

1 The Challenge of an Accountant

1-1 Briloff Appears: The Briloff's Testimony at the United States Congressional Hearing

On February 20, 1985, a certified public accountant was summoned as a witness to testify before one of the most powerful committees in the United States Congress. Despite approaching the age of 70, he carried an air of elegance, reflected in his calm demeanor, fair complexion, and the determination etched into his prominent cheeks. Chairman Dingell's opening remarks resonated through the hushed committee room.

"The committee will now commence a series of public hearings concerning the effectiveness of independent accountants who audit widely held corporations, as well as the Securities and Exchange Commission, which oversees these auditors. The responsibility of independent accountants lies in substantiating the publicly reported financial statements that collectively represent a company's financial condition. This responsibility transcends any employment relationship with their clients. Independent accountants, in fulfilling this role, bear the ultimate responsibility not only to a company's creditors and shareholders but also to the general public. As public watchdogs, accountants must maintain independence from their clients at all times and uphold unwavering loyalty to the public trust..."

As the witness approached the stand at Chairman Dingell's prompting, he reached out, touched the edge of the table, and murmured something in a low voice. To the audience, it sounded like a barely audible "Sorry." Only then did they realize that the dark sunglasses he wore were not a fashion statement but a necessity—his impaired vision rendered the table and people around him indistinct.

At first, his voice was difficult to discern, but as he continued, his rhetoric grew sharper, laced with sarcasm, mockery, and even traces of anger.

"Mr. Chairman, I am honored to testify before this subcommittee on my views regarding professional accountants. The frequent bankruptcies of financial institutions in the 1980s—such as Penn Central Bank and United American Bank—along with numerous savings and loan associations (S&Ls), raise a fundamental question: Why did they happen? In many cases, bankruptcy struck the day after an audit report had given a clean bill of

financial health. Where were the certified public accountants at that time? Given the fraudulent practices concealed under the guise of Generally Accepted Accounting Principles (GAAP), perhaps it would be more fitting to redefine GAAP as *Cleverly Rigged Accounting Ploys*. Furthermore, an even greater concern than GAAP is the excessively lenient accounting standards—Regulatory Accounting Principles (RAP)—that govern financial institutions like S&Ls...”

The next day, *The New York Times* ran an extensive report on the hearing under the headline: “**The Role of Accounting Faces Crisis.**”

From Washington, February 20— Today, Congress was presented with the following findings: The fundamental public oversight function performed by accountants in auditing the books of widely held corporations is being undermined by conflicts of interest within major accounting firms and lax supervision by the Securities and Exchange Commission (SEC). This marks the first in a series of hearings conducted by the House Subcommittee on Energy and Commerce to examine the integrity and conduct of professional accountants. Today’s hearing focused on recent cases in which financial crises followed clean audit opinions issued by accountants for banks and other companies. Subsequent investigations revealed fraud, misleading financial statements, and questionable lending practices.

The key witness in this hearing was none other than **Abraham J. Briloff**, a distinguished professor at Baruch College, City University of New York, widely known as “Abe.” Born in 1917, he was 79 years old at the time—a scholar, a practitioner, a prominent accountant with an office in the Gramercy Park Hotel in New York, a prolific writer contributing to the financial magazine *Barron’s*, a sought-after lecturer, and a fierce critic of the American accounting system. At the same time, he was a staunch advocate of free and democratic capitalism.

1-2 A Critic of the U.S. Accounting System

In 1985, Briloff received an honorary doctorate from Binghamton University, State University of New York. During the ceremony, a professor praised his achievements, stating:

“Abraham Briloff’s insights into accounting have captivated our students for years. He presents accounting not merely as a technical profession but as the guardian of corporate ethics and the protector of truth in practical

affairs. His words resonate with the innate idealism of our young students, striking a deep chord within them. What makes Professor Briloff especially compelling is his ability to elevate intricate accounting details into broader ethical discussions. This is possible only because of his unparalleled mastery of the technical aspects of accounting... It is no surprise that many auditors dislike his critical analyses of audit practices. But that is precisely why his role is indispensable. In every society, and in every field of study, when someone sees that the emperor is wearing no clothes, we need individuals with the courage to say: *'No matter what anyone else claims, the emperor is wearing absolutely nothing!'* And Abe Briloff embodies that courage fully."

Since then, Binghamton University has hosted the **"Abraham J. Briloff Lecture Series on Accounting and Society"** in his honor.

In August 1995, the Public Interest Section of the American Accounting Association awarded Briloff the **Accounting Exemplar Award** in recognition of his contributions to accounting education and ethical professional conduct.

However, in April 1996, events took an unexpected turn. Briloff and his beloved daughter were accused of professional ethics violations and summoned before the Peer Review Committee of the American Institute of Certified Public Accountants (AICPA).

What exactly happened to him?

2 Briloff is Being Sued

Are auditors professionals or just robots? In August of last year, while casually reading the one-week-old Sunday edition of *The New York Times* (August 4, 1996 issue) at the library, College of Economic, Nihon University, my attention was caught by an article. With the somewhat exaggerated headline, "*Auditors: Are They Experts or Just Robots?*" the article begins with the question: "*Are accountants independent professionals who exercise judgment, or do they merely follow rules and checklists?*" Unexpectedly, the article then transitions to discussing the case of Briloff.

Mr. Abe Briloff, along with his daughter Leonore, runs a small accounting firm. He is currently under investigation for professional ethics violations. However, the investigation is not due to allegations of improper services rendered to clients, but rather his candid manner of speaking. The controversy began when Briloff's accounting firm underwent a peer review by the American Institute of Certified Public Accountants (AICPA), which identified deficiencies in their handling of professional matters—something Briloff himself considers absurd. According to the article, ironically, the New York State Society of Certified Public Accountants was about to honor Briloff for his contributions to accounting education. However, *The New York Times* barely covered this aspect of the story.

Curious, I immediately contacted Briloff directly and obtained documents related to the peer review investigation, as well as letters presenting the perspectives of both parties. Later, I received a two-hour tape of Briloff passionately discussing the matter. After reviewing and listening to these materials from a neutral standpoint, it became apparent that the root of the problem ran deep. This is how the incident unfolded.

Briloff's accounting firm was reported to the peer review committee by an unidentified complainant on two counts of deficiencies. The first count pertained to a 1993 financial statement preparation report for a small charitable trust. The firm prepared the financial statements without conducting an audit or review, yet included the following "assurance" statement:

"While we have not performed an independent examination of the financial statements attached hereto, we have performed all the procedures we deemed necessary to reflect properly all transactions and adjustments that

we considered necessary to present fairly the financial position and results of operations of the trust for the year.”

In other words, they provided assurance without conducting an audit—an explicit violation of the AICPA’s *Statements on Standards for Accounting and Review Services*, which requires CPAs to disclose when financial statements have not been compiled, reviewed, or audited.

The second count concerned a 1995 audit report for a research and development foundation supporting small psychoanalytic research initiatives. Briloff’s firm failed to obtain a representation letter from the foundation’s prominent psychiatrist and did not disclose the resulting audit scope limitation in the report. This was suspected to be a violation of *Auditing Standard No. 19*.

For a small accounting firm with only two accountants, the peer review committee’s investigation was particularly challenging. The committee scrutinized them according to strict regulations, asking questions such as:

- “*Was the quality control system of your firm, which allowed such engagements, adequate?*”
- “*Was the internal inspection system in your firm truly sufficient?*”
- “*I would like to discuss the facts of the ethics violations with the AICPA’s Professional Ethics Division. I request your response within ten days.*”

2-1 Briloff’s Defense: Standards Are Not Rules

However, Brilov’s official response to the peer review committee chairman suggests that his actions were deliberate. He asserts:

“The alleged deficiencies pointed out by the reviewers are not ‘sins of omission.’ The measures we took were the result of careful consideration. If our actions were indeed abnormal, it is not due to a lack of ‘supervision’ by our office, but rather due to significant deficiencies determined by your reviewer and approved by your committee.”

Briloff further argues that professional accounting standards are not rigid rules but guidelines that require professional judgment, considering time and circumstances. Notably, the first issue involved a minuscule public charitable trust with total assets of only \$120,000 and cash holdings of just \$39. Briloff contends that including an assurance statement in the tax

return was necessary to fulfill their professional duty to the trust and its operators. Essentially, they had to choose between assuming responsibility for preparing financial statements without audit assurance or providing appropriate assurance under the Internal Revenue Code and relevant state laws.

Regarding the second issue of the missing confirmation letter, Briloff mockingly remarked:

"The conclusion is no different than considering it inappropriate for me to ask a renowned psychiatrist, who is a foundation operator, for confirmation about the application of Freud's teachings and practices."

Briloff then revealed a crucial point: when submitting a tax return for a private foundation, the operator is required to attach a sworn statement attesting to the accuracy and completeness of the report. Thus, he argues, a separate confirmation letter was unnecessary.

His response concludes with a sharp critique:

"It is ironic that accounting firms that express the truth and proper representation through unbiased and freely interpreted professional standards are stigmatized, while firms that fabricate facts with a rigid interpretation receive praise from the AICPA's high-ranking committee. Isn't that ironic?"

An article in *Accounting Today* (June 17, 1996 / July 7, 1996 issue) features a statement from Professor Burton, former Chief Accountant of the SEC and now a professor at Columbia University. He asserts:

"It's ridiculous to attack Abe Briloff by raising objections about an ethical issue of all things."

As the magazine suggests, is it possible that this incident merely involves minor errors in routine procedures and that the AICPA is retaliating against Briloff?

Currently, Briloff is said to be fortifying his position for the battle ahead. With characteristic sarcasm, he remarks:

"I'm 79 years old, and this incident will surely continue for at least four or five more years."

Long live Brilov! (*To be continued in the next issue.*)

3 Criticism of Briloff Lowers Stock Prices!?

The December 14, 1981, issue of *Barron's* magazine extensively covered the debate between Abraham Briloff and Professor Siedler of New York University, featuring their photographs across several pages. I purchased the magazine, Barrons, at a transfer station in Chicago while traveling from the University of Michigan's Payton Accounting Center, where I was studying since June, to the University of Missouri, Columbia.

Though it was merely a photograph, this marked my first encounter with Briloff during my time abroad. Late at night, as I watched the Christmas trees adorned with neon lights flicker in the houses visible from the Greyhound bus, I immersed myself in the debate between the two scholars under the dim reading light.

3-1 The Briloff-Siedler Debate

In the July 6 issue of the same magazine, about five months earlier, Briloff criticized the accounting practices of SafeCard Corporation, revealing that the company's reported profit for 1980 was, in reality, an equivalent loss. As soon as *Barron's* published the article, SafeCard's stock price plummeted from \$25 per share to \$10. When confronted with Briloff's critiques, companies typically take one of three approaches: remaining silent, issuing press releases or filing lawsuits, or seeking third-party opinions. SafeCard Corporation opted for the second and third options.

The company released a strongly worded statement to newspapers:

"For those unfamiliar with the true nature of Abraham Briloff, this 'professor' is nothing more than a wolf in sheep's clothing, parading under the guise of an affiliation with New York City College. He is merely a figurehead for Dow Jones & Company, the parent company of *Barron's*... It is unfortunate that this 'professor' is legally considered visually impaired, as he bears no obligation to ascertain the facts. Such matters are of no concern to *Barron's*. The 'professor' simply revels in voicing his 'opinions' openly... *Barron's* has always provided a makeshift stage for the 'professor' to lecture the public. Continuing to preserve such a platform under Briloff's name is merely a plaything for him."

Additionally, SafeCard sued Dow Jones & Company rather than Briloff himself, but the lawsuit was dismissed in a lower court in 1982 and again in an appellate court in 1983.

Professor Siedler, acting through a brokerage firm he advised, strongly refuted Briloff's analysis in a letter, which SafeCard subsequently distributed to shareholders and the financial industry—an example of the company's third strategy against Briloff's criticism. *Barron's* attempted to invite Siedler to present the letter's contents, but he declined, stating it was a personal study. Consequently, *Barron's* published the aforementioned article, revisiting Briloff's arguments in light of Siedler's counterpoints. However, the two finally faced off in a seminar at Columbia University the following April.

3-2 The Core Issue: Accounting for Marketing Costs

The primary point of contention was whether it was appropriate for SafeCard to capitalize its substantial marketing costs related to membership recruitment and extend the amortization period from three to ten years. Siedler countered Briloff's critique by referencing fundamental accounting principles. He supported SafeCard's accounting approach, arguing that when discounted to present value, expected future membership fees justified the capitalization of marketing costs and ensured sufficient cash flow.

At first glance, the debate between Briloff and Siedler appears technical, but a key question remains: did Briloff's criticism actually cause stock prices to decline? Some might argue that stock price drops coinciding with Briloff's publications were mere coincidences. However, a detailed study comparing the stock prices of 21 companies criticized by Briloff in *Barron's* between 1968 and 1984 showed an average decline of 8.11% the day after publication. Furthermore, when Briloff's critiques extended beyond accounting inconsistencies to management decision-making, the decline reached 9.39%, compared to a 4.9% drop when GAAP violations were the sole focus. Based on this data, SafeCard's case falls more in the latter category.

3-3 The Broader Impact of Briloff's Criticism

Briloff's influence on stock prices remains a topic of interest in U.S. accounting circles. If capital markets are efficient and investors

incorporate publicly available information into stock prices, then any stock price decline following Briloff's critiques must be due to other factors. However, repeated instances suggest a correlation between his criticism and market reactions. Briloff was known for being a sharp critic, not only of corporate accounting but also of accountants themselves.

In *Revolution in Financial Reporting*, a well-known accounting book by William Beaver, Briloff's critiques are extensively discussed. If his papers do, in fact, impact stock prices, several explanations could be considered: Does Briloff possess insider information? Does he uncover unique insights through interviews with executives? Or does his superior methodology generate new information? However, a review of Briloff's papers suggests that he does not introduce new, undisclosed information.

So, what is the source of his influence? Unless one assumes that capital markets are inefficient, the answer must lie with Briloff himself. This is why, in the U.S., some say that even without presenting new information, "he knows more than what is written in the paper," making his criticisms credible. Additionally, his critiques may influence government regulations on industries, leading to more pessimistic future outlooks for the companies he scrutinizes. Briloff's arguments often go beyond accounting practices, questioning the ethical foundations of management decisions.

In a letter to Professor Foster of Stanford University, who conducted a detailed analysis of Briloff's work and stock price movements in 1987, Briloff remarked:

"Given the current psychological state of the general public, I believe that thorough investigative analysis like mine would hardly generate much excitement anymore."

Is Briloff attempting to shed light on the shortcomings of modern U.S. accounting from a new perspective? To explore this, we may need to return to his starting point—the 1960s, when his criticisms sparked significant controversy. *(To be continued in the next issue.)*

4 Criticism of Briloff's Dirty Pooling

Anthony Sampson, a non-fiction writer from the United Kingdom, is well known in our country for his books such as *The Seven Sisters*, which explores the inner workings of major international oil corporations. His book *Corporate State ITT* (Simar Publishing) thoroughly exposes the reality of ITT, a conglomerate that led major corporate mergers in the United States during the 1960s. In Chapter 5, titled "ITT Castle: Tactics of Management and Accounting," Briloff is introduced as follows:

"The opacity of conglomerate accounting sparked criticism from accounting experts. One of the most outspoken critics was Abraham Briloff, an accounting professor at Baruch College in New York. A passionate advocate for transparency, Briloff maintained his office in the Gramercy Park Hotel and did not mince words. He authored a witty and incisive book on 'unaccountable accounting,' analyzing the deceptive tactics used in conglomerates." (*Translated version, p. 160*)

Through this book, I first learned about Briloff. Inspired by his work, I promptly wrote to him, expressing my thoughts. This marked the beginning of my correspondence with him.

4-1 Dirty Pooling and Dirty Patches

In 1965, Briloff became a professor at Baruch College, New York University. Despite being nearly 50 years old at the time, he continued to write prolifically, as the era demanded his expertise. The American economy was experiencing a significant boom, often referred to as the Third Merger Movement. This period saw the rise of new conglomerate mergers, in which companies from various industries merged without restrictions. However, the accounting treatments applied to these mergers were left largely to the discretion of the companies involved. Though accounting principles existed, they were often ineffective in practice.

Briloff boldly criticized this state of affairs, departing from his earlier style to confront two key issues. First, he targeted the pooling method of accounting, which facilitated "profit begetting profit." Despite its potential for manipulation, this method was largely ignored by both the Accounting Principles Board (APB), which set accounting standards at the time, and the Securities and Exchange Commission (SEC). His second major criticism was directed at certified public accountants, who failed to fulfill their

professional responsibility by passively accepting these questionable practices.

In 1965, Briloff published his influential paper "Dirty Pooling" in *The Accounting Review*. The following year, on July 15, his work was prominently featured on the front page of *Barron's* magazine under the ironic subtitle, "The Laws of Success in Business Without Real Effort." Over the next two years, *Barron's* published several of his critical articles, including:

- *All Jumbled Up – Computer Lease Accounting: Illusions and Unrealities*
- *Abuse After Abuse of Goodwill*
- *Misplaced Focus – The Accounting Practices of Film Chemicals Deemed Perfect by Accountants*
- *A Castle Made of Sand – Questioning the Accounting Practices of Real Estate Developers*
- *What Will Happen to Future Profits? – Telex Corporation Giving Too Much Profit Now*

His renowned book *Unaccountable Accounting* (1972), a compilation of his *Barron's* contributions, used unconventional and striking expressions for an accounting publication. He famously wrote:

"A balance sheet is much like a bikini swimsuit: it reveals intriguing aspects but conceals the vital parts... Ziggy is already out of fashion, and even bikinis have become outdated. Accountants should prepare a flexible ruler, like a skilled tailor dedicated to the art of business, allowing them to freely adapt to the question of 'how much is 2 plus 2?'"

Thus began Briloff's critique of dirty pooling. Instead of exchanging all shares with the acquiring company's stock in a corporate acquisition, a portion was converted into convertible preferred stock, which could be exchanged in a few years, effectively forming a subsidiary. By using the pooling method, which was permitted at the time, these shares were valued at face value rather than market value, allowing book values to be carried over. This accounting technique obscured the critical difference between the market value and the cost of the shares. Furthermore, as earnings per share were diluted due to the preferred stock, reported earnings per share appeared to increase artificially. Briloff referred to these manipulative practices as "deception towards shareholders through stock dilution."

One might assume that using the purchase method—where the acquired company's balance sheet is revalued at market value—would resolve these issues. However, this too had its pitfalls, which Briloff dubbed "dirty purchases." The difference between market value and book value was recorded as goodwill, which remained unamortized. Consequently, selling assets at book value generated artificial profits, and if the acquiring company was later sold without adjustments, its book value remained artificially low, creating further illusory gains. In Briloff's signature style, he described this phenomenon as follows:

"Liquidnix's report discloses the profits associated with the disposal of subsidiaries, while the previously recognized 'goodwill' lingers like the ironic laughter of the Cheshire Cat in *Alice's Wonderland*."

4-2 Accountants' Accountability

During this period, Briloff published his first major work, *The Effectiveness of Corporate Communication* (1967), based on his doctoral thesis. The book's preface was written by the esteemed Supreme Court Justice William O. Douglas, known for his consistent liberal stance during his over 30-year tenure on the Court. Although the nature of their personal relationship remains unclear, Justice Douglas's words perfectly align with Briloff's mission. He wrote:

"Mr. Briloff seeks to grant the independent auditor a duty that is omnipresent, transcending the narrow relationship with the client itself. This duty extends to all those who have the right to complete and fair disclosure of corporate activities... The strength of our capitalist society lies in trust—trust in those to whom power is delegated. This trust necessitates an effective system of checks and balances, ensuring efficiency in communication between all members of society. Accountants play a crucial role in this communication."

In the *Financial Analysts Journal* (May-June 1966), Briloff further argued that CPAs, by performing independent audits or attestation functions for modern American corporations, assumed broad responsibilities. These responsibilities extended beyond shareholders to pension funds, insurers, and bank subscribers who had invested in these companies.

The 1960s, when Briloff made his bold entrance onto the scene, saw a growing awareness of the "expectation gap" in accounting, much like the

concerns present in modern-day America. Lawsuits against accountants were increasing, and the diversity of Generally Accepted Accounting Principles (GAAP) became a subject of contention. Meanwhile, it became evident that regulatory bodies such as the APB and SEC were not adequately fulfilling their functions. These challenges, exemplified by the issues surrounding dirty pooling, ultimately led to the establishment of the Financial Accounting Standards Board (FASB). Briloff played a central role in these developments, and his critical stance remained steadfast for over 30 years.

Even today, Briloff continues to argue that merger accounting creates new and questionable accounting practices. Recently, he authored a paper titled "Revisiting Unaccountable Accounting." What concerns him most about the current American accounting system? (To be continued in the next issue.)

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6 Briloff in the U.S. Congress

Regarding recent administrative reform proposals in Japan, there was a brief debate on whether to establish a Japanese version of the U.S. Government Accountability Office (GAO), following the American model. However, the discussion quickly subsided. In contrast, the original GAO in the U.S. conducts policy research with remarkable vigor. Through email, I receive GAO reports almost daily, covering a broad range of topics from nuclear energy and agriculture to healthcare and accounting. Given its budget scale and the thoroughness of its reports, one might wonder whether a Japanese GAO could ever match such an extensive scope of activities if established.

6-1 The Hidden History of the American Accounting System

In September of last year, the GAO published two reports titled *Accounting Profession*, which provide a comprehensive analysis of the activities of various institutions—such as Congress, the SEC, FASB, and the American Institute of Certified Public Accountants (AICPA)—from 1972 to 1995 regarding financial reporting and auditing systems in the U.S. These reports serve both as a vast repository of historical data and as a policy recommendation.

Reading these reports with Briloff's perspective in mind, one can discern a clear correlation between the activities of these institutions and Briloff's persistent criticisms of the American accounting system. It is almost as if Briloff's critiques serve as an alternative historical account of the modern American accounting system.

The reports trace Congress's direct engagement with issues concerning the accounting profession, beginning in the 1970s. Briloff describes this period as follows: "The first direct and overt intervention by Congress in overseeing the accounting profession occurred in the mid-1970s. In my view, the benchmarks of this intervention were the House Interstate and Foreign Commerce Committee's Oversight and Investigations Subcommittee (Moss Committee) and the Senate Government Operations Committee's Reports, Accounting, and Management Subcommittee (Metcalf Committee)."

6-2 Briloff's Criticism in Congressional Hearings

The GAO reports devote considerable pages to the activities of these two committees. Briloff himself testified as a witness before both. In hindsight, these hearings marked his dramatic debut in Congressional proceedings.

The Metcalf Committee, in particular, later published a voluminous report titled *The Accounting Establishment* (1977), spanning over 1,700 pages, of which more than 100 pages consist of Briloff's testimony and supporting documents. In his testimony, Briloff meticulously exposed how approximately 85% of clients listed on the New York Stock Exchange were dominated by the then "Big Eight" accounting firms. He also revealed that the Financial Accounting Standards Board (FASB) was effectively controlled by the corporate sector and the Big Eight. Moreover, he expressed concern that these firms were shifting their focus from audit services to management consulting, thereby compromising the independence of auditors.

Another major target of Briloff's testimony before the Metcalf Committee was the controversial deferred treatment of research and development (R&D) costs for Lockheed's TriStar aircraft, which had also drawn attention in Japan. He rigorously analyzed whether the auditing firm's endorsement of this deferral was appropriate, especially given the sluggish sales of the new aircraft, which cast doubt on the recoverability of the massive R&D expenditures.

Meanwhile, Briloff's testimony before the Moss Committee on May 21, 1976, challenged a then-recent Supreme Court ruling on accountants' liability. He argued for expanding accountants' responsibility beyond corporate clients to the general public. As Briloff noted, the role of accounting had expanded unprecedentedly. The Energy Policy and Conservation Act of 1975, enacted the previous year, mandated the SEC to ensure the reliability of accounting information, in response to the widespread manipulation of energy cost calculations. The 1970s marked the politicization of accounting, with Briloff playing a key role in this transformation.

Possibly influenced by these Congressional committee activities, the Foreign Corrupt Practices Act (FCPA) was enacted in 1977. This law required American corporations to establish internal control systems and adhere to GAAP to prevent bribery of foreign government officials. Briloff

highly praised this legislation, particularly for two reasons: first, it entrusted accounting regulations to Congress rather than the accounting profession itself; and second, it extended accounting oversight to corporate internal controls, thereby enhancing disclosure reliability.

6-3 Accounting Scandals and Briloff's Continuing Testimony

In the 1980s, accounting scandals were closely linked to the collapse of financial institutions. The House Energy and Commerce Committee (Dingell Committee) took up this issue, launching deliberations in 1985. Once again, Briloff testified. He criticized the Federal Home Loan Bank Board for allowing struggling savings and loan (S&L) institutions to meet the regulatory 3% capital requirement by replacing the pooling-of-interests method with purchase accounting, which allowed goodwill recognition. He argued that this practice demonstrated how accounting principles were manipulated to serve political convenience.

In the 1990s, Congressional hearings focused on limiting accountants' liability in damages lawsuits. The Senate Banking, Housing, and Urban Affairs Committee's Securities Subcommittee convened a hearing on July 21, 1993, where Briloff questioned the claims made by the Big Six accounting firms regarding the supposed "liability crisis." He challenged their assertion that legal settlements and litigation costs had skyrocketed to \$783 million in 1992, constituting 14.3% of their revenues. Briloff pointed out that this calculation was flawed because it excluded revenues from tax and consulting services, which doubled the firms' total revenue to \$12 billion, reducing the actual impact to merely 6.5%.

He then delivered a scathing remark: "Audit services often serve as the initial foothold for firms to expand their business and increase fees. Given this mutual relationship, it is misleading to claim that only the audit and accounting divisions are incurring losses."

A Turning Point for the American Accounting System

Contrary to common perceptions in Japan, the U.S. Congress has continuously scrutinized accounting and auditing systems since the 1970s, marking several pivotal moments. At each of these junctures, Briloff has repeatedly testified before Congressional committees.

The extent to which his testimony has directly influenced subsequent institutional reforms remains uncertain. However, it is undeniable that Congress recognizes his significance.

Once again, the American accounting system appears to be at another turning point. The SEC's increasing intervention is amplifying the need for greater neutrality in FASB. At the same time, Briloff has intensified his criticism of the AICPA. The ongoing evolution of the accounting landscape suggests that his insights will remain relevant in shaping future reforms.

7 Briloff Takes on the Big Six

In the August 1994 issue of *The CPA Journal*, Briloff published an article titled "Jurassic Park, Where Our Profession Gathers." In it, he poses a critical question: "Have we been led astray by the temptation to provide highly lucrative consulting services, resulting in the creation of uncontrollable monsters?" Briloff warns that the accounting profession has come to resemble a Jurassic Park, teeming with such monsters.

7-1 The World of Monsters

At the time, a United Nations survey titled *Management Consulting* issued an urgent warning to accountants, highlighting the presence of a colossal "monster" within the accounting profession. Briloff urges accountants to take heed. According to the survey, management consulting services (MAS) constituted a significant portion of the Big Six firms' revenue, surpassing that of their audit divisions. Between 1987 and 1991, Arthur Andersen, in particular, saw a 170% increase in MAS revenue worldwide, with 46% of its domestic revenue stemming from MAS. Even KPMG, which relied on MAS the least, still derived a quarter of its revenue from these services.

For nearly 30 years, Briloff consistently raised concerns about the contradiction within the Big Six firms, which engaged in two conflicting activities: auditing and MAS. He voiced his concerns in congressional committees, lectures, and articles. Initially, ancillary services accounted for only 15% of the Big Eight firms' revenue. Given the dramatic increase, Briloff now views the situation with grave concern. He identifies several key issues:

- Inclusion of unqualified individuals in CPA firm partnerships
- Aggressive and ambitious MAS groups infiltrating the firm's professional environment
- Neglect of independent audit responsibilities and the professionals tasked with them
- The detrimental impact of escalating profit competition on those responsible for upholding professional standards

Furthermore, the nature of MAS is evolving. The United Nations survey states: "Management consulting is transitioning from providing detailed advisory services to specialized areas... If an advisory is proven incorrect, consultants can no longer escape responsibility. This reflects an

increasing trend toward contracts with clients that involve shared profits.” Consequently, some within the Big Six firms now consider themselves multidisciplinary professional service firms rather than solely accounting and auditing firms. What should be done?

Briloff proposes separating these two activities into distinct companies. He argues, “I have consistently maintained that accounting firms should sever ties with these ancillary service departments, rededicate themselves to the professional mission underlying our licensure, and focus on expressing opinions regarding the reliability of financial statements. By doing so, we honor our ‘contract with society.’” In 1989, Arthur Andersen took a step in this direction by establishing a legally separate entity, Andersen Consulting. Could such a measure be the radical solution needed to safeguard auditor independence?

7-2 Briloff Opposes the AICPA!

In 1994, the American Institute of Certified Public Accountants (AICPA) released a report titled *Strengthening the Professional Occupation of Independent Auditors*. This report, which sparked debate across the American accounting industry, addresses the very issues Briloff has long criticized.

“Independent audit firms need to focus on improving their auditing services rather than being overshadowed by large and diversified public accounting and consulting firms. To achieve this, firm leadership must reconsider their organizational structure and business strategies,” the report states.

However, Briloff argues that the report lacks practical effect. He highlights that at the previous year’s AICPA council meeting, firm partners were allowed to participate even without holding CPA qualifications, and a settlement was reached with the non-CPA MAS group.

Briloff’s criticism, however, extends beyond this issue. The report was prepared by the *Advisory Committee on Auditor Independence*, established by the AICPA in response to criticism from Walter Schuetze, then Chief Accountant of the SEC. Schuetze had raised concerns about auditor independence, describing four accounting treatments approved by auditors as “incredible.” Yet, the report fails to take a definitive stance on these treatments, a point Briloff meticulously exposes.

For example, he questions whether it is acceptable to attribute the issue of Coopers & Lybrand approving accounting treatments that allowed Florida insurance companies to circumvent loss reserve regulations—by selling junk bonds to Merrill Lynch at the end of the fiscal year and repurchasing Treasury securities of the same value in the new fiscal year—to individual accountants rather than to Coopers & Lybrand as a firm. In reality, substantial financial penalties were paid by those involved: Merrill Lynch paid \$45 million, Coopers & Lybrand paid \$50 million, and the GSL law firm paid \$5 million, suggesting an admission of wrongdoing.

Briloff also addressed this issue during a Senate hearing, stating:

“Regarding the role of Coopers & Lybrand, my view can be summed up in one word: awful. Why did C&L persist in these irrational actions, even if only accidentally? In my opinion, the firm lost sight of its own professional integrity. They violated and defiled the contract between our profession and society.”

Briloff recounts detailed anecdotes illustrating these concerns. Ironically, despite being a report intended to respond to Schuetze’s criticism, it ultimately advises the Chief Accountant to maintain a harmonious relationship with the industry. Even Schuetze himself, when asked about the report’s comments, responded vaguely: “I have answered the [report’s] comments.” He concluded his remarks by emphasizing the stance auditors should adopt—before resigning as Chief Accountant.

“I have lived and worked for over 30 years as a member of the accounting profession. I understand the difficulty of saying ‘no’ to clients—the prolonged and intense phone calls, visits, emotional tension, and economic losses that accompany such decisions. However, I also understand the rewards: a clear conscience, freedom from lawsuit anxiety, pride in the profession, and, ultimately, the reliability of financial accounting and reporting,” Briloff stated.

At a 1995 American Accounting Association conference, Briloff referred to Schuetze’s unexpected shift in opinion regarding the AICPA report, from initial disapproval to later support. Briloff concluded his speech by quoting Schuetze’s own words, expressing hope that he still upholds the values of “a clear conscience and pride.”

9 Briloff's Accounting Education

In 1996, the "Abraham J. Briloff Prizes in Business Ethics" were established at Baruch College, City University of New York. The inaugural recipients were freshman student Mr. Kurohoru, for his paper titled "Ethics Must Be Voluntary," and Professor Marilyn Kleinberg Neimark, for her paper titled "Selling Corporate Ethics: Corporate Ethics Must Align with Ethical Companies." The \$25,000 funding for the prize was provided by Mr. Dreyfus, a company president from New York and a former student of Briloff (graduated from Baruch College in 1966, MBA in 1973).

9-1 Thoughts on Establishing the Briloff Prize

Regarding why the Briloff Prize was established, Mr. Dreyfus reflects on Briloff's accounting education in an article published in *Britann*, which includes the first-winning paper. He states the following:

"I first encountered Professor Briloff during my graduate studies in the spring of 1968, not during my undergraduate years. I registered for an accounting course, but it was a course that only Abe could teach. What I learned in this course profoundly changed both myself and my life.

During my undergraduate years, I had good grades in accounting, but I had very little interest in the subject. I can honestly say that I had almost no desire to study it earnestly. However, during my graduate studies, my interest reversed. Abe Briloff brought to life what I needed to uncover—the true meaning behind the numbers, and who is responsible for those numbers. I vividly remember engaging in lengthy discussions with Professor Briloff even after the lectures ended."

This highlights Briloff's role as an educator who, even more than 20 years after his graduation from graduate school, continued to have a significant impact, not as an accounting scholar or accountant, but as an active analyst and portfolio manager. Mr. Dreyfus discusses Briloff's accounting education, saying, "Professor Briloff made us consider not only the responsibilities of those who create and audit financial statements but also the meaning behind the numerical values in those statements. He constantly challenged us to explore alternative methods beyond the prescribed accounting treatments. He explained the nuances and potential weaknesses of accounting principles. At that time, I was interested in stock markets and investment styles related to low stock prices. However,

Professor Briloff taught me to view them from a different perspective, in light of accounting truths.”

Briloff himself spoke about his approach to graduate education, stating that regardless of the accounting problem at hand—whether it involved consolidations or any other aspect—he would first reveal the actual accounting practices complying with the accounting rules. Then, he would ask, “Indeed, it may turn out that way, but is that truly the right way of thinking?” He would pose this question to his graduate students, sparking discussions with them. This must have led to intense dialectical exchanges with the students in pursuit of uncovering the “correct” accounting practices.

9-2 The Foundation of Accounting Education Lies in Ethics

Regarding the accounting education in the department, Briloff received the 1982 Faculty Education Award from the alumni association of Baruch College. In his acceptance speech, he said to the undergraduate students, “My education is not about giving credits for specific subjects or creating experts in the field, but rather about instilling values that can be shared with generations of students. The education at Baruch College aims not only to equip you with the skills necessary for economic independence, which is certainly a prerequisite for freedom in society, but also to go beyond these narrow objectives and create intellectually insightful individuals who can free their minds and understand themselves.”

Can accounting education instill values in students that have an impact on society? What did Briloff do for that purpose? When Briloff was responsible for teaching “Introduction to Accounting” before becoming an honorary professor, he would start his conversation with undergraduate students by asking, “What do you think accounting is?” Invariably, the students would respond, “It involves keeping records, preparing tax returns, and related technical tasks.” In response to this answer, Briloff would state, “Accounting, accounting practices, and accountants are deeply involved in communication with people who need data for better decision-making.” Through this, he would remind students that communication is the key concept in accounting education and urge them to understand it. This marked the beginning of his accounting education.

The classes would likely unfold as follows. With a vast amount of authority delegated to company managers, the managers, as the senders of

accounting communication, have a complete and fair accountability to all affected parties, including owners of funds such as pensions, insurance, and mutual funds. It was crucial for students to understand who is accountable to whom and what ethical standards those involved in accounting must adhere to, as this forms the foundation of accounting communication. Briloff constantly emphasized the importance of this issue to students. Therefore, the essence of accounting, which is communication, is deeply intertwined with ethics and thoroughly taught to students.

Briloff repeatedly asserts that while much of the semester is spent on extensive calculations, education in the ethical aspects of accounting is not something that can be acquired merely by memorizing accounting rules and calculation methods. It can only be achieved through persistent and continuous dialogue between students and teachers who are genuinely seeking to understand this challenge. However, what about the reality of the classes? It is doubtful that any of the seminars are engaging in meaningful discussions about the real problems we are currently facing, as they are all focused on mathematical operations. Briloff laments especially the current state of doctoral students, who are absorbed in arcane statistical calculations that have little relevance to the issues at hand.

It is easy to imagine how students would perceive Briloff's way of teaching. The class, which always began in a low, quiet voice, would have gradually transformed into Briloff's passionate and justice-driven tone as it delved into the lack of ethics in various accounting practices that are actually taking place. There may have been moments when he pounded the desk and directly expressed his anger to the students. It is not surprising that some graduates, captivated by his way of speaking, would share Briloff's values. It is likely that Mr. Dreyfus, who established the "Briloff Corporate Ethics Award," was one such student. He says, "Through this award, a path has been opened to further enhance the principles, goals, and values that Briloff did not cease to inspire in all of us." Briloff is also happy as an educator.

12 *Talk with Brilov*

Q: Abe, thank you very much for all your help with this series. Thanks to you, we have finally reached the conclusion. For this final segment, we would like to have an open discussion. Please answer a few questions.

Where is the accounting profession heading?

Q: The Financial Accounting Standards Board (FASB) seems to be facing political challenges again regarding accounting standard-setting. What are your thoughts on this?

A: The accounting profession in the U.S. is increasingly moving toward unprofessionalism and industrialization. The FASB, AICPA, and SEC, which are supposed to function as public oversight bodies, are failing to fulfill their responsibilities. Accounting is meant to ensure financial integrity and protect the less fortunate in our affluent society, but it is not meeting this role.

A similar transformation has occurred in the medical field. Doctors, once regarded as professionals, have now become part of the medical industry. While they are still tasked with protecting patients and society, their work has become increasingly commercialized, with massive financial flows from the government and patients. The same pattern is unfolding in the accounting profession.

Q: Recently, it was announced that Coopers & Lybrand and Price Waterhouse are merging. (Subsequently, KPMG and Ernst & Young have also decided to merge.) What impact do you think this will have on the accounting profession in the U.S.?

A: Giant accounting firms now employ tens of thousands of people, making it increasingly difficult to enforce professional codes of conduct across all levels. Decision-making at the top is disconnected from the realities of everyday audit work.

In many firms, management consulting has overtaken auditing as the dominant business activity. Audit work may appear prestigious, but in reality, it has become secondary. As the Big Eight shrank to the Big Five, and then the Big Four, these firms grew even larger. The concentration of power will inevitably pressure the FASB, AICPA, and SEC. If this trend continues, we may soon see giant accounting firms establishing offices

everywhere, much like fast-food chains, willing to audit anyone as long as they receive a fee.

I have been a long-standing critic of the Big Eight's expansion into management consulting, a stance I first articulated in my 1967 book, *The Effectiveness of Accounting Communication*. I will continue to oppose these firms as they stray from their fundamental responsibilities. As the Old Testament recounts, David, though not a warrior, stood up against Goliath—I, too, will continue to fight. Sure, I have bad eyesight, but I won't miss the "kryptonite" on my forehead. (Laughter)

Q: Japan is currently experiencing a severe recession following the burst of its economic bubble. You have referred to the U.S. as being in an "audit crisis," and now Japan seems to be facing a similar situation. What are your thoughts?

A: I have heard that Japanese accounting standards are looser than those in the U.S., leading to weaker auditor independence. This may be exacerbated by the close affiliations between auditors and the companies they review.

In Japan, even ordinary citizens—including housewives—invest in stocks and bonds. If a company collapses, millions of investors suffer. This makes the role of auditors even more critical in Japan.

Q: Given this, the issue of "accounting ethics" becomes crucial. How can we improve accounting ethics?

A: It's amusing that Japan is singled out for a lack of accounting ethics when the situation is similar in the U.S. The academic community should address this issue with serious intent, but instead, they are engaging in self-indulgent exercises.

University accounting education focuses too much on rote memorization of rules to pass the CPA exam rather than fostering a deeper understanding of ethical responsibilities. This needs urgent reform. I have been labeled a "howling dog" for my past critiques, but I remain committed to improving accounting ethics.

For Japanese Readers

Q: Let's shift the discussion to this series. The articles have aimed to present a complete picture of you—from January's "Brilov's Appearance," to February's "Brilov is Sued," and November's "Brilov's Writing Style." How do you feel about this project?

A: I have a Japanese friend in the U.S. who translates portions of *Business Accounting*, so I have a general idea of the content you have been publishing.

My writings and activities have been the subject of academic research before, but few have examined them from the unique perspective of this series. Interestingly, just this morning (October 7), a professor from Pennsylvania State University contacted me about organizing a lecture tied to the 25th anniversary of my book *Unaccountable Accounting* (1972). I expect to hear more details tomorrow.

This project has brought back many memories for me. As a Calvinist Jew, I believe in individual responsibility, which has been a guiding principle throughout my life. Additionally, my time with Professor Emanuel Sacks during my university years profoundly shaped my future.

Q: Japanese readers may be surprised to learn that, despite being legally blind, you continue to actively write and lecture. Would you be willing to share your thoughts on this?

A: I view my poor eyesight as a blessing from God. My vision deteriorated significantly around 1980, but by then, I had already absorbed a wealth of accounting knowledge. Now, I rely on that "stored charge" to continue my work.

My daughter reads books to me, and I draft manuscripts in large, nearly illegible handwriting. A certain Chinese woman deciphers them, listens to my corrections, and revises them five or six times before finalizing them.

I also enjoy mountain climbing. Though I cannot see the scenery, I can feel it.

Speaking of blindness, a 77-year-old accountant friend of mine from Baruch College, City University of New York, is also blind. He has a great sense of humor, an incredible memory, and delivers outstanding

presentations. Meeting him reinforced my belief in taking on challenges and never giving up. I consider him my role model.

As you can hear in my voice on the tape I sent you, I am doing well and am not lonely at all.

Q: Abe, thank you so much for your time. Take care!