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Property Rights in Accounting Data

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College of Commerce and Business Administration
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Abstract:

Studies of the nature of financial accounting data, as private or public good, cannot provide the necessary guidance for social policy choice among alternative accounting standards and institutions. However, studies of sanctioned human behavior relations, as private or common property rights, will provide insights for understanding the conflicting interests among corporate managers, investors, auditors and government regulators. This article surveys recent literature in law and economics dealing with property rights, and analyzes financial accounting data as a scarce economic good subject to alternative property rights assignments. Voluntary disclosure of data is seen as a private property right; mandatory disclosure is seen as state or common property right. From this perspective several propositions are deduced concerning accounting data users, valuation, measurement, changes in accounting standards, welfare and efficiency. The article concludes with hypotheses about effects of any institution having power to mandate accounting disclosure.


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"The great and chief end of men's uniting into commonwealths and putting themselves under government is the preservation of their property."

~John Locke (1690)

In the development of accounting thought, a study of alternative property rights configurations will provide insight for dealing with many obvious problems such as defining a firm's resources set and specifying the domain of accounting events. But neither of these is the main subject of this paper. The purpose of this paper is to raise the subject of property rights in financial accounting data (second section), in the context of Pareto-optimality (third section), and to derive some propositions relevant to the choice among accounting institution alternatives (fourth section). The introductory overview (first section) is minimal because of space limitation. Readers who wish to study the field will find the collection of articles edited by Furubotn and Pejovich (1974) and by Manne (1975) most helpful. Work in history by Noyes (1936) and Schlatter (1951) are valuable for perspective.

Property rights literature as a recent development in law and economics originated with Ronald Coase's classic article, "The Problem of Social Cost" (1960). To my knowledge institutional structure considerations, with financial accounting data viewed as an economic good, have not been systematically presented in accounting journals. "Indeed, in so far as the accounting literature is concerned, all that is typically available on alternative institutional arrangements is a somewhat emotional objection to governmental influence on accounting," [Gonedes, Dopuch and Penman, 1976, p. 100] This neglect has coincided in recent

decades with an (over?) emphasis on accounting data for management decision and control, where "information" is defined as data useful for decision. [Goldberg, 1965] This paper is concerned strictly with financial accounting data, hereafter FAD, as an economic good with regard to which there are conflicts of interest that can be illuminated by a property rights perspective.

ON PROPERTY RIGHTS

Two traditions in Anglo-American jurisprudence provide alternative grounds for considering property rights. Common law looked on property as a thing owned by a person. Courts in equity looked on property as behavior claimed of other persons. [Commons, 1924, p. 234] Both of these traditions are reflected in accounting. Managers are concerned for control relations over things, that is, "property" in its original common law sense of physical possession, the asset side of the balance sheet. But in recent literature in law and economics, property rights are the behavioral relations among men, formal and informal rules which specify what an individual may and may not do with things (including FAD). [Pejovich, 1972] In both traditions the difference between anarchy and social order is the extent and stability of property rights specification. [Stubblebine, 1972] This specification involves distinctions between what only one person may do with a scarce resource (often called "private property"), what anyone may do (often called "common property"), and what a government may do (often called "state property").

The term "property" is used here to emphasize behavioral relations. The term "good" is used to emphasize the nature of the scarce resource. For distinguishing among kinds of goods, the degree of potential excludability is important. A thing is called "private good" if all but one consumer can be excluded (as when an individual eats a cookie). A thing is called "common good" if (1) an additional consumer does not affect consumption by other persons (as when another television set is turned to some channel), and (2) no consumer can be feasibly excluded (for example, national defense). A thing is called "public good" if (1) an

additional consumer does not affect consumption by other persons, and (2) exclusion of potential consumers is feasible (for example, subscription cable television). The expression "public goods" and "private goods" are often used ambiguously to include both ideas, thing and behavior, with public including notions of both state and common.

In general, production and control of both private and public goods may be subject to private, state, or common property specifications. Conceptually, there may be not only private property rights in private goods, but also private rights in public goods; not only state rights in public goods, but also state rights in private goods; not only common rights in public goods, but also common rights in private goods. While the distinction between private and public goods may be valuable for theory speculation, the present understanding of the nature of goods is deficient as a tool for social policy decisions to improve production and distribution of anything (including FAD). [Demsetz, 1969a] A more useful distinction for studying social policy choice of accounting institution alternatives is between abundant free goods (of which there may be none) and scarce economic goods. Economic goods (including FAD) may be further classified according to the relative benefit/cost relations of production under alternative property rights: private property markets, state government control, and anarchy, which is the absence of feasibly enforceable property rights. [Demsetz, 1964]

The social phenomena of property rights assignment is a necessary and practical solution to the problem of coordinating economic activity so as to realize and stabilize benefits from interaction. Any change in property rights assignments will effect both an instantaneous wealth

transfer and also, especially where transactions are not costless, a change in the use of economic resources. [Demsetz, 1972] Thus the controversy over accounting institution alternatives is a controversy over property rights in FAD. [See, for example, Watts and Zimmerman, 1978]

A private enterprise, free market system can operate if and only if private property rights are assigned with regard to behavior involving the scarce good. The advantages of a free market include diversity, adaptiveness, low-cost production of valuation data (as a joint effect of exchanging goods), equity, and individual freedom. "In fact, a fundamental interdependence exists between the personal right to liberty and the personal right in property. Neither could have meaning without the other." [Pennock and Chapman, 1977, p. 35, quoting Justice Potter Stewart in *Lynch v. Household Finance Corp.*, 405 U.S. 538,552. See also Director, 1964; and Moore, 1969.]

These advantages of the free market should cause us skeptically to examine assertions (such as that of Demski and Feltham, 1976, p. 214) that "market failure" has been "documented in principle". "Whether the alleged forms of "market failure" really exist is, of course, an empirical issue about which there is little reliable evidence." [Gonedes, Dopuch and Perman, 1976, p. 106] But further, illusions of "market failure in principle" rest upon strict analytic concern for end-state equilibria with limiting assumptions such as independent utility functions, a complete pattern of property rights assignment, and a set of equilibrium prices for all goods. Concern instead for the behavioral process of free market adjustment with interdependent utilities, incomplete property rights assignments, and the absence of market prices for some goods casts

doubt upon claims of market failure, whether attributed to fraud, moral hazard, bluffing, punishing, freeriding or adverse selection. Such "pathologies" are more basically analyzable as either (A) correct rational behavior where (1) private transaction costs are in excess of private benefits, or (2) where social policing costs are in excess of social benefits; or (B) institutional failures preventing the smooth functioning of the market by (3) the absence of specific property rights assignment or (4) prohibitions against free exchange. None of these should be called market failure. But even if these cases were to be appropriately termed market failure, "If markets be ends as well as means, their non-efficiency is hardly sufficient grounds for rejection." [Bator, 1958, p. 378] In a free society, markets can be considered ends as well as means.

The legal system functions to maintain clarity of rights on the basis of which voluntary negotiated exchange can take place. Full ownership (that is, complete property rights to behavior) would include rights to possess (e.g., to use, manage, lend, destroy, abandon, etc.); the rights to income (e.g., profits, rent, fruit, etc.); the rights to security (e.g., from theft and expropriation without due process and just compensation); and the rights to transfer (e.g., to sell, give, will, etc). [Honoré, 1961] These different behavioral rights to some good may be exercised by different owners, each restricted to the behavior appropriate to his particular private or social contract. Private ownership is never absolute, and constraints on private property rights affect the market value of resources. Indeed, market value is not a characteristic of goods, but rather a property rights relation.

The corollary to property rights, or ownership behavior privileges, is the commensurate duty or liability of non-owners, including governments as provided in the Bill of Rights of our Constitution. For example, if property rights to indulge in the side-effect of air pollution were given to smokers, then non-smokers would have the liability not to interfere. Conversely, if property rights to impose clean breathing were assigned to non-smokers, then smokers would have the liability to refrain. Owners of property rights will enforce liabilities only when the remedy benefits are greater than private enforcement costs. [Bator, 1958; Demsetz, 1964; Arrow, 1977]

Subsequent to, and integrated with the problem of assigning property rights, is the problem of discovering which liability rule would be more efficiently subject to adjustment through costly market transactions if an "error" is made in the original assignment. [Calabresi, 1968] Only voluntary market exchange can incorporate individual utility weighting to improve property assignments. In sequence, custom or statutory law assigns property rights to avoid anarchy; then to avoid permanent error, the possibility for free market voluntary negotiated transactions is required for optimality. As a corrective device, if smokers were to have pollution rights, then non-smokers should be free to buy abstinence from them; or if non-smokers were to have clean air rights, then smokers should be free to buy indulgence from them. But which alternative would have lower negotiating, transacting and policing costs? With regard to accounting, would it be more efficient for corporate insiders to have private property rights in FAD with outsiders buying disclosure? Or for outsiders to have common property rights in FAD with insiders buying

secrecy? Or for no clear property rights to be maintained under law concerning the production and distribution of FAD?

Private property rights assignment enables internalization of externality, or side-effect, problems for free market resolution. Local markets do develop where the expected benefits are greater than transaction and policing costs. The "Coase Theorem" corrected a basic error in Pigovian welfare economics by showing that where transaction costs are zero and private competitive markets exist, then the allocation of production resources is not affected by different (reciprocal) liability rules. However, where transaction costs are not zero, the property rights alternative (e.g., to clean air breathing or smoking, and to FAD secrecy or disclosure) will have allocative effects leading to different optimality equilibria. [Crocker, 1971] Analytically, there is no way to tell the difference between a primary product, a secondary product, and a side-effect. The distinction is empirical and pragmatic, not analytic. All production is joint, with many physical, pecuniary, and psychological consequences. Accountants allocate costs just to the products that are traded in a market (or perhaps controlled by government). This arbitrary allocation is often made according to ratio of expected revenues. The result is zero costs assigned to products (such as air pollution and FAD) not sold in a market.

The costs of having a market for some product may be greater than the benefits. Then either (1) special government regulations might attain benefits greater than total costs (including costs of discussing, administering, monitoring, litigating, enforcing, punishing, etc.); or (2) neither market nor government arrangements can be made whereby total

costs are less than total benefits from ordering the behavior relations. Contrary to a common bias, this second case would be Pareto-optimal, with the good--such as FAD--remaining in anarchy by voluntary consensus rather than being ordered explicitly by the imposition of either a subsidized market or a coercive state. [Demsetz, 1964] "There are also enormous external costs to the citizenry associated with...[state political control]...which, like a few private market externalities, may be impossible to internalize." [Manne, 1974, p. 32]

A classic example of side-effects involves the production of apples and honey by separate entrepreneurs. This example illustrates the irrelevance of ideal alternatives [Meade, 1952; Bator, 1958] for considering the real alternatives of whether there can be or should be explicit, separate markets not only for consumption goods (apples and honey) but also for side-effect producer goods (nectar and pollen transportation). Other social side effects, such as bee stings and blossom aroma have not been explicitly studied in this context. It may be "too costly" to establish either market or government control over the pollinating and nectar gathering activities of the bees. Obviously, conglomerate merger would eliminate the side-effect problem. Also obviously, the issue is symmetrical and not subject to equity resolution. Less obviously, the concepts of external economies and diseconomies are irrelevant because one side of the "exchange" is a mirror image of the other. Since both apple and honey growers are both victims (i.e., the apple grower is not paid for his nectar, and the honey grower is not paid for transporting pollen) and culprits (i.e., the honey grower is a thief of nectar and the apple grower is a thief of transportation) there is no a priori ethical solution.

Anarchy (that is, no explicit voluntary market exchange) may prevail with first come, first serve. Alternatively, there is ample evidence that where expected private benefits exceed the transacting and policing costs of having a market, contracts do efficiently emerge both for apple growers buying pollination service, and for honey growers buying nectar. [Cheung, 1973] Thus it would be inefficient for government through tax and subsidy arrangements to (try to) impose order where (1) free markets can function, or (2) where the benefits of anarchy exceed the costs. Private contracts do not emerge (or if they emerge, do not persist) where total benefits of having a market are less than the costs of having a market. Similarly government control of any side-effect including FAD should not emerge if total costs of having government control are greater than total benefits from control. [Demsetz, 1969] Consider the hopelessly ideal assertion, "If the nectar in apple blossoms is scarce and carries a positive shadow price, it must be possible to make [emphasis added] every beekeeper pay for his charges meals" [Meade, 1952, as cited by Bator, 1958, p. 355]. Interpreted as an argument for regulation and control, this implies an assumption of zero direct costs for accounting records, transactions, and enforcement; and even zero opportunity costs of eliminating private property.

Just as the existence of a market price for some good does not in itself indicate either equitable endowment of property rights, or optimal resource allocation, "A price for every produced good or service is not a necessary condition for efficiency, so that the absence of a price [for some good, such as FAD] does not imply that either market transactions or substitute government services are desirable." [Demsetz, 1964, p. 14]

The usual methods for dealing with side-effects (in addition to voluntary transactions in a market redistribution of wealth) include (1) outright prohibition, (2) political regulation (time, place, amount, price, etc.), (3) tax and subsidy redistribution by government, and (4) preventive devices. [Mishan, 1971] But these alternatives all involve some version of political voting with majoritarian decisions that ignore the intensity of minority preferences.

Free markets are often spuriously criticized by comparison with some assumed costless end-state ideal structure. The proper comparison for imperfect mankind is not between imaginary static conditions of heaven or hell; but rather between real, non-stationary earthy alternatives where private property and voluntary exchange take place under many uncertainties and miscalculations, and where the negative side-effects of government action affected by similar uncertainties and miscalculations may be far greater than external diseconomies of private markets.

ON ACCOUNTING DATA

The accounting profession faces both definitional issues and policy problems with regard to assignment of property rights in FAD. The concern in this paper is strictly with the monetary accounting record of firm performance and position, and not at all with the informational content (such as positive or negative forecasts or technological discoveries as discussed by Demsetz (1969b), Hirshleifer (1971) or Ronen (1977).)

FAD could be considered an abundant free resource only under two strict assumptions: (1) all joint costs of producing knowledge along with real output are analytically associated with marketable goods; and (2) no incremental costs are incurred to process, complete, and distribute the finished reports. Since these assumptions do not hold realistically, FAD is not an abundant free good. It must be considered a scarce economic good whose production cost is indeterminate.

One definitional issue is whether FAD, pragmatically a side-effect of other production, possesses the characteristic nature of a private good or of a public good. But it is impossible to identify the nature of FAD as strictly private or strictly public. If FAD were in nature a public good, then voluntary or mandatory disclosure to one more user would not affect useage by other consumers. But clearly, the last investor to learn some FAD will find his use of it impaired (if FAD is useful for investor decisions and if the stock market is efficient) because stock price changes will have already fully reflected the revised expectations of earlier investors who learned the data first and acted on it as either inside traders or fortunate outsiders. Alternatively, if FAD were in nature a private good, exclusion would be feasible and

owners would enjoy the benefits of secrecy. But exclusive benefit is in fact tenuous.

As noted above, the private/public good dichotomy cannot provide guidance for social policy decisions as to efficiency or equity. The nature of FAD does not guide the accounting profession or the government in the determination of either standards or institutions. FAD is a scarce economic good conceptually subject to three general arrangements: private property and free market exchange, state or common property and government control, or anarchy. An essential issue is this: "What are the total benefits and costs under each institutional arrangement?" We have virtually no empirical research to help answer this question, nor is it clear how empirical research on this issue should proceed.

The policy problems for the accounting profession include (1) whether individual persons, private associations, the state, or everyone in common should be assigned property rights in access to the (joint productive) source of FAD; (2) whether private or governmental entities should bear the cost and have control over the distribution of FAD; and (3) whether the producer or everyone in common should have property rights in FAD after production. These policy problems need not necessarily be resolved by explicit governmental decision. Conventional justification and evolution of customary expectations might be less disruptive and more efficient than either legislative, executive or judicial decision.

The social role of private property (including the right to privacy, which is the right to keep data from becoming common knowledge) is to prevent the excessive use of scarce resources by providing incentive for economizing. [Knight, 1924, p. 586] Common property rights do not

provide such incentives. Rather, goods subject to common rights will tend to be used excessively. But what empirical meaning can be given to the phrase "excessive use of common property" in the case of FAD which, unlike common grazing ground or ocean fishing banks, is not technically depleted by an increase in the number of "users" even though consumption benefits are depleted by additional users? For example, if a television broadcast is an example of a common property, what "excessive use" results from non-exclusion and zero pricing when TV signals are not depleted in character by additional receivers? Perhaps "excessive use" should be defined not in respect to an altered condition of the good, but rather in respect to the effects of overindulgence on the behavior of users. The dire consequence of overgrazing common grassland or overfishing common water is not just a technical matter of bare ground and empty banks.

Rather, the social cost of "excessive use" means reduced human welfare as an economic matter, and should be defined in respect to foregone alternatives, the opportunity cost of individuals using other non-zero priced goods. For example, "excessive use" of free television could be discussed in respect to the marginal utility decisions made by parents and the consequences for children. That is, the total results of "excessive use" would include the chronic effects on children viewed by network executives as a product delivered to their advertisers. As passive spectators, they may see free too much violence, to the neglect of higher priced goods. These bad effects could include reduced mental ability from too little reading, reduced physical ability from too little exercise, and reduced social ability from too little family interaction. The bad

effects of TV violence may be less in the stimulation of violent criminal acts, and more in the behavioral conditioning of potential victims who, out of anxiety and fear, will turn for security to the reassuring promises of a police state.

The effects of "excessive use" of TV broadcasts as a good subject to common rights are not well known--and neither are the effects of FAD as a scarce good subject to state and common property arrangements. Does the "excessive use" of FAD mean resources wasted by users manipulating the publicly available data in vain attempts to earn higher than normal stock market returns? Does "excessive use" include the failure to experiment, develop, and employ non-free alternatives with potentially greater profitability?

The difference between private and common property rights in FAD as a scarce good may be seen in the different decision behavior of individuals using FAD produced and distributed under voluntary disclosure (implying private property) and mandatory disclosure (implying state property).

The owner of private rights in FAD would be able through voluntary disclosure to prevent other persons from acting in certain ways that would infringe his property rights. Knowing is equivalent to possessing FAD, which means that policing costs to assure exclusive use are likely to be high. For social efficiency, private rights in FAD would require that policing costs after publication be less than the negative effects of illegal use thereby prevented (as with patent law protection). Realistically, private property rights in FAD may be exclusively exercised only if there is a low cost way of keeping knowledge secret (as with

closely guarded trade secrets). But it would not be in the best interest of corporations to keep all FAD secret. Owners of this joint-cost good (for which there may be no explicit market) may realize benefits from disclosure as a form of advertising. The joint benefit of a zero price for FAD may be greater than the transacting and policing costs associated with separate revenue from FAD market exchange. Certainly the aggregate search costs by individual investors are reduced by corporate publication, and this could have a favorable effect on the demand for stock shares. Do firm managers and auditors regard investors as a product delivered to their corporate clients?

To argue for (or against) a change in disclosure "requirements" is to argue for (or against) a change in property rights. As noted above, abrupt changes in legal rules of endowment effect wealth transfers by altering expectations, and lead to different equilibria where transaction costs and policing costs are not zero. At the Constitutional level, this accounting policy problem is part of a broader social issue, namely the private property right to privacy (i.e., voluntary disclosure of information) [Gross, 1971] versus the common property right of the public to know, or the state property right of the government to know (i.e., mandatory disclosure). At the Constitutional level, this issue requires an explicit examination of the criteria for social change: Why would any realignment of property rights be worthwhile? From an efficiency point of view, what are the characteristic behaviors of alternative equilibria where imperfect knowledge, indivisible products, transactions costs, interdependent utilities, heterogeneous tastes and incomplete markets affect both business competition and government control?

ON PARETO-OPTIMALITY

Pareto-optimality is at best a static concept, implying some complete set of individual endowments (property rights) given by social institutions and modified by strictly voluntary exchange in a free market structure of equilibrium prices. Pareto-optimality does not indicate that any normative criterion other than conditional efficiency has been satisfied. [Bator, 1958; Sen, 1970] Pareto-optimality can be defined as any situation from which any move would make at least one individual worse off, where "worse off" is defined as a position that would be voluntarily rejected. Thus a social change would be desirable only if no one would become worse off and at least one individual better off, where "better off" is defined as a position that would be voluntarily chosen.

Pareto-optimality loses its significance when voluntarism is eliminated from exchange and production and some presumptive social welfare function is imposed to constrain some individual preferences in order to "make" someone better off. [Buchanan, 1959, p. 125] There is a difference between arguing that a social welfare function does not exist and arguing that it cannot be determined or constructed under our present state of knowledge. Either way, a presumptive welfare function is likely to be "wrong" in some significant way which can't be known apart from expressed individual choice. Even if we had a social welfare function, it would require some ground for individual utility comparison--the very obstacle that Pareto sought to overcome by his definition of an optimality position. Voluntary unanimity is the only assurance that a change from some social position is toward a Pareto-optimal equilibrium. Pareto developed the concept of optimality for only exchange and production, but not for

p. 366-367, emphasis added]. "Best" may be defined with regard to criteria concerned with either the original endowments structure among persons and groups, the exchange process, or the outcome. Any dissatisfaction with the outcome pattern of wealth distribution can be viewed as dissatisfaction with either the original property rights assignment or the exchange process. Given an endowment that is "equitable" (whatever that may be), voluntary exchange will assure not only equity in distribution but also maximum efficiency in production. Or given an endowment that is "unequitable" (whatever that may be), government control over exchange might be able to secure someone's notion of equity in distribution but only at the (perhaps very high) cost of reduced production.

The social policy choice between (1) reassigning property rights in FAD, (2) controlling disclosure, or (3) directly redistributing outcome (for example through a negative income tax tied directly to personal income from stock ownership) cannot be made on the grounds of Pareto-optimality analysis which (A) takes as given some property rights configuration and voluntary exchange, and (B) accepts the outcome as both equitable and efficient. Knowing the actual operating characteristics of real alternative arrangements is necessary for making institutional choice a rational process. [Demsetz, 1969]

While empirical research into types of FAD and methods of dissemination is necessary, such research into data and disclosure is not sufficient for rational choice among alternative social policies concerning private property rights in FAD. Regardless of whether FAD is generally considered in nature a private or public good, the property rights issue,

distribution which he assumed determinable only through reference to considerations other than economic ones [Pareto, 1971, p. 267]. For Pareto, only private interest is real; public interest is imaginary [pp. 75-76], in part because one man's taste is another man's obstacle [p. 110].

If a contemplated change were endorsed by everyone, then assuming the accuracy of expressed individual preferences, the change would increase efficiency as the free market mechanism allocates resources to attain maximum individual utility. Without revealed preferences, social scientists can never say that one social situation is more efficient for attaining utility than any other (even though it is common for many social scientists and administrators to act as if they presume omniscience and impose their private preferences as constraints on other persons). Naturally, this general statement applies fully to choice among alternative FAD standards and institutions--a policy choice which is substantially a choice among alternative assignments of property rights.

"The preoccupation of traditional welfare theory with static optimization problems and the abstract conditions for [hypothetical] Pareto-optimality has tended to divert attention from [real] institutional considerations." [Furusbotn and Pejovich, p. 172]

The choice of FAD property rights should be made with the "realization that institutional choice involves the comparison of alternative arrangements which are necessarily non-optimal in the [voluntary] sense of Pareto... The problem is to choose from a feasible set of institutional arrangements that particular one which gives the most suitable or "best" allocation of that good under consideration." [David and Whinston,

the sanctioning of behavioral relations, is more fundamental. It should be addressed separately as of paramount importance.

Because it is not necessarily ideal in principle to require explicit market exchange or government control for all goods, the empirical issue involves a comparison of the total effects of different institutional arrangements for dealing with FAD side-effects and indivisibilities.

It is not sufficient in a policy debate to show only that the expectation of ideal government control has some benefit, or even that actual anarchy has some costs. The full comparison should be made between the total effects of different arrangements, with (1) the understanding that state and common property, no less than private property, may lead to external diseconomies; and with (2) the presumption that advocates and opponents speak for the alternative that is in their own self interest. [Watts and Zimmerman, 1978; Benston, 1969; Manney, 1966, 1969, and 1974] The burden of proof should be placed unequivocally upon those who advocate any form of coercive control of FAD by the elimination of private property rights.

SUMMARY PROPOSITIONS

State laws give de facto ownership of corporations to the managers by legal devices such as limited control, limited access to data, limited liability, and limited participation in profit for the investor. [Winter, 1977] Corporate managers have most of the usual behavior prerogatives of ownership (rights to use, manage, lend, abandon, destroy, etc.; and rights to security). Investors really "own" nothing more than their equity shares (rights to transfer, contingent rights to income, and rights to vote). This separation between investors and managers creates the basis for an efficient inequality of information between corporate insiders and outside investors. This FAD inequality gives rise to independent auditing of fiduciary reports.

Alternatives, such as "guarantees, warranties, and other forms of insurance that protect, for a fee, a capital market agent against losses from distorted information, which can be viewed as being analogous to a defective product" [Gonedes, Dopuch and Penman, 1976, p. 102] were not prohibited by law. But the fact that they did not arise as a free market response to the problem of FAD authentication should be taken as some evidence that voluntary auditing is the more efficient solution, with the role of the auditor restricted to attesting that management did what it claimed in FAD to have done. There are grounds for thinking [Benston, 1969a, 1969b, 1973] that mandatory disclosure, with auditors (private or state) controlling what management may choose to do in FAD, is in fact not socially efficient.

"A straight forward criminal enforcement program against fraud may have been more appropriate and less costly than has the so-called

disclosure approach," [Manne, 1974, p. 26] and more in keeping with our private property traditions.

Institutions and standards associated with FAD have become the center of a four-way conflict of interest over property rights: managers, investors, auditors and government regulators. Since the nature of FAD (as private or public good) cannot provide the necessary insight for theory or policy, the remainder of this paper seeks to derive from the perspective of property rights certain propositions relating to:

(1) FAD users, (2) valuation, (3) measurement, (4) FAD changes, (5) welfare, and (6) efficiency; and two hypotheses about the effects of any accounting institution having power to mandate FADs.

Each corporation has a natural lowest cost monopoly over the production of its own unique FAD. The absence of viable competition in the production of firm specific FAD is the reason for independent auditing to authenticate reports. The de facto ownership of FAD by corporate managers is consistent with (1) the labor theory of entitlement [Locke, 1690]; (2) recent court decisions that records are the private property of record keepers [Linowes, 1977, p. 7, citing United States v. Miller 425 U.S. 435 (1976)], and (3) the AICPA position that accounting reports are the responsibility of their clients, corporate managers. If it is true that owners of a good generally are its major users because they have the property rights, then...

1. Corporate managers, rather than outsiders like investors, creditors, and regulators, are the major users of FAD for both internal and external purposes.

Even though FAD is a scarce good, and even though it were seen as potentially useful by both insiders and outsiders, it is not valued on the balance sheet because it does not meet the criteria of "generally accepted accounting principles" for assets, namely: (1) FAD is internally generated, (2) it has zero allocated joint production cost, and (3) it has no market price. But there is no analytical ground for distinguishing between products and side-effects, and therefore no analytical ground for either excluding or including in FAD any non-marketable goods. If there can be no non-arbitrary basis for recognizing and valuing non-market goods (including FAD), then...

2. Pragmatic emphasis on verifiable, objective market transactions as the basis for both recognition and valuation in FAD is sound.

If this is true, then assertions of "present values" and "social indicators" as part of FAD should be viewed with grave skepticism.

No attribution of monetary value can represent an inherent characteristic of either (1) separately disposable assets, (2) separately extinguishable equity claims, or (3) or the organization as a separate entity. Monetary magnitudes are at best dated market relations in which owners voluntarily contract for the exchange of some property right(s) where money reduces private transaction costs below what would prevail in a barter economy. Incurable allocations over time periods and products make accounting numbers an index of market relations--not a measure of things. These allocations are justifiable not at all by a priori criteria, but only by reference to pragmatic criteria. If all production is joint, if monetary costs are allocated over only a (perhaps

small) marketable subset of the identifiable products (physical, pecuniary, and physic), and if value relates to property rights rather than to the nature of goods, then...

3. Accounting cannot comply with the requirements of measurement theory (such as extensivity and additivity) and so cannot be a measurement science.

Before mandating any non-compensated (Michelman, 1968) wealth redistribution in the form of reassigned property rights, the rational dictator (no matter how selected or how benevolent) would demand research into the (most likely) effects from revising endowments and constraining voluntary market readjustments. "Clearly the SEC's favorite argument: without mandatory disclosure the public would lose confidence in the securities markets and refuse to invest in American industry...rests on the totally unverified and even illogical notion that fraud and deception, not financial losses, drove the public out of the market after October 1929...The SEC's confidence argument has some of the characteristics of a confidence game." [Manne, 1974, p. 64] If FAD affects stock prices, and if the stock market is efficient in a Pareto-optimal sense, then...

4. Any change in the published FAD system will make someone worse off.

For a rational choice of social policy change, we need to know precisely who will be harmed by changing the property rights in FAD; who (if any) will be helped, in what way, and by how much.

If the stock market is efficient, then FAD is economically worthless as common property for trading purposes. Since generally accepted accounting principles are based on historical costs, FAD may have little worth as private property for decisions that depend upon forecasts and future implementation. Whether FAD (as private or common property) is useful for production (as private or public good), if FAD is not a consumption good, then...

5. Reassigning property rights in FAD as a means of welfare redistribution is at best an inefficient way to reduce inequality of consumption between the "rich" and the "poor".

If that is true, then equity arguments by the SEC and FASB that tend to support mandatory disclosure rules on the grounds of welfare transfer are misplaced. The "equal access" argument overlooks (1) the fact that reducing ignorance is costly, and (2) the probability that information inequality is socially efficient.

The fact that private property rights do have social consequences is not sufficient reason for advocating either common property rights in FAD or state property regulation of FAD production and distribution. If private property rights in FAD were not violated, then the choice among accounting alternatives would be strictly private (subject, of course, to tort and criminal laws governing fraud, deception, etc.). This pluralism in the market place for financial ideas about accounting data would maintain the necessary conditions and incentives for experimenting with various monetary indices. This would foster a healthy skepticism about the "useful meaning" of accounting numbers. Each

corporation would be free to perform its own cost/benefit analysis of accounting alternatives with effective emphasis on economizing scarce resources. But if subjected to ideological determination by hard core metaphysical "beliefs" of accountants, then...

6. State or common property rights in financial accounting data with mandatory disclosure and uniform standards will be wastefully inefficient and ineffective.

If these six propositions are accurate, then it is likely that relevant empirical research to permit total benefit/cost comparisons among alternative actual institutional arrangements for financial accounting data would confirm the following hypotheses. Non-voluntary increases in accounting disclosures, whether imposed directly by SEC or indirectly through FASB-AICPA, will effect this illfare tradeoff:

- 7a. The mandatory increase in demand for strictly monitoring services will make accountants and regulators better off.
- 7b. The increased direct costs, both private and public, and the production opportunities foregone by resource reallocation, will make corporate managers, investors, and the public at large worse off.

CONCLUSION

The nature of FAD as private or public good has not provided the necessary insight for developing accounting theory to resolve the crisis of accounting standards and institutions. Property rights, defined as sanctioned social and economic behavior relations among persons specifying what individuals may do with things, emphasizes the difference between private and state or common property rights. Recent developments of property rights literature in law and economics suggest that ideological unformation is likely (1) to expand FABLES about the merit of common property, and (2) to eliminate private FADS. The result will be uncentive effects of an illfare state. If a free market economy is to survive, the full burden of empirical proof must be placed squarely on those who advocate reducing private property rights and constraining voluntary decisions. Thus far this burden has not been carried by the SEC/FASB/AICPA power proponents. Has our ideology shifted so far from freedom to control that proof is not required?

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