

# Cash Wealth Maximization: The Jewel in the Crown (Reductionism in its Worst Form)

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**Abstract** The essence of the four most famous documents relating to the formulation of objective(s) of financial reporting (statements) issued by the Trueblood Committee's Report, SFAC No. 1, IASB's CF and IASB-FASB's Joint CF, clearly indicates that they are fully saturated with the Milton Friedman's neoclassical economics doctrines. Friedman's espoused belief in restricting the objective of a commercial enterprise within the realm of cash wealth maximization, reflects an absolute reductionism. All actions, behaviours, activities and decisions, by the management of a commercial enterprise are required to march on a narrow and intentionally chosen path; that is, cash wealth maximization. This type of reductionism is unusual and runs counter to the natural and fruitful reductionism adopted in all human endeavours, including scientific endeavors. The single objective of cash wealth maximization, adopted by the four accounting documents, actually restructures the definition of reductionism in accounting as a social science and activity, to result in an inevitable conclusion that the whole universe is built on cash, lives for cash, and can enjoy a prosperous viability, if only cash is maximized. Everything is required to revolve on the single objective of cash wealth maximization. It emphasises, explicitly and implicitly, that all other issues, commercial or otherwise, are secondary to achieve the goal of cash wealth maximization. As a result, all other issues would be resolved if the objective of cash wealth maximization is achieved. The position of accounting professional bodies, when formulating the objective(s) of financial reporting (statements), reflects a literal adherence to Friedman's doctrines. They look at cash wealth maximization as the single important goal of all business enterprises, and accounting must be geared to offer information conducive to this goal. All goals of all other interested parties (all non-owner groups) are reduced to this single goal. It appears that the thinking of professional accounting bodies' reflects a position of being the staunchest ally of Friedman's doctrines. Thus, the goal of cash wealth maximization is crowned by the professional accounting bodies on the top of all commercial enterprises' objectives, ambitions and aspirations. Since the goal of cash wealth maximization has no competing rival, as an objective of financial information reported, then the goal of cash wealth maximization is the jewel in the crown. This is a lamented use of reductionism. Actually, this is reductionism in its worst form.

**Keywords** Cash Wealth Maximization, Objectives of Financial Statements (Reporting), Friedman, Reductionism, Jewel in the Crown

## 1. Introduction

In his famous article "The Social Responsibility of Business is to Increase Profits", Milton Friedman, the godfather of neoclassical economics, clearly declares that "a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as *much money as possible* -emphasis added- while conforming to their basic rules of society, both those embodied in law and those embodied in ethical custom"[8]. For Friedman, the activities by corporate executives reflecting social responsibility

approach frauds, and the whole doctrine of social responsibility is "fundamentally subversive".

Thus, two intimately connected doctrines emerge from the previous quotation: the doctrine of cash wealth maximization and the doctrine of a replicate thinking; a commercial entity is an instrument required to be nothing but a completely literal reflection of its owners' thinking. A commercial entity's existence is assumed to be solely conferred by its owners and accordingly, it must exactly behave in a manner of how its owners want. Therefore, public interest in a commercial entity has no sense. The creators of a commercial entity are its owners not the society. Investing cash per se is a license for dictating anything on a commercial entity. All other licenses required by a commercial entity for commencing and continuity of operations which collectively reflect society's approval for its existence is perhaps nothing but mere cosmetic formalities stipulated by laws and regulations anywhere and

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at any time.

Three universal generalizations that are not bounded by time and space can be established based on above two doctrines. First, whenever and wherever there is a private commercial entity, the whole universe is only concerned about the interest of only one group; i.e. its owners. Second, whenever and wherever there is a private commercial entity, the relationship between a commercial enterprise and its owners is completely centered on cash wealth maximization. Third, whenever and wherever there is a private commercial entity, the whole universe is concerned about achieving the goal of cash wealth maximization.

According to Friedman's thesis, in economics, theorists are divided into two camps: the camp of the majority who disagree with Friedman's thesis and the camp of the minority who agree with Friedman's thesis [21]<sup>1</sup>.

In accounting, there are also two camps; the camp of the minority who disagree with Friedman's doctrines and the camp of majority who agree with Friedman doctrines. The first camp in accounting is represented by theorists who disagree with accounting practice and theory that advocate Friedman's doctrines. Theorists who advocate social and environmental reporting naturally belong to this camp. The other camp is mainly represented by authors (theorists) of accounting textbooks and professional accounting bodies. For example, authors (theorists) of financial accounting textbooks used in elementary accounting courses belong to the camp that fully advocate Friedman's doctrines since they educate accounting students to believe that a commercial enterprise is its owner(s); all revenues, expenses, withdrawals and dividends are treated as either increases or decreases in owner's equity. Friedman's doctrines are also reflected through various accounting concepts and methods adopted by various authors of financial accounting textbooks such as earnings per share in various financial accounting textbooks, general purchasing power accounting method and Chambers' continuously contemporary accounting in various accounting theory textbooks. All authors of cost and management accounting textbooks who advocate opportunity cost and marginalism doctrines, both of which are a reflection of wealth maximization, are actually advocates of Friedman's wealth maximization doctrine.

Accounting professional bodies belong to the camp that advocates Friedman's doctrines. [18] argues that "professional accountancy students are encouraged to learn rules and techniques, but with little reflection on their social consequences. The aim of "maximizing shareholders wealth" takes precedence over any sense of equity, fairness or justice". This is attributed to the failure of the accounting profession to "acknowledge that accounting is fundamentally an ethical, rather than a technical, course" [20].

Actually, accounting professional bodies' position on advocating Friedman's doctrines could be considered as the

most extreme one. They look at cash wealth maximization as the single most important goal of business enterprises, and accounting must be geared to offer information conducive to this goal. All goals of all interested parties are reduced to this single goal. It appears that professional accounting bodies' thinking is saturated with Friedman's doctrines to the extent that they can be considered as more royal than the king. They disseminate Friedman's doctrines around the globe without being objected to by fellow accounting professionals due to the strong hegemony of the neoclassical economics doctrines on accounting teaching at both professional and academic levels and due to the perpetuated difficulty of discerning the submerged economic doctrines in accounting numbers. Professional accounting bodies are the staunchest ally of Milton Friedman's doctrines since they look at cash wealth maximization as a jewel in the crown.

A case in point is the formulation of objective(s) of financial statements (reporting) by professional accounting bodies. The four most important documents in modern accounting history that dealt with the formulation of the objectives of financial (statements) reporting are the Report of the Study Group on the Objectives of Financial Statements (hereafter the Trueblood Committee's Report, named after Robert M. Trueblood, the chairman of the Study Group) issued in 1973 by the American Institute of Certified Public Accountants (AICPA), Statement of Financial Accounting Concept No. 1 (hereafter SFAC No. 1) issued in 1978 (amended and reissued in 2008) by the Financial Accounting Standards Board (FASB), the Framework for the Preparation and Presentation of Financial Statements, issued by the International Accounting Standards Committee (IASC) in 1989 and adopted by the International Accounting Standards Board (IASB) in 2001 (hereafter IASB's CF), and the conceptual framework issued in 2010 as a joint effort by both IASB and FASB (hereafter IASB-FASB's Joint CF)<sup>2</sup>.

There is one common distinctive feature in these four documents; cash wealth maximization is the single most important goal of the objectives of financial reporting. No other goals are allowed to compete with this goal. Thus, the goal of wealth maximization is a jewel in the crown. All important goals, such as society's prosperity, are replaced with (reduced to) a single goal.

Reductionism is greatly based on this distinctive feature. In certain cases, reductionism is justified. However, the justification presented is weak to extent that can be easily deconstructed and shown as baseless. In some other cases, no justification is presented. For both, the justified but easily deconstructed and proven to be baseless reductionism and

<sup>1</sup> Among those who disagree with Friedman's thesis are [14], [15], [9], [11], [22], and [2]. Among those who agree with Friedman's thesis are [17] and [5].

<sup>2</sup> The Joint Conceptual Framework Project of the FASB and IASB consists of eight phases. Phase 1 was issued in 2010. Phase 1 consists of two chapters. Chapter 1 deals with the objective of general purpose financial statements and chapter 2 deals with qualitative characteristics of useful financial information. The FASB issued phase 1 as SFAC No. 8 and the IASB issued it as Conceptual Framework for Financial Reporting 2010. Only chapter 1 is used in this paper. There are very few minor differences in these two documents related mainly to the prefaces of both documents. In this paper, the IASB-FASB Joint CF is used since it is more expressive than other titles used either jointly or separately by the FASB and IASB.

unjustified reductionism, the arguments can be characterized as logicless. Thus, the worst form of reductionism is used in the four documents issued by the above professional accounting bodies.

There are two main themes that direct the arguments in this paper. First, the objectives of financial statements (reporting) formulated in the four documents are completely captured by the above two doctrines implied in Friedman's position on the relationship between a commercial enterprise and its owners, or the above three generalizations derived as consequences of Friedman's position. Second, this capturing has far reaching consequences on the objectives of financial statements (reporting) particularly the structured role of the financial information provided.

The main contribution of this study is to clarify that the four professional accounting bodies (the Trueblood Committee's Report, the SFAC No. 1, the IASB's CF and the IASB-FASB's Joint CF) are supporting the concept of cash wealth maximization as a jewel in the crown. To pursue this goal, this study tries to demonstrate that the four documents take for granted the environment of the entire universe is cash, cash is invested for the purpose of generating as maximum cash as possible, and all human beings focus only on the goal of cash wealth maximization and they seek unlimited cash wealth maximization.

The remainder of the paper is organized as follows: section 2 presents and defines the concept of reductionism. Section 3 demonstrates that the four documents use reductionism in its worst form for the purpose of holding cash wealth maximization as a jewel in the crown. Section 4 summarizes and concludes the study.

## 2. Reductionism

Merriam-Webster Online Dictionary[13] presents the following two definitions of reductionism: "1. explanation of complex life-science processes and phenomena in terms of the laws of physics and chemistry; also: a theory or doctrine that completes reductionism is possible 2. a procedure or theory that reduces complex data and phenomena to simple terms. The Business Dictionary[19] presents the following two definitions of reductionism: "1. Material world-view in which complex phenomenon is broken down into conceptual chunks small enough to be analyzed or measured. The basis of all analysis, reductionism is useful in understanding inanimate things or simple systems. 2. This philosophy (specially when taken to extreme), however, dismisses environment as merely a set of resources to be consumed, and human beings as tools to be manipulated and exploited...".

According to the above definitions, reductionism could be very fruitful and fundamental for all advances and developments in all types of endeavor by human beings. On the other hand, reductionism could be the worst of all worlds.

As far as natural phenomena and sciences are concerned, the definitions provided by the Merriam-Webster Online

Dictionary and first definition provided by the Business Dictionary rightfully confer on reductionism the proper status it deserves as far as natural sciences are concerned. This same proper status is also conferred on reductionism by John Henry Holland due to its role in bringing about a tremendous advancement in science[3].

When properly understood and adequately implemented, reductionism could be a fundamental approach in creating a huge development in all fields of scientific inquiry. It is very important to focus on the most relevant and fundamental independent variables. Thus, a phenomenon is only explained in terms of these variables. In addition, it is the usual case that either the number of all possible variables is so huge, uncontrollable, or unknown. Restricting an endeavor at the theoretical and practical levels within the most important variables is dictated by both practicality and pragmatism. Actually, both materiality and relativism are based on reductionism.

As far as social phenomena and sciences are concerned the italic and bold parts in the above definitions show how reductionism cannot be useful for social sciences. This is because social phenomena can hardly be explained in terms of the laws of physics and chemistry. Laws of physics and chemistry are fundamentally less influenced by the human dimension. In addition, it can never be true that the environment of a single social phenomenon amenable for reduction to a single element.

It is beyond doubt that the Trueblood Committee's Report, the SFAC No.1, the IASB CF and the IASB-FASB's Joint CF fully and strictly go, in their adoption of reductionism, beyond the point of forcing a strictly social phenomenon to be dressed up in the cloths of natural science. They adopt reductionism that perhaps fits best a pure science situation. Thus, we develop the following definition of reductionism:

**A materialist and instrumentalist approach that looks at the environment of the entire universe, that actually consists of huge number human and material of resources, as merely consisting of only one single resource i.e. cash, that must be maximized, and human beings can be looked upon as mere materials and instruments to be manipulated and exploited for the sake of satisfying a single goal, i.e. cash wealth maximization, desired by only one group of human beings, i.e. owners or shareholders, since all other groups of human beings believe, are assumed to, or must believe that if this group of human beings is satisfied, then goodness and prosperity for all other groups would definitely prevail.**

Thus, as long as the duality of cash invested and a private commercial entity exists anywhere at any time in the universe, there is one goal to emerge, that is, cash wealth maximization. The four documents, when formulating the objective(s) of financial statements (reporting), adopt the position that cash wealth maximization is the center of everything in the universe. Almost everything can be achieved and all problems can be solved if the fundamental objective of cash wealth maximization is literally adhered to. Thus, everything is reduced to cash wealth maximization.

This is an improper use of reductionism in accounting intended to perpetuate biases in the provision of accounting information. The reductionism employed by the four documents is simply an attempt to force homogeneity on what is naturally heterogeneous. All this would result in the negation of the others, disavowal of responsibility for a multitude number of social goals and legitimating of hegemony by specific group(s) with vested interest. These are just few consequences of what is espoused by Friedman and his disciples including the professional accounting bodies<sup>3</sup>.

### 3. A Jewel in the Crown: A Clear Manifestation of Adherence to Reductionism

#### 3.1. Trueblood Committee's Report

The goal of cash wealth maximization is given by the Trueblood Committee's Report two characteristics: primacy and immortality. Primacy, since it overrides any other goals such as accountability (PP. 25-26) and social goal (PP. 53-55). The immortality characteristic is reflected in the assumption that the goal of using cash by an enterprise to generate more cash "remains unchanged"[1]. To emphasize the importance attached to cash wealth maximization, the Trueblood Committee's Report requires all interim accounting measurements of an enterprise's progress to serve the goal of cash wealth maximization[1].

To pursue the goal of cash wealth maximization, the Trueblood Committee's Report establishes a clear connection between earnings and cash generated. It is stated that "Over longer periods, cash generation and earnings come closer. Over the entire life of an enterprise, they are the same. That is, earnings can only come from cash generated by operations; cash generating ability and earning power are equivalent"[1]. The implication is that cash wealth maximization requires more earnings and then conversion of this more earnings into cash. It is the provision of the highest cash to its owners that is taken to represent a test of the earnings ability of an enterprise. This represents, beyond any doubt, a traditional capitalistic approach to a commercial entity's goal. The goal of a commercial enterprise is the goal of its owners (the capitalists).

Since cash wealth maximization requires the achievement of more earnings and the ability of converting this more earnings into cash, the Trueblood Committee's Report gives both earnings (profit) as well as earning power a very prestigious position. "Earnings as reported in financial

statements have come to be, and in all probability will continue to be, the single most important criterion for assessing the enterprise's accomplishments and earning power"[1]. To emphasize the required connection between earnings and earning power, the whole statement of periodic earnings is assigned one task in objective 8, that is, providing information useful for predicting, comparing and evaluating enterprise power[1].

The most important issue is to establish a logical connection between the goal of cash wealth maximization and the provision of information. Accounting is required by the Trueblood Committee's Report to furnish information that allows owners to assess the earning power ability of an enterprise since, according to the Trueblood Committee's Report; they are watching this ability on almost a daily basis[1]. In this regard, a brief discussion of certain objectives formulated in the Trueblood Committee's Report is useful. Among its 12 objectives, objectives 3 and 4 could be regarded as the most fundamental objectives. Objectives 7, 8, and 9 are closely related to objectives 3 and 4 in a sense that they simply enhance what is dictated by objectives 3 and 4.<sup>4</sup>

Objective 3 requires financial statements "to provide information useful to investors and creditors for predicting, comparing, and evaluating potential *cash flows*—emphasis added- to them in terms of amount, timing and related uncertainty"[1].

Objective 4 requires financial statements "to provide users with information for predicting; comparing and evaluating enterprise *earning power*—emphasis added"[1].

Objectives 3 and 4 complement each other. Objective 3 discusses the possibility of a change in wealth expressed only in cash and objective 4 covers the provision of information on the source of that change in cash wealth. Therefore, earning power is about an entity's futuristic ability to bring in more cash derived mainly from its operating activities. Taken together, these two objectives require the provision of information on the twin interdependently interwoven tasks: the task of achieving earnings and the task of converting earnings into cash. However, it is obvious that objective 3 has priority over objective 4. This is important in order to mould objective 4 in a narrowly restricted path of converting earnings into cash and not to anything else. Accordingly, a commercial entity has only one task, which is a cash maximization seeker; i.e. a replicate of its owner(s). Objectives 7, 8 and 9 cover the information channels to send messages to outside users of financial information that are literally included in objectives

<sup>3</sup> The Business Council of Australia[4] is among the disciples of Milton Friedman. The BCA strongly adheres to the objective of wealth maximization of shareholders. The BCA believes that "The litmus test for any activity or responsibility is whether the performance of that activity or responsibility can reasonably be seen to be contributing to the growth of shareholder value. While some may argue that this is too restrictive, the BCA believes that it is a paramount principle entrenched in the basic nature of the corporation and its arrangement with the owners of its capital, the shareholders."

<sup>4</sup> A brief summary of the other non-fundamental objectives formulated by the Trueblood Committee's is necessary. Objective 1 and 2 are general. Objective 1 requires the provision of information for economic decision making. Objective 2 specifies the type of users of accounting information. Objective 5 requires the provision of information useful for judging management's performance. Objective 6 requires the disclosure of basic assumptions. Objective 10 requires the provision of financial forecasts. Objective 11 is related to the non-for-profit organization. Objective 12 is about social goal which will be discussed later in this paper.

3 and 4.

The statement of financial position (Objective 7), statement of earnings (objective 8) and statement of financial activities, related only to significant cash consequences, (Objective 9) are all required to provide one type of information, that is, “useful for predicting, comparing and evaluating enterprise earning power”[1]. As result, we can conclude that the Trueblood Committee’s Report considers cash wealth maximization is a jewel in the crown.

### 3.2. SFAC No. 1

The position of SFAC No. 1 is not different from the Trueblood Committee’s Report. It assumes that there are universal tendencies held by both people and commercial enterprises reflected in being preoccupied with assessing the amounts, timing, and uncertainty prospects of cash invested. For example, it is stated in par. 38 that “People engage in investing, lending, and similar activities primarily to increase their cash resources. The ultimate test of success (or failure) of those activities is the extent to which they *return more (or less) cash than they cost*-emphasis added” ([6]. The phrase “The ultimate test of success and failure” should not be overemphasized. The universal tendencies are extended from people to include business enterprises (the assumed replicate phenomenon). In par. 39, it is stated that “business enterprises, like investors and creditors, invest cash in noncash resources to earn more cash. The test of success (or failure) of the operations of an enterprise is the extent to which the cash returned exceeds (or less than) the cash spent (invested) over the long run...”[6].

Just like the Trueblood Committee’s Report, SFAC No.1 gives earnings and earning power a very prestigious position. It is stated in the HIGHLIGHTS that “The primary focus of financial reporting is information about earnings and its components”[6]. Earning power is also emphasized in the HIGHLIGHTS either directly through the use of the term “earning power” or indirectly through an emphasis on provision of information useful “...in assessing the amounts, timing and uncertainty of prospects of cash receipts...” (P. 2). The HIGHLIGHTS are also used as a platform to establish a relationship between earnings and earning power. This locus of interest on both earnings and earning power is also adhered to in an elaborate manner in the section entitled “Enterprise Performance and Earnings”. Five out of six paragraphs of this section are either directly devoted to establish a relationship between earnings and earning power or indirectly through emphasizing the importance of providing information useful for assessing the prospects of future cash flows[6].

To find out the relationship between the goal of cash wealth maximization and the provision of information, the objectives formulated by SFAC No. 1 should be analyzed. SFAC No. 1 contains seven objectives. Objective 1, 2 and 5 are the core objectives. Objectives 3, 4, 6 and 7 are only enhancing objectives. Objective 3 is general and covers an enterprise’s resources, claims to those resources and changes in them. Objective 4 addresses the information of economic

resources, obligations, and owners’ equity. Objective 6 discusses the information of liquidity, solvency and funds flows. Objective 7 covers the information for assessing stewardship function of an enterprise’s management by its owners.

Objectives 1, 2 and 5 are the most important, complementary and intimately related to the core of a capitalistic model of a commercial enterprise.

Objective 1 reflects a jewel in the crown. It states that “financial reporting should provide information that is useful to present and potential investors and creditors and other users in making *rational investment, credit, and similar decisions*-emphasis added-...”[6]. It is well-known in economics literature that a rational economic decision is the one that seeks cash wealth maximization.

Objective 2 states that “financial reporting should provide information to help present and potential investors and creditors and other users in *assessing the amounts, timing and uncertainty of prospective cash receipts*- emphasis added- from dividends or interest and the proceeds from the sale, redemption, or maturity of securities and loans”[6].

Objective 5 states that “financial reporting should provide information about an *enterprise’s financial performance* –emphasis added- during a period[6].

Therefore, taken together, objectives 1, 2 and 5 presents an integrated whole consisting of an entity, its finance providers, mainly owners as this is made clear in pp. 14-15/par. 51, and the specific type of language dictated by the finance providers. Owners and creditors invest in an entity for one assumed purpose; i.e. cash wealth maximization. The investee, i.e. a commercial entity, is assigned only the task of achieving this one assumed objective (the assumed replicate phenomenon). The information provided must be useful for two things simultaneously as far as cash wealth maximization is concerned. First, it reflects an entity’s past period performance. Second, it guides the formulation of expectations (futuristic perspective) by the investors. Again, we can conclude that SFAC No. 1 considers cash wealth maximization is a jewel in the crown.

### 3.3. IASB’s CF

The position of the IASB’s CF is slightly different from that of both the Trueblood Committee’s Report and SFAC No. 1 in that the word “maximization” or any other word representing “maximization “ are avoided. In addition, the term “earning power” is never used by IASB’s CF. However, the difference is in appearance rather than in content. The content is identical. The primacy of the goal of cash wealth maximization requires an analytical and evaluative discussion. First of all, earning power, through an entity’s ability to generate future cash flows, is overemphasized in paragraphs 15, 16, 17 and 18[10].

Par. 15 assumes that the relationships between users of financial information and a commercial entity are solely restricted to economic decisions. These decisions are only based on the evaluation “of the ability of an entity to generate *cash and cash equivalents* –emphasis added- and of the

timing and uncertainty of their generation". Therefore, users of financial information only make cash-based economic decisions solely related to the ability of an entity to generate cash and cash equivalents characterized by the uncertainty dimension. It is obvious that the assumed replicate phenomenon up to this point is partially achieved since only cash is emphasized in the relationship between them. Cash wealth maximization has to be found.

The language required by the investors is delineated in paragraphs 16, 17 and 18, but most importantly clarifies the real substance of the objective of financial statements, i.e. cash wealth maximization. These paragraphs describe the role of three financial statements in the provision of financial information which together lead to achieve the goal expressed in par. 15. In addition, this language reflects the role of an investee as a cash wealth maximize.

Par. 16 assigns, in a rhetorical and oratorical style, to the statement of financial position the task of providing "information about economic resources controlled by the entity and its capacity in the past to modify these resources in predicting the ability of the entity to generate *cash and cash equivalents*—emphasis added- in the future".

Par. 17 requires the income statement to provide information about an entity's profitability in order "to assess the potential changes in the economic resources that is likely to control in the future". This in turn requires "information about variability in performance". All these information is assumed to be "useful in predicting the capacity of the entity to generate *cash flows*—emphasis added- from its existing resource base".

Par. 18 requires the statement of changes in financial position of an entity to provide information leading to an assessment of its investing, financing and operating activities which is, in turn, useful in providing the users with "a basis to assess the ability of the entity to generate cash and cash equivalents and the needs of the entity to utilize those cash flows".

There are three points worthy of emphasis in the above argument related to IASB's CF. First, it is obvious that IASB's CF targets is establishing a link among the three financial statements. Financial position is required to indicate the amount of economic resources controlled by an entity. Income statement is required to indicate the effectiveness and efficiency with which these controlled resources are managed. Statement of changes in financial position is required to indicate the possible cash changes in these resources classified among investing, financing and operating activities. The link among the three financial statements reflects two important roles: their role individually and collectively in providing information based on historical perspective to assess an entity's ability to generate cash and cash equivalents, and their role of reflecting the assumed replicate phenomenon. On the other hand, there is a lack of providing practicable and workable guidelines on how historically based information can be used by users in predicting an entity's ability to generate cash and cash equivalents in an uncertain future. It appears that

IASB's CF masks its incompetency in this regard with a rhetorical and oratorical style based on traditional accounting.

Second, earnings and its components are not emphasized as strongly as earning power. However, in par 17, performance, particularly profitability, is linked to earning power. Profitability is considered useful for assessing the possible changes in the economic resources that an entity is likely to control in the future. Thus, a futuristic perspective of the possible changes in economic resources is based on the relationship between earnings and investment. Information about performance is also assumed to be "useful in predicting the capacity of the entity to generate cash flows from its existing resource base"[10].

Third, nothing indicates directly that IASB's CF adopts the goal of cash wealth maximization. Par. 9 (a) states that investors (providers of risk capital) are interested in two pieces of information: "risk inherent in, and return provided by, their investments"[10]. In the same paragraph, IASB's CF provides two reasons for the emphasis on these two pieces of information. The first is to make specific economic decisions related to their shares (buy-hold-sell decisions). The second is to assess an entity's ability to pay dividends. The main source of dividends is earnings. Of course, cash dividends is ultimately what is sought by investors (providers of risk capital). Therefore, it is an entity's ability to transfer the changes in economic resources mainly through earnings into cash, that most matters. This means that cash wealth maximization is indirectly sought. The assumed replicate phenomenon is clear as the sun in the daylight.

This emphasis on the cash wealth maximization can also be indirectly derived in different ways by analyzing three positions stated by IASB's CF in both the section entitled "users and their information needs" and the section entitled "The objectives of financial statements"[10]. First, it is stated in par. 10/P. 35 that information needs of investors as providers of risk capital "will also meet the needs of other users that financial statements can satisfy". In par. 1/P.35, investors are only represented by shareholders. Second, it is stated in par. 12/P. 36 that financial statements should provide information for making economic decisions. No other type of decisions is mentioned. Third, in par. 15/P. 36, only the information to evaluate the ability of an entity to generate cash and cash equivalents and the amount, timing and uncertainty of their generation is required to be provided by financial statements for the purpose of making economic decisions. All financial statements mentioned in paragraphs 16/P. 36, 17/P. 37 and 18/P. 37 are specifically required to provide information useful in predicting the ability of an entity to generate cash and cash equivalents in future. In addition, in par. 17/P.37, profitability or variability in performance is emphasized for its role in predicting the entity's ability in generating future cash inflows.

Therefore, the fundamental objective of financial statements is the provision of financial information useful for judging on an entity's ability to maximize the cash wealth of

its owners (shareholders).

It is very interesting to note that IASB's CF, unlike the Trueblood Committee's Report, and SFAC No. 1, does not put owners, creditors and other economic decision makers on one boat. It puts owners in a boat and all other groups in a society in another separate boat tagged by the owners' boat. The fate of the boat of all other groups in a society is dependent on the fate of the owners' boat. All other groups in a society must accept this situation for one, and only one, reason that is, owners are providers of risk capital. It is important to discover that the generalizations set by the IASB's CF are not restricted by time and place. The implied assumptions are that either cultural differences among societies do not exist or the replicate phenomenon has nothing to do with cultural differences. Even in natural sciences, phenomena are only capable of being replicated when certain conditions are available. For example, adding one atom of oxygen to two atoms of hydrogen would result in water only if certain conditions are met. Without these conditions, the addition would not result in water. IASB's CF suggests that whenever and wherever there is an investor who invests his cash in an investee, the result is bound (imperatively) to be a maximization of cash.

### 3.4. IASB-FASB's Joint CF

Just like the IASB's CF, the IASB-FASB's Joint CF tries to avoid giving the impression of advocating an explicit and direct preferability to cash wealth maximization. An evaluative analysis is also required.

In OB3, it is assumed that expectations about returns on/of investment are assumed to be the basis for making decisions by participants in capital markets[7]. It is also assumed in OB3 that the basic source of these expectations is the assessment by participants in capital markets of the amount, timing, and uncertainty of future cash inflows to an entity. Therefore, participants in capital markets seek information that allows them assessing the prospects of future net cash flows. In OB16, the financial performance, expressed as returns on the economic resources used by an entity, is considered to be the sole measure of the efficient and effective use of an entity's resources[7]. This is the only measure of performance that is considered by IASB-FASB's Joint CF. In addition, information about the variability and components of returns are assigned the task of assessing the uncertainty of future cash flows[7]. In OB18 (PP. 3-4), information about financial performance is also assigned the task of revealing an entity's ability to generate net cash inflows through its operations. This represents a connection between earning power and cash wealth maximization.

However, it is stated in OB3 that all decisions by existing and potential investors, lenders and other creditors depend on returns[7]. These returns consist of dividends for equity investors, principal and interest payments for holders of debt instruments, market price increases for both equity investors and holders of debt instruments, and principal and interest payments and other returns for other lenders and creditors. Therefore, according to IASB-FASB's Joint CF, returns

include both returns on investment and returns of investment. In OB16, it is made clear that an understanding of the returns on an entity's economic resources is based on financial performance[7]. Here, the emphasis is on "returns on economic resources". This represents a shift in the emphasis from returns in general to returns on economic resources. To be sure about this shift of emphasis, returns on economic resources are assumed in OB 15/P.4 to be important for two purposes. It is useful for judging on how management efficiently and effectively discharges its responsibilities related to an entity's economic resources and useful *"especially in assessing the uncertainty of future cash flows"*—emphasis added. The replicate phenomenon should not be overemphasized. In addition, it is stated in the same paragraph that historical information about returns and the way management discharged its responsibilities are important for the prediction of an entity's future returns on economic resources.

Perhaps OB18 is a little bit less implicit and less indirect in its emphasis on the provision of information useful for assessing an entity's earning power and in establishing a link between earnings and earning power since "information about a reporting entity's financial performance during a period ... is useful in assessing the entity's past and future ability to generate net cash flows. That information indicates the extent to which the reporting entity has increased its available economic resources and *thus its capacity for generating net cash inflows through its operations*—emphasis added- rather than by obtaining additional resources directly from investors and creditors"[7]. Again, the replicate phenomenon should not be overemphasized. Then, it is very difficult to avoid the conclusion that earnings information and information useful for assessing an entity's earning power are the locus of interest.

The fundamental issue is the relationship between the locus of interest and the provision of information. The IASB-FASB's Joint CF generally wants the information provided in the general purpose financial reports to have the quality of allowing the formulation of expectations by the participants in capital markets about the amount, timing and uncertainty of an entity's future cash flows. This can be inferred from OB3 through the following logic[7]: First, decisions by participants in capital markets depend on their expectations about returns on and of their investment. Second, expectations about returns on and of the investment by participants in capital markets depend on their assessment of the amount, timing and uncertainty of an entity's ability to generate those cash flows. As a result, we can conclude that decisions by participants in capital markets depend on their assessment of the amount, timing and uncertainty of future cash inflows.

As an evidence of the importance accorded to the information on cash flows, 9 out of 21 OBs includes the term "cash flows". In addition, these 9 OBs are directly related to the importance of providing financial information in assessing by participants in capital markets of the prospects of future cash flows of an entity. Although the remaining 12

OBs do not mention cash flows, they are indirectly related to issues and terms discussed in the other 9 OBs. OB4, requires judging on efficiency and effectiveness of an entity's management and the governing board in utilizing an entity's resources to be based on the assessment by participants in capital markets of an entity's future cash inflows[7]. OB13 and OB14 are respectively related to the importance of analyzing various types of resources and claims against these resources in assessing future cash flows[7]. OB15 and OB16 emphasize the importance of information related to changes in an entity's economic resources and claims in assessing future cash flows[7]. OB17, OB18, and OB19 explain how information on financial performance reflected by accrual accounting is important in assessing future cash flows[7]. OB20 explains how information on financial performance reflected by past cash flows is important in assessing an entity's ability to generate cash inflows[7].

As a result, all OBs are either directly or indirectly involved in emphasizing the importance of providing financial information that is only useful in the formulation by participants in the capital markets of assessment (the creation of perception) of an entity's ability to generate cash inflows. Of course more cash is preferred. Then the fundamental objective of financial reporting is the provision of information that helps participants in capital markets creates perception about an entity's ability to maximize cash wealth. It is very important to note that the IASB-FASB's Joint CF requires the existence of capital markets as the only condition for setting the generalization that cash is maximized whenever and wherever an investor invests cash in investee. All other cultural differences among countries are assumed either to be non-existing or neutral.

#### 4. Implications and Conclusions

The four documents' positions on the objectives of financial statements (reporting) imply a strictly pure mathematical situation. As long as there is (are) investor(s) who invest(s) in an investee, there is only one inevitable result; that is, stockholders' wealth maximization.

Although the IASB's CF and IASB-FASB's Joint CF are constructed through different phrases and perhaps on different logic, the end result is identical. All give considerable attention to stockholders' cash wealth maximization and the structuring of information closely related to cash wealth maximization. For all the four documents, the entity is simply considered as instrument created only by owners for achieving the goal of cash wealth maximization.

Cash wealth maximization is fundamentally the most important feature in the four documents analyzed in this paper. It enjoys the undisputed constellation since it is looked upon as though it is a jewel in the crown. First, the four documents consider the goal of cash wealth maximization to be a "MUST". For both the Trueblood Committee's Report and SFAC No. 1, the "MUST" is an explicit conclusion resulted from their explicit exposition of

the U.S. culture. However, the Trueblood Committee's Report transcends the U.S. cultural environment and sets its logic for the whole universe. The IASB's CF and IASB-FASB's Joint CF indicate, albeit implicitly, that cash wealth maximization is a "MUST" within a universal generalization. The reason for the implicit "MUST" in case of IASB's CF and IASB-FASB's Joint CF is the lack of an explicit discussion of a cultural background. There is of course a cultural background for both the IASB's CF and IASB-FASB's Joint CF. Their cultural background resembles more or less the U.S. culture. This is because the IASB's CF advocates the provision of financial information based on a shareholder's perspective and the IASB-FASB's Joint CF advocates the provision of financial information based on investor-lender's perspective. The investor-lender's perspective is also adopted by the Trueblood Committee's Report. However, the difference between the Trueblood Committee's report and the IASB-FASB's Joint CF is that the Trueblood Committee's Report has nothing to be embarrassed about when it explicitly connects the goal of cash wealth maximization to the U.S. culture. Such a connection is an embarrassing one at the international level. Thus, its cultural background is an implicit one. Second, although each document expresses the goal of cash wealth maximization using different phrases or words, the essence of cash wealth maximization is a crystal clear. The Trueblood Committee's Report uses the term "earning power" which is defined as the ability to generate more cash though the conversion of earnings into cash[1]. Earning power is used as a tool for assessing the ability to achieve cash wealth maximization. SFAC No. 1 argues about an entity's "ability to generate favorable cash inflows"[6]. The IASB's CF uses "the ability of an entity to generate cash and cash equivalents" and "the capacity of the entity to generate cash flows from its existing resource base"[10]. The IASB-FASB's Joint CF prefers to argue about "future net cash inflows to an entity", "future cash flows from the reporting entity", "ability to generate cash flows" and "future cash flows"[7].

There are three problems with universal usefulness of cash wealth maximization of owners. First, it is very hard to accept that economic decisions always represent the prime goal of all users (e.g. governments, employees, public at large). Second, it is very hard to accept that all those who make economic decisions seek maximization of their wealth. It is only owners (shareholders) who are always seeking maximization of their cash wealth. Third, it is very hard to accept that owners' cash wealth maximization truly represent the most important common interest shared by all other interested parties.

The immortality accorded to the cash wealth maximization of the owners advocated by the Trueblood Committee's Report is totally based on a reductionistic approach to the culture of the U.S. In the U.S., it is indoctrinated that shareholders "are the corporations"[12]. The common law confers the legal status on this doctrine by advocating that "public companies must maximize the returns to shareholders"[12]. Accounting education is no less



enthusiastic than the common law in indoctrinating the belief “that the purpose of business is to maximize shareholder value”[16]. The whole financial accounting system is accordingly developed. “A primary bias built on that the financial statements is the notion that stockholders are to be paid as much as possible, whereas employees are to be paid as little as possible”[12]. This means that the Trueblood Committee’s Report and SFAC No. 1 are in harmony with the classical capitalistic model of a commercial enterprise that fits the U.S. environment.

It is quite clear that the prominent position accorded to cash wealth maximization by neoclassical economics permeates the four documents. The position of both the IASB’s CF and IASB-FASB’s Joint CF are the most difficult to explain. This is by itself requires a thorough research investigating three possibilities or any combination thereof. The first possibility is that IASB’s CF and IASB-FASB’s Joint CF are simply echoing the U.S. approach to the setting of objective of financial reporting. The second possibility is that the position of both the IASB’s CF and IASB-FASB’s Joint CF, like that of the Trueblood Committee and FASB, is influenced by the hegemony of the doctrines of the neoclassical economics worldwide. The third possibility is that the position of both the IASB’s CF and IASB-FASB’s Joint CF is a reflection of both echoing U.S. approach and the hegemony of the doctrines of neoclassical economics.

However, there is one obvious result of the IASB-FASB’s Joint CF; the influence of the U.S. accounting heritage is now officially extended to the international arena backed by perhaps the two most influential accounting organizations in the accounting history at the international level.

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