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Abstract

This article examines the evolution of practice strategy and organizational structure at the US accounting firm Lybrand, Ross Bros. & Montgomery from its inception in 1898 through to its merger with Price Waterhouse in 1998. We focus on the interaction between the firm and its broader economic, social and political contexts as we analyze key drivers of organizational change. The accounting enterprise developed a dual strategy involving both horizontal integration and service diversification for adapting successfully to changes in markets, professional knowledge, technology and regulation. Organizational learning was fundamental to its successful evolution in scale and scope as it enabled the firm to develop strategies and structures that responded effectively to changing external challenges and opportunities.

Keywords

Coopers & Lybrand, historical case study, horizontal integration, organizational learning, service diversification, theory of the firm

1. Introduction

The historiography of accounting, unlike its first cousin business history, has not addressed the problems of a theory of the firm. Scholars have failed to explain the evolutionary factors leading to the market concentration that characterizes the modern profession. This is surprising given both the

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business and professional literature on the shaping of modern society, surprising also because the historical development of major accounting firms provides insight into the development of accounting itself. Multinational firms are where “accounting practices emerge, become standardized and regulated, where accounting rules and standards are translated into practice, and where professional identities are mediated, formed, and transformed” (Cooper and Robson, 2006: 416).

Our study examines the evolution of the venerable US firm of Lybrand, Ross Bros. and Montgomery through to the twentieth century. In identifying the key drivers of organizational change, we focus on the interaction between the firm and its broader contexts. In the first half of the firm’s life this context was primarily American, and so generalizations made about this timeframe may not reflect the experience of the international accountancy profession. However, as the twentieth century progressed, business in general became globalized, and members of the accounting profession who served international clients faced similar challenges. Without addressing the problems which confront firms operating under multiple regulatory bodies, we nevertheless argue that success in the formation of a practice of great scale and scope depended on the firm establishing responsive organizational structures and on professional strategies to confront changes in markets, regulation, technology and professional knowledge. Beginning with its founding in Philadelphia in 1898, we trace the firm’s history until its merger with Price Waterhouse & Company in 1998 and consider briefly the impact on practice organization of subsequent environmental changes.

The remainder of the article is in six sections. Section 2 discusses the principal schools of thought about organizational change that informs our analysis. Section 3 focuses on the founding of the firm in 1898 through the passing of the last of the original partners in the 1950s. Growth resulted from horizontal integration across a national market and from service diversification based on accounting and information systems. Increases in the size, scope and complexity of major clients in a dynamic economy provided strong incentives for strengthening practice competitiveness through the expansion of internal knowledge capabilities. This trend was reinforced by the expansion of the federal government’s role in regulating national economic affairs through the advent of such policies as income taxation in 1913 and securities market oversight in 1933. Growth in the range of requisite knowledge from these and other developments created pressures for practice expansion to spread the burden of these overheads over a larger operating base. This led ultimately to greater market concentration as the leading professional units grew either through new local office openings or the acquisition of established firms. Section 4 analyzes the second era, spanning the years from 1957 to 1980 during which period accountants’ services responded to the new forces of global competition. Foremost in this regard was the union with Cooper Brothers, a leading British practice, which vastly increased the firm’s international service capabilities. The period was also marked by continued concentration in domestic markets and by enhanced diversification into management consulting. Section 5 examines the third era, 1980–1998, during which the firm pursued new opportunities in consulting that arose in part from advances in information technology (IT). However, new crises that broadly affected the entire profession of public accountancy led to regulatory intervention in order to maintain auditor independence and to assure engagement effectiveness. This led to the curtailment of diversification and reinforced the firm’s position in traditional attestation and assurance markets through a merger with Price Waterhouse & Company. Section 6, the concluding section, places our analysis within a brief historical model of large accounting firm growth.

2. The framework of organizational analysis

Our study draws on scholars whose work has materially advanced organizational theory including Alfred D Chandler, Louis Galambos, Douglass C North, Richard R Nelson and Sydney Winter.

Their contributions examine large-scale organizations' role in transforming American polity from rural-agricultural to urban and industrial. New entities of great scale and scope coordinated and controlled many interdependent elements to assure the smooth integration of a complex socio-economic environment.

Our analytical framework is linked directly to business history, a specialization that came to new prominence in the 1960s when Chandler began to extend the understanding of the role of giant enterprise in US industry. Chandler's contribution has three aspects. The first (or Chandler I), focuses on the dynamics of oligopolistic competition in the US and Europe. In his classics, *Strategy and Structure* (1963) and again in *Scale and Scope* (1980), Chandler's synthesis is at variance with the then regnant neoclassic model, that is, an economy composed of many small, price-taking units with very limited market power. Chandler, instead, emphasizes the role of the few center firms that accounted for the research and development and capital investing which were the primary sources of wealth enhancement in advanced economies. Special advantage also accrued to first movers who could dominate a market by exploiting economies of scale and scope, thus creating barriers to entry for later entrants. Unlike traditional price-taking firms, center firms exercised market power and competed on the basis of product or service differentiation. The advantages of these firms stemmed from their ability to exploit economies of scale and scope.

Chandler II extends understanding of organizational sociology through the rise of a class of business managers in the Pulitzer Prize winning *The Visible Hand* (Chandler, 1977). The findings of this work stands in contrast to that of the earlier school of Progressive History of Beard, Parrington and Turner who, while admitting big businesses' contribution to material improvement and higher living standards, worried that such a concentration of economic power might prove corrosive to the cherished democratic values on which the nation had been founded (Hofstadter, 1968). Chandler presents an alternative view of business professionals as economic rationalists intent on new modes of management and technology in the quest for industrial leadership and stability and the efficient allocation of scarce economic resources (Chandler, 2001: chap. 1).

Chandler III (2001, 2005) becomes increasingly sensitive to the literature on organizational learning emphasized by Nobel Prize winning scholar, Douglass C North, who perceives the learning process as a major driver of business change (North, 1990). His nexus is institutions, which are the rules that guide human agents working in economic units. The lessons learned in the enterprise's recent history shape future actions when they become institutional practices that order firm activities. Defining what succeeded in the past and should be perpetuated and what failed and should be avoided helped to define best practices in confronting business risk and optimizing resource utilization. North argues that the firm's capacity to absorb and adapt useful knowledge functions is a major determinant of competitiveness. Chandler's later work also increasingly responds to the scholarly agenda of the rising field of evolutionary economics pioneered by Richard R Nelson and Sidney G Winter (1982). The evolutionists stress the importance of firm-specific learning and innovation in understanding what competitive factors in individuation explained the long-term industrial leadership, especially in high-growth sectors.

In Chandler III, the traditional organizational emphasis is broadened by new linkages to learning that strengthened corporate competitiveness over time. Focusing on the firm-specific factors that conditioned the long-term global leadership in two high-tech industries (electronics and chemicals and pharmaceuticals), Chandler argues that market leadership is not solely a function of scientific discovery, but also requires organizational changes to support the requirements of new markets and products. This involves integrating: (1) technical knowledge (product creation); (2) functional knowledge (marketing and production); and (3) high-level managerial knowledge to coordinate and control corporate resources and operations by forming strategies, defining broad policies and evaluating performance.

Recent years have seen challenges to the Chandlerian models I and II (but not III) that emphasize the role of large, vertically and horizontally organized firms in transforming the American economy. In particular, Lamoreaux, Raff and Temin (2003) have criticized this model for its purported “Whigishness”, the sense that the rise of these center firms was an inevitable step on the road of business evolution. Instead, these researchers have pointed out alternative structures that succeeded as carriers of economic progress, such as the Chicago Board of Trade that facilitated the growth of the wheat trade, or the formation of “industrial districts” where many small-scale manufacturers operated in close physical proximity. They are especially dismissive of the contemporary importance of such large, vertically integrated firms, stating that “during the 1990s, as giant managerial enterprises (especially in the U.S.) gave way to more specialized, less vertically integrated competitors, the Chandlerian paradigm lost much of its luster” (Lamoreaux et al., 2006: 20). Though Lamoreaux and her co-authors note that other coordinating structures have arisen to handle the costs of information asymmetry in complex transactions, nevertheless the dominant form of organization for accounting professionals, over the twentieth century and into the twenty-first, appears to conform to the Chandlerian model: the industry has become dominated by large international firms offering clients a multitude of services.

In addition to organizational learning, factors that have shaped the evolution of professional and industrial entities are derived from their complex socio-political environments that influence the development options they pursue. These factors have been blended in two models advanced by Louis Galambos, known respectively as, the “organizational synthesis” and “triocracy” (Galambos, 1970, 1983, 2005). Defined in three essays, the most critical component of organizational synthesis from the perspective of our article identifies elements affecting a society dominated by large organizations: technology, the political economy and professionalization. These forces are significant not only to understanding the evolution of large-scale industrial enterprises but also in explaining the dynamics of giant knowledge-based businesses that came to dominate the service sector. In the latest iteration of this model, Galambos (2005) also includes globalization as a major factor in organization design. Within the accounting profession itself, some practitioners have suggested that globalization may become the most important factor influencing the accounting profession in the future.¹

Galambos’s notion of triocracy, on the other hand, looks to the New Institutionalism in political science as analyzed by Stephen Skowronek (1982) to illuminate government relations with giant business enterprises in a mass society. The triocratic model analyzes interactions among professional and business groups, governmental bureaucratic agencies and representative bodies, such as the US Congress, in establishing public policy. Triocracy, thus, serves as a construct for evaluating the public opinion on the oversight of business and professional groups. It predicts, for example, that during normal times professional and business groups enjoy a high degree of autonomy over their affairs because of deference to agents responsible for maintaining stability and protecting the public interest. However, socioeconomic flux leads to intervention on the part of government bureaucracies as the public turns to their political representatives for relief.

Thus far, accounting history has not utilized Chandler, Galambos, North or evolutionary economists to explain the significance of the rise of giant, global practices. Instead, historians have focused on a wide range of themes such as the evolution of methodology (Wootton and Kemmerer, 2007; Yamey, 1978), the impact of measurement practices on decision processes (Brief, 1966; Johnson and Kaplan, 1987), the rise of professionalism (Cooper and Robson, 2006; Previts and Merino, 1998; Walker, 1988; Zeff, 1966) and the role of accounting in socio-cultural evolution (Fleischman and Tyson, 1998; Neu and Graham, 2004; Saravanamuthu and Tinker, 2003). Moreover, the early practice-sponsored historical chronicles neither sought to amplify the theory of the firm nor explain how their experience provides useful insight into epochal developments.

Instead, they focused narrowly on high points in organizational change (Arthur Young and Company, 1948; DeMond, 1951; Ernst and Ernst, 1960; Haskins and Sells, 1935, 1947, 1970; Wise, 1982). Other works were essentially biographies of key leaders (Higgins, 1965; Jordan, 1923; May, 1936; Montgomery, 1939). However, later studies began to appear in the 1980s that provided deeper insight into the dynamics of firm growth. Studies by historians such as Edgar Jones (1981) and David Grayson Allen and Kathleen McDermott (1993) have raised the quality of practice analysis. They provided a much richer contextual analysis that stressed how practice growth became closely integrated with changing patterns of economic development and corporate governance.

The evolution of Lybrand, Ross Bros. & Montgomery stresses organizational learning in firm growth; however, the models, particularly of Chandler and the evolutionary economists, require some modification. Unlike high-tech manufacturers, accounting firms could not expropriate legal rights to competitive knowledge through patents. Innovation in public practice did not create legal barriers to block the market entry of competitors. Instead, innovation took the form of applying common bodies of knowledge for a complementary core of services including auditing, tax and management consulting, to serve informational needs. This differentiated a practice by enhancing its reputation for technical proficiency. Second, innovation helped advance particular firms when their members were perceived as leaders in determining how professional knowledge should be standardized for practice. The firm's image of authority benefited from defining how knowledge should be applied. Third, the cost structure of large professional practices differed in significant ways from large industrial businesses. Because of the heavier dependence on the work of human agents rather than on machinery and other capital assets, accounting practices were characterized by a high variable cost structure. Consequently, the ability to achieve economies of scale through increases in throughput was very limited. However, the establishment of large networks of local offices afforded the opportunity for accounting practices to benefit from economies of scope. Large office networks facilitated the ability of firms to serve the giant enterprises that were transforming the global economies. Broader scope was also advantageous for forming connections with potential clients, regional economies and industries. Fourth, bigness enabled leading firms to bear the high overhead costs that helped to distinguish their practice, especially the costs of engaging and training high-quality personnel. It also spread the burden of high overheads associated with participation in associational and governmental affairs and supporting publications that underlined the organization's special competencies.

3. Horizontal expansion in a continental market, 1898–1957

The late 1800s and early 1900s saw the beginning of the accountancy profession in the US; early accounting firms frequently relied on the skills of expatriate British accountants to establish themselves (Miranti, 1990). The firm of Lybrand, Ross Bros. & Montgomery, however, was an exception in that all of its founding partners were native-born Americans. The formation of the partnership in Philadelphia in 1898 occurred amidst the expansion of a new urban-industrial economy and the rise of the profession of certified public accountancy. Accountants in New York, for example, had successfully militated for the passage of the first CPA licensing law in 1896. Five years later, the House of Morgan launched the United States Steel Company, the nation's first billion-dollar business.

The corporate and professional transformations created significant asymmetries and the need for more comprehensive and standardized business information to inform managers, investors and other stakeholders. The establishment of a national income tax and central bank, the expansion of the national defense establishment, and the formation of administrative agencies to monitor

activities in a host of industries created new opportunities for accounting-based compliance and planning services. Investor concerns about informational reliability and objectivity fostered the growth of audit and assurance services, initiatives that became deeply entwined in the fabric of corporate governance under the requirements first of individual securities markets and later of the Securities Acts of 1933 and 1934.

During this era of expanding opportunity, forward-looking public accounting practices including the Lybrand firm grew through diversification related to the application of accounting knowledge. First, auditing used accounting knowledge in examinations to assess the fairness of client financial reporting. Second, taxation involved the use of accounting knowledge to allow corporations and individuals to comply with federal, state and local imposts. Third, management advisory services primarily helped clients develop more effective accounting systems. The latter service, however, was recognized early as a potential conflict of interest in auditing if system advice trailed off to controllership. In fact James O McKinsey, who originally practiced public accountancy along with his teaching duties at the University of Chicago, may have eventually decided to focus exclusively on consulting in part to avoid any such conflicts.

The Lybrand firm developed early a local office network to serve clients. Very few contemporary rivals sought growth through horizontal integration to the same degree as that experienced by the Philadelphia practice. Table 1 details the firm's domestic expansion through the 1960s.²

In some cases, local office expansion was achieved by the acquisition of established practices such as the firms of Peter and Moss in Dallas or Klink, Bein & Company in Los Angeles (*L.R.B. & M. Journal*, 1925, 1934). Serving as a correspondent in distant markets for local firms also created opportunities for growth through merger. In this latter case, a second office in New York

Table 1. Expansion in US cities, 1902–1962.

Year opened	City
1902	New York
1908	Pittsburgh
1909	Chicago
1915	Boston
1919	Washington, DC
1920	Detroit
1923	Cleveland, Cincinnati
1924	Baltimore, Los Angeles, San Francisco
1926	Newark
1929	Rockford (IL)
1930	Atlanta, Dallas, St Louis
1931	Louisville
1932	Houston
1948	Seattle
1952	Tulsa
1953	Birmingham
1958	Hartford
1959	Portland (OR)
1960	Phoenix
1961	Columbus (OH)
1962	Fort Wayne, New Haven, Niles (IL), Oakland (CA), Portland (ME), Salt Lake City, Springfield (MA)

eventually resulted from the absorption of Hilditch & Company that maintained a midtown office on Madison Avenue (*L.R.B. & M. Journal*, 1928). In addition, Lybrand maintained small representative offices in London, Paris and Berlin (until 1938). All of this merger activity, however, was dwarfed by the impact of the union with Coopers Brothers in 1957 that vastly increased the firm's international practice.

The increased geographic scope that resulted from the creation of the nationwide network created several advantages for the firm. The first was the reduction in overall practice risk due to diversification across major regional economies and industries. Exposure to risk resulting from local downturns or recessions in specific industries was offset through the business vibrancy of other segments of the national client portfolio. The opening of a New York office in 1902, for example, was propitious because it drew the Philadelphia firm closer to the leading practices in the profession that were largely New York based. Besides being the fastest growing of the East Coast cities during the first three decades of the twentieth century, New York's financial service and retail industries provided great demand for accountants' services. The cities of Detroit, Pittsburgh and Cleveland served the requirements of the fast-growing automobile market in which Ford Motor Company was a major client. The economic fate of Dallas reacted to developments in the oil industry. Los Angeles brought the firm close to developments in the movie industry.

Moreover, broad geographic scope made it possible for the firm to serve giant clients whose operations were spread across the nation, thus eliminating the need to negotiate with correspondent accounting firms to do part of a professional engagement. Maintaining complete control over an engagement helped reduce risk by providing assurance that the fieldwork and reporting services conformed to the firm's high standards. The best example of this was the relationship with the American Telephone and Telegraph Company (AT&T) and its regional operating subsidiaries. Although the parent company was based in New York, its "Long Lines" operation provided long-distance service throughout the country. Its research arm, the Bell Telephone Laboratories, also operated as a separate subsidiary. AT&T operated through a host of regional subsidiaries spanning the country. In addition to consolidated statements, the Bell System companies frequently issued their own financial reports.³

The office network also helped reduce information costs through internal communications between offices. This form of business intelligence could be very useful to the accounting firm's partners and clients. Such connections served as informal channels of knowledge about regional and national economic industrial trends. In addition, the local office structure increased the leverage of the firms in professional governance and associational activities. Local office members increased the influence of the firm by pursuing positions of leadership in state associations and professional oversight boards. Successful activism on the state level also often translated to leadership in national associational affairs.

In a period when advertising was prohibited, the existence of many local offices indirectly served to promote the firm's image and prestige in the eyes of the public. Although Lybrand, Ross Brothers & Montgomery did not become a brand recognized in every household as was the case with such consumer giants as General Motors or Philip Morris, it was well known by the end of World War I to leaders in business, education and government.

The establishment of a network of local offices provided an opportunity for the firm to leverage competencies developed in a single market area to a broader national or regional market for professional services. An early example of this was the Lybrand firm's development of deep industry expertise in retailing. The initial nexus came through the acquisition of the giant Wanamaker's Department Store in Philadelphia as a client. This connection was partially the result of Robert Montgomery's personal contact made through military service in the unit commanded by John Wanamaker's nephew, Barclay Warburton, during the Spanish-American War (Montgomery, 1939:

chaps 1–4). The internal service capabilities developed through this client linkage provided a knowledge base for the further expansion among the emergent, large store organizations primarily in cities on the East Coast. In future decades Lybrand included within its clientele such prime names as Associated Dry Goods, the Hecht Department Stores, Stern Brothers, Lord and Taylor, Lane Bryant, Coward Shoe Company and the specialist delivery enterprise, the United Parcel Service (Bell, 1959: 68–70, 72–76, 93–97, 122–156).

Retailing further strengthened the firm because it encouraged greater internal diversity that facilitated its ability to attract clients from a broad range of social backgrounds. Most significant in this early period was the positive relationship that the firm established with Jewish entrepreneurs who played a leading role in the transformation of mercantile endeavor. The connections with these clients were made firmer by engaging staff to serve them that shared a like cultural heritage. Partly because of this, by the 1930s men of Jewish faith would rise to partnership status. This differentiated Lybrand from most of the other leading national practices of this era whose leaders predominantly shared a White-Anglo-Saxon-Protestant background. This early model of practice growth through greater inclusiveness continued in the future. It would serve the firm well as its mix both of staff and clients became more reflective of the cultural and gender diversity of the local, regional, national and ultimately global markets that it served.

Larger clients also benefited from scope economies made possible through the local office network. Large, multi-location clients benefited from lower contracting and coordination costs associated with the provision of major services such as auditing. Clients could also derive useful business intelligence because of the practice's broad knowledge of industries and regions. Since size became equated with professional excellence in the public mind, client reputation also benefited from association with a highly respected, leading accounting firm. Also, large practices serving national markets incorporated a broader range of expert skills in accounting and allied fields for resolving the complex reporting problems that often confronted clients operating on the cutting edge of developments in technology or management. Finally, broad scope facilitated the development of specialized industry knowledge.

Local offices subsidized the national office which supported publications bolstering the firm's reputation as a source of authority and training that helped to assure practice excellence. These initiatives responded both to changes in markets and regulation. In the earliest of these ventures Robert H. Montgomery published the first American text on auditing and, after World War I, annual compendia on many aspects of federal income and estate taxation, the latter volumes continued by his partner, Walter Staub.⁴ The firm scored another triumph in launching partner Louis H Rappaport's *SEC Accounting Practice and Procedure* (1956). Many partners contributed technical articles to professional journals. As early as 1916, the firm began to consolidate training by holding summer staff training programs for junior accountants. In 1920, publication began of the *L.R.B. & M. Journal* which provided news of the firm, discussions of technical accounting matters and economic trends for the edification of staff and clients.

The costs of senior partner participation in associational affairs – involvements that gave the firm voice in debates about the direction of accounting professionalism – could also be subsidized in part by the local offices. Robert Montgomery, for example, twice served as president of the national representative association. His leadership was also critical in reuniting a profession in the 1930s which had polarized because of the competing ideas about the nature of accounting professionalism during the previous decade (Miranti, 1990). The firm's image as a bastion of technical leadership was further augmented by senior partner service on committees responsible for defining accounting and auditing standards.

The contribution of local offices similarly facilitated the participation of senior managers in government service, which not only strengthened the firm's reputation but also gave rise to

tangible benefits in the form of new client acquisition. Again Robert Montgomery was a prime exemplar. Through his service on the War Industries Board in World War I, Montgomery developed a close relationship with, among others, financier Bernard Baruch and Walter S. Gifford, later president of AT&T, a firm that after the war became a major client. Montgomery later played a leading role at the National Recovery Administration during the New Deal.

The strategy, based on extensive horizontal integration and a moderate degree of service diversification, served the firm well into the 1950s. With the passing of the last of the original partners, Montgomery in 1953, a new generation of leaders continued to build on the strong foundations created in the past, while also confronting new challenges associated with the steady trend toward economic deregulation and globalization.

4. Globalization, competition, and practice concentration, 1957–1980

After World War II, American businesses expanded both domestically and internationally. Lybrand management recognized that audit firms needed to mirror this growth, or their clients would go elsewhere. Growth could occur either organically, through greater hiring and in-house development of staff, or through mergers, and Lybrand pursued both. In the 15 years beginning in 1954, the firm expanded into 40 additional cities and tripled its personnel (Jennings, 1998: 26). In a 1997 interview, former Coopers and Lybrand (C&L) managing partner Eugene Freedman (1991–1994) was asked what were the three main factors that transformed the profession of public accounting over the span of his career in the post World War II era. He identified increased competition, international growth, and the advent of computer technology (Freedman, 1998: 2–5). These factors, moderated by regulatory adjustments, influenced the changing face of the Lybrand firm in the 1950s through the 1970s.

In the US, the desire of the senior partners of many successful regional firms to liquidate the equity that had built up over the course of a half-century of growth provided an opportunity for Lybrand to round out its national presence and industry exposure. This perspective was demanded by clients who were growing nationally. As an example, one client, the paper manufacturer Crown-Zellerbach, started as a West Coast firm, then expanded east. In response, merger partners were sought in order to provide a regional presence – for instance, the 1958 acquisition of King, Mahony & Arner which brought Lybrand into Florida, and the Baker & Gillette merger in 1965 which brought Lybrand to the Hawaiian Islands (Warner, 1998: 6). Mergers with other accounting firms also brought in personnel with sought-after skills. The Thomas and Moore merger (1957), for example, brought in expertise in supermarkets and the metals industry (Warner, 1998: 5); metals expertise was consolidated when Lybrand merged with Loomis, Suffern & Fernald the following year. Similarly, the 1962 merger with Scovell, Wellington & Co. not only made Lybrand 20 percent larger (*New York Times*, 1962), but it increased the firm's consulting base, especially in engineering.⁵

Even more striking was the firm's international growth, which responded to the increasing globalization of business. While companies throughout the world were expanding internationally, American investments abroad outpaced all others, doubling from 1950 to 1957 (*L.R.B. & M. Journal*, 1957). This pushed Lybrand to provide global services; sometimes the overseas work could be done by local associates, sometimes not. Ford, for example, demanded that all locations, whether in America, Europe or Asia, be served by the same audit personnel. Even without such stringent staff continuity requirements, overseas clients meant overseas travel. Lybrand personnel headed off to Hong Kong and Sumatra to audit Bechtel; work for Aramco required travel to Saudi

Arabia; the Morrison, Knudson audit required staff go to Morocco; and for Sun Oil the firm audited operations in Mexico, Germany, Austria and Greece (Cranz, 1998: 21).

One way to cut down on costly travel and achieve a local presence was by establishing offices overseas; indeed, Lybrand already operated offices in London and Paris.⁶ However, this approach had its own set of problems. It required high outlays of capital and demanded facility in local languages. Culturally, there was often resistance to “American style management” overseas (Scanlon, 1998: 8). These problems were addressed by entering into partnership with an existing firm abroad.

On both sides of the Atlantic, accounting firms recognized the need to develop partnerships with their overseas counterparts.⁷ As part of an effort to aid such cooperation, the American Institute of Accountants’ (AIA’s) membership voted in 1947 to recognize parallel regulatory bodies in other nations as “international associates” of the association. This allowed members to rely upon the credentials of overseas professionals with training equivalent to that of a CPA (Carey, 1970). While this was a valuable step forward, it still left to the individual practitioner or firm the problem of identifying and developing relationships with suitable overseas professionals. Lybrand’s managing partner, Alvin Jennings (1953–1962), wondered if there was a more efficient way to handle such relationships, and in 1955 Jennings approached Greville Gidley-Kitchin, the partner in charge of the New York office of the British firm Cooper Bros., about possible collaboration. Two years later, their talks led to the formation of the international firm, Coopers & Lybrand.

Cooper Bros. had begun its existence as an accounting partnership in 1854. A UK firm, Cooper Bros. had offices in several European and African countries⁸ and working relationships with firms in Canada, Australia and New Zealand. In Canada, the relationship was with the McDonald, Currie⁹ partnership. This latter firm became the third partner in the 1957 merger that created the global accounting firm Coopers & Lybrand (C&L).

Prior to the merger, Cooper Bros and Lybrand had not had routine working relationships with each other, but the firms did share similarities that enhanced the likelihood of successful collaboration. Both firms had long traditions of contributing to the development of the profession by the production and dissemination of professional literature. They shared a strategic vision – the need to develop global accounting services—as well as an interest in developing consulting services. The British firm’s Management Consulting Services (MCS), begun in 1954,¹⁰ had a heavy emphasis on data processing, which was also an area of interest for the Lybrand partners. After the merger, US-based personnel traveled regularly to the Cooper Bros. offices in Britain to learn about their consulting and actuarial practices (Holland, 1998: 31).

Early on, the merger created shared knowledge and relationships rather than a blended enterprise. As the merger’s architect stated, “It was not intended that the international firm should itself practice accounting. Its function was to serve as the agency to coordinate the standards of the practice of the participating firms” (Jennings, 1998: 27). The name “Coopers & Lybrand”¹¹ was initially reserved to indicate work referred from one of the three founding firms to another. Three distinct identities remained until 1973, when Coopers & Lybrand was adopted as a single firm name.¹² Each part of the triumvirate oversaw activities in different geographic regions: Lybrand & Ross in the US, Latin America and Japan; Cooper Bros in Europe, Africa and the Middle and Far East; McDonald, Currie in Canada and the Caribbean (Hobson, 1979: 30). The existing Lybrand & Ross operations in both London and Paris were essentially shut down, with responsibility for these clients transferred to Cooper Bros.’ partners. Meanwhile, the work of Cooper Bros. in New York shifted to the Lybrand office.

At the time of its initial formation, the international firm operated in 19 countries with 89 offices. By 1979, the numbers had increased to 89 countries with 360 offices (Hobson, 1979: 34). The expansions represented both mergers – initiated by all three of the founding firms – and newly established offices. Two prominent international mergers also occurred in 1957, the year the

international firm was formed: Despacho Robert Casa Alatraste in Mexico and Treuhand Vereinigung in Germany. In the following year, an Australian merger was effected with Buckley & Hughes.¹³

In addition to global expansion, the post World War II period also saw a marked increase in scope of services, particularly the provision of consulting services. This trend responded largely to a growing client interest in accounting automation through electronic data processing. In the US, Lybrand had entered the 1950s officially providing only audit and tax services; unofficially, it had provided its clients with consulting services for years. Indeed, Vincent O'Reilly, one-time Chief Operating Officer and vice-chairman (1994–1997), declared that “the first services that audit firms rendered were consulting services...” (O'Reilly, 1998: 21). Whether or not one accepts this statement at face value, it shows how the accounting profession was attempting to legitimize its practice of management consulting. As Cooper et al. (1994) have noted, when moving into new product areas, accountants establish the legitimacy of the expansion by defining the new service as being within the domain of the existing profession. The Lybrand partners accomplished this by claiming that the new services were actually just a repackaging or leveraging of work already performed by the profession.

In 1951, Lybrand established a management advisory services organization (MAS), under the direction of Herman Heiser, an audit partner based in Philadelphia. Consulting services were to be available to any audit client; consultants would work on projects in response to the requests of audit partners throughout the firm. The early consulting groups were scattered throughout the firm, organizationally reporting to the regional auditing partners. Formal organization of a separate national consulting practice did not occur until 1960 (Kaufman, 1998: 40). Philadelphia became the lead consulting office, and it guided the practice towards Electronic Data Processing (EDP) work.¹⁴ This was initially attempted by educating existing personnel in computer sciences, in effect trying to turn auditors into computer professionals. This practice was never fully abandoned, although its deficiencies were recognized, and Heiser soon began trying to bring in computer experts. The first high-level professional IT hire was Felix Kaufman, who entered as director of EDP services in 1957.

Kaufman and many others that followed him were well regarded EDP professionals, but they were not accountants.¹⁵ While some early consulting personnel did have the necessary audit background and so could be admitted to the partnership,¹⁶ without an accounting background most could not. The firm was facing the possibility that these valuable assets could be lost, and potentially become competitors. To avoid this, there needed to be changes in the firm's structure, and the result was the creation of the position of principal. First used to recognize the contribution of Frank Smith,¹⁷ director of personnel and training, the principal position was soon routinely awarded to non-accounting personnel deemed otherwise worthy of a partnership position.¹⁸

Whereas the provision of tax services raised few questions of independence,¹⁹ forays into consulting services brought this issue to the front and center. In auditing, the profession's ultimate client was the public. In contrast, in consulting services, the public interest was absent, and the firm worked solely to maximize the client's interests. The potential infringements on independence varied with the services offered: selection and oversight of an EDP system installation was much less problematic than conducting an analysis in support of management decisions such as business acquisitions or closures. The question of independence was regularly debated, both within the profession and externally.²⁰ Within the firm, resistance to consulting was clothed in terms of independence concerns, but in reality often reflected animus towards consulting. There was a strong sense that auditing came first, formalized in firm policy bulletin E-20 that stated that the audit partner was to be the senior partner in all client relationships (Kaufman, 1998: 33). Unlike auditing, with its clearly defined deliverable (the audit opinion), consulting was a much riskier enterprise: the project could fail to deliver a product. These problems were exacerbated by the fact that

until the late 1970s, consultants were entirely dependent upon the auditing partners for marketing their services. The Federal Trade Commission, concerned with anticompetitive practices among firms, began to push the AICPA to allow firms to advertise in the late 1970s. By 1990, virtually all restrictions on firm advertising had been lifted. Institutional changes (the ability to advertise, the ability to enter into partnerships with non-accountants) and organizational changes (the creation of the position of principal, the formation of a national consulting division separate from the auditing division, a rewording of firm policy to increase the role of consulting partners in defining client relationships) helped lay the groundwork for an era of tremendous growth in consulting that would begin in the 1970s and then accelerate in the 1980s and 1990s.

Computer consulting was the largest, but not the sole non-accounting product C&L developed. The firm developed a specialty in industrial engineering consulting which eventually led to an operations research practice. The engineering expertise was strengthened by another merger, the purchase of the industrial engineering firm, Joseph Cook and Company, in the 1960s. Lybrand also began to provide actuarial benefit services (called ABC – Actuarial Benefit Consulting, later known as Human Resources Consulting). Entry into this field was largely a client-driven move as prior to the creation of ABC clients requesting actuarial services had to be referred to practitioners outside of Lybrand. For example, the San Francisco partners disliked having to refer such clients to Peat-Marwick (Schroeder, 1998: 24). The international merger was also instrumental in alerting the US offices to the potential benefits of pursuing actuarial work. Actuaries were already a regular part of the British accounting profession and were integrated into their practice, with actuarial topics included in the accountant's certification exams (Jones, 1981). Jennings, the partner who engineered the international merger with Coopers, was aware that Coopers provided actuarial services to their clients, and he felt that Lybrand should do the same. The US firm's commitment to this business was signaled by the acquisition in 1961 of the TerryBerry Company (Martin, 1998: 7), an established provider of actuarial services.

By the 1960s, though auditing and tax services were still the primary products offered by C&L, the step towards broadening its scope of services had been irrevocably taken and the firm was no longer solely a professional accounting firm. Though not yet an integrated professional organization, it could and did provide worldwide services to its clients. It also had begun to hybridize, beginning its transformation from an accounting firm to a professional services firm which offered audit, tax, EDP, consulting, and pension and benefits services.

5. Technology, consulting and consolidation, 1980–1998

Although the third era began with a strong drive to diversify into new opportunities in a rapidly expanding knowledge economy, it ended with the imposition on the profession of limits on the scope of services. This induced a reversion among some leading firms, including C&L, to reduce practice risk by pursuing a strategy of horizontal integration. During the 1980s and 1990s, large accounting firms in the US and Europe worried about the slow growth and marginal profitability of audit services (Elliott, 1998; Previts, 1985). Many believed auditing had become a mature industry whose growth would be limited to the rate of expansion of the economy. Beate Morrow, one of the first women to achieve partner status, noted, “the emphasis has been, in the last few years, somewhat away from the audit, which is a commodity, to rendering more specialized services to clients – in the consulting area and out-sourcing and other areas” (Morrow, 1998: 13). In addition, the profitability of audit practice among the larger firms was further eroded because of the rising incidence of malpractice litigation.²¹ The big accounting firms paid out \$1 billion in litigation payouts and settlements in the early 1990s, prompting Coopers and Lybrand to set aside approximately \$130 per share in practice protection costs for the 1994 fiscal year (Moore, 1998). Profit margins

were further squeezed by sharp price competition in winning engagements and the costs of engaging high quality professional labor. Ultimately, these high costs would encourage C&L to look for a merger partner.

Changes in the nature of IT also affected the economic environment in which C&L operated. During the 1950s and 1960s data processing had been revolutionized by the introduction of highly efficient mainframe computers that reduced the costs of accounting record keeping, particularly among firms that could afford to invest in the costly new equipment and to hire specialized personnel. By the 1980s and 1990s, however, the development of new generations of mini and micro computers made possible the design and implementation of both local and wide area networks for enhancing the efficiency of communication and information processes. In addition, the maturation of the Internet (the founding of which dated back to the 1960s) with its integration of computer and telecommunication capabilities, provided a strong technological basis for the expansion of an information-based economy. These changes attracted Wall Street's interest and led to a boom in venture capital financing and initial public offering (IPO) to support the so-called "dot com revolution". Stock market expansion accompanied by the telecommunications deregulation in 1996 and the anticipation of the Year 2000 (Y2K) problem led firms to significantly increase IT investments. The impact was so great that in May 1996, the Securities Exchange Commission began requiring public companies to file financial statements and other reports electronically via its Electronic Data Gathering and Retrieval (EDGAR) system.

The collapse of the Equity Funding Corporation in 1970 helped to focus accounting firms on changes to auditing practice which could limit auditors' liability exposure. Though the AICPA committee investigating the fraud did not find Generally Accepted Auditing Standards (GAAS) deficiency, members did highlight the need to adequately test internal controls, especially with regard to the IT environment of clients. In response to this report many firms developed specialist audit teams to assess such risk; at C&L, this resulted in the Computer Audit Assistance Group (Donald Warren, 2012, personal communication). Additionally, the committee highlighted the hidden independence problems inherent when small accounting firms were absorbed by the Big 8; acquired clients, though a relatively small fraction of a total Big 8 firm's revenue, could still be significant as a proportion of the fees contributed by the merging partners. This placed more importance on the need for upstream oversight of work performed by subsidiary auditors (Stone et al., 1975).

The rapid growth of IT had two major effects on strategic development at C&L. First, it could increase the efficiency of the traditional core service of auditing and tax compliance work. Second, it opened new opportunities to enhance practice growth through the development of new services that capitalized on the firm's basic competency in data evaluation and the measurement of business performance.

Technology held out the promise of cutting costs by reducing costs for the highly labor-intensive service of auditing. Specialized computer software made possible the rapid recovery and testing of accounting data, capacities which shortened significantly the time required to complete audit field work. Audit software facilitated data gathering and evaluation for both compliance and substantive testing. For larger clients with strong internal control and extensive electronically stored business data, it allowed greater reliance to be placed on analytical review in planning and fieldwork. In the view of Nicholas G Moore (2004: 5), global vice chairman, savings would accrue from "a continuous learning cycle, stronger linkages with our CAS [computer auditing specialists], and a leveraging of available technology". The firm also experimented with new technology to develop more standardized ways to bolster audit efficiency for smaller, less profitable clients.

Audit practice contributed to new capabilities for the management of business risk. During the 1980s the auditing profession came under public scrutiny because of the incidence of examination failures and malpractice. In response to this, Coopers & Lybrand broke with its tradition of

internally assessing the business risk associated with audits, turning instead to outside consultants. Reflecting the multi-dimensional nature of the audit business, these consultants came from diverse specialties – a consulting psychiatrist, as this was a “people business”; an actuarial consultant specializing in insurance pricing; and a former statistician for NASA who had experience in “calculating probabilities of moon shots” (O’Reilly, 1998: 1–17). The consultants worked with a multi-line business team to recommend a risk management program. This audit-derived concern with risk led to the development of capacities for providing consultancy to clients for addressing the problems of business uncertainty.

Access to client data facilitated the development of a high degree of specialized industry knowledge that enhanced C&L’s competitiveness. Such data provided deep insights into the relationships that bound the client to other elements in its business infrastructure – what economists would term the “industrial sector”. This knowledge provided the lead for C&L to expand its practice by addressing the attestation service needs of financiers, customers and suppliers of existing clients. This knowledge improved firm competency in providing audit services to business entities within an industrial community. It created opportunities for rendering assurance services that certified the quality of information transfers for contract and regulatory compliance. It also laid the groundwork for the establishment of information assurance services between firms operating within e-commerce networks that became vital to global business at the beginning of the twenty-first century.

Although management consulting had long been important in the US profession from its late nineteenth-century beginnings, this dimension began to explode during the 1970s. In 1975, on average, management consulting services comprised 11 percent of the Big 8’s total revenues; by 1998, revenues from management consulting increased to an average of 45 percent, ranging from 34 to 70 percent of the Big 5’s revenues for that year (GAO, 2003).²²

The search for new market outlets began in the 1980s under the leadership of managing partner Peter Scanlon and his successor Eugene Freedman. Consistent with industry trends, firm leadership decided to take “a fresh look at the business, a fresh look at the industry, at our competition, at ourselves” (Freedman, 1998: 2–12), with the desire to become more service diverse and profitable. One early dimension of this was a new division to outsource professional and communication services for clients. Particularly strong in this regard was the provision of internal audit capabilities for clients, reflecting the increasing sensitivity among large international clients for the maintenance of adequate systems of internal controls mandated by the Foreign Corrupt Practices Act of 1977. Management argued that by engaging a public accounting firm for internal audit the firm could be assured of high-quality talent. This arrangement could also minimize the potential conflicts that could undermine the effectiveness of internal audit teams responsible to top financial management in client enterprises. These arguments were a bit disingenuous, as cost concerns played a prominent role in the decision to outsource.

A second use of C&L’s information networks and global IT was in supplying advisory services to a client’s marketing call centers, particularly outside the boundaries of the United States. Outsourcing in the global era made corporate supply chains more complex and softened the boundaries between corporations. In this context, the firm found itself

less consultative and observing, and one where we’ll really be part of the problem or part of the solution ... We’ll be expected to do some of the things that drive value, that service customers, that service employees, or that help produce and distribute and sell their product. (Martin, 1998: 27)

Diversification also enabled the firm to focus on providing assurance rather than auditing services through the consolidation of fragmented service capabilities scattered through the firm. One example of this was a new practice unit that provided specialized financial and litigation services

for companies in bankruptcy. Accountants had vast experience in compiling data for winding up liquidating businesses and in preparing special reports about these matters for bankers and lawyers. Because of this counter-cyclical service, demand for C&L workouts and bankruptcies remained strong during the recession of 1989–1990 brought about in part by the Savings & Loan crisis. Troubled situations also provided knowledge and experience that spilled over and reinforced mergers, acquisitions and consulting. This provided the firm's practice with business in both economic boom and bust periods, making it virtually recession proof.

Scanlon and Freedman also gave partner Seymour Jones the task of organizing a wide array of services required by entrepreneurs – including personal estate and financial planning, budgeting, cash management, financing and auditing (Jones, 1998: 2–5). Success in this area gave C&L exposure to the lucrative IPO market as an increasing number of start-up clients went public. By the 1990s, the firm built a large and thriving practice in entrepreneurial business services, which provided a valuable learning base for the development of its consulting practice. Building on the learning base developed from the entrepreneurial business services, Jones later extended its scope through the formation of “Financial Advisory Services” to serve a full range of clients.

Diversification also created impediments for the execution of client-focused knowledge-based services. Gene Freedman (1998: 13) grew worried that the firm, “had become a bureaucracy, like many big businesses”. Internal competition between regions and lines of business served neither clients nor the overall firm. There was also a mismatch between the firm and the markets it served. As Freedman (1998: 15) said, “. . .the market knew what it wanted. It wanted technology. It wanted knowledge. It wanted responsiveness. It wanted an international network”.

Structure followed strategy. The firm became more responsive to client needs during the mid-1990s by eliminating two layers of management and reducing the number of profit centers from 120 to about 20. The new organizational structure established lines of business in the areas of: (1) consulting (largely systems advisory services); (2) human resources (primarily actuarial services); (3) tax; (4) audit; and (5) financial advisory services.²³ In addition, the firm established core competencies – for example technology, knowledge and international expertise – that would both distinguish the firm and be foundational to all the industries and functions. In this process, the firm transformed its traditional business as well, from a predominantly audit focus to an assurance business which had “a much broader focus . . . in terms of pieces of the business, of procedures, of aspects beyond the narrow . . . focus of an audit and the financial statements” (Freedman, 1998: 19).

The new strategic direction under Freedman revolutionized the firm's consulting operations. Previously, consulting units were diffused as they were organized into six regions and a national operation. They competed with one another and were essentially appendages to the audit business. Recognizing new opportunities in the changing marketplace, the firm reorganized its consulting into a national business, Coopers & Lybrand Consulting. The new structure eliminated regional competition, improved client focus by shifting personnel and resources where they were needed, and helped strengthen industry proficiency. A central element in this new structure was the creation of hub centers to coordinate multiple lines of service. These hubs served as pockets around the country for the allocation of nationally managed and focused resources.

Continued global expansion increased the pressure for further organizational modifications that would allow for seamless global integration, for the firm “to really act bigger and act as really a collection of . . . 20,000 people in the U.S. and 70,000 people worldwide, as opposed to just acting . . . as the actuarial group in Chicago” (Martin, 1998: 12). This required moving from thinking about firm resources geographically to accessing resources efficiently throughout the firm in an effort to satisfy increasingly complex and multidimensional client needs. To do this, the firm not only relied on newly developed communication tools, but also pursued a systematic approach to solving client problems that encompassed technology, personnel and organizational structure.

Thus, while organizing along five product lines, the firm also employed a matrix structure that emphasized industry knowledge. The depth of knowledge represented by industry specialization took years to develop, but once acquired the matrix organization allowed for the expertise to be shared across regions and product lines.

The emphasis on industry specialization was not new to the firm; indeed, one partner estimated that by the late 1970s people were expected to spend half of their time working in only one industry (Morrow, 1998: 9). But, firm leadership reorganized the firm in the 1990s in a way that formally entrenched industry specialization, going so far as to create multi-disciplinary industry teams (that is, teams with members from across the five product lines) (Moore, 1998: 4). In this way, specialized knowledge was accessible to line consultants and partners throughout the firm, ensuring that the firm's sizeable investment in expertise could be efficiently utilized. This would enable partners to focus on a client needs – globally and across product lines – as opposed to employing a more parochial perspective. At the same time, the firm attempted to disseminate standardized approaches to problem solving, a “Coopers & Lybrand way of doing things” (Martin, 1998: 15). Such standardization would be critical to effectively leveraging distributed knowledge. Learning how to integrate diverse sources of knowledge to solve complex problems encountered by clients became central in the drive to establish a responsive organizational structure during the closing years of the twentieth century.

Practice diversification, did not, however, go uncontested. The failure of the AICPA's “Cognitor” initiative was an early signal of changing attitudes about the wisdom of practice diversification. In 2000, the AICPA had proposed an international business credential named Cognitor, which was designed to certify competency in financial-oriented knowledge on a global level and could be used by professionals from a number of disciplines including accounting, law, and even engineering. The Cognitor designation met with so much resistance from its membership, which largely saw it as a dilution of the CPA franchise built up over the course of over a century, that the AICPA abandoned the scheme in 2001.²⁴ Efforts to find a global professional designation that blends knowledge both of financial and managerial accounting and information systems still continue. The profession has increasingly looked to the provision of attestation services – such as the continuous auditing of online transactions – as a way to expand businesses while reaffirming their core competencies. This reflects the changing landscape of the profession clearly evident since the last quarter of the twentieth century.

More problematic were criticisms claiming that service diversification undermined auditor independence. SEC Chairman Arthur Levitt (2000) and others argued that the large fees generated by non-audit services would undermine the accountants' ability to protect the public interest. Such fee leverage, he reasoned, would make it difficult for auditors to take strong positions if they disagreed with their clients about the application of accounting principles. Practice risk also increased throughout the profession because of the collapse of the technology boom at the turn of the twenty-first century and the subsequent intensification of investor malpractice litigation.

Anticipating a major reform of financial market governance (which eventually emerged with the passage of the Sarbanes-Oxley legislation in 2002), the leaders of Coopers & Lybrand charted a new course just as the firm was celebrating its centenary in 1998. Their initiative focused on stabilizing the firm's market position through a merger with another global public accounting practice (Coopers & Lybrand, 1997). The reversion to horizontal integration in a global context took place through the merger with Price Waterhouse & Company to form PricewaterhouseCoopers (PwC). This move better enabled the two former rivals to steer through the new crises confronting the profession. Larger size helped to reduce adverse litigation, and consolidation enabled the successor firm to reduce risk by eliminating connections with clients deemed marginal. By July 2003,

after several rounds of downsizing to reduce duplicated locations resulting from the merger, PwC operated offices in 768 cities in 139 countries (PricewaterhouseCoopers, 2003: 9).

After the merger, governmental impediments to a diversification strategy became more acute. In 2000, the SEC adopted a new rule, the Auditor Independence Rule (Securities Act Release No. 33-7919) prohibiting audit firms from providing certain types of consulting services to clients. In addition, proxy disclosures for audit and non-audit fees paid to the company's independent auditors were required. Mounting public pressure during a period of economic recession, which included the failure of the Enron Corporation, induced two of the Big 5 firms to sell or spin off their consulting arms, the sole exception being Deloitte & Touche.

In the aftermath of the spectacular accounting scandals following the stock market crash of 2001, the professional firms once again were targets of public ire. Enron was blamed for how "greed helped sink the respectability of accounting" (Dugan, 2002). The *Sarbanes-Oxley Act* of 2002 (SOX), enacted in response to these and other accounting irregularities, further limited the scope of services auditors could provide. In response, PricewaterhouseCoopers Consulting was sold to IBM in October 2002. Moreover, *Sarbanes-Oxley* authorized the formation of the Public Company Accounting Oversight Board (PCAOB) to exercise oversight over public accounting firms with public clients, and specifically prohibited the involvement of registered accounting firms in 11 lines of business, including outsourcing of internal auditing and actuarial benefit advisory services.

The revenue loss from prohibited services was somewhat offset by the increased stringency of fieldwork and internal control reporting requirements mandated by the new legislation. While the auditing of financial statements remained a commodity (Palmer, 1989), SOX turned provision of assurance services for client internal control evaluation into a growth area. Moreover, with the expansion of e-commerce, auditors saw the possibility to exploit the trend in assurance services by special engagements for assessing the reliability of economic information transmitted through the Internet (known as continuous auditing).

6. Conclusion

What then does the history of Lybrand, Ross Bros. & Montgomery tell us about the nature of large practice evolution during the twentieth century?

To a large extent, the course pursued by C&L follows the Chandlerian model: size facilitated large customers and allowed the firm to develop knowledge specialization. A network of local offices made possible the economies of scope to serve the giant organizations that emerged to dominate many business sectors. Their organizational capabilities facilitated services to these enterprises of great scale, scope and complexity. In effect, the office units were expert networks capable of deploying knowledge to satisfy clients within the context of local, regional and national markets and then, later, within a global business environment.

Size facilitated the concentration of knowledge to serve the complex needs of diversified clients. The large size of the Lybrand firm allowed offices to develop specialized knowledge, as exemplified early on by the Philadelphia office's venture into management consulting. Firm-specific capabilities served as barriers that impeded competition from later market entrants. C&L pursued this successfully in both EDP consulting and actuarial services. The firm could then attract outstanding personnel whose skills could be further sharpened through in-house training and from experience gained in helping to resolve the challenges of a varied clientele. Size made feasible the achievement of efficiency through the division of labor. Besides their activities around auditing, tax and systems work, the firm also developed special industry knowledge. Moreover, large entities had sufficient resources to acquire new knowledge about resolving practice

problems. This range of experience also qualified members of large firms to advance learning by participating in the process of defining standards for financial accounting, auditing and other practice dimensions.

The special acumen developed in giant enterprises qualified firms like Lybrand to participate in professional, business and governmental affairs to influence the direction of socioeconomic change. This enabled the firm to shape initiatives that influenced the interest of the firm, its clients and the profession. Such linkages also provided feedback about developments vital to practice leaders in strategizing how best to prepare for an uncertain future.

Size and scope also reduced the overall risk and assured practice continuity. It provided a buffer to counter losses incurred from adverse practice litigation. It also minimized risk through the diversification of practice over multiple markets, companies and industries. Large firms generally had sufficient resources to avoid the possibility of liquidation or merger at the end of the careers of key principals.

Size enhanced practice quality and reduced risk by providing leverage in dealing with problematic clients. The economic disruption of the loss of a single client was less difficult to bear for a firm serving a large clientele. This was especially important in disputes on accounting principles or matters dealing with tax and business law.

For knowledge-intensive firms, unlike industrial enterprises, scale economies were difficult to exploit because of a dependence on the variable costs of expert labor and a limited investment in fixed capital. In industry, average unit costs could be dramatically reduced by increasing production through-put in a high fixed cost environment. In public practice, however, increases in service demand led to a proportional increase in labor costs, thus, negating realization of efficiencies from higher activity levels. Efficiencies could result to some extent from the integration of data processing capabilities within the practice, but it was still a labor-intensive business. Efficiencies were attained, however, from leveraging the knowledge base of a specialized cadre of professionals. Costs associated with lower level employees, proportional to increase in service, might be substantial, but these costs could be managed as long as the firm was able to develop in-house specialized knowledge pools.

Building up a base of professional knowledge reduced costly learning curves and enabled the firm to respond to the service needs of clients operating in diverse businesses. This is one reason why C&L aggressively pursued merger partners with industry expertise. Developing a deep knowledge base in a variety of industries also placed firm personnel in a good position to assimilate new knowledge as it evolved. When a new technology came on the scene, C&L personnel were in a prime position to understand the challenges and opportunities it represented. Minimizing the learning curve could therefore give C&L first mover advantage in emerging industries. This may explain why the evolutionary path followed by accounting firms more closely followed the Chandlerian model of large-scale industry rather than the more specialized, niche-focused models identified by Lamoreaux and her co-authors as predominating among today's manufacturers.

The application of computer technology increased the labor productivity of accounting firms such as C&L. But, in general, technology's impact on accounting practice differed from the circumstances contemplated by evolutionary economists in their analysis of high-tech competition. Accounting firms specialized in the application of general-purpose technologies particularly relating to computing and data processing. For the most part, they did not try to compete by acquiring exclusive property rights through patents and other contracts from research and developmental activities. The large accounting firm's advantage in knowledge derived largely from its range of experience in serving the needs of large clients as well as the technical proficiency of its staff. The primary exception to this generalization was internally generated proprietary software for auditing and other services.²⁵

The strategic conception of the firm had an important bearing on practice in the local office network. Historically, two models affected how knowledge was ordered to serve client needs. For most of the firm's history its leaders conceived it as a CPA practice. By the close of the twentieth century, however, the leadership viewed the organization as a diversified provider of knowledge-based services.

Under the CPA conception of the firm, local office practice was organized around auditing, the activity to which professional licensing directly pertained. Each office had separate pyramidal hierarchies headed by a senior partner supported by a staff of managers and accountants. Each pyramidal group was assigned a particular mix of clients. In this context tax and management consulting were ancillary to auditing. The timing and scope of tax and consulting services were a function of the basic audit plan.

Under the knowledge-based system, however, the increase in the degree of diversification made the CPA organization unwieldy. Many of the new information services employed managerial protocols more appropriate to regional than local markets. Local office demand was often insufficient to support full-time personnel. In addition, the number of services grew to such an extent that the firm required new structures that went beyond the bounds of the organizational arrangements previously established to accommodate the industry specialization and the three basic functions of audit, tax and management advisory services. This increased the degree of administrative complexity. Under these circumstances, the formation of hub offices to coordinate the growing lines of practice specializations on a regional basis proved most effective. This also shifted power away from the traditional leadership based in auditing. The planning of service promotion was no longer primarily dependent on satisfying the priorities of audit practice. Under the new structure, the firm was able to pursue opportunities in fast-growing, more lucrative non-audit services.

Eventually, both professional and regulatory requirements in audit practice imposed limits on the scope of practice. Leaving aside the inherent difficulties associated with managing the numerous regulatory bodies encountered when operating globally, the very purpose of the accounting profession had evolved. The profession's services were broadened beyond the auditing of financial statements to include the provision of new attestation services (IT reviews, valuation services, etc.). At the same time, other services were deemed incompatible with the attestation role. The central constraint derived from the need for independence and objectivity in providing assurance to those who relied on auditor attestations about the reliability of client financial statements. Although firms historically had shown some sensitivity to the possibility that certain services were incompatible to maintaining auditor independence, these proscribed activities were clearly specified under the *Sarbanes-Oxley Act*. Concurrently, this lessened formal concern about whether professional fees for non-audit services could grow so significantly as to undermine perceptions about firm independence.

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Notes

1. See, for example, a speech presented by KPMG partner, Robert Elliot (1998).
2. L.R.B. & M. Announcements (1909–1930); L.R.B. & M. Announcements and Ads (1931–1993; 1947–60); *L.R.B. & M. to C&L Scrapbook* (1924–58); *L.R.B. & M. Scrapbook* (1924–1960); Scovell, Wellington and Co. (1923–1961).
3. Lybrand provided auditing services to all segments of AT&T except for its internal manufacturing arm, Western Electric, which was served by Arthur Young and Company.
4. Examples of the firm's competency and source of authority in several fields of practice include publications such as Robert H. Montgomery's *Financial Handbook* (1925) and *Income Tax Practice* (1918).
5. Scovell, Wellington & Co. had been formed in 1939 when Wellington, a senior partner with an engineering practice, left the consulting firm of McKinsey, Wellington, & Co.
6. A third office was opened in Berlin, but this was shut down in the days before World War II.
7. Since the early twentieth century, CPAs had felt that the increasingly international nature of business required an international accounting perspective. As a partial step towards such a perspective, from 1904 the American Institute of Accountants had begun sponsoring international accounting conferences. These Congresses were slow to take off; after the first one was held in St Louis, no further congresses were held until 1926 in Amsterdam. The pace then increased: the 3rd Congress, in 1929, was held in New York (with over 2,500 delegates representing 14 countries), followed by the 4th in London in 1933, and the 5th in Berlin in 1938. World War II disrupted the meetings, but in 1952 they resumed in London. From this point on, the conferences would be held every five years, with the first US event occurring in New York in 1962. Lybrand personnel were active in the pre World War II Congresses, indicating their interest in establishing a more global perspective early on.
8. At the time of the merger, Cooper Bros. also had offices in New York and Montreal.
9. The association of Cooper Bros. with McDonald Currie began in 1948, at which time the Montreal branch of Cooper Bros. was shut down.
10. In 1946, in an early consulting foray, the Organisation Department was created at Coopers, but this effort was short-lived, disappearing by the early 1950s (Hobson, 1979: 30).
11. Partners familiar with the circumstances of the merger stated that in selecting a firm name, Cooper Bros. insinuated to the Lybrand partners that "you really need us more than we need you", hence the decision to place Cooper first (Cranz, 1998: 19).
12. Sir Henry Benson, the managing partner of Cooper Bros. proposed the name change as a way to increase recognition of the firm globally as a unified, integrated practice (O'Reilly, 1998: 28).
13. A chronological list of countries into which C&L entered through to 1996, is included as Appendix 1.
14. Most of the EDP work in this era involved electromechanical data processing system development. This changed in the late 1960s with the advent of the first IBM system 369 and the beginning of the electronic computer.
15. Kaufman actually became a CPA in order to join the partnership.
16. For example, Holland, from MAS, was made a partner in 1963.
17. Smith was also a CPA, but with an academic rather than professional career.
18. In 1964, the AICPA allowed CPAs to form partnerships with non-accounting professionals (in a vehicle separate from the accounting partnership), thus obviating some of the need for the principal position (Carey, 1970).
19. However, the question of independence had earlier been aggressively raised by lawyers who opposed allowing CPAs to represent clients in tax cases (Carey, 1970).
20. Independence was one of the subjects in the 1976 "Metcalfe Report" which investigated US accounting practices.
21. Litigation settlements included \$200 million in punitive damages related to MiniScribe's 1989 collapse (*LA Times*, 1992) and an undisclosed 1995 settlement in the Phar-Mor bankruptcy where defendants sought \$950 million (Knight Ridder, 1995).
22. The Big 5 were Arthur Andersen, Deloitte & Touche, Ernst & Young, KPMG, and PricewaterhouseCoopers.
23. Outsourcing was also originally proposed as a sixth business line.

24. The Cognitor debate was extensively covered in contemporary professional media. For an overview, see Wyhe (2007).
25. C&L did have an in-house Computer Assisted Auditing Group (CAAG) that developed software which was also sold to clients.

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Appendix I

Countries	Year C&L became active
United Kingdom	1854
United States	1898
Canada	1910
Belgium	1921
South Africa	1931
Kenya, Tanzania, Uganda, Zimbabwe	1947
Australia, New Zealand	1948
The Netherlands	1949
Zambia	1952
Nigeria, The Congo	1953
Singapore	1956
Germany, Malaysia, Mexico	1957
Ghana, Iran	1959
Switzerland	1960
Bermuda, Sweden	1961
Bahamas, Denmark, Jamaica, Liberia, Papua New Guinea	1962
Norway, Puerto Rico, Spain, Venezuela	1964
Hong Kong, Ireland	1965
Japan, Nicaragua, Swaziland, Uruguay	1966
Austria, Brazil, Grand Cayman, Malawi	1967
Honduras, India, Korea	1968
Barbados, Botswana, British Virgin Islands, Italy, Lebanon, Turks & Caicos	1969
Angola, Brunei, Dominica, Fiji, Greece, Grenada, Malta, Portugal, St Lucia, St Vincent	1970
Argentina, Bolivia, Cyprus, El Salvador, Mauritius, Paraguay, Vanuatu, Zaire	1971
Afghanistan, Indonesia, Mozambique	1972
Finland, Trinidad	1973
Chile, Columbia, Costa Rica, Ecuador, Egypt, Kuwait, Laos, Luxembourg, Panama, Peru, Saudi Arabia, Sultanate of Oman, Thailand	1974
Dominican Republic	1975
Iceland	1976
Philippines, Qatar, Senegal, Solomon Islands	1979
China, Sri Lanka, Tahiti	1981
Netherlands Antilles, Tunisia, Turkey, Western Samoa	1982
Gabon, Monaco	1983
Morocco	1985
Cameroun, Gibraltar, Lesotho	1986
Taiwan	1987
Bahrain	1988
Hungary, Somalia	1989
Antigua, Aruba, Czechoslovakia, Guinea, Liechtenstein, Namibia, Nepal, Poland, Russia	1990
Romania, Pakistan	1991
Estonia, Jordan, Macedonia	1992
Burundi, Ethiopia, Latvia, Lithuania, Slovakia, Slovenia, Ukraine	1993
Bulgaria, Israel, Kazakhstan, Myanmar, Palestine, Surinam, Vietnam	1994
Bangladesh, Cambodia, Maldives, Uzbekistan	1995
Croatia, Yugoslavia	1996