UNIFORMITY VS. FLEXIBILITY:
THE ACCOUNTING DILEMMA

by Dr. Khalifa Ali Dau *

In order for accounting data to be useful to their users, they have to permit comparison of alternatives. To achieve this goal, accounting data must be comparable. Should we have a uniform body of accounting principles and procedures in order to have comparable data? This is the problem that is dealt with in this paper.

UNIFORMITY

The uniformity approach is based on the idea that items are comparable if they are measured by the same method or rule. Adhering to one rule and not varying seems to be the essence of the uniformity approach. However, proponents of uniformity differ as to how strict the rule should be and how variable practice should be.

One view supports absolute uniformity. It may be illustrated by the following statement, which appeared in a brochure issued by a New York securities dealer a few years ago:

* Lecturer, Department of Accounting, Faculty of Economics and Commerce, University of Benghazi. Dr. Dau holds an M. A. S. from the University of Illinois, and a Ph. D. from Louisiana State University. He is the Director of the Economic and Business Research Center.
Uniform accounting practice is the answer to a security analyst’s prayer. What a joy to produce long spread sheets where each vertical column represents a different company and to compare each item of the balance sheet and earnings statement by merely running one’s finger across the line. To be able to come to the definite conclusion that the stock of this particular company represents truly the best value.1

A similar extreme statement holds that:

For each kind of transaction, there should be only one prescribed accounting treatment. Principles assuring this one treatment can be developed and enforced. Financial statements resulting from this approach can reveal one figure, described as net income for the year, which will represent the “true” income of a business.2

Another view would take into account the effect of circumstances. Proponents of this view say that uniformity in accounting means identical treatment except where circumstances differ.3

A similar approach is the one holding that all accounting should be subject to the same broad principles but that latitude should be allowed in the methods of applying these broad principles in practice. Selection of the methods to be used in individual situations would be left to the judgement of management, subject to review by auditors.4

Proponents of flexibility claim that the business environment is complex, and therefore, accounting should be flexible and diverse, not simple and meaningless. As a defense for uniformity, one might argue that even though it is true that the business
environment is complex, reporting noncomparable data will do nothing but increase the complexity of decisions for users. Another argument usually presented by proponents of uniformity is that the essence of all business transactions is the same and thus they should, principally, be treated in the same manner.

The Committee to Prepare a Statement of Basic Accounting theory stated its arguments for “uniformity of practice within and among entities” as follows:

Where various alternative methods of measuring an economic activity exist, it is important that the best available one be used uniformly within a firm, by different firms, and, to the extent practicable, by different industries. This uniformity refers to consistent classification and terminology as well as consistent measurement, and it requires precise meanings. This guideline is required in order to meet a basic need of managers, investors, and creditors to compare results and financial conditions of different segments of firms, different firms, and different industries ...

For example, in a period of rising prices use of the last-in, first-out inventory method results in reporting income that is lower than would be produced by certain other inventory methods; and indeed, LIFO has been widely adopted for that very purpose because of the consequent deferral, perhaps indefinitely, of a portion of the taxes on income. 5
FLEXIBILITY

There are diverse sets of generally accepted accounting principles. For many transaction there are two or more accounting alternatives. In most cases management can decide which alternative to use for each transaction. Different managements usually choose different alternatives. The result is that the reported accounting data of several firms, which represent a summary of what has been recorded, are not derived from the same set of accounting alternatives. Good or bad, this is what accountants have been doing since the Pacioli era. It should be noted, however, that the AICPA has been trying to limit this vast diversity. As a matter of fact, one of the main tasks the Institute assigned to the Accounting Principles Board was that of "narrowing the areas of difference and inconsistency in practice". The Board did make some progress in this direction. The new Financial Accounting Standards Board is expected to continue the struggle for this goal. Many competing accounting alternatives still exist, however, and management still has a vast choice.

Flexibility has some theoretical support. Proponents of diversity hold that accounting, like management, is a complex art which requires carefully considered exercise of judgement in development and application of principles. They believe that there simply is no universal truth built into any one principle of accounting and no simple universal way to operate a business in the vast complexities of our society. Accounting principles must be flexible enough to meet the demands of reality, thus permitting the adoption of appropriate methods that will make accounting relevant and responsive to the particular entity, rather than to some "nameless and faceless mass".7

Proponents of flexibility believe that even if we agree that uniformity is desirable, the cost of uniformity is too high.
Mr. Dudley E. Browne wrote:

One price accounting must pay for greater uniformity is less usefulness both to management and to the free enterprise system. There are also other prices. One is the inescapable price we always seem to pay for uniformity and conformity in any field - mediocrity... Allied to mediocrity is a third cost - loss of creativity...

The whole concept of freedom is opposed to uniformity and conformity. It is opposed to anything that suppresses individual effort, discourages creativity, and imposes rules from above, whether under the name of principles or any other authority.8

In his challenging empirical research project, Professor R. K. Mautz concludes that, "In stating and applying corporate financial reporting requirements minimum essential flexibility must be provided so that maximum effective comparability may remain a possibility.

A. Minimum essential flexibility may be defined as the absence of any constraint that would inhibit employment of that accounting or reporting treatment most responsive to the substance of the transactions, conditions, or events to be reported.

B. Maximum effective comparability results from applying that accounting or reporting treatment most responsive to the substance of the transactions, conditions, or events to be reported".9

Proponents of diversity also contend that consistency and disclosure will make the reported accounting data sufficiently comparable.10 Consistency, to them, means that a company must
apply the same accounting methods from year to year. Thus differences from year to year will cancel out. Disclosure means that the firm must explicitly report the particular set of accounting alternatives used to prepare the reported accounting data. The flexibility doctrine implies that consistency will make the accounting data for the same firm comparable from year to year, while disclosure will make accounting data for different firm comparable.

**PRODUCER ORIENTED VS. USER ORIENTED FLEXIBILITY**

Flexibility has been generally advocated from the point of view of the information producer: i.e., management and/or the accountant. That is, the producer is the best one to decide what accounting alternative to be used in each situation. He is the best because he knows the facts of the situation as he sees them, and interprets them. He perceives the facts of the situation, however, through his own frame of reference; i.e., his own decision-making model. Therefore, he would produce information that is relevant to his own model(s).

The problem is, however, that he is supposed to produce information that will be used by other users, whose decision models are not perfectly known to him. The latter decision models might be completely different from the information producer models.

Nobody knows for sure. Nevertheless, accounting practice, proponents of flexibility, and proponents of uniformity have been assuming that the decision models of the information producers are not completely different from those of the users. The validity of this assumption needs to be investigated. If it is proven, and this is very likely, that the two groups of models are different, then accounting practice should be reconsidered. Accounting information should be user-oriented information by either: (1) indentifying the users decision models and their information needs, or
(2) reporting all information deemed to be relevant by the users. The first alternative is theoretically appealing. Practically, however, it is very difficult, if not impossible, to apply. The other alternative, on the other hand, is not theoretically appealing. The information users may not know what is relevant for them. Furthermore, much information may hurt their decision-making process. This might be true, but it is hard to imagine that the situation will be worse than the present state of the art.

SUMMARY

In order for the accounting data to be useful for decision-making purposes, they should facilitate comparison; i.e., be comparable. Comparability of the accounting data is referred to in the accounting literature as "uniformity vs. flexibility" of accounting principles and/or alternatives. Proponents of uniformity believe that accounting data are comparable only if they were prepared according to the same principles and alternatives. On the other hand, proponents of flexibility believe that consistency and disclosure of the accounting methods used by each firm should make the reported accounting data comparable. Both approaches presume that the information producer is the best one to determine what alternatives to be used in each situation. This might be true if he knows the decision models of the information users. The fact is however that he does not know these models. Therefore, the information producer uses his own perception and decision model as a frame of reference. If the users' decision models are different from those of the producer's, and if these models cannot be explicitly identified, accountants should report all information deemed relevant by the users.
REFERENCES


4. Ibid. P. 678. (emphasis added).


