Chapter two

STEWARDSHIP FUNCTION OF ACCOUNTING
The concept of stewardship: its origin and relation to accounting:

'Stewardship function' which has been included in the objective of accounting by a committee of the American Accounting Association (AAA), refers to "maintaining and reporting on the custodianship of resources". Literally, stewardship refers to the efficient discharge of custodianship of resources and the execution of plans for conserving and consuming them. In accounting, stewardship refers to a functional system of record keeping that provides the owners of wealth with a means of safeguarding it from theft or embezzlement. The concept of stewardship thus found to be originated in the possession of wealth and the employment of servants who are called 'stewards' today, for its proper maintenance. The wealthy men, in all ages, have been found to employ stewards to manage their property. These stewards rendered an account periodically of their stewardship. The stewardship concept has been found in use with the dawn of recorded history and intended to serve the limited purpose of the time i.e.; to keep accurate records of acquisitions.

1. AAA; Report of the Committee on the Objectives of Accounting, 1966, pp.4-5.
and outgoings, both in kinds and currency. It was also intended that stewardship report will help in the detection of any loss due to dishonesty or negligency on the part of the stewards either employed or held as slaves. Stewards were traditionally employed as managers whose status usually varied from that of slaves in antiquity to that of freeman in Roman period and freeman in the middle ages. In all ages, the incumbent upon them was the obligation to keep accounts for the master and to make periodic reports to discharge of their stewardship. More precisely, stewardship concept had its origin in property rights - the right to possess, the right to use and others related to the same. Right of possession, right of use or any other right is derived from ownership of property which has to be acquired by some legitimate means among a large number of contestants. It naturally made people feel about the limitations in the supply of resources and warranted judicious utilization of them. But people, until medieval period, gave little consideration to this idea of limitation in the supply of resources. It is probably, from this time, not the entire but the wealthy people became conscious of the reckless or whimsical use of resources. Alternate uses of resources from the point of view of benefit to individual as well as

society have been found to be a matter of constant search. Since reckless use of anything limited in supply can by no means be warranted, some sort of accounting was essential for imparting a discipline in its use. Whenever accounting, in the beginning, had not been found to be possible by owners of the resources themselves, a system developed in the process of accountability. Its application was separately recognized as involved in stewardship responsibility pressed for the pursuit of the immediate owner's interest and for the attainment of social welfare.

Historically, the concept of stewardship had its foundation on a strong religious philosophy, particularly related to Christianity. It is based on a belief that man is the steward of God for the consumption and administration of all resources. In the course of this consumption and administration, man should obviously have to possess the property. Without possession one can not possibly use the property. But such a possession enjoyed by one individual evidently denies the same to another. Thus one uses the property in exclusion of others though all properties and resources are created and given by God for common use. Thus,

it is believed that irrespective of ownership rights all resources should be used not only for owner's interest but also for the interest of the whole society. Stewardship thus could be seen inherent in the enjoyment of the right of the ownership of property because of the social responsibility with regard to the use of such property either directly by the said owner or through an agent. Book keeping and later accounting gradually evolved to help proper discharge of such responsibility bestowed upon property. Stewardship accounting, therefore, could be seen to reflect the socio-economic ethos of a society which was concerned with the control of personal wealth and proper role of master and servant in the exercise of that control.

The idea of protection and the concept of verification of stock:

It will, possibly, not too much to presume that personal stewardship i.e.; keeping the records of one's own resources oneself, has been in practice since the day property

right and ownership was recognized. This practice lead to the growth of a concept in a more complex frame of social relationship, particularly relationship between the employer and the steward. During the medieval period, the concept of stewardship had been widely practised under the Feudal system or Manorial system. Employment of agent for the administration of the most important piece of inheritance or acquisition or both i.e., estate or landed property was seen during this period as organized by the Feudal Lords. Feudal Lords, at that time, operated under a system of land ownership and administration, known in the history as 'Feudalism'. Feudalism upheld a system encompassing a group of nobles of a distinct hierarchy with the King at the apex, on the one hand, and thus establishing a chain of relationship with a definite understanding based on rights and obligations on the other. Under this system the power to use land flew downward to the vassals and obligation to pay a price in exchange went upward to the king. Based on this political and land system, Clough and Cole described the ownership to be essentially

amounting to stewardship itself as associated with a responsibility to fulfill the obligations to the overlords. Wealth and resources, for the sake of ownership interest, necessitated full protection against theft, embezzlement or misuse. It was essential both from owner's point of view as well as the society's. The owners of the resources were naturally found to be content with the satisfactory verification of stock in respect of cash, inventories, real assets, debtors, creditors, and so on. Such verification would evidently ensure protection of resources i.e., safe keeping and facilitating in the discharge of obligations between parties. Written records of transactions, as obtained under what we are calling book keeping today appeared from such a background and had been presumably maintained throughout the medieval period to help, particularly, verification of stock or protection of resources. Glastrier and Underdown\(^{11}\) also inferred that accounting as a science originated in the need to record possessions and later on transactions relating to them as a means of safeguarding the interest of the owners of wealth and preventing any loss through theft or embezzlement. The objective of recording had been limited to verification of stock only for which the practice had been content with recording the changes in the stock of resources and the flows over time leading to it. Accounting thus, in

its origin, was meant to keep a watch over resources and their disposition, and specially of changes in those resources through time. It probably, as observed by F.S. Bray, started as a means of taking stock of changes in possessions, which apart from mere transfers of wealth, were later revealed as difference between income and spending. Any wilful effort for their increase or decrease in totality by way of profit or anything else had been unknown till that time. Such records of transactions, specially in the case of debtors and creditors served as evidence in the settlement of disputes either in the law courts or across the negotiation table. The law of inheritance, as already mentioned, also gave rise to a demand of records as an aide to the discharge of legal problems associated with property and its inheritance. Thus protection of resources seems to have been the principal objective of record keeping from the very beginning. During the medieval period, most of the feudal and manorial estates and houses had been found to be particularly concerned about this objective of account keeping. A good number of references could be made to the organization of old manor's house and estate during fifteenth and sixteenth century where work places had been identified as recording centres and the whole house or estate had been divided according to such recording centres.

Proper records in all those work areas would have helped tracing responsibilities with regard to the functioning of the estate or house. 14

The idea of accountability and the process of charge and discharge in accounting:

The protection objective was not found predominant in the practice of accounting throughout the ancient and medieval period only. With the passage of time that led to so many additions to the list of objectives of accounting, the protection objective did not cease to be primary even in modern times. Again from a very simple case of self custodianship, growth in accounting records had to make room for agency custodianship. In other words, accounting came to be signified by accountability that devolved, as already stated, originally on the owner himself but ultimately shifted to someone else, as agent. That means, agents had been found to come forward to assist the owners in record keeping as well as in the exercise of protection of resources in response to accountability. In the medieval period, those agents, as mentioned in the past, were called 'stewards', * and the job

* Literally, steward designates one, who manages an estate on behalf of the owner. 15

to be accomplished or responsibility borne by those agents was known as stewardship. Stewardship responsibility evidently required, by way of discharging the obligation or vindicating accountability, preparation of periodical reports based on a summary of the records of various transactions. It was in these reports that the protective functions of record keeping moved towards a new era of further expansion for the cause of accountability with regard to the same resources. The said accountability would obviously mean in addition to looking after protection of the resources, supplying a satisfactory explanation through accounts of how the resources had been obtained and disposed of. Throughout the medieval period, precisely upto Paciolo's time, these aspects of accountability had been adhered to according only to the personal fancy or desire of the owner concerned. In most cases the objectives remained confined to what might have been called the natural aims of self accounting. There could be found various types of accounts and records that reveal holding and use of wealth in the medieval history of Europe. After the Norman Conquest (1066), properties in England, under the feudal system, were held in trust by the stewards. Record keeping at that time had been designed with the principal purpose of keeping the owner informed of the discharge of these responsibilities (maintenance and up-keeping of feudal estates and households) and of their periodic estimations. In the royal finance this
gave rise to the Tally-stick method of recording part remittances from tax collections. In the case of the management of individual manors, it gave rise to a system of 'charge and discharge account' by which stewards of the lords of the manor used to report upon their activities. The steward's statement had been plainly the descriptive report of an agent, not a statement of indebtedness and ownership, as found in today's financial statements. This type of statement had not been a personal account because the stewards would not owe the lord of the manor like other creditor. Neither had it been a receipt and disbursement account nor a calculation of gain or loss. It was simply a well organized report upon the agent's responsibilities with regard to custodianship of resources placed at their disposal, and the state of their accountability with regard to their treatment in accordance with the mandates of the owners. In the absence of any wilful effort for increase or decrease, ancient wealth had not been purposely tried to be productive and as such the stewards had usually been called upon to keep accurate records only of where the resources came from and went to, and subsequently who owned them and to whom they were owed.

The growth of the idea of capital and profit:

Record keeping with a very limited objective prevailed till the resources were started to be exchanged against each other through an active process of trading. In other words, wealth, under the pressure of an extensive and profitable commerce, entered into a new era of productivity after being employed as capital. With the introduction of the employment of capital in productive ventures, i.e., reproduction, recording function had been extended to a more complex accounting function with dual responsibility of maintaining custodianship of resources and keeping people informed about the changes or the growth of such resources. Though there could be found scattered evidences of venture accounting revealing its results, the medieval history provides to enormous extant examples mainly of charge and discharge accounts of the stewards regarding their custodianship or accountability. The organization of the Royal Exchequer in Great Britain (1100-1135), however, with the objective of administering and protecting royal resources probably, prompted for the first time, systematic accounts keeping. The basis of accounting thus had its start with royal revenues and other receipts placed at the charge of the Royal Treasurer who in turn discharged himself of his stewardship responsibilities.

through a great pipe Roll in which all the issues and authorised expenditure and the balance were clearly mentioned. The beneficial influence exerted on the advancement of initial accounting by the elaborate system of accounts of the royal finance employed at the exchequers in Great Britain must have been great and far reaching. The organization of exchequer was not only a reform in the management of royal finance, but it also gave an example of a mode of keeping accounts which was gradually adopted by individuals and great families of Great Britain in the management of their estates. Royal wealth, in most cases, originated in tributes and taxes and exhausted themselves by consumption and display of wealth. Investment in gainful enterprises had not till then, been started. It was in this period, a well organized form of account in the name of 'Charge and discharge' account was found to develop in the estates of England which dated as far back as the early thirteenth century. Protective objective of ancient accounting were found to be achieved well through this particularly organised accounts. It is in these accounts,


the stewards earnestly sought to maintain an equilibrium between the charges and discharges concerning wealth and they, from a sense of sheer practical expediency, sought to make a segregation of entries in respect of transactions that made a person debtor from those that made him creditor. Reference could be made of such accounts of the city of Edinburgh for the year 1552-1553, the accounts of the treasurer of Glassgow for the year 1573-74, the accounts of the merchant house of Glassgow for the year 1660-61. Considerable improvements had been shown in each of the succeeding accounts with regard to forms, presentation and other aspects. But the objective of stewardship, probably, remained unchanged throughout this long period.

By the beginning of the eighteenth century, the accounts had been found to be much improved in which duality of entry became a feature that led to an equilibrium of totals in every occurrence as well as in totality. Paciolo's treatise of double entry system, as had already been well established in the late fifteenth century, induced significantly the objectives of charge and discharge accounts being further improved. Paciolo's treatise had been sought to give a framework of accounting rules to enable them to keep all accounts

and books in an orderly manner. In this treatise, it has been made possible the extension of the personal account keeping to suit the impersonal aspects of mercantile affairs and sought to establish that book keeping possesses a characteristic methodology* of its own.23 The true objective of book keeping, in its real sense, which has been expounded in Paciolo's treatise, lied far deeper. It did not end in a mere incidental test of mechanical accuracy of records that, on the surface, appeared to depend on a duality process. The transformation of idle resources into productive capital and the development of systematized book keeping during the fourteenth and the fifteenth century in dealing with the same, prompted a new consciousness among the owners of wealth. This consciousness resulted in, among other things, a rise in the interest for identifying and measuring financial relationship with each and every party connected through equivalent exchanges. Book keeping upto fifteenth century would reflect merely the proprietary requirement of identification and

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* The term Methodology/defined in Webster's dictionary as 'a body of methods, rules, and postulates employed by a discipline; a particular procedure or set of procedures'.

intimation of changes in relation to each transaction. Yet, such book keeping resulted in greater emphasis paid to accountability, which actually amounted to the judgement made of one's own actions as one shared in common with other men. Such an approach made the owner of wealth accountable to his own conscience because he was the sole judge of whether his performance was meritorious. 

Modern civilization possibly had its beginning with each individual to constitute a separate unit of economic activities by himself. There was no problem of distribution and the choice of consumption was limited to his nature and ability of production. With the passage of time, the individual units were replaced by household units and later on a social-economic unit emerged out of them. It naturally required the transformation of idle resources into capital by the effort of a single or a number of groups of individuals. As a result, development of numerous factors of production set in and distribution in a constantly changing social environment emerged as a problem. The medieval purpose of the employment of capital and credit changed from mere consumption or display to gainful operations in satisfaction of newly felt wants by collecting goods from distant sources. The ideas of earning

profit through economic activities by creating additional capital and the ideas of maintaining old productive capital had been first heard during those good old days. These ideas naturally created a fertile soil for more systematizing book keeping records. The owners of wealth had grown to be merchants and their activities of consumption and display had been extended to trading ventures through economic exchanges. The development of economic operations created a new environment and as such broadened the scope of record keeping. Before the advent of trading and merchandising, the idea of capital, profit, growth etc. did not, on reasonable grounds, have any specific import. It is not only the accounts of household but also those of manors of feudal lords maintained by stewards that suffered from these limitations. Thus the record keeping that had so far been maintained for the efficient discharge of mere custodianship of household ownership necessitated expansion to encompass records of proprietorship of economic enterprises. It may, however, be presumed that by an evolutionary process, the household unit judiciously grew into the business enterprise, though of a very simple form of organization in the beginning, for dealing with the manipulation of those social resources commonly called economic goods.28 Household ownership thus transformed into enterprise proprietorship. Though the two

are completely separated now, the old forms of their existing together still continues with small farmers, craftsmen, etc.

The idea of stewardship equilibrium:

In its origin commercial endeavour would have ended in a single terminable venture. In case of a single venture, the responsibility was obviously shouldered by an individual. Otherwise it was joint. The record keeping of those days were merely agency book keeping. It was adopted to enable an agent or steward (the owner being the steward of his own business) to report upon the activities of the ventures with regard to the stewardship responsibilities for and on behalf of himself. As the volume of trade expanded rapidly, individual merchant found it hard and at times impossible to supply capital needed to undertake big ventures and to bear the risk involved in it. The gradual expansion of trading ventures attracted groups of individuals to form joint enterprises and to distribute the risks in operating the trading ventures. This new development in the formation of economic units brought accounting to expand further to deal with newer problems. Stewardship responsibility had, along the line of development, been widened and reached to individuals in groups rather than in oneself. In this period Paciolo's treatise of double entry book keeping helped tremendously in the organization of commerce and trade.
While abridging the German historian Sombart's doctrine, Enthoven attributed to double entry book keeping as exerting a major influence on past economic development. He stressed that it released, activated and stimulated the realistic pursuit of profit by the employment of capital. Development of proprietorship and other forms of enterprises thus happened to be the outcome of a continuously going economic operations in a growing capitalistic economy. Quoting Sombart, Enthoven claimed that, "one can scarcely conceived of capitalism without double entry book keeping."

Paciolo's contribution was not limited only to securing the equality of debit and credit that resulted in an equilibrium of balances. It also significantly exhibited the mechanism of the proprietor's capital account and its relation to nominal and other accounts. "Paciolo" as inferred by Littleton, "does not theorize about proprietorship but throughout he shows a clear consciousness of that element, it underlies every mention of 'capital', 'profit and loss', 'mercantile expenses' and every intimation of their relations". The progress or growth of the business and

of the position of capital must have been reflected through these relations. Though closing of books was not an exception in medieval records, capital accounts were maintained to show its increases or decreases with every venture or ventures. Capital accounts, very possibly, considered significant to reflect financial resources as compared with financial obligations. As the state of an excess of resources over obligations made for a financial affluence, an excess of obligations over resources pointed to a situation opposite to it. Record Keeping, up to that stage, possibly stood for such comparison of resources as against obligations by way simply of displaying a stewardship equilibrium.

Paciolo's exposition helped to raise a feeling of consciousness of that dual aspect always present in every financial occurrence and helped merchants and outsiders to restore their confidence in business relations.

Accounting must have begun, in its true sense, at such a moment when an outsider first acquired an interest in a business carried on by a single; or a group of individuals and the business also first accepted a responsibility to the said outsider. Business itself raised its identity to a

32. Dohr, J.L; On the understanding of accounting, The Journal of Accountancy, March, 1941, PP.200-05
separate entity, though not initially as a legal one except
in case of a company developed later on. Thus some disjointed
transactions acquired the status of pulsating as a being. The
enterprise, in course of time, had also been entrusted by the
counters with the responsibility of utilising gainfully some
of their resources and creating some of their welfare.34 The
nature of business and its responsibilities changed through
an evolutionary process constantly and made ways for the
continuing ventures as a single being in place of splitting
it into a number of repeated terminable ventures. Accounting
also had to change and evolve in order to continue to meet the
new challenges which resulted through those business changes.
When continuing ventures replaced single ventures and occasional
agreements, the recording problem also became more and more
complicated. It passed from irregular reporting by an agent to
a continuing process of the same as required in case of invest-
ment of capital variously employed in a permanent way for which
the said reporting had got to be periodically summarised.35
Thus a form of cash to cash accounting had to be replaced by a
'periodical one' that necessitated recognition of accruals and
valuation of stocks and resources left. The other most
important development that occurred simultaneously with this

34: Ladd, D.R; Contemporary Corporate Accounting, Illinois,
change was that 'time', and not the 'venture', turned to be the criterion for the recognition of profit. It was realized that by itself, the amount of profit (loss) is meaningless unless it is measured in relation to the time cycle of capital movement. With this development, the objective of bookkeeping moved ahead from 'to account for wealth' towards 'to account for invested capital'. In case of a venture, the rate of profit is expressed as $\frac{S - C}{C} = \frac{S}{C} - 1$ (where $S$ stands for sale and $C$ for cost), whereas the said rate in case of periodical profit of a continuing concern, when deduced in the same way, produces a different equation. Thus, profitability is given by $\frac{TS - T \cdot C}{C} = T (\frac{S}{C} - 1)$, where $T$ is the number of times the capital turnover ratio is enhanced. In this case costs in totality turned to be capital, which in case of determining profitability plays the most vital role. Rate of profit in case of a continuing venture is significantly influenced by the number of times the capital turnover ratio is increased.

The Concept of Proprietorship in Accounting:

In the midst of expanded business environment, bookkeeping had been conceived to grow into a comprehensive system, step by step, and acquired the potentials of showing the effects of changes upon accumulated wealth in a systematic manner. A.C. Littleton's attempt of defining bookkeeping could well be related to this stage of development which enriched the
foundation of book keeping for further progress.

"Book keeping" in the description of Littleton, "is a quasi-statistical method of recording the sequence of conversion through which various forms of property are passed in the effort to produce a proprietary profit".36

Paciolo's description of capital account (capital, profit and loss, expenses, etc.) would also bear a semblance of proprietorship account. Proprietor, in such accounts, in respect of both ownership of resources and obligations to outsiders would figure in every transaction and charges and discharges would have accordingly been made in the proprietor's account. Proprietorship thus, could be seen to stem from the need of maintaining systematic accounts and acted as the central pivot around which that need gradually moved. In the process of evolution and from the background need of the formation of a coherent scheme of keeping interrelated accounts, with the proprietorship capital at the centre, the expansion of account keeping was made possible to step into systematic book keeping. An enterprise thus has been viewed as the proprietor's investment and all the assets and liabilities was owned and obliged by the proprietor. Net income was considered to be the increment

to the proprietor's stock. Chen Rosta\textsuperscript{37} termed the proprietorship as essentially one of classical stewardship responsibility.

The transformation of stagnant wealth of antiquity into commercial capital, the appearance of proprietorship and the evolution of double entry bookkeeping system even though seemed to have come independently, all the three were destined to the same goal i.e., proper protection and maintenance of wealth. As the society progressed, all those antecedents of modern civilization as well as of accounting, were found to be effectively coordinated to serve the purpose of the time. More precisely, all efforts were directed towards effective utilization of resources. Ownership and proprietorship, at this juncture, began to have been identified with a distinct separate unit, which ultimately evolved into the concept of separate enterprise entity. Such an evolution necessitated better and better accounting. In the face of constantly changing circumstances double entry system of bookkeeping transformed into a very utilitarian technology.\textsuperscript{38}

Book Keeping procedures were much formalized and resolved into

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\textsuperscript{37} Rosta, Chen; Op.Cit., p.537. \\
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a body of rules, in course of time, to fit with the circumstances. The subsequent steady developments in the methodology of book keeping produced comprehensive ledger books as the primary step for the development of balance sheet (financial statement) in the long run. Financial statements also were required to show the state of enterprise resources and obligations as at the end of each accounting period. In the process of evolution, refinement and development, the double entry system had been prepared, bit by bit, to set for general acceptance to the commercial world. Specific rules to suit the prevailing circumstances were framed, newer and newer rules were evolved to replace the old ones that had lost its importance in a changing environment. Business transactions, value exchanges, price events, etc. were precisely identified to be the basic elements of book keeping. Recording, classifying and analyzing the financial effects of these elements relating to an enterprise had been conceived of as being the primary objective of accounting. Long drawn experience in this matter resulted in a well defined methodology of accounting to obtain completeness of records as well as a means of testing the accuracy of the same. All these developments in the surrounding environment caused, double entry book keeping to sound as a system of recording financial changes which are of interest to proprietors according to a certain technique which result in
a convenient and arithmetically accurate summary of enterprise data. \textsuperscript{39} Quoting A.C. Littleton, accounting or "book keeping" thus can be defined as

\begin{quote}
"a process of recording and classifying financial data in a systematic manner for the purpose of showing the effects of value exchange upon wealth\textsuperscript{.} \textsuperscript{40}
\end{quote}

Though the word theory could not be heard in early eighteenth century, a few of the contemporary writers on book keeping, have been found to seek logic and reasonableness in all acts of record keeping as the foundation of book keeping methodology. Their earnest search led them to consider proprietorship as the keystone for initiating and conducting all business activities and that inevitably led to an equilibrium of the complete set of accounts. Reference could be made to the eighteenth century Scotch writer Malcolm\textsuperscript{41}(1718) who emphasized the equilibrium of proprietor's capital and its constituent parts. In author's interesting language, it goes,

\begin{quote}
"the stock you are to look upon as the root, from which all the other accounts in the book
\end{quote}

\textsuperscript{39} Littleton, A.C; Op.Cit., p.159.
\textsuperscript{40} Ibid, p.160.
\textsuperscript{41} Malcolm, A; A new treatise of arithmetic and book keeping, (Edinburgh), 1718, pp.132-33, quoted in Littleton, A.C. Ibid. p.166.
do flow, for whether there be increase
or decrease or equality by the various
changing of somethings for others, it is
the capital stock that is affected, and
either raised or diminished in value or
simply changed in its constituent parts.

From the above extract it can be concluded that,
right from the eighteenth century, the idea of exercising
through transactions an opposite but reciprocal effect upon
each other was recognised as a result of which a systematic
control of the one over the other had been largely in practice.
This led to the logic of the double entry system of book keeping
that each transaction has its origin in an exchange of equal
values and has its effects upon capital as a whole as well
as its constituent parts. Accordingly, accounting objective
had been rightly conceived to be the finding out of the
individual effect of each of these transactions and also of the
combined effect of all of them on the financial position of the
business. That means the component parts of property employed
in trade and business are in a state of continual transformation
and change. But whatever variations they undergo, and whether
the whole capital increases, diminishes or remains stationary,
it is evident that it must constantly be equal to the sum total
of all its parts. 42 Though an undeniable progress could be

42 Cronholm, F.W. Double entry by single, London, 1818, in
traced in matters of book keeping, all would possibly agree that nothing worthy of the name 'theory', as mentioned earlier, existed in the field of accounting literature prior to 1800. Peragallo in this respect comments, "no theory of accounting was devised from the period of Paciolo down to the opening of the nineteenth century. Suggestions of theory appear here and there, but not the extent necessary to place accounting on a systematic basis".

**Equilibrium and Proprietorship**

In the history of book keeping and accounting, nineteenth century had been the most eventful period both in terms of growth and achievements. By the beginning of the century, the principle of equilibrium of proprietorship and its constituent parts had been firmly established and as such the purpose of book keeping was well recognized in terms of this fundamental principle. "The purpose of book keeping", as described by Cronhelm in 1818, "as a record of property, is to show the owner at all times the value of his whole capital and of every part of it". There the author earnestly tried to uphold the prestige of accounting as a discipline by drawing the equality principle in line with the primary axioms of exact sciences.

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that the whole is continually equal to the sum of its parts. In an attempt of formulating theory of book keeping, Cronhelm defined book keeping as

"the art of recording property so as to show all the times the value of the whole capital and its component parts."

This attempt pioneered the foundation of book keeping theory with the objective of emphasizing on property, recording and equivalence and widened the scope of formulating specific rules for avoiding reliance on rules of thumb. The wide range of book keeping activities had subsequently been so systematized that by the first quarter of the nineteenth century it was skilfully symbolized into a form of equation or identity, obviously keeping proprietorship at the center. Thus, Cronhelm's equation of book keeping i.e.,

Positive property - Negative property = Proprietor's Stock, possibly might have come first in the history of accounting. It has been provided that any increase in positive property results in an increment of proprietor's stock and vice versa. In Cronhelm's explanation negative property originated through the introduction of credit into commerce and such other actions that caused any obligation over property. This equation

46. Ibid. p.169.
had further been expanded by Thomas Jones in quite easy and specific accounting term. In his explanation the modern terms of Asset and Liabilities had been used, for positive properties and negative properties respectively and proprietor's stock had been replaced by Proprietorship. With identical results Jones's equation would read

\[ \text{Assets} - \text{Liabilities} = \text{Proprietorship}. \]

At the beginning, proprietorship would consist of proprietor's investments and plus and minus profit and loss realized and retained since beginning. Proprietorship thus consists of the entire beneficial interest of a holder of a set of assets in those assets. Such modern items as 'prepaid expenses', 'accrued liabilities', etc. had not been used. During the first half of the nineteenth century proprietorship concept had been raised to a fundamental theory said to be "Proprietorship Theory" of bookkeeping and much of the discussion had been centered around the area of proprietorship and profit. Much of interest had been shown in the legal relationships, i.e., ownership and debts. No distinction was yet been made between losses and expenses and as such both had been deducted from proprietorship as negative property. Book Keeping,

\[ \text{Assets} - \text{Liabilities} = \text{Proprietorship}. \]


specially double entry system of bookkeeping was being sought in keeping accounts of changes in proprietorship in a manner that could produce, as already said, equilibrium of the whole property and all of its constituent parts. Thus bookkeeping under the proprietary notion had been conceived as an accounting meant for the proprietor for his own property in total and also in fragments. Referring to a German writer (G.D. Augsburg, 1872), Littleton\textsuperscript{49} termed the concept of accounting for proprietorship, in a sense, to be stewardship. The author's proposition was based on the thesis that the capital account (the account for the investment) stands as creditor opposite to the positive property (asset) and as debtor opposite to the negative property (liability). The whole system of bookkeeping thus precisely designated as "property account" which merely represents the discharge of only stewardship. William\textsuperscript{50} Paton also lauded the significance of proprietary notion in the evolution of accounting who, during the first quarter of this century wrote, "the accounts are kept by the employees of the business enterprise and consequently from the standpoint and in the interest of the private owners and that the functions of accounting and explanations of its principles and procedures must be stated in terms of the needs and purposes of the owners."


\textsuperscript{50} Paton, W.A.; Accounting Theory, New York, Ronald Press Co., 1922, p.16.
Equation Approach:

During the last quarter of the nineteenth century, equation approach, as already mentioned, of explaining the fundamentals of double entry gained enormous popularity in the commercial world. The result of every transaction had been sought to be finally analyzed as soon as it was completed in terms of equilibrium. The introduction of equation made transaction analysis so systematized that the fundamental nature of the double entry bookkeeping was deductively reduced to simple increase or decrease or in other words, formal debit and credit. Such an approach based on logic and reasoning had been largely discussed and enriched in subsequent periods of the nineteenth century. While advocating the application of the equation approach in bookkeeping practice, C.E. Sprague 51 gracefully argued that the fundamental characteristics of double entry bookkeeping i.e., equilibrium and proprietorship had been best exhibited through an equation. Sprague in his interesting article "philosophy of Accounts" in 1880 significantly attributed accounting method with Cronhelm's contentions and went on saying that "if nothing is owed to others then the proprietorship must be equal to the value of all possessions". The author, in his explanation, however, used different notations and skillfully sought to extend the boundaries of the equation to

encompass both liabilities of the enterprise as well as liabilities to the enterprise. In author's language, the equation stands,

\[ H - T = X = 0 \]

\((H = \text{what I have}, \ T = \text{what I trust and} \ X = \text{what I am worth}, \ O = \text{what I owe})\)

The equation has been quite different from that of Cronheim's in form and components, but satisfies the same fundamental objective of equilibrium. Negative properties of the equilibrium had been shown through a transposition to the opposite side instead of subtracting them from the positive properties alone. In this equation, equilibrium has been maintained through increase and decrease in the components of the equation with every change in value caused by a transaction. More precisely, all changes in the values of the whole property and its constituent parts have been expertly reflected through the process of debit and credit alone. This led the author to propose, in the late nineteenth century, a complete rule for Balance Sheet and described the elements of the value at rest in a balance sheet format. This was:

<table>
<thead>
<tr>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have</td>
<td>Owe</td>
</tr>
<tr>
<td>Trust</td>
<td>Worth</td>
</tr>
</tbody>
</table>

Thus, though preparation of balance sheet had not been in
practice at that time, it would be too much to presume that the concept was entirely unknown at that time. Yet, almost all of the ancient efforts could be seen intended to compute the state of present proprietorship. Sprague's deductive reasoning made book keeping much formalized that led to a complete rule for resolving each business occurrence into its debit and credit elements along with shifting of values. The process of systematic journalizing possibly originated following Sprague's concise description as preparatory to recording the transaction in the technical book keeping form. His explanation had undoubtedly been an extended step and led book keeping and accounting towards definite progress.

The advent of the idea of separate business entity:

Today, it is possibly beyond controversy to say that as concepts of society change, so do concepts of accounting. Newer methods were evolved and tried by the businessmen in the solution of their specific recording problems of changing times. It is true that not all of these new techniques could stand the searching analysis of the following generations, nor were all of them rejected. Some were rejected, some continued and others were modified for the system to step into further progress.

By the middle of the nineteenth century, commercial world witnessed the most remarkable change in the history of economic and business activities. It was with the Industrial Revolution that came into full bloom in such countries as England, Germany, United States, etc. Industrial revolution caused a reawakening in the field of accounting. Though the proprietorship theory marked to be a constant source of influence for guiding the accountants in the development of their ideas up to the beginning of the present century, some new concepts emerged at about the same time. Business entity concept would rank fundamental among them which appeared at about the middle of the preceding century in the environment of rapid industrial growth due to the said industrial revolution. It was found to be quite sharply accepted. The entity concept, in contrast to the proprietorship, stresses the separation of business unit from its owners. Such a separation was nevertheless useful for accounting purpose only. At its origin, it was not considered a legal unit or entity but strictly limited to the area of accounting entity. The main idea behind this concept was that the business, irrespective of its form of ownership, was generally considered to be an entity in its own right which was primarily concerned with accounting to outsiders, including the owners, for all properties entrusted to it and dedicated to its purpose. The basic proposition of the entity concept is perhaps best expressed in the following words of Paton and Littleton:

53 Paton, W.A and Littleton, A.C; An Introduction to Corporate Accounting Standards, Chicago, AAA, 1940, p.3.
"That the business undertaking is generally conceived of as an entity or institution in its own right, separate and distinct from the parties who furnished the funds, and it has become almost axiomatic that the business accounts and statements are those of the entity rather than those of the proprietor, partner, investor or other parties or groups concerned."

The significance of this concept could also be imagined from the following remark of another late nineteenth century French author on the subject as referred by Littleton. J.D.Courellos Senevil (1870) remarked that:

"The principle of double entry bookkeeping is that all commercial capital is a capital entrusted to the firm to manage, which must be able at any time to say where it is, in whose hands and in what form it is to be found, and how and when it has been increased or decreased."

The above description of the principles of double entry system strangely struck a similarity of thoughts with that of an earlier Greek writer, Lodivicco Crippa (1838). He also stressed on the

separateness of ownership from the business and held that the capital account is essentially the traders own personal account with the business. That, to an accountant the operation of an account with a 'proprietor' is not different in principle from that of an account with a lender or a borrower as stressed by Leon Gomberg, when he says "yet book keeping is concerned with the movement of values within a business enterprise, not with the affairs of the proprietor as such".

In its background, the entity concept stems from such question as whether the person (for whom the books are kept and to whom the reports are communicated) is the proprietor or the body of proprietors in their human selves or a separate abstract being, in the guise of a fictional entity, corporate or otherwise. Though the earlier instances of separation between business and proprietor could be found to exist before the medieval period, yet the modern significance of the business entity, separate from the owners has been the outcome of industrial revolution. Industrial revolution resulted in mass production and caused rapid institutional changes and technological transformations. The company form of organization was found to be largely organized and it made ways for a pretty big number of people, rich and poor alike to combine to participate in the company capital. The separation of ownership and control fostered the rise of an independent management group.

that undertook the stewardship for and on behalf of the remote and dispersed owners. Limited liability concept appeared in those days in order to guard the absentee owner's interest and founded the business unit to be a creature of the state as a legal real unit. Indeed, the new technology not only destroyed the existing social framework, but altered completely the method by which business was to be financed. Large scale participation in company capital caused a change in the environment that the doctrine of stewardship had been restated in a legal form in order to safeguard the interest of shareholders and investors. It made disclosure of information to interest groups a condition attached to the privilege of joint stock status and of limited liability. Different laws were passed by the legislative bodies to regulate such corporate organizations in different countries during the late nineteenth century. Among the developed countries Britain came first, to incorporate such companies by general laws passed by the parliament for the first time in the year 1855 and at about the same time in America the individual State legislatures adopted resolutions in support of such corporation laws. The main features of the corporations created by the law were the provision for perpetual life, provision for transferable shares without the consent of other


shareholders and the limited liabilities for the shareholders. With the widespread recognition of business as a legal real unit, the basic pattern of proprietary interest has been changed and related not to one or a few irreplaceable individuals, but to a constantly changing group of people. Profit or loss could no more be determined from the mere comparison of proprietary net worth at two different points of time. The simple notion of profit expressed as the personal gain of the proprietor became irrelevant in such a corporate environment owing to the constant movement of the owner-shareholders in and out of the area of proprietary interest. This changed notion caused the separation of business from their actual owners and made them operated under an assumed trust arrangement between the legal entity and the legal owners. Because of this separation of the business from the legal owners and because of the varying legal status of those owners, it became necessary for the fictitious business entity to account for both the kinds of goods and services making up the property in its possession and for the kind of ownership claims attaching to those properties. The contribution of the entity theory in the discharge of stewardship responsibility and the development of accounting had been assessed by Gilman who argued that, the entity, as such,


is not concerned with the economic measure of valuation but rather symbolizes in terms of money various transactions reflecting a charge and discharge relationship between entity and proprietor. These changed setting in the legal and the economic environment aroused the necessity for improvements in accounting and prepared the ground for business unit to stand on the concept of a distinct and separate entity.

The multiple ownership of proprietary capital in corporate organizations required a complicated system of capital accounting to grow. Thus, the entity concept produces a different balance sheet equation, which reads

$$\text{Assets} = \text{Investments}$$

The employed capital, according to this concept is the sum total of the total property active in the business from whatever sources derived. Accordingly, long term liabilities are also considered to be a capital source. E.G. Folsom, an American writer asserted in 1873 that properties to be considered capital should be active and thereby constitute a business which from the beginning establishes a relation between itself and all parties dealing with it. This concept brought about a change in the structure of book keeping equation of the earlier period.

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63. Folsom, E.G; Logic of Accounts, New York, 1873, mentioned in Littleton, A.C; Ibid., P.199.
But the fundamental objective of maintaining equilibrium and determining financial relations remain unchanged, possibly till even today.

Management stewardship and beginning of reporting:

It can thus be stated that the entity theory achieved its full stature by imparting an organized exposition of the nature of double entry system of bookkeeping during the last quarter of the nineteenth century. The impact on the legal environment created by this concept witnessed, in a few years, the formation of hundreds of companies in the developed countries. Such a shift of importance in the organization of business enterprises resulted in a greater tilt to the stewardship responsibility. In contrast to proprietary theory, the entity theory introduced the idea of management stewardship and caused general awareness by the creation of various interest groups in company affairs. Rapid industrial developments made it more and more necessary to measure and report results of operations to those who could not observe them at close range but held substantive interest. The question of fiscal and stewardship responsibility warranted more analytical consideration with regard to the utilization of resources. It obviously gave rise to the need for the protection of the interests of the owners and investors. Historical essence of accounting thus

could be found to lie in 'recording', in order to show financial relations in terms of equilibrium within enterprises. The enactment of laws relating to verification made fiduciary responsibility more prominent as an objective in accounting and resulted in the gradual emergence of several new concepts and techniques in the discharge of this responsibilities.

Accounting thus by the end of the last century grew into a formidable discipline and played a definite role in the economic system. It ably met the needs of the business and society throughout the ages of economic emancipation and continued to serve powerfully to the formation of a new phase of modern civilization. Its use did not remain confined to the discharge of traditional stewardship or management stewardship but, in course of time, extended to the governmental activities, in terms of its accountability to the nation. Accounting for governmental activities, precisely, is nothing more than the discharge of stewardship responsibility for and on behalf of the nation, because the governments are thought of as the custodian of nation's wealth for its maintenance, effective utilization and national welfare as a whole. Interest thus gradually built up in the preparation of accounting reports covering all aspects of economic operations. 'Reporting' consequently emerged as a necessary companion of the accounting function towards satisfactory discharge of stewardship function.