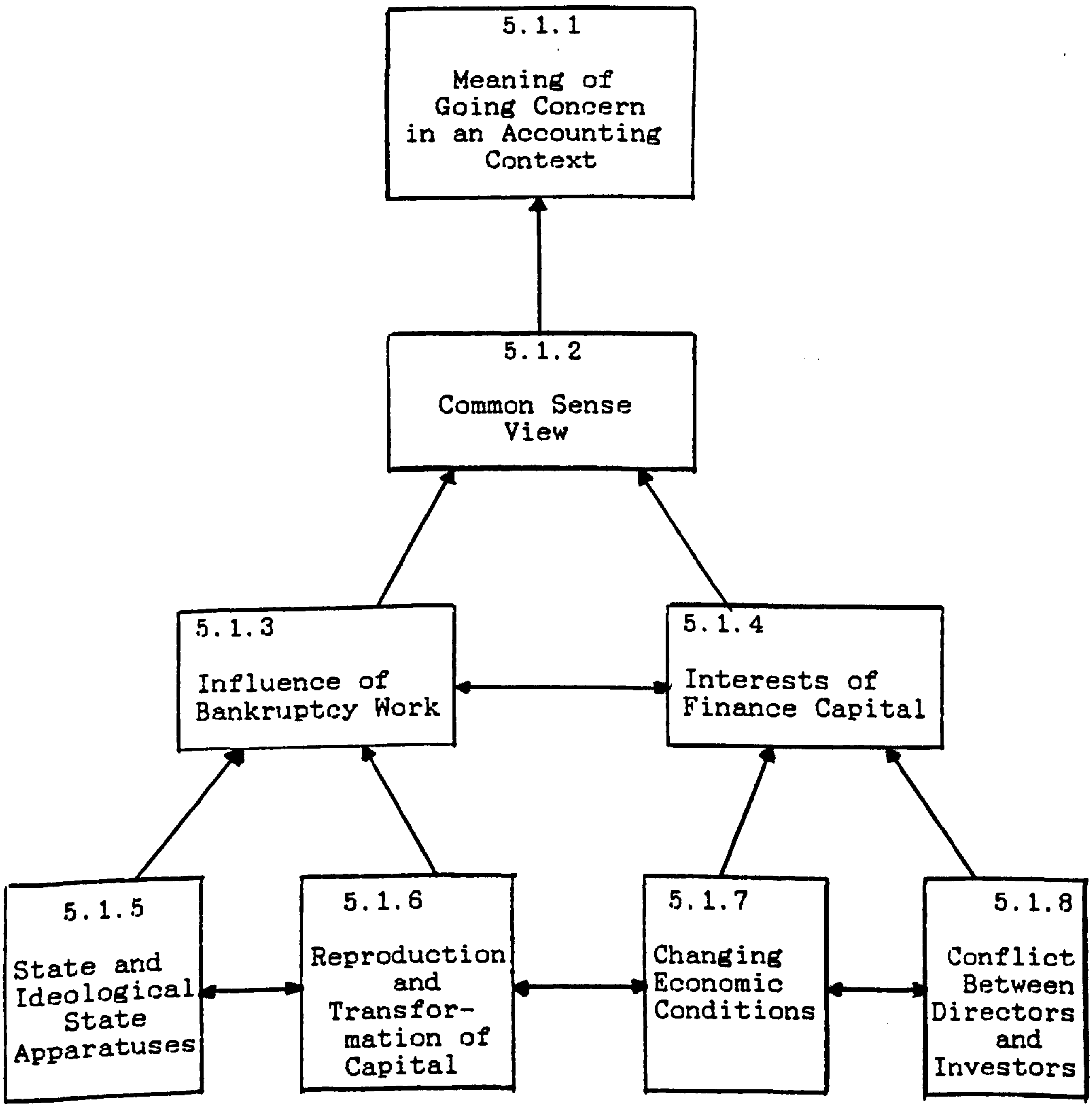


Figure 5.2
An Overview of Section 5.1

The section begins (5.1.1) by referring to the technical meanings which earlier writers assigned to the going concern concept. Section 5.1.2 argues that the earlier views reflected the 'common sense' meanings of the going concern concept. Such views were shaped by the accountants' involvement in bankruptcy work (5.1.3), their sympathy for finance capital (5.1.4), which in turn were influenced by the State and ISAs (5.1.5). The early meanings of the concept were also shaped by pressures relating to the reproduction and transformation of capital (5.1.6), changes in economic conditions (5.1.7), and the accountants' role in conflicts between directors and investors (5.1.8). The last four factors are heavily interconnected and had particular influence on the bankruptcy practices and interests of finance capital, which in turn shaped thinking about the going concern concept. This is shown in figure 5.2. Section 5.1.9 summarises the first section of the chapter.

5.1.1: Early Meanings of the Concept

By the 1930s, numerous competing meanings were assigned to the going concern concept. These were summarised in figure 3.1 (page 108) and are only briefly reviewed below.

In the earlier years, the concept represented 'permanence'. In accordance with the profit motive, the contemporary view was that no one would start a business unless there was an expectation of a very long term existence to enable the traders to earn revenues and profits. The going concern concept tended to be associated with valuation of assets individually. The focus was with valuations either at the change of ownership or at an interim stage, i.e. before the sale or liquidation of a business. Whilst a few authors associated the concept with the use of market values, realizable values and replacement costs, most rejected such associations of the concept and argued that it justified valuing fixed assets at 'cost less depreciation'. At the same time, the concept was used to justify valuing current or floating assets at the 'lower of cost and market value rule'. Writers such as Pixley argued that the concept justified the directors' maintenance of 'secret reserves'. The meanings of going concern were being elaborated at a time when the profession was receiving its formal recognition through Royal Charters and was keen to distinguish itself from its competitors by referring to its technical competence and a body of knowledge.

The explanations of the concept will argue that its meanings are likely to reflect the ideologies of capitalism. Upon these basic ideologies, various periods and developments left their mark. This would include, the early accountants' reliance upon bankruptcy work for their livelihood. Many accountants also worked for bankers and financiers who were frequently responsible for putting other businesses into bankruptcy or for managing bankrupt estates. Within a legal framework, the financiers were concerned with safeguarding their investments by making very conservative valuations. The accountants' involvement with such interests would have required them to take an interest in particular kinds of valuations and meanings of going concern. The legal developments would also have influenced the meanings of going concern, especially as the early accountants emerged from the shadows of the legal profession and were expected to show considerable familiarity with such developments. Most of the early accountants were trained to apply the law.

The influence of the State is also likely to have been decisive on the meanings of the going concern concept. The increasing number of late-nineteenth century bankruptcies threatened the State's legitimacy and the State legislated in the long-term interests of capital by enacting the Bankruptcy Acts and making capital mobile. The legislation was also designed to enhance confidence in limited liability companies and the integrity of directors. At the same time, the State nurtured the UK accountancy profession through bankruptcy statutes other legislation and Royal Charters. The accountants could thus hardly ignore the influence of the State in elaborating any meanings of the concept.

The early views on going concern also had to cope with conflicting demands and pressures. For example, the lenders, in order to protect their loans were interested in conservative values of assets yet at the same time the State required companies to show costs in the balance sheets, something which could be regarded as 'factual'. These aspects applied to businesses which in the ordinary language were regarded as 'going concerns'. Such conflicting pulls of legislation and practices of powerful bankers created tensions in the meanings which came to be associated with the going concern concept. The 'great depression' and the late nineteenth century deflation also influenced the meanings assigned to the concept. In view of the falling prices, it appears that the conservatism of the accountants, acquired during bankruptcy days, persuaded them to value some assets at realizable values.

The remainder of this section now provides details of the arguments outlined above.

5.1.2: 'Common Sense' and Going Concern

Gramsci argued that 'common sense' is a residue of myth, history, folklore and social practices. It is episodic and fragmentary and, therefore, likely to contain contradictions. 'Common sense' is not immobile, but is continuously renewing itself. It is influenced by everyday experiences. It is shaped by competing ideologies which interpellate individuals, influence their worldviews and move them to modify meanings of their concepts. The thinking on 'going concern' can also be understood in a similar manner.

The meanings of the going concern concept are best seen as 'common sense' views representing a sedimented residue of period practices and developments. The State and 'ideological state apparatuses' play a particular part in formulating the 'common sense' meanings of the concept. It is extremely unlikely (contrary to the claims of Yamey, 1956, 1979) that the concept was a spontaneous response to mass industrialisation. Contrary to the views of Kitchen (1974, 1979) and Edwards (1938), one should not be surprised to discover that ideas on going concern are contradictory and confusing.

The early views on going concern can be understood by referring to contemporary events and dominant ideologies. In such a world, the privileged classes had exercised 'economic' influence and the subordiante classes fully expected this to continue for the forseeable future (Ingham, 1984). Businesses owned by powerful classes and run under State sponsorship had been considered to be perpetual. Companies such as the P&O shipping company had close contacts with the State and made enormous revenues by carrying supplies for the British army to all parts of the world. By the 19th century, such companies were regarded as "semi-national institutions" (Harcourt, 1982, page 6) and gave every appearance of 'permanence'. In accordance with their Charters, such major companies could undertake a series of transactions and thus point to a continuity of existence. Many companies, especially those created under Royal and Parliamentary Charters, with the State's help continued to flourish and avoided bankruptcy even when major scandals burst (Hadden, 1977, page 14). The companies incorporated under Royal Charters, such as the Russia Company, (chartered in 1555), the East India Company (chartered in 1600) and Hudson Bay Company (chartered in 1670) all enjoyed huge large-scale monopolies and even became masters of colonies in Asia and Africa. Such riches and empire promoted a picture of everlasting prosperity and influence for the families for whom the early accountants were working (Scott, 1985). In any commercial practice, the early accountants were hardly going to assume that the influence of the privileged classes would not last for the forseeable future. The early accountants material rewards (wages) depended upon the economic wellbeing of the dominant classes.

The railways were the biggest industry of the nineteenth century and the experts felt that the lines owned by the railway companies would last from one hundred to one hundred and fifty years (Edwards, 1986; 1989). Such was the confidence in the new industrial age that some claimed that "the railroad is built to last forever" (Littleton, 1933, page 10; also see Pollins, 1971). 'Permanence' was to be achieved not by magic, but by creating material conditions for the reproduction and transformation of capital. Such conditions were created by the State. Towards this end, the Company Clauses and the Consolidation Act 1855 prohibited the railways companies from paying dividend out of capital. The forced maintenance of capital ensured that sufficient funds would be available to enable capital to reproduce itself. Within the constraints of capitalism, any business which was unable to reproduce itself did not have any hope of remaining a 'going concern'. Thus ideas on capital maintainence became synonymous with 'going concern'.

Ideas on going concern do not arise singly. They arise in clusters, with each meaning invoking other connotations, setting off a chain. When 'going concern' is associated with survival or continuation of a business, this also raises questions about how this will occur. This has implications for the resources which can be withdrawn or retained within the business. Therefore, the discussions of 'going concern' also had to address issues relating to maintenance of capital, depreciation, solvency, distributable dividends etc.

As accounting and auditing assumed a greater significance for accountants, they relied on the 'common sense' ideologies of the business world and bankruptcy experience of an earlier era to guide them. In discussing going concern, Dicksee (1892) appealed to the sedimented residue of 'common sense' to suggest that the

> "primary object of most ordinary undertakings was to continue to carry on operations" (pages 117-118).

It is significant that Dicksee (1892) started his discussions of 'going concern' by referring to the perpetual succession of railway and Parliamentary companies, whose continuity was also assured by State intervention and legislation. Guthrie (1883) prefaced his discussions of going concern by insisting that

> "Manufacturers and traders do not construct business premises or lay down special plant in the intent of a short period ......" (page 7).

By the time Dicksee started articulating technical meanings to going concern, the concept had already entered into every day language and 'common sense' use. For example, Lindley, L.J. in the case of Gloucester Bank v Rudry Merthyr Steam and House Coal Colliery (1895), interpreted going concern in a literal way, assuming that a firm was expected to continue in business in accordance with the nature of its main asset, a lease. Such literal meanings were also considered to be relevant in banking circles, where a banking dictionary published in 1923 explained 'going concern' as "an undertaking which is in full working order"[1].

In the years to come, such meanings would seek space within the professional discourses (see chapters 6 and 7), but for the time being ideas on going concern continued to be influenced by contemporary discourses, practices and developments. As Brown (1905), writing on the 50th anniversary of the emergence of the Scottish accountants noted,

> "......... we can not point to any striking revolution. The development has not been characterised by any startling discoveries of new principles or the introduction of entirely novel methods, but rather by the steady working out, with modifications suited to changing conditions, of those principles and methods which were already well understood and practiced by the old 'accountants' " (page 315).

The meanings of going concern continued to be a modification of previous meanings, depending upon the discourses into which the concept was inserted. These related to depreciation, capital maintenance, dividends etc. In each case, the writers modified the previous meanings and added additional layers. In this context, under the influence of bankruptcy work and connections with powerful families, accountants interpreted the going concern concept to privilege the interests of 'finance capital'.

5.1.3: Connections with Bankruptcy Work

Bankruptcy practices are of particular relevance in understanding the early meanings and interpretations of the going concern concept because they shaped the way accountants thought about accounting and auditing problems (Brown, 1905; Spicer, 1929; Briston and Kedslie, 1986).

The privileges won by accountants were mainly due to their work in connection with bankruptcies and liquidations. They were keen to form associations to influence legislation and protect their interests (Brown, 1905, page 209). Such interests were furthered by building alliances with the socially and economically powerful groups to enable accountants to secure Royal Charters and the related recognition. The 1854 petition for a Royal Charter by the Scottish accountants primarily referred to the administration of bankruptcies (see Brown, 1905, page 210) and estates. Despite the increasing influence of merchants, commercial traders and the emergence of huge industries such as the railways, the Royal Charter contained no mention of auditing or corporate accounting practice even though reference to auditors (not professional auditors) and a need to prepare balance sheets was made in the Joint Stock Companies Act, 1844; Joint Stock Banks Act 1844; Companies Clauses Consolidation Act, 1845 and Joint Stock Companies Act, 1855.

By the mid-nineteenth century, accounting and auditing functions were not developed and were certainly not performed by professional accountants. For example, Cooper (1886) notes that in 1836, only 9 of the 107 banks had auditors (not professional) of any kind. However, financial reporting and auditing practices were emerging. The Companies Act 1862 required companies to prepare a balance sheet. Following the collapse of the City of Glasgow Bank, the Companies Act 1879 made audits compulsory for banks and insurance companies. But the Scottish Institute took little interest in this legislation. Instead, it devoted more attention to other matters such as the Trust Investment Acts and the Forged Transfers Act (Brown, 1905, page 213). On 22nd January 1876, The Accountant (page 4) published what the editor thought was a stimulating article on auditing but on 27th May the editor expressed disappointment in that the article had attracted no response. When in 1877, the ICAEW President was asked by the Select Committee on the Companies Act, 'Have you in your business had much to do with joint stock companies? In reply, he did not mention auditing or accounting, but stated that,

> "with the liquidation of them I have had a great deal to do ..... mostly ...... compulsory liquidations"[2].

Accounting and auditing, despite the introduction of compulsory audits for banks by the Companies Act of 1879 had not become a major source of revenue for accountants. Bankruptcy work continued to be the distinguishing feature of the profession. The Royal Charter of the ICAEW, dated 11th May 1880 was granted for

> "increasing importance in respect of their employment in the capacities of Liquidators acting in the winding-up of companies and of Receivers under decrees and of Trustees in bankruptcies or arrangements with creditors and in various positions of trust under Courts of Justice and also in the auditing of

> the accounts of public companies and of partnerships and otherwise".

It is important to note that auditing only appears to get a mention as an afterthought. Even by the late 19th century, bankruptcy and liquidations remained the main work of accountants and continued to shape their way of thinking about accounting and auditing problems (Cooper, 1921). For example, the Bankruptcy Act 1883, removed personal bankruptcy work from the private sector, thus forcing accountants to pursue work in other areas. The importance of bankruptcy can be seen by statistics relating to the number of accountants. Prior to the loss of this niche, the number of accountants in 1881 was 11,000, but in 1891 despite the introduction of compulsory audits for banks and insurance companies, the number of accountants barely reached 7,900 (Cooper, 1921).

The earlier writers on going concern such as Dicksee, De Paula, Pixley, Leake and others all received their training at a time when bankruptcy was the mainstay of an accountant's work. Its influence affected the way they thought about the nature of accounting. The early accountants also emerged under the shadows of the legal profession and devoted considerable attention to learning legal matters (Cooper, 1886, 1921; Brown, 1905, page 182; Jeal, 1937, page 522). Much of their concern lay with recording matters relating to property ownership and rights for the benefit of lenders. Most of the bankruptcy accountancy practices reflected the interests of 'finance' and the meanings of 'going concern' had to reflect the interests of such dominant groups and classes. Further details are given below.

5.1.4: Interests of Finance Capital

Historically, 'finance capital' has enjoyed a privileged position in the British State, institutions and society (Ingham, 1984). For its survival, bankruptcy work is of considerable importance, as it helps to salvage capital and paves the way for its redeployment in the quest for economic surpluses. The bankruptcy legislation and practice legitimised a pecking order and determined which group shall have the first or any bite of the surviving capital. In this context, 'finance capital' was the most privileged and its interests ranked above the interests of any other fraction.

Many early accountants derived most of their income by performing tasks for banks and insurance companies (Brown, 1905, page 195) and had to consider the interests of 'finance capital'. In the nineteenth century, it was a common practice for many accountants

> "to seek the local agency of one of the chartered banks, or to become secretary or treasurer of a private or country bank. This gave them position of unparalleled powers in the community over the disbursement of loans and the discounting of bills for local farmers, merchants and businessmen" (Donnachie, 1977, page 275).

Such organisations were frequently responsible for starting a large number of bankruptcy proceedings and provided accountants with their livelihood and prestige. During bankruptcy and liquidations, the assets of the borrowers were foreclosed and sold off thus not only making capital more mobile but also protecting the interests of 'finance capital'. Such practices also promoted the spirit, competition and efficiency necessary for survival of capitalism.

The practice of bankruptcy was built upon a view common to early capitalism, that businesses were formed with a view to earning a return. The practice of bankruptcy further demonstrated that only businesses under threat of bankruptcy were forced to sell their fixed assets and that a forced sale would result in lower price. In the main, the assets were seen as intended to be used to generate income and remain in business within the constraints of capitalism. It is the power of 'finance capital' to protect its interests, which gave rise to the belief that a going concern was one which expected to remain operational and did not intend to sell its fixed assets. In his discussions of going concern, de Paula argued that fixed assets were held

> "not with a view to re-sale, but with a view to earning income by the use thereof during its working life" (de Paula, 1912, page 905).

Such views were shared by magazines such as The Accountant, which wrote that

> "fixed assets .... are not for realisation in the ordinary course of business, but to be used in their existing form" (4th December 1909).

The financiers lent money to those businesses which they expected would remain in existence long enough to repay the loans and interest. With foreclosure always a possibility, questions of recoverability of loans and valuations of assets were important. In such circumstances assets were likely to be sold one by one. Therefore, the value of each asset, rather than the collective value of a business, was of significance. It is interesting that early discussions of going concern by Dicksee, De Paula, Leake and Pixley are accompanied by valuation of each separable asset rather than the collective valuation of assets. In contrast, the economists (for example, Edwards, 1938) criticised accountants for not dealing with the value of going concern and indeed urged them to consider ways of valuing the whole business entity.

The nineteenth century is also marked by a surge in bankruptices and liquidations. Many of these followed in the wake of the introduction of limited liability and the formation of many speculative and fraudulent companies (Shannon, 1932; Todd 1932; Shannon, 1933). The high number of bankruptcies forced financiers and accountants to further consider the valuation of assets in a forced sale situation, i.e assuming that the business would not be a going concern. In such an environment, financiers looked for adequate cover on loans to safeguard their financial interests. Bankers insisted on itemised lists of all assets and liabilities from the borrowers as this gave a good indication of the potential assets and cover for the loan (Dev, 1974). The asset classification in the balance sheet depended on the realisability of assets from a liquidation viewpoint. The most difficult to realise assets, e.g. 'permanent assets' such as plant and machinery and land and buildings appeared first, followed by the assets somewhat more easily capable of being realised.

With an eye on security, financiers preferred a highly conservative value of each individual asset (Chatfield, 1977). The need for conservative values continued to be reinforced by major financial crises (Hobsbawm, 1968) and some spectacular failures throughout the late nineteenth century (Collins, 1989). For example, West Hartlepool Railway Company collapsed in 1863; the Great Eastern Railway Company collapsed in 1865; London Chatham and Dover collapsed in 1866. In May 1866, Overend Gurney, a reputable bank collapsed owing £8.5 million to investors. The City of Glasgow Bank collapsed in 1878, owing some £12 million. Such collapses and the resulting 'great depression' made property harder to sell. In times of falling prices and speculative ventures, the bankers feared that the market prices of assets would decline. Their value could not always give an easy indication of the recoverability of loans. The only sure way of gauging security was by focusing on the assets which could easily be converted to cash. The conversion of assets to cash was indicative of the ability of a business to ride out any economic setbacks and remain a 'going concern'. Thus in order to judge the ability of a borrower to repay the loans, bankers and financiers valued current assets at the 'lower of cost and market value'. In times of falling prices, such policies made economic sense and provided a suitable hedge. When writing on going concern, writers such as de Paula (1914) reflected such views by arguing that floating assets should be valued upon the lower of cost and market value rule (page 71) and that

"on no account should floating assets be valued above cost price" (page 72).

Spicer and Pegler (1925) referred to the going concern concept to argue that

> "floating assets must not be valued above cost ....., the proper basis being cost, market or realizable value, ... whichever is the lower" (page 343-344).

The lenders also developed simple ratios and rules of thumb from limited data to estimate the ability of a business to repay its loans and thus remain a 'going concern' (Horrigan, 1968). Some of the rules were that current assets must easily cover current liabilities. In order to compensate for the likely significant shrinkage of assets at times of falling prices, they looked for a current ratio of 2:1. Indeed, the current ratio of 2:1, together with other ratios came to be regarded as a predictor of solvency and entered the folklore of solvency prediction (see Dev 1974 for a review). Such has been the influence of tradition and custom that even the modern day literature (Beaver, 1966; Altman and McGough, 1974, Mutchler, 1984) has been advising auditors to use ratio analysis to determine whether a business will remain a going concern for the forseeable future.

The next sub-section examines the actions of the State and 'Ideological State Apparatuses', such as the courts, which influenced the meanings and interpretations of the going concern concept. Such actions were particularly responsible for associating costs, depreciation, secret reserves and dividends with the concept.

5.1.5: State and Ideological State Apparatuses

The meanings of going concern are also shaped by the policies of the State. Such policies were part of managing the continuing legitimation crisis and affected the contemporary accounting thought.

The introduction of limited liability in 1855 was followed by the formation of a large number of companies which turned out to be 'speculative and fraudulent' (Todd, 1932). Of the first 5,000 companies formed during 1856-1865, almost 36% ceased to exist within the first five years whilst 4.5% were restructured; within the first ten years of their formation, some 54% ceased to exist whilst 7% had to be restructured (Shannon, 1932). Of the 6,240 companies registered during 1866-1883, only 799 survived by 1929 (Shannon, 1933). The pressures to clearly identify the assets for going and non-going concerns and ideas on the appropriate ways of recording their valuations were further reinforced by economic depressions (Hobsbawm, 1968) and financial collapses of the 1860s and 1870s (Cooper, 1921).

In this environment, the losses suffered by many investors and creditors threatened confidence in the ability of the State to promote capitalism and protect investors. The State was forced to act in the long-term interests of capital by influencing the desirability of some corporate practices. It had already played a particlular part in enacting bankruptcy legislation to promote and protect some privileged interests. Such terrains affected the way accountants operated and thought about their craft and further legislation continued to mediate the meanings of the going concern concept. At a time when accountancy was being promoted as a "science dealing with facts and the practical application of law" (Spicer, 1929, page 705), not surprisingly it was influenced by the statutory requirements.

The State intervened via the Joint Stock Companies Acts of 1844 and 1862 to arbitrate between directors and shareholders and redefined the boundaries between 'public' and 'private' information. Since 1844, with the passing of the Joint Stock Companies Act, balance sheets had become a significant document. In this Act, the emphasis was on prevention of fraud and following the practices developed by successful financiers, lists of assets and liabilities and the capital utilised to acquire them were of considerable importance (Irish, 1948). A 'going concern' was required to provide a 'factual' indication of the capital utilised and this could be done by showing the cost of the assets. By referring to 'costs', directors could give a clear account of the manner in which they utilised the finance contributed by investors. By citing cost, the management could show their honest conduct of the business. Thus reference to 'costs' assumed importance in demonstrating the propriety of the directors' stewardship. Without a public demonstration of such propriety, the directors could not secure external finance and legitimacy to enable a business to remain a 'going concern'.

In order to promote the long-term interests of capital, the

Companies Act 1862 established the balance sheet as the prime document for shareholder scrutiny. It required inventories and plant to be valued at 'cost'. In the wake of major railway company failures, the Railways Act 1868, required companies to show their assets in the balance sheet at cost. This demonstrated 'facts' and director propriety and created environment for the continuation of the businesses.

Early writers such as Dicksee, de Paula, Leake, Pixley and others started writing about 'going concern' at a time when 'cost' had already been established as an acceptable way of recording (valuing) assets in the balance sheet. A profit and loss account was not considered to be important in the early legislation and indeed, early writers had little to say about the implications of the going concern concept for income calculation. The 'cost' as a 'factual' and acceptable basis of calculation continued to be associated with a continuing business by the policies of the State.

During the first world war, the State controlled profiteering on government contracts by relying upon 'costs' (Loft, 1986). The government inspectors, frequently partners in prominent firms of chartered accountants, visited many companies to inspect the record of costs. The government's use of accounting numbers to control profiteering and a push for efficiency also brought many eminent accountants to the Ministry of Munitions (Stacey, 1954). The Defence of the Realm Act of 1916 stated that "in determining such prices regard need not be had to the market price, but shall be had to the cost......"[3]. Depreciation was regarded as part of 'costs' and was based on 'original cost'. Such views further reinforced the points that a continuing business must make provisions for depreciation and that costs are the relevant focus of attention. During such times, Leake, who linked going concern with 'original cost less depreciation', argued that only depreciation based on original cost should be recognised as an expense (see a letter in The Accountant, 8th July 1916, page 39). Men such as de Paula were acting as advisors to the government (Kitchen and Parker, 1980) and insisted that the going concern concept meant the use of original costs for fixed assets. In discussions of depreciation, de Paula (1912) referred to the going concern concept and argued that,

> "no regard need be taken to fluctuations in the market price of similar plant, whether such price be either up or down. The particular plant is held as a fixed asset, and is not held with a view to re-sale .... as a going concern, all that is necessary is that the net cost should be written off over the working life" (pages 905-906).

The above arguments have suggested that the actions of the State and the ISAs linked going concern with original costs, depreciation and capital maintainence and helped to shape meanings of the going concern concept.

5.1.6: Reproduction and Transformation of Capital

Within the dynamics of capitalism and concern with the ability of capital to reproduce itself, the topic of depreciation became significant. In order to remain a 'going concern', resources had to be found to reproduce and transform capital. In this context, depreciation was seen as a kind of a 'fund' out of which assets could be replaced and capital reproduced. The details of depreciation were not revealed to any outsiders and any suitable figure could be adopted in the accounts. In bad years, directors could reverse depreciation provisions to declare a higher profit and dividend. Thus depreciation is related to discussions of 'secret reserves' and director discretion as well as reproduction of capital. Within the ideologies of capitalism, accountants sympathised with the need to replace capital and almost all early discussions of 'going concern' justified the need to make depreciation provisions. The State provided a lead by requiring the railway companies to maintain their assets (Pollins, 1956), thus creating material conditions for the reproduction of capital.

'Common sense' views on depreciation were occasionally challenged. For example, the case of Lee v Neuchatel Ashphalte Co (1889, 41, Ch.1) decided that a company formed with a view to working a single asset only, need not make any depreciation provisions. In such a case, little purpose was to be served by the maintenance of capital. The interests of capital could best be served by returning it to the hands of the owners, making it mobile and seeking new niches. It is significant that Dicksee (1892) was writing about going concern in the immediate aftermath of this case and was unhappy with the court decision as it undermined the contemporary views on the continuation of a business. He continued to link depreciation with discussions of going concern and felt that by retaining profits, a business would be able to replace its assets and thus ensure its continuation. In the accounting literature, the need for depreciation continued to be justified by referring to the concept of a 'going concern', but cases such as Bolton v Natal Land and Colonisation Co. Ltd (1892, 2 Ch 124); Verner v General and Commercial Investments Trust (1894, Ch. 239) and Kingston Cotton Mill (1896, 1 Ch 331) and others established the need to show floating assets at their realizable values. It is also significant that the language of courts influenced the language of accounting. Whereas in the 1892 book, Dicksee's discussions of 'going concern' referred to 'permanent' and 'floating assets', after the Verner case, Dicksee (1904, page 291) referred to 'fixed' and 'circulating' capital.

Within the dynamics of capitalism, businesses are frequently bought and sold. In this context, an important question arises about the valuation of businesses as 'going concerns'. In active markets, the obtaining of such valuation may be less complicated, but greater problems are experienced in the absence of such markets. As previously stated, under the influence of bankruptcy practices, early accountants paid little attention to the collective value of assets and were primarily concerned with the value of individual items. When selling a business, it is possible that some of the assets may only be partially consumed. In this context, some simple method for estimating valuation is useful. The early accountants were trying to develop such methods during times of economic volatility. As Appendix 4 shows, during the late nineteenth century prices were ~~e~~genrally falling. During such a deflationary economic environment, cost minus an estimate for wear and tear (depreciation) may give a reasonable estimation of market value, though some businesses may wish to call upon professional valuers to occasionally verify the valuation of assets. Here 'cost' had already been established as a benchmark by legislation. It is interesting that in discussing going concern, Guthrie (1883) wrote,

> "for fuller occasional satisfaction, prudent manufacturer will periodically call in professional valuers ...... to value their plant and machinery, not necessarily annually .... But every valuation so taken ...... should be made with regard to normal cost rather than to the value of the day of the valuation. Matters and things fixed in a permanent working position must not be treated in account as following the fluctuations of the market. Such valuation is for purpose of check ......" (page 7).

In subsequent years, Dicksee (1907) defined going concern value as

> "at such a price as a willing purchaser would be prepared to give .... [that] is to say, the assets should be written down from time to time to provide effectively for depreciation" (page 199).

Similar views can also be found in Dicksee (1904, 1912), Leake (1912) and others. de Paula (1914) wrote that

> "For commerical purposes ..... assets are valued according to certain conventional rules ...... At any intermediate date, therefore, the fixed assets will appear in the Balance Sheet at cost, less depreciation ...... and this represents the present value of such assets to the particular undertaking as a going concern, or in other words, the value of such assets to the proprietors of the particular business" (de Paula, 1914, pages 70-71).

The broad view appeared to be that a reasonable approximation of the market value of each asset could be arrived at by deducting some measure of depreciation (wear and tear) from the original cost of an asset. In Guthrie's case, at the time of his writing, as appendix 4 shows, prices were falling and asset values may have been declining. This may be the reason why he spoke of 'for purpose of check' and advocated calling in professional valuers. But subsequent authors regarded 'original cost' as the basis of all fixed asset valuations. Whether they were assuming stable price levels is not clear. However, through education and professional literature, the 'cost less depreciation' basis of valuing fixed assets entered 'common sense' and has remained a dominant accounting thought even today. Edwards (1938) came to conclude that accountants did not not have any logical and coherent theory of going concern values. Nevertheless, within the context of the contemporary debates, exposition of going concern may have struck a chord with practitioners. It is notable that many writers (Mather, 1876; Harris, 1883; Bogle, 1889; Dawson, 1900; Pixley, 1918, 1922; Couchman, 1924; Hatfield, 1927; Cutforth, 1928) associated going concern with the use of 'cost minus depreciation'.

The meanings of going concern were not always fixed. The next sub-section shows that at times, its meanings came to reflect contemporary economic events and developments.

5.1.7: Changing Economic Conditions

The State had already legitimised the use of 'original costs' and this became synonymous with the valuation of fixed assets for a going concern. However, the implications of 'going concern' could not be fixed. Chapter 3 noted that on occasions writers such as Dicksee, Carter and others advocated the use of realisable values with going concerns. Such implications of the going concern concept were always competing for space and found support during times of rapid economic change. This can be seen through the debates relating to the use of realizable values for valuing inventory.

The Companies Act 1862 required that stock be valued at cost with a deduction for deterioration. Whilst a considerable diversity of practices may have existed, the model answers to the ICAEW's 1885 examinations were suggesting that stock in trade should be valued at net cost price (Walker, 1974, page 286). For most of the nineteenth century, this remained a dominant basis for valuing stock (Parker, 1965). However, at some time during the late nineteenth century, the view that inventories ought to be valued at the 'lower of cost and market value' gathered momentum.

The meanings of the going concern concept are also episodic and are influenced by contemporary economic crises and developments. The modifications of the stock valuation policies are likely to be influenced by what historians call the 'great depression' (Hobsbawm, 1968). The available statistics suggest that prices of most goods during the second half of the 19th century were falling (Appendix 4). Such economic factors accompanied by the influence of 'finance capital' and the residues of bankruptcy practices gave rise to a revised valuation rule.

During times of falling prices, the rule of valuing inventories at the 'lower of cost or market value' gave lenders conservative values[4]. This enabled the lenders to gauge the recoverability of their and loans protect their interests. During deflationary times, solvency and prevention of losses were considered to be synonymous with going concern (Dawson, 1900). During deflationary times, the 'lower of cost and market value' figure could also be seen as providing a reasonable approximation of the market value of assets and thus provide an approximation of the liquidity needs of a business. It is during such an economic environment that de Paula (1914) felt that the going concern concept justified the valuation of stock at the 'lower of cost and market value' rule. The State also legitimised such thinking. Since 1917, the rule of 'lower of cost and market value' has been accepted by the Board of Inland Revenue and is now a firm part of accounting practice. Such a legitimation of the rule was also supported by cotemporary writers. For example, Spicer and Pegler (1925) invoked the going concern concept to argue that

> "Floating assets should not be valued above cost, ... the proper basis being cost, market or realizable value, which is the lower" (page 343-344).

The link between going concern and the 'lower of the cost and market value rule' also received support from Dicksee (1907, 1916) and de Paula (1914) amongst others. During the times of economic turbulence, Dicksee (1907) also felt that the conversion of floating assets into cash at the earliest opportunity was a major business aim (page 202). Having used the going concern concept to argue that the assets should be shown at 'original cost less depreciation (Dicksee, 1892), in 1907 Dicksee seemed to have changed his mind and argued that

> "the amount at which all assets are stated in the balance sheet -except where a special statutory provision to the contrary obtains -should be regulated by the realizable value of such assets on the basis of a going concern" (Dicksee, 1907, page 197).

The next section examines the influence of director/investor conflict on the meanings of the going concern concept.

5.1.8: Conflict between Directors and Investors

Chapter 2 argued that a capitalist society is marked by tension and conflict. Such tensions raised questions relating to measurement of business expenses and distributable profits and went on to infuse the 'common sense' views and meanings of the going concern concept. In accordance with capitalist ideologies, investors wanted to secure as high a return as possible from businesses with good prospects of continuing in the forseeable future. In addition to reassuring investors, such policies may also help directors to remain in office. However, there are also tensions. High dividends could result in a rundown of corporate resources and pose a threat to the directors' jobs and the ability of capital to reproduce itself. Directors may prefer investments from internally generated resources, especially as this enables them to exercise considerable discretion in the use and generation of resources compared to instances where they had to seek finance from outside sources. Such dilemmas and disputes were arbitrated by the courts (French, 1977). In accordance with capitalist ideologies, they required companies to ensure that after payments of dividend, the nominal paid-up capital should not be less than the value of the assets. Significantly, in his discussions of going concern, Dicksee (1892) also paid attention to the legal aspects of payment of dividends and made a case for maintenance of capital.

The perceived importance of dividends also creates other problems. In poor years, the directors might not be able to maintain dividends and thus risk attracting adverse publicity. Therefore, within the existing modes of thinking, ways had to found of either maintaining dividends and/or dampening investor expectations by adjusting the profit figures. The conflicting interests of directors and investors are managed by allowing directors to operate 'secret reserves'. The courts respected the directors right to create secret reserves (French, 1977). In such struggles, many railway companies had also started to operate depreciation accounting, mainly in an effort to create secret reserves. In such discourses, accountants lined up with the interests of directors, especially as they relied upon corporate patronage for economic rewards. Accountants such as Dicksee (1904) and Pixley (1918, 1922) appealed to the going concern concept and argued that the 'secret reserves' were beneficial as they created a climate for continuity of a business. He felt that

> "Many companies have passed away which would probably at the present moment be in existence had they been provided with a secret reserve. ..... the Directors' business is to preserve the capital of company and

> keep it in existence as a going concern, and if a Secret Reserve is created to this end they are, undoubtedly - from a financial and commerical point of view - justified in so creating it (Pixley, 1918, pages 518-520; 1933, pages 537-539).

The use of 'secret reserves' continued to be justified by the going concern concept until the Royal Mail case in the 1930s (Hastings, 1962). In view of the adverse publicity surrounding that case, going concern concept was no longer used to justify 'secret reserves'.

5.1.9: Section Summary

This section set out to trace the early influences on the meanings and interpretations of the going concern concept. Within the limited evidence, it has been shown that the earlier meanings depended upon inherited wisdoms or 'common sense' views of accounting. This reflected the early accountants' association with the interests of 'finance capital'. The financiers only lent money to the businesses with the possibility of a long life. Within the dynamics of capitalism, this was dependent on whether a business maintained its capital and remained solvent. Thus early meanings of going concern reflected concerns with capital maintenance and solvency. Capital could be maintained by retaining profits (funds) to enable capital to renew itself. Thus depreciation became associated with going concerns.

Through the practices of bankruptcy, the accountants played a part in making capital mobile again and paid attention to the calculus associated with protecting the interests of financiers and bankers. To some extent, this gave recognition to the point that early accountants were dependent upon corporate patronage for their economic wellbeing. Frequently, after foreclosing the assets of a borrower, the financiers were only able to sell assets individually. Therefore, ways of valuing individual assets had to be found. In this sense 'cost minus depreciation' may have provided a simple 'rule of thumb' for ascertaining a going concern value. It is significant that the early discussions of going concern were associated with valuing assets individually rather than collectively. The concept was associated with a need for conservative values as this frequently gave the financiers an indication of the safety of their loans. They and the accountants used accounting ratios to diagnose the ability of a business to remain in existence. So deep has been the influence of such practices that the use of accounting ratios by auditors to diagnose going concern symptoms is considered to be a 'common sense' idea.

The going concern concept appears to become involved in wider social conflicts. In order to maintain the supremacy of company directors, the early accountants invoked the going concern concept to justify the need for 'secret reserves'. Such views were also supported by the courts who as the ISAs also promoted particular social order. However, the meanings of going concern cannot be fixed. In this context, it has been shown that up to the 1930s, the use of realizable values continued to be a competing meaning. However, when in the late nineteenth century, Britain experienced particular economic turbulenece, going concern began to be associated with the use of realizable values, at least in valuing stock. It is as though the economic changes provided a particular cradle for the transformation of the concept.

Many of the early views on going concern were encouraged or developed in an environment created by the State. The early accountants trained under the shadows of the legal profession and paid particular attention to the extant legislation. Nineteenth century corporate legislation required major businesses such as the railways (expected to have a very long life) to use 'costs' in their balance sheets. Within the ideologies of capitalism, for any business to remain a going concern, ways had to be found to reproduce capital. Thus legislation also required such companies to make depreciation provisions. These developments occured at a time when the State was trying to promote confidence in capitalism. As individuals specialising in legal matters, accountants were influenced by such laws and through their practice came to associate going concern with original costs and depreciation. By the 1930s, the meanings attached to the concept reflected a sedimented residue of traditions, bankruptcy practices, statutory requirements, case law, economic changes, corporate patronage and director/shareholder conflict.

5.2: GOING CONCERN FROM THE 1930s TO 1970s: THE AMERICAN CASE

After the initial formulations of its meanings, the going concern concept continued to receive numerous competing interpretations. These were shown in figure 3.2 (page 128). One of the major developments of the period was that the concept received explicit support from the accountancy profession and the state agencies. Despite being regarded as a relatively new concept (Littleton, 1933; Chatfield, 1968, 1977) it was described as a 'generally accepted accounting principle' (AIA, 1936, page 2). After this, as chapter 3 showed, the position rapidly changed. The concept continued to receive support (for example, Paton and Littleton, 1940; May 1943) and forceful criticisms (for example, MacNeal, 1939). Its scholarly scrutiny and institutional support continued through to the 1970s and 1980s. A major question then is why did the going concern concept receive institutional recognition and support in the USA in the 1930s?

In explaining this, the remainder of this section will argue that as a result of the economic crises, accounting came under particular scrutiny by the State and was found to be deficient. It was thought that by appealing to 'concepts' and 'principles', confidence in accounting and its role in workings of markets could be enhanced. In accordance with the dominant traditions of laissez-faire, it was expected that the Stock Exchange and the accountancy profession would take a lead in reforming accounting, but this was not to be the case. In such circumstances, the State had to intervene and create mechanisms for reforming accounting. However, this was not be an easy matter. After, the initial hostilities, a mutually supportive relationship between the State and the profession developed. In this context, the State and the profession continued to appeal to concepts and principles to restore confidence in capitalist ideologies and institutions. The State and profession were keen to invoke only certain meanings of the concept, but academics and others under the influence of economic theories were also able to invoke competing meanings of the concept.

In order to develop the above arguments, this section consists of five sub-sections. Section 5.2.1 shows that the economic crises provided the cradle for development of the going concern concept. Section 5.2.2 shows that many businessmen persued their short-term interests and devoted little attention to the legitimating role of accounting. Thus the State was forced to act in the long-term interests of capital and a State-Profession axis developed (section 5.2.3). However, intellectuals also played a part in legitimising some dominant meanings and promoting some secondary meanings of the concept. Therefore, section 5.2.4 examines the influence of the intellectuals on the forumlation and development of the meanings of the going concern concept. After a connective summary and discussion (5.2.5), the chapter moves to the third section.

5.2.1: Economic Crises

This section argues that the economic crises provided the cradle for the institutional recognition of the going concern concept.

For a considerable time, the American State within the contradictions of capitalism had actively sought to promote share ownership to the masses by relying on moral and market regulation (Merino and Neimark, 1982). Such an approach, encouraged some to indulge in fraudulent trading, manipulate financial statements and pursue private speculative goals which threatened the long term interests of capital. In view of the bull markets and increasing economic prosperity such practices went unchecked (Merino and Neimark, 1982, pages 43-44). The fact that over 90% of the companies listed on the New York Stock Exchange were independently audited did little to control unsavoury practices and furnish investors with useful information. Many companies resisted any attempts to explain their accounting methods or to provide additional information as such disclosures were seen as damaging to their competitive advantages (Carey, 1969). Contemporary accounting scholars (for example, Canning, 1929; Hatfield, 1927) influenced by economic thought (Whittington, 1986) were highly critical of the laissez-faire accounting practices and increasingly called for more disclosures to safeguard the interests of 'finance capital'. With the absence of "authoritative accounting or auditing standards" (Carmichael and Winters, 1985, page 56), some scholars called for the development of accounting concepts and principles to legitimise corporate disclosures and prevent manipulations in financial statements. In the wake of highly critical press comments (Zeff, 1984), the American Institute of Accountants (AIA), sought to co-operate with the New York Stock Exchange but with little success. Whilst the AIA was deliberating, events of great economic significance occurred and eventually led to a greater interest by the State in financial statements, accounting principles and concepts.

Such pressures came in the aftermath of the October 1929

Wall Street stock market crash. Until September 1929, the securities prices had been rapidly rising but began to decline in October 1929. Within a few weeks, fluctuations described as "technical readjustments" (Hawkins, 1986, page 387) turned into a full scale crash and some $30 billion was wiped off the value of listed companies. The public's confidence in capitalism was severely undermined (Galbraith, 1979). By 1930, the economy was in a definite decline and continued on its downward spiral until 1932. Hawkins (1986) describes the extent of crisis by noting that

> "the Dow-Jones industrial stock average fell from 386.10 to 40.56; the Dow-Jones railroad stock average sank from 190.60 to 13.16; the Dow-Jones utility stock average went from 144.61 to 15.78 and the New York Times average for 25 industrials fell from 469.49 to 57.62. By July 1932 the aggregate value of securities listed on the New York Stock Exchange stood at $15 billion- some $70 billion less than in September 1929 ...... between 1929 and 1933 the nation's gross national product fell from $104 billion to $56 billion; national income sank from $87 billion to $40 billion and per capita disposable income declined from $678 to $360. Unemployment rose from 1.5 million to 12.8 million; aggregate corporate profits fell from $10.3 billion to a net loss of $2 billion and the farm product price index sank from 105 to 51 (1926=100) ..... of the country's 24,000 banks in 1929 over 6000 had failed in 1933" (page 388-389).

The Wall Street crash helped to foster the feeling that information necessary for informed investor decisions was not being given to the wider public, especially when the investors were given financial statements described as 'correct' and then within days they heard that the company failed (MacNeal, 1939). The existence of numerous acceptable practices raised questions about the reliability and adequacy of information (May, 1943, chapter 3). Many managers, regulators and accountants also found it difficult to appeal to any coherent body of accounting principles to justify or explain their policies.

The existing accounting and disclosure practices were seen as a threat to the 'common sense' ideas of property rights and the individual's economic participation in economic welfare (Hawkins, 1986, chapter 8). Pressures for State intervention in the field of accounting grew, even though the American society tended to view such intervention with some suspicion. Some groups, such as the accountants and the Stock Exchange, were opposed to any widespread State intervention, especially as the ideologies of laissez-faire and caveat emptor had deep roots within the American culture. This ideology was, however, contested by those who felt that the corporations were unlikely to adopt meaningful voluntary reforms and that investors interests could only be protected by State intervention. The changing nature of society in which mass mergers, large corporations, capital and financial markets influenced everyday life, created further pressures for the State to intervene (Galbraith, 1979). However, in the first instance, the American accountancy profession and the Stock Exchange made half-hearted attempts to formulate accounting principles, but these were not to receive widespread support, as some representatives of capital continued to pursue their short-term aims.

5.2.2: Short-term Interests of Capital

The Wall Street crash and the ensuing economic decline led to a demand for reform in financial statement disclosure practices, but its shape was by no means clear. Traditionalists, which included the Stock Exchange and the AIA argued that improvements in disclosure and accounting practices could be achieved by market pressures and through the adoption of voluntary accounting standards. In the event, the AIA and the Stock Exchange sought to impose standards of disclosure on businesses (Zeff, 1984). As a part of this co-operation, the American Institute of Accountants[5] appointed a Committee under the chairmanship of George May, a Price Waterhouse partner, to develop accounting standards and policies. Similar arrangments had been mooted four years earlier in 1926, but now a new urgency existed. By 1932, the Committee advocated[6] some uniformity of practices and disclosures. Its report, dated 22nd September 1932, contains what is probably the first reference to 'accepted principles of accounting'. The 'principles' were concerned with the uniformity of accounting practices and disclosures rather than any underlying concepts such as the going concern concept. It echoed the residues of accounting 'common sense' by arguing that balance sheets should not show present value of assets and liabilties. The attempts of the Stock Exchange and the AIA to impose some accounting standards on businesses appeared to be too little too late and were not successful. Many capitalists were concerned with protecting their short-term aims and the main problem was the

> "continual unwillingness or inability of a number of corporate executives, aided and abetted by several segments of the financial community to correctly perceive and respond ..... toward financial disclosure" (Hawkins, 1986, page 449).

In the face of hostility from the business sector, the profession remained reluctant to approve any accounting principles (Zeff, 1984). Thus the stage was set for the State to intervene and take steps to restore the public's faith in capitalism and maintain an environment for accumulation of economic surpluses. In this context, the State and the profession co-operated and the going concern concept came to be described as a 'generally accepted accounting principle'.

5.2.3: The State-Profession Axis

The seeds of a more direct State intervention in the field of accounting were sown by the Presidential campaign of 1932. The Democrat candidate Franklin Roosevelt appealed to the 'common sense' ideologies of justice and fairness and promised that if elected, he would enact laws to protect investors and creditors from unscrupulous businesses. Greater information and accountability through the enactment of Securities Exchange Acts was to be part of this weapon. The 1932 book, 'The Modern Corporation and Private Property' by Berle and Means, which was highly critical of accounting practices, became a blueprint for the Securities Act of 1933 (Carey, 1969). In March 1933, Roosevelt became the 32nd President and in May 1933, the Securities Act (the first of a series) was passed.

The Securities Exchange Acts of 1933 and 1934 were designed to shift the boundaries of 'public' and 'private' information. Within the constraints of capitalism, the laws maintained the "social and economic status quo while restoring confidence in the existing system and its institutions" (Merino and Neimark, 1982, page 49). A Securities Exchange Commission (SEC) was set up and its major function was to enhance confidence in the securities market. It needed to encourage the investors to invest and to prevent them from withdrawing their investment funds. This had to be done by encouraging belief in 'shareholder democracy' and the belief that as 'owners' they would be entitled to information which would be useful to enable them to judge continuity of businesses and hence security of their investments. The belief in capitalism was further to be promoted by arguing that investors would be given reliable information based on 'principles', not just opinions. Such promises, in an era when people were witnessing advances in natural and physical sciences, frequently underpinned by 'principles', were further designed to persuade investors to have confidence in the contents of financial statements. The reluctance of many investors to invest was to be further attacked by reassuring them that all businesses were expected to be remain going concerns and that the management did not expect to liquidate or significantly curtail operations in the forseeable future.

Prior to 1933 there was "no authoritative compendium of accounting principles" (Hill, 1987) and "there were no generally accepted accounting principles" (Carey, 1969; Cochrane, 1950, page 450). In such an environment, the SEC needed the help of accountants, the assumed experts, in developing a compendium of acceptable accounting procedures and principles. But an uneasy relationship existed between the SEC and the American accounting profession. The profession, aided by the interests of 'finance', was keen to emphasise its relative autonomy from the State, but the government was concerned with the long term restructuring of industry which was inevitable after the great crash. Improved financial disclosure and accounting reforms were part of this programme. With accounting practices and lack of disclosure singled out for criticisms by the SEC, a Committee of the accountancy profession under the Chairmanship of George May continued to issue statements on accounting matters. This Committee in co-operation with the Stock Exchange in 1934, specified principles (procedures) of accounting, focusing on recognition of profit, revenue, etc.[7]. Belatedly, in October 1934, the Council of the American Institute of Accountants (AIA) approved the 'five basic principles'. In the quest for legitimacy, these were now to be described as 'generally accepted'. The 'going concern' concept did not receive any institutional recognition at this juncture, possibly because it was still regarded as a relatively new concept (Littleton, 1933; Chatfield, 1977). In 1934, the AIA also challenged the SEC's power to prescribe uniform accounting and opposed proposals for reform, but it nevertheless agreed to co-operate with the SEC and a mutually supportive relationship between the two continued to develop. By 1935, George May[8] argued that "Primarily, accounting is historical in its approach, with valuation entering into it at times as a safeguard. The emphasis is on cost"[9]. This emphasis on 'cost', as the previous sections argued was frequently legitimised by appealing to the going concern concept.

By 1936, the AIA began to refer to "adherence to generally accepted accounting principles [and] increased emphasis on accounting principles and consistency in their application" (AIA, 1936, page 1). It invoked historically and ideologically rooted ideas in accounting by adding that

> "one of the most important accounting conventions is that the balance sheet of a going concern shall be prepared on the assumption that the concern will continue in business ..... plant assets, permanent investments and intangibles are usually stated at cost or on some other historical basis without regard to present realizable or replacement value" (page 2).

With the above words, the going concern concept received its institutional baptism. Here going concern is taken to mean a business which is in full working order. The AIA (1936) legitimised the 'lower of cost or market rule' for valuing inventories and added that "an annual valuation of all the assets is neither practicable nor desirable for a going concern using its property only for production purposes" (page 2). Such views underlined the 'common sense' ideologies of capitalism and reflected the meanings which Dicksee, De Paula, Leake, Guthrie, Harris, Dawson and others had associated with going concern. Such authors considered 'cost' to be important and had downgraded the relevance of realizable and replacement values in balance sheets. The institutional support contended that accounting was concerned with the value of individual assets rather than the collective value of assets.

Intellectuals such as May (1943, 1948), despite being partners in accountancy firms continued to ignore the auditing contexts and appealed to the going concern concept to justify historical cost accounting. Through its policies, on controlling war time profiteering (Irish, 1948), the State further associated 'going concern' with 'costs'. It also used the going concern concept to rule out the use of replacement cost accounting (Chatfield, 1977). Further homage to the going concern concept and its traditional meanings continued. For example, in 1953, the American Institiute of Certified Public Accountants (AICPA) singled out going concern (now called the 'permanence postulate') for special attention. The concept was once again used to justify conservatism and historical cost accounting (AICPA, 1953) to paint a picture of permanence and stability. Further explicit support for the concept came from the American Accounting Association (AAA, 1957, page 2). The State-Profession co-operation meant that the profession maintained its relative autonomy over accounting and auditing whilst the State avoided becoming directly embroiled in accounting controversies. Indeed, to this day in the USA, there is no equivalent of the British Companies Acts, which regulates accounting.

Having penetrated the folklore of accounting and the heart of accounting education, the going concern concept continued to be invoked whenever the profession faced any challenge to its social legitimacy. For example, when the Accounting Principles Board (APB) faced challenges to its status, it appealed to the going concern concept (and other concepts) and plugged into the 'common sense' and historical meanings of the concept to assure its critics of the knowledge mandate of the profession (for example, see Moonitz, 1961; Sprouse and Moonitz, 1963; Grady 1965). The 'common sense' views of the concept continued to be invoked to justify valuing stock at the 'lower of cost and market value rule', historical costs, capital maintenance (Goldberg, 1960), allocation of costs (Spiller, 1964) and others. When in 1970 the profession faced severe criticisms, once again the going concern concept was wheeled out (AICPA, 1970), even though some critics were arguing that the concept should "no longer be regarded as fundamental" (Arthur Anderson, 1972, page 126). Seemingly, much of the appeal of the concept lay in demonstrating the knowledge mandate of the profession and securing its social legitimacy via such an appeal.

5.2.4: Intellectuals

Much of the pressures for recognition and transformation of the going concern concept also came from intellectuals who supported competing meanings of the concept. Their involvement legitimised some meanings and at the same time created tensions by supporting the others.

In this context, it is interesting to note that much of the academic respectability to 'principles' and historical cost was given by the publication of 'A Statement of Accounting Principles' (Sanders, Hatfield and Moore, 1938). This occurred at a time when the SEC had been pressurising the AIA to provide a

> "substantial authoritative support for the development and acceptance of accounting principles" (Zeff, 1972, pages 134-139).

The SEC, on the one hand professed its desire to furnish investors with relevant and reliable information, yet on the other hand under the influence of going concern and other accounting concepts, it became a firm supporter of historical cost accounting and conservatism. These contradictions were not lost on some scholars, who under the influence of economic theories had alternative images (Davis, Menon and Morgan, 1982) of whatever counted as relevant and reliable accounting information. For example, MacNeal (1939), writing at a time when the SEC supported the need for balance sheets to show historical costs of assets, felt that the institutional interpretations of the going concern concept were being used as a "defence for misrepresentation" (page 46) and argued that 'going concern' meant information about market values and replacement costs. Paton and Littleton (1940) argued that going concern justified information about the earning potential of a company. To counteract the competing discourses which were giving prominence to replacement costs, market values, etc., the SEC formally rejected such alternative bases (Chatfield, 1977, page 244). Academics such as May (1943, 1948) continued to invoke the going concern concept to maintain faith in historical cost accounting.

The traditional meanings of the concept went through rigorous academic analysis (Storey, 1959; Fremgen, 1968, Sterling 1968; Yu, 1971) and in a changing economic environment were found to be too static. Thus at times of economic instability, some felt that it justified focus on current costs (Edwards and Bell, 1961), constant purchasing power accounting (Gynther, 1966), exit values (Chambers, 1966), present values (Helfert, 1966; Gordon and Shillinglaw, 1969) and economic values (Hendriksen, 1970). One consequence of the various invocations of the meanings was that it created a sense of unease about accounting. Whereas in the past accounting may have been portrayed as 'factual' and 'objective, the academics increasingly exposed it as highly subjective and imprecise. During times of crisis, various interest groups could now make such competing meanings more critical and argue for a preferred type of accounting. In order to re-establish its authority, the profession, with the full approval of the State agencies, has again and again appealed to going concern and other concepts, apparently, in an effort to manage a crisis of legitimacy. During such crises, a ritual homage is now paid to the going concern concept but various writers also continue to invoke the sedimented residue of earlier meanings.

5.2.5: A Connective Summary and Discussion

This section has briefly explored the factors which led to the institutional recognition of the going concern concept in the USA. The concept received its institutional support in the cradle of a severe economic crisis. In the aftermath of the 1929 stock market crash and the related economic decline, accounting was seen as failing to provide the necessary information to investors and the requisite legitimacy to corporate disclosures. In an effort to restore confidence in financial disclosures and capitalism generally, both the State and profession appealed to the existence of 'generally accepted' accounting principles. In this context, for the first time in 1936, the concept received institutional recognition. Having recognised the concept as 'generally accepted', the earlier 'common sense' meanings of the concept continued to be elaborated. The concept frequently tended to be associated with historical costs, solvency, capital maintenance, etc., thus reflecting a sedimented residue of its historical meanings.

Subsequently, under the influence of economic theories, some scholars used the going concern concept to justify the need for replacement costs, realizable values, exit values, present values, etc., but in order to sustain the imagery of a stable environment, the institutions continued to appeal to 'common sense' views to legitimise past meanings. Appeals to the going concern and other accounting principles have also been made to manage the periodic crises which the American accountancy profession has been facing. Such appeals have now become part of a political tactic, through which the profession asks 'significant others' to have faith in its craft and knowledge base (Hines, 1989). Such appeals also bring benefits to corporations in that their disclosures may be considered more legitimate.

In contrast to the American position, the going concern concept did not receive institutional recognition in Britain until 1971. This is despite the fact that the earlier discussions of the concept were to be found in British books. Why did the concept receive an early recognition in the USA, but not in the UK until the 1970s? Whilst a large number of factors may have been responsible for this, figure 5.3 draws attention to some major influences.

Figure 5.3

Factors Influencing the Development of the Going Concern Concept During the 1930s

USA	BRITAIN
Deep economic crisis brought about by the Stock market crash and the ensuing decline.	The crisis was not so deep.
Professional bodies such as the American Institute of Accountants were not enthusiastic in helping the State.	Professional bodies had a privileged consultative status.
A State agency such as the SEC responsible for overseeing financial disclosure	Legislation on pragmatic and piecemeal basis.
A legitimation crisis managed by appealing to 'principles'	Legitimation crisis managed by periodic revisions of company law.
Reform of corporate practices was part of Presidential election pledges.	No such pledges.
Large number of accounting academics	No full-time accounting academic in the UK. First Chair established in 1947.
Academics challenged the SEC view.	No such development.
Going concern used to justify historical cost accounting with explicit support from profession and the State.	Going concern used to justify historical cost accounting with implicit support from profession and the State.

These factors include the extent of economic crises, the close relationship between the State and the profession which enabled a mutually supportive relationship to develop over a considerable period, the readiness of the State to intervene and legislate in the field of accounting via the Companies Acts and the relative lack of accounting academics in the UK. In explaining the institutional recognition of the concept, the next section will focus on these factors.

5.3: GOING CONCERN FROM THE 1930s TO 1970s: THE BRITISH CASE

The going concern concept received its institutional recognition in the USA in the 1930s. In sharp contrast, the concept did not receive this institutional support until the 1970s. This is despite the fact that British writers such as Dicksee, Leake, de Paula, Pixley, Dawson etc. were the first to discuss it. Such writers had firmly associated going concern with 'original costs', depreciation, secret reserves, dividends, capital maintenance etc. However, the question remains why the concept did not receive its institutional recognition earlier and why in the 1970s? In providing an answer, this section will focus on a number of issues identified in figure 5.3. It will be argued that unlike the USA, in the UK, a strong and mutually supportive relationship between the profession and the State existed. Therefore, the SEC type of zeal for reform was absent. Unlike the USA position, the British government, on a pragmatic basis, had been regulating accounting through the Companies Acts. Thus the pressures for reform were less in the 1930s. Through its 'insider' status, the profession was also able to influence legislation and protect the interests of its clients. This prevented the accounting ills from receiving greater public exposure and a crisis of legitimacy did not develop until the 1970s. Unlike the USA, Britain also had less academics.

Consequently, the competing discourses into which various meanings of the concept were inserted were less powerful. Accounting continued to be dominated by the practitioner's technocratic interests and thus little discussion of principles of concept occurred. From the late 1960s, a crisis of legitimacy for the profession developed and this was mediated by appealing to the going concern and other accounting concepts.

Following the above arguments, this section consists of three sub-sections. Section 5.3.1 focuses on the relationship between the British State and the accountancy profession. Section 5.3.2 examines the role of the academics and section 5.3.3 examines the crisis of legitimacy which eventually persuaded the profession describe the going concern concept as 'generally accepted' and 'fundamental'. Section 5.3.4 summarises the arguments of this section.

5.3.1: State-Profession Axis

Britain also experienced a stock market crash in 1930 but unlike the USA, its banking system and economy did not suffer as badly (Aaronovitch, Smith, Gardiner and Moore, 1981). The existence of an empire and a leading role in the international trade coupled with the Bank of England's role as a lender of last resort may have been the mitigating factors. Britain had previously experienced major banking failures and as a result various support and stablising systems had sprung up (Coakley and Harris, 1983).

In the field of company law, the British State had taken considerably more interest in regulating financial statement disclosures. The legislation was on a piecemeal and pragmatic basis. Even at the time of the stock market crash, the Greene Committee was considering revision of the corporate legislation. The issue of whether some information was to be regarded as 'public' or 'private' had resulted in legislation such as the Joint Companies Act 1844, 1856; Companies Act 1900, 1908 and so on. Such Acts concentrated on the balance sheet and had little to say about profit and loss accounts. It is noticeable that the early writers (Guthrie, 1883; Harris, 1883; Dicksee ,1892, 1904, 1912, 1915, 1928; Reid, 1897; Dawson, 1900; Leake, 1912; Dickinson, 1913; de Paula, 1915) invoked the going concern concept to discuss balance sheet aspects and rarely used it to discuss income statement aspects, though Pixley (1918, 1922) used it to justify secrecy.

In view of the influence of accounting on bankruptcy administration, price controls, taxation, bank audits and control of profiteering, a close and mutually supportive relationship between the State and the accountancy profession existed. Consequently, the UK profession had acquired the status of 'insider' and was consulted on regulatory matters. In keeping with this, the ICAEW was invited to give evidence to the Greene Committee. In its written evidence, the ICAEW opposed the publication of a profit and loss account on the ground that such disclosure may provide useful information to competitors and thus threaten the continuation of a business (Edey, 1979). The close relationship between the profession and the State did not mean that the State would always accept the ICAEW's recommendations. In order to act in the long-term interests of capital, it also had to consider the wider constituencies. By 1929, with an economic recession on the horizon and its implications for 'finance capital', a considerable amount of opinion favoured the publication of a profit and loss account (Bircher, 1988). The Greene Committee without referring to the going concern or any other accounting concept, recommended the provision (not publication) of a profit and loss statement to shareholders (though without the auditor's comments). This was made compulsory by the Companies Act 1929.

The Greene Committee permitted companies to maintain secret reserves. Pixley (1918, 1922) had already supported the desirability of secret reserves by citing the going concern concept. 'Secret reserves' were preferred by directors as it gave them considerable flexibility in disclosure and choice of accounting methods (Pollins, 1956). On numerous occasions, in cases involving shareholder and director conflict, the courts also respected director discretion and legitimised the creation of secret reserves (French, 1977). However, some within the profession, (for example, The Accountant, 21st November 1925, page 802) were opposed to the maintenance of secret reserves. In its evidence to the Greene Committee, the ICAEW argued that shareholders are entitled to clear, relevant and unambiguous information, but supported the need for 'secret reserves' (Hein, 1963a, 1963b). Under pressure from industrialists and corporations, the ICAEW continued to side with company directors and supported the need for secret reserves by arguing that secrecy would ensure continuity of operations (Edwards, 1981). Such views were, however, soon to be challenged by a publicly visible scandal relating to the Royal Mail Steam Packet Company.

On 20th July 1931, Lord Kylsant, the chairman of the Royal Mail Steam Packet Company and its auditor Mr. Morland of Price Waterhouse & Co. were charged with presenting a false and fraudulent balance sheet. Ironically, the action was brought by the State and centred around the question of secret reserves (Hastings, 1962). During 1929, the company sought to restructure its debt obligations to the Treasury, which in turn enquired into the company's financial affairs. Upon noticing secret reserves, the Treasury alleged that the balance sheet was fraudulent and commenced criminal proceedings against Lord Kylsant and Mr. Morland. Lord Plender, a leading accountant of the day, was called as an expert witness and defended the practice of secret reserves, which by then was deeply ingrained in accounting thinking. Both of the defendants were acquitted of the charge of presenting a fraudulent balance sheet[10]. After the Royal Mail case, there were demands for additional disclosures (Bircher, 1988) rather than any efforts to identify any 'generally accepted' concepts.

In the aftermath of the Wall Street crash, de Paula in the preface of his 1933 book 'Principles of Auditing', advocated the search for principles and lamented the lack of any progress by citing the absence of any "accepted and established principles governing these several matters"[11].

But the government was content with the current legislation and saw little need for reforms. In 1936, the American profession explicilty appealed to 'generally accepted accounting principles', but in the UK, the Board of Trade undertook a review of company law and concluded that the current state of affairs had no immediate and serious defect (Bircher, 1988). Neither the State nor the accountancy profession found any need to appeal to the going concern or any other accounting principle.

Despite the apparent satisfaction, various pressure groups continued to call for reforms (The Accountant, 25th October 1941; 25th April 1942). Perhaps, the next legislation would lead to an invocation and institutional support for the going concern concept. The mounting criticisms of company law led to the formation of the Cohen Committee in 1942, appointed to examine the existing company law. By a seeming coincidence, the ICAEW also started issuing its 'Recommendations on Accounting Principles' in 1942 under the chairmanship of F.R.M. de Paula. It should be recalled (see chapter 3) that important personalities such as de Paula and Leake firmly associated going concern values with 'cost minus depreciation'. De Paula's faith in costs may have been further enhanced during his time at the War Office, where he advised the government on ways of controlling profiteering on government contracts. Here 'costs' rather than realizable values were considered to be relevant. In his oral evidence to the Cohen Committee, de Paula stated that the

> "going concern value is represented by the cost of acquisition less a proper allowance for wear and tear"[12].

By 1943, the ICAEW reversed its support for secret reserves and Statement N6 argued that if such reserves do exist then they should be disclosed. After this the going concern concept was not used to justify 'secret reserves'. Eventually, the Companies Act 1948 also prohibited 'secret reserves' by ordinary commercial concerns, but privileged the interests of 'finance capital' by permitting banks, discount houses and insurance companies to continue operating secret reserves. None of the ICAEW's recommendations made any explicit reference to the going concern concept, but the sedimented residue of earlier meanings is clearly there. For example, Statement N9 (issued 12th January 1945) noted that fixed assets

> ".... are held with the object of earning revenue and not for the purpose of sale in the ordinary course of business. The amount at which they are shown in the balance sheet does not purport to represent realisable value or their replacement value, but is normally an historical record of their cost less amounts provided in respect of depreciation, amortisation or depletion" (para 1).

Statement N10 (issued 15th June 1945) on 'The valuation of Stock-in-Trade' excavated the residue of historical meanings attached to the going concern concept and recommended that stock be valued at the lower of cost and market value. Statement N12 (ICAEW, 1949) rejected replacement costs and N15 asserted the supremacy of historical costs (ICAEW, 1952). Infused with the 'common sense' ideologies from the days of bankruptcy practices, a belief continued to exist that somehow original cost is 'factual' and anything else is suspect. Such faith had also been encouraged by State policies which in an effort to control war time profiteering had also made 'costs' the prime focus of accounting (Loft, 1986). The profession and the State did not directly appeal to the going concern concept to legitimise the preferred accounting choices. Perhaps the going concern concept was still not important in the UK, or that neither the State nor the profession as yet had faced a legitimation crisis which required rationalisation of accounting practices by an appeal to 'principles'. Recent writers such as Pickles (1934), Rowland and Magee (1934, 1936), Bace (1937), Binnie and Manning (1938) and Tovey (1948) certainly made no direct references to the going concern concept and Leake (1947) continued to associate it with historical cost.

However, new challenges to accounting were emerging and diverse demands for financial information were being made by the emergence of major institutions as investors. The Cohen Committe's report (Cmnd 6659, 1945), which formed the basis of the Companies Act 1948 made references to 'going concern' to make a case for the publication of the profit and loss account. It argued that

> "..... the profit and loss account is as important as, if not more important than, the balance sheet, since the trend of profits is the best indication of the prosperity of the company and the value of assets depends largely on the maintenance of the business as a going concern" (para 96).

Here, it took going concern to mean a business which is in full working order. The Cohen Committee ruled out the use of realizable values. It invoked the deeply rooted meanings of going concern to argue a case for historical costs by stating that

> "if a balance sheet were to attempt to show the net worth of the undertaking, the fixed assets would require to be revalued at frequent intervals and the information thus given would be deceptive since the value of such assets while the company is a going concern in most cases have no relation to their value if the undertaking fails" (para 98).

The next major reform of accounting and auditing came in the shape of the Companies Act 1967. In paving the way for the Act, the Jenkins Committee issued a questionnaire inviting certain organizations and individuals to comment on various parts of the exisiting legislation. Unlike the proliferation of accounting concepts in the USA and the search for conceptual frameworks, the questionnaire made no explicit references to going concern or any other accounting concept. However, the 1,607 pages of oral and written submissions did raise questions about the valuation of assets at historical cost, especially as more and more companies were involved in contested take-over bids and serious questions were being posed about the adequacy of the balance sheet figures. Any suggestion of revaluing assets was opposed by some interest groups. However, in order to accommodate the various competing demands, the Jenkins Committee endorsed the historical cost basis for valuation of assets, but left the door open for companies to show such assets at a valuation, should the directors so choose. The ideological struggles over the meaning of accounting and 'public' and 'private' information continued, but the existing practices had still not been sufficiently ruptured to warrant an appeal to 'principles'.

Despite direct and indirect references to going concern, neither the State nor the profession described it as a 'fundamental' or a 'generally accepted' concept. One possible reason for this may be the comparative lack of interest in accounting theory which frequently arises from academic circles.

5.3.2: Academics

In the USA, full-time accounting academics such as MacNeal, Littleton, Paton, Hatfield, Edwards and Bell, Moonitz, Canning, Sterling and others debated the meaning of the going concern concept. Each author, under the influence of economic theories, appealed to the multi-accented meanings of the concept to argue a case for replacement costs, realizable values, cash flow and other varieties of accounting. In contrast, in the UK there was comparatively little equivalent reaction or debate. This is partly due to the fact the USA had a comparatively large number of accounting academics.

In Britain, the first full-time professor of accounting was not appointed until 1947[13] and the second chair was not created until 1955. Accounting only began to be studied as a 'degree course' in the early 1960s (Solomons and Burridge, 1974, page 40). Most of the early writers on going concern were partners in accountancy firms, though some held academic posts. The practical problems were uppermost in their mind and this was frequently reflected in their discussions of the going concern concept. In the UK, Lawrence Dicksee was the holder of the first part-time Chair of Accounting at the

University of Birmingham in 1902 and subsequently became the first teacher of Accounting at the London School of Economics (LSE). He became Professor of Accounting in 1912 and retired in 1926 (Kitchen and Parker, 1980). Dicksee was concerned with valuation of assets and saw cost minus depreciation as being a good approximator of the value of an asset. Such ideas also enmeshed with the contemporary concerns on distribution of profits, where a major concern was with ascertainment of profits. Depreciation provisions were considered to be essential for replacement of assets and reproduction of capital.

F.R.M. de Paula, a writer on going concern, also held part-time academic posts at the LSE until 1929. He became the Vice-chairman of the ICAEW's Taxation and Financial Relations Committee (TFRC) in 1942 and was responsible for formulation of the 'Recommendations on Accounting Principles'. Both Dicksee and de Paula firmly associated going concern with original cost. In recognition of de Paula's privileged position both as an intellectual and a spokesperson for the ICAEW, the Cohen Committee in 1942 also asked him to give evidence on company law (Kitchen, 1979). In his evidence, de Paula continued to associate going concern with 'cost less depreciation'. However, at no point, did he describe going concern as a 'fundamental' or a 'generally accepted' principle. Stanley Rowland, the secretary of the TFRC was also a partner in Dicksee's firm and also gave accounting lectures at the LSE. Rowland's books hardly made any explicit references to the going concern concept. Other writers on going concern, such as Leake and Pixley, were also partners accountancy firms, but did not describe the concept as 'generally accepted'.

Earlier authors in the main tended to be practitioners concerned with their immediate technocratic interests, rather than any theoretical and conceptual issues. Men like Rowland and de Paula were powerful influences on the formulation of professional pronouncements. Indeed, the ICAEW's 'Recommendations on Accounting Principles', despite appeals to 'principles' do not identify any theoretical structure of financial accounting or auditing. The professional education system required students to devote most of their attention to learning professional pronouncements and legal aspects and little attention was devoted to any conceptual discussions (Edey, 1989). Books by Dicksee and de Paula were the standard recommended texts and set the mould for the future generations. It is noticeable that after the issue of 'Recommendations on Accounting Principles', many accounting books made increasing references to professional pronouncements and made no direct reference to the going concern concept (for example, Pickles and Dunkerley, 1960; Rowland and Magee, 1961), even though the concept was dicussed by early writers such as Dicksee and de Paula and had received institutional recognition in the USA. Unlike the American position, the British books continued to reflect the inherited wisdom of the nineteenth century (Edey, 1989). By 1961, the ICAEW started to issue 'Statements on Auditing', but these were designed to guide practitioners on technical matters and did not contain any references to the going concern concept either. In the well established mould, professional education continued to be pre-occupied with imparting technical skills (Hastings and Hinings, 1970; Solomons and Burridge, 1974).

Indeed, compared to the USA, between the 1930s and 1960s, the UK experienced very little conceptual or theoretical discussions of accounting and auditing, so much so that Bromwich (1985) has labelled the period as the "dark ages" (page 21). However, from the mid-1960s, the picture began to change, as accounting began to emerge as a respectable subject worthy of academic study (Hopwood and Bromwich, 1984). This, coupled with economic, social and political developments set the scene for a critical scrutiny of accounting and paved the way for institutional recognition of the going concern concept.

5.3.3: Crises of Legitimacy

During the 1960s, the average rate of profitability in the British industry continued to decline (Fleming, Price and Ingram, 1976). The government sought to arrest the economic decline by promoting mergers in the hope that this would make the larger units more efficient and thus enable them to compete effectively in the international markets (Hannah, 1976). The mergers focused increasing attention on the role played by accounting in constructing and reporting corporate affairs. The measurements of efficiency were difficult because the published balance sheets were widely regarded as misleading (Hein, 1963a, page 253). In view of the developments in financial and capital markets, influential magazines were arguing for the need to publish market values of fixed assets so that informed decisions could be made about business continuity (Aranya, 1979). As part of this debate, the Stock Exchange felt that disclosure such as that relating to turnover would be helpful, but the ICAEW was opposed to it (Aranya, 1979). In such debates, the UK profession did not appeal to the going concern or any other concept to legitimise its interests, or to support/oppose accounting reforms. It is as though the corporate accounting and disclosure practices in the UK had not confronted widespread scepticism by 'significant others' experienced in the USA and thus little need existed to appeal to 'principles'.

The State sponsored mergers, concerns with efficiency, economies of scale and London's role in international financial markets, increased pressures for the scrutiny of accounting practices. These were frequently fuelled by some well known corporate failures, such as the Fire & Auto Insurance and Rolls Razor. In 1964, soon after receiving an unqualified audit report, Rolls Razor collapsed. The Economist (25th July, 1964) argued that

> "shareholders have not been given all the information about the company's affairs" (page 401).

Whilst some accountants were aware of the highly selective and subjective nature of accounting, it nevertheless retained an aura of exactness and precision. This aura was soon to be challenged by further exposures. In 1967, GEC made an unwelcome takeover bid for AEI (see Zeff, 1972 for further details). In this contested bid, the AEI directors produced a profit forecast just 10 weeks before the end of the year, showing a profit of £10 million. Such a forecast was authenticated by a reputable firm of auditors. In the final analysis, GEC was successful in its bid. Upon preparing the accounts, the AEI segment of GEC revealed a loss of £4.5 million. The difference was attributed to judgements about stock valuation and long term contracts. Amidst the recriminations, the Daily Telegraph (27th July, 1968) criticised published accounts by referring to the

> "pathetic belief in the validity of accounts and in the declared asset value of businesses".

Whilst the dust from the GEC/AEI merger was settling, further criticisms of accounting emerged in the aftermath of Leasco's takeover bid for Pergamon Press. Pergamon's accounts carried an unqualified audit report, but its accounting policies were criticised by the press. The Economist (30th August, 1969, pages 43-44) attacked the profession for its failure to specify appropriate practices. The Times (29th August 1969, page 9), expressed its disapproval of current accounting and auditing practices. Much of the auditing business was conducted by the Big-Eight firms who were also expanding into new areas, such as management consultancy. In the eyes of some, this posed a threat to auditor independence. The Sunday Times (7th September, 1969) commented that

> "the auditor is very much in the pocket of a company's board of directors".

The Guardian (22nd October, 1969) described the auditing practices as "highly unsatisfactory ..... [which] cannot be tolerated" (page 15).

So incessant were the criticisms of accounting, auditing and other practices that the government appointed inspectors to investigate the Pergamon affair (The Times, 10th September 1969, page 21). The interim report on Pergamon Press (DoT, 1971a) highlighted the lack of accounting uniformity and principles as a major factor contributing to the difficulties in isolating good accounting and auditing practices from bad. The DoT inspectors were particularly critical of auditors (DoT, 1973, para 1244). The critical debates about accounting were given a sharper edge by the intervention of an academic, Professor Edward Stamp. He felt that the lack of any coherent accounting theoretical framework was responsible for a multiplicity of accounting rules and procedures (The Times, 11th September 1969, page 25). The practitioners had been arguing that their practice was firmly based upon 'principles', but Stamp argued that they were just technical rules and not 'principles'. In reply (The Times, 22nd September, 1969) the ICAEW President, Mr. (later Sir) Ronald Leach emphasised the difficulties of assessing "the profit of a going concern for so short a period of 12 months" (page 25), evidently using going concen in a literal sense, i.e. a business which is in full working order. Leach saw little immediate prospect of developing simple, unambiguous, generally accepted principles. Further pressures were added by the Chairman of the City Panel on Take-overs and Mergers, who openly called upon the ICAEW to more closely define the 'correct practice' (The Accountant, 27th November 1969, page 747). Statements by representatives of productive capital and finance capital added to such pressures (Cooper et al, 1989).

The widespread press criticisms unmasked the dominant view of accounting as a 'precise scientific language' and threatened its appearance of objectivity and independence. This unmasking was seen as damaging not only to the interests of professional accountants, but also to the companies whose disclosures and accounting practices were being legitimised by auditors.

The criticisms were seen as a threat to professional autonomy, especially as the State had already set a number of Department of Trade investigations in motion. Under such circumstances, on 12th December 1969, the ICAEW announced its intention to issue Statements on Standard Accounting Practice (SSAP) and the Accounting Standards Steering Committee (ASSC) was formed in January 1970. The ASSC was to work closely with the City interests and the Confederation of British Industry (all representing capital), though the full membership was restricted to accountants. In the face of criticisms, the profession sought to legitimate accounting practices and its interests by appealing to 'accounting principles'. Such appeals to 'principles' in the American context were already helping the profession to answer its critics (Zeff, 1972). Therefore, the case for referring to them in the UK was fairly persuasive. In this context, the 'going concern concept', for the first time, received institutional support in the UK. It was described as a 'fundamental accounting concept' (ASC, 1971) and was seen as part of a

> "whole new terminology .... beginning of a UK accounting theory .... an area in which Britain seems to have lagged well behind the United States" (Accountancy, February 1971, page 54).

At a time when the number of bankruptcies and liquidations in Britain were on the increase and the industry's rate of profitability and investments was significantly declining (Armstrong, Glyn and Harrison, 1985), the concept was defined to mean that

> "the enterprise will continue in operational existence for the forseeable future. This means that the profit and loss account and balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operation" (ASC, 1971, para 14).

Such an interpretation invoked the sedimented residue of meanings deeply rooted in historical and ideological factors. It helped to mediate the crisis facing the profession and its allies. Through the concept, the profession appealed to the 'common sense' views of practitioners, even though the recent major books had little to say about it. SSAP 2 itself, had actually nothing to say about the consequences of the concept for specific accounting practices, valuation bases, disclosures and auditing aspects. Despite issuing 'Statements on Auditing' at the time, the ICAEW made no attempt to issue any auditing pronouncement on either the going concern or any other 'fundamental' accounting concept. Whether the profession was serious in describing the concept as 'fundamental' is unclear. Indeed, Arthur Anderson (1972) were less than enthusiastic about the concept and argued that "it precludes reflection of economic realities in the financial statements" (page 125). In view of the mid-1970s secondary banking crisis and the related collapse of the property market[14], the ICAEW soon argued that going concern valuation base is

> "unsuitable for use in relation to property assets of a company" (ICAEW, 1974, para 3).

Seemingly, the interests of capital required the profession to downgrade one of its own fundamental concepts. Perhaps, the labelling of the 'concept' as 'fundamental' had enabled the profession to manage a crisis of legitimacy and reassert its ideological identity as a learned profession.

5.3.4: Section Summary and Discussion

The purpose of this section has been to explain the institutional recognition of the going concern concept in the UK. This recognition came in the 1970s, wheras in the USA, the concept became 'generally accepted' in the 1930s. Some of the major factors responsible for this divergence were highlighted in figure 5.2 and subsequently discussed in this section.

Both Britain and America experienced economic crises, but in the UK the crisis was not so deep. In order to manage the crisis, numerous management mechanisms were instituted and co-opted into the State. In the USA, this led to the creation of a new regulatory agency, the SEC, with powers to regulate financial reporting. In the UK, since the late nineteenth century, a close relationship between the profession and the State had existed. Further, the State undertook regular revisions of the Companies Acts and a specific body was not created to push for any uniformity of accounting practices. Consequently, neither party found a need to appeal to going concern or any other accounting concept or principle to either articulate its demands or defend its position.

In the USA, the stock market crash and the ensuing economic decline led to demands for more relevant and reliable information. This demand was further fuelled by the fact that there were no equivalents of the Companies Acts to guide the preparers and issuers of financial statements. To fill this void, a regulatory body rather than legislation was enacted. In order to enhance confidence in capitalism, the SEC became a guardian of historical cost accounting and conservatism and frequently invoked the going concern concept to justify this. The going concern concept continued to be used to justify valuing fixed assets at 'original cost minus depreciation' and the 'lower of cost and market' value rule.

In Britain too, the State became a defender of historical costs, but unlike the USA, the academic opposition to it was absent. In the USA, many academics contested this dominant meanings of the going concern concept and with it the scope of accounting. Scholars, influenced by economics, appealed to the going concern concept to argue a case for current costs, constant purchasing power, cash flow reporting and other varieties of accounting. However, none of these received the required institutional support and going concern remained firmly associated with historical costs.

In Britain, a number of elements came together in the late 1960s to create pressures for the formulation of accounting principles. Such pressures emanated from economic changes relating to falling profitability, merger activity, the workings of finance markets and the newly emerging interest from academics and the press. 'Significant others' alleged that accounting practices were deficient and were failing to provide the required legitimacy to corporate disclosures. Prior to this, the ICAEW, in its accounting and auditing pronouncements, did not make any explicit mention of the concept, though the sedimented residue of historical meanings of the concept lingered on in its statements. However, when faced with new challenges, the profession appealed to the going concern concept to regain control of its immediate environment. The institutions became defenders and promoters of 'cost minus depreciation', 'lower of cost and market value rule' and other traditional meanings of the going concern concept. Seemingly, as though the concept was invoked not to develop any theoretical framework, but to defend either the interests of the profession or perhaps the interests of an elite within the profession.

5.4: CHAPTER SUMMARY AND DISCUSSION

This chapter set out to explore the relationship between accounting and society by looking at the changing meanings and interpretations of the going concern concept. The meanings of the concept are influenced by a wide variety of factors. These relate to the deeply rooted 'common sense' ideologies of capitalism, influence of the State, the courts, bankruptcy practices, sympathy with the interests of directors, changing economic environment and the crises of confidence faced by the profession at various times.

The early meanings of the concept were shaped by statutes which legitimised 'cost' as a reporting base for railways, banks and insurance companies. Adherence to 'costs' was designed to promote the long-term interests of capital and give assurances to investors about director propriety. The State legitimised the use of 'costs' by using them to control profiteering during its war time management of the economy. Under such influences, 'original costs' took a firm hold in accounting thought and continued to be associated with 'going concern'. In order to reproduce capital, the early legislation also specified a need for depreciation and the courts pronounced on these issues through matters relating to dividends and secret reserves. In view of their earlier association with legal matters, the accountants paid attention to legal developments and came to associate discussions of going concern with dividends and secret reserves.

The economic crises have provided the cradle for the institutional recognition of the going concern concept. In the face of an economic crisis, the American State scrutinised accounting practices in order to redraw the boundaries between 'public and 'private' information. It had to act in the long-term interests of capital, espcially as some businessmen were more concerned with pursuing their short-term interests. Such intervention was initially resisted by the profession, but it too saw an opportunity to enhance its social status and thus appealed to accounting principles. In this context, the going concern concept was invoked to promote confidence in accounting practices and enhance legitimacy of the corporate accounting practices. Seemingly, the going concern concept became part of a legitimation crisis management.

Not only the institutional recognition, but the meanings and interpretations of the concept have also been shaped by the economic crises. The case of stock valuation shows that in the face of falling prices, accountants modified their practices and invoked the concept to justify the 'lower of cost and market value rule'. In the absence of any further research, this association with the economic must, however, remain tentative. The institutionalisation of the concept in Britain shows that an economic crisis alone may not be the only reason for institutional support for the concept. It is rather as though a number of diverse elements coming together, pose a challenge to the functions of accounting and its institutions, who in turn appeal to the going concern and other accounting concepts to manage this crisis. In the UK, this occurred at a time when the economy was going through considerable restructuring through mergers and other means. Such events combined with press comments, intervention of academics, industrialists and the State revealed the selective nature of accounting and posed a threat to the profession. This threatened to unmask the 'independent' and 'objective' image of accounting and posed dangers to the legitimacy of the published financial information. In such circumstances, the profession (and possibly the State) legitimised its interests by appealing to the going concern concept.

The interpretations of the going concern concept also reveal that accounting principles/practices are frequently mobilised to support the interests of directors and finance capital. The concept was used to justify the rights of directors to maintain secret reserves. After the Royal Mail case, such privileges were removed from ordinary companies, but retained by 'finance capital'. Much of the earlier associations of the concept with valuations, conservatism and 'lower of cost and market value rule' also show sympathy with the interests of finance capital and carries a residue from the times when accountants were primarily concerned with bankruptcy practices.

Going concern concept is a multi-accented concept. Its various meanings compete for ascendancy. Meanings are unlikely to be permanent. After the Royal Mail case, the Companies Act 1948 prohibited 'secret reserves' and subsequently, no book justified such reserves by invoking the concept. Various groups have also been invoking competing meanings to justify the use of replacement costs, realizable values, present values, cash flow accounting etc. It is possible that under some conditions such associations may become stronger. Particular meaning may be dominant because they legitimise some institutions and ideologies. For example, the American profession and the State promoted the association of going concern with 'original costs' and notions of 'permanence' to give investors an illusion of stability, rather than reminding them that under capitalism, bankruptcies and liquidations are inevitable. It rejected the association of the concept with replacement costs and exit values.

Over a period, mythology and tradition have become powerful influences on the way going concern concept has been invoked and interpreted. Much of the thought on going concern was developed by early accountants who occupied prominent positions in the profession. Through the educational processes, the early accountants were concerned with learning basic rules and often accepted the wisdom of the pioneers such as Dicksee, de Paula, Leake, Pixley and others. Such men had received their training when 'original costs' and conservatism were the mainstay of accounting. Their influence lingered on, not only in books and professional writings but also in legislation. By the early twentieth century, the traditional meanings of going concern were well embedded in folklore, myth and 'common sense'. Most authors now find an irresistable need to refer to its well established and historically rooted meanings. Despite its contradictions, it is also remarkable that the meanings given to the concept by institutions have changed so little.

The further investigation of the meanings and interpretations of the concept in the subsequent chapter may reveal that the concept continues to be modified by the economic crises, actions of the State, widespread criticisms and a legitimacy crisis facing the profession. The subsequent chapters will focus on such matters to explain the changing meanings and interpretations of the concept and thus illuminate the complicated relationship between accounting and society.

Chapter 5 Footnotes:

1) As quoted in Strachan, 1985.

2) As mentioned in Jones, 1981, pages 48-49.

3) As quoted in Loft, 1986, page 144.

4) This is not to say that some contemporary accountants were not concerned with technical discussions such as the recognition and realization of profits.

5) At the time, the Institute had a membership of about 2,000. It is now known as the American Institute of Certified Public Accountants (AICPA).

6) Further details will be found in the two volumes edited by Zeff and Moonitz (1984).

7) The full list is reproduced in The Accountant, 19th May 1934, pages 698-709.

8) George May's training was almost entirely in bankruptcy work. He trained during an era when historical cost was regarded as the basis for valuing fixed assets (Grady, 1962, page 10). Also see earlier parts of this chapter.

9) As quoted in Storey, 1964, and reproduced in Chatfield, 1968, page, 363.

10) From his analysis of the case Royal Mail case, Ashton (1986) came to conclude that the prosecution failed because it did not adequately use the going concern concept i.e. arguing that the information presented was deficient and did not enable the plaintiffs to make informed judgements about corporate survival. However, his analysis overlooks the point that at this juncture, the concept had not received any explicit UK institutional support by being described as 'fundamental' or 'generally accepted'. Indeed, at the beginning of the case, going concern was not described in these terms even in the USA, where since the 1929 stock market crash, there had been comparatively greater discussion of accounting theory and concepts.

11) As cited in Kitchen and Parker, 1980, page 96.

12) As quoted in Kitchen, 1979, page 289.

13) This was Professor William Baxter at the London School of Economics.

14) The impact of secondary banking crisis and the property market crash is discussed in chapter 6.