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EPISTEMOLOGY IN

ACCOUNTING

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ABSTRACT

The aim of the study was to investigate different epistemological approaches to accounting in order to distill the most appropriate methods for the future. All methods of analysis available in either the social or the traditional sciences have been evidenced in accounting, thus there was no need to examine techniques outside the discipline.

This study examined and compared five approaches to theory construction and knowledge gathering in accounting as representative of the primary methods of epistemology in accounting. These were:-

rules and standard setting,  
convention derivation,  
induction and scientific analysis,  
normative-deductive, and  
weltanschauung.

Having defined the limits of the discipline, the study reviewed each approach analysing their strengths and weaknesses. Conclusions and future methodological prescriptions follow logically from the first sections but are normative in nature.

The results indicated that no one method could meet all of the requirements of the discipline, yet empirical research held the most promise for the future. Two further conclusions were made. Firstly, other methods of inquiry may be quite legitimate in certain cases and should be judged on what they offer. Secondly, accounting should now be viewed as a social institution, involving political and social factors in its developmental and theory construction processes as well as in accounting questions per se.

## INTRODUCTION

Accounting has developed over many thousands of years in a generally ad hoc manner. The discipline has, in the main, responded to pressures and demands from its environment in a relatively passive manner. The result of this type of growth has been the piecemeal development of conceptual issues and lack of a coherent set of rules and procedures. Those rules and procedures which have been developed tend to be problem specific and hence when complex requirements are made of these, or broad generalisations derived, anomalies and contradictions frequently occur.

*"Accounting practice has evolved to meet the needs of society as accountants have devised techniques and methods for performance of the tasks at hand. For this reason, accounting practice has been greatly influenced by tradition and expediency. Accountants have frequently relied on trial and error as a means to improving accounting practice ... the primary purpose of theory has been to serve practice with the result that practice has sometimes developed in advance of and without due consideration for good accounting theory."*<sup>1</sup>

Since the rules, procedures and structures which exist are the result of action to cope with past problems in a very practical manner, they provide inadequate guidance for coping in a dynamic interactive environment. Thus the problem specific approach to 'theory' formulation has resulted in a patchwork of conceptual ideas and relationships.

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(1) Imke, F.J., "Relationships in Accounting Theory", Accounting Review, April 1966, p. 318.

Many writers have expressed a desire for a more sound theoretical basis to accounting or, at least in the interim, for a series of conceptual areas covering different aspects of accounting. These views have been coupled with a call for a greater matching of theory and practice in a coherent, logical and complementary manner.<sup>2</sup>

*"Ideally, good accounting practice can be explained and justified by good accounting theory; but when tradition and expediency (rather than order and logic) influence the development of practice, unsound accounting practice may result."*<sup>3</sup>

On the same theme Ijiri says:-

*"Unfortunately, conventional accounting is a collection of many different principles and practices, which in some cases are mutually inconsistent."*<sup>4</sup>

Writers in the accounting theory area have been (and still are) plagued by the lack of a clear goal or target. Furthermore, research has been undertaken in a fragmented and compartmentalised manner, resulting not only in repetition but also in a lack of cohesion.<sup>5</sup>

There also appears to have been a demand for theories, per se, as opposed to theory formulation within a broad

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- (2) Sprague, C.E., as early as 1913 The Philosophy of Accounts (Ronald Press Company, New York, 1913) wrote 'as a branch of mathematical and classificatory science, the principles of accountancy may be determined by a priori reasoning and do not depend upon the customs and traditions which surround the art.' (p. iii).
  - (3) Imke, op cit, p. 318.
  - (4) Ijiri, Y., The Foundation of Accounting Measurement: A Mathematical Economic and Behavioural Inquiry, Prentice Hall, 1967, p. 88.
  - (5) This problem is seen in New Zealand at present where most Accounting Departments are independently pursuing sharemarket research.

conceptual framework.<sup>6</sup> Thus writers have been motivated by this demand to produce theories for their own sake rather than to advance the conceptual structure of accounting.

The problems may therefore be summarised as follows:-

- there has been a trend for theory to proceed from practice;
- theory development has taken place in a non-integrated manner;
- there has been a lack of clearly stated aims for accounting;
- theory production seems in some cases to have been for its own sake, rather than for the building of a more cohesive and articulated structure.

Hylton has summarised the first three problems when he says:-

*"Up to and including the present time, most accounting theory has evolved from the pragmatic approach ... that the sole test of truth, or soundness lies in practical results ... no control exists over the aims or desires of business ... there exists no usable criterion for testing either theory or application ... one difficulty with present accounting theory lies not in the existing differences of opinion, but in the lack of any sense of direction ..."*<sup>7</sup>

Although the nature of accounting theory has, in the past, been the subject of considerable controversy this debate has not been resolved. Therefore the question still

- 
- (6) See Watts, R.L. & Zimmerman, J.L., "The Demand and Supply of Accounting Theories: The Market for Excuses", Accounting Review, April 1979, pp 273-305.
- (7) Hylton, D.P., "Current Trends in Accounting Theory", Accounting Review, Jan 1962, pp 24-27.

remains as to the most appropriate form of future epistemological methodology.

### Discipline Parameters

Before addressing the question of theory formulation in accounting, the scope and activities of the discipline should be determined, since methodology will, of necessity, be constrained by the bounds of the discipline. Thus the question of what is actually encompassed by accounting (although, open to dispute) is of critical importance to the ensuing discussion.

The American Accounting Association (AAA) defined accounting as:-

*"... the process of identifying measuring and communicating economic information to permit informed judgments and decisions by users of the information."* <sup>8</sup>

This approach clearly defines accounting as a communication system and brings into consideration the users of the information and their uses of it. This definition moved much further than earlier attempts, which had been concerned primarily with such questions as what accountants do and classification/recording functions. The major criticism, however, of the A.A.A. definition is that it does not describe the place of accounting within the community, that is, the relationship between accounting and the various elements of society is avoided.

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(8) American Accounting Association, A Statement of Basic Accounting Theory, (A.A.A. Sarasota, 1966, p.1.)

The Accounting Principles Board (A.P.B.) subsequently added a vital new factor to the above definition when they said that accounting is:-

*"a service activity. Its function is to provide quantitative information, primarily financial in nature about economic entities that is intended to be useful in making economic decisions, in making reasoned choices among alternative courses of action."*<sup>9</sup>

The new element introduced here is that of accounting as a service activity, thus placing accounting within the context of society. The main criticism of the definition is the restriction of accounting information to 'quantitative information'. While it is true that accounting is largely concerned with quantitative information, there is now a move towards the inclusion, or at least discussion, of more qualitative information.<sup>10</sup>

Both these definitions tend to artificially restrict the boundaries of accounting and a more open-ended definition (one that provides opportunities and which is amenable to new ideas and views) would better serve the functions of providing information useful in making economic decisions. Thus the writer would suggest the following working definition of accounting as the basis for this paper:-

- (9) Accounting Principles Board Statements Number 4, Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprise, New York, AICPA, 1970, para 40.
- (10) Mathews, M.R., "New Areas in Accounting: Some Clarifying Comments", Occasional Paper No. 37, Faculty of Business, Massey University, 1981.

*"Accounting is a service function, that identifies, measures and communicates economic information to permit informed judgments by the users of that information, within the social, economic and political parameters of the community."*

Thus accounting is seen as a structure or subsystem within the greater system of society implying a new emphasis for the place of accounting i.e. accounting as a social institution.

### METHODOLOGY

This paper reviews the methods used in theory formulation in the past and evaluates their strengths and weaknesses. A strategy for accounting methodology in the future and evaluation criteria for the same is developed.

Five methodologies will be reviewed:-

- (a) The drawing up of accounting conventions which are essentially policies or guidelines for action. These conventions may be considered to be two steps removed from practice viz:-

Practice  $\leftrightarrow$  Rules  $\leftrightarrow$  Conventions  $\leftrightarrow$  Theory

- (b) The detailed prescription of rules for dealing with specific problems and cases.
- (c) The formulation of methods and principles based on the empirical examination of accounting problems.

- (d) A priori, deductively derived theory.
- (e) The weltanschauung<sup>10a</sup> view of accounting within the social context.

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<sup>10a</sup> Weltanschauung, meaning world view taken from a German philosophical perspective which was concerned with the nature of the Universe.