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THE PUBLIC ACCOUNTING PROFESSION IN
SELECTED ARAB COUNTRIES OF
THE MIDDLE EAST

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IN THE MIDDLE EAST

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ABSTRACT

The public accounting profession is a derivative function. It is a business service which can exist only in a free enterprise economy and can reach a developed state only in a corporate environment. These two factors first gave rise to public accounting in the more developed nations and are now influencing the growth (or the decline) of public accounting in the Middle East.

Professional public accounting in the Middle East started as a British activity serving foreign enterprises. As local business firms started to emerge, so did local public accountants. At the outset, however, such local accountants were not sufficiently qualified; British accounting firms thus remained the dominating influence among foreign and local businessmen for a long time.

British accounting firms were first established in Egypt. Egypt was also the country with the greatest number of foreign-qualified local accountants and the only country to develop its own profession. Under the impact of the government's socialistic measures, however, the economic importance of public accountants started declining. As a result, the profession's whole structure was shattered.

The economic pattern of Egypt is influencing the trend in Iraq and Syria. Thus public accountants in Iraq and Syria may soon be facing a similar fate as those of Egypt.

As things stand now, public accountancy's chances of development are only in Lebanon, Kuwait, Jordan and Saudi Arabia, all of which are free enterprise economies. The legal framework covering statutory audits to shareholding companies exists in the companies' legislation of all these countries. A legal deficiency, however, exists in public accountancy legislation, where the competence demanded of licenced public accountants is insufficient.

A further deficiency exists in the profession itself due to its being unorganized on the private level. The independence, ethical conduct and auditing standards of practitioners are without effective supervision. Under the present circumstances, the only public accountants with formalized ethics and standards are those affiliated with foreign accounting societies. They are few, but they dominate the field. Still, the reputation of the Middle Eastern profession as a whole is tarnished by the practices of the many unqualified practitioners.

Further economic development and increasing international business relations emphasize the need for a sounder local profession. The solution must be found on the legal level, by raising the standards of competence to licenced public accountants, and on the professional level, in the form of a properly organized professional body which can command the support of official authorities and the business community.

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INTRODUCTION

The growth in size and complexity of the business organization has directly and indirectly enhanced, and sometimes actually gave birth to a host of related professions, an important one being that of public accounting.

Public accounting as it is known today can trace its birth to fairly recent history. Until late in the nineteenth century, the public accountant was primarily engaged in writing up the records of a number of small businesses. His auditing activities were secondary; they consisted mainly of checking upon the accuracy of cash and bookkeeping entries and of assisting in the distribution of profits among partners.

The public accountant has since come a long way. With the birth and development of the shareholding company, the public accountant's role rapidly changed and gained new stature. He became an invaluable member of the business community, an independent expert upon whom the investing public and the official authorities rely to certify the credibility of the financial representations of the corporate management.

The role of the public accountant further increased in significance with the growing complexity of business institutions and the economic framework in which they

operate. He became an advisor to businessmen on financial and organization matters, and a tax specialist who helps them through the maze of fiscal legislations. Although the profession is, by choice, mainly unnoticed and untrumpeted, its presence is nevertheless real and keenly felt in the advanced industrial nations of the west.

In their progress towards their present role, public accountants have sought, in various different forms, to achieve recognition as members of a dignified profession. Their efforts have been successful in most developed countries, where they established a tradition built upon competence in service and integrity of character. The degree to which a similar tradition can be built up in the other countries determines the success of the public accountant in fulfilling his economic role.

The efforts of the Middle Eastern Arab countries at development, the varying degrees of success achieved, and the diverging trends followed have left their impact upon all wakes of economic life. The role that public accountants can play in this contexture is limited by the economic system of the country, the level of development attained and the traditions of the business community. Public accounting is an outgrowth of the system of free enterprise -- of its corporate form of organization and diffused ownership of business, and of its intricate fiscal system. The extent to which the economic structure of the country is patterned along these

lines determines the extent of development of the profession.

This thesis attempts to study the present state of the profession and the laws governing its practice in the Arab countries of the Middle East. I have chosen the designation of "public accounting" for the profession. It is also referred to as "auditing" or just plain "accounting". The last designation is mainly used in Great Britain where the accountancy bodies are advancing the use of the word "accountant" to include all persons in public accounting practice. The idea is to give "the word 'accountant' the widest possible interpretation in the eyes of the public."¹ For our purposes, however, the designation of "public accounting" is more embracing than just "auditing", even though auditing is a major public accounting activity, while the term "accountant" implies too comprehensive a designation.

I have started out, in the first chapter, to define the various types of services normally rendered by public accountants; and, in the second chapter, to give a brief description of the development, the role and the organization of the profession in the more advanced countries of the world. As the profession in the Middle East has no special traditions of its own and, as a result, is completely dependent upon the trends in the more advanced countries for its principles and

¹The Association of Certified and Corporate Accountants, "Pronouncement by the Council", Sept. 1954 as restated in the Report of the Council for 1961, p. 16.

character, such a route to the subject is unavoidable.

The third chapter is devoted to a discussion of the origins of public accountancy in the Middle East. It is important, in an analysis such as the one attempted in this paper, to give a brief exposé of the factors that led to the initiation of professional practice in the Middle East, and of the various types of influences that it was subjected to before it reached its present level.

I have devoted the fourth chapter to the profession in the United Arab Republic, thus excluding it from the main course of subsequent analysis. Professional practice in Egypt had always developed in a rather isolated manner in relation to the other Arab countries, and had achieved a comparatively higher level of development. Egypt was the first country to import the British public accounting profession and was later the first to develop a nationally organized profession of its own. The vast structural changes that swept the Egyptian economy in the past few years have, however, left their impact upon public accountancy. The recent socialistic trend of the country has checked the growth of the profession and may eventually bring about its gradual extinction; the laws which existed less than a decade ago are no more in effect now, and the economic atmosphere in which present day practice is being carried out is fundamentally different from the one in which the profession started to develop. These basic differences in

the historical evolution and present structure of the Egyptian profession as compared to the other Middle Eastern countries necessitate a separate exposé of the subject as it relates to Egypt.

The fifth chapter deals with the present legal framework in the other countries covered by this study, which are: Lebanon, Syria, Jordan, Iraq, Kuwait and Saudi Arabia. This includes the description and evaluation of the role of the independent auditor as recognized by the various commercial or company laws presently in force, and of any other legislation regulating the qualifications, standards, liabilities and responsibilities of the auditor.

The sixth chapter attempts to analyze the present state of public accountancy practice in the above countries, i.e., the structure of the market, the types of services offered, the standards and principles governing the relations of public accountants with the business community and with each other, and the overall organization of the profession.

In the final chapter, I have attempted to evaluate the role of the profession in the economic setup of the area as compared to the role it is playing in the more advanced economies. I have tried to draw conclusions on its future course of development based on perceived or extrapolated trends.

The material in the first two chapters was largely collected from books and articles by authoritative writers in

the field and from a study of the legislation of the more advanced countries. The rest of the material in the paper was based upon past and present legislation in the Middle Eastern Arab countries, upon personal experience in the field, and upon interviews with the leading members of the profession and personal contacts with key representative members of the business community.

CHAPTER I

THE SCOPE OF PUBLIC ACCOUNTING SERVICES

Within the present structure of free-enterprise economies, public accountants provide the following set of services:

1.- Auditing Services

Auditing is the basic activity of public accountants and the one which gives their practice its distinct professional status. The other public accounting activities are mainly incidental to this primary activity.

The main purpose of independent audits is to add credibility to the financial representations of the management. In essence, auditors represent the interests of shareholders vis-a-vis the management; but interested parties other than shareholders also depend on the auditors' reports in many of their financial decisions. Thus auditors fulfill in the economy the primary function of helping to maintain "the mutual confidence which is necessary in business relationships;"¹ hence, the fundamental

¹Paul Grady in his summary of the Technical Programme of the 8th International Congress of Accountants, as cited in The Accountant, Oct. 6, 1962, p. 444.

requirement of independence in auditors, which shall be discussed later on in this paper.

Auditing services can be generally classified as follows:

- a) **Statutory audits:** -- These are required and defined as to scope by law. They pertain mainly to publicly-owned shareholding companies, and they normally result in a formal statement of opinion on the company's financial statements as prepared by the company's directors. Such certified financial statements are essentially prepared for the benefit of shareholders and official regulatory agencies, but are not restricted in their distribution to these parties. They may be submitted to other interested third parties of the business community, as long as no more than a regular expression of opinion is required. In a number of countries (Egypt, Lebanon and Syria, for instance), the law provides that the certified financial statements must be published in local journals or newspapers.
- b) **Non-Statutory audits:** -- This category includes all audits conducted at the request of businessmen for purposes other than the fulfillment of legal requirements. Their scope is determined by the contractual relationship between the auditor and the engaging party. They may result just in certified financial statements and/or in

detailed reports on the subject of the audit. They include: audits of closely-held corporations not required by law, but by their own articles of association, to submit certified financial statements;¹ audits of publicly-owned corporations beyond the scope set down by the law; audits of the accounts of individuals, partnerships, and other unincorporated businesses; and special-purpose audits or investigations of the accounting records requested by management (such as in the case of a suspected fraud),² shareholders, bankers, creditors, potential buyers of the business, or other interested third parties.

2.- Accounting Services

Accounting services are the oldest of public accounting activities. They consist mainly of writing up accounting records and extraction of financial statements therefrom, and the installation of bookkeeping systems. Being essentially

¹In the Netherlands, for instance, there is no law requiring even publicly-owned companies to have independent auditors, but independent audits are nevertheless an established business practice provided for in the corporations' articles. (Drs. P.J. Van Stoten, "Auditing", European Congress of Accountants, 1963, Papers, pp. 143-148.)

²A regular audit whose purpose is to render an opinion on the fairness of financial statements is not designed, nor can it be relied upon, to uncover all frauds and irregularities, unless they are of such a magnitude as to affect the fairness of the financial statements or they are of such a character as to have been possible to uncover in the normal course of a reasonably well-conducted audit.

a service to small businessmen, they are more prominent in underdeveloped countries, which are characterized by the preponderance of small-size business units in their economic structure.

3.- Taxation Services

Taxation services emerged as a major public accounting activity in Great Britain and the United States during the years 1910-1920. In those years, the income tax rose sharply in England¹ and was introduced for the first time in peacetime (in 1913) in the U.S. Taxes on corporate profits, graduated tax rates on the incomes of individuals, and excess profits taxes (a war measure) were imposed. Their complexity, and their close connection with accounting and financial matters, drove many firms and individuals to seek the advice of public accountants. In both countries today, the preparation of tax returns of companies, unincorporated businesses and individuals,² and the rendering of tax advices form a

¹The income tax was known in Great Britain in one form or another since William Pitt introduced it in 1798. The highest it reached before World War I was 1s 4d to the £ in 1860, falling shortly afterwards, and 1s 3d to the £ during the Boer War in 1899-1902. In 1919, it reached 6s to the £.

²In the U.S., the number of individuals seeking the assistance of public accountants in the preparation of their tax returns was estimated in 1960 at 750,000. This figure roughly corresponds to the number of persons whose taxable income exceeds \$20,000 per year each. (T.A. Wise, "The Auditors Have Arrived," part I, Fortune, Nov. 1960, p. 154.)

substantial portion of public accounting activities.¹

4.- Management Services

Management services by public accountants are a natural outgrowth of the audit function. Actually, a certain amount of management counselling occurs in the normal course of auditing activities. But the specialized knowledge of business organizations and procedures that the auditor acquires has built up a demand for him as a management consultant, in a capacity distinct from that of auditor.

In a growing economy, expanding business firms, especially the dynamic smaller ones, keep facing major organizational problems until their basic business structure -- legal and internal -- becomes geared to handle the expanding volume of business. The public accountant has first-hand contact with such problems, especially if he is handling the audit of the firm in question. He is thus a natural adviser to business on all management problems of accounting, finance, systems, control, costing, budgets, and related matters, as well as on the legal structure most appropriate for the business.

¹In Great Britain, the public accountant prepares his client's tax returns and submits them himself to the Inland Revenue. He then directly handles any queries the Inland Revenue might have, and enters into tax negotiations with them on his client's behalf. (G.S.A. Wheatcroft, "Ethical Restraints on Tax Practice in Great Britain," The Journal of Accountancy, Feb. 1961, pp. 59-66.)

The public accountant is becoming increasingly preoccupied with management problems in our present world of sprawling corporations and business complexities. Already, public accounting firms are changing the composition of their staff to accommodate for the special skills required for this new field.¹ As compared to the customary functions of auditing or taxation services, where the market is already stabilized and where future expansion will follow the normal course of business development, the broadening scope of activities in the management services field promises to be of great future potential and to develop into a major breakthrough for public accountants.²

5.- Other Specialized Services

As accounting and financial specialists, public accountants are called upon to perform various other specialized services. The following are most frequent:

- a) Executors, administrators, or trustees of deceased persons' estates -- this activity is most common in Great Britain;

¹Wise, Op.Cit., pp. 185-186.

²The rising importance of this new function to public accountants is very evident in the extensive amount of literature being devoted to it in such accountancy organs as The Journal of Accountancy in the U.S., and The Accountant, Accountancy, and The Accountant's Journal in England.

- b) Advisors on problems of company formation, such as those of registration and of financial structure;
- c) Specialists in liquidations and bankruptcies;
- d) Assessors of the financial position of businesses for the purposes of sale, refinancing, reorganizations, or mergers;
- e) Arbitrators in disputes.

The significance of the above activities and the principles governing their performance vary between countries. A number of factors -- such as the level of a country's development, its particular business structure and business traditions, its commercial legislation and the pattern of development of its accounting profession -- affect the relative importance of each activity in the economy.

In underdeveloped countries, accounting services, coupled with certain elementary audit steps, are most prominent. Local firms in general are not appreciative of the role of the independent auditor. Shareholding companies tend to regard him as an unnecessary expense imposed upon them by law (when such laws exist), or as a person whose basic concern is to uncover frauds and detect bookkeeping inaccuracies. In fact, such attitudes persist in the minds of many people (including sophisticated businessmen) in the most developed countries. Businessmen with such a state of mind not only deny themselves the benefit that might accrue

to them from the audit, but also tend to have a depressing effect upon auditing standards in their community.

With a country's rise on the scale of development, and the resulting increase in the number of corporate organizations and the diffusion of corporate ownership, the public accountant's role grows in prominence. Also, a shift of emphasis between his various functions results. Accounting services are driven to secondary importance and auditing comes to the fore as the major activity, acquiring a much broader scope in the process. In addition, taxation and management services, which flourish on the complexities of economic life, start acquiring a major significance as taxes get increasingly entangled and business units keep expanding endlessly in size.

The presence of foreign firms in underdeveloped countries attracts foreign auditors. Historically, British auditors were the only ones of significance to spread beyond their borders. This was a natural result of the widespread economic expansion of the British, and of the developed audit concepts which had evolved in their country. The British accounting profession thus became a model for most countries (even the U.S.); and, by keeping its doors open for admittance of persons of any nationality, it carried over its concepts to a great many developing countries.

CHAPTER II

PUBLIC ACCOUNTING IN DEVELOPED ECONOMIES

-- GREAT BRITAIN, THE UNITED STATES AND FRANCE --

A. Early History

Accounting is, in a sense, as old as wealth. In its broadest meaning, it is the means of keeping track of wealth. Man, therefore, must have started to practice accounting of a sort ever since he started to accumulate wealth.

Accounting, as we know it today, originated in the trading centers of Italy in the early days of the Renaissance. Some people like to trace its origin to Fra Luca Pacioli, a fifteenth century monk whose work the "Summa Arithmetica", published in Italy in 1549, is the first known treatise on double entry bookkeeping. However, "Pacioli himself wrote that he was describing Venetian practice as he found it, and we know now that the practice was probably two centuries old when he wrote his famous 'summa'".¹

With the expansion of commerce in Italy, accounting started to develop into a recognized profession pursued by persons of special skills which they offered in an independent

¹B.S. Yamey, "Introduction", Studies in the History of Accounting, ed. A.C. Littleton & B.S. Yamey (Illinois: Richard D. Irwin, Inc., 1956), p. 2.

capacity to the public. The concept of professional competence in public accounting was recognized as early as 1581 in Venice when the world's first association of accountants, the Collegio dei Raxonati, was formed.¹

The profession must have been important enough in Milan in 1742 for the government there to establish a scale of charges for public accountants.² Rudimentary existence of public accounting could be traced in England to as early as the seventeenth century when the lords of the large manor estates used to engage public accountants to audit their accounts.³

¹Dr. Mary Murphy, CPA, in "The Profession in Italy", The Accountant, Aug. 4, 1962, p. 125, sums up its admission requirements as follows:

The Collegio prospered, and by 1669 it had attained the status of a craft guild, membership of which was obligatory before an accountant could pursue his craft. Candidates had to obtain from a magistrate a declaration of their fitness to enter the profession; they served an apprenticeship of six years in the office of a public accountant. A commission of examiners, consisting of forty-five persons, of whom thirty were accountants, conducted a preliminary examination, and successful candidates then appeared before a panel of controllers of the Collegio and five 'learned merchants of the city'. If they secured a three-fourths majority of this body, they were granted their certificates.

²"Accounting," The Encyclopaedia Britannica, 1962, Vol. I.

³A.C. Littleton, Accounting Evolution to 1900, as referred to by M.H. Stans, "The Profession of Accounting", The CPA Handbook, ed. R.L. Kane, (N.Y.: The American Institute of Accountants, 1952), Vol. I, chap. i, p. 2.

Until the early part of the nineteenth century, the progress of public accounting was rather limited. Its functions were mainly confined to bookkeeping services to small business, assessment of partners' shares of profits, and elementary audit steps consisting of checking the accuracy of bookkeeping entries and the handling of cash. The practice was carried on by a scattering of persons, sometimes simultaneously with other occupations.¹ This early history, however, was not precursory of further development in that the function of independent audits, which is the backbone of the profession at present, was not yet existent; it came about with the birth of the institution of absentee ownership during the Industrial Revolution.

B. The Evolution of Independent Audits

1.- General Considerations

Public accounting services in the modern business world emerged as a result of two major economic developments: the birth of the institution of the shareholding company, which created the need for independent audits as a safeguard for the

¹G.F. Saunders, F.C.A., in his paper "The Accountant in Practice," Proceedings of the Sixth International Congress on Accounting, 1952 (London: Gee & Co., 1952), p.365, mentions that "a certain accountant in Liverpool in 1790 had the additional description of dealer in tinslates, and for many years the business of stock broking was carried on by accountants."

investments of shareholders; and the increasing complexity of economic relations, which created the demand for specialized knowledge in the solution of business problems.

Legislation played an important role in the development of independent audits; not so much in the initial stages of the birth of the shareholding company as in later years when the ownership of shares became widespread and the relation between the individual shareholders, particularly the smaller ones, and the management became increasingly detached. Realizing that the shareholders had no means to exercise effective supervision upon the company's financial transactions, the government stepped in with provisions for the compulsory appointment of independent auditors by all publicly-owned companies.

Even if not stipulated by law, independent audits would normally be requested by shareholders. The function became a well established business practice with the diffusion of corporate ownership. However, the provision for compulsory independent audits by legislation, usually accompanied by specifications of the auditors' qualifications and the scope of their examination, fulfills a number of purposes, mainly:

- a) It ensures that the shareholders are actually given the benefit of independent audits;
- b) It ensures a minimum level of competence in the discharge of auditing duties;

- c) It minimizes government inspection of the accounts in its fiscal relations with the business community, and in its function as guardian of the public interest.

2.- Great Britain

The accountancy profession in Great Britain has probably done more to influence the auditing practices of the world than that of any other country. Three major reasons account for this fact:

- a) The early development of the profession in Great Britain, the high professional standards that its members adopted from the start, and the international character it has assumed.
- b) The readiness of British accountants to expand and establish practices all over the world.
- c) The growth of the British Empire and the effect of British legislation and business practices upon those countries falling within its realm.

The modern history of public accounting in Great Britain unfolds in the first half of the nineteenth century when the Industrial Revolution was rapidly gaining momentum. Prevalent legislation was not then conducive to the needs for the large amounts of capital required by the new industries; joint stock companies could only be formed by the costly and difficult to obtain Royal Charter.

Responding to public need, the British Parliament in 1844 passed the first Joint Stock Companies Act, which made possible the creation of joint stock companies by registration. The Act prohibited the establishment of large unincorporated companies (which were actually large partnerships with transferable shares very popular at the time), but did not limit the liability of the joint stock company members. For our purposes, however, the most important provision of the Act was the compulsory appointment of independent auditors by all registered companies.

With the passing of the first limited liability laws in 1855, the shareholding company entered a new historical phase in its development as the major form of business organization. The Limited Liability Act of 1855 also reflected the first official concern over the element of public interest in independent audits: the auditors of registered companies were to be approved by the Board of Trade.

Compulsory audits were, however, abandoned a year later in the Joint Stock Companies Act of 1856, apparently due to "the strong contemporary feeling that matters of accounting should be dealt with by private contract between

shareholders and directors."¹ Nevertheless it carried an appendix of a model set of articles of association -- to be used by all companies not registering their own articles -- which included remarkably advanced clauses pertaining to the engagement of professional auditors.²

The historical importance of the 1856 Act, and of the subsequent 1862 consolidation Companies Act, lies in the comparative ease with which they allowed the registration of limited liability companies, thus further stimulating the country's industrial expansion.

Auditing services by public accountants were expanding rapidly with the multiplicity of companies in the latter half of the nineteenth century -- unsupported by legislation³ but demanded by shareholders. Initially, the audit of a company was entrusted to some of its shareholders elected at a general meeting;⁴ but this practice was soon abandoned for the more expert services of professional accountants. The greatest expansion, however, came about when the Companies Act, 1900,

¹H.C. Edey and P. Panitpakdi, "British Company Accounting and the Law, 1844-1900," Studies in the History of Accounting, p. 361.

²Ibid. pp. 362-364.

³Except in the case of banking companies where compulsory audits were reinstated by the Companies Act, 1879, due to the element of public interest, other than that of shareholders, involved in their case.

⁴Edey and Panitpakdi, Op. Cit., p. 364.

made the appointment of independent auditors, to be elected annually by shareholders, compulsory for all registered companies. Enormous opportunities opened up for public accountants as hitherto unaudited companies started demanding their services. More significantly, the new Act subjected to professional scrutiny the accounting practices of the leading business enterprises, marking a historical step in the long attempt to define accounting principles and to bring about a uniformity in financial reporting:

The rapid formation of companies in the latter part of the nineteenth century and the resulting complexities of business created another function for public accountants -- that of specialists in liquidations and bankruptcies. In fact, such work was receiving more emphasis at the time than actual audit work.¹ With the impressive growth of auditing

¹F.R.M. de Paula in "The Accountant in Industry," Proceedings of the Sixth International Congress on Accounting, p. 322, cites a section of the petition submitted by the Institute of Chartered Accountants in England and Wales to obtain the Royal Charter in 1880:

"The profession of public accountants in England and Wales is a numerous one and their functions are of great and increasing importance in respect of their employment in the capacities of liquidators acting in the winding up of companies and of receivers under decrees and of trustees in bankruptcies or arrangements with creditors and in various positions of trust under Courts of Justice as also in the auditing of the accounts of public companies, of partnerships, and otherwise."

services in subsequent years, such type of work was driven to secondary importance, but it still forms an important activity of public accountants in Great Britain.

3.- The United States

Corporations in the United States are created by State laws and as such are not subject to the same regulations all over the country. There were apparently no provisions for compulsory audits in the state corporate laws; "the profession developed in the United States with relative freedom in an atmosphere in which the auditor's services were sought voluntarily".¹ The first time independent audits became compulsory by legislation was in 1933 when the Securities Act was passed.²

Factors other than legislation have influenced the growth of the independent audit function in the United States. The most important was the sound start the U.S. profession had at the hands of British professionals arriving in the latter part of the nineteenth century to check upon the American securities of their clients.³ They were the first professional accountants in the country. They brought with

¹H.F. Stettler, Auditing Principles (N.J.: Prentice Hall, Inc., 1961), p. 18.

²Ibid., pp. 18-19.

³Mary Murphy, "The British Accounting Tradition in America," The Journal of Accountancy, April 1961, pp. 54-63.

them the knowledge and skills that had been developing for a few decades in their home country.

The multiplicity of corporations and the important business mergers of the late 1800s and early 1900s, coupled with a continuous diffusion of business ownership, provided the necessary stimulus for the rise of an American accounting profession.¹ The importance of public accountants was later enhanced by the introduction of the excess profits tax during World War I and the development of the income tax at about the same period. Then came in the 1920s the requirements of the New York Stock Exchange for more financial information from listed corporations.²

The passing of the Securities Act, 1933, regulating the public distribution of Securities, and of the Securities Exchange Act, 1934, regulating their listing on national stock exchanges, created in the auditing field in the United States a condition comparable to Great Britain in 1900 when the Companies Act made independent audits compulsory. Corporations affected by the Acts were required to file with the Securities and Exchange Commission (which was the official agency administering the Acts) financial statements certified by independent public accountants.

¹Ibid., Also Wise, Op. Cit. Part I, p. 153.

²Wise, Op. Cit. Part I, p. 153.

The stock exchanges now also have their own requirements. "But if the information required by the S.E.C. is obtained in full, it should enable compliance with the requirements of any stock exchange."¹

Companies other than those regulated by the S.E.C. are not subject to any federal accounting or audit requirements.² This is in contrast with Great Britain, where all limited companies (except exempt private companies) are required to be audited by professional accountants.³

There is an essential difference in approach towards the duties of the statutory auditor between Great Britain and the United States. This difference, however, consists more of technicalities than of basic divergences in auditing standards.

In Great Britain, the duties of the statutory auditor consist of ascertaining the compliance of the company's directors with the accounting requirements of the Companies Act, 1948. In the United States, his duties are to ascertain the company's adherence to "generally accepted accounting principles". The American profession and the S.E.C. have

¹J.F. Shearer, "The Securities & Exchange Commission," Part I, Accountancey, April 1961, p. 200.

²Ibid., Part II, May 1961, p. 277.

³Great Britain, Companies Act, 1948, Section 161.

sought in many forms to define these "generally accepted accounting principles".

With regards to auditing procedures, there has been a noticeable departure in the United States from British practices since the early part of the twentieth century.¹ But probably the most important landmark in the independent development of American auditing practices is the McKesson and Robbins case in 1938.² The fraud involved was of considerable proportions and had been going on for a number of years unnoticed by the company's auditors (Price Waterhouse & Co.) who were one of the leading American accounting firms.

The McKesson and Robbins fraud was based upon the manipulation of stocks and receivables records. The American profession realized that its auditing procedures in this connection were deficient. As a consequence, the practices of attending at the client's stocktaking and ascertaining the correctness of receivables by direct confirmation were conceived. The attendance of the client's stocktaking has been receiving increasing attention in Great Britain lately, but it is not yet a generally accepted practice; the direct confirmation of receivables is even less of an accepted practice.³

¹Stettler, Op. Cit., p. 18.

²For a comprehensive summary of the case, see Ibid., pp. 725-734.

³Shearer, Op. Cit., p. 201.

3.- France

France in the nineteenth century was witnessing economic developments similar to those taking place in Great Britain. Thus the Law of Shareholding Companies (Societes Anonymes), which was passed on July 24, 1867 and is still the basis of present French company legislation, required all "societes anonymes" to have independent auditors to be appointed annually by shareholders.¹

Although French legislation recognized compulsory audits by shareholding companies earlier than both Great Britain and the United States, the French profession lagged behind these two countries.

Before 1935, no competence requirements were attached to the statutory auditor. This has hindered until then the building up of a respectable French accounting tradition and the assumption by the auditor of his serious role in the economy. One analysis of the role of French auditors during that period said:

¹France, Law of July 24, 1867 on Shareholding Companies, Art. 32. The auditor's appointment was extended to a three-year period by Decree dated Aug. 31, 1937.

Appointed for a financial period without a guarantee of competence, exercising their functions only in the short period preceding the general meeting, depending in fact upon the directors to nominate them for the shareholders to approve, the auditors of the Law of 1867 could not have properly fulfilled their functions of control. Very often their report was a brief endorsement of the accounts, given without any serious examination.¹

It is only after 1935 that the function of independent audits started to be taken more seriously by French legislation. The basic concern was about the public interest in companies resorting to the public for capital. Decree dated Aug. 8, 1935 required such companies to choose at least one of their auditors from a list of "Auditors Approved by the Court of Appeal" (Commissaires Agrees par le Cour D'Appel); and if no such auditor is chosen, the Commercial Court has the power to appoint one itself.² Other regulations aimed at maintaining the auditor's independence were also included.³ In this manner, the official authorities hoped to control the standard of qualifications of persons examining the accounts of public shareholding companies.

¹G. Ripert, Traite Elementaire de Droit Commerciale (Paris: Librairie Generale de Droit et de Jurisprudence, 1954) p. 500.

²France, Law of July 24, 1867, as amended by Decree dated Aug. 8, 1935, Art. 33.

³Ibid.

C. The Organization of the Profession

1. Types of Professional Structure

Public accountancy has not yet achieved the status of a universal profession with a universally accepted body of knowledge. In the western economies, the profession's pattern of development was characteristically national, even though in most cases British influence was considerable. Thus, while the broad lines of public accounting activities and the basic principles governing them are largely similar between countries, there are varying degrees of difference in the standards and methods applied in their performance. Apart from that, national peculiarities are witnessed in the organization of professional practice within the countries.

Two general distinctions can be drawn between types of professional structures. In the first, typified by Great Britain, the ultimate power rests with the profession itself; public accountants are organized in professional societies membership to which is all the requirement that they need for professional and legal recognition. In the second, typified by the United States and France, the ultimate power rests with the law; professional recognition is accorded to individuals by an official authority; professional societies usually do exist, and may wield great moral power, but their role is confined to that of spokesman and coordinator.

2. Great Britain

Public accountants achieve professional recognition in Great Britain by being admitted as members in one of the privately organized accountancy bodies. The business community highly regards such membership, and the law, vesting the authority in the Board of Trade, recognizes it as sufficient qualification for a public accountant to certify financial statements as long as the accountant is practicing in an independent and personal (i.e. not as a body corporate) capacity.¹

The Board of Trade recognizes the following accountancy bodies:²

¹Great Britain, Companies Act. 1948, Sec. 161 (2); the text of the article is as follows:

None of the following persons shall be qualified for appointment as auditor of a company:

- (a) an officer or servant of the company;
- (b) a person who is a partner of or in the employment of an officer or servant of the company;
- (c) a body corporate:

Provided that paragraph (6) of this subsection shall not apply in the case of a private company which at the time of the auditor's appointment is an exempt private company.

²C.M. Schmitthoff and T.P.E. Curry, Palmer's Company Law (London: Stevens & Sons Ltd., 1959), p. 615.

- a) The Institute of Chartered Accountants in England and Wales -- incorporated by Royal Charter in 1880.
- b) The Association of Certified and Corporate Accountants -- the result of an amalgamation of the Corporation of Accountants (founded in 1891), the Institution of Certified Public Accountants (founded in 1903), and the London Association of Certified Accountants (founded in 1904).
- c) The Institute of Chartered Accountants of Scotland -- the oldest existing body of accountants in the world. It is the result of an amalgamation of the Society of Accountants in Edinburgh, incorporated by Royal Charter in 1854, and the accounting societies of Glasgow and Aberdeen which were chartered in 1855 and 1867 respectively.
- d) The Institute of Chartered Accountants in Ireland -- incorporated by Royal Charter in 1888.

(Another society "The Society of Incorporated Accountants and Auditors," incorporated under the Companies Act in 1885, has amalgamated in 1957 with the chartered institutes of the respective countries.)

The rise of these societies, especially the chartered institutes, as organizers of the profession during the second half of the nineteenth century was in itself a sign of

professional maturity. They have promoted the adherence to high professional standards among public accountants. Their members thus earned the respect and confidence of the business community and the official authorities, and their role, as independent auditors or otherwise, became appreciated not only in Great Britain but all over the world.

It is worth pointing out at this stage that there is no law in Great Britain which licences public accountants or regulates their profession. In theory, anybody can be a public accountant; the recognition by the Board of Trade applies only to those persons certifying the financial statements of companies as specified by the Companies Act, 1948. The public, however, has such a high confidence in the recognized accountancy bodies that it is very unlikely for any non-qualified practitioner to be able to build up a significant clientele.

The British accountancy bodies have acquired an international character in that their membership is open to any person, of whatever nationality, who satisfies their requirements. In countries which have no organized profession, or whose national societies are either weak in standards or internationally unknown, accountants aspiring for national and international recognition have sought

membership in these bodies. A number of countries, of which I cite Iraq and Kuwait in the Middle East, have accorded official recognition to members of these bodies. Some non-British members have formed in their countries national accounting societies patterned along the lines of the British societies, an example being the Egyptian Society of Accountants and Auditors. The British accounting tradition has thus left its everlasting imprint on the rest of the world, and made possible the laying of many a cornerstone for an accounting profession in underdeveloped countries.

The total membership of the British accountancy bodies is presently as follows:

- a) The Institute of Chartered Accountants in England and Wales = 36581 members on January 1, 1963 (of whom 4279 were not in the United Kingdom).¹
- b) The Institute of Chartered Accountants of Scotland = 7248 members on July 31, 1963 (of whom 1176 were not in the United Kingdom).²
- c) The Institute of Chartered Accountants in Ireland = 1770 members on January 1, 1963.³

¹The Accountant, July 6, 1963, p. 13.

²The Institute of Chartered Accountants of Scotland, Official Directory, 1963-64, p. 614.

³The Accountant, July 6, 1963, p. 13.

- d) The Association of Certified and Corporate Accountants = 11200 members on January 1, 1964¹ (of whom about 1550 were not in the United Kingdom).²

To become a member in any of the British chartered institutes a candidate must serve under articles (apprenticeship) for five years (three years for a graduate of a British university) with a member in practice as a public accountant in great Britain, and pass the Institute's written examinations.³

Candidates in the past used to pay a premium to the firm of chartered accountants for the privilege of being accepted as articled clerks. The demand for junior level employees, especially in the post-World War II years, has, however, resulted in the gradual extinction of this procedure; articled clerks can now expect a reasonable return for their services.

¹The Association of Certified and Corporate Accountants, List of Members, 1964, p. 15.

²Ibid., compiled from pp. 425-675.

³Examinations fall into three parts: Preliminary, Intermediate and Final. A university graduate or a holder of the General Certificate of Education can hope to be exempted from the Preliminary examination. The Intermediate examination of the Institute of Chartered Accountants in England and Wales of May 1963 consisted of: Bookkeeping and Accounts, limited companies, partnerships, and executorships; Auditing: General Commercial Knowledge: and Taxation and Cost Accounting. The Final examination of the same date consisted of: Advanced Accounting; Auditing; Taxation; General Financial Knowledge and Cost and Management Accounting; and English Law.

The requirements of membership of the Association of Certified and Corporate Accountants (A.C.C.A.) are less rigid. A person may be admitted as member of the Association upon passing its written examinations¹ and satisfying its council as to experience and character. But to be allowed by the Association to practice as a public accountant, a member must have additionally completed thirty months of employment with an accounting firm acceptable to the Association.

A member of the Association can either call himself a "Certified Accountant",² or use the designatory initials A.A.C.C.A. if an Associate, and F.A.C.C.A. if a Fellow.³

¹Examinations fall into three parts: Preliminary, Intermediate and Final. A university graduate can hope to be exempted from the Preliminary examination, and from certain subjects of the Intermediate depending upon the courses covered in college. The Intermediate examination of December 1963 covered: Bookkeeping and Accounts, Costing, Mercantile Law, Auditing, and Economics and Business Statistics. The Final examination of the same date covered: Advanced Accounting, Executorship and Bankruptcy, Company Law, Taxation, Auditing and Investigations, Management Accounting, and Industry and Finance. (The A.C.C.A., Examination Regulations and Qualifications for Membership, 1963).

²Any reference in this paper to the title of "Certified Accountant" indicates a member of the A.C.C.A.

³A member is first admitted as an Associate; then, if he has been in public practice for five continuous years, or served in a senior position with a practicing accountant or an official body or in another professional position acceptable to the Council for at least ten years, he becomes eligible for fellowship. (The A.C.C.A., Articles of Association, Art. 5).

The Association has acquired a special importance to non-British subjects. Whereas the chartered Institutes require all candidates to be apprenticed in Great Britain, the Association's requirement of thirty months public accounting experience applies only to candidates aspiring to go into public practice; and even then it can be satisfied outside the United Kingdom. The Association has thus offered a large number of non-British subjects, who cannot afford the time and expense of residing in Great Britain, the opportunity to earn professional accounting qualifications.

The profession in Great Britain is governed by the councils of the accountancy bodies; they administer the general rules of their societies, occasionally issue statements as recommendations to practicing accountants or to state the position of the society on certain specific issues, and supervise the ethical conduct of their members. British societies have no written codes of ethics. The ethical standards of British professional accountants are to be found in the fundamental rules of the societies, which cover the subject in a general manner, in the guiding statements issued by the councils, and in the traditional standards of conduct which have gained general acceptance over the years. Any departure from proper ethical conduct renders the member liable to caution, reprimand, suspension, or outright

expulsion, all of which are harmful to his reputation. As the law recognizes membership in the accountancy bodies as sufficient qualification to act as an auditor of public limited companies, expulsion is ruinous to a person's career.

3.- The United States

By contrast to Great Britain, professional recognition in the United States is handed down by legislature, at the State level, in the form of a certificate entitling the holder to assume the title of Certified Public Accountant (CPA).

This trend started in 1896 when the State of New York enacted the first public accountancy law,¹ which provided for the creation of a State Board of Accountancy to grant CPA certificates to candidates satisfying the State's requirements. By 1925, all states enacted similar laws with varying degrees of difference in requirements.²

Initially all such laws were 'permissive', in that they did not bar non-certified accountants from practicing as long as they did not hold themselves out as CPAs. Over the years,

¹L.H. Penney, "The American Institute of CPAs -- Past and Future," The Journal of Accountancy, Jan. 1962, p. 32

²Ibid.

however, many states shifted to 'regulatory' laws (there were thirty-one such states in 1961)¹ which provide for the licensing of all public accountants. Most of these laws specified that accountants thereafter entering the field of public practice must be CPAs.

The various accountancy laws, whether permissive or regulatory, lack in uniformity. They vary in admission requirements (such as educational level, experience and residence), in ethical codes, in interstate rights to practice, and others;² but the major requirement -- the CPA examination -- is presently a uniform one prepared by the American Institute of Certified Public Accountants (AICPA) as a service to the states.

The AICPA is the only national organization of public accountants in the U.S. Its history dates back to 1887 when a handful of accountants, mainly British professionals residing in the U.S., formed the American Association of Public Accountants³ in an attempt to create an institution with which the public can identify professional competence.

¹C.V. Heimbucher, "Fifty-Three Jurisdictions," The Journal of Accountancy, Nov. 1961, pp. 42-50.

²Ibid.

³The name was changed in 1916 to the "Institute of Accountants in the United States of America"; in 1917, to the "American Institute of Accountants"; and in 1957, to the "American Institute of Certified Public Accountants."

They hoped then to pattern it along the lines of the British institutes.¹ With the States taking over the awarding of qualification certificates, the AICPA evolved into the uniting force of American qualified accountants, and assumed the role of spokesman and coordinator of the profession. Membership to it, though voluntary and entailing no special privileges, has a high prestige factor.

The AICPA is governed by a council; the presidents of the state societies of CPAs are automatically considered as members of the council. It has a written code of ethics which is highly respected as a moral deterrent and exerts a major influence on the ethical codes adopted by the state societies of CPAs and by the State Boards of Accountancy. In fact, there are too many ethical codes in the U.S. due to the manner in which the profession is organized. The AICPA's code is the only national one, but those of the State Boards of Accountancy are the ones which are legally enforceable. The AICPA's strength is basically moral; it is not supported by legislation. Any disciplinary action its council takes on a member, though harmful to his reputation, does not

¹In 1917, the American Institute developed its own examination to test applicants for membership. It offered the same one to the State Boards of Accountancy for use on CPA candidates, eight of them accepted at the time; but by 1952 all of the States had adopted the AICPA's uniform examination.

affect his legal standing as a CPA or throw him out of public practice unless the State revokes his certificate. Even then in the 'permissive' states this will not stop him from practicing, though not as a CPA.¹ Furthermore, the AICPA exerts a considerable influence on professional practice through its directive statements, its research bulletins, and its various publications for the guidance of practicing accountants. Of an estimated 83,234 CPAs in the United States on August 31, 1963, 47,851 were members of the AICPA.²

The public accounting profession in the U.S. is confined to its national boundaries. All states require CPA candidates to be U.S. citizens; a number of them specify that the applicant must have a place of residence in the State itself,³ the CPA certificate being in a way considered as a licence to practice within the State. The few non-Americans who were able to obtain CPA certificates had taken advantage of a provision in the laws of certain states making a person eligible to become a CPA if he declares his intention to become a U.S. citizen.⁴

¹Heimbucher, loc. cit.

²The Journal of Accountancy, Jan. 1964, p. 15.

³Heimbucher, loc. cit.

⁴La Salle Extension University, Requirements for the CPA and other Examinations and the Practice of Public Accounting (1951), pp. 5-26.

The Securities and Exchange Commission does not restrict the qualifications of auditors certifying the financial statements filed with it to CPAs. It is ready to accept the certificate of any public accountant in good standing and "entitled to practice as such under the laws of the place of his residence or principal office."¹

4.- France

There are in France four types of professional accountants:

- a) The unqualified auditor (Commissaire aux Comptes).
- b) The auditor approved by the Court of Appeal (Commissaire Agree par le Cour I'Appel).
- c) The Expert Comptable.
- d) The Comptable Agree.

The right to act as an auditor is not subject to any legal restrictions in France. But shareholding companies which resort to the public for capital were required in 1935 to chose at least one of their auditors from the list of those approved by the Court of Appeal.² To be registered on that list, a person must be an "expert comptable" or submit

¹U.S., The Securities and Exchange Commission, Regulation S-X, rule 2-01.

²France, Law of July 24, 1867, as amended by Decree dated Aug. 8, 1935, Art. 3.

for an examination supervised by an official committee.¹ At present, about 80% of the auditors approved by the Court of Appeal are experts comptables.²

Before 1942, the title of "expert comptable" was free for any person to use. With the passing of the law creating the "Ordre des Experts Comptables et des Comptables Agrées" on April 3, 1942 (it was later replaced by Ordinance of September 19, 1945), the use of the titles of "expert comptable" and "comptable agréé" became restricted to those persons registered with the "Ordre".³

The "expert comptable" was defined by law as "the technician who, in his own name and under his own responsibility, is habitually engaged in the profession of organizing, verifying, appraising and rectifying accounts and records of all kinds. The expert comptable can also analyze, by the use of accounting techniques, the condition and operations of enterprises from the economic, financial and

¹France, Decree of June 29, 1936, Art. 2 and 3.

²Institute Francais des Experts Comptables, Privately received letter dated February 11, 1964.

³France, Ordinance of September 19, 1945, Art. 3 and 9.

legal aspects."¹

The "comptable agree" was defined as "the technicien who, in his own name and under his own responsibility, is habitually engaged in the profession of keeping, coordinating, opening, closing and supervising accounts and records of all kinds."²

It is interesting to note that the function of independent audits in public accounting was not clearly referred to in the above definition, at least not as a distinct function. Thus, while no person can practice any of the public accounting functions defined above without being registered with the "Ordre",³ the auditing function itself was left free of any special regulations other than those pertaining to the audit of companies raising capital by public subscription.⁴

¹France, Ibid., Art. 2, which reads as follows:

"Est expert comptable le technicien qui, en son propre nom et sous sa responsabilite, fait profession habituelle d'organiser, verifier, apprecier et redresser les comptabilites et le comptes de toutes natures.

"L'expert comptable peut aussi analyser par les procedes de la technique comptable la situation et le fonctionnement des entreprises sous leurs differents aspects economique, juridique et financier."

²France, Ibid., Art. 8, which reads as follows:

"Est comptable agree le technicien qui, en son propre nom et sous sa responsabilite, fait profession habituelle de tenir, centraliser, ouvrir, arreter, surveiller les comptabilites et les comptes de toute nature."

³Ibid., Art. 20.

⁴Institut Francais des Experts Comptables, Op. Cit.

The "Ordre" is a government institution. The "experts comptables" have organized themselves on July 1, 1962 in a private professional body, called the "Institut Francais des Experts Comptables," in order to further their interests and promote the development of the profession.¹ But membership to the "Institut" is not obligatory; of 2300 "experts comptables" in France, 1700 are members of the "Institut".²

An interesting peculiarity in France is that limited companies can practice the profession of "experts comptables". The capital of the company should not be less than 500,000 francs, and the majority of its shares must be held by "experts comptables" who must be at least three in number.³

D. Professional Standards and Ethics

The fundamental concepts underlying the practice of all professional activities are: Competence, independence, integrity, and a sense of public service. These same concepts form the foundations of public accounting practice.

Public accounting covers a set of accounting and derived activities performed by independent persons as a service to the business community. It is implied that such

¹Institut Francais des Experts Comptables, Op. Cit.

²Ibid.

³France, Ordinance of Sept. 19, 1945; Art. 7.

activities cannot be performed by the individuals or business organizations themselves either due to the specialized nature of the work or due to an inherent nature in the activity requiring that it be performed by independent persons for the purpose of obtaining an unbiased opinion.

The basic activity of public accounting, and the reason for its existence as a distinct profession, is that of auditing. The institution of public ownership of business entities necessitated the creation of the function of independent audits, conducted by persons having no interest in the operations of the business, to safeguard the investments of the large body of owners who have vested the authority of administering the business into a group of hired managers.

Legislation in advanced countries provides for all the above concepts, expressly or implicitly, in the provisions governing statutory audits. The auditor of a publicly-owned company is considered to represent an element of public interest which transcends the contractual relationship between a professional man and his client. Furthermore, professional societies have always endeavored to give expression to all these concepts in their efforts at defining sound public accounting principles, and in the professional standards which they enforce upon their members.

1.- Competence

A profession is, by definition, the offering of a service requiring special skill and knowledge to the public. The public accounting profession thus implies the embodiment of a field of technical knowledge in which the public is not normally proficient -- hence the requirement of competence.

The concept of competence is legally recognized in relation to the audit of organizations which have an inherent public interest, mainly shareholding companies. Most laws -- and this is a basic weakness -- do not provide for competence in the practice of other public accounting activities; this is left to the public to judge and evaluate.

In Great Britain, for instance, the Companies Act, 1948, states:

A person shall not be qualified for appointment as auditor of a company unless either -

- (a) he is a member of a body of accountants established in the United Kingdom and for the time being recognised for the purposes of this provision by the Board of Trade; or
- (b) he is for the time being authorised by the Board of Trade to be so appointed either as having similar qualifications obtained outside the United Kingdom or as having obtained adequate knowledge and experience in the course of his employment by a member of a body of accountants recognised for the purposes of the foregoing paragraph or as having before the sixth day of August, nineteen hundred and forty-seven, practised in Great Britain as an accountant:

Provided that this subsection shall not apply in the case of a private company which at the time of the auditor's appointment is an exempt private company.¹

¹Great Britain, Companies Act, 1948, Sec. 161(1).

The concept of competence with respect to the audit of publicly-owned companies is thus established; membership in the recognized accountancy bodies is considered as sufficient evidence (preserving at the same time the acquired rights of practitioners at the time the Act was passed). But such requirements are waived with respect to shareholding companies whose shares are closely held (members not exceeding fifty) and did not obtain their capital through public subscriptions.¹ British law is apparently more concerned about those investors who do not have the means or the power to control the company's accounting policies.

Similarly in the United States, the Securities and Exchange Commission regulates only those companies which resort to the public for capital. The SEC, however, delegates the right to determine competence to the States, thus:

The Commission will not recognize any person as a certified public accountant who is not duly registered and in good standing as such under the laws of his residence or principal office. The Commission will not recognize any person as a public accountant who is not in good standing and entitled to practice as such under the laws of the place of his residence or principal office.²

¹If the recommendations of the Jenkins Committee on Company Law, presented to the British Parliament on June 21, 1962, are adopted, this exception (as well as the one relating to Sec. 161 (2) (6), cited in footnote on p.30) with regards to the auditors of exempt private companies will disappear. (F.H. Jones, "The Jenkins Committee Report," The Accountants Journal, July 1962, p. 254).

²U.S., SEC, Regulation S-X, Art. 2.01(a).

In France too the law shows a concern over the public interest. It specifies that at least one of the auditors of shareholding companies (societes anonymes) raising their capital through public subscriptions should be chosen from a list of approved auditors drawn up by the Court of Appeal.¹ By controlling the qualifications of such auditors, official authorities theoretically guarantee the existence of a certain level of competence in the audit of publicly-owned companies.

In any case, the CPA certificate in the United States and the privately organized accountancy bodies in Great Britain afford the public a recognized measure of competence to guide their choice of auditors and protect them from pretenders to professional knowledge.

The law in Great Britain, as expressed in the Companies Act, 1948,² and other relevant acts,³ sets down, apart from the qualifications of auditors, the matters that

¹France, Law of July 24, 1867, as amended by Decree dated Aug. 8, 1935, Art. 33.

²G.B., Companies Act, 1948, Ninth Schedule.

³The Building Societies Act, 1960; the Charities Act, 1960; the Friendly Societies Act, 1896 to 1958; the Solicitors Act, 1957; the Prevention of Fraud (Investments) Act, 1958; the Larceny Act, 1861 and 1916; and the Falsification of Accounts Act, 1875. For a description of the auditor's duties under these acts, see Walter W. Bigg, Spicer & Pegler's Practical Auditing (London: HFL, Publishers, Ltd., 1962), pp. 338-341 and pp. 380-443.

auditors should expressly state in their report; in other words, it defines the minimum duties of the auditor.

Many countries, most Middle Eastern countries included, have based their definition of the auditor's duties in their legislation upon the provisions of the British Companies Act, 1948, as shall be discussed later on in the paper.

In addition, the law in both countries sets down additional provisions which affect the statutory auditor's performance of his duties. In the first place, British and, to a lesser extent, U.S. legislation defines certain basic accounting principles that management has to abide with in its preparation of the financial statements submitted to the responsible official authority.¹ The auditor should naturally see to it that management has complied with the provisions of the law.² In the second place, the law sets down the basic duties of the statutory auditor himself, in

¹Great Britain, Companies Act, 1948, Eight Schedule; and U.S., S.E.C., Regulation S-X, Art. 5. The British auditor is tied to the accounting requirements of the Companies Act, 1948 while the U.S. auditor is committed to "generally accepted accounting principles".

²It should always be remembered that financial statements are the management's representations and not the auditor's. The auditor's duty is to certify their fairness or, should he have any objection, to disclaim an opinion on all or part of the represented figures.

the form of matters that he should specifically state in his report,¹ thus defining the minimum scope of his examination and establishing upon him a definite legal responsibility.

The protection that legislation affords should not be overrated. In all its provisions concerning the auditors' qualifications and standards of duty the law sets down the acceptable minimum, and can only attempt to control the tangible aspects of the issue. It is not possible for the law to guarantee the necessary display of competence by the auditor in the performance of his duties. Thus a lot is really left up to the personal integrity of the auditor. This in turn depends to a large extent upon the professional traditions that the auditor grew up in.

This is where the role of respectable accounting societies comes in. They set their standards higher than the minimum imposed by the law; they extend them to cover the whole range of public accounting activities, rather than just auditing; and they try to build up a tradition of integrity, sound service, and high ethical standards for its members to live by.

The first service they render is to enable the public to identify professional competence by restricting their membership to well-trained persons. This contribution

¹Great Britain, Companies Act, 1948, Ninth Schedule; and U.S., S.E.C., Regulation S-X, Art. 202.

is especially valuable in those areas where membership in the accounting societies is the only gateway to professional status, as in Great Britain. Whereas in Great Britain there are no restrictions on public accounting practice other than those relating to the audit of limited companies, non-qualified practitioners find it difficult to build up a worthwhile clientele in view of the general recognition that members of the recognized accountancy bodies enjoy.

In the United States, public authorities have taken it upon themselves to identify professional competence. Therefore, membership to the state accountancy societies or to the national society (AICPA) is not in itself a sign of competence inasmuch as it is an expression of one's willingness to abide by the code of the majority.

The second contribution to competence that accountancy societies offer lies in their elaboration of this concept in their written codes of ethics (U.S.) or in the generally accepted standards of conduct which they enforce (U.K.). They try to make sure that the member applies in his work the foundation of competence that he has acquired. The competence standards that respectable accountancy societies -- whether British, American or otherwise -- enforce on their members in

public practice are generally along the following lines:¹

- a) The public accountant should not purport to perform more than his abilities or qualifications justify.
- b) The public accountant should not certify the results of any work not conducted, examined, or properly supervised by him or by another qualified person.
- c) The public accountant should not allow a person to practice in his name other than his employees or partners.
- d) The public accountant should perform his examination in accordance with auditing standards generally accepted as adequate and sufficient by the profession in his business environment or in his circle of professional affiliation.²
- e) The public accountant should acquire sufficient information to warrant the expression of an opinion on the financial statements.

¹Based upon: The AICPA, Code of Professional Ethics; J.L. Carey, Professional Ethics of Certified Public Accountants (N.Y.: The American Institute of Accountants, 1956); The Inst. of C.A.s in England and Wales, Members Handbook, Section E; Sir Thomas Robson, "Ethics for the Accountant in Practice", The Accountant, Apr. 23, 1960, pp. 478-483; and D.V. House, Professional Ethics (London: Gee & Co. Publishers, Ltd., 1956).

²The auditing standards generally accepted in the U.S. are in certain instances different from those of Great Britain. I have passed over some of them in Chapter II, Section 3.

2.- Independence

"Independence, in the sense of being self-reliant, not subordinate, is essential practice to all professions. It is part of professional integrity."¹ In auditing, however, the concept of independence acquires a special significance; it is the *raison d'être* of the function's existence.

The fundamental role of the 'independent' auditor is to present to the shareholders, whom he represents, or to the directors, who represent the shareholders, and to other parties (bankers, creditors, the investing public and official regulatory agencies) who might be relying on his opinion, a fair and unbiased evaluation of a firm's state of affairs. His opinion is thus rendered for the benefit of persons whom he does not normally know or have any relation with. His attitude should, therefore, be that of a complete detachment from the interests of any of the parties involved in an assignment, including his own and those of the party which hired him. He should always be motivated by a desire and an insistence to tell the truth, unembellished and undistorted, regardless of the results, if he is to maintain public confidence in the profession's role as guardian of investors' interests. He stands not as a servant of the client, as is the case in other professions, but as a servant of the public. The public's faith in him stems not from its

¹Carey, Op. Cit., p. 20.

faith in his individual abilities, as these are not universally known, but from its faith in the whole profession.

The concern over the independence of auditors has been stressed in the laws. Practically all laws disqualify an accountant's appointment as a statutory auditor if he is in any way connected with the company's operations.

British company law disqualifies an auditor's appointment as the statutory of a limited company if he is an officer or servant, or a partner of an officer or servant, of the company, or if he is acting as a body corporate.¹

French law further disqualifies the statutory auditor if he is related to the fourth degree to any of the company's directors. In addition, a statutory auditor cannot be elected to the company's board except after five years from the cessation of his services as an auditor of that company.²

In the United States, the SEC's regulations attempt to cover the whole independence concept. They disqualify an auditor if he has a direct financial interest or an indirect

¹Great Britain, Companies Act, 1948, Sec. 161 (2).

²France, Law of July 24, 1867 (as amended by Decree Aug. 8, 1935), Art. 33.

material financial interest in the subject company,¹ or when any of his relationships with the company are such as to be considered by the SEC as affecting his independence.²

Another basic factor in the auditor's independence is the problem of his appointment. When appointed by the management or by the directors the auditor might become subservient to their interests. To avoid this possibility, British company law vests the authority in the shareholders who are to appoint the auditors annually in a general meeting and fix their remuneration,³ and it is to the shareholders that the British auditor addresses his report.

A basic difference in U.S. legislation, which could probably explain the over-publicized concern over the auditor's independence, is the absence of any provisions as to the group in whom the authority to appoint auditors is vested. To avoid the possibility of auditors becoming indebted to management for their appointment, many U.S. corporations have delegated the responsibility to the board

¹Such a provision is usually found in countries influenced by U.S. legislation such as Mexico and Japan. (L. Rappaport, SEC Accounting Practice and Procedure, N.Y.: The Ronald Press. Co., 1963, pp. C.1 - C.14.) It is not common in countries affected by the British influence. The U.S. attitude probably stems from an over-consciousness of the reliance that the business community, other than shareholders, place on the auditor's report.

²U.S., SEC, Regulation S-X, Art. 2.01 (b) and (c).

³Great Britain, Companies Act, 1948, Sec. 159.

of directors, who are considered more detached than the management from the operations of the business, while some corporations have placed the final responsibility with the shareholders by having the board of directors submit for their approval the nominated auditors.¹

Laws, obviously, can only refer to specific situations where the auditor's susceptibility to partiality in attitude is apparent, and then only with regards to statutory audits. They cannot, however, cover the whole issue. An auditor might lose his objectivity more by his fear of losing a client than by his being a relative of a director or officer. Independence, being basically a mental attitude, becomes more a question of personal integrity than an enforceable well-defined regulation. The new rule 1.01 of the AICPA's code of Professional Ethics clearly shifts the issue to the auditor's own sense of integrity by stating:

Independence is not susceptible of precise definition, but is an expression of the professional integrity of the individual. A member or associate, before expressing his opinion on financial statements, has the responsibility of assessing his relationships with an enterprise to determine whether, in the circumstances, he might expect his opinion to be considered independent, objective and unbiased by one who had knowledge of all the facts.

In British practice, where the code of ethics is unwritten, more is left to the personal integrity of the individual accountant. Nowhere in the law or in the official

¹Stettler, Op. Cit., p. 32.

statements of accounting societies is there any specific mention of an auditor's disqualification from appointment should he have any financial interest in an enterprise or should he have any blood or marital relationship to the enterprise's executives. Mr. V. D. House aptly sums up the attitude of the British profession in this respect:

It would in my view be a sad reflection on the integrity of chartered accountants if we had to consult a large family tree, or to count our shareholdings, before deciding whether we were eligible in law for appointment as auditors.¹

A recent statement issued by the Institute of Chartered Accountants in England and Wales on the subject of displacement of auditors touched upon the essence of the independence question in the auditors' relations with the company's directors. The statement was prompted by the problem created by the proposal of the directors of the City of London Real Property Company to the shareholders requesting them to replace their present auditors because of an unreconcilable difference of opinion between the directors and the auditors. The Statement said:

.....

4.- The fact that auditors disagree (with the accounts submitted by the directors), if they do so, is not a justification for their displacement unless the reasons for their disagreement are such that the shareholders no longer have confidence in the judgement, competence or conduct of the auditors as their representatives.

¹House, Op. Cit., p. 57.

5.- Confidence between directors and auditors whilst obviously desirable, is not indispensable for the adequate performance by the auditors of their onerous duties on behalf of the shareholders; indeed in some circumstances the performance of those duties may lead inevitably to differences of opinion between the directors and auditors and to a report to this effect by the auditors to the shareholders.

6.- The existence of such a possibility is among the reasons why auditors are appointed. The work of auditors and their freedom to perform it with a sense of complete independence can only continue as long as it is generally accepted that the issue by auditors of a report expressing disagreement with the directors of a company of which they are auditors does not of itself provide a reason for the removal of auditors from office. The purpose implicit in the appointment of auditors under the Companies Act would be defeated if there were to grow up a practice of displacing auditors whenever a disagreement between them and the directors of a company occurs on a matter of accounting principle.¹

Professional societies, in the ethical standards they enforce upon the profession, try to take over where the law leaves off. Apart from stressing the factor of personal integrity in the concept of independence, they specify certain practices and circumstances which public accountants should strictly avoid if they are to act in an independent capacity; such as:²

¹The Institute of Chartered Accountants in England and Wales, "The Displacement of Auditors," as quoted in The Accountants Journal, July 1963, p. 266.

²Based upon: The AICPA, Code of Professional Ethics; Carey, Op. Cit.; The Inst. of C.A.s in England and Wales, Members Handbook, Section E; Robson, Op. Cit.; and House, Op. Cit.

- a) Accounting services which take the form of original work on accounting records or put the auditor in a decision-making capacity with regards to the accounts (or with regards to any of the company's operations, for that matter). This would disqualify the auditor from certifying the financial statements of a company, since he would be certifying his own work.
- b) Intentional non-disclosure of a material fact or point of principle in the report, or rendering an opinion without basing it upon an examination sufficient to justify an opinion. This would imply subordination to the client's interests, if not outright collusion.
- c) Financial interest, either in the form of shares in material amounts in relation to the company's capital or to the auditor's personal fortune, or in other forms such as loan transactions or outside business relationships between the auditor and his client.
- d) Fees contingent upon results (such as those calculated as a percentage of profits or sales). The auditor's independence in such cases would be impaired by becoming involved with the destinies of the company.
- e) Sharing of fees with persons not in public accounting practice. Apart from being unethical, the practice of paying a commission or part of the fee to persons outside the profession for referring him assignments would place the public accountant in a subordinate position with

regards to the assignment and to the person who referred it.

- f) Non-communication with the previous accountant of a client before accepting an assignment inquiring as to the professional reasons behind the client's decision to shift. This is mainly a British practice not required in the American profession, but voluntarily followed by a large number of American firms.¹ This practice strengthens the auditor's independence vis-a-vis the client. Should the client insist upon misrepresentation or concealment of facts and refuses to accept the auditor's qualified report on the accounts, he would find it difficult, with this system of communication between public accountants, to obtain another accountant's unconditional certificate.

Public accountants in Great Britain or in the United States are not only concerned with abiding by the text of the law or with maintaining their integrity and objectivity, but also with appearing so in the eyes of the public. They try to avoid any relation which might be interpreted as affecting their impartiality of attitude. Many public accounting firms, especially the larger ones, bar their partners and staff from owning any shares, even in immaterial amounts, in their

¹Carey, Op. Cit., p. 190

clients' companies.¹ Apart from insuring the independence of the firm, this practice would preclude the use of any inside information obtained during an audit for personal benefit, and would above all assure the public of the firm's complete independence in the assignment.

3. Integrity and a Sense of Public Service

It is a truism that integrity and a sense of public service are at the basis of behavior of every professional man. Public accountants, as servants of the public, are no exception; their professional and personal integrity should be above reproach, especially that they are entrusted with the secrets of many businessmen and that one auditor can very well serve a number of clients in a competing line of business. The list of matters which can affect integrity can become endless. Professional accounting societies specify some of the more common instances, and cover the whole subject by providing that their members are not to perform any acts discreditable to the profession, leaving it to the societies' councils to determine the discredibility of any act as the problem arises. The rules pertaining to integrity which are most often stressed are:²

¹For example, a partner in Price, Waterhouse & Co. is barred from owning shares in 400 companies listed on the stock exchange. (T.A. Wise, "The Auditors Have Arrived," Part II, Fortune, Dec. 1960, p. 147.)

²Based upon: The AICPA, Code of Professional Ethics; Carey, Op. Cit.; The Inst. of C.A.s in England and Wales, Members Handbook, Section E; Robson, Op. Cit.; and House, Op. Cit.

- a) Violation of the confidential relationship with a client.
- b) Negligence in the performance of one's duties.
- c) Advertising or publicity of any kind; including press notices or advertisements, circulars or direct solicitation of business. The profession maintains that the only allowed promotional activity is competence and good service. The intention is to protect the public accountant's independence and the performance of his practice in a dignified atmosphere unmarred by the detrimental effects and loose morals of unbridled competition. On the same principle, price-cutting is forbidden and competitive bidding is frowned upon.
- d) Incorporation of public accounting practice. Public accounting services are based upon the personal element, and incorporation, in an attempt to avoid the assumption of one's full financial responsibilities, is forbidden.¹ This is common in the U.S. and U.K. in all professional bodies conferring a professional status on their members.²
- e) Engaging in a business which is not compatible or consistent with public accountancy, or holding positions which are not compatible with assignments handled in the capacity of independent accountant (as, for example, auditing one firm while holding an executive position in a competing firm.)

¹France and Germany allow incorporation of public accounting practice.

²Colin A. Perry, "The Use of Unlimited Liability Companies by Professional Persons," The Accountants Journal, Nov.1960, p.493.

CHAPTER III

THE DEVELOPMENT OF PUBLIC ACCOUNTANCY
IN THE MIDDLE EASTA. Origins

Public accountancy as a profession can exist only in a developed economic environment. The very existence of independent audits assumes a business structure the backbone of which is the shareholding company. The other public accounting activities, such as taxation and management services, are of any significance only under a developed fiscal system and in an expanding industrial economy. Otherwise, whatever public accountancy exists is more of the nature of public bookkeeping.

In the Middle East, as in all other areas, the development of public accountancy as a local profession is thus closely related to the development of the shareholding company. It is also greatly affected by the type of foreign influence, economic and legislative, that the local business practices were subjected to.

Before 1945, the Middle East was characterized by a widely underdeveloped -- in some cases, primitive -- economic structure. The predominant business unit was the sole proprietorship or the simple partnership. Shareholding

companies were, apart from Egypt, few in number and mostly foreign-controlled. In the few cases where shareholding companies were locally-controlled, they were characterized by a concentration of ownership in the hands of a few.

Such an environment does not induce the growth of a local public accounting profession. But the presence of foreign interests, either in the form of branches of foreign firms or in the form of control over local shareholding companies, induced the establishment of a foreign public accounting profession.

Foreign enterprises, more advanced in character than the surrounding economic environment, demanded qualified independent auditors. The British profession was the only one developed enough internationally to provide such services.

Generally speaking, it can be said that the British accounting profession travelled with British economic expansion. This is far enough in itself, but it travelled much further than that. The demand for the services of British accountants was almost universal due to the tremendous goodwill that they had built up for their profession all over the world.

Other than that, the British profession set the pattern of development of local accounting professions in most of those countries with which it came in touch and for a long time remained the fountainhead upon which they drew for their standards, principles and form of professional organization.

The high esteem of the British accountancy bodies, and their willingness to admit foreign members, naturally interested a few locals -- first in Egypt, then in the other Arab countries. These persons were, and still are (with one exception: Dr. Fauzi Saba, CPA), the only professionally qualified accountants in the area, and the only real constituents of the local public accounting profession.

The origins of professional public accounting practice in the Middle East are thus basically British. The British profession came to be established as a by-product of foreign economic expansion to serve a clientele of foreign-owned or foreign-controlled firms. For a long time since, British accounting firms dominated the field, even after the entry of qualified local accountants.

With the gradual progress of economic activity an increasing number of local practitioners entered the public accounting field. In the absence of any local measures of professional competence, memberships in the British accountancy bodies were the only qualifications sought by enterprising Arab accountants. There were always more such qualified accountants in Egypt than in the other Arab countries due to the country's earlier development and broader economic structure. Actually, only Egypt had before 1948 any local chartered accountants in public practice.¹

¹There was in Lebanon a Mr. Noel Kahla, chartered 1937, but he was not in public practice.

There was a total of seven Egyptian chartered accountants in Egypt in 1946.¹ Outside Egypt, only Palestine then had any professionally qualified public accountants -- three certified accountants.² In the other Middle Eastern countries, the economies were so underdeveloped that no public accountancy could possibly have existed at the time, or whatever public accounting services the business community required were provided by the British firms.

There was of course a number of non-professionally qualified practitioners; but their field of practice did not generally extend much beyond the provision of accounting services to the smaller businessmen and the performance of some small audit jobs. This is characteristic of public accountancy in the early stages of its development.

The qualified local accountants of Egypt and Palestine were themselves very active in accounting services. With the advent of fiscal legislation, they started becoming involved in tax work, though this never amounted to a sizeable portion of the practice as a whole, except in later years in Egypt. With the British accounting firms controlling most of the important audit assignments, the qualified local practitioners

¹The Royal Egyptian Society of Accountants and Auditors, Statutes and Bye-Laws (Cairo: 1946), Art. 7 of Statutes.

²Mr. Fuad Saba, certified 1929; Mr. Fuad Hawit, certified 1941; and Mr. Karim Khouri, certified 1947. There was in Iraq a Mr. Shawki Dallal, certified 1937, but he was not in public practice.

had to depend upon such other activities to maintain themselves in practice.

Even with the presence of a few local qualified accountants, public accounting remained until very recently virtually a foreign domain. The market superiority that British accounting firms for a long time enjoyed can be attributed mainly to the following factors:

- a) The world-wide reputation of British accountants, plus their being the first ones, and for a long time the only ones, to practice in the area.
- b) The presence of extensive foreign interests in the economy, including control over a great number of locally-registered companies.
- c) Until local accountants became well-established, an auditor's certificate signed by a British accountant rated much higher in financial and commercial circles. For one thing, it weighed much more in international business relations; for another, the area's financial sectors were largely dominated by foreign, especially British, interests.
- d) The stable tendency of audit assignments. Reputable, well-established firms do not normally change auditors unless the reasons are overwhelming, so as not to create any suspicion in the minds of interested parties.

B. The Influence of Legislation

1.- General

In those countries falling under British dominance, the economic role of the auditor received official and business recognition in much the same manner as in Great Britain. British dominance carried with it a business philosophy which included well-developed concepts of independent audits. This had a profound influence upon local legislation and business practices.

2.- Iraq and Palestine

The first countries to adopt any advanced corporate legislation, including well-developed audit provisions, were Palestine and Iraq in 1919. The Companies and Partnerships Ordinance passed in Palestine in May 1919 was based upon companies legislation prevalent in Great Britain.¹ The Commanding-in-Chief of the British forces in Iraq decreed in June 1919 that the Indian Companies Act No. 7 of 1913 with its amendments be applied in Iraq.² The Indian Companies Act was in turn based upon British law.

¹Palestine, Ordinance No. 118 of 1919 (The Companies & Partnerships Ordinance, 1919). (N. Bentwich, ed., Legislation of Palestine, 1918-1925, V. I; Alexandria: Whitehead Morris, Ltd., pp. 213-244.)

²G.F. Macmunn, Major-General Officiating Commanding-in-Chief, Mesopotamia Expeditionary Forces, Companies Proclamation, 1919.

With regards to independent audits, the provisions in both countries were generally the same. They provided for:¹

- a) The independence of the auditor: Directors or officers were disqualified as auditors.² The auditor was to be appointed by the shareholders.
- b) The competence of the auditor: He has to be properly qualified by membership to some approved society or institute, or be licenced by the government.³
- c) The rights of auditor: He has the right of access at all times to the books, accounts and vouchers of the company and is entitled to require from the directors all information he deems necessary.
- d) The duties of the auditor: He shall report to the annual general meeting of shareholders, stating: (1) Whether he has obtained all information and explanations he

¹Palestine, The Companies & Partnerships Ordinance, 1919, Secs. 74-79; and The Indian Companies Act No. 7 of 1913, Secs. 144-145.

²The Indian Companies Act also disqualified partners or employees of officers or directors.

³The Palestinian Ordinance also admitted properly qualified university graduates.

required; and, (2) Whether, in his opinion, the balance sheet was drawn in conformity with the law, and whether it exhibits a true and correct view of the company's affairs.¹

The Companies Ordinance, 1929, of Palestine maintained basically the same auditing provisions of the former act. The only important addition was that corporations and partners or employees of officers or directors were prohibited from acting as auditors.²

The Companies Ordinance, 1929, remained in force in Palestine until 1948 and, after that, in the Palestinian part of Jordan until 1962 when a new companies law was enacted and made applicable for the whole of Jordan.

The Indian Companies Act remained in force in Iraq until 1957 when it was replaced by an Iraqi companies Law. In 1958, public auditing in Iraq became governed by a special law regulating entry into the profession.

¹In Palestine, a sample certificate recommended in 1922 for cooperative societies (which, at the time, had nearly the same audit provisions as limited companies) read as follows: "I/We having had access to all the Books and Accounts of the Society and having examined the foregoing Balance Sheet and verified the same with the Accounts and Vouchers relating thereto, now sign the same as found to be correct, duly vouched and in accordance with the law." ("Balance Sheet of Funds and Effects Prescribed by Regulations under Cooperative Societies Ordinance, 1920," June 22, 1922; appearing in Bentwich, op. cit., V. II, p. 26.)

²Palestine, Companies Ordinance, 1929, Sec. 105. (R.H. Drayton, ed., The Laws of Palestine, 1933, V.I. London: Waterlow & Sons, Ltd., 1934, pp. 161-355.)

3.- Syria and Lebanon

Syria and Lebanon, which fell under French dominance, were, as far as public accountancy is concerned, at a disadvantage in relation to the countries falling under the British. France had no developed public accounting profession to export; and its commercial legislation, which was at first the model for Ottoman legislation and later for Lebanese and Syrian legislation, reflected an undeveloped view of independent audits, widely divergent from the advanced concepts of the British.

The French occupation authorities did not attempt to effect any major alterations in the Ottoman Commercial Code in force in both Syria and Lebanon since 1850 (1266 hegira). The Ottoman Commercial Code was actually nearly an exact translation (and a poor one at that) of the French Commercial Code of 1807 which carried no provisions on the appointment of auditors by shareholding companies.¹

When the French law governing shareholding companies was completely modified on July 24, 1867 (to include, among other things, provisions for independent audits), the Ottoman Code was not amended accordingly.² The Ottoman authorities, however, published in 1882 a model set of articles of

¹R. Lahoud, "Les Commissaires de Surveillance dans les Societes Anonymes," Rev. Jud. Lib., 1946, p. 21

²R. Antaki, Commercial Law (Damascus: Syrian University Press, 1948), p. 146, (Arabic).

association for shareholding companies based upon the French Law of 1867.¹ These articles did not have the strength of the law, but the administrative organs of the government made them in fact compulsory by imposing upon shareholding companies to correspond their articles very closely to the model articles if they are to obtain government sanction.²

The model articles remained the only real guide to the organization of shareholding companies in Lebanon until 1943, when the Lebanese Commercial Code was enacted, and until 1949 in Syria, when the Syrian Commercial Code was enacted.

The model articles, based upon an outdated French law and never amended in line with the reforms that France introduced in its law in 1935, did not exhibit any real appreciation of the role of the professional auditor in the economy. They carried no provisions regarding the auditor's competence or independence (other than the stereotyped clause that he should be appointed by the shareholders). The Law of 1867 never stimulated the development of a serious public accounting profession in France; its imitation in Syria and Lebanon achieved no better results.

The Lebanese Commercial Code of 1943 did nothing to improve the professional standards of auditing in the country. Apparently as an admission of their inability to

¹Ibid.

²Ibid.

solve the problem of the auditor's competence, the legislators of 1943 devised the concept of two auditors: One appointed by shareholders and another by the court. No qualifications were demanded of the first one. The guarantee of competence is theoretically provided by the other auditor under the assumption that his qualifications are controlled by the government.

The Syrian Commercial Code of 1949 was an improvement, at least in theory, over the Lebanese in this respect. It defined certain elementary duties for the auditor and admitted the principle of the auditor's competence by providing that he should be licenced; though the law regulating such licencing was passed only in 1958.

In both Syria and Lebanon, British and Arab qualified accountants have exercised a considerable influence upon professional practice. But the wrong start had already created in business attitudes towards public audits certain distortions which have weakened, not to say hindered, the growth of the profession and the assumption of its true role in the economy; even though in France itself steps were and are being taken to eliminate the imperfections.¹

¹Such as the amendments of the Law of July 24, 1867 by Decree of Aug. 8, 1935 and Decree of Aug. 31, 1937, Law of April 3, 1942 creating the Ordre des Experts Comptables et des Comptables Agrées, and the private efforts of the Institut Francais des Experts Comptables.

4.- Egypt

In spite of the relatively large number of shareholding companies, legislation in Egypt did not specifically provide for independent audits before 1954. Until then audits were compulsory for shareholding companies only by indirect inference and actually dictated more by generally accepted business practice than by definite legal requirements.

Audits were first referred to in legislation in 1923¹ in a government decree which stated: "The documents representing the company's year-end condition (balance sheet, statement of profit and loss, and the reports of the board of directors and the auditors) shall be published in full in two newspapers..."²

It appears from this side reference that the concept of independent audits was recognized enough by Egyptian companies at the time for the government to take it for granted. This is understandable considering the widespread foreign influence in the economy.

In 1926, the auditor received more official recognition when the Legal Committee of the State (Le Comite du Contentieux) approved a model set of articles of association for companies' guidance. These included the first detailed

¹Sami B. Ghali, Companies (Cairo: Kamaliya Press, 1952), p. 122. (In Arabic.)

²Egypt, Decree on the Organization of Companies, July 18, 1923, Art. 4. (V. Sisto & Y. Shalaleh, ed., Permanent Compendium of Egyptian Legislation, "Shareholding Companies," p. 4; in Arabic.)

audit provisions to appear in an official manner in Egypt.¹

The only change that came about over the years in the auditing provisions of the above articles was the requirement, which appeared in the 1945 edition, that the auditor must be Egyptian.²

In the period 1950-1955, the independent auditor acquired a great significance in Egyptian legislation. Three major events taking place during that period are indicative of the heavy reliance that official authorities came to place upon the independent accountant.

First, a public accountancy law was passed (Law No. 133 of 1951) restricting admission to public practice to persons with certain minimum standards of qualifications.

¹They stated that the auditor is to be appointed annually by the shareholders, who are to fix his remuneration; that he is to ascertain the directors' compliance with the company's statutes, to check the inventory lists, the year-end accounts and balance sheet, and to report thereon to the shareholders; and that he has the right to check the company's cash and securities at any time and to call, in cases of utmost necessity, an extraordinary meeting of shareholders. (Egypt, Legal Committee of the State, Model Articles of Association, Feb. 23, 1926, Arts. 36-40; as appearing in A. Sfeir, ed., Collection of Laws & Statutes, Cairo: 1940, pp. 1171-1172.) These model articles were in large part based upon the French Law of July 24, 1867 and were published in Egypt at the time only in the French language.

²Egypt, Legal Committee of the State, Model Articles of Association, Jan. 14, 1945, Art. 36. (V. Sisto & Y. Shalaleh, ed., Permanent Compendium of Egyptian Legislation, "Shareholding Companies," p. 14; in Arabic.)

Second, company legislation was finally organized by Law No. 26 of 1954 which drew heavily upon British legislation, especially in its very elaborate accounting and auditing provisions.¹

Third, in 1953, an amendment to the income tax law provided for the first time that all tax returns (with a few exceptions regarding small businesses) have to be certified by independent accountants.²

Furthermore, the government greatly depended upon the independent auditor in its efforts to supervise all those organizations involving a public interest. Labor unions, brokerage houses,³ banks, insurance companies, charitable institutions ... were all subjected to special audit requirements.

¹The full name of the law is "Law No. 26 of 1954 Covering Certain Regulations Pertaining to Shareholding Companies, Partnerships Limited by Shares and Companies with Limited Liability", but for brevity's sake it is referred to just as Law No. 26 of 1954.

²There are no similar regulations in Great Britain or the United States. In those countries, it is a general business practice to seek the public accountant's assistance in the preparation of tax returns, and tax authorities always prefer to have certified tax returns; but the law does not make this a compulsory requirement.

³The audits imposed upon brokerage houses were among the earliest statutory audits in Egypt. (See chap. iv, sec. A-3.)

C. Early Professional Structure

1.- Egypt

a) A foreign-influenced start -- The early existence of shareholding companies in Egypt in significant numbers explains the earlier development of public accountancy there. As early as 1929 there were in Egypt 232 shareholding companies with principal operations in Egypt. In 1937, the number rose to 332; in 1946, to 375; and in 1954, to 506.¹

The above figures include a few companies registered outside Egypt. But even those which were registered in Egypt were dominated by foreign interests,² which again explains the early consciousness of the need for public accountants and

¹Egypt, Ministry of Finance and Economy, Annuaire Statistique, 1929/30, pp. 611-623; 1941/42, pp. 662-681; 1945/47, pp. 622-649; and Census of Shareholding Companies with Principal Operations in Egypt, June 1953 and 1954 (Cairo: 1956).

²Since the shareholding company was first recognized in Egyptian legislation in 1883 (The National Code of Commerce, Nov. 12, 1883, art. 32-45) until 1947, foreign ownership of shares was subject to very little restrictions. Government decree dated July 18, 1923, tried to bring about some egyptianization by stipulating that at least 25% of the shares must be offered for subscription in Egypt (without specifying whether the subscribers were to be Egyptians) and that at least one of the directors must be Egyptian. In 1927 (per Decree dated May 31, 1927) Egyptians were to participate in at least 80% of the shares offered for subscription in the country (i.e. 20% of all new capital subscriptions) and the minimum number of Egyptian directors was raised to two. In 1947 (per Law No. 138 of 1947, art. 4 & 6), the minimum number of Egyptian directors was set at 40% and Egyptian participation in subsequent capital subscriptions at 51%. Law No. 120 of 1952 later reduced minimum Egyptian ownership to 49%. (Sisto & Shalaleh, op.cit., pp. 1-15.)

the dominance of British accountating firms which persisted until their withdrawal in 1956.

A certain researcher came up with the following estimates about the extent of foreign capital in Egyptian shareholding companies at the end of 1948:

TABLE 1
OWNERSHIP OF EGYPTIAN SHAREHOLDING COMPANIES

	<u>Egyptians</u>	<u>Foreign</u>	<u>Total</u>
	£E	£E	£E
Capital of companies established before 1933	6,006,635	60,733,751	66,740,386
Capital of companies established between 1933 and 1948	21,041,566	5,677,048	26,718,614
Increase in capital during 1933-48 distributed in same proportion as above	19,260,632	5,213,378	24,476,000
TOTALS	46,308,823	71,624,177	117,935,000

Source: A.F. Abatha, "Foreign Capital in our National Economy," Lecture given on Mar. 26, 1951; as quoted by Dr. A. M. El Bey, Foreign Investments in Egypt (Cairo: Cairo University Press, 1953), p. 18.

In percentage terms: At the end of 1933 only 9% of the capital employed in Egyptian shareholding companies was Egyptian. At the end of 1948, it was still only 39%.

b) British qualifications -- Due to this preponderant foreign influence, the British and, in later years, the British

qualified Egyptian accountants were always the most highly regarded.

The first public accountants in Egypt were the firm of Russel & Co., Chartered Accountants, who established their office there in around 1895.¹ Price Waterhouse & Co. followed sometimes in 1910-1920, and Hewat, Bridson & Newby in about 1920-1925.²

Before 1946, when the Royal Egyptian Society of Accountants and Auditors ("Royal" was dropped from the name in 1952) was formed, the only professionally qualified Egyptians were the chartered accountants.

The first qualified Egyptian to enter the field was Mr. Zaki Hassan, who became a chartered accountant in 1928. He was to remain in that position for nearly ten years.³

The number of British-qualified Egyptians started to increase after 1938. In 1952, they numbered ten chartered and five certified accountants. Nine of the chartered and one certified were in public practice (either full-time,

¹Personal interview with Mr. J. Scott Smith of Russel & Co., Beirut (formerly Cairo) on April 24, 1964.

²Ibid.

³There was at the time another Egyptian chartered accountant (A.M. Ahmad, chartered in 1930), but he was not in public practice.

including one who was a partner in Hewat Bridson & Newby, or part-time, as some of them were at the same time university professors).¹

By comparison, the British accounting firms had between them in 1952 fourteen British, one Egyptian and one other foreign chartered accountants (six with Russel & Co., four with Price Waterhouse Peat & Co., and six with Hewat Bridson & Newby).²

By 1963, the total number of Egyptian chartered accountants had risen to about thirty-eight, and certified accountants to about ten.³ But at this moment, the drastic changes that are coming over public accountancy in Egypt are reducing the number of those in independent practice. In fact, many of them are now out of Egypt, mostly employed or in practice in the other Arab countries.

¹Z. Hassan (chartered 1928); A. Tawakol (1938); A.K. El Ibyari (1940); A.M. Hamza (1940); Y. Nawar (1941); M. Mikhael (1952); M. El Gamal (1951); H.M. Ragheb (1951); and F. El Sawaf (1938) who was a partner in Hewat Bridson & Newby. Also M.K. Harouni (certified 1945). Based upon: The Inst. of CAs in England & Wales, List of Members, 1956; The A.C.C.A., Year Book, 1957-58; and Egypt, Ministry of Finance & Economy, Census of Shareholding Companies, 1953 and 1954.

²Egypt, Decree No. 191 Limiting the Number of Foreign Accounting Firms in Egypt and their Non-Egyptian Members, June 30, 1952.

³Based upon: The Inst. of CAs in England & Wales, List of Members, 1963, pp. 881 and 941; The A.C.C.A., List of Members, 1964, p. 459; and personal knowledge of those presently out of the country.

c) Egyptian qualifications -- In 1946, the Royal Egyptian Society of Accountants and Auditors was founded by nine Egyptians (seven chartered accountants and two university professors) and seven British accountants residing in Egypt.¹ Its proclaimed aim was "organising in Egypt the profession of accountancy and auditing with a view to maintain a high professional standard."² It was the first private attempt to organize public accountancy in any Middle Eastern country. Until 1964, when the Middle East Society of Associated Accountants officially came into being in Lebanon, the Egyptian Society remained the only privately organized accountancy body in the area.

After the formation of the Society in 1946, professional qualifications became more accessible to Egyptians. Other than the chartered or certified accountants who were admitted to the Society by virtue of their British qualifications, there were at the end of 1960 twenty-six other persons who had qualified solely through the Egyptian Society.³

The Egyptian Society was closely patterned along the lines of the British chartered institutes. It provided for

¹The R.E.S.A.A., op. cit., Art. 7 of Statutes.

²Ibid., Art. 2.

³In 1960, the Egyptian Society had a total membership of 67 persons, 32 of whom were also chartered accountants and 9 were certified. (Based upon a privately-distributed list of members issued by the Society in 1960.)

a period of articles (apprenticeship) to be completed by candidates and for a series of examinations sponsored by the Society. Articled clerks had to be the holders of a bachelor's degree in commerce or its equivalent.¹

Candidates for the Society's membership had to be residents of Egypt. Apparently, no other Arabs cared to go to that trouble in order to qualify. Thus the only foreign members of the Egyptian Society were the British accountants residing in Egypt.

The Egyptian Society easily acquired the position of leader of the Egyptian accounting profession, due to its high standards of qualifications and the eminent status of its founders. Although the public accountancy law of 1951 did not give members of the Society a monopoly over statutory audits, yet it recognized their special qualifications. It gave them the right to audit shareholding companies without having to fulfill any other requirements, and provided that three of the eight members of the Committee administering the law were to be chosen from the members of the Society.²

The Egyptian Society is still in existence at present, but it is no more an active body.

¹The R.E.S.A.A., op. cit., Art. 9 of Statutes and Art. 35-43 of Bye-Laws.

²Egypt, Law No. 133 of 1951, on the Practice of the Profession of Accountancy and Auditing, Sept. 15, 1951, Art. 11 (1) and 15. (Sisto & Shalaleh, op. cit., "Accountancy and Auditing," pp. 2 and 4.)

d) Non-qualified practitioners -- Before 1951, when the first public accountancy law was passed regulating entry into Egyptian public accounting practice, the field was open to any person ready to call himself a public accountant.

Naturally, the field attracted a number of practitioners who had no recognized professional qualifications. The most important ones were those with university education and sufficient practical experience with the British accounting firms.¹ For all practical purposes, however, such persons could not be considered to constitute a significant element of the profession in a business atmosphere influenced, not to say dominated, by a foreign business mentality accustomed to the services of British chartered accountants. Their activities must have consisted primarily of bookkeeping or minor auditing services (a universal characteristic of public accountancy in the early stages of its development) and, after 1939, of tax advices to the smaller firms.

¹The Royal Egyptian Society of Accountants and Auditors allowed for the admission of such persons if they had reasonable standards of qualifications. Art. 5 of its Statutes states: "The Council may, at their discretion, invite persons who have been in Practice as Public Accountants in Egypt for at least ten consecutive years prior to 31st December 1943 to become Members of the Society." Similarly, Law No. 133 of 1951 (art. 11 and 12) recognized their acquired rights to practice.

2.- Palestine

The first non-Jewish accountants to practice in Palestine were again the firm of Russel & Co., who established their Palestinian office in about 1924.¹

They were shortly followed by a Palestinian Arab, Mr. Fuad Saba, in 1929. Mr. Fuad Saba, who became a "Certified Accountant" from England in 1929, was the first Arab outside Egypt to establish an independent accounting practice.

The firm Saba & Co. which was founded by Mr. Saba probably did more to affect the practice of accountancy in the Arab countries than any other institution. In a number of Arab countries, Saba & Co. remained for many years the only firm of qualified Arab accountants. It is still the only accounting firm with branches in practically every part of the Arab world.²

In the persons of Mr. F. Saba and his partners, Palestine has thus played a major role in the development of public accountancy in the Middle East, in spite of the limited number of qualified accountants it produced. All existing indications suggest that it will continue in that role for many years to come.

¹Personal Interview with Mr. J. S. Smith.

²Saba & Co. presently has branches in every Arab country except the U.A.R. (where it only has a representative) & Algeria.

3.- Syria and Lebanon

Public auditing was of very little economic importance in Syria and Lebanon before the second world war -- and less so in Syria than in Lebanon. In 1948, a directory published by the Banque de Syrie et du Liban listed 77 active shareholding companies registered in Lebanon, of which 31 were registered before 1940, and 46 in the period 1941-1948.¹ The same directory listed another 31 foreign shareholding companies with branches in Lebanon at the end of 1948.² A similar directory for Syria listed 37 active Syrian shareholding companies, of which 7 were registered before 1940, and 30 in the period 1941-1948.³ Foreign shareholding companies (excluding Lebanese companies) with branches in Syria amounted at the end of 1948 to 16.⁴

In such an environment, public accountancy was late to develop; and, due to the complete freedom of entry into the practice that the law allowed (until now in Lebanon and until 1958 in Syria) and unenlightened businessmen encouraged, there never developed a respectable public accounting profession in

¹Banque de Syrie et du Liban, Annuaire 1948 -- Principales Societes Exercant une Activite au Liban (Beirut: Imprimerie Catholique, 1949) pp. 101-393.

²Ibid.

³Banque de Syrie et du Liban, Annuaire 1948-1949 -- Principales Societes Exercant une Activite en Syrie (Beirut: Imprimerie Catholique, 1949) pp. 101-312.

⁴Ibid.

any of the two countries. There rather developed various categories of public accountants ranging from those professionally qualified by international standards to persons who do not rank very high in their accounting and auditing knowledge but who are ready to certify any set of financial statements for a fee.

Before 1940, Russel & Co. was the only serious firm of accountants practicing in Syria and Lebanon,¹ where it was established since about 1927.² Today in Lebanon, Russel & Co. is still one of the leading firms, if not the leading one, in the country. In Syria, though still registered, it does not have any regular Syrian clientele at present, but serves any of its occasional clients there from its Beirut quarters.³

In 1942, Saba & Co. started branching out of Palestine and established its Lebanese branch, which was later to become its head office. There was also in Lebanon Mr. Fouad Abou-Izzedin, an AUB graduate, who started practicing in the

¹F. Abu Izzedin, "Accounting Practices in Lebanon" (Unpublished Master's dissertation, Jafet Library, A.U.B., 1948), p. 12. (In Arabic).

²Personal interview with Mr. J. Scott Smith.

³Personal interview with Mr. Nuhad Ibrahim Pasha, public accountant in Syria, on May 21, 1964.

early 1940s,¹ and eventually became a "Certified Accountant" from England in 1951.²

In the 1950s, the public accounting field in Lebanon started growing at a very rapid pace. One of the developments is the large number of shareholding companies that were being established in the country, as well as the number of foreign companies operating in the country, as is illustrated by the following table:

TABLE 2
REGISTRATION OF SHAREHOLDING COMPANIES IN LEBANON

<u>During</u>	<u>Societes Anonymes Libanaises</u>	<u>Foreign Shareholding Companies</u>
1958	346	241
1959	436	246
1960	482	260
1961	578	278
1962	670	Not Available
1963	781	Not Available

Source: The Chamber of Commerce and Industry of Beirut.

Foreign shareholding companies operating in the country do not necessarily engage the services of locally-established accounting firms. A number of them are just small offices which do not require the services of an auditor

¹F. Abu Izzedin, loc. cit.

²The A.C.C.A., List of Members, 1964.

and a number of others are served by foreign auditors with no established offices in the country. Still, enough foreign companies do engage the services of locally-established public accountants to make it a worthwhile market. Naturally, only the internationally qualified accountants could cater to that market. In recent years, there has been a noticeable tendency for such qualified accounting firms to establish practices in the country. Until 1962, the internationally qualified accounting firms operating in Lebanon were Saba & Co., Russel & Co., Whinney Murray & Co. and Fouad Abu Izzedin. During 1963, the Egyptian firm of chartered accountants, Nawar & Co., and the British firm of chartered accountants, Keen, Talor & Co., have established permanent offices in Lebanon; and there are strong rumors that Price, Waterhouse & Co. might be establishing an office very soon.

In Syria, the public accounting market, and hence the number of public accountants, remained relatively limited. Saba & Co., in 1948, was the second firm to establish an accounting practice in Syria. During the 1950s, a few local accountants started to enter the field. By 1960, two relatively large accounting firms emerged: Saadi Tillo & Co. and Nuhad Ibrahim Pasha. But the recent economic and political instability of Syria, including nationalization, denationalization and renationalization of the bulk of Syrian shareholding companies, have adversely affected the activities of the few accounting firms established in Syria.

4. Iraq

The first professional accountants in Iraq were the firm of Whinney, Murray & Co., who were established there since 1929,¹ then mainly to serve the Iraqi Petroleum Company. They remained the only ones in the country until 1948, when Saba & Co. established its Iraqi branch.²

It was only in 1954 that the first Iraqi accountant entered into public practice. He was Mr. Nazhat Al-Tayib Al-Hawiz, chartered accountant 1954. Since then a number of Iraqis qualified as members of the British profession, but none of them seriously became public practitioners other than Mr. A.M. Al-Shamri who joined Al Hawiz as a partner. Some of them, however, were employed by the accounting firms.³

Due to the provisions of the Indian Companies Act, 1913, restricting entry into public practice only to those licenced by the Governor General or to those belonging to an

¹Personal interview with Mr. H. Traboulsi of Whinney Murray & Co., Beirut, on May 7, 1964.

²Personal interview with Mr. F. Saba.

³There are at present nine Iraqi chartered accountants and one certified accountant in the Middle East. Two chartered (Al-Hawiz and Al-Shamri) and the only certified (S. Dallal, certified 1938) are in independent practice, two are employed by Whinney, Murray & Co. in Iraq, and two by Saba & Co. in Libya. The other three chartered are privately employed, but two of them have part-time public accounting practices. There is also a British lady chartered accountant, Iraqi by marriage, who is in public practice. (Based upon: The Inst. of C.A.s in England & Wales, List of Members, 1963, p. 889; The A.C.C.A., List of Members, 1964, p. 431; and upon personal information.)

institute or society approved by the Governor General, there never developed in Iraq a category of semi-qualified accountants operating on the fringes of public practice, similar to what happened in the other Arab countries. The few public accountants that ever practiced in Iraq before the passing of the first public accountancy law in 1958 were all professionally qualified.

The public accountancy law of 1958, however, created two classes of public auditors: Auditors of Accounts, who are authorized to certify the financial statements of all companies without exceptions, and Licenced Accountants, who can certify the accounts of all companies but public shareholding companies.¹

Accounting consciousness in Iraq is such that British qualifications are considered foremost by all parties interested in external audits. British qualified accountants have dominated the field for so long that lesser qualified entrants cannot really encroach upon their established practices. This is strengthened by the preponderance of British business interest in the economy and by the fact that Iraqi businessmen have learned to expect more of their auditors than just to sign the certificate.

¹See chap. V, sec. B-3 for the qualifications required of each.

Therefore, the creation of the title of Licenced Accountant to certify the accounts of other than public shareholding companies had little, if any, effect on established professional practice. As of 1962, only two persons had qualified as Licenced Accountants and their practice remained insignificant in relation to the market as a whole.¹

5.- Jordan

What little public accounting services as were required in Transjordan before 1944 were provided from Palestine. The major accounting firms now operating in Jordan are the former Palestinian firms.

The first accounting firm to establish a permanent office in Transjordan was George Khadr.² The firm later came to be called Khadr, Ramadan & Co. as more partners were taken in. It was followed by Saba & Co. in 1946.³

In 1955, there was a total of nine accounting firms registered in the whole of Jordan.⁴ The most important of those, other than the above two, are: Russel & Co.,

¹The two persons are a certain Ahmad Abdel Razzak and Hikmat Miri. (Personal interview with Mr. Edward Haddad of Saba & Co., Baghdad, in February, 1964.)

²Jordan, Ministry of National Economy, Annual Statistical Yearbook, 1955, p. 110; and The Official Gazette, No. 1196, Sept. 16, 1954, Supp. 1.

³Personal interview with Mr. Fuad Saba on Mar. 12, 1964.

⁴Jordan, Ministry of National Economy, loc. cit.

registered in 1952,¹ Whinney, Murray & Co., registered in 1952,² and Fuad Hawit. The total number of firms is not presently available, as the source from which the above figure was obtained discontinued showing such details, but all of them, other than the ones mentioned, are occupied mainly in providing bookkeeping services.

In 1961, public auditing in Jordan became governed by a special law restricting the right to practice as public auditors only to those persons obtaining a special licence for the purpose.

6. Kuwait

The modern economic history of Kuwait begins in 1946 when oil production started.³ Since that date, the progress of business activity in the country has been stupendous.

The British authorities in Kuwait applied, as they did in Iraq, the Indian Companies Act, 1913, to regulate locally-registered companies.⁴

In 1960, Kuwait passed its own companies law (No. 15 of 1960), which included more elaborate auditing

¹Personal Interview with Mr. J. Scott Smith.

²Personal Interview with Mr. H. Traboulsi.

³S.H. Longrigg, Oil in the Middle East. Its Discovery and Development (London: Oxford University Press, 1955) p. 137.

⁴The Kuwait Order, 1953, Sec. 12. (Supplement to the Persian Gulf Gazette, Sup. 1, Oct. 1, 1953, p. 103.) For a summary of the auditing provisions of the Indian Companies Act, 1913, see the previous section about Iraq.

provisions than those previously in force. This was followed by Law No. 6 of 1962 regulating the practice of public auditing.

In spite of the rapid surge in economic activity in Kuwait, the number of Kuwaiti shareholding companies remained very limited. In 1962, they amounted to a total of 17 companies.¹

Public accountants have, however, found a broad market for their services in the numerous other types of companies which were being established mainly with the help of foreign entrepreneurs.

Since 1948, Whinney, Murray & Co. was established in Kuwait, then mainly to serve the Kuwait Oil Company.² Saba & Co. followed in 1954.³ By 1963, there was no less than six accounting firms operating in the country,⁴ aside from any single practitioners usually undertaking accounting services. Whinney, Murray & Co., with the huge KOC account in its portfolio, remains the largest accounting firm in the country;

¹Kuwait Chamber of Commerce & Industry Bulletin, July 1, 1963, p. 2.

²Personal interview with Mr. H. Traboulsi.

³Personal interview with Mr. Suhail Saba on May 13, 1964. (Saba & Co. was operating in Kuwait since 1948, but established its permanent offices there in 1954.)

⁴Whinney, Murray & Co., Saba & Co., Farid Mansour (chartered accountant), Nawar & Co., Issa El Ayyouti & Co., and Zahar, Hamed & Co.

on December 31, 1962, it had seven British chartered accountants on its staff.¹

7.- Saudi Arabia

Saudi Arabia's modern economic history also starts with the production of oil in commercial quantities after 1945.² The trend of the country's development has not been, however, comparable to Kuwait.

The country is still officially without company legislation. There was a complete draft of a companies law completed in 1960, but the Royal Decree which would release it never came -- the powerful religious "lobby" in Saudi Arabia has so far opposed the promulgation of such a law on religious grounds.

The government administration is, however, considering the proposed law as final and is in fact quietly applying it.

Professional practice in Saudi Arabia is thus unregulated. In any case, there are no Saudis in the practice. All accounting firms with established offices in the country are from the neighboring Arab countries.

¹The Institute of Chartered Accountants in England & Wales, List of Members, 1963, p. 1052.

²Commercial production was declared in 1938, but in the six years from 1939-1944 it averaged 5.1 million barrels yearly. In 1950, production reached 200 million barrels; in 1955, 352 millions; in 1960, 455 millions, and in 1962, 554 millions. (Based upon ARAMCO's Report of Operations for 1955 and 1962.)

Egyptian public accountants are the strongest in the market: They have two major firms (Nawar & Co. and Issa El Ayyouti) with branches all over the country, and a few smaller single practitioners in Riyad and Djeddah. The other major firm is Saba & Co., also with branches all over the country.

It is peculiar of Saudi Arabia that some of the largest audit assignments are handled by firms with no permanent offices in the country. Russel & Co. handle some important assignments in Saudi Arabia from their Beirut offices, and a few Egyptian with no established offices in the country are responsible for a number of audits. But the most important case is ARAMCO, which is audited by Haskins & Sells from New York.

The public accounting situation in Saudi Arabia being as it is -- unregulated, unpracticed by Saudis and in many instances practiced from out of the country -- does not give any body much more to write about in the form of a serious analysis. Saudi Arabia will not, therefore, be included in subsequent discussion.

CHAPTER IV

PUBLIC ACCOUNTANCY IN EGYPT

A. Statutory Audits1.- Shareholding Companies

a) Law No. 26 of 1954 -- The basic features of the law with regards to independent audits of shareholding companies can be summarized as follows:¹

(1) Appointment of the auditor:

- (a) Shareholders are to appoint the auditors annually in a general meeting and to fix their fees.
- (b) Should the company have more than one auditor, at least one of them should be Egyptian.
- (c) The auditor should not be a director, officer, promoter, or connected in any other permanent capacity with the company's operations; nor should he be a relative to the fourth degree of any person thus connected.

¹Arts. 52-54.

(2) Duties:

To attend the general annual meeting of stockholders and to report:¹

- (a) That he has obtained all the necessary information;
- (b) That the company keeps proper books of accounts;
- (c) That the balance sheet and the profit and loss account are in agreement with the books;
- (d) That, in his opinion, the accounts give the information required by law and the company's articles in the manner so required, and that the balance sheet and profit and loss account clearly reflect the true position of the company at the end of the year and the results of its operations for the year;
- (e) That the stocktaking was carried in accordance with generally accepted principles consistent with the preceding year;
- (f) That no breach of law or of the company's articles, in a manner adversely affecting the company's operations or its financial condition, occurred during the year.

¹Sub-articles (a) - (b) are closely similar to the Ninth Schedule of the British Companies Act, 1948.

Law No. 26 of 1954 distinguishes between three types of limited companies:

- (1) The Shareholding company -- which can invite the public at large to subscribe in its capital;
- (2) The Partnership Limited by Shares;
- (3) The Company with Limited Liability -- which cannot invite public subscriptions, nor can it undertake insurance, banking or any business dealing with the public's funds; its members can consist of a minimum of two and a maximum of fifty natural persons.

Within the law the auditing provisions applicable to shareholding companies were made applicable to Partnerships Limited by Shares,¹ but there was no indication to their being made applicable to Companies with Limited Liability.² In the latter, when the number of shareholders exceeds ten, the examination of the books, checking of cash, negotiable securities and other documents, and the supervision of the preparation of the balance sheet and the annual report was vested in a supervisory board consisting of three shareholders.³

¹Art. 55.

²There was also no indication as to the appointment of auditors in the model set of articles of association for Companies with Limited Liability that the government published for guidance purposes.

³Art. 79. (French influence is apparent here; as practically the same requirements apply to the French "Societes a Responsibilite Limitee" having twenty or more partners. See E. Archaylis et. al., "Auditing", European Congress of Accountants, 1963, Papers, p. 101.)

The law, however, extended the provisions of compulsory audits by Egyptian auditors, (and in fact the publishing, in the special bulletin issued by the Ministry of Economy, of certified financial statements covering their Egyptian operations) to all branches, subsidiaries, offices or agencies of foreign limited companies operating in Egypt.¹

Theoretically, Law No. 26 of 1954 is still in effect at present. But many of its provisions, including those pertaining to independent audits, have either been superseded, acquired a different interpretation, or have just lost the purpose of their existence as a result of the nationalization measures which swept the country since 1960.

b) Other statutory requirements -- When a company invites public subscriptions to its shares, its prospectus must include (among other things) the names, qualifications and addresses of its auditors and their report on the content of the prospectus. If the invitation is for public subscription to an increase in capital, the prospectus must carry certified financial statements for the preceding two years of operations and a report, also prepared by the auditors, showing the assets and liabilities and profits and losses of the company for the past five years.²

¹Arts. 90-91.

²Egypt, Appendix to the Ordinance Describing the Information to be Set Forth in the Prospectus, Sept. 23, 1954, Sec. 1, Art. 12 & 18, & Sec. 5, Art. 1 & 2. (Sisto & Shalaleh, op. cit., "Shareholding Companies" p. 78.)

All adjustments to the company's capital, whether an increase or decrease, also involve the submission to the concerned government authority a certified set of financial statements, along with certain other special reports also certified by the auditors, about the company's old and amended capital structure.¹

2.- Tax Legislation

The introduction of the first income tax law in 1939, followed in 1941 by the excess profits tax, greatly broadened the scope of public accounting services, in much the same manner that they did in Great Britain and the United States. The complexities of taxes drove many businessmen -- the large corporate organizations as well as the unincorporated traders who most likely had no previous relations with public accountants -- to seek the expert advice of public accountants. Egyptian public accountants, whether professionally qualified or not, were to benefit most from this new development. For one thing, the smaller businessman seeking professional advice for the first time is more inclined to approach local, rather than British, experts with his problems. For another thing, taxation business requires a close connection with the staff of the tax departments, which local accountants can more easily cultivate.

¹Egypt, Decree No. 383 Regulating the Register of Applications for Establishing Shareholding Companies, Sept. 23, 1954. (Sisto & Shalaleh, op. cit., "Shareholding Companies," p. 81.)

The role of the public accountant as a tax expert became so well established in business practice that an amendment to the income tax law passed in 1953 made the auditor's certificate on tax returns a compulsory requirement for all companies, and for all individual taxpayers with a capital in excess of £E 1,000 and employing more than ten workers, or with annual profits in excess of £E 600.¹

The amendment is an obvious recognition of the independent nature of public accountancy. It relies heavily upon the professional integrity and ethics of public accountants to regularize the relations of the private sector with the fiscal authorities.

Naturally the amendment gave the public accounting profession a new stimulus. It caused a vast number of unincorporated traders and individuals to seek the services of public accountants; (the larger business firms were already resorting to their public accountants anyway for tax assistance).

The public accountancy law of 1951 allowed public accountants of lesser qualifications than those required of the auditors of shareholding companies to certify the accounts and tax returns of unincorporated businesses. More

¹
Egypt, Law No. 253 of 1953 Amending Certain Provisions of Law No. 14 of 1939, May 31, 1953, Art. 1 amending Art. 43, 44 & 48 of Law No. 14 of 1939. (Sisto & Shalaleh, op. cit., "Taxes," p. 250.)

of the expansion caused by the 1953 amendment to the income tax law naturally accrued to these smaller accountants than to the larger accounting firms. Even in the absence of anything else in their favor, their fees for such services being normally much lower than those of the larger accounting firms is enough to make them dominate this particular section of the tax services market. In fact, at least one of the larger accounting firms, Russel & Co., never, as a policy, certified tax returns. The determination of the tax liability usually involved negotiations with tax officials which the firm preferred not to be associated with, although it used to offer tax advice to its clients.¹

3. Other Statutory Audits

Although relatively unimportant in relation to the whole scope of professional practice, the following instances are significant examples of the extent to which the official authorities came to depend upon the independent auditor in their attempt to protect the public interest:

- a) Since the early 1930s, brokers on the Egyptian Exchanges (the Stock Exchange, Commodities Exchange and Spot Sales Exchange) had to have their accounts examined by independent auditors appointed by the exchange boards, in order to ascertain the soundness of the broker's financial

¹Personal interview with Mr. J. Scott Smith.

position, his possession of the required amount of capital and his compliance with the regulations of exchange in the preparation of his accounts.¹

- b) In 1952, labor unions were required to submit certified financial statements to the labor office in whose jurisdiction the union falls.²
- c) Banks were required in 1957 to have their accounts examined by two auditors. An auditor was not allowed to audit the accounts of more than two banks, nor was he allowed to obtain a loan, secured or unsecured, from the bank he audits.³
- d) All private societies with total assets exceeding £E1,000 were required in 1956 to have their accounts examined by an authorized auditor.⁴

¹Egypt, Regulations of the Commodities Exchange, Nov. 5, 1927, Art. 20 as amended by decree dated July 31, 1930; Regulations of the Cotton and Cottonseed Spot Sales Exchange, Oct. 29, 1931, Art. 28; and Regulations of the Stock Exchange, Dec. 31, 1933, Art. 38. (Sfeir, Op. Cit., pp. 426-427, 468-469 and 532.)

²Egypt, Decree No. 319 re Labor Union, Dec. 8, 1952, Art. 20. (Sisto & Shalaleh, Op.Cit., "Labor Unions" p. 12.)

³Egypt, Law of Banks and Deposits, July 13, 1957, Art. 25-26. (Sisto & Shalaleh, Op. Cit., "Banks", p. 6.)

⁴Egypt, Law of Private Societies and Organizations, Oct. 29, 1956, Art. 15. (Sisto & Shalaleh, Op. Cit., "Societies", p. 11.)

4.- Public Accounting Legislation

(a) Law No. 133 of 1951 -- Law No. 133 of 1951 was the first official attempt in any Middle Eastern country to organize the practice of public accountancy. Peculiarly enough, the law was passed in Egypt three years before company law itself was organized.

The Law distinguishes between three types of practicing public accountants: The Accountant and Auditor, the Assistant Accountant and Auditor, and the Accountant and Auditor under Training. No person is allowed to practice public accountancy unless he is registered as belonging to one of these three categories in the separate schedule maintained for each in the Ministry of Economy.

To be registered as Accountant and Auditor under Training, the applicant must have a bachelor's degree in commerce or its equivalent.¹ An Accountant and Auditor must either be a member of the Egyptian Society of Accountants and Auditors, or an Accountant and Auditor under Training who has completed three years in the service of an Accountant and Auditor.² The acquired rights of existing experienced

¹A few other alternate qualifications were recognized if they had been obtained before the enactment of the law.

²The period of training ranged from 4 to 6 years for persons having the alternate qualifications mentioned in above note.

accountants were preserved. Such persons were allowed to register as Accountants and Auditors if they had attained, at the time the law was passed, a specified level of experience.¹

The title of Assistant Accountant and Auditor was apparently meant to be temporary; all the conditions required of candidates to this title must have been fulfilled at the time the law was passed. They can later become Accountants and Auditors upon passing a special examination.

The Accountant and Auditor can certify all types of accounts but to be allowed to certify the accounts of shareholding companies he must be:

- (1) either a member of the Egyptian Society of Accountants and Auditors; or,
- (2) has audited the accounts of three shareholding companies while practicing on his own for a period of not less than five years before the passing of the law; or,
- (3) has practiced the profession on his own in the capacity of Accountant and Auditor for a period of not less than five years.

¹Such as being public practitioners for periods ranging from 3 to 10 years (depending on their basic educational background), or in the position of chief accountant in a public organization, or tax expert practicing for 10 consecutive years before the Egyptian courts, after being screened by the committee administering the law.

This meant that for a person to be able to certify the accounts of shareholding companies he must spend eight years in public practice (three under training and five as Accountant and Auditor) after obtaining his bachelor's degree, or become a member of the Egyptian Society.

The Accountant and Auditor under Training and the Assistant Accountant and Auditor were allowed to certify the accounts and tax returns of all companies but shareholding companies, of all taxpayers subject to the commercial and industrial profits tax with a capital not exceeding £E10,000 or annual profits not exceeding £E600, and of all taxpayers subject to the general income tax with annual revenues not exceeding £E10,000. The Assistant Accountant and Auditor can establish a practice in his own name but the Accountant and Auditor under Training cannot.

Persons already in practice at the time the law was passed, but not fulfilling any of the above conditions, had to submit special applications so as to obtain the necessary licence to certify the accounts and tax returns of shareholding companies.

All persons registered under any of the designations created by the Law cannot practice any other profession or undertake any commercial activity. They cannot also solicit business by advertising or by any other means discreditable to the profession.

An amendment to the Law passed in 1954 specified that public accountancy can only be practiced in a personal capacity, i.e. not as a body corporate, nor under a firm name. It further stipulated that an accountant cannot certify the accounts of a shareholding company if he is on its board of directors or in which he is, or has worked, in any permanent capacity as an officer, promoter or technical adviser, or if he is a partner, employee, or relative to the fourth degree to any person thus connected.¹

(d) Syndicate of Accountants and Auditors -- The public accountancy law of 1951 laid down the basic principles governing the practice of public accountancy in Egypt. It defined the qualifications and the ethical basis of professional practice, but stopped short of providing the institution which would control and supervise it. This came about in 1955 in the form of a law (Law No. 394 of 1955) creating the Syndicate of Accountants and Auditors.²

The declared purposes of the Syndicate is to "work towards the raising of the standards of the profession of accountancy and auditing and to protect its dignity --- and

¹ Egypt, Law No. 456 Amending Certain Provisions of Law No. 133 of 1951, Aug. 26, 1954, Arts. 1 and 2.

² Such a professional structure bears a certain similarity to the one devised in France by the law which created the "Ordre des Experts Comptables et des Comptables Agrées". (See chap. ii, sec. C-4.)

to develop the spirit of cooperation between members and to protect and further their interests."¹

All persons qualifying as public accountants under Law No. 133 of 1951 were allowed to be members of the Syndicate. Only Syndicate members were allowed to practice as public accountants.²

The Syndicate laid down the general rule that a member convicted by the disciplinary committee of negligence or of acts discreditable to the profession would be subject to either warning, reprimand, suspension of not more than two years, or expulsion.³

By far the most important contribution of the Syndicate was the promulgation, under the designation of "Constitution of the Profession of Accountancy and Auditing", of a set of principles governing the whole function of independent audits. The "Constitution" defined basic auditing procedures, professional standards and ethics, and the duties and responsibilities of auditors in a manner which compares very well with the professional standards guiding the profession in Great Britain and the United States.

¹Egypt, Law No. 394 of 1955, Art. 2.

²Ibid., Art. 10.

³These disciplinary measures were previously part of Law No. 133 of 1951, but were repealed from it when the law creating the Syndicate was enacted.

B. Market Structure Before 1956

1.- Classes of Public Accountants

British professional accountants initiated public accountancy practice in Egypt and remained its leaders until the Suez crisis in 1956 brought about their withdrawal. The reasons for their market superiority have already been fully explored.

Until 1956, there were in Egypt three British accounting firms: Russel & Co.; Price Waterhouse Peat & Co.; and Hewat, Bridson & Newby.¹

Egyptian accountants in public practice were of four categories:

- a) The professionally qualified, i.e. chartered, certified or qualifying to the membership of the Egyptian Society of Accountants and Auditors.
- b) The persons qualifying under Law No. 133 of 1951 as Accountants and Auditors authorized to certify the accounts of all companies (including shareholding companies) and all taxpayers, but not possessing the professional qualifications of persons in the first category.

¹Egypt, Law No. 133 re the Practice of the Profession of Accountancy and Auditing, Sept. 15, 1951, Art.3.

- c) The persons qualifying under Law No. 133 of 1951 as Accountants and Auditors authorized to certify the accounts of all companies but shareholding companies and of all taxpayers.
- d) The persons qualifying under Law No. 133 of 1951 as Assistant Accountants and Auditors, who are authorized to certify the accounts of all companies but shareholding companies and all taxpayers subject to the commercial and industrial profits tax with a capital not exceeding £E10,000 or annual profits not exceeding £E600, and taxpayers subject to the general income tax with annual revenues not exceeding £E10,000.

2.- Audits of Shareholding Companies

The following analysis compiled for the year 1954 shows the distribution among public accountants of audit assignments arising from shareholding companies, in an effort to get a fair idea about the prevailing market structure. Total audit assignments were taken as equal to the total number of shareholding companies, plus the total of companies having two assigned auditors each, less the total of companies whose two auditors were partners in the same firm.¹

¹Apparently in those cases, two certifying auditors are a matter of formality required by law (as in the case of banks) or by the company's articles. The same financial statements certified by two partners in the same firm cannot in reality be considered as two different assignments -- even though legally they are, since Egyptian public accountancy law recognizes the auditor in his personal capacity and not as an accounting firm. (Law No. 133 of 1951, as amended by Law No. 457 of 1954, Art. 1).

TABLE 3
AUDIT ASSIGNMENTS ARISING FROM SHAREHOLDING
COMPANIES AT THE END OF 1954

	Registered up to 1950	Registered 1951-54	Total
Egyptian Shareholding Companies	421	54	475
Foreign Companies with Principal Operations in Egypt	31		31
Total Companies	452	54	506
Egyptian companies having two auditors	214	17	231
Foreign Companies having two auditors	18		18
Total audit assignments	684	71	755
Less: Companies with two auditors both auditors being partners in same firm	(138)	(8)	(146)
NET AUDIT ASSIGNMENTS	546	63	609

Compiled from: Egypt, Ministry of Finance and Economy, Census of Shareholding Companies with Principal Operations in Egypt, June 1953 and 1954 (Cairo: 1956)

TABLE 4

DISTRIBUTION OF AUDIT ASSIGNMENTS OF SHAREHOLDING COMPANIES AT THE END OF 1954

Name of Certifying Auditors	Number of Persons in Practice		Registered up to 1950		Registered 1951-1954		Total	
			Number	%	Number	%	Number	%
1. British Firms:								
Hewat, Bridson & Newby	6		163		10		173	
Price Waterhouse Peat & Co.	4		58		1		59	
Russel & Co.	6		87		4		91	
Totals	16		308	56.6%	15	22	323	53.4%
2. Egyptian Chartered or Certified Accountants:								
Z. Hassan	1		24		7		31	
A.K. Hamza	1		11		2		13	
A. Tawakol	1		13		2		15	
A.K. El Ibyari	1		4				4	
Nawar & Co.	2		8		1		9	
Ragheb, El Gamal & Co.	2		2				2	
M.K. Harouni	1		2		2		4	
Totals	9		64	11.6%	14	22	78	12.7%
3. Members of Egyptian Society:								
S. Youssef	1		7		1		8	
M.K. Saleh	1		8				8	
M. Shawki	1		6		1		7	
A.A. Delgawi	1		4				4	
Others	5		7		2		9	
Totals	9		32	5.7%	4	6	36	5.5%
4. Other Local Accountants:								
I. El Ayouti	1		25		3		28	
J. El Abd	1		4		2		6	
M. El Moghallawi	1		11				11	
J. Hilal	1		8		2		10	
T. Afifi	1		9				9	
S. Riyad	1		5				5	
Others	52		46		22		68	
Totals	58		108	19.8%	29	46	137	22.6%
Sub-totals	92		512	93.7%	62	98	574	94.2%
5. Foreign Auditors Not Established in Egypt								
	7		7	1.3%			7	1.2%
6. Unidentified								
			27	5.0%	1	1	28	4.6%
GRAND TOTAL	99		546	100.0%	63	100	609	100.0%

Compiled from: Ibid.

We can thus draw the following summary regarding the construction of the market from Table 3:

TABLE 5
CONSTRUCTION OF THE MARKET IN 1954

<u>No. of Assignments Per Person</u>	<u>No. of Persons</u>	<u>Total Assignments</u>
10 and above each:		
Partners in British firms	16	323
Egyptian chartered accountants	3	59
Other local accountants	<u>3</u>	<u>49</u>
Sub-total	22	431
4 - 9 each	11	64
3 and less each	<u>59</u>	<u>89</u>
TOTAL	<u>92</u>	<u>574</u>

It is therefore an obvious fact that in as late a period as 1954, when there was a fair number of professionally qualified Egyptians and after the public accountancy law of 1951 legalized the entry of a number of practitioners who did not belong to any professional body, British firms still held the lion's share of the basic public accounting market -- that of shareholding companies.

The fact that Law No. 26 of 1954 (and previously the 1947 edition of the model articles of association) required that at least one of the company's auditors had to be Egyptian did not bother the British firms very much. Two of them (Hewat Bridson & Newby and Price Waterhouse Peat & Co.) had an Egyptian partner each. In any case, it was not difficult to

have one of the local accountants countersign the certificate. Evidently, Hewat Bridson & Newby capitalized on their Egyptian partner to the utmost: of the 173 assignments that they handled in 1954, 142 were taken in the name of their Egyptian partner, Fouad El Sawaf. In the case of Price Waterhouse Peat & Co., 12 of their 59 assignments were in the name of their Egyptian partner, Hanna Y. Hanna; this actually becomes significant when we consider that Mr. Hanna joined Price Waterhouse as a partner only in 1954, the same year one which the above statistics were based.

In the cases where the assignment was taken in the name of only one British auditor, the company had another Egyptian auditor appointed to countersign the certificate. In most cases, this was only a formality, without the second auditor undertaking any real audit. This actually accounted for no less than 80 audit assignments handled by Egyptian auditors.¹

The trend, however, pointed towards a wider distribution of audit assignments among local public accountants as new companies were being formed. The natural tendency in well-established companies to avoid any changes of auditors would, however, preclude any major shifts in the market construction of auditing activity, except in a gradual manner with the

¹There were a few assignment still handled solely in the name of one British partner or in the name of the firm, apparently due to the fact that the law was passed in the same year taken as a basis for our analysis and a number of companies had not yet had the time to comply with the full provisions of the law.

formation of new companies and the entry of new practitioners in the field.

What the previous analysis does not show, though it would not really affect our conclusions, are the sizes of the various audit assignments as allocated between the public accountants. If this were in any way determinable, it would most probably show a distribution of income arising from audits of shareholding companies more in favour of the British firms, since they handled more of the larger companies.

3.- Other Aspects of the Market

Audit and tax business arising from the various other forms of commercial establishments would naturally be more numerous than those arising from shareholding companies, but the individual size of each engagement is usually much smaller. After 1954, all limited liability companies (including foreign branches, but excluding "companies with limited liability")¹ were required to have independent audits; and after 1953, all companies, and all unincorporated individual taxpayers (with a capital in excess of £E1,000 and employing more than 10 workers, or with annual profits in excess of £E600) were required to have their tax returns certified by public accountants.² Furthermore, numerous private business would, of their own accord, require the services of independent auditors.

¹ Discussed in the first section of this chapter.

² Egypt, Law No. 253 of 1953 Amending Certain Provisions of Law No. 14 of 1939, Art. 1

Obtaining the total of engagements arising in this section of the market for any one year and analysing their distribution among practitioners is so vast a venture as to be impossible to undertake or to determine with any reasonable degree of accuracy. In any case, such an attempt would not result in any significant conclusions that we cannot arrive at by deductions based upon the prevailing market structure at the time.

The public accountancy law of 1951 gave public accountants of lesser qualifications than those allowed to handle shareholding companies the right to certify the statements and tax returns of all companies other than shareholding companies and of the smaller classes of taxpayers.¹ Therefore, the number of persons serving this vaster market of smaller companies and unincorporated traders is much greater than the number of those serving shareholding companies.

A basic feature of this market is the absence of the issue concerning the auditor's responsibility towards absentee shareholders. Such assignments are either for the benefit of tax authorities and other government regulatory agencies, or, in fewer instances, for the owners' own benefit.

¹Egypt, Law No. 133 of 1951, Art. 21 and 22.

Therefore, the attraction of a certificate signed by a well-known public accountant is, in many of these cases, negligible. If it is matter of just meeting legal requirements, the tendency is to be less concerned with quality than with cost and, where tax liabilities are involved, to try to avoid as much of the tax as possible. Such advantages would be more readily provided by the smaller accountants who are eager enough for business to accede more willingly to the desires of their clients and to perform the assignment at a level of fees much lower than those charged by the more qualified, older-established public accountants.

Under such conditions, the tendency of this market is to be very diffused, i.e. with a large number of practitioners each having a limited number of assignments.

C. Recent Developments in Public Accountancy

The withdrawal of the British accounting firms in 1956 brought about a windfall of business for local public accountants. The Egyptian partners of the departing firms, who inherited the well-established practices that controlled so much of the public accounting market, and a few other professionally qualified Egyptians, were to benefit most from this development.

A scramble for business was bound to ensue. Local companies, some of which were Egyptianized foreign companies, had to take new positions with regards to their auditors now

that the old accounting firms were no more existent. The prize was too precious for the smaller accountants to relinquish very easily.

Unable to compete effectively on the professional level, due to the deep-rooted confidence of the upper strata of the business community in the British-qualified accountants, the other smaller accountants took the issue to official circles. On November 19, 1956, they submitted, through the council of the Syndicate of Accountants and Auditors which they controlled, a memorandum to the Ministry of Economy requesting government interference in the alleged "professional monopoly" that a few public accountants enjoyed.¹

As a result, a special committee was formed to look into the complaint. On November 7, 1957, the committee came up with a proposal for a law limiting the scope of a public accountant's practice to ten shareholding companies. But, in spite of the Syndicate's continuous efforts, nothing came out of this proposal before March 1961 when the President of the Republic advised the public institutions (which were the organisms created to carry out the government's economic activities) to limit the audit assignments to any one public accountant to ten, and his maximum total fees to £E10,000.² This directive, however, could only affect those auditors

¹Rose El Youssef, No. 1746, Nov. 27, 1961, p. 10.

²Ibid.

practicing in the public sector, i.e. auditing the accounts of companies controlled by the public institutions, and the public sector at the time was just starting to grow at the expense of the private sector.

The period of prosperity of the larger accounting firms was coming to an end. The new composition of the public accountancy market that followed the withdrawal of British accountants barely had time to take effect when the whole structure of the Egyptian economy started drifting on a course of socialization which affected the basic pattern of development of public accountancy.

The trend started in 1960, when the Bank Misr group was nationalized.¹ But the first large-scale measure in this connection took place on July 20, 1961. On that eventful day, a series of laws were passed bringing a large number of private companies into the public sector. Law No. 117 completely nationalized all banks, insurance companies and 50 other business establishments; Law No. 118 imposed at 50% government ownership on 81 companies (and was followed by Decree No. 819 of 1961 stipulating that all persons owning shares in these companies should cede 50% of them to the

¹All previous economic measures before that date could be interpreted in a capitalistic context in that they were not strictly aimed at curbing private enterprise inasmuch as harnessing it within a general economic plan.

government); and Law No. 119 listed 143 companies in which any shares owned by a natural or juristic person in excess of a market value of £E10,000 were to accrue to the government.¹ Subsequent laws greatly increased the number of companies affected by these initial laws.²

All companies thus coming into the sphere of the public sector were organized, according to their type of activity, into autonomous economic units -- called public institutions -- which would supervise and control their operations in coordination with the government's overall economic plan.³

In its nationalization measures, the government has not stamped out the principle of the shareholding company, nor has abolished the basic law (No. 26 of 1954) governing them, but

¹Egypt, Laws No. 117, 118 and 119 of July 20, 1961. (Sisto & Shalaleh, op. cit., "Shareholding Companies," pp. 134-140.)

²E.g.: Laws No. 41, 42, 91, 129 and 132 of 1962, Decrees No. 618 and 944 of 1962, and Laws No. 72 and 73 of 1963. These subsequent laws or decrees added more companies to the public sector, including many unincorporated businesses, and imposed a 100% government ownership on most of the companies previously partially government owned. (Sisto & Shalaleh, op. cit., "Shareholding Companies," pp. 143-201).

³Egypt, Law No. 265 Organizing Public Institutions of an Economic Nature, July 19, 1960; and Law No. 60 on Public Institutions, April 29, 1963. (Sisto & Shalaleh, op. cit., "Public Institutions," pp. 10-12 and 86.)

has substituted itself for the shareholders. The public institutions were to act as agents for the government, and their boards of directors were given in principle the same rights of the shareholders in their relations with the shareholding companies falling under their control.¹

A period of confusion resulted concerning the audit of these nationalized companies. The issue was whether they shall be audited by private practitioners or by the State Audit Board. The prevailing laws passed on to the boards of the directors of the public institutions the rights of the shareholders in the general annual meeting, which include the right to appoint auditors.² On the other hand, the law of the State Audit Board stipulates that the auditor of any company in which the government participates in at least 25% of its ownership is to be appointed by a presidential decree out of three persons nominated by the company's board of director.³

To end this confusion as to who appoints the auditor, Law No. 167 was passed on November 2, 1961, regulating the audit of public institutions and of companies in which they participate in ownership. This law could mark the beginning

¹Egypt, Law No. 60 of 1963 on Public Institutions,
Art. 25. (Sisto & Shalaleh, op.cit., "Public Institutions," p.86.)

²Ibid.

³Egypt, Law No. 230 of 1960 re the State Audit Board,
Art. 25. (Sisto & Shalaleh, op.cit., "State Audit Board," p. 20.)

of the end of any serious public accountancy in Egypt. Its main provisions are as follows:¹

- (1) There shall be established in every public institution an audit department which will be responsible for the examination of the accounts of all companies in which the public institution participates in ownership to the extent of 25% and over. The audit departments shall replace the accounting firms in all companies affected by the law.
- (2) The auditors shall be appointed to the audit departments by presidential decree.
- (3) The boards of directors of public institutions shall appoint the auditors of companies falling within their control from the staff of their audit departments.
- (4) The staff of the audit department cannot undertake any outside work, nor can they accept any other additional employment. They cannot also be transferred to any other department of the public institution without their consent. This last provision is obviously intended to preserve the auditors' independence in their relation with the institution's directors.

The law thus clearly abolishes the function of the independent auditor, or rather any hope that the companies in the public sector will continue to engage his services.

¹Egypt, Law No. 167 Organizing the Audit of Public Institutions and of Companies in which they Participate in Ownership, November 2, 1961. (Sisto & Shalaleh, op. cit., "Public Institution," p.37.)

The law, however, has not yet been fully applied. In 1962 and 1963 special presidential decrees were passed authorising the boards of directors of public institutions to appoint, at their discretion, the auditors of the companies they administer for the current financial years.¹ This obviously means that the audit departments that Law No. 167 of 1961 intends to create had not yet been fully established.

D. The Future

The future of the independent auditor in Egypt with regards to shareholding companies is, as things stand now, unmistakable. Law No. 167 of 1961, though not yet fully enforced, is still in effect and it is a matter of time before it would be applied. Its implications are obvious: the role of the independent auditor in shareholding companies is eliminated. With the majority of shareholding companies falling under state control, they become subject to the provisions of Law No. 167 of 1961, in which the auditor is reduced to the status of a government employee.

The whole issue lies basically in the fact that the economic philosophy which led to the rise of the auditor is being challenged in the very premises upon it is based. The

¹Egypt, Law No. 119 of 1962 and Law No. 167 of 1963, Empowering the Boards of Directors of Public Institutions to Appoint the Auditors of Companies they Control for the Years Ending June 30, 1962 and June 30, 1963. (The Official Gazette, No. 201, September 5, 1963).

result is that the country's basic economic structure is being very differently reconstructed, with the independent auditor having no economic role to play in the emerging structure. With the extinction of the shareholding company as a mass-owned institution and the shrinking size of the private sector, the auditor's usefulness in the economy starts to disappear.

The situation right now, however, still has room for the independent auditor, though only in a transitory manner. Until Law No. 167 of 1961 becomes fully enforced, the services of the independent public accountant will continue to be sought to examine the accounts of government-controlled enterprises. From a long-run point of view, the main consideration is that as long as there is a private sector, there will always be a certain demand for independent audits and for taxation services, though the number and the size of the individual assignments would be smaller. In addition, there are now in Egypt, and there might be more in the future, a limited number of foreign concerns, usually in partnership with the government. These would maintain a certain demand for the services of the more qualified accountants. In fact, it is this area which is helping to keep the professionally qualified accountants in practice so far. At least in one case I am familiar with, audit and tax services to foreign enterprises form more than 60% of the practitioner's activity.

In the auditor's function of examining the accounts of government-controlled enterprises, the concept of independence acquires a different interpretation. In this area, there is naturally no question of a mass of shareholders whom the auditor represents; there is just one shareholder: the government, represented by the boards of directors of public institutions. There is also no question of third parties who might be relying on the auditor's certificate in their financial or investment decisions. The auditor, therefore, becomes restricted to reporting to the government whether the managers of its companies are truthfully and correctly representing the results of their operations and whether they are properly administering the assets that they are entrusted with.

Being appointed by the boards of directors of public institutions and reporting to them, the auditor can become subordinated to their interests, and thus lose the independence that so much distinguishes his profession. It can be argued here that the same thing is true in a mass-owned company where the auditor is appointed by the shareholders, and that the board of directors of the public institution is only replacing the shareholders and it is too detached from the companies' operations to really have any interest in influencing the auditor's report. The answer to this argument would get us deep in the workings of a state-controlled economy and its inherent bureaucratic tendencies; it is not uncommon

for the directors of a state enterprise to want to inflate sales or profits or otherwise improve the picture by the manipulation of financial statistics. It is beyond the scope of this paper to get into the administrative setup of a socialist economy in detail. Suffice us to mention here two points which reduce the analogy between the relations of the shareholders and those of the board of directors of a public institution with the auditor.

The first is that the shareholders as a group are not the same in every company. To the auditor, they are theoretically one of many clients. He is not, therefore, theoretically under pressure to bow to their interests. The loss of one assignment does not (or rather should not) disrupt his whole practice. By contrast, the board of directors of one public institution controls a number of companies. Therefore, any difference of opinion between the auditor and the board might affect more than one of his assignments. Consequently, there is a stronger compulsion to always be on the good side of the board.

The second is that in the auditor's relations with the shareholders, there is the mass opinion of the public, or the business community to be more specific, to take into consideration, and there is the watchful eye of an impartial party, the government. In the state-owned enterprises, the business community becomes a disinterested party, and the government is no more an impartial party. The auditor is thus

in fact reporting about one state organ to another state organ. In case of conflict with the organ he is reporting to, he is placed in a weak position, as the ultimate party with whom he should take up the issue -- the people, who are theoretically the real owners -- is too far out of his reach.

So far the discussion has centered around the relation of the independent auditor with a state enterprise in a state-controlled economy. As I have previously mentioned, this situation is transitory. Eventually, the independent auditor shall be replaced by the audit department of the public institution. The argument presented above remains, however, essentially the same. Granted that the effective law (Law No. 167 of 1961) provides the auditor with a certain degree of independence from the institution's directors (such as being appointed to his position in the audit department by presidential decree and not being exposed to transfer to another department except with his own consent) he is effectively still a government employee, and as such is more prone to subordination to the interests of the board of directors of the public institution he is tied up to. Even though he is appointed to the audit department by presidential decree, his appointment as auditor to a company is the decision of the board of directors of the public institution.

What is already happening now is an indication of things to come. A large number of public practitioners have closed up their practices and entered into government service. The more

qualified of them have taken up full-time teaching jobs at the universities or have started to expand into the other Arab countries. Egyptian public accountants have built up important practices in Libya, Saudi Arabia and Kuwait, and there are indications that they might attempt to expand in Lebanon and Iraq where there is already one Egyptian accounting firm in each of the two countries.¹ This is aside from those who have taken up employment in the Arab countries. The ones who are still in public practice in Egypt are either waiting for Law No. 167 of 1961 to become finally in effect before making their final decisions, or are still dependent upon enough tax and audit business of still unnationalized companies, unincorporated individuals, and a few foreign companies to keep them going.

¹In Libya, there is Nawar & Co. and Mohammed Shawki; in Saudi Arabia, there is Nawar & Co., Issa El Ayyouti and Mohammed El Moghallawi; in Kuwait, there is Nawar & Co., Farid Mansour and Issa El Ayyouti; in Iraq, there is Issa El Ayyouti; and in Lebanon, there is Nawar & Co.

CHAPTER V

STATUTORY AUDITS IN THE OTHER ARAB COUNTRIES
OF THE MIDDLE EASTA. General Observations1. Prevalent Legislation

All the Middle Eastern countries covered by this study now have legislation governing the establishment and operations of shareholding companies; except Saudi Arabia, which has, as I previously mentioned, an unratified but unofficially enforced law. Our concern here is with the role of the auditor in shareholding companies as regulated by the prevalent statutes.

The oldest of current laws is the Lebanese Commercial Code of 1943, followed in 1949 by the Syrian Commercial Code. Both the Lebanese and the Syrian Code replaced the Ottoman Commercial Code of 1266 hegira (1850 a.d.).

The laws of Iraq, Kuwait and Jordan are all relatively very recent. When they were enacted, however, they succeeded not an outdated Ottoman Code, but a more progressive form of legislation, British in its origins. In other words, they were promulgated in a business environment already educated to the economic role of the independent auditor.

The Iraqi Law No. 31 of 1957 for Commercial Companies replaced the Indian Companies Act No. 7 of 1913 in force in the

country since 1919. The Kuwaiti Law No. 15 of 1960 for Commercial Companies also replaced the same Indian Companies Act in force in the country since 1953. The Jordanian Provisional Law No. 33 of 1962 (called Companies Law, 1962) replaced the Palestinian Companies Ordinance No. 18 of 1929 and Companies Registration Law of 1927 of Transjordan. As the latter law was not a comprehensive companies law, but just a short regulation on the registration of companies,¹ it was the Palestinian Companies Ordinance of 1929 which until 1962 governed in fact the operations of companies in Jordan.

2. Types of Limited Liability Companies

The legislation of Iraq, Kuwait, Syria and Jordan recognizes the following types of limited liability companies:²

- (a) The public shareholding company (called Public Limited Stock Company or Societe Anonyme) which acquires its capital through public subscriptions. The number of founders is limited to at least seven in Iraq and Jordan, and to five in Syria and Kuwait.

¹Jordan, Companies Registration Law of 1927. (Syndicate of Lawyers, ed., Collection of Laws and Regulations of the Hashemite Kingdom of Jordan as on 1957, Amman: National Press, 1958; pp. 641-644.)

²Iraq, Commercial Companies Law, 1957, Arts. 33, 37, 189, 191; Kuwait, Commercial Companies Law, 1960, Arts. 42, 70, 185 and 187; Jordan, Companies Law, 1962, Arts. 33, 39 & ; and Syria, Commercial Code, 1949, Arts. 103, 284, 285 and 314.

(b) The private shareholding company (called Private Limited Stock Company or Company with Limited Liability) whose capital is privately raised. It has a minimum of two members and a maximum of 25 in Syria, of 30 in Kuwait, and of 50 in Jordan and Iraq. In Iraq it is prohibited from dealing in insurance matters. In Syria and Kuwait it is additionally prohibited from undertaking any banking business or investing funds for the account of third parties. There are apparently no legal restrictions on its activities in Jordan.

(c) The limited partnership (or commandite company), which consists of two groups of partners: those with unlimited liability entrusted with managing the business, and those whose liability is limited to their capital contribution. The commandite company is of two types: simple commandite and commandite limited by shares.

Lebanese commercial law does not distinguish between a private and a public shareholding company. Societes Anonymes can, however, be formed with a minimum of three members.¹

3. The Audit of Limited Liability Companies

All company legislation in the Middle East provides for the appointment of external auditors by public shareholding companies.

¹Lebanon, Commercial Code, 1943, Art. 79.

Syrian and Iraqi law further provide for the appointment of auditors by companies with limited liability and by commandite companies limited by shares. In Syria, the duties, responsibilities and qualifications of the auditors of these companies are no different than those of the auditors of public shareholding companies. In Iraq, however, the auditors of public shareholding companies have more defined duties, and the qualifications required of them are more stringent.¹

Kuwaiti law takes a different attitude. If the members of the company with limited liability or of the commandite company limited by shares exceed seven, a supervisory board of three persons must be set up to examine the accounts. They can (but not necessarily should) have independent auditors, in which case the auditors shall be subject to the same regulations as those governing the auditors of public shareholding companies.²

Jordanian law does not differentiate between a public and a private shareholding company in connection with the appointment, duties and obligations of the auditor. Limited partnerships are not required to be audited.³

¹Syria, Commercial Code, 1949, Arts. 306 and 320; and Iraq, Commercial Companies Law, 1957, Arts. 23 and 192, and Public Accountancy Regulation, 1958, (No. 18 for 1958), Art. 2.

²Kuwait, Commercial Companies Law, 1960, Arts. 51, 206 and 213.

³Jordan, Companies Law, 1962, Arts. 168-174.

B. The Appointment of the Auditor

1. First Auditors

The company's first auditors have to be elected along with the board of directors in the first statutory general meeting which announces the final incorporation of the company. The statutory general meeting is composed of the subscribers to the company's shares and generally has to be called for within one month (two months in Jordan) after announcing the close of subscriptions; (in the case of Lebanon, within one month after the date of the report of the experts appointed by the court to appraise the company's assets).¹

2. Subsequent Auditors

The auditors are always appointed annually by the shareholders in the annual general meeting.² Their remuneration is fixed in the order of their appointment. The shareholders are required to appoint only one auditor, but they can, if they so desire, appoint more than one, in which case all auditors are jointly responsible for the company's audit.

¹Lebanon, Commercial Code, 1943, Arts. 90-93; Syria, Commercial Code, 1949, Arts. 116-119; Iraq, Commercial Companies Law, 1957, Arts. 60-61; Kuwait, Commercial Companies Law, 1960, Arts. 88-90; and Jordan, Companies Law, 1962, Art. 57.

²Ibid.: Lebanon, Art. 172; Syria, Art. 235; Iraq, Arts. 208-211; Kuwait, Arts. 157-161; and Jordan, Art. 168.

Only in Lebanon is an additional auditor specifically required by law. This person has to be appointed by a decision of the President of the Court of First Instance and must be chosen from among the "accounting experts" registered with that court. His fees should be the same as those of the shareholders appointed auditor, and he has the same rights, duties and obligations.¹

This interesting peculiarity in Lebanese law appears to be an elaboration of a concept existing in the French Law of July 24, 1867, as amended by decree on August 8, 1935.

Since 1935 in France, societies anonymes resorting to the public for capital have had to choose one of their auditors from the list of approved auditors drawn up by the Court of Appeal. If this is not done, any shareholder can request the commercial court to appoint an auditor from those registered on that list.

Apparently using this French regulation as a base, the Lebanese came up with their innovation. Like the French, the Lebanese law created the institution of "accounting experts approved by the court", but further provided that every shareholding company (not just the ones resorting to the public for capital, since the Lebanese law does not distinguish between various types of shareholding companies) has to have two auditors: one appointed by the shareholders and another by the court.

¹Lebanon, Commercial Code, 1943, Art. 173.

3. Qualifications of the Auditor

a) General -- In Lebanon and Saudi Arabia, the practice of public auditing is free from regulations. In Syria, Iraq, Kuwait and Jordan, legislation provides for the licencing of public auditors and regulates their profession. Each case shall, therefore, be discussed separately.

b) Lebanon -- The qualifications of the auditor that the shareholders are to appoint are not at all defined -- any person can be elected to that function. The other auditor, who is appointed by the court, must be an "accounting expert" registered with the Court of First Instance.

To become an "accounting expert", a person must file an application to the Chief of Council of the Supreme Court enclosing the following:¹

- (1) A copy of his personal record at the Department of Justice;
- (2) An academic certificate or other certificate of technical proficiency;
- (3) A proof of experience of at least five years in the accounting field in a bank or commercial establishment or as a court expert if he does not possess a diploma in commerce from an academic institution.

¹Lebanon, Legislative Decree No. 54 of 1953, Art. 11.

This is all that is required. The application would then be studied by the Council of the Supreme Court which has the final decision in the appointments.

"Accounting experts" are elected for a term of three years, subject to renewal. Their number in each of the country's regions is fixed. In Beirut, they are now 72.¹

The absence of any qualifications requirements regarding the auditor that the shareholders can appoint has created in Lebanon a class of semi-qualified or completely unqualified auditors whose services are sought by companies not interested in any real audit, but just to live up to the minimum requirements of the law.

Furthermore, the number of approved "accounting experts" being limited to 72 persons, elected for a three-year period subject to renewal, has created in that sector of the activity a professional monopoly restricted to persons, with or without qualifications, who have the influence or the luck to get themselves elected as approved "accounting experts."

c) Syria -- Public accounting in Syria is regulated by Presidential Decree No. 1109 of 1958 as amended by Decree No. 144 of 1961. Public accountants must be licenced from the Ministry of Economy and Commerce and their names must appear on the Register of Statutory Accountants kept at the Ministry.

¹Lebanon, Decree of the Supreme Court No. 16. (The Official Gazette, Feb. 4, 1963, pp. 409-411.)

To be licenced, the applicant must be:

- (1) A graduate of a college or institute of advanced commerce, with a specialization in accountancy, and with three years experience in any of the activities listed below; or a holder of an advanced diploma in Business, Economics or Finance (provided that the program includes accountancy subjects) with five years experience in any of the following activities:
 - (a) An auditor in a public accountant's office;
 - (b) In a senior accounting or audit position with a company or private or public organization subject to statutory audits;
 - (c) Practicing as an independent auditor before the enactment of this Decree;
 - (d) A tax inspector or an auditor with the State Audit Board;
 - (e) A teacher of accountancy or audit subjects; or
- (2) A graduate of law school with five years experience in (a) to (d) above, or a graduate of a secondary commerce school with ten years such experience, after passing a special examination held for the purpose. This section was made temporary in that the qualifications stated therein would no longer be accepted after 1963.

In 1961, the total number of persons qualifying as Statutory Accountants under the above law amounted to 117

persons in all of Syria.¹ But as government and other public employees are prohibited from acting as public auditors (even if registered as Statutory Accountants under the public accountancy law),² the number of persons actually in public practice is in fact much smaller; they did not exceed twenty in 1961, six of whom were the partners and employees of Saba & Co.³

d) Iraq -- Public auditing in Iraq is governed by Regulation No. 18 of 1958⁴ which specifies that no person can practice as a public auditor unless he is registered either as an Auditor of Accounts مراقب حسابات or as a Licenced Accountant محاسب مجاز with the Department of Commerce.

The Auditor of Accounts can examine the accounts of all companies, including public limited stock companies. The Licenced Accountant can audit the accounts of all commercial establishments except public limited stock companies or their subsidiaries. Thus the potential statutory audits market of

¹Syria, Sup. to the Official Gazette, No. 21, June 1961.

²Ibid.

³Privately secured from Saba & Co.

⁴Regulation No. 18 of 1958 replaced a public accounting law which was passed only a year ago (Regulation No. 52 of 1957) and which created an outcry at the time because it restricted the practice of public auditing only to those professionally qualified, thus making it practically impossible for Iraqi commerce graduates to go into public practice without having to fulfill the conditions of British accounting societies.

Licensed Accountants lies in companies with limited liability and commandite companies limited by shares.

The Auditor of Accounts must be a member of any of the three British chartered institutes, or of the Association of Certified and Corporate Accountants, or of the American Institute of Certified Public Accountants, or recognized as Accountant and Auditor under the U.A.R. public accountancy law.

The conditions of admission as a Licensed Accountant are less rigorous. The candidate has to be a Bachelor of Commerce from a recognized university, must have five years' experience with a firm of accountants who fulfill the conditions required of the Auditor of Accounts, and must undergo a written examination sponsored by the Ministry of Economics.

There were about fourteen Accountants and Auditors¹ and two Licensed Accountants² in Iraq at the end of 1963.

e) Kuwait -- Public auditing in Kuwait is regulated by Law No. 6 of 1962. Only persons whose names appear on the Register of Auditors kept at the Ministry of Finance and Economy are allowed to practice as auditors. Only one class of auditors is recognized for all types of companies.

¹They were: The resident partner of Saba & Co.; the resident partner, three British and two Iraqi employees in Whinney Murray & Co.; both partners of Al Hawiz & Co.; a British lady (Iraqi by marriage) chartered accountant; one Iraqi certified and one Egyptian certified practicing independently; and two Iraqi chartered accountants practicing independently on a parttime basis.

²See page 91.

The qualifications for admission are as follows:

- (1) A university degree or the equivalent in Business, Economics or Finance, provided that the program included accounting subjects; and
- (2) Either a membership in one of the accountancy bodies recognized by the Minister of Finance and Economy;¹ or three years consecutive experience, after obtaining the academic qualifications required in (1), in any of the following:
 - (a) An auditor in a recognized accounting firm;
 - (b) In a senior accounting or audit position in companies, private or public organization, or government ministries;
 - (c) A teacher of accountancy or audit subjects;
 - (d) In independent accounting practice before the passing of the law.

f) Jordan -- Public auditing in Jordan is regulated by Law No. 10 of 1961. Public auditors have to be licenced and their names registered with the State Audit Board. One class of auditors is recognized for all companies.

¹The accountancy bodies that the Ministry recognizes are: The Chartered Institutes of Great Britain, Australia, Canada and India, The Association of Certified and Corporate Accountants, The American State Societies of CPAs, and The Egyptian Society of Accountants & Auditors. (Kuwait, Ministerial Decree No. 4, Oct. 6, 1962).

The required qualifications are:

- (1) Membership in a recognized accountancy body. (No listing of recognized bodies is given) ; or,
- (2) A university degree or the equivalent in Business, Economics or Finance, and one year's experience as audit manager or senior auditor in a government department or with a licenced accounting firm; or,
- (3) A secondary education, or the equivalent, and four years experience as above; or,
- (4) An intermediate secondary education and six years' experience as above.

Persons who practiced the profession in Jordan for at least two years before the passing of the law were exempted from the above conditions.

The public auditor in Jordan has to be of Jordanian nationality. Foreign auditors in practice in Jordan for at least two years before the passing of the law were admitted, provided Jordanian auditors are given the same treatment in the foreign auditor's country.

4. The Independence of the Auditor

The only provision relevant to the auditor's independence in Lebanon is the one prohibiting the auditor from being connected with any persons whose object is to influence the prices of the company's shares on the stock exchange.¹

¹Lebanon, Commercial Code, 1943, Art. 177

Syrian law disqualifies from appointment as auditors:¹

- (a) All persons in the service of the company or of any of its directors or of any shareholding company owning 10 % of the company's capital, or of any person whose personal capital is owned to the extent of 10 % and over by the company.
- (b) A partner or relative to the fourth degree of any director.

In addition, the Syrian auditor is prohibited from accepting an assignment in a company whose management or accounts are being handled by any of his relatives to the fourth degree.²

In Iraq and Kuwait, the auditor cannot participate in the formation of the company, or be a member of its board of directors, or be employed in a full time capacity in any technical, managerial or advisory work. He also cannot be a partner or employee or a relative to the fourth degree of any person thus connected. Similar conditions are present in Jordan, only without reference to family relations.³

¹Syria, Commercial Code, 1949, Arts. 234-236.

²Syria, Public Accountants Regulation, 1958, (Presidential Decree No. 1109 of 1958 as amended by Decree No. 144 of 1961), Art. 3.

³Iraq, Commercial Companies Law, 1957, Art. 209, Kuwait, Commercial Companies Law, 1960, Art. 162 and Public Accountancy Law, 1962, (Law No. 6 for 1962), Art. 5; and Jordan, Public Accountancy Law, 1962, (Law No. 10 for 1962), Art. 14.

The auditor in Jordan and Kuwait is further prohibited from being a "partner" or "member" of the company. As it stands in the text, the clause is somewhat ambiguous. One is left to wonder whether the legislator intended to prohibit the auditor from being a shareholder in the company, or just from being in its service, or some other connotation. The Arabic word "شريك" used in the text can be interpreted in different ways; or if it is interpreted literally as "partner", it stops having any meaning since we are talking about shareholding companies not partnerships.¹

Other than the above clause in Jordan and Kuwait, none of the relevant laws prohibit the auditor from being a shareholder in the company he audits.

5. Professional Conduct Prescribed by Statute

(a) Incompatible activities -- Iraq and Kuwait prohibit the auditor from engaging in any activity not compatible with public accountancy; commercial activities are specifically prohibited. In Jordan, the auditor is expected to be fully occupied in his profession; for this reason he should be residing in Jordan and should not be in the employ of the government or of any public

¹The Jordanian text is as follows: "ان لا يكون مدقق حسابات لشركة شريكا بها او عضوا بمجلس ادارتها..." (Public Accountancy Law, 1962, Art. 14). The Kuwaiti text is very similar: "لا يجوز ان يكون مراقب حسابات الشركة شريكا في الشركة او بمجلس ادارتها" (Public Accountancy Law, 1962, Art. 4).

institution.¹ These conditions in Jordan are obviously a direct reaction to the fact that a number of government employees had part-time public accounting practices and their government positions made it easier for them to help their clients out of taxes.

b) Solicitation of business -- In Iraq, Kuwait and Jordan, the auditor is prohibited from soliciting business by means discreditable to the profession; advertising is specifically prohibited in Jordan and Iraq.² Apart from that the acts discreditable to the profession are not specified. This is an obvious discrepancy resulting from unimaginative copying of the regulations governing professional practice in more advanced countries. The warning against "acts discreditable to the profession" is normally included in the internal regulations of privately-organized societies rather than in public statutes. Professional societies are always in a better position than legal authorities to supervise professional practice and take corrective measures when necessary against misbehaving members. Furthermore, such a clause has a very definite meaning in Great Britain and the United States where the profession in its century-old progress has built for itself a rich tradition. In the Arab

¹ Iraq, Public Accountancy Regulation, 1958, Art. 9; Kuwait, Public Accountancy Law, 1962, Art. 5; and Jordan, Public Accountancy Law, 1962, Art. 14.

² Ibid.

countries where no local profession with its own sets of principles and standards has yet evolved and where public accountancy itself is barely a decade old, how are practicing accountants (when they are not affiliated to a foreign accounting society) to know what acts is the law warning them against? In addition, what institution has the law created to supervise them and to ensure the non-performance of unprofessional acts; and how can the court decide what acts are considered discreditable in the absence of any legal definition of such acts and in the absence of any local professional tradition?

c) Professional secrecy -- The laws of Syria, Jordan and Kuwait explicitly specify that the auditor is to maintain professional secrecy.¹ In Iraq and Lebanon, where there is no such explicit mention in the commercial law, it is definitely assumed that the auditor is committed to professional secrecy under the general principle that a professional man cannot divulge any secrets obtained in the course of practice of his profession.²

¹ Syria, Commercial Code, Art. 241; Kuwait, Public Accountancy Law, Art. 11; and Jordan, Companies Law, 1962, Art. 174.

² A.I. Al-Bassam, Principles of Commercial Law (Baghdad: Al Ani Press, 1961), p. 403, (In Arabic); and Lahoud, op. cit., p. 27.

6. The Statutory Auditor -- An Evaluation

The auditor's activities are based upon two premises: First, they are specialized; and, second, they are independent. The absence of any of these two attributes rules out the necessity for engaging a public auditor. His competence must naturally be compatible with his specialized services to the economy, and his independence is the keystone of his economic role as a preserver of mutual confidence in business relationships.

The basic questions that pose themselves are: By what standards should the auditor's competence be measured, or, in other words, how can the most satisfactory level of competence be determined? Who is to determine such minimum standards? How can independence in public accounting be controlled? And what institutions are to be created to grant professional recognition?

This leads inevitably to one major question: Who can do the most efficient job of organizing professional activity: the profession or the state?

The best system is the one that succeeds. Systems which have proven themselves in other more advanced countries in the world should be our guide. In certain matters, especially those dealing with economic development, we cannot afford to be innovators; the world is moving much too fast for us to afford losing time in trial and error.

With regards to the organization of public accounting activities, we have two proven methods to guide us: (a) the British way, where competence is determined, tested and controlled by the profession itself; and (b) the American way, where competence is tested by the state, though unofficially controlled by the profession.¹

In Great Britain, the law recognizes the profession as a whole; in fact, the law was based upon the existence of a sound profession. In the United States, the law recognizes individuals, who become part of the profession after their recognition by law; in essence then, the accountancy profession in the U. S. draws its existence from the public accountancy laws.

Though both systems are different in the type of professional structure, one thing is common: The standards of competence are determined by the profession (directly in Great Britain and indirectly in the U. S.), and independence (though undefined in Great Britain and strictly defined in the U. S.) is stressed in both cases as a question of personal integrity.

¹I have previously mentioned that in the U.S. the states give the examination and issue certificates, though the examination itself is prepared by the American Institute of CPAs as a favor to the states.

There are no proven methods by which the state determines professional competence completely independent of the profession. The reason is simple. In a specialized field such as public accountancy, who can better decide the type and level of knowledge required than the profession itself, i.e. than those who have lived and practiced it ?

In the Middle East, only Iraq has taken a definite stand on the issue of the auditor's competence. Recognizing the non-existence of a local profession, it insisted upon foreign professional qualifications.

The other Middle Eastern laws are indecisive. Kuwait recognizes foreign professional qualifications, but further admits university graduates with three years' experience in any of the broad lines of accounting activities, such as auditing, teaching, or accounting in private industry or government. It is open to doubt whether an industrial or government accountant or a teacher of accountancy can efficiently practice as an auditor without the benefit of practical experience in the field.

The same criticism applies to Syria. Without allowing for any professional qualifications, Syria, as Kuwait, admits university graduates with three years' accounting experience and further admits non-university graduates with five years' experience.

The criticism becomes more marked in the case of Jordan which, though admitting professional qualifications (without

defining any), also admits university graduates with one year's accounting experience and non-university graduates with four years' experience.

Middle Eastern countries do not necessarily have to be as strict as Iraq in order to create a class of well-qualified auditors in the country. They can, however, show enough appreciation of the extent of specialization in auditing services to admit only those university graduates with advanced accounting education and whose experience includes a number of years in the offices professionally-qualified accountants.

It would not be advisable for any Middle Eastern government to get involved in granting professional certificates on the strength of examinations sponsored by the state. The level of integrity and efficiency in local state organs is not up to standards considered safe enough to be entrusted with such an important function as awarding professional certificates.

A fact to be appreciated is that no Middle Eastern Country got itself tangled up in such a problem, though Lebanon's system of "accounting experts" approved by the court has incorporated all the disadvantages of a state-controlled qualification and added to them that of creating a professional monopoly in one area of public accounting activities.

One hopes that Iraq's title of "Licenced Accountant" (given to candidates who pass a professional examination sponsored by the state) would not spread to the other countries, because of the obvious abuses it might entail. One also hopes that the services of Licenced Accountants in Iraq,

now limited to all companies but public shareholding companies, would not be extended to include the full range of public accounting activities. There has been some talk in Iraq, (and some people are pressing for it), of "liberalizing" the field of public accountancy.¹

It is not a difficult matter to provide for a minimum level of competence by statutes; but the problem of independence, and of the other matters of professional conduct, are not, however, that easy. Since they all depend primarily on personal integrity, no law can really cover the issue adequately.

There is no objection against stipulating for certain aspects of independence by law. Middle Eastern laws (Lebanon excluded) have followed in general the pattern of more advanced laws. They stipulated that the shareholders are to appoint the auditor and that the auditor should not be involved in the company's operations, or be connected with its directors by partnership or relations. They warned against soliciting business by discreditable means (some of them prohibiting advertising), prohibited incompatible activities, and insisted upon professional secrecy.

All the above are, however, tangible issues whose violation is possible, with some effort, to detect. There are, however, other more important issues, intangible by nature and thus

¹Al Bassam, op. cit., p. 407; and personal interview with Mr. Edward Haddad, audit manager of Saba & Co., Baghdad, in Feb. 1964.

difficult to legislate on, whose effect upon the auditor's independence is greater than any of those covered by the law. Examples are endless. The most obvious is the auditor's financial dependence upon a client's business, making him ready to accede to his will rather than loss the account.

Statutes are, therefore, helpless on the real question of independence. They can only lay certain foundations; but the real test is in the auditor himself, and only the auditor with a sound professional training can fully appreciate the concept of independence in his profession.

Professional societies have always done a better job at instilling in their members the importance of independence, and of controlling it, than any government.

It is, therefore, the duty of Middle Eastern governments to shift the issue of independence to the auditors themselves. Two things can be done in this respect: (a) Encourage the formation of a local or regional professional society, (now that this is formed, it should be supported)¹; and (b) encourage attempts to qualify in respectable professional societies or, alternately, insist that the period of training required of university graduates be completed under professionally qualified public accountants. Only professionally qualified persons, or university graduates with a few years professional training, should be allowed to practice as auditors. In addition, the audit of certain areas of general public interest

¹See pp. 182-185

(such as banks, mutual funds, insurance companies etc.) should be restricted to professionally qualified accountants. Ideally, only professional qualifications should be accepted in all public audits; but these, being foreign (the Middle East Society of Associated Accountants, formed in March 1964, is still too new to be considered an effective substitute for foreign qualifications), are not easily obtainable. It would not, therefore, be fair to bar well-trained university graduates totally from public practice.

C. The Duties of the Auditor

1. General Principles

In the definition of the auditor's duties, Middle Eastern laws follow the basic principles set forth by the British and/or French laws. The following are common to all Middle Eastern countries:¹

- (a) The accounts are the responsibility of the board of directors;
- (b) The accounts should be presented to the shareholders for sanction once every year in the ordinary general meeting;

¹Lebanon, Commercial Code, Arts. 161-165 and 172-176; Syria, Commercial Code, Arts. 235-248; Iraq, Commercial Companies Law, 1957, Arts. 167 and 198-213; Kuwait, Commercial Companies Law, 1960, Arts. 157-169; and Jordan, Companies Law, 1962, Arts. 170-180.

- (c) The auditors are to report to the shareholders in the general meeting on the accounts presented by the board of directors. The shareholders cannot sanction the accounts without the auditors' report.
- (d) In the fulfillment of their function, the auditors are given the right to request from the board of directors all information they find necessary.
- (e) Apart from their regular statutory duties, the auditors have the right to call an extraordinary meeting of shareholders any time they find it necessary.
- (f) First auditors are responsible to ascertain the legality of the company's formation.

The content of the accounts prepared by the directors and the matters that the auditors are requested to report about vary widely between Middle Eastern countries. These range from the very vague (Lebanon) to the very elaborate (Iraq). The result is that the form of the auditors' report in certain countries is subject to very definite legal requirements, while in other it is left totally to the discretion of the profession.

2. The Contents of the Accounts¹

It is beyond the scope of this paper to go in details into the contents of the accounts that the law requires the

¹Ibid.

board of directors to present. In short, the directors are expected to prepare a balance sheet, a profit and loss account, a report on the company's operations for the preceding year (though this is not specifically mentioned in Lebanon and Jordan), and a proposal regarding the distribution of the net profits.

In addition, the directors in Syria and Iraq are required to submit details of all outstanding commitments of the company and of all remunerations, compensations and allowances paid to any of the directors. Iraqi law further requests details of all sums spent on donations and advertising.

Following the example of the British Companies' Act, 1948, (The Eighth Schedule), Iraq and Kuwait appended to their companies' law a detailed schedule on the preparation of the Balance Sheet and Profit and Loss Account.

A French peculiarity¹ which was adopted by Lebanon and was carried over to Syria, Jordan and Kuwait is the set of provisions requiring shareholding companies to build up a statutory reserve by setting aside 10 % of their net profits. Jordanian law apparently takes this statutory reserve so seriously that most of the articles appearing under the section of the law dealing with companies' accounts are on the workings of the statutory reserve.

¹Rappaport, op. cit., p. C.5.

3. The Content of the Auditor's Report

a) Lebanon -- The duties of auditors in Lebanon start with the general statement that they "are to maintain a continuous supervision on the running of the company's operations."¹ The real meaning intended by this statement, which is carried over from French law, is not quite clear in Lebanon. It can be interpreted to make the auditor responsible for the supervision of the company's administration, something which he cannot, or should not, attempt to be involved in. He is supposed to report on the presentation of the company's financial condition not on how it is being run.

In order to appreciate the real meaning of the clause one has to dig into its origins. One explanation is that it was first included in French law (in 1935) to assert that the function of the auditor is that of continuous control in the sense that he can start his examination any time of the year he sees fit. Previous to that, companies used to withhold their books from the auditor until fifty days before the ordinary annual general meeting, making it ineffectual for him to carry out a reasonable examination.² If such is its origin, the clause can in no way be interpreted to refer to administrative supervision.

¹Lebanon, Commercial Code, Art. 174.

²G. Ripert, op. cit., p. 507; and personal interview with Mr. Joseph Tasso, accounting expert approved by court, on Aug. 28, 1964.

The Lebanese auditors are also requested, in general terms, to report at the end of every year on the company's condition, its balance sheet and the accounts presented by the board of directors; on the directors' proposal regarding the distribution of profits;¹ and -- what can be considered a surprisingly progressive requirement -- on any inconsistencies from year to year in the preparation of the accounts.

The Lebanese auditor is thus not bound by any detailed legal accounting requirements. As a result, and with the profession unorganized, one finds little similarity between the forms of auditors' reports in Lebanon. Accounting firms tend to use a form of certificate based on British or American usage. Saba & Co. use the form recommended by the American Institute of CPAs, adding to it when applicable an appropriate phrase on the distribution of dividends, thus:

"We have examined the Balance Sheet of XYZ Company as at ... and the related Statement of Profit and Loss for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion the accompanying Balance Sheet and Statement of Profit and Loss present fairly the financial position of XYZ Company at ..., and the results of its operations for the year then ended, and were prepared

¹This is obviously intended to commit the auditor to the process of verifying that no dividends are declared without their being justified by actual profits, and thus to preclude any attempts to bleed the company out of its capital or to fraudulently boost the price of its shares.

inconformity with generally accepted accounting principles applied on a consistent basis. We agree to the distribution of a dividend of ... per cent, as proposed by the Board of Directors."

Taken in the context of Lebanese or Middle Eastern practice, the reference in the above certificate to "generally accepted accounting principles" and "generally accepted auditing standards" tends to have very little meaning. There is no general acceptance of any such principles and standards in the Middle East. Those of Great Britain, the United States and France, as well as some peculiar local ones, are all being applied, depending upon the practitioner's background, with none of them gaining general acceptance.

It would be incorrect to assume that the certificate might be referring to internationally accepted accounting principles and auditing standards, for there is no such thing. What principles are generally accepted in one country are not necessarily accepted in another. Granted that the accounting profession in the various western economies is striving very hard towards internationalization, as can be perceived from the numerous accounting congresses that were held in recent years, but it is still very far from that goal.

The following is another form of certificate in use. It is a British-based one used with minor variations by Whinney, Murray & Co. and Russel & Co. and copied by many of the smaller firms:

We have examined the Books and Accounts of XYZ Company for the year ended 31st December 19.. and have obtained all the information and explanations we have required. We are of the opinion that the attached Balance Sheet and Profit and Loss Account show a true and fair view of the state of the Company's affairs as at 31st December 19.. in accordance with the best of our information and the explanations given to us and according to the Books and Accounts of the company.

The above form is at least more adapted to the country's local conditions. There is no reference to "generally accepted" principles and standards in a country where such a statement does not apply.

It is obvious that, in the absence of any specified scope of examination or any reference to some definite accounting principles or to some basic requisites in the form and content of the accounts, the auditors are left completely on their own to determine the type of examination they see fit. There would still have been nothing wrong with this had there been a recognized accountancy body in the country supervising the standards and ethics of practicing members and controlling entry into the profession. But as it is, the above types of short-form reports, so effective in Great Britain and the United States where they are backed by a rich accounting tradition and supported by court decisions, are open to abuse by persons who cannot appreciate the real meaning behind every word.

In some cases, the report itself is worded in such a manner as to effectively illustrate the inadequate scope

of examination of some auditors in connection with statutory audits. One set of accounts published in the Lebanese Official Gazette carried the following certificate:

I have examined the above Balance Sheet and the Profit and Loss account for the year ended December 31, 1962, in accordance with the books and documents of the Company and I have obtained all the information and explanations that I considered necessary for the fulfillment of my duties. In my opinion, the company keeps proper books of accounts and the Balance Sheet and Profit and Loss account are in accordance with the books of the company.¹

The basic deficiency in the above certificate is that it misses giving an opinion on the overall fairness of the accounts in representing the company's financial condition. It is not enough, according to the modern concept of the role of the statutory auditor, to state that the financial statements were extracted from properly kept books of accounts; this should be followed by an opinion on whether the company's financial condition was properly and correctly stated.

b) Syria -- As in Lebanon, the auditor in Syria is expected to "maintain a supervision upon the running of the company's operations;"² (the qualifying word "continuous" before "supervision" which appears in the Lebanese Law is omitted).

The report of the Syrian auditor should contain:³

¹The Official Gazette, No. 50, Jun. 24, 1963, Supplement, p. 1201.

²Syria, Commercial Code, Art. 237.

³ibid., Arts. 237-238.

- (1) The extent of agreement of the balance sheet and profit and loss statement with the books, their disclosure of the financial condition of the company and their compliance with the law;
- (2) Comments upon the proposals for the distribution of dividends;
- (3) The extent to which the directors and the management have cooperated with the auditor;
- (4) Any violations of the law or of the company's statutes that the auditor came across.

c) Jordan -- The auditing provisions of the Jordanian law are nearly an exact copy of those of Syria. There is thus nothing to add in this connection.

d) Iraq -- Of Middle Eastern laws, the Iraqi law appears to be the most studied and with the greatest comprehension of the role of the auditor in company accounts. It carries no such sweeping but vague statements as the one that the auditor must supervise the running of the company's operations.

The report of the Iraqi auditor shall include:

- (1) The extent to which he has been able to obtain the necessary information and explanations for performing his task;
- (2) His views about the soundness of the Company's accounts and the extent of his accessibility to the activities of the Company's branches;

- (3) That the balance sheet, and profit and loss account, referred to in the report are in conformity with the accounts and summaries;
- (4) Whether, in the light of information and explanations given to him, such balance sheet embodies all that the law and articles of association require to be included and whether such balance sheet clearly exhibits a true and correct view of the exact financial standing of the Company at the end of the financial year and whether the profit and loss account exhibits a true picture of the Company's profits or losses;
- (5) That stock-taking was carried out according to procedure and the change that has taken place in the method of the stock-taking followed in the preceding year, if any;
- (6) Whether the statements mentioned in the reports of the Board of Directors and referred to in Article 199 of the law are in conformity or otherwise with the Company's registers and resolutions;
- (7) The defaults which have taken place to the law or Company's articles in a way affecting its activities or financial standing and whether such defaults in view of the information and explanations available to him under this article still existed at the time the balance sheet was drawn up.¹

As a result, the auditors' certificate of a public shareholding company is quite an elaborate one. The following form used by Saba & Co. is a representative sample of what is required:

I have examined the Balance Sheet of ... (A Public Company) of Baghdad as at ... and the Profit and Loss Account for the year then ended and the Report of the Directors pursuant to Article 199 of the Commercial Companies Law No. 31 of 1957. I have obtained the information and explanations which in my opinion were necessary for the purpose of my audit. My audit was made

¹Iraq, Commercial Companies Law, 1957, Art. 213.

in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and other auditing procedures as I considered necessary in the circumstances.

In my opinion, and as far as my examination revealed, the Company kept proper books and records and the financial statements annexed and bearing my signature are properly extracted therefrom.

In my opinion and as far as my examination and the information and explanations given to me revealed, the Company kept suitable stores records, and a physical inventory of its stock has been made by the Company in accordance with generally accepted accounting principles and on a basis consistent with that of the previous year, and I have received the pertinent certificate from the Directors.

In my opinion, the financial figures appearing in the Report of the Directors, bearing my signature, are in accordance with the books and records of the Company; the books have been kept in accordance with the requirements of the Commercial Companies Law No. 31 for 1957, the regulations made thereunder and the Memorandum and Articles of Association of the Company, and in my opinion and to the best of my information and according to the explanations given to me and as shown by the books and records of the Company, the Balance Sheet and Profit and Loss Account exhibit a true and fair view of the state of affairs of the Company as on ... and its operations for the year then ended.

Since Iraqi law does not prescribe the same elaborate requirements on the auditor of a company with limited liability, the auditor's certificate in that connection is much shorter and expressed in more general terms. The following is again a representative sample of the form used by Saba & Co.:

I have examined the Balance Sheet of ... (with limited liability) as on ... and the related Profit and Loss Account. I have obtained the information and explanations which in my opinion were necessary for the purpose of my audit. My audit was made in accordance with generally

accepted auditing standards and accordingly included such tests of the accounting records and other auditing procedures as I considered necessary in the circumstances.

In my opinion and according to the best of my information and the explanations given to me and as shown by the books and records of the Company, the accompanying Balance Sheet and Profit and Loss Account are properly drawn up in conformity with the Law and present fairly the financial position of the Company at ... and the results of its operations for the year then ended.

e) Kuwait -- The legislation of Kuwait must have depended to a large extent upon that of Iraq in its auditing provisions. The report of the Kuwaiti auditor is very similar to that of Iraq, though with lesser elaborations. The only important omission is the one pertaining to stock-taking. Whilst Iraqi law requires the auditor to report on any changes from the preceding year in the method of stock-taking, Kuwaiti law just requires the auditor to report that the stock-taking was conducted in accordance with generally accepted procedure. The Iraqi law exhibits an awareness of the concept of consistency in financial reporting which the Kuwaiti legislator, apparently aiming at simplicity, has decided to overlook.

D. The Liability of the Auditor

1. The State of Middle Eastern Legislation

The auditor's liability is an involved legal issue which should inevitably lead us into a discussion of various foreign laws and their interpretations. Middle Eastern commercial laws are in essence based upon foreign legislation, some of them incorporating both the British and French stands on the same subject.¹

The task of analyzing the auditor's liability in the Middle East is further made arduous by the fact that the matter has not been tested in local courts. Nowhere in the annals of Middle Eastern judicial history (Egypt excluded) was I able to find a recorded case of an auditor's liability being subject to a court decision under the currently prevailing laws.² The sole exception is the auditors' liability in the bankruptcy of the Banque Fonciere Libanaise which I shall discuss further on in this chapter.

Under the circumstances, it would throw me far beyond the scope of present analysis to even attempt to give the issue a comprehensive technical coverage which takes into consideration the various foreign stands on the subject. I

¹This is most obvious in Jordan and Kuwait. While both countries fundamentally depended upon British law, they however, drew occasionally upon Syrian and Lebanese laws which were in turn based upon the French.

²Assisted by Mr. Jubran Ghantous of Saba & Co.'s Tax and Commercial Law Service, I found no such records in Saba & Co.'s files, which would have had then had they existed. Also, interview with Mr. Joseph Tasso, one of the two auditors involved in the case of the Banque Fonciere Libanaise, on Aug. 28, 1964.

shall, however, attempt to discuss the relevant provisions in local commercial laws, naturally without the support of local court interpretations but touching on what foreign interpretations are of assistance.

In any case, however, it is worth noting that legal cases against auditors are always relatively few in number. Auditors are generally very careful not to allow their professional reputation get endangered by legal suits. They always endeavor to settle any disputes by negotiations and, if unsuccessful, by arbitration.¹ It is only in extreme cases that the matter gets taken to court.

2. Types of Liabilities

As a professional person serving simultaneously the interests of his clients and of the public, the auditor assumes basically two forms of liabilities: moral and legal.

On the moral side, he is expected to be a man of integrity and independence, conscientious in the task he is entrusted with, a preserver of confidence, and a defender of the public interest.

The moral responsibilities of the auditor are formalized by professional societies and public accountancy laws. They subject the auditor to disciplinary action if he violates any prescribed regulations, standards or basic ethics. Such action

¹Interview with Dr. Fauzi Saba on Sept. 11, 1964.

might entail, in its most severe form, the loss of professional status or of the licence to practice.

Legally, he is responsible for his opinion and for the preparation of his report in conformity with the law and, we might add, with generally accepted practice. In countries where generally accepted practice has reached a reasonably well-defined state, non-conformity is as much subject to legal or professional disciplinary action as is violation of the law. Legal liability can be criminal or civil or both.

A criminal liability results in cases of willful violation of the law.

The auditor in the Middle East is criminally liable for deceit if he approves of a distribution of profits when he is aware of misrepresentations in the accounts or if he willfully submits a false report on the results of his audit. In all cases, any action of liability is time-barred on the lapse of a five-year period.¹

He is, furthermore, subject to criminal liability if he violates professional secrecy.²

A civil liability exists when, as a result of deceit or negligence in the statement of opinion, the auditor has caused

¹Lebanon, Commercial Code, Art. 107; Syria, Commercial Code, Arts. 278-280; Iraq, Commercial Companies Law, Arts. 150 and 307; and Jordan, Companies Law, 1962, Arts. 225-226. (It is surprising that Kuwait's Commercial Companies Law does not provide for the auditor's criminal liability.)

²See page 145.

financial loss to those parties relying on his report. It must naturally be proven that "there is a chain of causality between the misbehaviour of the auditor and the damage suffered."¹

Two parties might involve the auditor's civil liability: his clients (either the company itself or its shareholders) and third parties. His relations to his clients are bound by contract, hence theoretically defined. With third parties the matter is not as clear-cut; although there is no contractual relationship, yet he might considerably hurt any person relying on a false opinion by him.

A false opinion can result from deceit, which is by nature intentional; gross negligence, which can in fact amount to deceit; simple negligence; or just errors of judgement. Cases of negligence brought up against the auditor are most often the result of: (a) the existence of fraud within the company not discovered by the auditor, or (b) bankruptcies, where the ensuing investigations lay bare before public eyes any misrepresentations in the accounts or non-disclosure of material facts to which the auditor was silent.

There is a general consensus of opinion in both Great Britain and the United States that an auditor's regular examination is not expected to uncover all frauds and irregularities. If the examination was conducted with due care and in accordance with generally accepted standards, the

¹Archavlis et. al. op. cit., p. 105.

auditor cannot be held liable if he missed a fraud. The attitude of the American profession is best expressed by the Committee on Auditing procedures of the American Institute of CPAs:

The ordinary examination incident to the issuance of an opinion respecting financial statements is not designed and cannot be relied upon to disclose defalcations and other similar irregularities, although their discovery frequently results. In a well-organized concern reliance for the detection of such irregularities is placed principally upon the maintenance of an adequate system of accounting records with appropriate internal control. If an auditor were to attempt to discover defalcations and similar irregularities he would have to extend his work to a point where its cost would be prohibitive ...¹

One of the classic legal utterance on the subject is Lord Justice Lopes pronouncement in the Kingston Cotton Mill case in 1896:

It is the duty of an auditor to bring to bear on the work he has to perform that skill, care, and caution which a reasonably competent, careful and cautious auditor would use. What is reasonable skill, care and caution must depend on the particular circumstances of each case. An auditor is not bound to be a detective, or as was said, to approach his work with suspicion or with foregone conclusion that there is something wrong. He is a watch-dog, but not a bloodhound ... Auditors must not be made liable for not tracking out ingenious and carefully-laid schemes of fraud, when there is nothing to arouse their suspicion and when those frauds are perpetrated by tried servants of the company and are undetected for years by the directors. So to hold would make the position of an auditor intolerable.²

¹The AICPA Committee on Auditing Procedure, Codification of Statements on Auditing Procedure (N.Y.: The American Institute of Accountants, 1951), p. 12.

²In re Kingston Cotton Mill Co. Ltd., 2 Ch. 279 at pages 288-90, (1896); as quoted by The Inst. of CAs in England and Wales, "General Principles of Auditing," Accountancy, Aug. 1961, pp. 488-491.

Bankruptcies do not in themselves involve the auditor in any liability. It is just that his previous examinations become subject to investigations and an otherwise concealed misbehavior on his part may be brought to light. In the Middle East, for instance, the auditor has the right to call an extraordinary meeting of shareholders whenever he finds it necessary.¹ He might, therefore, be prosecuted when, aware of the financial situation of the company, he did not take any action to warn the shareholders of the impending crisis,² or when the last financial statements he certified were prepared in such a manner as to show a healthy financial situation when in fact it was not.

The auditor's legal liability for negligence is complicated by the existence of third parties who might have been prejudiced by his report. When the auditor's negligence is unintentional would he be held liable to compensate the injured parties, whether they be his clients or third parties?

¹See page 153.

²Whenever the company's losses amount to more than three-fourths of its capital, the directors (or the auditors if the directors are delinquent) should call an extraordinary meeting of shareholders to discuss the situation. (Lebanon, Comm. Code, Arts. 176 and 216; Syria, Comm. Code, Arts. 220 and 266; Iraq, Comm. Comp. Law, Arts. 167 and 255; Kuwait, Comm. Comp. Law, Art. 171; and Jordan, Comp. Law, Art. 172.)

In Great Britain and the United States, this issue falls within the scope of the unwritten common law, the counterpart of which does not exist in France or in the Middle East.

The auditor's liability for negligence under common law in Great Britain is summed up in Spicer and Pegler's *Practical Auditing* as follows:¹

This liability springs from the general principle of law that where a person is under a legal duty to take care, whether imposed by specific contract or otherwise, the failure to exercise a reasonable standard of care will make that person responsible for any resultant damage or loss to those to whom the duty is owed. This liability does not, however, extend to third parties who may have been prejudiced by the negligence, as there is no contractual relationship between the auditor and such parties.

It would thus appear that British law (as of the date of publication of Spicer and Pegler's book) did not hold the auditor liable to third parties as long as there is no fraud.²

In a recent case in 1963, however, the court adopted a new attitude with respect to professional negligence, which in essence implies that a contract or a fiduciary relationship

¹W.W. Bigg, *Spicer and Pegler's Practical Auditing* (London: HFL Publishers Ltd., 1961), p. 338.

²In *Le Lievre and Dennes v. Gould* (1897), which involves a negligent surveyor, the judge held that "a man is entitled to be as negligent as he pleases towards the whole world if he owes no duty to them. (As quoted in E.M. Taylor, *Summary of Auditing Case Law* [Cambridge: W. Heffer & Sons, Ltd., 1961], p. 68.) Taylor also refers in the same book to two other relatively recent cases involving auditors (*Candler v. Crane, Christmas & Co.* [1951] and *De Sarary v. Holden Howard* [1960]) where it was held "that an auditor owes no duty of care to any third party outside the contractual relationship existing between those who instruct him to audit the accounts and himself, provided no contractual relationship exists between the auditor and the third party in regard to the subject matter of the negligence claim."

does not have to exist in order to establish a liability for negligence upon a professional man.¹

American courts have also ruled against making an auditor liable for negligence to third parties when there is no intention to deceive. When there is such an intention, however, or when the auditor is aware that his report would be used for the benefit of third parties, American courts have exposed him to claims by third parties.²

3. The Auditor's Civil Liability in the Middle East

a) Liability to clients -- When there is a criminal liability, a civil liability can also ensue, if the deceit has caused financial loss to the company or its shareholders.

In addition, the auditor's civil liability can be engaged in Lebanon under the following sections of the Commercial Code:

(1) Art. 178 -- which states that "the auditors are individually or jointly liable, even to third parties, for any mistake committed in their audit ..."

¹Hedley Byrne & Co. v. Heller & Partners Ltd., (1963). (Discussed in "Professional Negligence -- A Dissenting Judgement Becomes Law," The Accountants Journal, July 1963, pp. 275-277.) The above article goes on to state that the judgement in this case was in fact a reversal of the one in Candler v. Crane, Christmas & Co. (1961) (see p. 170, fn. 2) and the adoption of the view of the then dissenting judge, Lord Denning, who said:

"In my opinion, accountants owe a duty of care not only to their own clients but also to all those whom they know will rely on their accounts in the transaction for which those accounts are prepared."

²S. Levy, Accountants' Legal Responsibility (N.Y.: The American Institute of Accountants, 1954), p. 29.

(2) Art. 167 -- which states that in cases of bankruptcy the commercial court has the power to hold "members of the board of directors or any other person entrusted with the management of the company or its supervision liable for the company's debts..." (The term "supervision" here could have been ambiguous, as it might be interpreted as "administrative supervision", were it not for the fact that the auditors of the bankrupt Banque Fonciere Libanaise were held liable under this section of the law.)

Nearly the same provisions are found in articles 195 and 240 of the Syrian Commercial Code, with the difference that article 240, which corresponds to the Lebanese article 167, omits the emphatic clause "even to third parties."

Jordan's provisions, while essentially similar to those of Lebanon and Syria, are so specific as to eliminate any ambiguity. Article 129 of the Companies Law, 1962 states:

(1) The chairman and members of the board of directors are also responsible towards the shareholders for willful breach of duty or gross negligence. They are not responsible in principle to other parties for such defaults.

(2) But in the case of a company's liquidation and the existence of a deficit in its assets as a result of willful breach of duty or gross negligence, the court has the power to hold the chairman and members of the board of directors, or the company's managers or auditors, liable for all or part of the company's liabilities.

(3) The court shall determine the amounts for which they shall be liable and whether such liability shall be joint or not.

¹See pp. 175-176

(4) In order to waive this liability they must prove that, in the conduct of the company's affairs, they have exercised due care as required of a paid agent.

Furthermore, art. 173 states that the auditors are responsible for any mistake committed in their audit.

Jordan's law thus specifies that the auditor is liable for willful or gross neglect; the clause is not left open to make him liable for any mistake. It is also made clear that his liability to third parties can be engaged only in liquidations. In the presence of article 129 above, the latter article 173 cannot be interpreted to refer to any kind of mistake, nor to hold the auditor liable to third parties without there being a liquidation.

The auditor's civil liability in Iraq is also engaged in liquidations only when his criminal liability has been established. Art. 150 thus states:

In the case of the Company's insolvency accompanied by a deficit in its assets, the court may, on an application presented to it, investigate any criminal liability attributed to the chairman and members of the Board of Directors or any person entrusted with any company business or the audit of its accounts. If such liability is established the Court shall compel him to pay compensation.

Aside from that, the auditor's civil liability in Iraq might be engaged by article 213 (d) which states that "in his capacity as agent for the entire shareholders, the auditor shall be responsible for the accuracy of the statements made in his report ...". This provision attributes to the auditor the capacity of an agent, and thus establishes his responsibility towards the shareholders in accordance with the general rules

of the agency contract.¹

Kuwait's commercial law does not include any provisions under which the auditor can be prosecuted criminally, and none relating to his civil liability in bankruptcies. The only provision of relevance is article 165 which, like Iraq's article 213 (d) above, defines the auditor as an agent of shareholders.

b) Liability to third parties -- In Lebanon and Syria the auditor is made liable for his mistakes, without further details; it is not clear whether such mistakes include those resulting from unintentional negligence.

Lebanon extends this undefined civil liability towards third parties. Syria extends it to third parties only in bankruptcies.

In Iraq and Jordan the auditor incurs a criminal and a civil liability in cases of deceit or gross negligence. This is extended to third parties in bankruptcies.

Kuwait's commercial law does not refer to any liability to third parties.

As expected, Lebanese and Syrian law draw their sweeping definition of the auditor's liability for his mistakes from French law.² In general terms, Jordan and Iraq's stand

¹Al Bassam, op. cit., pp. 405-6.

²Ripert, op. cit., p. 509.

engaging the auditor's civil liability in bankruptcies only when a criminal liability exists coincides with the British Companies Act, 1948.¹

c) The case of the Banque Fonciere Libanaise -- The bank was declared bankrupt by the Court of First Instance on April 6, 1964 and the bank's directors and auditors were prosecuted for deceit and gross negligence under Section 167 of the Commercial Code and made personally responsible for any deficit between the bank's assets and liabilities.² The auditor appointed by the shareholders, Mr. Joseph Tasso, was made responsible to the extent of 20% of such deficit and the one appointed by the court, Mr. Mohammed Juma, for 10%.³ The decision stated:

... The duty of the auditor extends beyond adding and subtracting figures. He has to supervise in fact the operations (Comm. Code 174) and should any violations arise, at least the flagrant ones, he should not approve of them but express his protests (V. Jurisclasseur: Societes Anonymes, Fascicule No. 2255, Parag. No. 30). Mr. Tasso was the one who submitted the report to the board confirming that Mr. George Debbas actually paid his share of the increase

¹Bigg, op. cit., p. 338.

²Al Nahar, April 9, 1964.

³The responsibilities were as follows: Mr. George Debbas, the bank's manager, 100%; Mr. Ahmad Daouk, chairman of the board, 50%; Mr. Samir Naja, director, 50%; Mr. Anis Daouk, director, 33%; Mr. Khaled Naboulsi, director, 33%; Mr. George Khouri, employee, 15%; Mr. Elias Barakat, employee, 10%; Mr. Joseph Tasso, auditor, 10%; and Mr. Mohammed Juma, auditor, 5%. The responsibilities were doubled as an extra precaution for creditors.

in capital amounting to L.L.3 million. Anybody could have very easily noticed that the payment was fictitious and that Mr. Debbas had debited the amount to his personal account ...¹

With the auditors' involvement thus explained, it is an obvious and simple case of gross negligence. It does not bring into light the weaknesses of local audit standards. Still, the Banque Fonciere bankruptcy might become a milestone in Lebanese, and possibly Middle Eastern, practice. It made all those "certificate signers" uneasy at the possible implications of their careless attitude. In this sense, and regardless of whether the hapless auditors can in the future clear themselves of the liability imposed upon them, the Banque Fonciere case may have accomplished an invaluable service to the Lebanese public accounting profession.

Before I close off this section I have one criticism on the decision. There is a departure from an obvious legal principle in the differentiation between the responsibilities of the two auditors. With both responsible for the same assignment and having by law the same duties, power and fees (Art. 173), they should naturally be held liable to the same degree.

4. Difficulties in Determining the Auditor's Liability

The auditor's relations with the company being contractual, his services should theoretically be to fulfill

¹Al Nahar, April 9, 1964.

the terms of the contract. When the audit is non-statutory, i.e. covered by a special contract for a particular assignment, any dispute would normally be settled on the basis of the terms of the contract. In statutory audits, the contract is by nature a standard one and its provisions are regulated by the law of the land and not by any written agreement between the contracting parties.¹ This is where the first weakness in determining the auditor's liability in the Middle East lies: the audit contract is not sufficiently defined in legislation; there are not enough provisions setting forth the duties of the auditor. An exception is Iraq where this matter is comprehensively covered and where high professional qualifications are demanded of the auditor.

The second problem is that the audit contract is not sufficiently defined in professional practice. There are not enough generally accepted standards of work which everybody can assume as having to be carried out. Again some Middle Eastern firms are better in this respect than others. In Iraq where only British professional qualifications exist one can assume that the standards of the British profession are universally followed. In the absence of generally accepted standards,

¹The auditor or his client cannot individually contract out of any legally required audit steps and still expect the auditor's certificate to be officially accepted in fulfillment of the legal requirements of a statutory audit. Thus any departure from basic audit procedures should be expressed in the certificate in the form of a qualification.

there is bound to be a difficulty in determining the extent of an auditor's negligence or failure in duty.

The third problem is the absence of any legal precedents, in the form of court decisions or interpretations, to supplement the law in defining the auditor's duties and responsibilities.

It still might not be as difficult to build up a case for fraud or deceit against an auditor when he is party to such fraud as it would be for negligence. To establish negligence one must be able to measure up the standards of the prosecuted auditor against those of the profession.

Lebanese, Syrian and Jordanian laws hold the auditor liable for any mistake committed in his audit; in Lebanon, even to third parties. Who is to determine the seriousness of the mistake and against what audit standards is it to be measured? Shouldn't we also differentiate between a mistake committed in good faith in the course of a reasonably well-conducted examination and another resulting from gross carelessness? Starting from the premise that no man is infallible, including auditors, how can a law hold a person responsible for a mistake committed in good faith, especially when this same law has not set forth in clear terms what it expects this person to do?

There is furthermore a misconception regarding the nature of the auditor's duties implied in the Lebanese law (art. 174), the Syrian law (art. 237) and the Jordanian law (art. 168). These laws tend to make the auditor responsible

for supervising the administration of the company's affairs,¹ something which by nature he should not be involved in. In fact, the audit function is based upon the premise that a person not connected with the administration is to examine the company's accounts. In principle, therefore, he should not be held responsible for administrative failures as long as the company's accounts which he certifies are truly representative of the state of affairs.

In Iraq and Kuwait, one wonders under what principle of law would an auditor be held liable for damages to third parties as a result of negligence on his part. Granted that in case of deceit both a criminal and civil liability can ensue towards the auditor's clients and their creditors, but would that also apply to cases of negligence without an intention to deceive? If British common law is to be used as a guide, which is very likely in these two countries, then, according to the latest British court decision, it is possible for a civil liability for negligence to result towards a third party with whom the auditor is not bound by contract or fiduciary relationship.²

¹They all state that the auditor is responsible to check the running of the company's operations.

²Hedley Byrne & Co. v. Heller & Partners Ltd. (1963), (See p. 171, fn. 1.)

CHAPTER VI

PROFESSIONAL PRACTICE IN THE OTHER
MIDDLE EASTERN COUNTRIESA. Professional Structure1. Professional Organizations

a) An unorganized practice -- Apart from Egypt, there never was in the Middle East a regional or national accountancy body to organize professional practice by granting professional qualifications, and at the same time promote the application of respectable standards of work and behavior.

This deficiency has resulted, primarily, in wide differences in the auditing standards and accounting principles applied by the various accountants. Accountants in practice are naturally apt to be of different training and educational backgrounds. They are consistently drawing upon different foreign sources for their accounting and auditing principles (this is assuming they are drawing on any at all) and are bound to be affected by the various, sometimes conflicting, trends or schools of thought evolving in the more advanced countries. Middle Eastern laws are of no help in this matter as most of them do not show any real awareness of the existence of developed accounting principles.

It is a truism that two accountants with the same set of figures can come up with two different set of statements while both using "generally accepted accounting principles". In more developed countries, however, there is some sort of general acceptance of basic accounting principles and auditing standards due to the influence of the law and official regulatory agencies and the recommendations of recognized accountancy bodies. In the presence of some conflicting but generally accepted principles, the final criterion in the acceptability of financial statements is always the consistency of their application; and the final criterion in the quality of an audit is its measurement up to the standards of the profession.

In the Middle East, however, one cannot expect much similarity in the interpretation or application of accounting principles, nor can one expect any uniformity in auditing procedures. This is the case not only between the qualified and the non-qualified accountants, but also between the qualified accountants themselves since they do not all have the same background.

The absence of any unifying body of accountants in the area has thus resulted, among other things, in a complete lack of uniformity in financial reporting. This makes it practically impossible to undertake any comparative analysis of the financial condition and operating results of companies or industries. Furthermore, in the absence of any recognized set of auditing standards, there is a general ignorance of the type

of examination conducted by auditors; hence, an interested party cannot place any reliability in an auditor's certificate unless the auditing firm is of recognized standing.

Another deficiency whose cause can be traced to the absence of any recognized local accountancy body is the entry of a large number of semi or non-qualified persons into public accounting practice. This is more marked in some countries than in others, and is most serious in Lebanon. Not all businessmen, not even the more sophisticated, can appreciate the difference between a well-trained and a semi-trained public accountant, and not all businessmen can be expected to appreciate the professional qualifications acquired outside the area. There are a number of persons with certificates from correspondence schools in England who claim to be fully-qualified persons. A number of businessmen are thus left to the mercy of quacks out of their inability to determine what makes a good public accountant.

A third deficiency is the dirth of ethics in the practice of the profession, especially in Lebanon. With no accountancy body to supervise the ethical conduct of practicing accountants, professional practice is left to abuse and loss of dignity at the hands of pretenders whose sole purpose is personal income, whatever the means.

b) The Middle East Society of Associated Accountants -- After many years of waiting, the first accounting society in the area came into being on March 12, 1964. Its birth owes a

great deal to Mr. Fuad Saba, who has been elected as its first president.

The objects of the Middle East Society of Associated Accountants are just what any enlightened accountant or businessman can hope for. They are worth mentioning here in the same words of the Society's constitution:

- (1) To elevate the professional, ethical, moral and educational standards of the accounting profession;
- (2) To assist in the maintenance of high standards in licensing persons qualified to be public accountants;
- (3) To develop and maintain standards for the examination of candidates for admission to Fellow membership;
- (4) To engage in and assist in the development of accounting research, and improve technical accounting principles and Arabic accounting terminology for local use;
- (5) To develop and improve accountancy education;
- (6) To encourage the professional exchange of knowledge, advice and assistance with accountants of other countries;
- (7) To supply its members with information on developments in accountancy, and to encourage the exchange of knowledge among its members in its meetings, conferences and conventions.¹

Members of the recognized British accountancy bodies and of the American Institute of Certified Public Accountants are automatically accepted in the Middle East Society. In addition, admission is open to any secondary school graduate who has five years experience in an auditing post with a member of the Society and who passes its preliminary and final examinations.

¹Middle East Society of Associate Accountants, Constitution, Art. I, Sec. 2.

The contents of the examinations are as follows:¹

(1) Preliminary:

- (1) Bookkeeping and Financial Statements,
- (b) General Commercial Knowledge,
- (c) Elementary Economic Theory and History,
- (d) Elementary Auditing,
- (e) Elementary Mercantile Law, and
- (f) Credit, Money and Banking.

(2) Final:

- (a) Advanced Accounting Problems (in two parts),
- (b) Advanced Auditing,
- (c) General Company Law,
- (d) Mercantile Law, and
- (e) Financial Statement Analysis (or Income Taxation).

Furthermore, the Society is ready to admit the following persons as members, upon the recommendation of two Fellows of the Society: Persons with a secondary school education who have been in an auditing position or practicing for their own account as public accountants for at least five years, provided that at least three of the five years were in the position of manager or sole practitioner. Applications from such persons are accepted for only one year from the date of official registration of the Society.

This grandfather clause, as it is usually called, is obviously intended to preserve the acquired rights of existing practitioners. This is customary practice in any newly-formed society of this sort. Actually, when practitioners already in practice are admitted to the Society, they become committed to

¹M.E.S.A.A., By-Laws, Art. 9, Sec. 2.

follow its rules and ethics; it is, therefore, one way of improving present standards. My personal criticism, however, is to the provision allowing managers to become members. With no reflection upon the quality of the managers in some audit firms, there are undeniably a number of unsuitable managers in a number of others. Moreover, managers have earned no acquired rights as public practitioners, and there is no need to worry about their standards of ethics once their employer is admitted to the Society. The protection against admitting undesirable managers afforded by the clause that they must be recommended by two Fellows of the Society is too subjective.

Members of the Middle East Society are called Fellows and they use the designatory initials of F.A.A.

The Middle East Society is now registered only in Lebanon. It has not yet been officially recognized in Iraq and Kuwait where the law specifies the names of approved accountancy bodies.

2. Firms in Practice

a) The professionally qualified -- The Middle East Society is still too recent to be considered as a provider of professional qualifications. Therefore, existing professional qualifications in the Middle East are all acquired from foreign countries, mainly Great Britain.

The accounting firms having professionally qualified owners or partners in the Middle East are the following:¹

¹Reference is made only to those countries forming part of our study.

- (1) Saba & Co. -- offices in Lebanon, Syria, Iraq, Jordan, Kuwait and Saudi Arabia. It is made up of the following partners, all Arabs:
- (a) Fuad Saba, F.A.C.C.A. (1929) -- residing in Lebanon.
 - (b) Karim Khouri, F.A.C.C.A. (1947) -- residing in Lebanon.
 - (c) Najib Dabbikeh, non-qualified -- residing in Morocco.
 - (d) Suhail Saba, non-qualified -- residing in Lebanon.
 - (e) Fawzi Saba, CPA from Virginia, U.S.A. -- residing in Lebanon.
 - (f) Aldo Naim, A.A.C.C.A. (1956) -- residing in Iraq.
 - (g) George Ghali, A.A.C.C.A. (1958) -- residing in Libya.

Saba & Co. also has on its staff three chartered accountants: an Egyptian stationed in Lebanon and two Iraqis in Lybia.

- (2) Russel & Co. -- offices in Lebanon, Syria and Jordan, (Syrian and Jordanian offices generally inactive). It has two British partners in the Middle East, both chartered accountants, residing in Lebanon: H.W. Wilson and J. Scott Smith.
- (3) Whinney, Murray & Co. -- offices in Lebanon, Iraq and Kuwait, and a registration, but no permanent office, in Jordan.¹ It has the following partners in the Middle East, all chartered accountants.

¹It serves its few Jordanian clients from its Beirut quarters. (Personal interview with Mr. H. Traboulsi.)

- (a) R. Grant -- Britisher, residing in Lebanon.
- (b) G. Maksoud -- Lebanese (formely Egyptian), residing in Lebanon.
- (c) C.G. Bell -- Britisher, residing in Iraq.
- (d) R. Jackson -- Britisher, residing in Lebanon.

In addition, Whinney, Murray & Co. has six British and one Egyptian chartered accountants on its staff in Kuwait, and three British and two Iraqi chartered accountants on its staff in Iraq.

- (4) Fouad Abu Izzedin, F.A.C.C.A. (1950) -- offices in Lebanon and in Riyad, Saudi Arabia.
- (5) Nawar & Co. -- offices in Lebanon, Kuwait and Saudi Arabia. It is composed of two partners, both Egyptian chartered accountants: Y. Nawar and M. Mikhael.
- (6) Fuad Hawit, F.A.C.C.A. (1941) -- office in Ramallah, Jordan.
- (7) Al Hawiz & Co. -- offices in Iraq and Lebanon, (Lebanese office inactive). It is composed of two Iraqi chartered accountants, both residing in Iraq: Nazhat Al Tayib Al Hawiz and A.M. Al Shamri.
- (8) Mrs. Vivian Mohamed, chartered accountant -- offices in Iraq.
- (9) Farid Mansour, chartered accountant -- office in Kuwait.
- (10) Adib Khouri, A.A.C.C.A. (1964) -- office in Beirut.

- (11) Shawki Dallal, F.A.C.C.A. (1938) -- office in Baghdad.
- (12) Issa Al Ayyouti & Co. -- offices in Kuwait, Saudi Arabia and Iraq. It has only one qualified partner, A.M. Vestarkis (A.A.C.C.A.), who operates in Iraq under his own name.
- (13) Kean, Talor & Co. -- offices in Beirut. It is a British firm of chartered accountants which has only recently been established in the country.
- (14) Mufid Mirza and Abdul Aziz Hafiz, both Iraqi chartered accountants -- offices in Iraq.

b) International affiliations -- of the Big Three of Middle Eastern public accounting, only Whinney Murray & Co. (considering the various partnership arrangements they have all over the world) are of an international scale. The other two firms Saba & Co. and Russel & Co. practice in a smaller geographical area: Saba & Co. have branches all over the Arab world and Cyprus; and Russel & Co. have branches in Lebanon, Greece, Cyprus, Sudan and Ethiopia, and registrations, but no active offices, in Syria and Jordan.

Both firms, however, have international connections. Saba & Co. have a correspondent arrangement with Arthur Andersen & Co. whereby they are referred Arthur Andersen's Middle Eastern assignments and they refer to Arthur Andersen their international assignments.¹ Russel & Co. are in

¹As of July 1964, a partnership was formed between Arthur Andersen & Co. and Saba & Co. under the name of Arthur Andersen, Saba & Co.

partnership in the Middle East with Arthur Young & Co. under the name of Arthur Young & Co. They handle all the Middle Eastern assignments of their international affiliate under their affiliate's name.

There are additionally a few international accounting firms with audit assignments pertaining to branches of foreign firms in the Middle East, but with no established offices or correspondents in the area. They usually handle the larger assignments themselves (for example, Haskins & Sells, who audit Aranco, and Price Waterhouse, who have a number of local assignments) and refer to the locally established firms the smaller ones.

c) The non-professionally qualified -- It should be again pointed out that the term "non-professionally qualified" as it is used in this thesis refers to those persons who have not earned their accounting qualifications through a recognized professional body, and thus are not bound by the ethics and standards of any society. This in itself need not reflect upon their ability or integrity. In any case, all such practitioners in the Middle East, excepting Lebanon, are properly licenced in their respective countries, and must have thus attained the legally required minimum level of training and education.

In Iraq, there are no non-professionally qualified persons in public practice. The public accountancy law is rigid in this respect; it allows only professionally qualified persons to certify the accounts of public shareholding companies. Though persons with lesser qualifications are allowed to certify the accounts of other types of companies, only two persons have been licenced under this clause, and they were not able to build up a significant practice.

In Kuwait, there are two non-qualified firms: Zahar, Hamed & Co. and Abdul Majid Hamadeh (former branch manager of Saba & Co., Kuwait). Licencees under the public accountancy law are over 40 in number, but most of them are professionally-qualified or employed by the major accounting firms, or in commercial employment.¹

In Jordan, there are quite a few non-qualified practitioners, but the only ones of significance are the firm of Khodr, Ramadan & Co. whose founder Mr. George Khodr was a public auditor since the 1940s in Palestine.

Similarly in Syria, there are a number of such practitioners, but the only significant ones are Saadi, Tillo & Co. and Nuhad Ibrahim Pasha. Both these firms are only of recent history. They started acquiring importance in the late 1950s; until then the market was a thin one divided between

¹Personal interview with Mr. Talal Abu Ghazaleh, manager of Saba & Co. in Kuwait, on May 27, 1964.

Saba & Co., Russel & Co., and a few individual "certificate-signers".¹

In Lebanon, the number is the greatest and the effect most significant. Their total cannot be determined with any reasonable degree of accuracy. There are in Beirut at least the 72 "approved accounting experts", but a number of them are only part-time practitioners. In any case, the majority of non-qualified public accountants are active mostly in bookkeeping services. The most important of the non-qualified firms are:

- (1) Attiyyeh Auditing and Accounting House
- (2) Katbeh Accounting Office
- (3) Bahout Accounting Office
- (4) Benny Aweida & Co.
- (5) William Mitri & Co.
- (6) Farajallah Fayad and Joseph Tasso
- (7) Andrawes Tabbah
- (8) Saba Accounting & Auditing House (Joseph Saba)
- (9) Al Bawarshi
- (10) Nakhle Khalifeh
- (11) Elias Basseel

¹Interview with Mr. Nuhad Ibrahim Pasha.

3. Types of Services Offered

a) General -- The major types of services are: Auditing, tax services, bookkeeping services, and systems consulting. Occasionally there are some other services offered, e.g. arbitration, but they are too few and too occasional to be considered as significant in relation to the practice as a whole. One firm (Saba & Co.) offers a service not usually handled by public accountants -- registration of trade marks and patents.

In general, however, the services of Middle Eastern accountants are no different than those offered by the profession anywhere in the world. It is just that certain activities are more important to some firms than others, for instance auditing is the primary activity of the larger firms while for the smaller firms it is secondary to bookkeeping services.

b) Auditing -- Auditing is the bread and butter of the profession and the major activity engaged in by the larger accounting firms. Auditing services are of various types, generally classified as: Statutory audits, which are required by law, and non-statutory audits, which are beyond the scope required by law.

The lesser qualified accountants are rarely sought in other than statutory audits and usually only by the smaller companies. In most cases of the sort they end up as certificate-signers for those companies who want to comply with

the text, rather than the spirit, of the law at the least possible expense. This phenomenon is most marked in Lebanon.

The more important business firms which are conscious of the importance of a certificate by a respected auditor on their financial statements usually engage the services of the professionally qualified accounting firms, whether they are required to do so by law or not.

By definition, non-statutory audits are conducted at the request of the businessman on his own initiative. There is, therefore, the implication that the engaging party is interested in the auditor's competence. Assuming that he can properly evaluate the auditor's competence, the businessman is more likely than not to go to those persons whose competence is evidenced by the proper qualifications.

Another form of audits occasionally of importance to some auditors is that of government enterprises or of enterprises in which the government has a financial interest. This activity was never of importance in Lebanon and Jordan, and only rarely in Syria. It is of greatest significance in Iraq, due to the traditional appreciation of the auditor's role by the Iraqi government.

The Iraqi government had no problems with the selection of auditors before 1954 (there were only two of them, Whinney Murray & Co. and Saba & Co.), and government enterprises were few in number. In later years, however, the number of government enterprises started increasing and so was the number

of auditors. In an attempt to avoid any accusations of favoritism, the government started offering the audit of its enterprises on a tender basis, inviting all accounting firms to join. Saba & Co., holding on a point of principle of not participating in public bids, never took part in these tenders, but I understand that the other accounting firms participated.¹

Also to be considered are the audits of oil companies which, in money terms, are the most significant in the Middle East and the reason for the establishment of many audit offices in the oil producing areas.

The biggest of oil companies' assignments are handled by two firms: (a) Whinney Murray & Co., which audits the Iraq Petroleum Company (and its sister companies, the Mosul Petroleum Co. and the Basrah Petroleum Company), the Kuwait Oil Co., the Bahrain Petroleum Company, and the Qatar Petroleum Co.; and (b) Haskins & Sells which audits Aramco. It is to be noted that Haskins & Sells has no established office in the area and, contrary to Whinney Murray & Co., has not attempted to enter the local public accounting field. Saba & Co. has one smaller oil Company assignment: Getty Oil Company in the Kuwait/Saudi Arabia Neutral Zone.

c) Bookkeeping services -- The Big Three (Saba & Co., Russel & Co. and Whinney, Murray & Co.) do not offer any bookkeeping services. Other qualified practitioners

¹Interviews with Mr. Fuad Saba and Mr. Edward Haddad.

occasionally offer such services, but they do not form a substantial portion of their billings. This particular section of the market is, therefore, dominated by the lesser qualified practitioner and the part-time bookkeeper.

d) Tax services -- In the Middle East tax returns are not required to be certified by independent accountants. Normally, however, all companies who have their accounts audited submit a copy of their certified statements to the tax authorities, along with the required tax returns. Some companies, usually foreign ones, ask their auditors to prepare the tax returns and submit them to the tax department on their behalf, but this is more of a favour than a special activity. Public accountants naturally advise their clients on all relevant tax matters, but this is usually done in the normal course of the audit. Tax services as such do not, therefore, independently account for any significant share of public accounting activities anywhere in the Middle East.

In Lebanon, and to a lesser extent in Syria and Jordan, some of the smaller practitioners are involved in tax services in an unprofessional manner, by acting as middlemen between businessmen trying to avoid taxes and graft-ridden tax officials. In these cases, the success of the accountant depends upon his intimacy with the officials of the tax department.

e) Systems consulting -- Systems services are relatively new in the Middle East and are offered only by the more qualified accounting firms. Saba & Co., however, is the only one with a specialization in the field and with a separate department for the purpose. The other firms do offer one range of such services, the installation of accounting systems, by making use of their audit staff.

As things stand now, the bulk of systems jobs in the Middle East is handled by two firms: Planus, a leading French consulting firm, which dominates the Lebanese market; and Saba & Co., which dominates the rest of the area. A learned confidential source estimates Planus share of systems consulting in Lebanon at about 70%; Saba & Co., 15%; and others, including accounting firms and professional consultants, 15%.

Outside Lebanon, Saba & Co. has practically no rivals. Their problem is not to fight competition, but to educate businessmen to appreciate this new type of service. They hold important government assignments in Iraq, but their major market is in Saudi Arabia and the Arabian Gulf, where, as a result of the petroleum boom, a number of enterprises have grown very large in a very short time. As a consequence, and plagued by a deficient business tradition and a dearth of qualified management, they started facing immense organizational problems, enough to make them ready to pay the relatively expensive services of professional consultants.

f) Legal experts in commercial disputes -- This is a special public accounting activity formally recognized only in Lebanon and carried out solely by the "accounting experts" approved by the court. Actually these accounting experts are officially referred to as "accounting and commercial experts."

In commercial disputes reaching the court, the case is sometimes referred to any of the accounting experts for an objective appraisal of the situation. The expert's function consists of studying the matter under dispute and submitting his findings to the court. The court's decision is based upon the expert's report, and the court determines the expert's fee and who of the parties bears it.

g) Miscellaneous services -- Public accountants in the Middle East, as anywhere else in the world, perform various other advisory services, mostly of a quasi-legal nature. Examples are: assisting in the formation of companies (in fact, first auditors are responsible to ascertain the legality of the company's formation), drawing up simple contracts, legal advice on labor and personnel problems, assistance in personnel recruitment, etc... The public accountant in many instances, especially in smaller businesses, ends up as the company's general practitioner -- or family doctor -- referring his client to specialists, such as lawyers, only when the problem

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becomes too specialized for him to handle properly.¹

4. Market Structure

Saba & Co., Whinney Murray, and Russel & Co. are, as I said, the Big Three of Middle Eastern public accounting; between them they control the bulk of the market.

Auditing is by far their most important activity and their biggest money earner. Management consulting has been gaining importance in recent years, but it still does not form a large percentage of total activity.

It was not possible for me to obtain any reliable statistics on the size, in money terms, of the audit market in each of the Middle Eastern countries, as none of the accounting firms were willing to disclose their gross billings or the total number of their audit staff.

From one source, who prefers not to be quoted, I was, however, able to obtain rough estimates of the distribution of the audit market between the various firms. This information is tabulated herebelow; but I must warn the reader that these are only estimates based on reasonably well-informed sources; the picture might possibly be somewhat different if all required data were available:

¹
The overlap between the activities of public accountants and lawyers has created a cause for friction between both professions in the U.S. where, in at least two instances, the issue was taken to court. (Wise, op.cit., part I, p. 155.)

TABLE 6

ESTIMATES OF PERCENTAGE SHARES OF AUDIT MARKET AS OF 1963
(BASED ON GROSS BILLIS)

Firm	Lebanon	Syria		Jordan		Iraq		Kuwait	Saudi Arabia		
		Damascus	Aleppo	Amman	Jer.	Baghdad	Basrah		Jeddah	Riyad	Dammam
Saba & Co.	10	30	30	65	4	20	25	25	23	25	35
Russel & Co.	30										
Whinney Murray & Co. (excluding oil cos.)	20					30	45	30			
Saadi Tillo & Co.		30									
Nuhad Ibrahim Pasha			25								
Khodr Ramadan & Co.				20	3						
Mufid Mirza & Abdul Aziz Hafeth						15	5				
Nawar & Co.								10	20	20	23
Al Hawiz & Co.						23	20				
Issa El Ayyouti & Co.						5		10	50	40	42
Fouad Hawitt					2						
Others	40	40	45	15		7	5	25	7	15	-
TOTALS	100	100	100	100	100	100	100	100	100	100	100

Source withheld by request.

5. The Setting of Fees

Fees for audit jobs are determined in either of two ways: A flat rate for the whole assignment or according to the number of hours expended on it. There are variations combining both methods, such as assignments taken on an hourly basis but with a ceiling for the maximum total charge.

The hourly rate method is more ideal; it preserves the right of the auditor to do an honest job regardless of the amount of time it takes. It is, however, open to abuse,

especially in an area such as ours where professional integrity is yet far from satisfactory. The forces which act against the universal adoption of the hourly rate basis of charge are: (a) the risk of unproductive or idle hours by the auditor's staff being charged to the client; (b) the inability of the client to keep track of the time of the auditor and his staff, and (c) the inability of the client to know in advance the cost of the audit. Such factors are very important in the Middle East and very few local businessmen are willing to assume the risk of engaging an auditor on an hourly-rate basis. Only the large audit firms, whose integrity is well-established, are successful in negotiating such a basis of charge for their services and the clients are more often foreign companies accustomed to such a billing system.

When an hourly rate method is used, there is always a scale of charges covering the various categories of audit workers (i.e. partners, audit managers, senior auditors, semi-seniors and juniors).

I have compiled the following table from various confidential sources to show the ranges of hourly rates applied by the three big accounting firms (since they are the only ones who have any significant billings on an hourly rate basis) on audit assignments. The rates shown are only near-approximations of the average and not meant to cover special situations. The partners' rate per hour is the least

standardized, even within the firm itself, as it is greatly affected by the type of assignment.

TABLE 7
RANGES OF AUDIT CHARGES PER HOUR
(in U.S. Dollars)

Country	Partner	Manager	Senior	Semi-Senior	Junior
Lebanon	10.0-15.0	7.0-10.0	4.0-7.0	3.0-5.0	2.0-3.5
Syria	6.0-19.0	4.5- 5.5	4.0-4.5	3.5-4.0	2.5-3.5
Jordan		5.0-6.0	4.0-5.0	2.5-3.0	2.0-2.5
Iraq (Baghdad)	10.0-15.0	7.0-10.0	4.5-6.0	3.5-5.0	3.0-4.0
Iraq (Basrah)	10.0-15.0	5.5- 7.0	3.5-4.5	3.0-4.0	2.5-3.0
Kuwait	12.0-20.0	10.0-12.0	5.5-7.0	4.5-6.5	4.0-5.5

Considering the number rather than the money value of assignments, most audit assignments are handled on a fixed-fee basis. In money terms, the picture turns more in favor of the hourly basis of charge as the very large assignments are almost always handled on an hourly basis. Accounting firms have enough experience in the business to be able to quote a fixed fee in advance, but they usually try to negotiate a more flexible charge for the first year in order to appraise the amount of time the job takes more accurately.

There are, however, other considerations affecting the amount of fixed fee quoted. The most important is the number of idle hours the auditor has among his staff, and whether the

job is an off-season one. Auditing is a seasonal business, the biggest rush being at the end of the year and the first few months of the year and the slackest months being in summer. An assignment which can be completed within the summer months may induce the auditor to quote a lower than regular fixed fee, enough to cover his variable costs and recuperate as much as possible of his fixed costs (which are mainly the salaries of his staff).

Fixed-fee assignments present various problems to the auditor. The most important ones are:¹

- (a) Unforeseen complications in the assignment are not covered and may result in either a loss to the auditor or a laxness in his examination;
- (b) The client may start shopping around for the lowest quotation;
- (c) The extent of the auditor's examination may become a subject for dispute if the client expects more from the auditor than the latter can afford within the limits of his fixed fee;
- (d) Once a fee is quoted for one year it is often very difficult to change it in subsequent years if the job becomes more entangled. Similarly, the client may keep

1

Such problems are common everywhere and are not particular to the Middle East. J.K. Lasser refers to some of them in his Standard Handbook for Accountants (N.Y.: McGraw Hill Book Co. Inc., 1956), p. 1.68-1.69.

paying a higher than normal fee over the years even if the auditor is taking lesser time as he gets more acquainted with the job.

As with everything else, the question of fees has its peculiarities in Lebanon. I have mentioned previously that the Lebanese Commercial Code provides for the appointment of two auditors, one elected by shareholders and another by the court, both having an equal amount of fees. This clause becomes quite a burden for large enterprises where audit fees run in the thousands of pounds. It would be quite unfair if the shareholders-appointed auditor submits a large bill as a result of extensive work in order to be countered simultaneously by an equal bill from the court-appointed auditor who does nothing but sign the certificate. What happens, however, is that the shareholders appoint their auditor for a nominal amount (rarely above L.L.500.00) and the balance of the fees is charged separately as "financial charges" or "advisory fees". In this manner, the court-appointed auditor can claim only the L.L.500.00 considered as the regular audit fees.

This manner of avoiding a double charge from the auditors would have been an acceptable one were it not for one drawback: it places the auditor in a subordinate position to the company's directors who end up as the party approving the real audit fee (disguised as advisory or financial fees), while the shareholders approve only the nominal fee.

What it all amounts to is that the inherent aim of the clause providing for the appointment of the auditor by the shareholders is defeated. In an attempt to circumvent the law, the Lebanese auditor (the qualified Lebanese auditor to be more exact, for it is he who faces more of such situations) has placed himself at the mercy of the directors, thus putting his independence, the real cause of his existence, in precarious balance.

6. The Problems of Staff

The hierarchy in a public accounting firm starts with the partner (or sole owner) at the top down to audit manager, senior, semi-senior and junior auditor. The smaller the firm the shorter the hierarchy until one gets to the sole practitioner who is all five categories in one.

There is no sense in analyzing the quality of audit staff as this varies widely between firms and between countries. Talent is obviously more available and at lower pay in Lebanon than in Iraq or Kuwait, which explains the lower audit charges in Lebanon. Not even the staff of the Big Three accounting firms can be evaluated solely on the basis of educational or professional qualifications, as a number of them have none, their most important asset being experience.

Whinney Murray's managers and seniors appear to be the most qualified. They have seven chartered accountants (excluding partners) on their staff in Kuwait and five in Iraq

as compared to none in Saba & Co. None of Saba & Co.'s seniors in the whole area (I am not considering Libya), and only one of their managers (Beirut branch), is professionally qualified. Russel & Co. also have no professional qualifications among their staff in the area. Anyway, this is not the fault of the accounting firms; there are just not enough professionally qualified local accountants to go around.

The accounting firms have been apparently doing well with university graduates and non-graduates who worked their way up in the firm. Their biggest problem, however, is staff turnover.

A public accounting firm is looked upon as the best training ground by any person planning on a career in accountancy; and ambitious young people do not seem to last long in the employ of an accounting firm once they gain enough experience. The main reason is that the ladder of advancement in an accounting firm is not high enough. Once a person becomes a senior, he may rot before room can be found for him as a manager, and then usually in some desert outpost. Another reason for this staff turnover is that the salaries in accounting firms are generally lower than those paid for the same qualifications in business. Businesses usually love to steal away audit staff because of their varied experience. If left unsolved, this whole problem can result in a certain mediocrity in the quality of the remaining audit staff.

Accounting firms have been trying to remedy one part of the problem, that of salaries; they cannot do much about the other part. Saba & Co., who were plagued by a high staff turnover in all their branches, adjusted their scale of salaries radically upwards. This cut down greatly on turnover. What helped them also is their expansion over a wide geographical area. They have avoided losing some of their staff who reached their saturation level in one branch by moving them to a higher position in another branch. In this respect they offer local employees a better chance than does Russel & Co., who do not have as many branches, and than Whinney Murray, whose policy is to have only chartered accountants in managerial positions and, in the absence of enough locals with such qualifications, find it necessary to fill their upper vacancies with Britishers.

B. Professional Standards

1. Ethical Standards

The professionally qualified accountants of the Middle East generally adhere to the ethical standards of the professional bodies they belong to. Before the creation of the Middle East Society of Associated Accountants in March, 1964, there were only the British-qualified accountants, (with one sole exception, Mr. Fauzi Saba who is a CPA from Virginia, U.S.A.). Thus British ethical standards are generally followed. There were cases of breaches of such standards, but

they were individual incidents duly reported by the breacher's rivals to the accountancy body he belongs to.

Furthermore, in such countries as Iraq, Jordan and Kuwait, where British business influence is the greatest and the smaller non-qualified accountants, who usually have had their initial training in one of the qualified accountants' offices, have tended, to a certain extent, to emulate their former masters, at least in the obvious.

In Lebanon, however, ethical standards in the British or American sense are not only violated, but actually abused. Newspaper advertising is a common thing; the most conspicuous example is Atiyyeh Auditing & Accounting House whose advertisements have appeared continuously in papers for number of years. Calendars and diaries are given as publicity material by Mr. Farajallah Fayad and Mr. Joseph Tasso, who are among the better-known accounting experts at court. One could have even watched in April 1964 a television advertisement for accounting services by another accounting expert, Mr. Bishara Bahout.

Furthermore, whereas British and American ethical standards do not allow a person to use other than his professional title (such as "chartered accountant", or "certified accountant") on his letterheads, persons as the ones referred to above go on to enumerate whenever they have the chance all the various services that they perform. One extreme case is the following magazine advertisement by

Abu Shakra Accounting Office: "Auditing of Accounts, Investigations, and Photocopying of Documents."¹

The conditions of Lebanese practice being as they are, one can imagine that the more sophisticated ethical standards, such as communicating with the previous auditor before accepting an assignment, as literally unheard of.

Many accountants in Lebanon like to operate under impressive company names (such as, Atiyyeh Accounting and Auditing House or Abu Shakra Accounting Office or the Middle Eastern Accounting Co.), or they would call their practice by their name and add "& Co." after it without their having any partners. One court-approved accounting expert, Mr. J. Kfoury, signed the 1961 accounts of the Bank of Lebanon and the Middle East as a "chartered accountant", even though he is not; (probably not knowing that such a title is reserved to members of accounting societies chartered by the British crown.)

Price-cutting is also common practice in Lebanon. This is indulged in continuously by the smaller accountants. They are at their worst when acting as court-appointed auditors if there is a well-known firm acting as the shareholders-appointed auditors. In these cases, they might not even look

¹Al Masaref, (Arabic periodical on banking), Sept. 1963, Beirut. (This is reminiscent of British practice in the early days of its inception when one public accountant advertised the fact that he was also a dealer in tinsplates. See p. 17, fn. 1.)

at the books; they sign the certificate on the strength of first auditors' certificate, and any fee for such a service is good enough.

The implication of all such deviations from accepted ethical standards is their effect on the independence of the public accountant. When a person is so eager for business as to go on television exhibiting his adding machines or advertise his photocopying machine in a newspaper, one can imagine that he does not even have the question of independence on his mind. He is subordinated completely to the interests of his clients, or rather to the income he gets from them, and is ready to do anything to keep their business. As an auditor representing the interests of shareholders or of third parties, such a person is just useless. What certified financial statements he gives out cannot be respected for what they should be -- and they are not -- except probably by the tax official with whom he is in collusion.

In the other Middle Eastern countries, breaches of ethics are not such an obvious phenomenon as in Lebanon. For instance, advertising is not resorted to; in fact, it is specifically forbidden in Iraq and Jordan and its prohibition is implied in Kuwait. The use of trade names other than personal names is not a known practice. There are a few instances of persons setting themselves out as partnerships when they in fact have no partners. If there are other unethical practices -- and there very well could be -- such

as negligence in duties, direct solicitation of business and price-cutting, they cannot be measured.

The Iraqi government has created a controversial ethical issue by occasionally offering the audit of some of its enterprises for public bid. Saba & Co. have taken the more defined American view of public bids and refused to participate, but the other accounting firms did.

2. Standards of Work -- Auditing Procedures

a) General -- As this paper is not intended to be a textbook on auditing, it is not expected to dwell upon the details of auditing procedures applied in the Middle East. There is no sense in analyzing the activities of the lower-grade practitioners, and those who can be fitted in the designation of professionals follow, or attempt to follow, the broad lines of auditing principles of more advanced countries.

Middle Eastern practice is dominated, as we have seen, by three major accounting firms, and these have tended to set the pattern of auditing practice in the whole area. Russel & Co. and Whinney Murray & Co. are British firms and their procedures are those of the British profession. Saba & Co. has been, since the late 1950s, unconditionally applying American procedures down to their very details. Other serious practitioners have tended to imitate British practice. Saba & Co.'s introduction of American principles is only recent and

has not yet had time to significantly affect local practices.

b) Disclaimer letter or letter of arrangement -- This purely American concept is applied only by Saba & Co. The disclaimer letter is written by the accounting firm to its client "pointing out that the main object of the audit is the examination of the financial statements, and that it is not designed and cannot be relied upon to disclose defalcations and similar irregularities."¹

c) Internal control -- Any serious audit must take into consideration the internal control system of a company so as to determine the extent of sampling and other audit work. This is more important in an area such as the Middle East characterized by the smallness of the size of the business firm. In large companies, which tend to have a more scientifically built organizational structure, the auditor does not usually have the problems of weak internal controls and poor record-keeping that he faces in smaller companies.

Saba & Co. checks the internal control system by means of a questionnaire completed by the senior auditor. The methods of the other firms are not as formalized; the evaluation of the internal control system is left to the discretion of the auditor-in-charge.

¹Shearer, op. cit., p. 201.

d) Cash and bank accounts -- Cash is counted at least once a year, sometimes twice, with one of the counts being a surprise one. Bank accounts are usually confirmed by direct communication with the bank.

e) Accounts receivable -- As a rule, Saba & Co. confirms the receivables by direct communication with the debtors. The other firms apply this procedure, but not as a rule, and usually when they have a reason to doubt the accuracy of the debtors balances, or when they are auditing an American concern.

Many of the smaller firms circularize their client's receivables not in the hope of obtaining confirmations but rather to advertise their services. Sending direct confirmations is one way to make themselves known without being accused of advertising.

The experience of accounting firms with receivables confirmations has not been very encouraging in the Middle East. The percentage of replies is usually low. This being the case, accounting firms send in many instances negative confirmations which state that if no reply is received within a certain number of days the balance would be assumed correct, rather than the positive ones which demand a reply from the debtor approving or disputing his balance.

g) Physical inventory -- American procedures make it imperative for the auditor to be present at the physical

stocktaking at least once a year. This is a direct result of the McKesson & Robbins swindle mentioned earlier in this paper. This practice is not common in the Middle East. Only Saba & Co. endeavors to follow it all the time. Other firms occasionally try to be present at the stocktaking, especially if they are auditing an American firm, or at least make test checks of the inventory, but not as a general rule. The more common procedure is to place reliance upon a management's certificate of existing stock, same as the French or British auditor. British attitude has, however, been recently becoming more in line with the American approach to the question of verifying the actual existence of stock,² though, unlike the U.S., it is not yet a must to British auditors. Most Middle Eastern auditors, taking the easy way out and satisfied that at least in that issue they are backed in a way by British practice, make no effort to improve their standards.

h) Expenses and revenues -- The standard method is sample checking. No auditor can expect, or be expected, to undertake a full check on the expenses and revenue accounts. He can only satisfy himself by a properly chosen sample. This looks like a very simple statement of fact, yet it is surprising how many businessmen are not aware of it; they expect their auditors to be infallible detectors of all errors, even the simple ones, and all frauds.

¹Page 26

²The Inst. of C.A.s in England & Wales, Statements on Auditing: "General Principles of Auditing", and "Stock in Trade and Work-in-Progress", Accountancy, August 1961, pp. 488-491.

CONCLUSION

A. The State of the Profession

1. Absence of Local Professional Qualifications

Public accounting in the Middle East has not yet developed to the status of a well-developed profession. Though the practice is largely dominated by a few practitioners of professional standing, the professional status of such practitioners stems not from any recognition from within the area but from their affiliation to foreign professional societies.

A wide range of public accountants has thus resulted, extending from those qualified under the highest foreign standards to those with inadequate educational or training background, all equally recognized, in most cases, by law. Most local public accountancy laws, shy to extend recognition only to professionally qualified persons (which means admitting only foreign qualifications), have downgraded their admittance requirements to a level not compatible with the competence and ethical exigencies of sound public accounting.

2. Absence of Middle Eastern Standards

There is a general ignorance of the type of examination the Middle Eastern auditor conducts. Granted that the major accounting firms have evolved their own standards of work,

which compare well with the best foreign experience, yet there are differences in approach and procedures between the qualified firms themselves. As between qualified and non-qualified practitioners the differences are so great as to defy comparison.

What exists of public accounting knowledge in the Middle East is thus entirely foreign, and much of the problem lies in the inconsistency of this foreign influence. In some countries, notably Lebanon, public accountancy exhibits the influence of at least three countries -- France, Great Britain and the U.S. -- plus the locally developed standards, which are generally mediocre, of low-grade practitioners.

The major local firm, Saba & Co., which has done most to influence local public accountancy, has been in itself inconsistent in its own standards and procedures. The firm's initial pattern of practice tended to be British, (though not entirely so, for while the qualifications of the partners at the outset were British, none of them had significant practical experience in Great Britain or in a British firm). Since 1957, however, the firm's attitude shifted completely towards the American concept of auditing. Thus it cannot be said that Saba & Co. has consistently adopted and promulgated a certain defined school of accounting and auditing thought. Its influence in the area, though great, has not been stupendous.

Accounting principles in themselves are varied and inconsistent in their application. What principles are accepted anywhere in the world, plus some locally-developed ones, are all being applied. A financial analyst would find it difficult, if not impossible, to study or compare industrial and economic trends from corporate financial statements. This deficiency becomes more marked as expanding business concerns need to apply more elaborate principles.

3. Lack of Independence and Dirth of Ethics

While independence is one of the cornerstones of public accountancy, it is regrettable that the attitude of Middle Eastern practitioners, barring the few professionally-qualified ones, does not at all reflect the slightest appreciation of this fact. This is most seriously manifested in the practitioner's total financial dependence upon his client. All sorts of unethical acts (advertising, price-cutting, direct solicitation of business, assistance in tax evasion, etc...) are indulged in to obtain an account and then totally acceding to the client's desires so as not to lose it.

This situation is hurting everybody, including those whose ethics and integrity are above reproach. It inevitably reduces the public's faith in the whole profession. "There is a 'collective' aspect of independence that is important to the public accounting profession as a whole. The public accountant is not, as a rule, personally known to third

parties, such as stockholders,¹ who rely on his professional opinion, and such groups accept auditors' opinion principally on faith in the entire public accounting profession."² It is thus not strange in the Middle East that the auditor's certificate falls short of fulfilling one of the main purposes of its existence: that of maintaining mutual confidence in business relationships.

In any case, the auditor's independence is not protected, professionally or legally. In the more developed professional environments, an auditor cannot ethically accept an assignment before communicating with the previous auditor and clearing with him the reasons for his not handling the assignment any more. In this manner, an auditor feels reasonably safe that if he refuses to certify false or misrepresented financial statements, he would not easily lose the business to another less conscientious auditor. This system of communication is very strictly enforced by the accounting societies, and a violator runs the risk of losing his professional qualifications. In the Middle East, however, with no professional society to enforce such a system and with no law giving effect to a workable substitute, the auditor is in effect left without support in his ethical conduct.

¹Throughout this paper stockholders were referred to as clients, and not as third parties, since in our legislation they appoint auditors. In the U.S., where auditors are usually appointed by the board of directors, stockholders are referred to as third parties. (See page 55-56).

²Stettler, op. cit., p. 25.

The other side of the problem is that not only is the auditor's independence unprotected, but the businessman himself is also not protected from auditors of questionable ability or integrity, who for invalid reasons, be they lack of ability or morality, refuse to endorse his financial statements. With laws not providing for sufficient competency requirements (or practically none in the case of Lebanon) and with no accounting society to supervise ethical conduct, such instances could very well exist.

4. Dominance of a Few Firms

The businessman interested in a serious audit and/or a well-respected certificate does not have much choice of public accountants. In most cases, he has to pick out one of two or three big firms, two of which are British. Most other public accountants do not have the ability or the talent or the staff to adequately provide much more than bookkeeping services and elementary audit steps. Until recently the public accounting market has been too small to support more than one or two relatively important accounting firms. Even then, it was not large enough for any firm to afford hiring well-qualified personnel, nor sophisticated enough, apart from a few large foreign ventures, to demand such qualified personnel.

5. Business Reliance upon Auditors' Certificates

"The reliability of an audit is no better than the qualifications of the person who conducts it."¹ Due partly to

¹R.E. Witschey, "CPAs and Non-certified Practitioners," Journal of Accountancy, Dec. 1960, p. 64.

the looseness of ethics and low level of competence of a great number of Middle Eastern auditors, the reliance of the business and financial community upon the auditor's report has been generally very low. The business community must have general faith in the profession before it can be accustomed to place reliance on the certificate of one auditor. Obviously, whatever such reliance presently exists goes to the credit of the few professionally qualified accountants. But a collective lack of faith in auditors' reports is bound to reflect to some extent upon the most qualified, since not all businessmen appreciate the real difference between the qualifications of various accountants. Part of the relative dominance of British firms stems from the fact that local businessmen can more readily identify their competence and integrity with the high standards of the British profession.

The disinterest of businessmen in certified statements cannot, however, be laid solely at the door of the auditing profession itself. A major cause is in local business traditions and economic structure. The Middle East is only recently starting to come out of a primitive economic state. Businessmen, even corporations, are still motivated by a certain secretiveness about their activities; they are not yet used or willing to accept the idea of prying strangers. This behavior even extends to corporations, as these are generally closely-held and usually dominated by one person or family or an intimate group whose attitude is not much different from that of sole proprietors.

In any case, businessmen are not yet tuned to the procedure of having auditors examine their accounts and provide them with certified accounts and/or a detailed report on the subject matter of the audit with the intention of sending such reports to interested third parties, nor is the business or financial community used to the idea of receiving such reports. Banks, for instance, who are everywhere considered as one of the major recipients of auditors' reports do not fall in that category in the Middle East. Certified statements are important to a bank granting credit on the strength of the company's financial structure and earnings potential. Middle Eastern banking, however, is characteristically dominated by short-term commercial or fully-collaterized (mostly by real estate) credit, where certified financial statements are not of primary importance. Moreover, bankers are not so impressed by the competence and ethics of the local public accounting profession to base much value on local auditors' reports.

The overall picture is thus a cause and effect situation. The auditor does not command the importance that the nature of his profession demands, and he is in turn plagued by the dirth of competence and ethics in the area acting against building up a public faith in him as a member of a dignified profession.

B. The State of Legislation

Companies' legislation in the Middle East could not be considered as inadequate on the subject of auditors. Undeniably there is room for improvement, especially as regards the auditor's duties and responsibilities in Lebanon, Syria and Jordan, but it is doubtful whether the improvement of existing companies' legislation would significantly improve professional practice. The basic legal framework in this connection is generally existing, it need only to be properly implemented.

Much more can, however, be achieved by improving public accountancy legislation to provide for stricter competence requirements. In the absence of a local profession, according professional recognition by legislation is unavoidable. It would be too much for us to hope to create in the Middle East a profession similar to what Great Britain has taken years to build up. Even the United States has recognized early in the century the futility of waiting for a sound local public accounting tradition to develop and thus passed its public accountancy laws which grant professional recognition by legislation.

In order that legislation fulfills its major purpose of admitting only competent people the following has to be realized:

- (a) University education is a basic requirement, but it is not enough. A period of training in a qualified public accountant's office should be imposed.

- (b) Nothing should be left in the legislation for the discretion of government officials. The education and period and place of training should be clearly defined. Our experience with government administration should sufficiently warn us against leaving but the bare minimum of decisions to the discretion of government bureaucrats. Otherwise there is no telling of the degree of favoritism, nepotism or graft that might ensue.
- (c) That whatever controls or stipulations the law lays down, there is always the problem of administering them. The auditor's competence can be properly provided for, but there is a limit to official control of his independence and ethical conduct. Official action should, therefore, be directed towards promoting any private attempt to regularize the practice. In other words, support should be given to serious locally-formed professional societies as these are more equipped to control the practice of their members and have the necessary flexibility to take rapid corrective action.

The newly-formed Middle East Society of Associated Accountants might provide the answer for many of the profession's problems. Its admission requirements exhibit a full awareness of the skills and competence inherent in professional accounting practice; and its code of ethics, patterned mainly along the American Institute's code, provides for the highest standards of conduct needed to give

public accountancy the dignity and confidence that are so much the foundations of its existence.

One also hopes that in the presence of such a society some other problems of accounting and auditing in the Middle East will start to be solved. Other than the problem of defining the local standards and principles of accounting and auditing, there is the side problem of Arabic accounting terminology which needs to be developed and standardized as between countries and practitioners.

In addition, the Society can now assume the role of leader of the Middle Eastern profession and strive, in the name of the profession, to amend prevalent companies' and accountancy legislation and bring them more in line with the needs of modern business.

C. The Future of the Profession

One of our basic premises is that public accountancy is a natural by-product of the system of free enterprise. Any attempt to curb private enterprise will automatically reduce the usefulness of public accountants.

The socialistic trend is apparently gaining ground in Syria and Iraq. The future of public accountancy in these two countries is, therefore, uncertain as things stand now. What happened in Egypt could very well happen there, and there is no use theoreticizing on the profession's future in these two countries when the future of the free enterprise system itself is uncertain.

In Lebanon, Jordan and Kuwait, public accountancy is growing simultaneously with the expansion of private economic activity. The increase in the number of shareholding companies provides a guaranteed expansion in the size of the statutory audit market.¹ In addition, the increase in the overall number of operating companies, corporate or otherwise, would naturally enhance the importance of public accountants. Apart from statutory requirements, auditors would naturally be sought by expanding unincorporated enterprises. In Kuwait, for instance, where shareholding companies are quite few, partnerships and single proprietorships provide the auditors with a flourishing market. Expansion of any enterprise, whatever its legal form, brings about the need for stricter controls, which could be provided by external audits. Moreover such expansion can result in organizational problems, which public accountants can always assist in solving either in the normal course of an audit or as special management consulting assignments.

Furthermore, with the increase in size of the business unit the public accountants' services will come to be sought in other than auditing activities, and such a development works more in favor of the more qualified accountant.

¹See p. 87 for the trend of increase in Lebanon. Kuwaiti shareholding companies are still few (17 at the end of 1963, per the Annual Report of the Kuwait Chamber of Commerce and Industry for 1963); the Kuwaiti accounting market thus depends largely on sole proprietorships and partnerships. Statistics on Jordan are not readily available.

Prestige, international business relations, wide geographical coverage and a greater appreciation of the usefulness of the auditor's services to management all point towards an increased demand for more qualified public accounting services provided by firms of international standing.

It might be mentioned at this stage that the expansion in the size of the business unit in the Middle East is limited by the fragmentation of the area into small national entities and by the state of virtual economic confinement that some of the countries, the so-called socialistic ones, have drawn themselves into. The scope of inter-regional expansion by successful business enterprises is thus limited. It is only in the smallest countries of the area that free trade and private initiative are allowed a scope. Thus where expansion of private business is not unduly restricted by government interference, the size of the market itself could present a check on unlimited expansion. Such hurdles in the way of business would obviously limit the growth of public accountancy.

The above argument, however, does not necessarily hold true all the time, nor does it alter our main analysis. In some areas of business activity, private initiative has proved to be unlimited. Lebanon, though small by any standards but the most developed of the area in managerial talent and business acumen, has given rise to a few firms which have crossed the confines of their national boundaries into

the international sphere.¹ These are not very numerous, but they are indicative of the resourcefulness of private enterprises which have reached the saturation point of their growth within their geographical boundaries.

In any case, one need not go into the details of expansion in the nature of empire-building to justify the development of specialized public accounting services, Economic development within the country will naturally broaden the local market and thus provide room for the growth of public accountancy in step with the growth of private business.

One point to be mentioned while we are on the subject of business expansion is that bigness in business favors bigness in public accounting. A large business concern with many branches would obviously favor the accounting firm with a well-established reputation and the facilities to service the company's foreign branches. Furthermore, some of the more specialized public accounting services, such as systems or other types of management consulting which are a natural by-product of business expansion, require highly qualified talent which only the larger accounting firms can afford to hire. Thus in a country with a limited number of large business enterprises one cannot expect to find too many large accounting firms, which explains the very small number of such firms in the Middle East.

¹Intra Bank has branched out in Europe, the U.S. and West Africa. CAT company has extended its operations all the way from Pakistan to West Africa. This is not to mention the numerous Lebanese companies which have spread all over the Arabian Gulf area.

This is not to imply that the smaller accountant would gradually die out with increasing business expansion, or that the only room for expansion in public accountancy services lies in the ever-expanding size of the business unit. Economic development gives rise to business enterprises of all sizes and forms. With more of such enterprises growing into the category of large ones, one would expect the rise of some more large accounting firms and the further growth of the present ones. But there is always room for the smaller accountant, provided he is reasonably competent. He would always be sought by the smaller businessman seeking more personalized services (usually at a lower cost, because of lower overheads) and general advice on all sorts of complex business and tax problems. In fact, the public accountant's contribution to small business in an area such as the Middle East is probably greater than it is for big business. A large concern can afford to hire specialists in all lines of activity, leaving to the public accountant only the regular audit of the books and some occasional special assignments. But the smaller the business the less is this ability. The public accountant can, however, provide the smaller businessman with practically all the expert accounting, financial, legal, tax and management advice that he needs at only a nominal charge.

In a world of specialization, the public accountant's role is naturally enhanced. The forces of the market are such

that each level of economic progress will demand its level of specialized services. The demand for professional organizational advice has already reflected itself in an embryonic management consulting service in public accountants' offices. The increasing internationalization of economic activity has already resulted in a widening of the international relations of existing accounting firms, and promoted the establishment of a number of offices by foreign and local professionally qualified accountants.

The internationalization of economic activity should obviously highlight the importance of building up a dignified local profession. Aside from providing their regular auditing services, public accountants can be very useful in international flow of capital and in maintaining mutual confidence in international, over and above the national, business relations. They can promote capital inflow if foreign investors can depend on financial reports properly prepared in accordance with recognized accounting principles and supported by respected auditors' certificates. Furthermore, public accountants can greatly assist foreign investors in understanding local tax conditions, labor legislation and general legal and business environment. It is only when local public accountants can properly build up their professional integrity, prove their competence and cultivate their international relations that they can adequately fulfill this international role.

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MIDDLE EAST SOCIETY
OF
ASSOCIATED ACCOUNTANTS



CONSTITUTION
BY-LAWS
RULES OF PROFESSIONAL CONDUCT

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CONSTITUTION

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ARTICLE I

NAME AND OBJECTS

Section One : *Name and Headquarters :*

(a) The name of this organization shall be :

“THE MIDDLE EAST SOCIETY OF ASSOCIATED ACCOUNTANTS”

« جمعية المحاسبين القانونيين المعتمدين في الشرق الاوسط »

(b) The permanent headquarters of this organization shall be in Beirut, Lebanon.

Section Two : *Objects :*

The objects of this Society are :

- (a) To elevate the professional, ethical, moral and educational standards of the accounting profession ;
- (b) To assist in the maintenance of high standards in licensing persons qualified to be public accountants ;
- (c) To develop and maintain standards for the examination of candidates for admission to Fellow membership ;
- (d) To engage in and assist in the development of accounting research, and improve technical accounting principles and Arabic accounting terminology for local use ;
- (e) To develop and improve accountancy education ;
- (f) To encourage the professional exchange of knowledge, advice and assistance with accountants of other countries ;
- (g) To supply its members with information on developments in accountancy, and to encourage the exchange of knowledge among its members in its meetings, conferences and conventions.

Section Three : *Definitions :*

As used hereinafter, the following terms shall be understood to bear the meaning here appended to them :

- (a) “Qualified public accountants” – any persons meeting the requirements described in Article II, Section 2, of this Constitution, and the relevant sections of the By-Laws, of the Society, and who are Fellows of this Society.
- (b) “Approved public accounting firm” – a public accounting firm approved, at the time of consideration of the application for membership, by a majority vote of two thirds (2/3) of the Committee on Membership.
- (c) “Manager” – a public accountant employed as and bearing the title of “manager” and who is technically in charge of an office of an approved public accounting firm with three (3) public accounting employees at least in that office ; or who is in a supervisory post over no less than five (5) public accounting employees of such a firm.

- (d) "Director" - any member of the Council of the Society.
- (e) "Recognized Secondary School" - any school designated as such by a two-thirds (2/3) majority vote of the Membership Committee.

ARTICLE II MEMBERSHIP

Section One: *Classes* :

The membership of this Society shall consist of two classes: Fellow Members and Honorary Members. There shall also be Subscribers of the Society, who shall not be construed to be members.

Section Two: *Fellows* :

The Fellows shall include all persons who are found to be qualified under any one of the following subsections, according to the procedure set forth in Article VI, Section 1, of the By-Laws of this Society :

- (a) Persons recommended by two (2) Fellows of the Society, which persons are and continue to be members in good standing of one of the following Societies (listed in alphabetical order) :

- (i) American Institute of Certified Public Accountants,
- (ii) Association of Certified and Corporate Accountants,
- (iii) Institute of Chartered Accountants in England and Wales,
- (iv) Institute of Chartered Accountants in Ireland,
- (v) Institute of Chartered Accountants of Scotland.

The Committee on Membership is empowered to accept other societies for recognition in this manner, provided they are approved by three-quarters (3/4) vote of all the members of the Council.

- (b) Any person who is :

- (i) Twenty-one (21) years of age or over, and
- (ii) Of good moral character, and
- (iii) A graduate of a recognized Secondary School, and
- (iv) Who has served not less than five (5) years in the employ of a Fellow of this Society in an auditing post, provided further that experience for this purpose shall be with no more than three (3) employers over the five (5) year period claimed by the applicant, and that the last two (2) of these years, at least, must be with the same employer, and that during these last two (2) years, the applicant must have been a Subscriber of the Society, provided further that candidates holding at least a Bachelor's degree in accounting, commerce or business administration approved by the Committee on Membership shall be

exempted from two (2) of the five (5) years of service required hereunder, and

- (v) Who shall have successfully passed the examinations of this Society, as provided for in the By-Laws, and
- (vi) Who shall have been recommended by two (2) Fellows of the Society.

- (c) Any person engaged in the full-time teaching of accountancy who holds a rank of Assistant Professor or higher, or the equivalent thereof, and so long as he continues in such a capacity, in a College or University granting a Bachelor's degree in accounting, commerce or business administration, approved by the Committee on Membership, provided that not more than two (2) such members from the same University may be Fellows of the Society at any one time. Candidates under this subsection must be recommended by the head of their College or University, and by two (2) Fellows of this Society.

- (d) Any person :

- (i) Who shall have been continuously employed in an auditing position by an approved public accounting firm or for his own account as a full-time public accountant in the Middle East for a period of not less than five (5) years, and
- (ii) Who has been no less than three (3) years in a position with such a firm, as manager or above, or as a sole practitioner, and
- (iii) Who is of good moral character, and
- (iv) Who is a graduate of at least a Secondary School recognized by the Committee on Membership, and
- (v) Who is recommended by two (2) Fellows of this Society ;

provided further, that applications under this subsection shall be accepted only for a period of one year from the effective date of registration of this Society*, and that upon that anniversary the text of this subsection (d) shall be automatically deleted from this Constitution.

Section Three: *Subscribers* :

The Subscribers shall be persons :

- (a) Who have been employed for a period of not less than two (2) years as senior accountants or higher with reputable public accounting firms, or as sole practitioners, or as chief accountants supervising no less than five (5) accounting employees in a company or firm service with which is acceptable to the Membership Committee, or
- (b) Who are full-time teachers of accountancy at institutions recognized under Section 2 (c) of this Article.

Section Four: *Honorary Membership* :

The Council, by unanimous vote, may confer Honorary Membership on any person or persons who by their standing and celebrity in the community may be considered as entitled to receive such an honor. An Honorary Member is not entitled to practice as a Fellow of the Society.

*March 12, 1964

Section Five: Elevation to Fellowship:

When a Subscriber shall have met any group of requirements enumerated in the subsections of Section 2 of this Article, he shall be elevated to Fellow membership in this Society; no Subscriber having met the requirements for Fellowship shall be allowed to remain a Subscriber. Any Subscriber whose qualifications for subscription under Section 3 no longer exist shall forthwith cease to be a Subscriber of the Society.

Section Six: Military Service:

The status of any Subscriber who enters the military service of his country shall remain unchanged during the period of such service and one year thereafter, except in case of his voluntary resignation from the Society; provided, however, that he maintains himself in good standing and pays all dues which he may be required to pay by the By-Laws.

Section Seven: Admission Procedures:

Election of Fellows and admission of Subscribers shall be by personal or mail ballot of the Membership Committee, provided that an affirmative vote of all the members of the Membership Committee shall be necessary for election under this procedure. One or more dissenting votes, or one or more abstentions, shall be deemed to constitute a refusal of the application. A refused applicant may resubmit his application to the Council, and an affirmative vote of three-quarters (3/4) of all the Directors shall be necessary for election at that time.

Section Eight: Reapplication:

Refusal of an applicant for election to Fellowship or admission to subscription shall be deemed to be a refusal of that application only; the applicant may resubmit his application for consideration on no more than five (5) separate occasions, and appeal to the Council his refusal by the Membership Committee on no more than five (5) further separate occasions.

Section Nine: Certificates:

- (a) Upon election, each Fellow shall be entitled to a certificate setting forth that he is a Fellow of the Society and the date of his admission, signed by the responsible officers and carrying the Seal of the Society.
- (b) No certificate shall be issued until receipt of the Fellow's dues for the current year.
- (c) Each certificate shall show whether the Fellow is in practice or not in practice, and a new certificate shall be issued upon change of status of the Fellow as provided in the By-Laws of the Society.
- (d) Certificates of Fellowship shall be returned to the Secretary upon suspension or termination of membership for any cause except the death of a Fellow; the certificates of Fellowship remain the property of the Society.
- (e) No other persons shall be entitled to certificates of the Society, nor may any person other than a Fellow or Honorary Member of the Society describe himself as a Member of the Society, or Honorary Member of the Society, respectively.

Section Ten: Description:

A Fellow of the Society shall be entitled to designate himself as an "Associated Account-

tant", and may use the initials "F. A. A." after his name; firms shall be entitled to describe themselves as "Associated Accountants" only if all the partners are Fellows of this Society, provided that such description is used only in accordance with the Rules of Professional Conduct of the Society.

ARTICLE III OFFICERS AND DIRECTORS

Section One: Council:

- (a) The governing body of the Society, in the interim between meetings, shall consist of a Council which shall have full power to act within the limitations of this Constitution and the By-Laws.
- (b) The Council shall consist of nine (9) Directors: - the elective officers of the Society, and four (4) other members and the immediate Past President of the Society, all of whom must be Fellows. Officers and Directors of the Society shall serve as such without fee or remuneration.
- (c) If the offices of the Secretary and Treasurer are held by the same person, there shall be five (5) non-officer Directors elected; provided further that in the first year of the operation of the Society the Fellows signing the Constitution shall elect a Council of six (6) Fellows (including officers) from among themselves, and that Council is empowered to appoint three (3) additional Fellows from among the members to fill the vacancies for the said first year.

Section Two: Officers:

The officers of the Society shall be as follows:

President,
Vice-President,
Secretary, and
Treasurer,

all of whom shall be Fellows and Directors of the Society. The Council may, in its discretion, appoint or employ for remuneration a non-Fellow to perform certain duties with the title of Executive Secretary, as well as any other appointees or employees it may deem appropriate from time to time.

Section Three: Committees:

There shall be five (5) regular standing committees of the Society, namely:

- (a) Committee on Membership,
- (b) Committee on Legislation and Recognition,
- (c) Committee on Ethics and Grievances,
- (d) Committee on Accounts and Finances,
- (e) Committee on Technical Affairs.

All standing committees shall be appointed annually by the Council together with such

subcommittees or special committees as may be required from time to time. Each committee shall consist of three (3) or more Fellows of this Society, and the President shall be *ex-officio* a member. A Chairman shall be appointed for each committee, at the time of appointment of the Committee.

Section Four: Election of Officers:

Officers and Directors shall be elected at the annual meeting of the Society; they shall hold office until the next succeeding annual meeting or until their successors are chosen thereafter; the Council shall, by two thirds (2/3) majority vote fill any vacancy occurring between annual meetings; all elections shall be conducted as hereinafter provided in the By-Laws.

ARTICLE IV LOCAL SOCIETIES

Section One: Permission:

The Society may permit the establishment of affiliated local societies at a specified location, or in a specific region within or outside Lebanon, upon the approval of the Council.

Section Two: Membership:

Fellow membership in this Society shall be a prerequisite to membership in any affiliated local society.

Section Three: Finances:

The fiscal year of each affiliated local society shall conform to the fiscal year of this Society; no local society shall be permitted to collect, levy, assess, retain, disburse or otherwise deal in funds or dues not authorized to be so dealt in by the Council of this Society.

Section Four: Formation Procedures:

Prior to the submission of a proposal for the formation of an affiliated local society, not less than five (5) Fellows of this Society may constitute themselves an Affiliation Committee, and present to the Council for its consideration a proposed Charter; the Council shall certify whether such Charter is compatible with the Constitution, By-Laws and Rules of Professional Conduct of the Society.

Section Five: Affiliates:

Affiliates shall be self-sustaining and autonomous, and no affiliated local society may bind the Society professionally, financially or otherwise.

ARTICLE V SEAL

Section One: Seal:

The corporate Seal of the Society shall consist of two concentric circles, in the circumfe-

rence of which shall be the words "Middle East Society of Associated Accountants" in English, and

« جمعية المحاسبين القانونيين المعتمدين في الشرق الاوسط »

in Arabic, together with any appropriate device approved by the Council.

Section Two: Authority for Affixation:

The corporate Seal of the Society shall be affixed to documents only upon specific authority for such affixation, granted by vote of the Council, except that the Seal may be affixed to certificates of Fellowship granted under Article II, Section 9 of this Constitution upon authorization by the Committee on Membership.

ARTICLE VI AMENDMENTS

Section One: Amendment Procedures:

- (a) Amendments to the Constitution, By-Laws and Rules of Professional Conduct may be proposed at any meeting of the Society for which the notice or call recites that such amendments are to be proposed. If such proposed amendments receive an affirmative vote of a majority of Fellows voting in person or by proxy, they shall be submitted to each Fellow for vote by mail. The votes of three-quarters (3/4) of the Fellows whose replies are received by the Secretary within ninety (90) days from the day of mailing of the ballots will determine the disposition of the proposed amendments, provided further that ballots shall have been received in time from not less than two-thirds (2/3) of the Fellows of this Society. No votes shall be counted which are received after the lapse of said ninety (90) days.
- (b) Amendments of Article I, Section 1 and this Article VI, Section 1 of this Constitution, must as an exception carry the unanimous vote of the membership of the Society attending the Meeting and of the members voting by mail ballot upon such amendments.

Section Two: Notice of Results:

Within thirty (30) days of the close of voting [one hundred and twenty (120) days from the date of original mailing of the ballots] the results of the vote shall be mailed to each Fellow of the Society.

ARTICLE VII LANGUAGE

The official language of the Society shall be the Arabic language. The use of other languages shall be regulated by the By-Laws of the Society.

ARTICLE VIII
RATIFICATION

This Constitution and the enclosed By-Laws and Rules of Professional Conduct were unanimously adopted at a meeting of the undersigned Fellows of this Society in Beirut, Lebanon on the twenty-second day of August, A. D. one thousand nine hundred and sixty.

(Sgd.) Fuad S. Saba

(Sgd.) Alex. N. Siman

(Sgd.) Fauzi F. Saba

(Sgd.) George A. Ashkar

(Sgd.) William S. Mitri

(Sgd.) Karim G. Khouri

MIDDLE EAST SOCIETY
OF
ASSOCIATED ACCOUNTANTS

BY-LAWS

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ARTICLE I

DUTIES OF OFFICERS, STANDING COMMITTEES AND DIRECTORS

Section One: *President* :

It shall be the duty of the President to preside at all meetings, to act as Chairman of the Council, and to enforce all laws and regulations relating to the administration of the Society. He shall call meetings of the Society and of the Council when he deems it necessary, or upon the written request of at least ten (10) Fellows of this Society for a meeting of the Society, or two (2) Directors for a meeting of the Council.

Section Two: *Vice-President* :

In the absence of the President, the Vice-President shall have all the powers and prerogatives of the President.

Section Three: *Secretary* :

- (a) All resolutions and proceedings of meetings of the members, the Council, or of any committee or sub-committee, shall be entered in proper books by the Secretary, and the minutes of all such meetings when properly approved and signed by the chairman of the meeting and the Secretary shall be sufficient and conclusive evidence of the facts therein stated.
- (b) The Secretary shall conduct all correspondence and referenda relating to the Society, shall issue all notices of meetings, shall have charge of the Seal, and shall perform all duties pertaining to the office of Secretary.
- (c) The Secretary shall keep a register of the Fellows and Subscribers of the Society, which shall contain their business and home addresses and a complete record of their election, history and termination of their Fellowship or subscription. He shall also perform such other duties as are elsewhere provided for in these By-Laws.

Section Four: *Treasurer* :

All moneys payable to the Society shall be paid to the Treasurer, who shall deposit the same in a bank, and all moneys payable by the Society shall be paid by checks signed by the Treasurer. He shall keep regular accounts of the financial affairs of the Society, which accounts shall be subject to inspection by the auditor or auditors of the Society, and the members of the Committee on Accounts and Finances. He shall make a report in writing at each regular meeting of the Council containing such information as may be specified by the Council ; he shall be bound in all transactions by the directives and budgetary control of the Committee on Accounts and Finances.

Section Five: *Executive Secretary* :

The Council may appoint or employ an Executive Secretary who shall be *ex-officio* a member of the Council without a vote, and who shall perform such duties as may be assigned to him by the Directors and elected officers, including duties specifically assigned to the Secretary or the Treasurer by these By-Laws.

Section Six: Committee on Membership:

All applications for membership shall be forwarded to this Committee promptly upon receipt and examination by the Secretary as provided hereafter in these By-Laws. The Committee shall inquire into the eligibility and character of each person applying for membership and shall communicate to the Council, without undue delay, the results of its balloting upon each applicant. The Committee on Membership shall adjudge all educational requirements and qualifications submitted to it by making specific reference to the educational standards prevailing in Lebanon.

Section Seven: Committee on Legislation and Recognition:

The duties of the Committee on Legislation and Recognition shall be to assist in matters relating to legislation affecting the profession, and to consider all questions which may be referred to it by the Society or Council. In all countries where the Society is not yet recognized, and its Fellows not yet qualified upon its certificate to practice, it shall be the duty of this Committee to strive, either through the efforts of its members or through the appointment of local Fellows, to further recognition of the certificate, purposes and standards of the Society.

Section Eight: Committee on Ethics and Grievances:

The duties of the Committee on Ethics and Grievances shall be:

- (a) To investigate and arbitrate such differences of a professional character between Fellows of this Society as shall be referred to it by the President or Secretary, or by mutual consent of the parties thereto, or by a Fellow of this Society.
- (b) To investigate any complaint referred to it against a Fellow or non-Fellow for violation of the Professional Rules of Conduct of the Society or under Article VII of these By-Laws. If, upon consideration of a complaint, it appears to the Committee that a *prima facie* case is established showing a violation of any By-Laws or Rule of Conduct, the Committee shall obtain all facts with respect thereto and make a full and complete report in writing of its findings recommendations to the Council of the Society, which shall decide the appropriate action by two-thirds (2/3) majority vote.

Section Nine: Committee on Accounts and Finances - Auditors:

The Committee on Accounts and Finances shall be responsible for the management and policy in administration of the Society finances by the Secretary and Treasurer. The Annual Meeting of the Society shall appoint and fix the remuneration of an auditor or auditors for each fiscal year, which shall end June 30, and such auditor or auditors shall audit the accounts of the Society and submit a written report of the same to the next Annual Meeting of the Society. The Committee shall plan and approve all budgets and special expenditures, shall lay down procedures, and shall manage the finances of the Society, subject to the directives of the Council. The first financial year of the Society shall end on June 30, 1964.

Section Ten: Committee on Technical Affairs:

The duties of the Committee on Technical Affairs shall be to administer the examinations of the Society as provided in Article IX of these By-Laws, and to undertake the management

of all programs of education, technical research, publication and the formulation of sound generally accepted accounting principles for the use of the Society and the profession at large. At least one member of this Committee shall be a person admitted to membership under Article II, Section 2 (c) of the Constitution of the Society, if available, and the Committee shall have the right to engage or employ, from time to time, prominent accounting authorities, or any person necessary for the furtherance of its programs; provided further, that the Council shall decide what additional activities this Committee shall undertake, and shall appropriate funds to that end, after seeking and considering the advice and opinion of the Committee on Accounts and Finances.

Section Eleven: Council:

In addition to the general responsibilities of the Council set forth in Article III, Section 1, of the Constitution and the duties outlined elsewhere in these By-Laws, the following are designated as specific duties of the Council, at whose meetings a majority of the Directors shall constitute a quorum for the transaction of business except as provided in Article V, Section 1, of these By-Laws:

- (a) To authorize expenditure for, or reimbursement of, travel or other necessary expenses incurred by officers, Directors, and Fellows in connection with authorized Society business.
- (b) To adopt, in the light of circumstances then existing, a budget submitted by the Committee on Accounts and Finances covering authorized expenditures in connection with any meeting or convention of the Society, and to determine any registration fee which may be charged to Fellows, Subscribers and guests at such a meeting.

ARTICLE II MEETINGS OF THE SOCIETY

Section One: Annual Meeting:

The Annual Meeting shall be held at a place in Lebanon to be designated by the Council, or by the Society, on any day during August or September which the Council, or the Society, may select. Notice shall be sent to each member at least twenty days prior to such meeting.

Section Two: Special Meetings:

Special meetings may be called in accordance with these By-Laws, at which meetings no business other than that for which they were called shall be transacted. The place at which such meetings shall be held shall be determined by the Council. Notice of such meetings shall be sent not less than twenty days prior to each such meeting to every Fellow of the Society, stating the date and place of such meeting and the business to be transacted thereat.

Section Three: Quorum:

- (a) One-half (1/2) the Fellows of the Society qualified to vote, present in person or by proxy, of whom at least one is an officer of the Society, shall constitute a quorum authorized to transact any business duly presented at any meeting of the Society.

- (b) All Fellows shall be permitted to give proxies to other Fellows authorizing them to vote for specific items of business of the Society or allowing them a general power to cast their vote for any given meeting or any adjournment thereof, provided further that no Fellow may hold or cast votes upon more than five (5) proxies at any one time.

Section Four: Voting :

- (a) Every Fellow shall be entitled to one vote on any question, or to give a proxy therefor, provided such Fellow's dues are not delinquent, and provided that such Fellow is otherwise in good standing. Voting by mail shall be permitted only as provided by the Constitution in Article VI, or by specific action of the Society or its Council. Except as may be otherwise specifically provided, action on any question shall be decided by the majority vote of the Fellows voting in person or by proxy, a quorum having been established.
- (b) At each meeting of the Society, the Secretary shall furnish the Chairman of the meeting, upon his request, with a certified list of the Fellows qualified to vote.
- (c) Honorary Members and Subscribers shall not be entitled to vote in any of the meetings of the Society, and the Subscribers may be excluded from discussion upon motion from the floor, made and duly seconded, which carries not less than three-quarters (3/4) of the qualified votes cast on the motion.

ARTICLE III ORDER OF BUSINESS

Unless otherwise authorized by the Society or the Council, the order of business at all meetings shall be as follows :

1. Roll-call,
2. Confirmation of minutes of preceding meeting,
3. Reading of communications and motions relative thereto,
4. Reports of Officers, Council, auditors, and affiliates,
5. Unfinished business laid over from previous meetings,
6. Reports of standing committees,
7. Reports of special committees,
8. Election of officers,
9. Election of Directors,
10. New business, motions, and resolutions,
11. Special features,
12. Installation of newly-elected officers and Directors.

ARTICLE IV NOMINATION AND ELECTION OF OFFICERS AND DIRECTORS

Section One: Nominations :

Nominations shall be made at the annual meeting of the Society for Directors not

otherwise selected under the provisions of Article III, Section 1, of the Constitution.

Section Two: Election of Officers and Directors :

The election of officers and Directors shall be held at the annual meeting of the Society in September of each year, and shall be by secret ballot. First, nominations for Directors shall be made from the floor. Any number of persons may be nominated. Election of Directors shall be by cumulative voting. The candidates receiving the highest number of votes shall be declared elected, but if there is a tie vote for the last position to be filled, a second ballot shall be held between those receiving the same number of votes, to fill this position. After the Directors are thus elected, nominations may be made from among them for the posts of President, Vice-President, Secretary and Treasurer. Voting for each office in turn will then take place, the Director receiving most votes being elected.

Section Three: Term of Office :

The officers and Directors elected at the annual meeting shall hold office for one year, or until their successors are elected.

ARTICLE V MEETINGS OF COUNCIL AND COMMITTEES

Section One: Meetings of the Council :

Meetings of the Council of the Society shall be held at least once every month on a day to be fixed by the Council or the President or the Secretary. Seven (7) days' notice shall be given to each Director for each meeting, together with the agenda for that meeting. No business shall be transacted at any Council meeting unless a quorum is constituted by the presence in person of at least four (4) Directors, one of whom must be an officer.

Section Two: Calling of Council Meetings :

The President or the Secretary shall call a meeting of the Council upon receipt of a written request signed by at least two (2) Directors, which request must state the reason for calling the meeting, and such reason shall be communicated to the Directors in the call for the meeting.

Section Three: Committee and Subcommittee Meetings :

Procedures for the meetings of committees and subcommittees shall be laid down from time to time by the Council.

ARTICLE VI MEMBERSHIP, FEES, AND DUES

Section One: Membership :

Applications for subscription and Fellowship shall be made to the Secretary on forms to be

provided by him. As a part of such application, each applicant shall agree that, if elected, he will be bound by the Constitution, By-Laws, and Rules of Professional Conduct of the Society, and that he will surrender his certificate of Fellowship to the Secretary in the event of his withdrawal from the Society, or of his Fellowship otherwise ceasing. Every application for subscription and Fellowship in the Society shall be examined by the Secretary and certified as to the applicant's previous professional and financial record, if any, with the Society. After the Secretary has so certified the application, he shall forward it to the Committee on Membership for action as provided by Article I, Section 6, of these By-Laws.

Section Two: Admission Fees:

The admission fee shall be two hundred and fifty Lebanese Pounds (L.L. 250.00) for each Fellow in practice, and fifty Lebanese Pounds (L.L. 50.00) for each Fellow not in practice and for each Subscriber and, upon the elevation of a Subscriber to "in practice" Fellowship, or the change of status of a Fellow from "not in practice" status, to "in practice" status there shall be an additional fee of two hundred Lebanese Pounds (L.L. 200.00) or the equivalent thereof. A Fellow or Subscriber who is dropped for any reason, including non-payment of dues, shall be required to pay the admission fee for his class before he may be readmitted. There is no admission fee for admission to Honorary Membership.

Section Three: Certificate of Fellowship:

Upon admission of a Fellow to this Society, or upon advancement of a Subscriber to Fellowship, he shall be entitled to a certificate of Fellowship therein, according to Article II, Section 9 of the Constitution.

Section Four: Dues:

The dues for each fiscal year ending June 30, shall be one hundred Lebanese Pounds (L.L. 100.00) or the equivalent thereof for each Fellow in practice, and twenty five Lebanese Pounds (L.L. 25.00) for each Fellow not in practice and for each Subscriber, payable annually in advance. Upon admission to Fellowship or Subscription, dues are required to be paid *pro rata*, to the nearest month starting with the date of admission or election. Honorary members are not required to pay dues.

Section Five: Elevation of Subscribers:

A Subscriber, having satisfied the requirements for Fellowship in Article II, Section 2 of the Constitution, shall make application to the Committee on Membership and shall be notified by the Secretary when the Committee on Membership votes for his elevation to Fellowship, in accordance with Article II, Section 6, of the Constitution, and the Secretary shall cause the proper certificate to be engrossed and forwarded to him upon receipt of the elevation fee and the appropriate dues, as provided in Section 2 of this Article.

Section Six: Termination of Membership:

- (a) Whenever a Fellow has notified the Secretary in writing that he resigns his Fellowship, and returns to the Secretary his certificate of Fellowship, or when his Fellowship has been terminated under the provisions of Article VII of these By-Laws or Article II, Section 2(c) of the Constitution, the Secretary shall cancel the dues of such Fellow for the remaining portion of the fiscal year in which such resignation or termination occurs, prorated to the date thereof. Where such dues

have been paid in advance, a refund shall be made covering the remaining portion of the fiscal year.

- (b) When a Fellow or Subscriber fails to pay his dues or charges before January 1 of the fiscal year for which such dues or charges are assessed, all dues or other charges assessed against him shall be considered delinquent.
- (c) Whenever a Fellow or Subscriber becomes delinquent, the Secretary shall notify such member in writing that he is delinquent and that he will be dropped unless, within sixty days from the date of notification, he has paid in full all dues or other charges remaining unpaid. If such Fellow or Subscriber fails to pay such charges within the period of sixty (60) days, he shall be dropped from the rolls and the Secretary's records shall be marked to show such action.
- (d) The Secretary shall charge off the unpaid dues of all Fellows or Subscribers who are dropped or have resigned, and shall mark their accounts to reflect such action.
- (e) Whenever a Fellow or Subscriber is dropped for non-payment of dues or change of status, or resigns, without paying his account in full, he shall not be readmitted to good standing except as provided for new applicants, with full payment of the regular admission fee and all prior unpaid balances. The balance due by a dropped Fellow or Subscriber shall be the balance as of the close of the fiscal year within which notification was mailed to him by the Secretary.
- (f) In the absence of a request by the executors or administrators for a statement of the amount due, unpaid balances of deceased Fellows or Subscribers shall be charged off by the Secretary, their accounts being clearly marked to show such action.
- (g) Upon termination of Fellowship for any cause except death, the Secretary shall make demand in writing for the return of the Fellowship certificate.

Section Seven: Assessments:

In addition to the amounts provided for in Sections 2 and 4 hereof, the Council is hereby empowered to assess the membership, when and if the need for funds arises, an amount not to exceed fifty Lebanese Pounds (L.L. 50.00) per fiscal year for each Fellow not in practice and each Subscriber, and two hundred and fifty Lebanese Pounds (L.L. 250.00) per fiscal year for each Fellow in practice. The Council can only be overruled, in making an assessment of this nature, by a three-quarters (3/4) vote of the Fellows voting in person or by proxy at any meeting of the Society.

Section Eight: Waiver or Reduction of Dues:

The dues of all Fellows who have attained the age of sixty five (65) years shall be waived, beginning with the fiscal year following that in which the member becomes sixty five (65). The Council may, by two-thirds (2/3) majority vote, remit, reduce, postpone or waive any moneys due from or payable by a member of the Society, if the Council deems it fit so to do upon the grounds of unusual hardship or unfair burden upon such member.

ARTICLE VII EXPULSION OR SUSPENSION OF MEMBERS

Section One: *Grounds for Expulsion or Suspension:*

Any member renders himself liable to expulsion from the Society, or to suspension for a term of at least two (2) years, or to censure, if:

- (a) He is convicted of a felony, or a misdemeanor involving moral turpitude, or
- (b) He is finally declared by a court of competent jurisdiction to have committed any fraud, or
- (c) He is held by the Society, or its Council, on the written complaint of any person aggrieved, whether a Fellow or not, to have been guilty of any act or default discreditable to the profession, or
- (d) He is declared by any competent court or commission to be insane or otherwise incompetent, or
- (e) He is found guilty by the Society, or its Council, of infringing any of its By-Laws or any of its Rules of Professional Conduct, or
- (f) His certificate or registration upon the strength of which he gained membership under Article II, Section 2 (a) of the Constitution, is revoked or withdrawn by the organization, State or Government issuing it, and such revocation or withdrawal remains in effect.

Section Two: *Adjudication of Charges:*

- (a) For the purpose of adjudicating charges against Fellows of the Society for any of the reasons specified in Section 1 of this Article, after appropriate investigation and report by the Committee on Ethics and Grievances, as provided by Article 1, Section 8 of these By-Laws, the Council shall convene as a Trial Board. When convened as a Trial Board for the purpose of hearing evidence, minutes of each meeting shall be taken by the Secretary of the Society or his duly authorized representative. Written notice to the defendant and other interested parties shall be furnished by the Secretary at least twenty (20) days in advance of such hearing.
- (b) After hearing the evidence presented by the complainant and by the defence, the Council of the Society is hereby empowered to dispose of the case or cases before it in such manner as in its judgment is appropriate in the circumstances, by affirmative vote of at least two-thirds (2/3) of the entire membership of the Council except as otherwise hereinbefore provided.
- (c) If the Council, sitting as a Trial Board, finds the defendant guilty, and if it fixes a penalty of suspension or expulsion from the Society, the defendant shall have the right of appeal to the Society at any regular meeting of the Society, or at a special meeting called for this purpose alone upon the written request of not less than ten (10) Fellows; at such meeting the decision of the Council may be reversed by three-fourths (3/4) of the Fellows voting, in person or by proxy, provided that not less than twenty (20) affirmative votes are cast for reversal.

Written notice of such appeal shall be mailed to all Fellows not less than twenty (20) days prior to said meeting.

ARTICLE VIII RULES OF ORDER AND LANGUAGE

Section One: *Rules:*

The rules of parliamentary procedure as laid down in "Robert's Rules of Order" shall govern all meetings of the Society, as far as such rules are not inconsistent with the provisions of the Constitution and these By-Laws.

Section Two: *Language:*

The official language of the Society shall be the Arabic language, provided further that the English language may be used in the proceedings of the Society and as a supplementary language. Where documents or proceedings are published or rendered in both the Arabic and English languages, the Arabic version shall be the official version, and reference may be made to the English version in the event that the Arabic version is unclear.

ARTICLE IX EXAMINATIONS

Section One: *Administration:*

The examinations for admission to Fellowship in the Society under Article II, Section 2 (b) of the Constitution and the syllabus therefor, shall be formulated and conducted under the supervision of the Committee on Technical Affairs, or the Executive Secretary as the Committee's appointed examination administrator if the committee votes to so appoint him.

Section Two: *Contents:*

- (a) Examinations of the Society shall be in two (2) parts:
 - (i) Preliminary, and
 - (ii) Final

No candidate shall be allowed to take the final examination until he has passed or has been exempted from the preliminary examination.

- (b) The preliminary examination shall consist of six (6) papers in the following subjects:
 - (i) Bookkeeping and Financial Statements,
 - (ii) General Commercial Knowledge,
 - (iii) Elementary Economic Theory and History
 - (iv) Elementary Auditing,
 - (v) Elementary Mercantile Law, and

- (vi) Credit, Money and Banking.
- (c) The final examination shall consist of six (6) papers in the following subjects :
 - (i) Advanced Accounting Problems (in two parts), including proprietorship, partnership and company accounts, commercial and industrial accounting, cost accounting, fund and institutional accounting, and all other relevant accounting subjects,
 - (ii) Advanced Auditing,
 - (iii) General Company Law,
 - (iv) Mercantile Law, and
 - (v) Financial Statement Analysis (or Income Taxation).
- (d) All candidates shall be required to show adequate professional and technical proficiency in the subjects of the examinations ; the passing grade shall be seventy five (75) per cent ; all papers shall be corrected by mentor Fellows of the Society by arrangement with the Committee on Technical Affairs, and all corrected papers shall be reviewed by an independent Fellow member of the committee who has not participated in correcting papers for that examination. The committee shall review the grades given by the mentor Fellows and the comments of the reviewing member ; it shall also make procedural rules to supplement these By-Laws : evaluating papers, deciding the final grades, and announcing the results to the candidates. Decisions of the committee shall be final and not subject to any appeal.

Section Three : Exemption :

Candidates holding bachelor's degrees recognized under Article II, Section 2 (c) of the Constitution, shall be exempted from the preliminary examination upon presenting documentation of their degree and payment of a fee of L.L. 50.00 or the equivalent thereof.

Section Four : Place and Fees :

- (a) The examinations of the Society may be given at Beirut and at any place or places in the Middle East, at the option of the Committee on Technical Affairs, provided that they are given in Beirut at least in July of each year.
- (b) The fees for the preliminary examination shall be L.L. 100.00 or the equivalent, and they shall not be refunded under any circumstances after they have been received by the Treasurer ; the fees shall be payable for each time the preliminary examinations are taken either in whole or in part.
- (c) The fees for the final examination shall be L.L. 150.00 or the equivalent, and they shall not be refunded under any circumstances after they have been received by the Treasurer ; the fees shall be payable for each time the final examinations are taken, either in whole or in part.

Section Five : Credits :

No person shall be allowed to take either of the preliminary or the final examinations each in whole or in part, more than four (4) separate times ; a candidate who passes all of the subjects of the preliminary examination shall be allowed to retain credit for them until he

has exhausted all four(4) trials at the final examination, provided further that the period covering the four(4) attempts at either examination shall not exceed five (5) years. No credit shall be allowed candidates unless they pass at least four(4) papers of either examinations at one sitting; credit obtained in this fashion may be carried forward during the remaining attempts permitted candidates under this Section.

Section Six : Changes in Program :

The Council shall have the right to amend any of the provisions of this Article by a two-thirds (2/3) vote of all the Directors.

MIDDLE EAST SOCIETY
OF
ASSOCIATED ACCOUNTANTS

RULES OF PROFESSIONAL CONDUCT

PREAMBLE :

The following are declared to be the fundamental Rules of Professional Conduct of the Middle East Society of Associated Accountants, and each Fellow of the Society shall, upon being admitted to Fellowship, make an oath and solemnly undertake to observe them in letter and in spirit as precepts of his conduct in his professional relations and practice :

RULE 1 :

A firm or partnership, all the individual partners of which are Fellows of this Society, may describe itself as "Associated Accountants", but a firm or partnership, not all the individual members of which are Fellows of this Society, or an individual practicing under a style denoting a partnership when in fact there be no partner or partnership, or an individual or individuals practicing under any designation or style other than the name or names of any present or past owner, partner or partners, shall not use the aforesaid designation.

RULE 2 :

A member shall not be an officer, director, stockholder, representative, agent, partner, associate or employee of any of the following :

- (a) An individual practicing under a style denoting a partnership when in fact there be no partner or partners ;
- (b) Any corporation, limited company or other form of business affording its owners limited liability, which is engaged or engages or may engage in the practice of public accounting in the Middle East.
- (c) An individual or individuals engaged in rendering accounting services or giving business advice, practicing under any designation or style other than the name or names of any present or past owner, partner or partners ;

and any member found to be connected, associated, or joined with the above, shall be liable to immediate expulsion upon two-thirds (2/3) majority vote of the Committee on Ethics and Grievances.

RULE 3 :

A member shall not allow any person to practice as his representative or under his name, unless such person is his partner or his full-time employee. A member shall not maintain any office in his name or in the name of his firm, unless it shall be regularly staffed by himself or by a person entitled to practice as his representative or under his name under this Rule.

RULE 4 :

A member shall not approve, certify or express an opinion on the accuracy of accounts or financial statements which have not been verified under the supervision of himself or of another person representing him in conformity with the foregoing Rule 3.

RULE 5 :

A member shall not prepare, sign, or express an opinion on any report or financial statement which to his knowledge contains a material misstatement of fact, or omits or conceals such facts as will result in the material misrepresentation of the financial condition or operations of any business or organization, or of the relationship thereto

of any individual, firm, or organization. Reservations or qualifications relating to the opinion of a member with respect to financial statements or reports examined by him, if not clearly set forth in the body of the financial statements, shall be recited in footnotes or in an appended and signed recital or report, provided that a reference to such recital or report shall appear clearly on every page of the statements with which it is enclosed.

RULE 6 :

In expressing an opinion on financial statements which he has examined, a member may be held guilty of an act discrediting the profession, and upon recommendation of the Committee on Ethics and Grievances, may be liable to expulsion from the Society, if :

- (a) He fails to disclose a material fact known to him which is not disclosed in the financial statements, where such non-disclosure makes the financial statements misleading ; or
- (b) He fails to report any material misstatement known to him to appear in the financial statements ; or
- (c) He is materially negligent in the conduct of his examination or in making his report thereon ; or
- (d) He fails to acquire sufficient information to warrant the expression of an opinion ; or
- (e) He expresses his approval of financial statements in conjunction with exceptions which are sufficiently material to make his expression of approval meaningless; or
- (f) He fails to direct attention to any material departure from generally accepted accounting principles or to disclose any material omission of generally accepted auditing procedures during the conduct of his examination.

RULE 7 :

A member shall not express his opinion on financial statements of any enterprise, if he owns or is committed to acquire a financial interest in the enterprise which is substantial, either in relation to its capital or to his own personal fortune, or if a member of his immediate family owns or is committed to acquire a financial interest in the enterprise which is substantial either in relation to its capital or to his own personal fortune, or if his partner, employer, or associate in business owns or is committed to acquire such an interest, unless in all cases the member discloses in his report such an interest.

RULE 8 :

A member shall not directly or indirectly solicit clients by circulars or advertisements, nor by personal communication or interview not warranted by existing personal relations, and he shall not encroach upon the practice of other public accountants; provided further, however, that a member may furnish service to those who request it of their own accord, even though they may be or have been the clients of another accountant. Whenever a member acquires a client, if such client is or has been the client of another public accountant, the member must write a letter of inquiry to the previous accountant of the client, asking whether he has any professional objections, and shall refuse to serve the client if the previous accountant shows valid objections ; provided further, that the term "valid objections" shall be taken to mean objections which would result in a breach of one or more of these rules if such

objections are not considered.

RULE 9 :

A member shall not advertise his professional attainments or services ; all members shall be entitled to the following :

- (a) The use of a letterhead, report cover, visiting card, and office name-plate of a maximum size of 30 x 50 cm, provided that these bear no more than : (i) the name of the practice or firm, compatible with Rules 1 and 2 hereof, (ii) the location of its office or offices and the customary postal, telegraph, and telephone information, (iii) the names of the partners or the individual practitioner followed by initial letters indicating their professional memberships, degrees and diplomae, and (iv) a caption or phrase indicating the nature of the practice, as "Associated Accountants", where permissible under these rules, and as "Public Accountants" where the official designation of this Society cannot be used.
- (b) A paid listing in a directory restricted to the name, title, address and telephone number of the person or firm, which shall not appear in bold type, box, or other form of display, or a style which in any way differentiates it from other ordinary listings in the same directory. Listing of the same name in more than one place in a directory is prohibited.

RULE 10 :

A member shall not allow commissions, brokerage fees, or other participation in the fees or remuneration of professional work of any type whatsoever, directly or indirectly, to a non-accountant. Commissions, brokerage fees, or any other participation in the fees, charges, or profits of work recommended or turned over to non-accountants as incidental to services for clients shall not be accepted directly or indirectly by a member.

RULE 11 :

A member shall not engage in any commerce or occupation conjunctly with the profession of public accounting, which is incompatible or inconsistent therewith. *Prima facie*, the rendering of all types of professional business service for a fee shall be considered to be permissible under this Rule.

RULE 12 :

A member shall not permit his name to be used in conjunction with an estimate of earnings contingent upon future transactions in a manner which may lead to a belief that the member vouches for the accuracy of the forecast.

RULE 13 :

No member shall offer to render or in fact render professional service for a fee which is contingent upon the findings or result of such service. Fees which remain to be fixed by courts or other public authorities, and which are therefore of an indeterminate amount at the time when an engagement is taken are not to be taken as contingent fees within the meaning of this Rule.

RULE 14 :

No member shall make direct or indirect offers of employment to an employee of another accountant without first informing such accountant. This Rule shall not be interpreted so as to inhibit negotiation with anyone who of his own volition and initiative, or in response to public advertising, shall apply to a member for employment, but if such negotiation results in an offer of employment the prospective employing member must inform the past employing accountant before finally engaging the employee.

RULE 15 :

A member shall not make a competitive bid against other public accountants for any type of professional service. A competitive bid for professional engagements is defined as an offer made to a person, organization or public authority, other than a regular client, to perform a specified service for a specified sum, or any commitment or estimate having the same effect, when it is known to the bidding member that the aforesaid person or organization is considering more than one practitioner or firm with a view to choosing one of them.

RULE 16 :

A member shall hold as a sacred secret and in confidence all information obtained from any client, and shall only disclose such information with the specific permission of the client or as disclosure may be required by due legal process.

RULE 17 :

A member shall conduct his private life in such a way that he will not throw discredit upon the Society, and the conviction of a member for any felony or criminal act by a duly constituted court shall be sufficient cause for his expulsion from the Society.

RULE 18 :

A member in his practice of public accounting shall not permit an employee or representative to perform for the member's clients any services which the member himself or his firm are not permitted to perform.

RULE 19 :

A member who receives an engagement for services by referral from another public accountant shall not extend his services beyond the specific engagement thus referred to him without obtaining the referring public accountant's approval in writing in advance.

RULE 20 :

A member shall not permit his name to be associated with statements purporting to show financial position or results of operations in such a manner as to imply that he is acting as an independent public accountant unless he shall :

- (1) Express an unqualified opinion, or
- (2) Express a qualified opinion, or
- (3) Disclaim an opinion on the statements taken as a whole and indicate clearly his reasons therefor, or
- (4) When unaudited financial statements are presented on his stationery without his comments, disclose prominently on each page of the financial statements that they were not audited.