Pragmatic theories

Descriptive pragmatic approach:
• based on observed behaviour of accountants
• theory developed from how accountants act in certain situations
• tested by observing whether accountants do act in the way the theory suggests
• is an inductive approach

Pragmatic theories

• Criticisms of descriptive pragmatic approach:
  — does not consider the quality of an accountant’s action
  — does not provide for accounting practices to be challenged
  — focuses on accountants’ behaviour not on measuring the attributes of the firm
Pragmatic theories

Psychological pragmatic approach:
• theory depends on observations of the reactions of users to the accountants’ outputs
• a reaction is taken as evidence that the outputs are useful and contain relevant information

Pragmatic theories

• Criticisms of the psychological pragmatic approach:
  – some users may react in an illogical manner
  – some users might have a preconditioned response
  – some users may not react when they should

• Theories are therefore tested using large samples of people

Syntactic and semantic theories

• Semantic inputs are the transactions and exchanges recorded in vouchers, journals and ledgers

• The inputs are then manipulated on the basis of the premises and assumptions of historical cost accounting
Syntactic and semantic theories

• Criticised because there is no independent empirical verification of the calculated outputs

• The outputs may be criticised for poor syntax inaccurate e.g. different types of monetary measures are added together

Syntactic and semantic theories

• The outputs may be syntactically accurate but nevertheless be valueless due to a lack of semantic accuracy (a lack of correspondence with real-world events, transactions or values)

Syntactic and semantic theories

• Historic cost accounting may produce ‘accurate’ outputs but which nevertheless have little or no utility

• That is, they are not useful for economic decision making except to verify accounting entries
Normative theories

• 1950s and 1960s ‘golden age’
  – policy recommendations
  – what should be
  – concentrated on deriving:
    • true income (profit)
    • practices that enhance decision-usefulness
  – based on analytic and empirical propositions

Financial statements should mean what they say

Normative theories

• True income:
  – a single measure for assets
  – a unique and correct profit figure

Normative theories

• Decision usefulness:
  – the basic objective of accounting is to aid the decision-making process of certain ‘users’ of accounting reports by providing useful accounting data
**Normative theories**

The decision process

- Accounting system of company X
- Prediction model of user
- Decision model of user

**Positive theories**

- Expanded during the 1970s
- Based on ‘experiences’ or ‘facts’ of the real world
- Explain the reasons for current practice
- Predict the role of accounting information in decision-making

**Positive theories**

- The main difference between normative and positive theories is that
  - normative theories are prescriptive
  - positive theories are descriptive, explanatory or predictive
Different perspectives

• Scientific approach:
  – has an inherent assumption that the world to be researched is an objective reality
  – is carried out by incremental hypotheses
  – has an implied assumption that a good theory holds under circumstances that are constant across firms, industries and time

Different perspectives

• Criticism of the scientific method:
  – large-scale statistical research tends to lump everything together
  – it is conducted in environments that are often remote from the world of or the concerns of accountants

Different perspectives

• Naturalistic approach:
  – implies that there are no preconceived assumptions or theories
  – focuses on firm-specific real-world problems
Different perspectives

• Alternative ways of looking at the world:

**CATEGORY ASSUMPTION**
1. Reality as a concrete structure
2. Reality as a concrete process
3. Reality as a contextual field of information
4. Reality as a symbolic discourse
5. Reality as a social construction
6. Reality as projection of human imagination

Different perspectives

• For categories 1 – 3 it is more appropriate to use the scientific approach

• For categories 4-6 the naturalistic approach is more appropriate

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Different perspectives
Scientific approach applied to accounting

Misconceptions of purpose
- Make scientists out of accounting practitioners
- Researchers = practitioners
- The desire for ‘absolute truth’

Scientific approach applied to accounting
- The scientific method does not claim to provide ‘truth’
- It attempts to provide persuasive evidence which may describe, explain or predict

Issues for auditing theory construction
- Auditing is a verification process that is applied to the accounting inputs and processes
Issues for auditing theory construction

• Auditors provide an opinion on
  – whether the financial statements accord with the applicable reporting framework
  – whether the statements give a true and fair view

• The normative era of accounting coincided with a normative approach to auditing theory
• The positive era of accounting has led to a positive approach to auditing theory

Summary

• Many different approaches to theory formulation in accounting
• Evolution of accounting theory
  – positive v. normative
  – scientific v. naturalistic
Key terms and concepts

- Descriptive pragmatic approach
- Psychological pragmatic approach
- Syntactic and semantic theories
- Historical cost accounting
- Normative theories
- Positive theories
- Scientific approach to theory
- Naturalistic approach to theory
- Auditing theory