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ACCA

The Future of Financial Reporting 2009: A Time of Global Financial Crisis

A DISCUSSION PAPER BASED ON THE BRITISH ACCOUNTING ASSOCIATION FINANCIAL ACCOUNTING AND REPORTING SPECIAL INTEREST GROUP (FARSIG) COLLOQUIUM, 9 JANUARY 2009

ABOUT ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

We support our 131,500 members and 362,000 students throughout their careers, providing services through a network of 80 offices and centres. Our global infrastructure means that exams and support are delivered – and reputation and influence developed – at a local level, directly benefiting stakeholders wherever they are based, or plan to move to, in pursuit of new career opportunities. Our focus is on professional values, ethics, and governance, and we deliver value-added services through our global accountancy partnerships, working closely with multinational and small entities to promote global standards and support.

We use our expertise and experience to work with governments, donor agencies and professional bodies to develop the global accountancy profession and to advance the public interest.

Our reputation is grounded in over 100 years of providing world-class accounting and finance qualifications. We champion opportunity, diversity and integrity, and our long traditions are complemented by modern thinking, backed by a diverse, global membership. By promoting our global standards, and supporting our members wherever they work, we aim to meet the current and future needs of international business.

The paper is available in PDF from the ACCA website at: www.accaglobal.com/general/activities/library/financial_reporting/other

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The Financial Accounting and Reporting Special Interest Group (FARSIG) is a group set up under the aegis of the British Accounting Association (BAA). The main purpose of the FARSIG is to further the objectives of the British Accounting Association and for that purpose to

- encourage research and scholarship in financial accounting and reporting
- establish a network of researchers and teachers in financial accounting and reporting
- enhance the teaching of financial accounting and reporting
- provide support for PhD students in financial accounting and reporting
- develop close links with the accounting profession in order to inform policy
- publish a newsletter and organise targeted workshops
- develop and maintain relationships with the British Accounting Association and the professional accountancy institutes, and
- provide a forum for the exchange of ideas among accounting academics.

The symposium, which is one of an annual series, provides a forum for academic, practitioner and policy-orientated debate. Such forums are useful for expressing and developing rounded opinion on the current meta-issues facing financial reporting. They are also useful in that they serve to illustrate the policy relevance and impact of current academic thinking and outputs in accordance with The Economic and Social Research Council (ESRC)/ Advanced Institute of Managament (AIM) calls for relevant and rigorous research through a combination of practitioner and academic perspectives.

We would like to express our thanks to the five main contributors, both for their presentations at the symposium and for their subsequent time and comments during the development of this discussion paper. We have tried faithfully to capture the flavour of the original presentations. Nonetheless, although we ran our commentary of the presentations past the original authors, any errors or omissions remain our own. We would also thank ACCA for hosting the symposium and for its support in the publication of the discussion paper. Finally, for any readers who wish to learn more about FARSIG or to become a FARSIG member, please contact either of the authors.

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The Future of Financial Reporting 2009: A Time of Global Financial Crisis

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Foreword

I am very pleased to provide a few introductory words to this report on the FARSIG symposium held in January 2009.

The theme of the future of financial reporting at a time of global crisis was very topical. The papers and discussion, well captured in this summary, set out the main thoughts at that point, both on the role of accounting in the crisis and the impact of the crisis on accounting. The factors which provoked a crisis on that scale and the issues that needed to be thought about were then becoming clear and agreed upon, but the longer-term changes and preventative measures were only just starting to be mapped out.

It is very helpful to bring together accounting academics and those in the profession with more practical perspectives to consider these sorts of issues and the FARSIG colloquiums have been a great example of this. ACCA was therefore very happy to sponsor FARSIG and to host this event. We hope to continue our support in coming years.

Richard Martin
Head of Financial Reporting, ACCA

1. Introduction

Financial reporting itself is at an interesting juncture. The global financial crisis has meant a re-questioning of basic issues within accounting such as measurement principles, financial regulation, the conceptual framework and the future landscape of global accounting standards. The 2009 FARSIG symposium was held at ACCA, London, on 9 January 2009 and focused on the impact of the current global financial crisis on the future of financial reporting. The symposium was thus timely to capture the current financial situation and its significance to accounting. The symposium enabled five key presentations to be delivered followed by discussion. These five papers were:

1. Ian Mackintosh, ASB – *The Future of Financial Reporting in a time of Global Uncertainty*.

2. Peter Holgate, PricewaterhouseCoopers – *Organisational Politics: the IASB, the FASB, the EU et al*.

3. Ken Peasnell, Lancaster University – *Asset Securitization, Fair Values and the Credit Crunch*.

4. Alan Teixeira, IASB – *The International Spread of International Financial Reporting Standards (IFRS): Challenges and Opportunities*.

5. Paul Moxey, ACCA – *Corporate Governance and the Credit Crunch*.

The five papers and subsequent discussion expressed a range of views on the current financial crisis and accounting and reporting from accounting practitioners, standard setters and academics.

BACKGROUND TO THE SYMPOSIUM

The symposium was held at a particularly interesting time both economically and politically. The world has been buffeted by a credit crunch and this has affected all aspects of economic and political life, including accounting. The world's economic crisis had begun in the US, partly as the result of an over-heated housing market coupled with excessive risk taking, credit availability and lending practices within the banking sector and a surge in the trading of credit risk derivatives. The collapse of the US mortgage market, among other things, acted as a catalyst that ultimately led to an international banking crisis. However, the global financial crisis, like other financial crises that have preceded it (most notably the South East Asian crisis in 1997 and the Russian crisis in1998) is the culmination of a number of interrelated factors. The combination of these factors lead to events which could not have been predicted. They led, seemingly inexorably, to collapses in the world banking system, economic turmoil and then global recession.

From early 2000, US interest rates fell steadily, from over 6% to 1% by 2004, which stimulated growth in home ownership in the US mortgage market backed by corresponding increases in the value of real estate. Those involved in the housing market (banks, home buyers and indeed governments) all seemed to believe and act as if the cheap lending was effectively risk free, as any default would be more than covered by the security held on the underlying asset (real estate). This thinking led to an environment of high-risk lending and the growth of the US sub-prime mortgage market. In addition, to reduce individual bank credit risk exposure, there was a corresponding increase in the development of and trading in credit derivative products, most notably collateralised debt obligations (CDOs). This further increased the interdependence within the banking sector and bank exposure to the credit, and original mortgage, market. For instance, in 2006 Northern Rock moved into sub-prime lending through a deal with Lehman Brothers, who in turn underwrote the risk.

By 2005–2006 US interest rates had steadily increased to over 5%, owing to concerns about economic over-heating and the need to dampen down inflationary pressures. This general pattern of interest rate movement and real estate growth was mirrored in the UK where interest rates fell to 3.5% by 2004 before rising to near 5% by 2006. In the US, in particular, owing to the increased financing cost of debt, debt default rates rose and real estate values started to fall as the market reacted to forced housing sales and the realisation that the housing market itself had over-heated and that real estate was fundamentally over-valued. The banking sector was now exposed to credit default, no longer backed by an underlying asset value of equal or greater value than the loan. Banks themselves had obtained the initial finance for lending, and on-going refinancing, through revolving credit facilities from the wholesale money markets. As lending became exposed, owing to credit defaults and falling real estate prices, so liquidity in the money markets also began to tighten and refinancing became more difficult and more expensive to obtain. By 2007, the difficulties faced by banks – heightened by their exposure to the US sub-prime market, and also by their exposure and reliance on the wholesale money markets – began to become apparent. Just prior to the Symposium there were a number of high-profile banking and real estate credit collapses, the most important of which are summarised chronologically in the box.

CHRONOLOGY OF KEY EVENTS IN THE FINANCIAL CRISIS

August 2007:
Liquidity in credit markets tightened. PNB Paribas announced that three of its hedge funds were frozen owing to the complete lack of liquidity in the asset-backed security market, the result of US sub-prime exposure.

The European Central Bank injected 170 million euros into the banking market to provide short-term liquidity.

September 2007:
Collapse of Northern Rock owing to lack of liquidity and availability of finance in the wholesale money markets. Bank of England bail-out assistance as lender of last resort. Northern Rock was subsequently nationalised in 2008.

March 2008:
Rescue of Bear Stearns by JP Morgan Chase and US government guarantee of $30 billion against Bear Stearns losses.

September 2008:
Lloyds TSB takeover of Halifax Bank of Scotland.

Fannie Mae and Freddie Mac rescue by US government.

Bankruptcy of Lehman Brothers, citing bank debt of $613 billion after US government refused bail-out finance.

Merrill Lynch taken over by Bank of America.

AIG rescued by $85 billion loan from US Treasury.

Goldman Sachs and Morgan Stanley abandon their status as investment banks.

Collapse of mortgage provider Washington Mutual; sold to JP Morgan Chase.

October 2008:
US and European government interventions.

Approval of TARP – Troubled Asset Relief Program – authorising the US Treasury to spend up to $700 million to purchase distressed assets and provide banking sector liquidity.

Similar interventions approved in Germany (500 million euros), France (350 million euros) and Spain (100 million euros).

Icelandic government takes control of the three largest Icelandic banks: Landsbanki, Glitnir and Kaupthing.

November 2008:
G20 summit in Washington focuses on future financial regulation.

IMF approves $2.1 billion loan to Iceland.

December 2008:
US Federal Reserve interest rate is near 0%.

The impact of the crisis initiated in the banking and real estate sectors falls has fed through to the real economy. Global stock markets and national economies have taken a pounding. Economic problems have been reflected in lower levels of corporate investment, increased unemployment rates and a lowering of general consumer confidence. These factors, (alongside credit availability) have contributed to the collapse of a number of non-banking companies in the UK, for instance, Woolworths. The financial crisis and turmoil has wider implications for all businesses (and for auditors in expressing an opinion on their financial statements) with respect to the going concern assumption. Owing to the general tightening of credit, businesses are now faced with far greater debt exposure, which undermines the going concern basis on which their financial statements have traditionally been prepared and audited.

The immediate consequences of the banking crisis led to a focus by government and other regulatory bodies on, inter alia, the underlying regulatory, accounting and corporate governance aspects of the credit crunch. The risk and reward structures within the major banks were examined, with questions being asked about levels of risk taken and the remuneration structures of top executives and market traders – particularly where incentive bonus schemes were based on lending levels. Turning more specifically to accounting, questions were asked about the appropriateness of the current regulatory regimes. In particular, did existing accounting standards actually exacerbate the situation through the accounting recognition and measurement of derivatives and financial instruments traded by banks prior to and during the credit crisis? The role and influence of the international accounting standard board was questioned worldwide, and there was close scrutiny of recent pronouncements on recognition and measurement issues, in particular those on financial instruments. These issues are briefly covered below, but were covered in more depth by the speakers.

ISSUES RAISED BY THE SYMPOSIUM

The role of accounting in the financial crisis was much discussed during the symposium. One issue was the role of fair value. In essence, fair value is a relatively new measurement system that is, in the current thinking of the standard setters, more relevant for decision making than is historic cost.[1] Those who support the use of fair value during the credit crunch state that it merely records the present value of assets in line with their market value and thus serves to reflect current market conditions, so that assets are not held at over-valued or under-valued prices as shown on the balance sheet. However, its detractors are concerned that assets may be recorded at fire-sale prices that do not reflect the assets' true value, but rather reflect short-term volatility. An additional concern about fair value is that pro-cyclicality (self-reinforcing trends) may occur, resulting in a downward spiral of asset values. This could exacerbate the financial crisis owing to asset write-downs, and the downgrading of credit ratings based on asset values as shown on the balance sheet. Fair value has also led to enhanced concerns with going concern, because of the potential for such write-downs, with potential breaches of debt or loan covenants, and because of its possible effect on the ability of a business to safeguard, or provide assurances about, its future financing requirements.

Another issue was the role of financial instruments in the crisis, and their accounting recognition and measurement, captured in the discussion and controversy surrounding IAS 39 Financial Instruments Amendments in October 2008. Mortgages that had been advanced by financial institutions were wrapped up into complex packages, such as CDOs, and sold from one institution to another, resulting in a complex derivative market for mortgage-based, asset-backed products. The final owners of these securitised assets often had little idea of the true nature and value of their assets, or of the actual or potential levels of risk contained within the financial instrument held. This became apparent with the collapse of Lehman Brothers when the financial exposure of other financial institutions to Lehman's was not immediately known until derivative products were unravelled. Also, too many of these assets were held off-balance sheet which added to the uncertainty of financial exposure and levels of risk. Other financial instruments, such as Credit Default Swaps (CDS), have also been subject to public scrutiny for their role in the crisis.

Perhaps inevitably, the standard setting bodies have also come under close public scrutiny. The IASB in particular has been a recent advocate of fair value accounting. The political nature of this body is illustrated neatly by the controversy over IAS 39, which the speakers at the symposium discussed at length. Stakeholders in the European Union felt that this standard on financial instruments had been an exacerbating factor in the credit crunch. Therefore, considerable pressure was applied to the IASB, by EU leaders and finance ministers through the ECOFIN Council, to change this standard and, indeed, changes were made at very short notice. The key changes were connected with the reclassification of financial instruments. In its press release[2] the IASB commented that 'these amendments are the latest in a series of steps that the IASB has undertaken to respond to the credit crisis and [to ensure] that European financial institutions are not disadvantaged vis à vis their international competitors in terms of accounting rules and their interpretation.' The amendments to IAS 39 introduced the possibility for companies reporting under IFRSs to use reclassification amendments from 1 July 2008.

However, these changes were not without a political cost, particularly in respect of international standards convergence with the US. There was perceived to be a lack of due process in the IASB decision. This was particularly important as the FASB is working closely with the US to converge their standards in the so-called road map. This stems from the IASB/FASB Memorandum of Understanding after their joint meeting in 2002 and the Norwalk Agreement, which established the commitment towards compatible accounting standards. Each party acknowledged their commitment to the development of compatible accounting standards that could be used for cross-border financial reporting. This commitment to convergence was reaffirmed at the joint meetings in April and October 2005, aimed at producing a common set of high-quality global standards. In September 2008, the IASB and FASB issued a progress report and timetable for completion. Within a month the IAS 39 amendment had been approved, which re-emphasised the tension and the difficulties involved in achieving a single set of global accounting standards. It is also unclear what the attitude of other major global players, such as China, will be to the IASB's move.

Overall, therefore, the symposium came at a time of great political and economic upheaval. It was thus particularly interesting to have the views of five informed observers.

1. For a detailed review of fair value and its application to accounting measurement interested readers should see the FARSIG symposium 2008 discussion paper, *The Future of Financial Reporting 2008: Measurement and Stakeholders*, and in particular the symposium papers presented by Geoffrey Whittington and Richard Martin.

2. 'IASB amendments permit reclassification of financial instruments', 13 October 2008.

The Future of Financial Reporting in a time of Global Uncertainty

Ian Mackintosh, ASB

Informed by his role as chairman of the UK Accounting Standards Board, Ian's presentation was based on his insights about the present situation facing the accounting world, some possible responses to this, the potential scenarios that could unfold and their implications, and a review of UK GAAP in the future.

Ian outlined the present situation with a review of recent key events from August 2008 to date (January 2009).

August 2008
US announcement of SEC road map, being the first step towards the US adopting IFRS and the route to increasingly global accounting standards.

September 2008
Continuing credit crisis and falling equity markets put more pressure on financial reporting standards, with issues around financial instruments, capitalisation and the rise in political significance of accounting issues (such as fair value)..

October 2008
'Black Monday', IASB adoption of amendments to IAS 39 (and also IFRS 7) allowing some reclassifications in value relating to non-derivative financial assets, loans and receivables. The amendments were issued without the normal exposure draft process owing to the urgency stemming from market conditions and European Commission pressure.

October 2008
Further pressure on the IASB from the European Commission for further changes to IAS 39: fair value options (FVO), embedded derivatives and impairment. European pressure for faster change contrasted with the opposition already expressed elsewhere, such as by the US, to the lack of due process on IAS 39. This raised increasing objections from other constituents over the speed of change and the consultation process.

November 2008
SEC road map published, and a commitment made to make a decision by 2011 over whether to or not to adopt IFRS, but with no promises one way or the other. G20 pressure on IASB over global standards, valuation guidance and off-balance sheet issues.

Thus the backdrop to the current situation is one of reaction to events that are supported by some parties but resisted by others, either in terms of the proposed changes or whether due process was (or was not) followed. The European Commission demands more urgency with its continuing pressure for change, whereas the US and rest of the world is concerned about due process. In addition, the US is concerned with the longer-term issue of its position on adopting IFRS. The IASB has provided a range of responses to the present situation in response to requests from the European Commission and G20. This has included the IAS 39 amendments referred to above, valuation guidance, exposure drafts on consolidations, impairment disclosures, embedded derivatives, a proposed exposure draft on derecognition, and a fast-track project on fair value options. At the same, time there is also a concern for longer-term thinking on governance.

The result of this is a potential 'death-or-glory' scenario, summarised by Ian, as follows: 'I believe we are in a situation where the financial crisis the world is facing, and the pressures the IASB are having to deal with could ultimately lead to either the IASB securing its position as a long-term viable global standard setter [glory], or, alternatively, the demise of the present IASB as constituted [death]'. Four possible scenarios and outcomes were then presented.

Scenario 1:
Europe believes that the IASB has not responded appropriately and/or quickly enough, and seeks its own framework (a carve-out). Europe would no longer comply with IFRS and as a consequence the US would lose interest in adopting it, resulting in the demise of the vision of a global accounting standard. Alternatively, a better result for IASB would be that the US might persevere with its interest in adopting IFRS but, owing to its stance, Europe would become isolated over global accounting standard goals.

Scenario 2:
This is a more conspiracy theory formulated scenario. The G20 does not believe the IASB has responded appropriately to financial reporting issues. The outcome of which is that the G20 makes moves to take over, reconstitute or replace IASB.

Scenario 3:
The US decides not to adopt IFRS, at least not for the foreseeable future, and to stay with US GAAP. As a result, US and international GAAP remain – with the IASB battling on, working hard with other countries over IFRS adoption – with the possible isolation of US from global accounting goals.

Scenario 4:
The 'glory' scenario, where the IASB and FASB proposals on the credit crunch and the current financial crisis are accepted by the G20 and the European Commission and the US moves to adopt IFRS. This is the best result, and provides the long-term stability for global accounting standards after the credit crunch passes. This would represent an outstanding achievement for the present IASB and provide it with a more appropriate forum for political input to accounting issues. The IASB would then have the credibility and unity to examine how its future political influence could best be both ensured and used through due process and potential constitutional review.

The position of UK GAAP in the future was reviewed, based on the alternatives of death (scenarios 1 or 2) or glory (scenario 4). Assuming glory, following a six-month consultation period, IFRS would be extended to all publicly accountable entities. Based on what happens at a national level, micro entities may not need to report under IFRS at all, and small entities may retain the Financial Reporting Standard for Smaller Entities (FRSSE) which would be reviewed in due course. Those that are not micro, small or publicly accountable would report under IFRS for SMEs. At present, there is too much irrelevant disclosure currently required for subsidiaries under IFRS and this would need to be rationalised. The future for UK GAAP in the 'death' scenarios is clearly bleak, and bad news for the City of London as a global financial centre. The UK, possibly along with Europe, would be isolated from the rest of the world with the potential of the return of national standards in UK and European countries. Any idea of global accounting standards would clearly be ended.

QUESTIONS AND DISCUSSION

A range of issues was raised following the presentation. These have been summarised as follows.

- The reaction of China, India and Japan to current events: all of whom were concerned over lack of due process re the IAS 39 amendments. For Japan, there is a Memorandum of Understanding, and the IASB is moving ahead with this in line with a continued move towards IFRS global adoption if scenario 4 is the outcome.

- Whether it matters if there are differences in global standards, and the idea that competition between global accounting bodies is a good thing rather than not. The problem with this view is the current global disparities between the financial positions of companies across countries, and the consequent investment decision problems. While national standards bodies are important, they would still need to input into global standards.

- Increasing demands from Europe for changes in accounting standards, and the need to manage political pressure. Again under scenario 4, post-crisis the IASB would emerge as a strong body and a forum for due political input and management. If Europe were to be isolated, then the US may take the lead on international standards with the UK following.

- The role of the European Financial Reporting Advisory Group (EFRAG) advice on current and future technical issues, given the urgent adoption of the IAS 39 amendments without due process and consultation.

- The issue of reactive or proactive accounting changes and standards in the current global financial crisis and uncertainty. The problem with such crises is their unpredictability, and as a result changes tend to be reactive rather than proactive in nature. The dangers are those of over-reaction and the potential for political interference in such accounting changes.

Organisational Politics: the IASB, the FASB, the EU et al.

Peter Holgate, PricewaterhouseCoopers

Peter Holgate provided a practitioner and accounting professional insight into the current crisis, its implications for valuation, current reporting and going concern issues and his reflections on Ian Mackintosh's earlier presentation. He began his presentation by referring to the problems arising from the huge losses on financial assets with the associated problem of 'thin markets' lacking liquidity for normal trading of (financial) assets.

The consequent valuation and measurement problems arising from the 'thinness' of markets has added another, specifically accounting, dimension to the current problems. Owing to the market conditions, such transactions that have occurred have been at low prices, but these prices have been regarded as the best indicator of fair value. Applying these low benchmark prices has resulted in fair value losses elsewhere. This has led to criticisms of fair value. Some critics have argued for a retreat to historical cost. However, Peter argued that in the context of the current crisis we need even more (not less) fair value information on assets and liabilities.

There has not been a wholesale rush to abandon fair value, but a partial one; for instance, through the IASB's IAS 39 reclassification amendment. Deutsche Bank recently reported under this amendment. By using this reclassification, Deutsche Bank reported a profit, whereas without the reclassification a loss would have arisen. However, this is really a presentational change, as all the detail is still presented in the notes to the accounts. However, despite the adverse market conditions and limited application of the reclassification amendment, fair value continues in 99% of cases. In practice, the calls for the abandonment of fair value have translated into more disclosure, especially of impairment values.

The need for more disclosure and the impact of the crisis on the valuation and measurement of financial assets was highlighted by the IASB's new Exposure Draft, *Investments in Debt Instruments.* This would use twofold disclosure of losses on debt instruments – against amortised cost and against fair value. However, despite advocating more disclosure, the Exposure Draft was not supported for a number of reasons. First, the time for consideration and comment was limited to only a three-week exposure time, from 23 December 2008 to 15 January 2009. As well as worries over the abbreviated exposure draft time, there were concerns over the extended scope of the Exposure Draft, which had been widened to other debt securities ('scope creep'), and the practical difficulties of application. These difficulties would be even more pronounced if any revised standard were to be applicable immediately, that is, to 2008 year ends – indeed, such implementation would be almost impossible to achieve, as to collect the data in such a short time-frame appears infeasible.[3]

Peter then discussed what is currently happening in year end reporting and the issue of the going concern basis of preparation and its implications for the audit opinions. From a practice perspective, there is now a lot more scrutiny and detailed disclosures of the impairment of financial assets, property, plant and equipment and stock. The calculations and disclosures are not new but are particularly important in sectors such as construction where, if value in use (present value of cash flows) is being used, it becomes a very difficult exercise to estimate future cash flows and hence asset valuation.

With regard to the going concern basis for the preparation of accounts, if there are significant doubts then there is a need not only for detailed disclosure of these doubts by the directors, for instance, on refinancing assumptions, but also for directors and auditors to re-evaluate normal assumptions of going concern where appropriate. Going concern questions are occupying firms and the profession in general. One major issue with any question of going concern in the audit opinion is the impact on future financing for the business. This is thus a very sensitive issue given that it could affect the firm's ability to raise future finances in an already difficult market. In the financial sector and elsewhere auditors are drawing

3. Post-event note: in recognition of these difficulties, the IASB withdrew these proposals later in February 2009.

attention to the directors' disclosure on the availability of financing and of the company's ability to meet any financing needs for the foreseeable future (12 months).

Finally, Peter made a few remarks on Ian Mackintosh's commentary. Ultimately it is difficult to predict which of the four scenarios will be realised. Looking at the 2011/12 world map of countries that would potentially adopt IFRS – the EU, Central and Eastern Europe, China, Japan, South Korea, India, Canada, the Middle East and much of South America – it is possible that the current dominance and power of the IASB board of the US and EU would be watered down. It is possible that we could see the US retreat into isolation. If we look back a few years, Europe was the main power bloc using IAS. If we look forwards, however, we can envisage IFRS being used in most of the world. The more countries sign up to IFRS, the more the influence of the EU and the US declines. Over the last couple of years fewer companies have been seeking to list on the US market as foreign private issuers. This has demonstrated the relative unattractiveness of the US market and its potential decline in power against other global markets.

Looking back on our current times, it may be that we will conclude that we were naive in saying that a private body, the IASB, could set itself up as a world body and operate without political interference. It is hard to find other examples of successful private sector, non-governmental international bodies. The IASB has now become more engaged politically, and it will need to manage this process of engagement to ensure that it remains connected to the political process but still is independent and respected for that.

QUESTIONS AND DISCUSSION

Issues were raised around going concern, accounting principles, and theory and practice, as well as further reflections on Ian Mackintosh's earlier presentation.

- There was concern that deciding on the appropriateness of going concern was now placing a ridiculous burden on auditors. Thus, in the current financial situation, what would be wrong with including a going concern modification in the audit opinions of all companies?

  This suggestion was viewed as unrealistic. For a number of companies, the directors are (too) optimistic. They think they have a mixture of new financing and asset sales in place. They think they will be all right for the foreseeable future, and thus the going concern basis of preparation is appropriate. However, banks may not be as willing to provide financing as the directors had hoped; also it may be harder than expected to sell the assets in question. Is the board properly disclosing to shareholders the issues and assumptions regarding future financing? Thus it is important that auditors are not only content with the assumptions used by the board in preparing accounts on a going concern basis, but also recognise the need to evaluate the assumptions given the current financial situation. It is not easy, but professional judgement must be exercised and, if necessary, going concern issues will have to be referred to in the auditor's opinion if there are material uncertainties or disagreement about the basis on which the accounts have been prepared.

- A question was raised concerning practice as against principles. In the term 'GAAP', the 'P' means 'Practice' in the US, but in the UK it means 'Principles'.

  Peter expressed his personal view that he favoured principles applied with judgement. The role of a profession is to exercise judgement. The US profession has problems because it has been brought up using rules; but standards should be based on principles, not on rules, and the use of professional judgement in their application.

- Is the gap between theory and practice getting bigger, especially because of impairment?

  Practically speaking, impairment calculations are very tricky, but the underlying principles are sound. Peter's auditing colleagues think the standards are too theoretical and they criticise fair value in some circumstances. While fair value disclosure is sensible, often the presentation is very difficult, too volatile, not realistic, with data not easy to assimilate; for instance, the Exposure Draft on Debt Instruments referred to earlier. Is the current financial reporting system really broken? The amount of potential future disclosure may also be in danger of getting out of hand, leading to a revamping of financial statements and questions over their usefulness.

- Finally, reflecting on Ian Mackintosh's presentation (will glory prevail? – scenario 4).

  It is quite easy to see that the IASB is caught between a rock and three or four hard places. If we look forward a few years, we can easily imagine the US and Europe, China and others all lobbying the IASB, seeking to retain their own positions of influence. In the period 1970–1990, the standards issued by the UK Accounting Standards Committee had to be approved by all six of its sponsoring professional bodies, and any of them could reject its standards. This could happen on the international stage, and the result may be potential fragmentation of international standards on national lines.

Asset Securitization, Fair Values and the Credit Crunch

Ken Peasnell, Lancaster University

Ken's presentation focused on the current credit crunch, the issues around asset securitisation and whether accounting and financial reporting were in any way to blame for the current situation. This discussion may also serve to achieve a sense of proportion about the issues underpinning the crisis. Ken commenced the presentation with an appropriate quotation: 'when you see a depressed and lonely old man staggering away from his local turf accountant, re-lighting half a rolled up cigarette…you can comfort yourself with the knowledge that (a) at least it was his own money that he wasted, and (b) at least the horse he blew it on actually existed. Neither of these consolations applies to failed banks'. (Zaltman 2008) The lessons learnt from this quotation relate to the creation of derivative products, increased levels of risk, and undue confidence in past market conditions and returns.

The crisis itself is a macroeconomic phenomenon caused by a long economic boom, surging house prices and low central bank interest rates, all of which encouraged increasing levels of lending and resultant corporate and private household debt. As lending rose, banks increasingly financed this using the wholesale money markets backed by asset securitisation (such as on property), on the assumption that the growth in the value of the underlying assets would continue. These boom conditions resulted in a situation of over-confidence, increasing levels of risk and the growth of more dubious business dealings. However, proportionally, the American sub-prime mortgage market represented only a small percentage of total global debt, which made the crisis that did arise all the more unpredictable. Indeed, it represented the confluence and summation of a number of factors, including those mentioned above, and was not the result of sub-prime lending alone. When this is understood then the challenges facing the IASB in supporting the role of financial reporting in re-creating trust in the banking system are evident.

The key points about asset securitisation and its growth were then set out. First, what led to the development of asset securitisation? Factors included: banks seeking additional finance vehicles to back lending; investors' appetite for derivative products; regulators seeing this as a way of spreading risk; and governments as a way of financing increased levels of home ownership.. However, the risk behind asset securitisations took on unexpected forms. Good lending practices and financial prudence were driven out by more risky lending on the assumption of rising asset prices used to back loans. Risk was viewed as being spread by primary and secondary investment in securitisations; but this is not the same as risk being managed, so a growing false comfort resulted, with investors more and more unable to ascertain the real quality of the underlying assets and the actual credit rating of secondary securitisation products.

Along with unreliable credit ratings, there were other factors that also contributed to problems in asset securitisation: bank bonus schemes that encouraged excessive risk taking; lack of prudential board governance and management; as well as the huge growth of credit default swaps (c. $60 trillion). Hedge funds had invested in the riskiest tranches of securitisations, typically hedged by short positions in the ABX index. As the sub-prime problem became evident so the market feared the continued ability of securitisations to meet returns. This resulted in a collapse of the securitisation market, and the consequent funding crisis for banks that were dependent on that market for their own financial position.

So amid this market turmoil what, if any, was the role of accounting in the crisis? First, in the US, did the off-balance sheet treatment of securitisations mean that

transparency was impaired? (It should be noted that in the UK, for instance, Northern Rock's securitisations were on balance sheet.) However, did the fact that US securitisations were generally off the balance sheet delude investors? Research by Landsman et al. (2008) suggests it did not. Ken outlined that the research which consolidated SPEs [Special Purpose Entities] for 112 US firms, found that the weights attached in a residual income pricing model to the securitized assets and liabilities were no different to those for assets and liabilities already on-balance sheet. Other evidence also supports the view that the securities markets are mature and sophisticated enough correctly to value businesses, including any securitisations (see, for instance, Nui and Richardson 2006; Chen et al. 2008).

Second, and a key problem highlighted by the crisis, under regulatory rules such as Basel I and II, capital definitions start with accounting numbers. Thus, there appears to be a greater need to change the regulations rather than to blame the accounting that results from the implementation of such regulations. Look at the causes of the issue rather than the symptoms.

Qualifying Special Purpose Entities (QSPEs) were then outlined, noting the way in which they had been used, and consequent valuation issues within the crisis. QSPEs were meant to be purely passive pass-through vehicles for SPE security holders. However, QSPEs were increasingly used to handle complex bundles of securities (including derivatives) that required active management and financial support. Indeed, many SPEs had to be rescued by their originators, with SPE assets and liabilities ending up back on the balance sheet as a result, raising the question of whether they had actually been sold or loaned in the first place. Given their on balance sheet treatment, how were such SPEs to be valued? It is clear that property-backed financial assets lost value as the property and securitisation markets fell. However, fair value estimation becomes very imprecise in a now illiquid market suffering from the credit crunch, 'a fair value level 3 world' (no observable market data). In such an illiquid market even with observable data (levels 1 and 2), critics of fair value argue that true value is then understated and losses overstated because fire sales act as a market benchmark price on which other similar asset values are based.

The IASB response to this was encapsulated by its actions in October and December 2008. On 13 October 2008, amendments to IAS 39 and IFRS 7 permitted reclassification of certain non-derivative financial assets out of the profit or loss category, to be accounted for at cost (and thus left on the balance sheet), and the transfer of certain available-for-sale financial assets to loans and receivables. Readers should also refer to the previous commentary on Ian Mackintosh's presentation. On 22–23 December 2008, additional amendments to IAS 39 and IFRIC 9 were as follows:

- To require an embedded derivative to be separated out from a host contract when a hybrid financial asset is reclassified out of fair value through profit or loss.

- If the fair value of the embedded derivative cannot be reliably measured, then the entire instrument cannot be transferred

- Additional disclosures about the effects on profit or loss of using fair value and amortised cost for debt instruments, other than those included in fair value through the profit or loss category.

The issues challenging accounting at present are concerns over fair value application and whether it serves in a crisis to understate assets and overstate losses/liabilities. However, the stock market does not appear to believe that fair value is understating asset values, as the shares of 59% of all banks listed in the US were trading in November 2008 at less than their book value. Clearly fair value does work best when securities are traded in transparent, liquid markets with readily known prices, but that is not the case at present in a climate of uncertainty and forced sales. Overall perhaps, this issue needs to be set against a background of the still-primitive development of conceptual models of measurement within accounting.

Finally, the presentation then considered measurement issues and the importance of correlations in measurement errors. 'Earnings' is the difference between two numbers (book value at T_0 and book value at T_1) over a time period, and so correlation matters. The variance in income is found by:

$$\text{var (income)} = \text{var}(BV_0) + \text{var}(BV_1) - 2\text{cov}(BV_0,BV_1)$$

A simple worked example of uncorrelated errors and its impact was given, where measures are unbiased and independent (and so covariance is zero), but can vary by +/-10%, with equal probability starting at 100 at time T_0.

Book Value T_0	Book Value T_1
90	108
100	120
110	132

This gives us three earning situations as follows:

Earnings
Max loss = 110 at T_0 to 108 atT_1 = -2
Max income = 90 at T_0 to 132 T_1 = +42
'True income' = 100 at T_0 to 120 T_1 = +20

Thus a balance sheet error of 10% has resulted (and magnified) in an income error with a standard deviation of 63%. If errors are positively correlated across time, however, then the income error would be reduced. The new disclosures will present many opportunities for this to be researched in greater depth!

In conclusion, Ken Peasnell maintained that the nature of the current crisis poses no new issues for financial reporting, and is essentially a fundamental problem of bank regulation, governance and management. However, given the challenges that face accounting, such as those around fair value, the IASB and FASB will need steady nerves as they are faced with demands for change in response to the crisis.

QUESTIONS AND DISCUSSION

The questions were mainly concerned with asset value and the underlying securities markets.

- Are securitised losses currently over-estimated? Ken stated that clearly there is an economic risk of this owing to the current uncertainty and the difficulties of establishing valuations of derivatives resulting from swap defaults and counter-party risk positions. However, even if there is short-term market error, this will be corrected in future, with resultant gains.

- The issues of incentives around bank profit and share price and taking increased levels of risk were raised. Ken stated that the risks had been thought to be appropriately managed but, owing to more complex counter-party risk and the falling property markets, both the risk and market assumptions became unrealistic as the crisis developed.

- The failure of the securities market function to provide accurate valuations for equity investors and other debt claims. Ken believed that while this may be a short-term issue, the long-term position is that securities markets are mature and sophisticated enough to provide accurate values for financial products and furnish accurate corporate valuations.

The International Spread of International Financial Reporting Standards (IFRS): Challenges and Opportunities

Alan Teixeira, IASB

The views expressed by Alan in his presentation are based on his own personal reflections concerning global accounting standards, as a member of the IASB. The presentation covered three main aspects, namely: the benefits and challenges of global standards; the FASB-IASB Memorandum of Understanding (MoU); and a review of the credit crisis, specifically the reclassification process re IAS 39, and the steps that were taken in relation to this.

One of the main benefits of global standards is that of the consistency of financial reporting. Global standards are viewed as fundamental to achieving a high-quality global financial reporting system, which in turn results in increased transparency. This facilitates investment, and reduces both the cost of capital and overall reporting costs. The move towards creating a global platform has gathered momentum, with the establishment of, inter alia, the IASB in 2001; EU adopting IFRS in 2002; Australia, New Zealand, Hong Kong and South Africa committing to adopt IFRS in 2003; and, in 2006, a Memorandum of Understanding (MoU) between the FASB and the IASB.

By January 2009, IFRSs are used by listed entities in over 110 jurisdictions, and by unlisted entities in over 80 jurisdictions. More telling data about the adoption of global standards are provided by Fortune Global 500 reporting data from July 2008, and by comparing these data with forecast reporting to 2012, based on companies' announced plans. Using this data, at present 39% of Fortune Global 500 companies report using IFRS or IFRS equivalents, and this is forecast to rise to 49% by 2012. Thirty-one per cent currently use US GAAP and this is expected to remain at this level, and a further 31% currently use national GAAP which is forecast to reduce to 21%. This marks a shift away from national GAAP towards IFRS by 2012. As regards the US adopting IFRS, in November 2008 the SEC proposed its 'road map', with early adoption available to a limited group of companies by 2009, and with a decision in 2011 as to mandatory adoption of IFRS in the period 2014–16. This would be conditional on progress on the FASB-IASB MoU, IASB funding infrastructure and experience to date in the US. Thus adoption will be influenced by progress on current projects and is therefore tied up with issues arising out of the current credit crisis, which formed the third part of this presentation.

An ideal global standard would be the full adoption of IFRS as issued by IASB as the reporting framework, with the audit report confirming conformity to IFRSs without any localised endorsement. The overall vision is that of a single set of high-quality global accounting standards. This may be difficult to achieve, however, owing to local endorsement issues, local adaptations, translations and enforcement. Such issues may give rise to concerns as to what standard(s) the audit report should then refer to, and whether users would fully understand the nuances of full IFRS adoption against any localised versions and adaptations used in financial reporting.

Alan then addressed the issue of adoption versus adaption of IFRS and the use of 'jurisdiction equivalents'. Does adaptation really mean full adoption, the ideal scenario, or are there national variations which potentially would be a move away from true global standards? IFRS adaptation refers to cases where word-for-word adoption is not used. Local adaptations of IFRS are made and, consequently, the entities applying these are not conforming to true IFRS, despite their jurisdictions contending that such adapted standards are 'IFRS equivalent'. This problem does not relate to differences in effective date or other transition

arrangements which may be necessary for full adoption. Some jurisdictions can only adopt IFRS by law, and by their nature laws are hard to update and time consuming in process. This problem may also arise even when local professional bodies adopt IFRS word for word. The slow process of adoption was highlighted by the examples of time lags relating to IFRSs and IASs not yet endorsed in the EU including, among others, IFRS 1 and IAS 27, IFRSs 2 and 3, which were published in January 2008 and not yet endorsed, and IASs 1, 23, 27 and 39. Even with word-for-word adoption there may be difficulties; for example, where the audit report and the basis of accounts preparation in the accounting policies note still refer to national financial reporting standards. In such a case, all the hard work of adopting IFRS has been carried out without realising the benefits, and the financial reports may not necessarily be recognised as IFRS-compliant in other jurisdictions.

Alan then highlighted two other areas of complication: namely translation and enforcement issues. Translation issues arise from differences between the official translations of the IASCF and local unofficial translations, and the context of standards in different languages. For instance, in Germany the same word is used for amortisation and depreciation; and for Spanish-speaking countries, should Continental European or Latin American words be used? Can enforcement be rigorously and consistently applied across all jurisdictions? And what are the consequences of non-compliance and enforcement? Finally, Alan drew attention to the World Bank ROSC reports (Reports on the Observance of Standards and Codes (www.worldbank.org/ifa/rosc.html), the results of which suggest that for many countries compliance in the early stages of adoption is not uniform.

The second main aspect of the presentation related to the FASB-IASB MoU. The current crisis has forced greater focus on the core issues, which is to be welcomed, with the detail/minutiae to be dealt with later. Overall, the MoU will lead to an aligned conceptual framework. In the short term, the focus is to remove selected differences in current accounting standards, and in the medium term to issue new joint standards where significant improvement on current standards is required. The intention is to ensure that during the process of convergence standards will be developed in line with this longer-term goal and will not need to be changed twice. This could happen if short-term changes to standards were to be made without considering the overall aim of convergence.

The MoU sets out the convergence programme between the IASB and the FASB. The short-term projects were to be completed by 2008, with convergence scheduled for 2011 when the decision for mandatory adoption (as set out earlier) is to be made. Both the FASB and the IASB are providing ongoing guidance and time-frames for the completion of the MoU. A sequence of MoU milestones were then presented, highlighting the project area, progress towards milestones, the work done to date and the expected future work. A number of specific examples of these are set out below.

Project	Milestone	Work done	Expect
Financial statement presentation	2011 converged requirements	Preliminary Views Document (PVD) and Discussion Paper (DP) issued	Exposure Draft (ED) in 2010
Fair value measurement guidance	2010 converged guidance	SFAS 157 and DP Fair value Measurements issued	IASB ED in first half of 2009
Financial instruments	2011 converged requirements	PVD and DP on complexity issued and FASB ED on hedging issued	
Consolidation and SPE	2010 converged requirements	FASB EDs revising FIN 46R and FAS 140	IASB ED
Post-employment benefits	2011 converged requirements	SFAS 158 and DP issued	IASB ED in second half of 2009

The outcome of convergence under the MoU is for continued cooperation, bringing a closer alignment of principles and development of shared standards in those areas needing improvement. Standards would be based on principles, not rules, and tied to the conceptual framework.

It was apt that the final part of the presentation examined the problems caused by the current financial situation in relation to convergence, and the tensions arising from conflicting interests, such as US and European Commission (EC) pressure. The key issue identified was the reclassification out of fair value, and the events of October 2008 and the IAS 39 amendment. Readers should also see the issues raised by Ian Mackintosh and Ken Peasnell in their presentations.

The continued credit crisis brought increasing demands for reclassification from Eurogroupe (group of euro currency member states) and ECOFIN (the Economic and Financial Affairs Council) during the period 4–7 October. ECOFIN is a body of the Council of the European Union and composed of the economic and finance ministers of the member states, and meets on a monthly basis. On 9 October, the IASC Foundation trustees supported the accelerated steps to be taken by the IASB. A seven-day ED was initially planned, but increasing European pressure led to a straight amendment in order to prevent an EC ‘carve-out’. On 13 October, the IASB issued revisions to IAS 39 and IFRS 7 Reclassification of Financial Assets. Owing to EC pressure and the urgency of the situation there was no time for consultation, and on 16 October the endorsed standard was published in the EU, following positive advice by the European Financial Reporting Advisory Group (EFRAG) and a unanimous Accounting Regulatory Committee (ARC) vote. The ARC is composed of representatives from member states and chaired by the

European Commission. As a result of reclassification, appropriate full disclosures will be necessary to fully inform investors. The reclassification does, however, address one difference between Europe and the US, but does not create a level playing field with US GAAP. There are so many other differences between IFRSs and US GAAP in relation to financial instruments that the longer-term convergence goals will only be met when we have common standards. Although this period is clearly unusual and drastic measures were taken, the longer-term core agenda of convergence still remains and the next few years will be crucial in achieving progress over this.

QUESTIONS AND DISCUSSION

There were a number of questions raised around the sustainability of the convergence framework in the light of the current crisis.

- The impact of the current crisis on short-term and longer-term projects and the need for reflection and transparency. Two main aspects were highlighted. First, the need to race ahead with some short-term projects to restore market confidence; and second, the requirement to take a longer and more reflective view on issues such as the conceptual framework.

- Concern over the achievability of the ideal standard of adoption and the pragmatic need for adaption of IFRS. While adoption may be the ideal, how many times has this been fully achieved in practice? Often, adoption will be nearly achieved but then there may be a change of name, or other detail, which results in adaption. One solution may be to make adaption more difficult, in order to try and force full adoption of standards, but this would depend on the solidity and stability of the whole framework.

- Another real difficulty concerns the availability of reliable empirical data on which to base adoption of global standards. For instance, in relation to joint ventures, how many European joint ventures are currently in existence and what is their aggregate economic value, regardless of how that is measured? If there is a lack of such data it is difficult to identify the extent to which there are underlying differences in accounting – the starting point for trying to achieve a global change in practice.

Corporate Governance and the Credit Crunch

Paul Moxey, ACCA

Paul Moxey, Head of Corporate Governance and Risk Management at ACCA presented an overview of the credit crunch. He discussed its root causes, stating that a main cause is poor corporate governance. To explain this, he looked at ten principles of good corporate governance developed by ACCA's Corporate Governance and Risk Management Committee.

The last few years saw an unprecedented growth in the size and profitability of the global banking industry. According to McKinsey (2008), global banking profits in 2006 were $788 billion (over $150 billion greater than the next most profitable sector: oil, gas and coal). Global banking revenues were 6% of global GDP and its profits per employee were 26 times higher than the average of other industries. Some maintain that such profitability is due to regulatory anomalies (ie lack of competition, asymmetry of information, and externalities such as state support in times of trouble). The governmental rescue package has been put at $2 trillion. The cost to the global economy may be many times greater.

ACCA has met with groups of experts and identified several root causes of the credit crunch, including:

1. failure to manage the link between business risks and remuneration incentives
2. excessive risk taking and short-termism resulting from remuneration structures and bonuses
3. risk management departments clearly lacking influence and power
4. weaknesses in reporting on risk and financial transactions
5. poor oversight by senior executives, and lack of challenge by independent non-executive directors
6. a general lack of accountability.

These factors, combined with imperfections in regulation and monetary policy, led to an excess of money supply and, ultimately, to the market dislocation. Further contributory factors were:

1. product over-complexity and lack of managerial understanding of the associated risks
2. excessive leverage
3. interconnectedness of financial institutions
4. misalignment between the interests of the different parties involved in complex financial products
5. complacency after a prolonged bull market
6. failure to appreciate cultural factors, such as human greed.

Previous financial episodes – such as the savings and loans bank crisis in the US in the late 1980s, the East Asian crisis in the late 1990s and the failure of Enron and WorldCom – taught us the importance of sound corporate governance and risk management. We did not learn the lessons in the past: we must do so now.

ACCA's *Corporate Governance and Risk Management Committee Agenda* contains 10 principles of good corporate governance. The principles are set out here in the order given in the presentation, and are therefore not in numerical order (further, not all of the principles are detailed in this commentary). For a detailed discussion of all of the principles readers should refer to the ACCA Discussion Paper, *Corporate Governance and the Credit Crunch* (2008).

PRINCIPLE 1

> *Boards, shareholders and stakeholders should share a common understanding of the purpose and scope of corporate governance.*

Good corporate governance is about boards directing and controlling organisations in the interests of long-term owners and accountability.

PRINCIPLE 2

> *Boards should lead by example. Boards should set the right tone and behave accordingly, paying particular attention to ensuring the continuing ethical health of their organisations.*

This embraces the impact on their employees and on the wider society. While bank boards owe their primary duty to their shareholders, they also have obligations to other stakeholders (eg their borrowers, employees and savers).

PRINCIPLE 3

> *Boards should set clear goals, accountabilities, appropriate structures and committees, delegated authorities and policies. They should provide sufficient resources to enable executive management to achieve the goals of the organisation through effective management of day-to-day operations and monitor management's progress towards the achievement of these goals.*

A fundamental role of a board is to provide direction, control and monitoring. The non-executive directors of Enron and WorldCom failed to discharge this obligation. Reforms, such as the US Sarbanes–Oxley Act, the EC Corporate Governance Action Plan, and the Higgs and Smith reports in the UK are intended to address this failure.

PRINCIPLE 6

> *Executive remuneration promotes organisational performance and is transparent. Remuneration arrangements should be aligned with individual performance in such a way as to promote organisational performance.*

Performance schemes must be based on sound principles and applied properly. The incentive and career structure packages of banks meant enormous rewards, discouraged prudent risk management and worked against the interests of other stakeholders. Risk management, remuneration and incentive systems must be linked. Transactions with high-risk profits should trigger smaller bonuses than similar less risky projects and profit streams. Risk management should be linked with remuneration incentives. The status of risk managers should be raised and they should advise the remuneration committee.

PRINCIPLES 8 AND 9

> *Boards account to shareholders and, where appropriate, other stakeholders for their stewardship* [and] *shareholders and other significant stakeholders hold boards to account.*

Shareholders have limited ability to influence companies they own. Executive managements have therefore extracted increasingly larger proportions of corporate earnings. In addition, dispersed shareholdings create a fundamental governance challenge, exacerbated by the emergence of new strategies (eg derivatives) for participating in corporate profitability. The receipt by boards and shareholders of appropriate, clear and reliable information on risk and financial results will help to address both challenges.

PRINCIPLE 4

> *Boards ensure their strategy actively considers both risk and reward over time. Consideration of risk should be a key part of strategy formulation. Risk management should be embedded within organisations so that risk is considered as part of decision making. Boards need to understand the risks faced by the organisation, satisfy themselves that the level of risk is acceptable and challenge executive management when appropriate.*

Banks have highly sophisticated risk-management functions, yet recent events have illustrated their weaknesses. The Swiss bank UBS reported write-downs of $38 billion in 2008. Its explanation to its shareholders provides a clear and fascinating example of risk management failings such as the danger of having silos within organisations.

Credit ratings also seem to be widely misunderstood.Many investors bought 'AAA'-rated instruments with little or no further consideration of risk, thinking that such investments were totally 'safe'.

A low-inflation environment stimulated a desire to look for new ways to generate yield (eg derivatives). Huge increases in computing power added to complexity by generating many more transactions and, thereby, apparently deep markets. Chief executives of banks may have had insufficient understanding of these new products. Combined with this complexity, traders were given free rein. The newly created yields, helped by the apparent safety of AAA ratings, may have mesmerised top management.

Accounting for risk is a primary driver of capital value. Present prices, showing points rather than ranges are not always good indicators of future asset values. Many of the risk management tools, such as value at risk, assume an 'efficient' market predicated on the existence of normal distribution, which is not always the case.

PRINCIPLE 7

The organisation's risk management and control is objectively challenged, independently of line management.

Boards and their audit committees receive a massive amount of information on risk, and not all of it is useful. The information is rather like pieces of a jigsaw puzzle. Unfortunately, the audit committee does not have the box with the picture of the puzzle on it; nor does it know how many pieces there are; nor whether all the pieces are from the same puzzle. It is also tempting for managers to make sure that information prepared for non-executive directors does not raise too many difficult questions.

Internal auditors must be both objective and independent. To ensure their independence, they must not have any line or management responsibilities. Internal audit should include both risk management and the board's oversight of risk. Internal auditors should report to the non-executive audit committee chairman rather than to an executive. Audit committees could find their job easier if they had access to a dedicated function, separate from internal and external audit, bringing together all the sources of information to create an overall assurance picture.

At a recent debate held by ACCA, IFRSs were said to have added to the complexity and length of reports, but not to their clarity or ease of understanding. Accounts do not differentiate between price and value and nor provide a proper snapshot of either. The price of the UBS write-downs was calculated in early 2008 as $38 billion but these are not actually losses. It is also unclear whether the accounts of the banks which recently posted large write-downs have overstated profits in the past, or whether the write-downs and losses genuinely reflect a changed business environment.

The use of fair value can lead to some odd results. Concerns about a bank's credit worthiness concerns can reduce the 'fair' value of a bank's own debts. Strangely, a bank can even report a 'profit' on the reduction. A KPMG report (2008) noted that twelve European banks recognised such gains in 2007 (the largest such gain being £1.5 billion). For three banks this was more than 12% of pre-tax profit.

Recent events have highlighted the fragility of financial institutions. Banks, by their very nature, borrow short and lend long. Few banks can withstand a sustained run on their deposits. Preparing accounts on a break-up basis, or with a going concern qualification, would not help and could itself precipitate collapse. However, the fact that auditors have not qualified failing banks' financial statements is of concern to users, who need to know whether an organisation will continue as a going concern.

The credit crunch has posed other challenges for accountants. It may be time to take a more fundamental look at accounting by asking some basic questions.

1. What is the purpose of accounts? Is it to reflect an accurate picture of the past, inform the present, or help predict the future?

2. Is a set of accounts expected to do too many things? What responsibility do accountants have for the use of accounts?

3. What are the expectations of users? Are they realistic in the light of the credit crunch?

4. Should accounts pay more attention to cash?

5. If accounts are to reflect risk, should they also reflect the underlying probability or confidence?

6. Which information on risks should be communicated?

7. How can the complexity of accounts be reduced and their comprehensibility and value to shareholders enhanced?

8. Is there an expectation gap with regard to audit reports? For example, do people expect an unqualified audit report to mean that a company will remain a going concern?

The banking sector has a social function. It has a licence to operate from society and so is regulated. Regulation strongly influences bank operations, market forces and profitability.

Under the Basel Accord, capital requirements change according to the perceived quality of an institution's assets. The business cycle means that a lowering of asset quality tends to occur at the same time as a lowering of capital through losses. Banks, therefore, need more capital

at the very time that they have less. Assets are also reduced, so worsening the credit environment (ie the 'pro-cyclicality effect'). Basel II arguably increased pro-cyclicality. Inconsistencies in capital regulations encouraged banks to use off- balance sheet vehicles to lower the required regulatory capital. The credit crunch revealed that, because of reputational risk or liquidity recourse agreements, these off- balance sheet vehicles were still organisational liabilities. We need to explore appropriate banking balance sheet and capital requirements.

Basel II considers assets rather than liabilities and we probably need to consider liabilities more. Under IFRS and fair value accounting, price changes feed straight through to reported profits and capital requirements. This can reinforce pro-cyclicality.

We are in danger of having a system that allows profits to be retained in the private sector yet requires losses to be met by the public. This is clearly unacceptable, but finding a solution is challenging. ACCA does not claim to have a ready answer, but believes a solution will be easier to find if greater attention is given to the bigger picture and, in particular, if we ensure that organisations are properly governed, risks are more prudently managed, and accounts and related disclosures are clearer.

More detail on the corporate governance and risk discussion is provided in the ACCA discussion paper *Corporate Governance and the Credit Crunch*. Other relevant ACCA Publications are *Climbing Out of the Credit Crunch* and *Sure Enough to be Unsure? Questions for Audit Committees Thinking about the Credit Crisis*.

QUESTIONS AND DISCUSSION

Various questions were raised at the end of the presentation and are grouped below.

- What positive incentives do directors have to do a good job and discharge governance in an appropriate way? From a shareholder perspective, a director may not be acting in the interests of the shareholders and fail fully to discharge governance requirements, but may nonetheless make big profits.

  How should people within organisations be remunerated? Which incentives should drive businesses? (For example, in the management of credit risk sales representatives and organisational incentives may not be congruent.) It is extremely difficult to be a representative for shareholders and other stakeholders at the same time. In the UK, we recognise stakeholders but have not gone overboard in terms of regulatory change. In the current situation, it is hard to find either board directors or experienced risk managers. The definition of risk appetite is very hard to define and manage at all levels within an organisation.

3. Discussion

These five papers were presented in January 2009, against the backdrop of the credit crunch and of continuing and persistent criticism of accounting measurement policies, in particular the role of fair value. Each presenter took a different approach to this issue. Peasnell provided an academic view; Holgate gave a practitioner insight; Mackintosh gave insights from a national standard-setting perspective, while Teixeria provided an international overview from the IASB. Finally, Moxey gave a summary of a professional institute's views, namely ACCA. A brief précis of their presentations is provided before a comparative overview of the five presentations.

KEN PEASNELL

Peasnell's presentation tackled key issues of the current crisis: asset securitisation, fair values and the credit crunch. He also focused on accounting and financial reporting's role in this crisis. He stated that the crisis itself was a macroeconomic phenomenon caused by, inter alia, surging house prices and low interest rates. This led to increased lending which the banks financed through the use of, and reliance on, wholesale money markets backed by asset securitisation. The economic boom led to over-confidence. Asset securitisation was achieved by the banks seeking new finance vehicles to back lending and the development of more complex derivatives. Bad lending practices drove out good. Risk was spread rather than managed. The real quality of underlying assets and actual credit ratings deteriorated. Lack of prudential corporate governance, bank bonus schemes and credit default swaps also contributed to the potential sub-prime problems. Eventually, the securitisation market collapsed, causing a funding crisis.

Peasnell then investigated the issues relating to accounting. First, in relation to off-balance sheet financing, he observed that Northern Rock's securitisations were on balance sheet. He cited academic research in the US (eg Landsman et al. 2008) to show that the securities markets were mature and sophisticated enough to value businesses. Second, in terms of the regulatory framework, under Basel I and Basel II capital definitions start with accounting numbers. Therefore, accounting was a symptom and not a cause of the crisis; thus he blamed the regulations per se, rather than accounting, and was therefore of the opinion that the focus for change should be on regulation. Third, Qualifying Special Purpose Entities (QSPEs) were set up as possible financing vehicles for SPE holders. Increasingly, however, they handled complex bundles of securities (including derivatives) requiring active management and financial support. Many SPEs had to be rescued: raising doubts as to whether the original assets had been 'sold' or 'loaned'. So how should these property-backed assets be valued, given that they have lost value? In a fair value world, fair value estimates become imprecise in illiquid markets, with fire sales acting as market benchmark prices. Peasnell pointed out that the IASB response was to allow some reclassifications of certain non-derivative financial assets out of profit and loss to cost. In Peasnell's view, the stock market does not believe fair value understates asset values, as 59% of US banks were trading in November 2008 at less than book value. Peasnell then gave a numerical example of uncorrelated errors, showing that a balance sheet error of 10% could result in an income error with a standard deviation of 63%. Overall, therefore, Peasnell presented the potentially controversial view that the current crisis posed no new issues for financial reporting and is essentially a fundamental problem of bank regulation, governance and management.

PETER HOLGATE

Holgate investigated the credit crunch crisis from a professional firm's perspective. He pointed out the problems arising from huge financial losses on financial markets with 'thin markets' that lacked liquidity for normal trading. These transactions at low prices have caused fair value losses. This has led to criticisms of fair value. However, Holgate thought we needed more rather than less fair value information on assets and liabilities. There had been a partial abandonment of fair value by companies such as Deutsche Bank which reported a profit through reclassification rather than a loss. However, fair value continues to be used in 99% of cases.

The IASB's new Exposure Draft, *Investments in Debt Instruments*, issued in December 2008, highlighted the need for more disclosure. However, the short time period for discussion and its extended scope led to a lack of support. The financial problems have led to a lot more scrutiny and detailed disclosures on the impairment of financial assets, property, plant and equipment and stock. There is also widespread concern with going concern as the basis for the preparation of accounts. Negative audit opinions might well have effects on businesses' ability to obtain future financing. Holgate also commented on the world of potential IFRS adoption by 2011/2012. He thought that the current dominance of the US and EU would be watered down as more of the world adopted IFRS. Already, fewer foreign private issuers were listing on the US market. He also thought that it is hard to find examples of successful private sector, non-governmental bodies such as the IASB. The IASB will need to manage a policy of political engagement, given its recent profile, and will also need to protect the integrity and independence of financial standards.

IAN MACKINTOSH

Mackintosh outlined a number of potential scenarios for standard setting, and the role of UK GAAP in the context of current world events in accounting. He first outlined some key recent events: August 2008, the US announcement of a road map; September 2008, the continuing credit crisis and falling equity markets; October 2008 'Black Monday' when amendments to IAS 39 were adopted without following due process and under pressure from the European Commission; pressure from the European Commission on fair value options; November 2008 US promises to make a decision on IFRS adoption by 2011. There is currently a difference in approach to standards setting: the European Commission demands urgent change while the US and the rest of the world want due process. The US is also concerned about its future potential adoption of IFRS. Meanwhile, the IASB provided a range of responses to the present situation.

As a result of this Mackintosh set out four possible scenarios. In scenario 1, Europe believes the IASB has not responded adequately and seeks an EU ‘carve-out’. The US would then either lose interest in IFRS, or persevere thus isolating Europe. Under scenario 2, the G20 believes the IASB has not responded appropriately and makes moves to replace it. Scenario 3 sees the US isolated from IFRS, choosing non-adoption. Both regimes, US GAAP and IFRS, remain, with IASB continuing its efforts to win over the rest of the world. Finally, Mackintosh presented the ‘glory’ scenario – scenario 4, where IASB and FASB proposals on the credit crunch are adopted by the G20 and the European Commission, and the US moves towards adoption. The position of UK GAAP under scenario 4 would be that IFRS would be extended to all publicly accountable entities. Micro entities might be able to retain Financial Reporting Standards for Smaller Entities (FRSSE). Those entities that are not micro, small or publicly accountable could use IFRS for SMEs. Under the other scenarios, the UK and Europe would become isolated from the rest of the world.

ALAN TEIXERIA

Teixeria covered the benefits and challenges of global standards, the FASB-IASB Memorandum of Understanding (MoU) and a review of the credit crisis. Consistency of financial reporting is the main benefit of global standards. This will create a high-quality financial reporting systems that will increase investment and reduce the cost of capital. There has already been substantial progress towards world-wide adoption of IFRS. In January 2009, IFRS are used in over 110 jurisdictions by listed companies and in over 80 by unlisted companies. At present 39% of fortune Global 500 companies use IFRS, with 31% using US GAAP and 31% using individual GAAP. The percentage using IFRS is likely to rise. The SEC has prepared a road map for convergence, with a decision in 2011 about possible implementation in 2014–16. World adoption of a single set of high-quality global accounting standards would be ideal. However, there are problems, for example, of local endorsement, local adoptions, translations and enforcement. In a legalised jurisdictional framework adoption may be slow. Some countries do not have specialised financial terminology for translation, and auditing standards vary globally. The FASB-IASB MoU will lead to an aligned conceptual framework, removing selected differences in the short term and issuing common standards in the future. A number of firm dates are provided for financial statement presentation, fair value measurement, financial instruments, consolidation, SPE and post-employment benefits. A consequence of the continued credit crisis was European pressure for reclassification out of fair value. To prevent a European carve-out, the IASB issued revisions to IAS 39 and IFRS 7. This amendment addressed one difference with US GAAP, but the many other differences would only be met with common standards.

PAUL MOXEY

Moxey’s presentation provided a view from ACCA. It was given against the background of the credit crunch from a corporate governance perspective. Moxey outlined the unprecedented recent growth in the banking sector. ACCA had held a number of meetings to examine and potentially identify the key causes of the credit crunch (eg inappropriate remuneration structures, poor risk reporting and lack of accountability) as well as contributory factors (eg over-complex financial products, excessive leverage, complacency, greed and interconnected financial institutions). We have not learnt important lessons from the past such as the East Asia crises in the late 1990s, Enron and WorldCom.

Against this backdrop ACCA has developed ten principles of good corporate governance where boards direct and control organisations in the interests of long-term owners. Boards should be accountable and should obey the spirit not the letter of the regulatory framework. Moxey discussed several of ACCA’s principles and their implications. Performance schemes should be based on sound principles properly applied. Risk management and remuneration systems must be linked. In addition, boards and shareholders should receive appropriate, clear and reliable information on risk and financial results. The highly sophisticated risk management functions of banks have been found wanting. A lack of understanding of new financial products and their complexity at board level allowed traders free rein. This was compounded by a lack of detail on the range of risks and a belief in the efficient market. The role of audit committees and internal auditors needs to be strengthened. Audit committees need unsanitised information and internal auditors need to be objective and independent. These problems are compounded by the complexity and length of IFRS. The use of fair value can create anomalous results whereby if a bank holds debt and the value of the debt is reduced, the bank can report a ‘profit’ on the reduction.

Recent events have shown the fragility of financial institutions. Moxey pointed out that there was a need for debate and research on key issues such as: the purpose of accounts; the responsibility of accountants; the expectations of users; the key role of information in risk; the complexity of accounts; and the expectations gap. Under Basel requirements, when asset quality lowers then so does capital. Banks need capital at the very time when they have less, leading to reduced assets and a worsened credit environment. Basel II has increased this pro-cyclicality effect. Inconsistencies in capital regulations encourage banks to use off- balance sheet vehicles to hold assets to lower required regulatory capital. However, these off- balance sheet liabilities were still, in effect, institutional liabilities. There is an urgent need to reconsider their accounting treatment. The present system is in danger of permitting profits to be retained in the private sector, but losses to be met by the public. The ten principles of corporate governance set out by ACCA would hopefully improve the current situation.

The papers in Table 1 have been grouped into two broad categories rather than being dealt with in their strict order of presentation. In the first group, we look at the papers by Peasnell, Moxey and Holgate who give very different views of the role of accounting. In the second group, we have

Mackintosh and Teixeria, who present their views on where the current crisis has left standard setting both at the national and international level. There is, however, some overlap between the two groups, with Holgate's paper in particular straddling both groups.

The authors approach their topics from very different perspectives. Ken Peasnell is a very experienced accounting and finance academic from Lancaster University and was able to provide an academic perspective on the credit crunch, drawing in particular on some recent research published in the *Accounting Review* a top-quality US refereed academic journal. Peter Holgate by contrast, is a well-respected accounting practitioner. Peter is senior technical partner for the UK firm of PricewaterhouseCoopers and was able to provide an up-to-date and informed practice-based perspective on the topic. Paul Moxey provided a third perspective as Head of Corporate Governance and Risk Management of ACCA. ACCA has observed, researched and commented on the credit crunch from an independent, but very interested, perspective. Ian Mackintosh and Alan Teixeria both gave views on the present financial situation from a standard setters perspective. However, their perspectives varied widely. Ian approached the topic as head of a national standard setting body, the UK's Accounting Standards Board. He can, therefore, be seen as an informed outsider in his comments on the IASB. By contrast, Alan can be seen as an informed insider. He is Director, Technical Activities, IASB, and thus is intimately involved with the current practices and procedures of the IASB.

These differing backgrounds were reflected in the nature of their contributions. Peasnell provided an academic perspective on the current credit crunch, particularly the role played by accounting and challenged many widely held assumptions. Holgate investigated the role which accounting played in the credit crunch and then investigated, from a practitioner-perspective, the response of the IASB. Moxey investigated the nature and function of the accounting crisis from the perspective of a set of ten principles on improved corporate governance devised by ACCA. Mackintosh looked at a timeline of recent events before proposing four possible scenarios for the future of international standard setting. Finally, Teixeria looked at the benefits of global standards and the challenges facing international standard setters, the FASB-IASB Memorandum of Understanding, and reviewed the credit crisis from a standard setting perspective.

The first group of papers (Peasnell, Holgate and Moxey) therefore focused on the underlying credit crunch and the problems it poses for accountants. Interestingly, the speakers were divided in their views, demonstrating the problems which these catastrophic global events has caused for the accounting community. While all three speakers broadly agreed on the causes of the present crisis, their analysis of the part played by accounting was very different. Peasnell and Holgate saw accounting as basically a medium that did not affect the result, while Moxey was more critical of accounting per se. Peasnell, for example, pointed out that in the UK the spectacular failure of Northern Rock was not caused by off- balance sheet financing nor did academic research support the notion that in the US, off- balance sheet financing fooled investors. Peasnell was also of the opinion that the US stock market did not believe that fair value overstated asset values. Holgate also did not blame fair value, arguing that in the current crisis we need more rather than less information on current values. By contrast, Moxey was more critical of accounting in general and of fair value per se. He believed that the credit crisis asked fundamental questions of accounting, such as the purpose of accounts, the complexity of accounting, the role of cash and the relationship between accounts and risk. In addition, he highlighted deficiencies in IFRS. Recent developments in IFRS had added to their complexity and length, but not necessarily to their clarity or ease of understanding. Fair value was blamed for producing anomalous results and also for creating problems of pro-cyclicality. Unlike Peasnell and Holgate, he therefore did not see accounting as an innocent player.

Four of the speakers were concerned with IAS 39 reclassification. They approached this from slightly different perspectives. Peasnell's comments were mainly descriptive and he did not accept that there was a problem with fair value per se. Holgate suggested that IAS 39 was principally a presentational change with disclosures in the notes, and that few companies had actually made use of it. Mackintosh and Teixeria took a more political stance. Mackintosh saw the reclassification as an example of pressure from the European Commission, while Teixeria focused on the day-to-day background that had led to the revisions to IAS 39. He also pointed out that in the overall context of differences between IFRS and US GAAP, this was a minor difference and had highlighted the need to focus on core issues rather than detail.

Apart from their discussion of the IAS 39 carve-out; Mackintosh and Teixeria were particularly concerned with geopolitical standard setting. Mackintosh saw the credit crunch as leading to a fundamental crossroads for international standard setting. This could lead to (1) A European carve out with either an isolated US or Europe, depending on the US attitude; (2) A takeover by the G20 of the IASB; (3) Non-adoption by the US of IFRS and the current situation of US and international GAAP remaining; and (4) worldwide agreement, including agreement between the US and the UK. Under the fourth option, the UK would benefit, but under the other three options UK GAAP would suffer. Holgate commented on this scenario and suggested that, as more countries sign up to IAS European and US influence would decline. This takes Mackintosh's scenario even further as it suggests that even under scenario 4 the UK is likely to lose influence. Holgate also saw political aspects of the IASB's role as essential – especially given the current crisis. Rather than focus on the 'death or glory' options outlined by Mackintosh, Teixeria emphasised the relationship between US GAAP and IFRS. He outlined the current efforts by the US and IFRS to enhance and develop mutual understanding, and set out milestones on the way towards convergence and continued cooperation.

Table 1: Thematic overview of the five presentations

Author	Background	Context	Topic area	Key issues/findings
Ken Peasnell Lancaster University	Academic	UK, International	Asset, securitisation, fair value, credit crunch	A long economic boom led to increased loans and growth in asset securitisation. US securitisation was off-balance sheet, but this did not delude investors as sophisticated capital markets are able effectively to value business. Fair value problems re asset valuation in thin markets associated with financial crisis Current crisis, no new issues for financial reporting more a problem of bank regulation, governance and management.
Paul Moxey ACCA	Professional institute	UK, International	Accounting, corporate governance and credit crunch	Global banking has grown rapidly in recent years. The roots of the credit crunch were traced to poor corporate governance, inappropriate risk and reward structures, and poor levels of risk management information and reporting. ACCA proposes ten principles of corporate governance to redress these issues. It was argued that it was time to look at the basics of accounting, and ask some fundamental questions concerning the purpose and use of accounting information.
Peter Holgate PricewaterhouseCoopers	Practitioner	UK, International	Organisational politics	Huge losses on financial assets. Fair value has been criticised. More, not less, disclosure would be beneficial in determining the value of assets and liabilities. A partial retreat occurred through the IAS 39 reclassification amendment. Increasing problems with going concern questions and implications for the audit opinion. Can the IASB as a private sector body act without political interference?
Ian Mackintosh ASB	Standard setter	International regulations	Regulatory change	From August to November 2008, there was a sequence of events in accounting, set against the background of the credit crunch, such as amendment to IAS 39, SEC road map for IFRS adoption. The IAS 39 amendments highlighted tensions in achieving global accounting standards. Four potential scenarios: European carve-out; G20 replaces IASB; US rejects IFRS; and IASB/FASB and G20 all adopt IFRS. If latter option, IFRS could be extended to all publicly accountable entities. Micro entities would not report under IFRS; smaller entities would retain FRSSE.
Alan Teixeria IASB	Standard setter	International	Spread of IFRS	Benefit of IFRS is global consistency. In July 2009, IFRS used by listed companies in over 110 countries and unlisted companies in 80 countries. The ideal for global standards would be uniform adoption of IASB without localised endorsement or adaptation. Slow process of change hampered by differing legal systems and the status of accounting standards in law. Translation and enforcement issues are also significant. An ongoing convergence programme between IASB and FASB (MoU) with projects and key milestones outlined. Tension from conflicting interests and IASB amendments to IAS 39. Crisis has led to focus on core issues in convergence rather than detail.

4. Conclusions

The five papers were presented at a very interesting time, both economically and politically. The financial crisis and associated credit crunch has led to a re-questioning of aspects of accounting, in particular recognition and measurement issues, corporate governance and the current regulatory system that governs accounting. While some of these areas are not new, perhaps the financial crisis has led to a greater concentration on them and also provided the accountancy profession, regulatory bodies and standard setters with an opportunity to reflect on the core issues. The crisis has also contextualised some of the difficulties facing international convergence.

Given the impact of the current financial crisis it is not surprising that all the speakers used it as a context for their presentations – its causes, the interdependence of financial markets, its impact on accounting and governance issues, and the future challenges to the accounting profession and changes that need to be made. It is clear that there is no single answer, just as there was no single cause of the crisis. A multi-dimensional approach is therefore appropriate given the complexities associated with risk, reward structures, lending, governance, behavioural issues and accounting recognition and measurement.

The speakers dealt with different questions and approached the issues from differing perspectives. Ken Peasnell, for example, is a leading UK accounting and finance academic. He was supportive of the role of accounting in the credit crisis. He recognised that while asset securitisation was off-balance sheet, this did not fool investors as sophisticated capital markets are still able to value businesses. He believed the problem was connected with the actual levels and understanding of risk, and the trading volume of asset-backed derivatives, and not necessarily whether they appear on or off-balance sheet. He also did not believe that fair value understated market value, but rather that in times of financial crisis fair value is problematic in its application in thin markets. The main issues remained regulation, governance and management and these should be separated from any accounting issues, which are more symptomatic than causal. Peter Holgate, a PricewaterhouseCoopers partner, was also supportive of accounting. He dealt with the IAS 39 reclassification amendment and the increasing problems that practising accountants like himself had with going concern in the global financial crisis. Like Ian Macintosh, Peter Holgate discussed the political nature of the IASB, highlighting its unusual role as a non-governmental body. Ian Mackintosh also dwelt on the political nature of the IASB. He presented a series of possible scenarios which could arise in the future. In some of these the IFRS would flourish; in others it would not. Alan Teixeria came to the debate with an international accounting perspective given his role at the IASB. He showed how the use of IFRS has increased rapidly. He also demonstrated the problems involved in translation, adaptation and enforcement. His view as an international standard setter thus neatly complemented that of Ian Macintosh. Finally, Paul Moxey from ACCA provided an extremely critical look at the role of accounting. Indeed, he was probably the most critical of the five speakers. He analysed the roots of the credit crunch and proposed ten principles of corporate governance which, he argued, would improve the present system of board governance. Paul was extremely critical of business and banks in general, but also of accounting. He believed it was time to look at some of the basics of accounting, its purpose and use of financial statements.

Given these differences in background and perspective the authors suggest a range of questions which are summarised below.

- What should the appropriate measurement system for financial statements be? Is fair value appropriate in times of economic crisis?
- How should accountants treat going concern in times of economic downturn? What assumptions can be made about the surety of future financing requirements consistent with going concern?
- How do we balance being cautious and fair to investors without turning the going concern qualification into a self-fulfilling prophecy?
- Do we need to look again at the role of accounting practices such as off-balance sheet financing, credit default swaps etc?
- Will the IASB be able to survive as a private sector standard setting body?
- What will be the future relationship between the IASB, the FASB and the European Union, the G20 and individual countries, such as China?
- How will future potential changes to governance and risk reporting and requirements affect accounting and the accounting profession?
- What will be the effects of the financial crisis, especially the IAS 39 amendment process, on the overall ideal of global accounting standard convergence and the future of the US-IASB road map?

Such important questions are unlikely to be solved quickly. Although at the time of writing this report (November 2009) some of the pressures have eased, the underlying questions persist. What the speakers in the symposium have emphasised is the fundamental and problematic nature of key issues of accounting recognition and measurement. They have also tentatively mapped out some possibilities about the future development of accounting. Only time will tell whether their reflections are accurate or not.

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