Business World

Abused Accountants Say 'Take This Job and . . .'

By HOLMAN W. JENKINS JR.

What if an accounting firm had a conflicts-of-interest policy and nobody followed it? Maybe the accountants are trying to tell us something.

That's the story behind the story about PriceWaterhouseCoopers earlier this month. At the world's biggest accounting firm, the staff was on notice: Partners and associates, not to mention spouses and significant others, would have to liquidate any investments—stocks, bonds, bank accounts—in companies audited by the firm. Spouses were even called upon to give up jobs at employers audited by the firm. The SEC was watching. Let's show 'em we can give Caesar's wife a run for her virtue.

But you know how it is: The phone rings, the holidays come, and an aggravating and personally costly exercise in maintaining "appearances" slides off the agenda and ends up behind the refrigerator.

According to an outside investigator hired at the SEC's bidding, some 85% of PriceWaterhouse partners failed to properly sanitize their personal finances. That includes 31 of the firm's 43 top executives, and six of the 11 partners directly responsible for enforcing the policy.

When a set of rules is honored so universally in the breach, it raises questions, all right. The SEC has worked hard to persuade people that the system of audited accounts is what underpins our financial markets. Five PriceWaterhouse partners and an undisclosed number of associates were fired.

Then again, those of us inclined to view things ironically might see an act of passive resistance by PriceWaterhouse employees, saying "Let's not exaggerate the importance of the work we do here."

No doubt the world needs accountants and a common accounting language. Without them, businesses wouldn't know their costs and profits. Investors wouldn't know where to entrust their money.

But when the banks began pushing their commercial borrowers to adopt uniform accounting a century ago, accountants weren't policemen; they were educators, teaching business people (who were presumed to be honest) how to capture the dynamics of their business on a balance sheet. The hope was that with a better idea of their costs, companies would be less inclined to chase business they could only do at a loss.

It wasn't until the 1930s that the SEC began requiring every company that issues stocks and bonds to get an annual sign-off from a CPA. The accountants, seeing a recession-proof flow of business coming their way, didn't object, though they worried about liability, arguing—as they have ever since—that they shouldn't be held responsible for managements that lie or provide incomplete information.
Well, if it's not to catch fraud, what exactly is the purpose of the federal make-work project known as the public audit? That question never has really been answered.

On the rare occasions when auditors have issued "qualified" opinions or resigned accounts in protest, almost invariably they are blowing the whistle on problems the market has already uncovered. Meanwhile, the last few decades have treated us to a parade of companies that received clean bills of health and then promptly collapsed or were forced to acknowledge serious improprieties. To name a few: Continental Illinois, LTV, Braniff, the entire savings and loan industry, Sunbeam, Waste Management, Oxford Health and Cendant.

By now it should be permissible to state the paradox: Either the accountants aren't doing their job or the job has been puffed up in importance beyond its natural deserts. At worst investors are being misled if they believe an accountant's signature means very much. At best, the annual audit provides a forum for exchanging shoptalk with CFOs.

The SEC, however, seems to have convinced itself that the public audit can play a bigger role if the accountants would just become a little more "independent." The message coming from the PriceWaterhouse rank and file is "Don't press your luck."

Last year, Ernst & Young simply quit doing audits for Baan, the Dutch software firm, because it interfered with more lucrative work as a consultant promoting and installing Baan software. More of the same is coming. The annual audit is a ritual that neither companies nor investors nor the accountants themselves place much value on. When Tyco's accounting was criticized by a fund manager last October, waving a stack of favorable opinions from PriceWaterhouse didn't stop the stock from plunging. It was a chorus of Wall Street analysts that effectively defended the company's bookkeeping.

If companies aren't getting value from their accountants, they aren't going to pay top dollar. But the accounting firms somehow have to compensate their highly skilled human capital. That's why the Big Five have been tripping over their mothers to get into consulting, legal services, software, financial planning and insurance. The annual audit is a federal gravy train that hardly pays its way anymore.

PriceWaterhouse's outside investigator found the accounting behemoth rife with "serious structural and cultural problems." Yes, and one of them was management's embrace of an excessive and fussy definition of conflicts of interest. Any sane person would be satisfied with a rule prohibiting employees from investing in companies they are directly involved in auditing. Telling 10,000 employees and their spouses to ransack their lives for the sake of an accounting job is bizarre.

In a larger sense, these doings reflect the terminal throes of a primitive, mid-century approach to assuring performance and accountability in society.

From any functional perspective, the annual audit serves today mainly to give the lawyers somebody else to sue when a company goes bad. Yet the deluge of lawsuits in recent years has done nothing to improve the quality of financial reporting.

Creating hostages to litigation is a lousy way of incentivizing proper behavior, but it remains one of the approaches contesting for the future. More advanced sectors have recognized that creating webs of common interest works better than the punitive daddy. Shareholders shell out big money to give ownership stakes to senior management. Companies invest vast sums to create "brands" as a way of making themselves hostage to the good opinion of consumers.
This is the wave of the future. If the SEC wants to get ahead of the curve, perhaps it should start inviting the accounting firms to take long-term stakes in companies whose books they audit. Hectoring accountants to play a policeman role they've never been willing to play can only speed the exodus to better-paying lines of work.

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