Accountancy has lost its way

by John Hunter

I'm an accountant, not an auditor – I've always worked within business – but it's a profession I respect, or used to respect. I have in my time been considered an expert on accounting standards and financial reporting, I have been responsible for (and written much of) annual reports, I have engaged auditors, I have managed audit committees. But 'my time' was some time ago, and as an investor I have increasingly found annual reports – both the words and the numbers – deliver a very poor information return for (my) time spent so I don't look at them anymore, or concern myself with the nuances of how they are put together. So I'm no longer an expert on any of these things.

However, I am, once again, interested. And that's because I increasingly believe that the profession has lost its way – that much of its work is irrelevant to wealth creation. There has recently been a drip feed of data all pointing in the same direction: the various recent accounting scandals and business failures on which we await promised reports; the series of articles on accountancy in the Financial Times; the trenchant articles of Malcolm Howard; the sustained attack by the group organised by Natasha Landell-Mills of Sarasin Partners (and supported by UKSA) on the legality and sense of the profession's attempts to abandon the 'prudence' principle; Adrian Phillips in June TPI expounding on 'The Perils of a Craft Monopoly'; and the lack of any reasoned response from the profession on any of this.

And this matters to us private investors. Because if accountancy has turned into a sort of high priesthood closed to outside supervision or ideas and only comprehensible to insiders, then it is little use to us.

So I thought I'd start at the beginning – to take a step back to look at what the profession thinks it's for; search for a 'mission', 'objectives', 'fundamental principles', some other expression of long-term aims or underlying beliefs. There is an immediate problem in deciding where to trawl for the soul of accounting: the professional bodies?; the Financial Reporting Council (FRC) – responsible for oversight and standards in the UK?; equivalent bodies in the USA?.

I decided to start with the International Accounting Standards Board (IASB). This is responsible for International Financial Reporting Standards (IFRS). The FRC defers to it. UK quoted companies have to report according to IFRS. Therefore the principles governing IFRS determine the way that quoted companies report to shareholders. As an investor, it struck me as rather important to understand what those principles are.

Searching for IFRS

So I googled 'IFRS principles'. That was the first surprise. I was directed to the IFRS website but could not access its content without registering. A small point, maybe, but those with a well-developed sense of cyber-security do not register on websites needlessly. Nevertheless I ploughed on.

After giving up my email address and a password requiring just six letters (no need for Caps, figures or symbols) I was asked for my 'Role (required)'. This produced a drop-down menu of about twenty job titles. I looked in vain for 'retired' or 'investor'. I was about to settle on 'academic', which would have been untrue, when I noticed the magic 'other'. So I clicked that.

I then moved on to 'Industry (required)'. This was harder. There was no 'other'. I chose 'education/academia' as the least untrue.

It just remained to tick the required boxes to allow my personal data to be handled in a way I couldn't possibly have the time to read even if I could understand it and I was safely registered.

Anyway, I can’t find an easy link to 'basic principles' or some such, so I try ‘Issued Standards’ on the menu bar and get a nice list headed by ‘Conceptual Framework for Financial Reporting’. I’m not sure of the title but I give it a try. I get: ‘The revised Conceptual Framework is currently only available to Premium subscribers. The revised Conceptual Framework will be available to Basic subscribers after we publish the Issued IFRS Standards in early 2019. The Conceptual Framework issued in 2010 is still available to Basic users below.’ Oh, so as an investor – or ‘user’ - I have to pay to discover the basis of the way my company is going to communicate with me? But I can view the hot thinking of 2010 without charge?

Do you get an impression that this body regards itself as serving the producers of accounts, and not the users? Me too.

Anyway, I access the 2010 Conceptual Framework, and my heart sinks:
• There are over 10,000 words spread across some 30 pages;
• There is not a single definition of terms. Popular ones are ‘faithful, ‘probable’, ‘reliable’, ‘comparable’, ‘consistent’. (Sorry, I lied about ‘reliable’ – it is defined as ‘when information is complete, neutral and free of error’);
• There are just 148 words on ‘probability’ – fundamental, one would have thought, to any set of principles about uncertainty from which so many accounting problems flow. These include not a single word with any analytical or computational guidance (see box below);
• The ‘purpose of accounts’ is spread across many paragraphs and could loosely be defined as ‘anything that might conceivably help somebody to learn more’. Would it be cynical of me to rephrase that as ‘anything that might generate fee income’?

However, there is hope

The hope lies in the fact that the string of recent revelations about the profession has rightly led to a demand for answers. The Treasury commissioned Sir John Kingman to deliver a report on the function and effectiveness of the Financial Reporting Council. ShareSoc and UKSA have made a hard-hitting input to this report, delivering a picture of good people within the organisation struggling against confusion and inconsistency in its governance, funding and objectives. UKSA’s contacts with the profession have similarly shown a willingness to listen and change.

Westminster Business Forum – an organisation with strong links to Parliament – has booked a conference at the end of February to discuss the report and has invited UKSA to represent shareholder interests on a panel discussion. **This is a real opportunity to influence outcomes. Let’s hear members’ views.**