

# Vincent C. Ross Institute of Accounting Research

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To: Interested Colleagues

From: Nicholas Dopuch and Joshua Ronen

Re: Special Panel Discussion on the "State of Accounting/  
Auditing Research, Tuesday, August 13, 1991

About two years ago, a group of researchers--J. Demski, N. Dopuch, B. Lev, J. Ronen, G. Searfoss and S. Sunder--met in New York to discuss the state of accounting research. This was followed by a second meeting in New York last year during which the group heard suggestions for improving the relevance of accounting research from representatives of the FASB, the financial analysts community, managers and various government agencies. The product of these two meetings is the group's "Statement of the State of Accounting Research," a copy of which is enclosed.

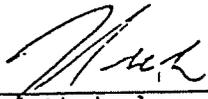
This Statement was sent to the Director of Research Committee of the AAA for the purpose of initiating some formal means of disseminating its contents for discussion and debate. That Committee recommended that a panel discussion of the Statement be scheduled at this year's AAA convention in Nashville.

We are writing to inform you that the panel discussion will be held from 4:00 p.m. to 5:30 p.m. on Tuesday, August 13, 1991 (meeting room to be announced), and to invite you to attend and take part in the discussion. The session will take place at the end of the

day which will allow more time for friendly, and no doubt spirited, debate. The panel members will be Baruch Lev, Robert Magee, Jim Ohlson, Ira Solomon and Richard West (Dean of the business school at NYU).

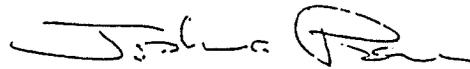
We hope you will plan to attend and we also ask that you pass this information on to your colleagues who would be interested in attending this session.

Sincerely,



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Nicholas Dopuch



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Joshua Ronen

# A STATEMENT ON THE STATE OF ACADEMIC ACCOUNTING

## I, The Problem

There is a widespread sense among accounting researchers and practitioners that academic accounting, particularly on the research level, currently faces a serious crisis. Following are some symptoms of this crisis:

1. Unlike many other professional disciplines, (e.g. finance, medicine, architecture), accounting research does not lead practice and/or policymaking. Indeed, it is difficult to recall one accounting research innovation in the last 20 or so years that has had a significant impact on the practice of accounting (having been adopted by CPA firms or by industry), or that meaningfully affected accounting standard-setting and securities' regulation. Audit sampling and human information processing in auditing research are exceptions that prove the rule. In fact, much accounting research (e.g., economic consequences of regulation) tends to significantly lag real-life developments.

2. Most academic research areas are characterized by cycles of significant innovations -- i.e., new ideas and concepts that periodically revolutionize the field, such as rational expectations in economics, and options models in finance. Such innovations in accounting research are practically non-existent. Indeed, information content studies in financial accounting and agency theory in managerial accounting have been imported from other disciplines. There do not appear to be any built-in regenerative forces in accounting research.

3. Despite considerable research effort, it does not seem that we are any closer

now than we were 20 - 30 years ago to addressing the fundamental issues in accounting, such as the optimal choice of accounting standards and the optimal structure of accounting institutions. This lack of progress is clearly manifested in accounting textbooks which are virtually no different today than those that were in use decades ago. Not surprisingly, the same is true for accounting instruction. There thus appears to be a general lack of progress in addressing fundamental accounting issues and in the instruction of accounting.

4. There appears to be no discernible demand for academic accountants or for accounting research by accounting firms (except in auditing), by industrial firms, or by regulators. A strong demand for academicians exists in most other professional disciplines, such as finance, computer science and the biotechnology industry. During the late 1970s and early 1980s, both the FASB and the SEC initiated a few research projects (e.g., on oil and gas and on inflation accounting). This demand for accounting research apparently subsided, despite the increasing complexity of the problems facing regulators (e.g., the FASB's financial instruments project). There appears to be a general lack of appreciation by our constituencies of accounting research. These constituencies are, of course, partly to blame for the lack of interest. But some of the fault also lies with us.

5. On the education front, in the last decade, the MBA student majoring in accounting has become an endangered species. Accounting is essentially a mere service area in graduate business schools, facing potentially diminished clout, budget support, and supply of Ph.D. candidates. While the low salaries paid by accounting firms to MBAs

is clearly an important factor in the disappearance of accounting majors in MBA programs, the lack of significant research and teaching innovations have also contributed to this troubling phenomenon. In some schools, deans are already questioning the justification of paying high compensation for accounting faculty who merely provide service courses. Indeed, the way accounting is currently taught does not provide "high-powered" (and high salaried) accounting researchers an advantage over broadly trained practitioners.

Thus, we seem to be witnessing a "market failure" phenomenon in academic accounting, particularly in research. Despite the serious weakening of demand for our product (by accounting and industrial firms, regulators, students), there are no self-correcting forces to provide inducements to change the nature and course of our research and teaching. What are some reasons for this "market failure?"

## II. The Reasons

There does not seem to be a single, dominating reason for the "market failure." Rather, a combination of reasons apparently led to the present unsatisfactory state of affairs. Following are some of our conjectures:

1. Accounting researchers apparently suffer from insecurity about their field of study, leading them to perturb fairly secure research paradigms (mostly those that have been accepted by economists) within an ever-narrowing circle of accounting academics isolated from the practice world. There is very little reward in the current academic system for experimentation and innovation that has potential for impacting practice.
2. Perhaps reinforcing this sense of insecurity is the relative weakness of entry-

level Ph.D.s in accounting and institutional knowledge. Such weakness in understanding one's own field can be maintained with impunity in accounting since, under existing incentives, thorough accounting knowledge is not needed for publishable research, and hence, promotion and tenure. The persistent use of old research paradigms and researchers' increasing ignorance of accounting institutional knowledge exacerbate the difficulties of communicating with our natural constituencies: accounting firms, corporations, government, etc.

3. Research funding and remuneration (mostly by accounting firms) is generally unrelated to the results and relevance of research. Again, an exception -- KPMG's Research Opportunities in Auditing -- proves the rule. This concerted funding with a clear objective contributed significantly to auditing research. In other accounting areas, however, research funds are disbursed independently of results. A much different situation exists in the sciences.

4. Increasingly more areas of research and curriculum have been surrendered to other disciplines. (Consider, for example, security analysis, the valuation of financial instruments, and other themes in corporate finance). In curriculum development, the domain of accounting seems to have been defined narrowly. We have not had much intellectual entrepreneurship in the field of accounting. Issues like mergers and acquisitions, leveraged buyouts, and corporate governance could just as well have been approached as issues in accounting/tax rather than in finance.

5. Reinforcing the above is a tendency for senior accounting academics to judge and reward the performance of juniors also on the basis of a narrow definition of what

constitutes academic accounting. This tends to discourage researchers from innovating in ways that would make our products more desirable and more in demand.

6. The regulation of financial accounting may be one of the reasons for the lack of interest of accounting practitioners in research. Much of the demand for financial accounting services presently stems from regulatory processes, i.e. the SEC, the FASB, the AICPA, and others. Contrast this with the finance industry which is much more responsive to market forces. There, the initiative comes from entrepreneurs who are alerted to market opportunities, whereas within the accounting industry, demands for new products are generated primarily as a result of the regulatory process.

### III. Agenda for Action

Objective: To encourage innovation, experimentation, and practical relevance in accounting research and instruction. To link more closely academic accounting with its constituencies, broadly defined.

Means:

(1) A systematic identification of issues and research questions which are of concern to our constituencies, broadly defined.

(2) Encouraging research on these issues and its integration in textbooks and instruction.

Specific Steps:

Short-Term:

(1) Organizing in the Fall of 1990 a Panel Discussion aimed at identifying a broad set of challenging, relevant research questions. The panel will consist of 12-15

participants, mostly representing our constituencies.

(2) The set of research questions compiled by the panel will be distributed to seasoned researchers who will be asked to develop detailed research proposals. A "proposals conference" will then be held close to the AAA Convention in 1991. The proceedings of this conference will be published and widely disseminated among academics.

Long-Term:

(1) Organizing periodic conferences dedicated to innovative and relevant research work, and publishing the proceedings of these conferences.

(2) Engaging in periodic roundtable sessions with members of the accounting profession and industry to identify research worthy issues of relevance for the accounting profession and industry.

(3) Developing proposals for evaluation criteria and performance measures for the tenure and promotion decisions of accounting academics in ways that would align incentives with the objective of encouraging innovation, relevance, and a more vital dialogue with our constituencies.

(4) Developing proposals that would address ways to interest our constituencies in supporting and encouraging relevant and innovative accounting research.

(5) Studying in detail the causes and possible remedies of the lack of interest by business students in accounting majors.