



The future  
of financial  
reporting 2019:  
Current developments  
in financial reporting  
(Private and public sectors)

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# The future of financial reporting 2019:

## Current developments in financial reporting (Private and public sectors)

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A discussion paper based on the British Accounting and Finance Association (BAFA), Financial Accounting and Reporting Special Interest Group (FARSIG) Symposium, 11 January 2019.

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## About FARSIG

**The FARSIG is a group set up under the aegis of the British Accounting and Finance Association (BAFA). The main purpose of the Financial Accounting and Reporting Special Interest Group (FARSIG) is to further the objectives of BAFA 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 closer links with the accountancy profession in order to inform policy
- publish a newsletter and organise targeted workshops
- develop and maintain relationships with BAFA and the professional accountancy institutes
- provide a forum for the exchange of ideas among accounting academics.

The symposium, which is one of an annual series that started in 2007, 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. Furthermore, they serve to illustrate the policy relevance and impact of current academic thinking and outputs, in accordance with calls from the Economic and Social Research Council and Advanced Institute of Management for relevant and rigorous research combining practitioner and academic perspectives.

The authors would like to express their thanks to the five main contributors, both for their presentations and for their subsequent time and comments during the development of this discussion report. The authors have tried to capture faithfully the flavour of the original presentations. Nonetheless, although the original authors were shown the commentary on their presentations, any errors or omissions remain our own. Thanks are also due to ACCA for hosting the symposium and for its support for the publication of this discussion report. Finally, could any readers who wish to learn more about FARSIG or to become FARSIG members please contact any one of the authors.

Mike Jones is chairman of the FARSIG Committee and professor of financial reporting at the University of Bristol, UK. Andrea Melis is on the FARSIG committee and professor of corporate governance and management accounting at the University of Cagliari, Italy. Silvia Gaia is a senior lecturer in accounting at the University of Essex, UK and Simone Aresu is a senior lecturer in accounting at the University of Cagliari. Luigi Rombi is a lecturer in accounting at the University of Cagliari and Penny Chaidali is a lecturer in accounting at the University of Cardiff.

# Foreword



**ACCA was pleased to host again the Financial Accounting and Reporting Special Interest Group (FARSIG) annual discussion of the future of financial reporting. The meeting continues to provide a valuable opportunity for discussion between interested parties – principally academics studying financial reporting and those involved with its practical application in one way or another.**

This year's symposium corrected an imbalance. It is commonplace to think in terms of corporate reporting, but public sector reporting is gaining increasing prominence and two of the presentations looked at developments in International Public Sector Accounting Standards (IPSAS). While not universally adopted IPSAS are the most significant basis for the future of reporting by the sector. When adopted they are not only a change from national standards, but most often the means for the more fundamental change from cash to accrual accounting. It is important that the advantages of accrual accounting are well understood, but equally so are the very significant issues that transition raises.

It is interesting that one of the issues raised in the discussion of IPSAS is the sense that the theoretical basis of the standards could be better developed. The Conceptual Framework for IFRS has been debated for many years, not least in the FARSIG symposia. This year's also followed that with two presentations considering the changes made in the last revision of the Framework, areas of remaining concern and the likely impact on the standards themselves. I think that practitioners expect that academics will have a special interest in, and contribution to, these conceptual and theoretical issues about accounting.

The other presentation in contrast had a very practical focus not so much on financial reporting as the wider corporate

reporting. It looked at the trends from reviewing the reports of the FTSE 100 companies and how in particular they tackled three different pieces of new regulation in the non-financial reporting space. These sorts of regulatory changes are only likely to increase in future as governments and others respond to the issue of climate change and to greater public interest in the impact of companies on the environment and society.

I am sure that practitioners discussing their current concerns and views are helpful in guiding those responsible for teaching and training to keep it up to date and relevant especially for students starting accountancy. The current concerns of those in practice can also help to direct research to the topics that will have the most impact. In the other direction academic research can provide evidence to support the development and revision of standards and regulations.

The need for interaction between practice and academia, such as provided each year by the FARSIG symposium, is therefore as important as ever.

I extend my thanks to FARSIG for organising the conference and to Simone Aresu, Penny Chaidali, Silvia Gaia, Mike Jones, Andrea Melis and Luigi Rombi for providing this summary of the event.

**Richard Martin**  
Head of Corporate Reporting, ACCA





# 1. Introduction

**In 2019, the world is facing a growing number of complex and interconnected social, economic and political challenges. Global risks are intensifying (WEF 2019). Problems range from slowing global growth and the persistent economic inequality to climate change, geopolitical tensions and the accelerating pace of the Fourth Industrial Revolution, which is fusing physical, digital and biological technologies. All these factors would represent daunting challenges even if taken in isolation.**

Macroeconomic risks have become more apparent. Financial market volatility has increased, and the rate of global economic growth appears to have peaked, with a forecasted gradual slowdown over the years ahead (IMF 2018a). The slowing global growth is mainly the outcome of developments in advanced economies and projections of a slowdown in China (WEF 2019). The European economy is continuing to grow at a moderate rate. On the other hand, the persistence of growth without increased employment, somehow associated with the so-called 'Fourth Industrial Revolution', continues to raise new challenges. There is a fear of growing inequality owing to the disruptions caused by intensifying patterns of automation and digitalisation (WEF 2019). Environmental risks continue to dominate, alongside the global risk, in both likelihood and impact. Extreme weather is the risk of greatest concern, together with environmental policy failure, which causes an acceleration in biodiversity loss, pollution of air, soil and water and failures of climate-change mitigation and adaptation (WEF 2019).

Geopolitical and geo-economic tensions are rising among the world's major countries. Following a period of globalisation that profoundly altered the global political economy, the world is evolving into a period of divergence, with the rise of popular movements that aim to re-establish the national state as the primary locus of power and legitimacy. This is occurring despite a more pressing need for a collaborative and multi-stakeholder approach to address the above global challenges (WEF 2019). In this scenario, the negotiations between the European Union (EU) and the UK, following the UK's decision to leave the EU, have continued to be problematic since the 2016 referendum. There has been continuing controversy and debate. It is still unclear, at the time of writing this (October 2019), not only what the details of an agreement might be, but also whether any agreement will be reached.

It was within this complex and uncertain social, economic and political scenario that the latest annual BAFA FARSIG Symposium on the 'Future of Financial

Reporting' was held at ACCA, London on 11 January 2019. Alongside this context and its problems, there have also been continuing financial reporting developments in areas such as the role of accounting in defining and measuring uncertainty, the long waited new IASB Conceptual Framework, and issues concerning accounting in the public sector and the emerging trends in narrative reporting in corporate annual reports.

The principles, concepts and elements that characterise how companies should report their performance are currently being debated. Relatively old questions (How do we define and measure uncertainty? When do you recognise a transaction? What is the meaning of prudence in accounting?) are still under discussion, together with relatively new questions: How do new technologies influence stakeholders' increasing empowerment? How should companies acknowledge the voice of stakeholders and address their concerns through their reporting? By using all its potential, accounting is able to (and should)

The main themes covered in 2019 were: the new IASB Conceptual Framework, the emerging trends in narrative reporting in corporate annual reports, and the macroeconomic relevance of standards-based accrual accounting in the public sector.

contribute to providing answers to these critical questions. If these answers could be found, proper decision-making and stewardship of all the different resources employed in business activities would be enhanced and better accountability towards corporate and public sector stakeholders would result.

The title of the 2019 FARSIG Symposium was 'The Future of Financial Reporting: Current Developments in Financial Reporting (Private and Public Sectors)', which reflected these current debates and developments. Five speakers provided their views on the major accounting issues, the future opportunities and challenges facing corporate reporting, from the perspectives of the accounting standard setters, accounting practitioners, reporting professions, and academia.

For 2019, the five speakers are listed here in alphabetical order.

Professor **Andreas Bergman**, University of Zurich and former chair of IPSASB: 'Current Developments in Public Sector Accounting'

Professor **Sheila Ellwood**, University of Bristol: 'Controversies and Topical Issues in Public Sector Accounting'

**Anne Kirkeby**, Lead Corporate Reporting Consultant, 'Black Sun: The Black Sun Review of Trends in Corporate Reports 2018'

Dr **Jianqiao Lu**, IASB member, formerly of the Chinese Ministry of Finance: 'The Conceptual Framework of Financial Reporting (2018) – the IASB view'

Professor **Geoffrey Whittington**, Emeritus Professor, University of Cambridge: 'The Conceptual Framework of Financial Reporting after the 2018 IASB Revisions'

In the tradition of the symposium, each presentation was followed by a lively and informed question and answer session and an overall discussion among the many symposium delegates.

## ISSUES RAISED BY THE SYMPOSIUM

Before introducing the presentations, the main topics presented and debated at the symposium are briefly summarised in Table 1.1. This table provides a summary of the key topics raised at symposia since 2008. The main themes covered in 2019 were: the new IASB Conceptual Framework, the emerging trends in narrative reporting in corporate annual reports, and the macroeconomic relevance of standards-based accrual accounting in the public sector.

During the symposium, and in the subsequent audience discussion, there was a critical examination of some of the basics of accounting and the accountancy profession (eg the role of accounting in defining and measuring uncertainty, the importance of conceptual frameworks in accounting) together with some new frontiers of corporate reporting (eg the use of narratives in annual reports) as well as the role of accounting in the public sector. Some of the issues raised and discussed were 'evergreens' that continue to present academics, standard setters and practitioners with fundamental challenges, such as the role and limitations of the IASB's Conceptual Framework and the macroeconomic relevance of (standards-based) accrual accounting of the public sector. In addition, the speakers also provided their views on emerging issues and aspects, such as the use of narratives in corporate annual reports, that are currently shaping, and will increasingly affect, corporate reporting and the way companies engage with their stakeholders. Some of common themes that emerged during the symposium were discussed in more depth after the commentaries.

Some of the main developments that have occurred in accounting and corporate reporting during the years 2018 and 2019 are discussed below. 'International accounting convergence', ie the harmonisation of the accounting principles and standards issued by different national and international standard setters remains of great importance in enhancing the consistency, comparability and, ultimately, the

**This evolving scenario in corporate reporting is influencing preparers and users of corporate reports as well as the accountancy profession and all stakeholders.**

usefulness of companies' financial statements. Nonetheless, the process by which the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) attempted to converge their respective financial reporting standards into one global set is still very far from being accomplished. The IASB–FASB joint convergence project has been stalled since 2012. In the meantime, the IASB has continued to examine and discuss various accounting concepts that, by March 2018, were eventually put together in the publication of the new, long awaited, IASB Conceptual Framework.

The IASB's agenda for 2019 includes several important research projects. More specifically, the IASB's research pipeline includes projects on important topics, such as business combinations under common control; dynamic risk management; extractive activities; financial instruments with characteristics of equity; goodwill and impairment; and provisions. IASB's agenda also contains many 'maintenance' projects, including amendments to IASs 1, 8, 12, 16 and 37 as

well as to IFRSs 9, 16 and 17. Importantly, the IASB has been working on three standard-setting projects: one on Primary Financial Statements (Discussion paper or Exposure Draft expected at the end of 2019), one on the Management Commentary and one on Rate-regulated Activities (both Exposure Drafts expected in 2020). In the meanwhile, the International Public Sector Accounting Standards Board (IPSASB) has been working on important issues in public sector accounting, such as those related to non-exchange expenses from collective and individual services (Exposure Draft published in January 2019).

This evolving scenario in corporate reporting is influencing preparers and users of corporate reports as well as the accountancy profession and all stakeholders. Many of these issues were, either directly or indirectly, discussed during the 2019 symposium. Each of the five speakers provided a range of informed and interesting viewpoints. The issues specifically addressed in the symposium are now presented, and then discussed, in more depth in the following sections.

**TABLE 1.1:** Overview of key symposia themes, 2008–19

| 2019                                   | 2018  | 2017                                       | 2016  | 2015  | 2014  | 2013  | 2012  | 2011   | 2010  | 2009   | 2008                    |
|--|---|--|---|---|---|---|---|--|---|--|-------------------------|
| Conceptual framework                   | The role of accounting in shaping capitalism                      | The evolution of corporate reporting       | The use of information by capital providers         | Accounting for goodwill                     | Conceptual Framework, measurement                 | Conceptual Framework, recognition and measurement         | Asset and liability recognition                             | Complex financial instruments, asset and liability recognition and measurement | The role and need for global accounting standards | Regulatory change                                | Conceptual Framework    |
| Narratives in corporate annual reports | The role of Big Data and AI in corporate reporting and investment | Corporate reporting vs financial reporting | Conceptual Framework: measurement                   | Corporate governance                        | EU Accounting Directive for SMEs                  | Regulatory Framework, governance and 'balanced reporting' | Measurement, fair value and confidence accounting           | Regulatory environment, complexity of financial statements                     | Understandability and usefulness                  | The convergence of global standards through IFRS | Income measurement      |
| Accounting in the public sector        | Digital reporting   | Financial narratives                       | Transparent corporate reporting                     | Integrated reporting                        | UK FRS: tax implications                          | IFRS adoption and national accounting practices           | Regulatory Framework and complexity of financial statements | IFRS adoption and political interface  | Political concerns                                | Fair value                                       | Fair value              |
|  | Conceptual Framework  | Accounting profession                      | Integrated reporting and the capital markets        | Sustainability accounting                   | The use of information by capital providers       | Nature and complexity of crises                           | Fraud and accounting scandals                               | Carbon accounting  | Sustainability accounting                         | Corporate governance                             | Financial communication |
|  | Integrated Reporting  | Future of Chinese and Western auditing     | The perceived role of the accountant in the society | IASB and politicisation of standard-setting | Compliance with mandatory disclosure requirements |   |   |  |   | Asset securitisation and the 'credit crunch'     |                         |

Sources: Jones and Slack 2008; 2009; 2010; 2011; 2012; 2013; Jones et al. 2014; 2015; 2016; 2017; 2018.





## 2. Symposium papers

(in alphabetical order by author)

### Current developments in public sector accounting

**Andreas Bergmann, Institute of Public Management**

Andreas Bergmann is Professor of Public Finance at the Zurich University of Applied Sciences. He has previously been a member of the IPSASB and chaired it from 2010. Andreas talked about the functioning of the IPSAS, illustrating the IPSASB work programme. He then talked about the macroeconomic relevance of (standards-based) accrual accounting of the public sector. Finally, he highlighted the lack, from an academic perspective, of a theoretical basis for analysing public sector accounting.

Andreas started by describing the structure of IPSAS, which have been issued since 2001. In particular, the original IPSAS consisted of 42 accrual basis standards, of which six were withdrawn/replaced resulting in 36 accrual-basis standards, plus one cash-basis standard introduced only as a temporary solution when implementing accrual IPSAS. Eighteen independent board members sit on the IPSASB; its aim is to improve public sector financial reporting worldwide through the development of IPSAS, for use by governments and other public sector entities around the world. Although working under the roof of the International Federation of Accountants (IFAC), Andreas pointed out that IPSASB is independent in its standard setting. In addition, since 2015, IPSASB has worked under the oversight of the Public Interest Committee (whose members are drawn from the International Monetary Fund (IMF), World Bank, OECD, and International Organization of Supreme Audit Institutions) in order to strengthen the public interest. He then described the future programmes of the IPSASB through the 'IPSASB Strategy and Workplan 2019–23', whose strategic objective is to strengthen public financial management globally through increasing adoption of accrual-based IPSAS.

Andreas then highlighted how IPSAS-based accrual accounting is part of sound and integrated public financial management. In particular, he pointed out how accrual accounting is part of a process that involves budgeting, accounting, auditing and governmental financial statistics. He then showed the worldwide development of accrual IPSAS by using the International Public Sector Financial Accountability Index (2018 *Status Report*). He also pointed out that the level of adoption and implementation of accrual accounting expected to be achieved by 2023 is based on a decrease in the number of countries adopting cash-based accounting (from 30% to 17.5%) and a rise in those using accrual-based accounting (from 25% to 65%). The remaining countries, ie those transitioning from cash to accruals, are also expected to decrease from 45% to 17.5% by 2023.

Andreas then proceeded by highlighting the current IPSASB work programme. In particular, he showed how three IPSAS have been approved (Cash Basis IPSAS Update, IPSAS 41 and IPSAS 42), three Exposure Drafts have been issued (ED 64, ED 65/66, ED 67), two consultation papers have been issued relating to the revenues and non-exchange expenses, and other projects have been started on measurement and infrastructures.

Several topics, such as social benefit, public sector measurement, heritage, infrastructure assets and leases, still have public-sector-specific conceptual frameworks.

Andreas then commented that there is some alignment between public-sector-specific content and the IFRS's position on non-exchange expenses, revenue and financial instruments. On the other hand, several topics, such as social benefit, public sector measurement, heritage, infrastructure assets and leases, still have public-sector-specific conceptual frameworks.

He then proceeded by showing how the new IPSAS 42 relates to social benefits and, in particular, to the moment when a liability related to social benefit can be recognised. IPSASB did not provide a definition of social benefit and is simply limited to cash transfers. Therefore, when a service is provided it is not considered a social benefit. Andreas agreed that although this approach may seem too narrow it was in line with the international consensus. He then questioned the stage at which a liability for such a cash transfer should be recognised. The IPSASB provided the solution in legal terms. Essentially, a liability is recognised at the stage at which the government has a legal obligation to pay a cash transfer to an individual (ie when an individual can litigate and ask the government to pay that cash transfer).

Then, Andreas analysed the work of IPSASB on non-exchange expenditures and revenues. In particular, he highlighted how there is no standard on expenditures but only on revenues, although this was heavily debated on several consultation papers. As regards revenues, the papers highlighted the continuum between exchange and non-exchange revenues. On the one hand, there is a category where there are no performance obligations or stipulations (ie non-exchange revenues) such as taxes and transfers. On the other hand, another category consists of enforceable agreements, with performance obligations to transfer goods or services to customers on commercial terms (ie exchange revenues) such when goods or services are sold commercially. In addition, a 'shaded area' also lies between these categories and constitutes the difficult part of standard setting. Revenues may come from enforceable agreements, with performance obligations or stipulations

to use or consume resources in a particular way, and/or other agreements requiring resources to be used over a specified period. As Andreas described, quite often governments do not sell goods and services, but they do sometimes have to meet certain conditions. As an example, he described a local government that obtains funds from national government to provide services for local inhabitants (eg funding to administer a specified number of vaccinations) – the local government does not buy or sell the vaccine but must commit to distributing it. This 'shaded area' is being analysed by IPSASB through a public sector performance obligation approach that will replace the current practice adopted under IFRS15 to cover this area. In addition, he pointed out how IPSASB is looking at other areas that need further discussion, such as services in kind (eg services not provided in exchange for cash).

Andreas then analysed the 'revenue roadmap' of IPSASB. In particular, at the time of the symposium IFRS15 convergence was expected to be delivered soon<sup>1</sup>, while the review on the current literature (ie IPSAS23) was due by mid-year 2021. No changes as regards recognition and measurements will be made on exchange revenues (ie IFRS alignment project) and only minimal changes on terminology, so as to reflect more accurately the nature of the public sector (eg moving from a focus on Profit/Loss to one on Surplus/Deficit) and IPSAS9 and IPSAS11 will be replaced.

Then, he described how the public sector performance obligation, ie the 'shaded area' discussed above, involves taking the five steps (identifying the binding arrangement; identifying all the performance obligations; determining the transaction price; allocating the price to the performance obligations; and recognising revenue as the performance obligations are fulfilled) specified in IFRS15. In particular, he emphasised how difficult it is to make the first step, ie identifying the binding arrangement, because most obligations are not identified by binding (negotiated) arrangements but by a law that defines these obligations. Therefore, the notion of having a contract, such as in IFRS15,

1 Revenue – IPSAS 23 Update was delivered in March 2019, just after the symposium.

Accounting research on the private sector, which is done mainly using principal-agent theory and by analysing how financial market data is presented, is theoretically well developed and established.

is not easily applicable to the public sector. Luckily, although there are difficulties on the second point too (ie identifying performance obligations) there is common consensus, and fewer modifications, on the remaining steps: determine the consideration, allocate the consideration and recognise expense.

Andreas then highlighted the measurement bases found in the Conceptual Framework for assets (ie market value, replacement cost, net selling price and value in use) and liabilities (ie current value measures, market value, cost of fulfilment, costs of release and assumption price) and the absence of fair-value. He pointed out how such absence is being discussed by IPSASB since, in the standards, there are fair value references that are, however, inconsistent with IFRS 13.

He then continued to discuss the aim and work of the European Public Sector Accounting Standards (EPSAS), which started in 2011 (*Budgetary Frameworks Directive, 2011/85/EU*). Essentially, Member States must have in place public accounting systems that comprehensively and consistently cover all subsectors of general government and contain the information needed to generate accrual data with a view to preparing data based on the standard and subject to internal control and independent audits. As he noticed, however, they are still working on the project and no standard has been developed so far. EPSAS are thus entering what is called Phase 2, which addresses comparability within and between the Member States in the medium to long term by stepwise implementation of EPSAS by 2025. He then argued that, since no EPSAS standard has been issued, compatibility with IPSAS could not be assessed yet. Even so, he pointed out that issued papers take IPSAS requirements as their main reference so it is quite likely that they are going to be very similar but it is too early to know.

Andreas then quoted an IMF study (2012) that analysed the correlation between transparency (ie compliance with IPSAS or other standards) and debt (ie Average Debt/GDP) and between transparency

and interest rates (ie average credit default swap (CDS) spreads). The Transparency Index does not explain much of the correlation, but it apparently explains why there is more variance of debt and of CDS spread respectively in low-income countries and high-income countries.

He then briefly discussed the differences between government finance statistics (GFS) and IPSAS. In particular, GFS is not a framework that imposes guidance on the financial reporting of governments around the world. In addition, GFS consolidates the finance of all levels of government but not that of their state-owned enterprises (SOEs), whereas IPSAS state that governments should consolidate what they control, including SOEs.

Andreas then argued that academics, prior to Jacobs (2016) and Steccolini (2019), admitted the lack of a theoretical basis for public sector accounting. Accountability theory, which is arguably the closest to accounting, is not a very strong theory that would provide clear guidance in an empirical study. The same is true for New Public Management since that is a very blurred concept and has been used in different ways in different countries. Some other studies have used critical theory, which can be adopted to analyse the resistance to the development of a specific project but is not really a theory designed to describe public sector accounting. The same applies to New Institutional Theory, which might explain how institutions do or do not work but is not a real accounting theory. As he noted, accounting research on the private sector, which is done mainly using principal-agent theory and by analysing how financial market data is presented, is theoretically well developed and established. This theoretical framework is developed in a sector that has different characteristics and has some features that may not fit well with governments/public bodies (eg governments issue bonds, not stock, and bond markets are less volatile than equity markets). Therefore, Andreas concluded by arguing that it is necessary to develop a theoretical basis for public sector accounting because that would help to produce some relevant results from future research.

**What is important is the development of a conceptual framework aimed at analysing public sector accounting rather than translating theoretical concepts from other sectors into the public one.**

### **QUESTIONS AND ANSWERS**

*Geoffrey Whittington (University of Bath)* argued that public accounting is related to a stewardship approach and that should be emphasised, rather than profit maximising. Andreas agreed with him and pointed out the utility of accruals on providing more information.

*Ron Hodges (University of Birmingham)* questioned whether academics should encourage a variety of theories in the public sector. Andreas answered by saying that what is important is the development of a conceptual framework aimed at analysing public sector accounting rather than translating theoretical concepts from other sectors into the public one.

*Lynn Bradley (Glasgow University)* asked Andreas' opinion on Mark Moore's public value concept and asked whether legitimacy and capacity were relevant in the public sector. Andreas answered that, in his opinion, the government's general purpose is changing financial reports rather than financial statements.

*Sue Hardman (Brunel University)* questioned whether social benefit, being a liability, is a political obligation. For example, UK child benefit could potentially be 18 to 19 years of legal obligation for the government. Andreas answered that the main reason why IPSASB went relatively timidly and restricted itself to legal obligation was because it could not answer this type of question.





## Controversies and Topical Issues in Public Sector Accounting

### Sheila Ellwood

Sheila Ellwood is a professor at the University of Bristol. She researches the impact of convergence of financial reporting practice across different modes of provision, in particular, across the private and public sectors. She was a member of the UK Treasury Panels on accounting for NHS and healthcare charities (2010–11) and the introduction of IFRS15 (2015–17).

Sheila gave a presentation on controversies and topical issues in public sector accounting. She started by showing data provided by the International Public Sector Accounting Standards Index (2018) and highlighted how the public sector is moving toward an accrual world. More specifically, she pointed out how public sector accounting (or government accounting) has historically been predominantly cash-based and still 30% of central governments worldwide, including some important countries such as Germany, continue to recognise transactions when cash is received or paid. Nonetheless, as she noted, 25% of governments have adopted an accrual basis and 45% are somewhere in between an accrual and a cash basis (ie some transactions are recognised on cash receipt or payment, others on accrual). The UK and Australia are the only countries that use IFRS for both the public and the private sector, whereas many countries are transitioning to IPSAS that are aligned to IFRS for public sector entities.

Sheila then started questioning whether public sector accounting is going through a logical, consistent process or a controversial one. In particular, she pointed out how the EU, although being in transition to EPSAS (a European version of IPSAS), is moving extremely slowly with, as yet, no EPSAS issued. On the other hand, New Zealand, which had adopted IFRS on a sector-neutral basis across the private and public sectors, changed in 2012 to using IPSAS for the

public sector. China is moving to an accrual basis with specific characteristics. The US provides some consistency across sectors at a transactional level, but government initiatives make public sector accounting quite different from private sector accounting as regards the information on budgets and programmes. Finally, she noted how developing countries suffer the imposition of sophisticated accounting practices from international authorities such as the World Bank and the IMF, but may lack the culture, training and expertise to operate such systems.

The arguments for an accrual basis for accounting are well accepted. Accrual accounting permits the effective measurement of goods and services consumed; income earned; and ownership capital (equity). On the other hand, the accrual basis is more costly to operate; introduces subjectivity; may be less effective in removing corruption and may allow governments and politicians to be 'creative' in financial reporting. In practice, accrual-basis information can take many forms, for example asset measurement can be historic cost, fair value, replacement cost, value-in-use and so on. The application of accruals in the public sector should not necessarily be based on private sector accounting such as IFRS and national Generally Accepted Accounting Principles (GAAP) or IPSAS aligned to IFRS. The public sector operates in a different context, not being concerned with shareholder wealth creation and market transactions, but

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rather with citizens' well-being, with services funded by taxation (these differences are developed further later in relation to conceptual frameworks).

Sheila then discussed the Conceptual Framework of IPSAS, whose aim is to set out 'the concepts that underpin financial reporting by public sector entities that adopt the accrual basis of accounting' (IPSASB 2014). Conceptual frameworks have been questioned for decades. Page and Spira (1999) use the metaphor of underwear to argue that the draft of the Conceptual Framework of UK GAAP, rather than providing the conceptual underpinning, perhaps enhanced the legitimacy of the standard setter, ie made the standard setter look better through attractive clothing rather than providing a foundation layer to hang the standards on.

Sheila then discussed the pros and cons of having a common (sector neutral) framework rather than a specific public sector framework. On the one hand, she listed the drivers for using a commercial accounting framework (ie translating a private sector framework to the public sector) such as the similarity of transactions, comparability, the reduction in scope for government manipulation. On the other hand, she pointed out the different context for financial reporting of the public sector rather than the private one. The organisational purpose is not to maximise shareholder wealth, but rather to improve citizens' well-being (such as public health, education). The sources of revenues are not predominantly market transactions based on consumer decisions but taxation (an involuntary payment) – customers have choices, citizens do not. Although suffering temporary turmoil, countries and public sector entities have potentially farther horizons than private sector organisations subject to bankruptcy. In addition, the relationship with stakeholders is different since in the public sector there is a higher involvement and demand for information on how money is spent, the concern is not for profit (return on investment) but spending to achieve public policy outcomes and value for money. Public sector accounting has different users, citizens and their representatives, and different user needs. Therefore, transferring a framework from the private sector may be unsuitable and may lead to manipulation and confusion.

Sheila then showed the differences in the stipulated aims of the conceptual frameworks provided by IASB and IPSASB. In particular, the IASB's stance is fairly clearly 'to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders and other creditors in making decisions about providing resources to the entity'. On the other hand, the IPSASB states clearly that it takes account of different primary users and adds a different objective, with accountability standing side-by-side with decision-making. Sheila quoted: 'The objectives of financial reporting by public sector entities are to provide information about the entity that is useful to users of GPFRs [general purpose financial reports] for accountability purposes and for decision-making purposes' (IPSASB 2013). She then questioned whether the existence of different objectives and different users as set out in IPSASB are reflected in the standards. She noted how the early standards of the IPSASB replicated IFRS Standards without looking at areas that were public-sector-specific (such as social benefits). Then, she proceeded to question further whether the existence of different purposes could give us different information needs. Indeed, previous analyses and studies (Whittington 2008; Cascino et al. 2016) highlight the difference in informational needs if one considers accountability/stewardship rather than decision-making purposes. On a more practical level, Irwin (2016) shows how implementation costs, complexity and political preference influence what is omitted. What is included is influenced very much by lobbying by accountants and how standards are implemented depends on previous experience, for example, in the UK public sector, fair value is judged appropriate only in very limited circumstances (Hodges 2016).

Recent accounting figures and statements reported internationally and from the UK public sector were then used to illustrate some of the problems in public sector accounting: audit qualification; measures of debt and deficit; and specific accounting issues.

The Whole of Government Accounts for the UK (WGA 2016–2017) have, as in every previous year, received a qualified audit report. Each year the Comptroller and Auditor General (C&AG) explains his

**Government assets do not include the right of governments to generate future revenue from taxation, yet take into account liabilities that may not be incurred for over 100 years.**

audit qualification on good accounting grounds. The WGA include more than 7000 entities and, although IFRS has been adopted, the accounting boundary for the consolidated statements does not follow the concept of control as in IFRS10. The C&AG points to some serious omissions: for example, since 2008 the UK government has been the major shareholder in many of the large banks (eg RBS) whose assets and liabilities should therefore be included under IFRS in the consolidated statements of WGA.

The assets and liabilities of RBS would dwarf the financial position of the UK public sector. Looking at RBS's financial position at 31 December 2016, it then had assets of £799bn (WGA £1,903bn) and liabilities of £749bn (WGA £4,324 bn). In addition, the C&AG points out that WGA includes many bodies with different (ie not IFRS) accounting regimes. As an example, local authorities and charities follow codes designed specifically for them. Road network assets held by local authorities are valued at historical cost whereas highways under the central government Financial Reporting Manual are reported at depreciated replacement cost. The C&AG estimates that infrastructure assets are therefore likely to be understated by at least £53bn. There are also problems with entities with different year ends (eg school-year and solar-year) and high levels of uncertainty. As an example, nuclear decommissioning costs are very uncertain, the provision of £185bn in WGA relates to the best estimate of the cost at today's prices of decommissioning the plant, land, buildings and equipment on each designated nuclear site and returning them to pre-agreed end states – a programme of work that is forecasted not to be completed before 2137.

Thus, the accounting boundary, inconsistent policies, different year ends, and high uncertainty cause huge problems in reporting for the whole of the UK public sector. The WGA also reports, in 2017 fiscal year, deficit and net liabilities that do not correspond with the deficit and Public Sector Net Debt (PSND) used in UK budget documents from the statistically based National Accounts (government financial statistics). This is largely because PSND does not include non-financial assets (eg property, plant and equipment) or pensions of public sector employees.

Government financial statistics are, however, becoming more inclusive. IMF staff estimated on October 2018 the comparative net worth of 31 countries: the UK was shown to be next to the bottom ie in 30th place in its net worth, just ahead of Portugal, while the top five were shown as Norway, Russia, Kazakhstan, Australia and Peru (IMF, 2018b). Sheila questioned whether such analysis was meaningful, as the assets and liabilities of governments are not of a similar nature or definition to those of commercial bodies. For example, government assets do not include the right of governments to generate future revenue from taxation, yet take into account liabilities that may not be incurred for over 100 years. On the other hand, many liabilities that governments take on are unknown or even unforeseeable, eg the huge liabilities of global banks in the 2007–8 financial crash. Furthermore, what does net worth (or taxpayers' equity) mean? It is not akin to shareholders' equity where a shareholder has limited liability and cannot be asked to contribute further; a government can raise further revenue from citizens without providing anything in return. Public sector net worth must be interpreted in a different context from that of corporations.

Finally, Sheila argued that accrual-basis accounts are useful and informative, but we have to think deeply about what constitutes the purpose of public sector accounting and how it serves the needs of its users. Individuals must be very careful in the interpretation of public accounts and in their comparisons. She also looked briefly at some financial reports from a local NHS trust and queried whether layouts for balance sheets and operating statements based on those applicable for large commercial companies using IFRS were the most informative for users of hospital accounts.

Sheila then concluded by pointing out how public sector accounting faces many controversies and difficulties and how IPSAS are playing an increasing role. She also stressed how the IPSASB Conceptual Framework already acknowledges differences, but that these are not essentially reflected in standards as yet. Democratic accountability has served public sector accountability for many years and is embedded in the IPSASB Conceptual Framework. She finished by

**‘Accounts would be better used if they were prepared more often with the ultimate readers in mind’.**  
 (House of Commons parliamentary report 2017)

quoting from a 2017 parliamentary report (House of Commons 2017), ‘Accounts would be better used if they were prepared more often with the ultimate readers in mind’.

#### QUESTIONS AND ANSWERS

*Rhoda Brown (Loughborough University)* asked how the plurality of objectives in the public sector might be reflected not only by conceptual frameworks but also by accounts. Sheila answered by stating that there is a lot of diversity in the public sector, perhaps more so than in the private sector and additional reporting measures, key performance indicators (KPIs) and formats can be developed for the public sector.

*Lynn Bradley (University of Glasgow)* argued that the challenge is that decision makers are not using accruals to make decisions but different tools such as budgets. Sheila answered that in the short term this is probably true, in particular in the health services. Even so, she highlighted that, in the long term, to analyse efficient management of service provision the sector must look at accruals information though it may not necessarily be information based on fair value accruals.

*David Cairns (former secretary general of IASB 1985–1994)* agreed that public institutions should account for things

differently from the private sector but was uncertain on what points they should differ and questioned what the differences between the reporting in the two sectors should be in practice. Sheila answered that, for example, historic cost was not available when the public sector moved onto the accrual basis owing to the acquisition of some assets decades previously. Therefore, public accounts were set up on the basis of depreciated replacement cost and for accountability purposes perhaps this value is a better measure than historic cost or fair value as permitted in IFRS.

*Andreas Bergmann (former chair of the IPSASB)* queried the comparative information of the net worth of countries. Sheila responded that she found it difficult to believe the net worth of Peru was so much higher than that of the US or UK, for example. One difficulty is that the net worth figure does not have regard to the wealth of the citizens it has the right to tax, but this is very valuable in meeting liabilities.

*Geoffrey Whittington (Cambridge University)* stated that the public sector has always tried to measure income without having a traditional balance sheet and noted that balance sheet measurement is a waste of effort and time. Sheila agreed with him, adding also that the IFRS format is not helpful and it is, therefore, necessary to improve it.





## The Black Sun Review of Trends in Corporate Reports 2018

### Anne Kirkeby

As lead corporate reporting consultant at Black Sun and leader of the Research and Strategy team, which undertakes research and advises clients, largely FTSE 350 companies, on best practice and emerging trends in corporate reporting, Anne provided an overview of trends in narrative reporting in annual reports.

In her presentation, Anne talked about the role of Black Sun, a stakeholder communications company whose clientele comprises UK companies listed in the London Stock Exchange and other international firms. Black Sun helps businesses engage with their stakeholders using a wide range of communication tools. The objective of the company is to enable their clients to articulate their purpose and communicate how they deliver value through reporting that inspires and influences their important stakeholders. To meet this objective, the work of Black Sun is inextricably intertwined with a focus on understanding stakeholders' needs. As Anne explained, this focus is underpinned by the increasing exposure of companies to a large number of external forces that affect their corporate reporting practice.

### IMPACTS ON REPORTING

One of the forces that plays an influential role on corporate reporting is stakeholders' increasing empowerment, aided by the capabilities and continuous evolution of technology. As a result, companies are nowadays expected to acknowledge the voice of stakeholders and address their concerns through their annual reporting or any other means of communication with them.

Drawing on the findings of the 2018 Edelman Trust Barometer, Anne emphasised that corporate trust is another factor that has an effect on corporate reporting. The findings of the

Edelman survey indicated how the significantly low level of trust in corporations translated into people's lack of trust on companies' reporting (Edelman 2018). 'We tend to trust the people we know', Anne said while discussing the findings of the survey. Although government officials were found to be in the last position on the trust barometer, Anne lamented that corporate executives such as CEOs and boards of directors are getting closer to the bottom of the trust list. For Anne, this is a problematic situation which indicates that the messages delivered in corporate communication are not necessarily seen as trustworthy by businesses' audiences.

A third issue that has an impact on businesses' reporting lies in investors' demands for information beyond the financial statements, which will aid them to perform a more holistic assessment of the business. Investors are nowadays looking for intangible information that will help them evaluate the riskiness and potential future growth of a business. Anne emphasised the existence of a wide range of parameters that investors take into consideration to assess the sustainability of a business, including the culture of the business and the engagement with its stakeholders.

Anne showed that the importance of intangible information and its impact on corporate reporting is reinforced by the findings of the Ocean Tomo's study (2017). The study shows that intangible value is now deemed as being of higher

Factors such as brand, reputation and the ability of a company to grow substantially in the future are not evident in the financial statements of a business. In fact, these factors have become increasingly important for the valuation of a business.

importance than tangible value (Ocean Tomo 2017). Anne then mentioned that factors such as brand, reputation and the ability of a company to grow substantially in the future are not evident in the financial statements of a business. In fact, these factors have become increasingly important for the valuation of a business.

In an attempt to serve the needs of a wider society and respond to a series of corporate scandals, the UK government has put a lot of pressure on the reporting practice of companies through a wide raft of new regulations over several years, such as the updated guidance on the Strategic Report (FRC 2018a), the 2018 Corporate Governance Code (FRC 2018b) and the Companies (Miscellaneous Reporting) Regulation 2018. As Anne said, although the Companies Act stated that companies should have regard for stakeholders, in reality, companies have largely ignored this or certainly not expressed this in reporting. The Companies (Miscellaneous Reporting) Regulation 2018 aims to improve this by specifically describing what companies should be reporting about their engagement with stakeholders.

Beyond the aforementioned factors that have an effect on corporate reporting, Anne mentioned the proliferation of a multitude of reporting frameworks that companies could consider and include in their annual report or other reporting. This rapid rise in corporate reporting initiatives and the increased regulation is a challenge for companies but, most important, it points to the lack of transparency and indicates a broader lack of trust in companies' reporting.

### COMPANIES' RESPONSE

For the last 13 years, Black Sun has been producing the 'Complete 100' report which looks at the Strategic Report and Corporate Governance sections of the annual reports of all companies in the FTSE100 index. The purpose of the 'Complete 100' report is to help Black Sun's clients to develop best-practice reporting. Anne and her team assess how the narratives of companies in the index change over time. They also review how companies respond to already familiar but yet not established future regulations.

With regard to the changes in regulation and the way companies respond to these, Anne first referred to the Companies (Miscellaneous Reporting) Regulation 2018. Among other issues, this new legislation requires companies to include in the directors' report a discussion of how the business engages with employees and other stakeholders. The results of the 2018 'Complete 100' report shows that 61% of companies clearly identify their key stakeholders, while 14% provide examples of how the board had considered stakeholders in decision-making during the year (Black Sun 2018).

Second, as Anne stated, the updated Corporate Governance Code and guidance on the Strategic Report now focus more on stakeholders and society and an improved linkage between the governance statement and companies' strategic reports. The updated Code also requires companies to explain the role of diversity in their strategy and the board's evaluation of risks and opportunities. Black Sun finds that 56% of company annual reports discuss key resources and relationships in their business model. Nevertheless, only 7% clearly explain how diversity supports their strategy (Black Sun 2018).

A third regulatory change that was considered was the introduction of the Non-Financial Reporting Directive, which unfortunately came into place without clear guidance. The findings of Black Sun's study (2018) demonstrate that since the implementation of Non-Financial Reporting Directive, 92% of company reports discuss the issues of anti-bribery and corruption, 58% discuss due diligence processes, and 59% refer to an environmental policy.

### PRINCIPLES OF TRUST

Building on the results of Black Sun's study (2018) and the requirements of new regulations, Anne presented Black Sun's six principles that contribute to corporate trust. The so-called 'Principles of Trust', which consist of Purpose, Culture, Stakeholders, Diversity, Wider Value Creation, and Long-term Thinking, work as a messaging board, Anne argued. They form a set of new themes on which companies will have to report,

**Companies need to understand how a culture emerges and becomes established, design the appropriate systems and training to develop the right culture, set the measures of success and find ways of encouraging its expression.**

and Black Sun has provided specific guidance on what needs to be reported under each theme.

Anne then explained the story behind the title of Black Sun's study: 'Less Perfection – More Authenticity'. The title was carefully chosen to reflect the fact that these reporting concepts will be relatively new to companies. To restore or gain trust, preparers of annual reports need to understand the importance of reporting in a way that is authentic and company-centric. Companies are thus strongly encouraged to avoid generic statements. Rather, they should focus, and report, on what makes them authentic.

For instance, 'purpose' is one of the concepts introduced by both the Corporate Governance Code and the guidance on the Strategic Report. Although there are many ways for companies to discuss their purpose, Black Sun suggests that companies that aim to build trust need to communicate how they are part of the solution to societal challenges, rather than being part of the problem. Anne argued that the concept of 'purpose' has to some degree been described in annual reports for some time. Typically, companies tend to report their purpose (or 'mission' as otherwise stated by some companies) on the inside front cover of the annual report. The findings of Black Sun's study (2018) demonstrate that 66% of companies refer to their 'purpose', while 60% claim to have a purpose that goes beyond creating financial value. In fact, only 20% of companies actually discuss this 'purpose' in any of the executive statements. Anne commented that this finding suggests that, currently, the concept of purpose is not deemed by companies to be the backbone of their current strategy and future growth, and she urged for more attention to be paid to its reporting.

Through time, three categories of purpose reporting have evolved. Some companies describe a purpose which defines how they contribute to society. The concept of the purpose in this category is usually found only in the inside of the front cover of the annual report. Another group of companies might set out their purpose in the strategy section.

These companies tend to leave the reader to make the connection between the purpose and strategy of the company. The third group discusses their purpose throughout the narrative part of the annual report. Companies in this group consider the concept of purpose as if it is their compass, used to examine their existence and reiterate their direction of travel and means of getting to where they wish to be.

The case of Vodafone was selected by Anne to illustrate the importance of purpose reporting. The company devotes more than seven pages in its annual report to discussing its purpose. The example of Vodafone reflects how different aspects of the business, such as the strategy and business model, might feed into the purpose of the company and be supported by company-centric case studies and the chairman's statement. Anne emphasised that not all companies that follow the example of Vodafone are truly purposeful. As she said, it is very difficult to assess whether a company is purposeful. Nonetheless, as mentioned earlier, an important indicator is the authenticity provided by the company's narrative reporting.

The second principle of trust is culture, which, Anne said, saw a peak a few years ago owing to the development of a culture coalition by the Financial Reporting Council (FRC). The culture coalition was a collaboration of a number of interest groups, associations and corporates working on the importance of culture and, in particular, board and corporate culture. The Black Sun team has observed a steady state in culture reporting but, as Anne explained, culture takes time to evolve. Companies need to set processes and identify what culture they need depending on the nature of the industry in which they operate. They need to understand how a culture emerges and becomes established, design the appropriate systems and training to develop the right culture, set the measures of success and find ways of encouraging its expression.

Companies have now moved on from culture commitment to more actions. Nevertheless, Anne admitted that there is still a long way to go to make culture truly

**Wider Value Creation is the fifth principle of trust. This concept requires companies to adopt a multi-capital approach and, subsequently, to report on their impact on the financial, human, natural and other kinds of capital.**

central. Like the concept of purpose, the concept of culture in corporate reporting has evolved into three categories. Some companies are merely stating the importance of culture and then go on simply to list their values. Other companies explain how their actions embed a culture that reduces risk, while at the other end of the scale are companies that discuss how culture supports their overall operations. Anne gave Coca Cola Hellenic Bottling Company as an example of a company that discusses how culture supports its strategy and sets out explicit cases that demonstrate its 'values in action'.

Another principle of trust as presented by Black Sun is the concept of 'stakeholders', which has gained increasing attention in companies' reporting. Anne clarified that the notion of stakeholders encompasses a wide raft of parties, including customers, investors, employees, suppliers, and the government. The findings of the Black Sun (2018) study suggest that approximately 95% of companies state how they engage with stakeholders. Nonetheless, only a small percentage (19%) discuss how they actually use this engagement to design the future of the company and set their strategy.

In the evolution of stakeholder reporting, Black Sun has identified three approaches followed by companies. The first approach considers stakeholders as an important sustainability issue rather than a crucial business issue. The second approach is to report on the company's engagement with stakeholders and state that this engagement affects how the company thinks about future. Finally, the third approach is to discuss how stakeholders' expectations shape the company's strategy. For companies adopting this approach, understanding of stakeholders' needs and expectations is considered vital for their licence to operate, from both a short- and long-term perspective.

To explain how a company might describe best how it takes its stakeholders into account, Anne used the example of Marks & Spencer (M&S). Given the industry in which M&S operates, understanding of a particular

group of stakeholders such as customers seems crucial for the viability of the business. Thus, within the 2017 M&S annual report and, more specifically in the corporate governance report of the company, one can find extensive information about a wide stakeholder spread which the board considers in decision making.

The next principle of trust is diversity. Black Sun's study (2018) points to the superficial coverage of diversity issues by companies and reveals that only 7% of companies clearly explain how diversity supports their strategy. Anne referred to the three approaches that companies follow in diversity reporting. First, there are companies that describe diversity as a moral issue, as 'the right thing to do'. Second, some companies see diversity as a tool for controlling underused resources. The third approach, which Anne encourages companies to follow, is different in that it embraces variable kinds of diversity (ie gender, religion, race, etc) in the workforce of companies. Fostering such an approach will signal that the company's people are seen as a mirror of their other stakeholders, whose needs and demands are of critical value for the sustainable future of the company. This approach will improve companies' ability to prepare for and respond to market changes. Anne gave the case of Rentokil Initial plc as a great example of a company with authentic discussion in its annual report on how diversity supports strategy.

Wider Value Creation is the fifth principle of trust. This concept requires companies to adopt a multi-capital approach and, subsequently, to report on their impact on the financial, human, natural and other kinds of capital. In the Black Sun study (2018), 68% of the companies it covers declare their commitment to value creation for their stakeholders. Although this is a good step in the reporting of the concept, companies should also focus on discussing how they create intangible value. Issues such as brands, intellectual property (IP) and reputation are important intangible factors that are not captured in the financial statements of a company, yet they are crucial elements for long-term success and, therefore, should be sufficiently covered in annual reports.



**The last principle of trust is Long-term Thinking. This is one of the factors that companies know they should be talking about in their annual report as it is an important issue for their investors and other stakeholders.**

Anne described the Wider Value Creation as an interesting concept from an accounting perspective. She noted that some companies are starting to produce their non-financial factors in the same form as the Profit & Loss (P&L) statement. Regardless of its preparation for internal purposes, this P&L statement enables companies to look more carefully at their inputs to society in terms of human capital and their use of natural capital, with all the resulting costs to the society's welfare. As Anne explained, one of the reasons companies are not publishing this statement yet is because they have not reached the stage where the net result is positive. She argued, however, that once the methodology becomes more robust, the publication of this information will become an interesting development in future corporate reporting. Anne used the example of Antofagasta annual report for the year 2017, which provides ample company-specific details of key inputs and the cost base.

The last principle of trust is Long-term Thinking. This is one of the factors that companies know they should be talking about in their annual report as it is an important issue for their investors and other stakeholders. Anne commented that many of her client companies are nervous about the long-term story they need to present and still think that long-term thinking should include financial metrics. The advice she gives to her clients is that, numbers aside, what really matters is how companies are investing in softer indicators of long-term preparedness such as technology, research and development (R&D), and human capital.

To date, three approaches of long-term thinking reporting have been identified (Black Sun 2018). The first is simply to state that the company is making investments in the future, without giving further details and sufficient evidence. The second approach highlights clearly in various sections of the annual report the investments and changes the company is making to its portfolio. Unfortunately, in this case, long-term thinking information is scattered through the document, missing an appropriate link that would put all the pieces together to form a strong story.

Only a small group seems to follow the third approach, which connects all the necessary information by discussing how they have future-proofed themselves and how their strategic planning enables them to respond to future long-term structural trends.

Drawing on the case of the Coca Cola Hellenic Bottling company, Anne concluded her presentation. She illustrated how the front section of the company's 2017 annual report covers all the things that the company does to secure and improve its future. The document offers an overview of the company, describes how the company successfully understood and implemented prominent changes and, on this basis, asks its stakeholders to trust it in dealing with future changes. Using this retrospective approach, Anne stated that Coca Cola Hellenic clearly sets out its ability to understand and respond to market changes and provides a good argument about why the company should be trusted by stakeholders.

## QUESTIONS AND ANSWERS

*Anne's presentation was followed by questions from the audience.*

One of the participants of the Symposium asked Anne to clarify whether Black Sun has evidence to suggest that the Principles of Trust actually provide benefits and help companies build trust.

Anne responded that Black Sun's Principles of Trust have emerged from the company's experience with stakeholders and understanding of their needs over the last 25 years. The primary aim of the principles is to help companies develop a more relevant reporting practice with an annual report that is company-specific. As Anne explained, the implementation of all the principles does not necessarily lead to companies being more trusted. The role of the principles is to help companies become authentic and to implement new regulations that are reflected in the principles in an authentic way. For Anne, authenticity and trust are two sides of the same coin. If companies apply the principles in their reporting, then it is quite possible that they will build trust because they are being authentic.

**It is difficult for one to provide assurance as to whether a company is 'purposeful' or not. What one could determine, however, is whether the reporting of a company is company specific and, therefore, authentic.**

*Richard Slack (Durham University)* commented that many companies nowadays employ market consultants and designers to develop an embellished annual report. Looking at the annual report of Sports Direct, Richard argued that the company's section on investment in people and how they value and look after their people was an overstatement made by the company. Richard argued that there are two issues in annual reporting. First, there is an immediate built-in bias because one could already have a suspicion about some of the companies that Black Sun analyses. Second, looking at the annual report, one might find it very difficult to disentangle what is real from what is imagined.

Anne agreed with Richard's view. As she mentioned in her presentation, it is difficult for one to provide assurance as to whether a company is 'purposeful' or not. What one could determine, however, is whether the reporting of a company is company specific and, therefore, authentic. Anne stated that the only way of ensuring that the new regulatory reporting requirements, and hence the Principles, will not become just a communication exercise in which companies merely 'tick the box' is for companies to deem the principles to be an 'authenticity tool' and use them to report in a balanced, understandable and authentic way.

*Ron Hodges (Birmingham University)* asked Anne whether there are any government departments or public sector organisations that might offer similar guidance to companies about their reporting.

Anne answered that the FRC publishes guidance on reporting regulations while the International Integrated Reporting Council has produced the Integrated Reporting (<IR>) Framework and publishes regular guidance to support this.

*Richard Martin (ACCA)* recalled that in her presentation of the Long-term Thinking principle, Anne said that this concept can be reported without the use of numbers. Richard's view was that numbers and targets are important in reporting.

Anne clarified that she is also in favour of quantified future aspirations, in the form of numbers, targets and objectives, reported in the annual report. Nevertheless, she stated that where this quantification is not happening then companies should at least tell their long-term story by other means.

*Diogenis Baboukardos (University of Essex)* found that Black Sun's six Principles of Trust overlap with the guidance of the <IR> Framework on integrated thinking and value creation. He wanted to learn whether there is data from the analysis of annual reports that Black Sun conducts on an annual basis indicating an overlap between companies with good reporting and companies that claim to follow the <IR> approach.

Anne replied that the introduction of new reporting requirements will ultimately lead companies to the adoption of a more integrated approach in their reporting. Having said that, Anne stated that only seven FTSE 100 companies clearly declare that they produce an integrated report. She believes that owing to cultural constraints, companies in the UK that use <IR> elements might not state that they produce an integrated report until they think their reporting is of a good standard. In contrast, Anne provided the example of Netherlands, where companies will state that they produce an integrated report from the first year of their journey in the <IR> concept. She concluded by saying that there are many UK companies that might not clearly state the adoption of <IR> but that demonstrate clear characteristics of its philosophy in their annual reports.



## The Conceptual Framework of Financial Reporting (2018) – the IASB view

**Jianqiao Lu, IASB Member**

Jianqiao worked for the Chinese Ministry of Finance and is now an IASB member.

He gave a speech on the main revisions of the new IFRS Conceptual Framework, with some examples that highlight the main changes.

Jianqiao's presentation covered the following themes within the new Conceptual Framework: its purpose, history and status; the objective of general purpose financial reporting; qualitative characteristics of useful financial information; the elements of financial statements; recognition, derecognition and measurement; and the presentation of profit or loss and other comprehensive income.

### **PURPOSE, HISTORY AND STATUS OF THE CONCEPTUAL FRAMEWORK**

Jianqiao started the presentation by discussing what the Conceptual Framework is and why it is so important. He said that it is important because it sets out concepts that address fundamental financial accounting issues, including the objective of general purpose financial reporting, the qualitative characteristics of financial information, the definition, recognition, derecognition and measurement of the elements of financial statements, and presentation and disclosure of objectives and principles, etc. The Conceptual Framework assists the IASB Board in developing the IFRS Standards, which are based on consistent concepts, so that similar transactions are treated similarly in different IFRS Standards. The Conceptual Framework also assists financial reporting preparers to develop consistent accounting policies based on it, in situations where no IFRS Standard applies to a particular transaction or where an IFRS Standard allows a choice of accounting policy; and it also helps all stakeholders to understand and interpret IFRS Standards better.

On the history of the Conceptual Framework, Jianqiao stated that, in 1989, the IASB's predecessor's body, the International Accounting Standards Committee (IASC), issued the first version, *The Framework of Preparation and Presentation of Financial Statements* (the '1989 Framework'). He noted that this originated mainly from the Statement of

Financial Accounting Concepts issued by the US Financial Accounting Standards Board (FASB), which was developed in late 1970s and early 1980s. In 2010, the IASB issued two chapters of a revised Conceptual Framework which updated the 1989 Framework on the objective of financial reporting and the qualitative characteristics of useful financial information. The IASB restarted the project in 2012. After consulting various stakeholders and numerous deliberations, the IASB finalised the revisions to the Framework and issued the revised Conceptual Framework in March 2018.

Jianqiao sees many improvements in the revised Conceptual Framework compared with the previous version. The main improvements include those listed below.

- The revised Conceptual Framework fill gaps in its predecessor by adding new concepts and guidance on measurement, derecognition, and presentation and disclosure, including the presentation of profit or loss and other comprehensive income (OCI) because these areas were not covered by the previous version.
- The revised version clarifies some important concepts, including the roles of stewardship and prudence in financial reporting, because these concepts were unclear in its predecessor.
- The revised version updates the definitions of an asset and a liability



**The main objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to users in their decision making.**

and recognition criteria because some of the elements in the definition and recognition of an asset and a liability in the previous version were out of date. In particular, the revised version clarifies how to take into account the role of uncertainty in recognition of an asset or a liability.

Jianqiao illustrated the importance and implications of these improvements to the Framework in the context of current digitalisation and the Big Data environment. He gave an example of the Alibaba Group, whose market value is much higher than the book value of its net assets recognised in the statement of financial position. He said that one of the reasons why investors preferred to pay a price much higher than the book value for Alibaba's shares might be that they considered that, given the market for big data (large, diverse data sets that grow at ever-increasing rates) and the relevant unrecognised intangible assets Alibaba held, these were its most valuable 'assets'. Jianqiao mentioned that the sources of a company's value creation, including the business models, have changed significantly in the current digitalisation environment. Therefore, the improvements made to the Conceptual Framework will be helpful in exploring whether a firm's Big Data and existing unrecognised intangible assets meet the updated definition of assets and recognition criteria, or whether enhanced disclosures are needed to provide more relevant information for investors.

As far as the status of the Conceptual Framework is concerned, Jianqiao stated that it is not a Standard and therefore it is not mandatory and does not override the requirements of the IFRS Standards. It underpins the IASB's decisions in setting Standards, but the IASB can depart from some of its aspects in some circumstances in order to meet the main objective of financial reporting. If so, these departures need to be explained in the Basis for Conclusions of the IFRS Standards, where the rationale for the amendments is explained and the considerations of the IASB summarised.

## **THE OBJECTIVE OF GENERAL PURPOSE FINANCIAL REPORTING**

The main objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to users in their decision making. Jianqiao said that the revised Conceptual Framework clarified the role of stewardship in the above main objective of general purpose financial reporting. The investors' decisions, as clarified in the revised version, are not only limited to buying, holding or selling shares and providing or settling loans but also include decisions made while holding investments, such as decisions about voting to retain or replace management or otherwise influencing management's actions. To make these decisions, investors need to assess not only the amount, timing and uncertainty of future net cash inflows to the entity, but also management's stewardship of the entity's economic resources. Therefore, financial reporting needs to provide relevant information to help users make both these assessments. Jianqiao also mentioned that financial reporting should provide relevant information not only about an entity's economic resources, but also about the risks inherent in those economic resources and how management has managed these risks. This information will help management discharge its responsibilities (eg risk-management responsibilities) and help users to evaluate management's performance and accountability.

## **QUALITATIVE CHARACTERISTICS OF FINANCIAL INFORMATION**

The revised Conceptual Framework specifies the two fundamental qualitative characteristics of useful financial information: relevance and faithful representation. They are two 'must-have' characteristics. Jianqiao said that the IASB did not make fundamental changes to the descriptions of relevance and faithful representation that were included in the 2010 version of the Framework. Nonetheless, the revised version did clarify the three following issues.



The notion of prudence should support the achievement of faithful representation and neutrality, discouraging the overstatement or understatement of assets, liabilities, income or expenses.

- **Firstly, it reintroduced the concept of prudence and clarified its role.** Jianqiao explained that the IASB decided to remove 'prudence' from the 2010 version because of concerns that 'prudence' could lead to 'cookie jar' reserves and earnings manipulation. When making this decision, the IASB was aware that the concept of 'prudence' was being used by some to justify the deliberate understatement of assets and income and the overstatement of expenses and liabilities. Therefore, the IASB decided to remove it from the Conceptual Framework. The 2010 Basis of Conclusion explained that prudence in this sense was inconsistent with neutrality because it introduced bias.

Jianqiao mentioned that the feedback the IASB received after the 2010 version was issued showed that some had misinterpreted the removal of the term 'prudence' as meaning that the IASB did not acknowledge the need for caution when making judgements. This was clearly not the intention. Therefore, the IASB decided to reintroduce the notion of prudence and clarified its meaning and role in the revised Conceptual Framework. 'Prudence' is defined as the exercise of caution when making judgements under conditions of uncertainty. It does not mean systematically recognising expenses and liabilities at an earlier stage than income and assets. The notion of prudence should support the achievement of faithful representation and neutrality, discouraging the overstatement or understatement of assets, liabilities, income or expenses. In the meantime, asymmetric requirements in some specific IFRS standards can emerge if they are intended to result in the most useful information. Jianqiao provided, as an example of the application of prudence and specific asymmetric requirements, the impairment test for a plant. In case of a significant decrease in the value of the asset, companies can recognise the impairment loss when the recoverable amount is lower than the carry amount. Nonetheless, if the recoverable amount is higher than the carry amount, the standard does not allow recognition of this higher value.

- **Secondly, the revised Conceptual Framework clarified the role of substance over form.** Jianqiao explained that the revised version makes it clear that financial information must faithfully represent the substance of the economic phenomena that it purports to represent. Jianqiao also emphasised that in most cases legal forms reflected the substance of a transaction, so considering the legal form was important for, and would normally be the first step in, understanding the substance of a transaction.
- **Thirdly, the revised Framework clarified the relationship between reliability and faithful representation.** Jianqiao also explained how the concept of reliability has been clarified. He said that the term 'reliability' was removed in the 2010 version. The main reason for the removal was that many companies seemed to equate 'reliability' solely with information being verifiable or free from material error, or even being accurate in all aspects. In the revised Conceptual Framework, the IASB clarified that the description of faithful representation is substantially aligned with the description of reliability in the 1989 Framework. It also affirmed that reliability does not mean a lack of estimation uncertainty. In some circumstances (eg when monetary amounts cannot be observed directly and need to be estimated), estimation is necessary and measurement uncertainty arises. In practice, even a high level of measurement uncertainty does not prevent such an estimate from providing useful information.

Jianqiao also stated that the revised Conceptual Framework had not changed the meaning of the following four 'nice-to-have' qualitative characteristics: comparability, verifiability, timeliness and understandability, which support the two fundamental qualitative characteristics of relevance and faithful representation. Jianqiao argued that the four 'nice to have' qualitative characteristics enhance the usefulness of information but cannot make non-useful information useful. On the cost constraint, Jianqiao said that there was no difference between the 2010 version of the Framework and the 2018 version.

An asset is now defined as a present economic resource controlled by the entity as a result of past events, and an economic resource is defined as a right that has the potential to produce economic benefits.

### THE ELEMENTS OF FINANCIAL STATEMENTS

Jianqiao pointed out that the five elements of financial statements, namely assets, liabilities, equity, income, and expense had not changed but changes have been made to the definitions of these elements, in particular the definitions of an asset and a liability.

Jianqiao mentioned that the revised definitions of an asset and a liability focus on an entity's rights and obligations rather than on the ultimate inflow or outflow of economic benefits.

An asset is now defined as a present economic resource controlled by the entity as a result of past events, and an economic resource is defined as a right that has the potential to produce economic benefits. The new definition of an asset clarifies several things.

- Firstly, the new definition of an asset focuses on rights rather than flows of economic benefits or physical objects or legal ownership of a physical object. Traditionally, when we described something as an asset, we may have focused on a physical object, but now we need to focus on the right to the object: a right based on the new definition of an asset. Jianqiao provided an example of leases. When an entity leases a property from a lessor for a few years, the entity does not benefit from the ownership of the physical asset it leased, but, rather, it obtains the right to use that asset in the next few years. Thus, that right should be recognised as an asset based on the new revised definition of an asset.
- Secondly, an asset is a right that has the potential to produce economic benefits. It does not need to be certain, or even likely, that there will be a flow of economic benefits. It is only necessary that the right already exists and that, in at least one circumstance, it would produce for the entity economic benefits beyond those available to all other parties.

- Thirdly, the inflows of economic benefits no longer have to be 'expected', as was the case in the previous definition, because the term 'expected' was interpreted by some people as a probability threshold. Given the new revised definition, a right can meet the definition of an asset even if the probability that it will produce economic benefits is low. Even so, that low probability might affect recognition and measurement decisions.

A liability is now defined as a present obligation of the entity to transfer an economic resource as a result of past events. Jianqiao mentioned that the key to understanding the new definition of a liability was that the new definition emphasises that the obligation should lead to a potential transfer of economic resource and, importantly, that the entity had no practical ability to avoid the transfer. Jianqiao provided an example of a furniture shop that sells furniture to a customer to illustrate how to apply the concept of 'no practical ability to avoid' when making a judgement about whether an obligation exists. There is no explicit contract signed between the customer and the shop on the guarantee of the furniture. Nonetheless, a general announcement of two-years' guarantee on the furniture is stated on the shop's website. From the shop's perspective, the guarantee shall be treated as a liability because there is a responsibility arising from the shop's published statement and the shop may not have the practical ability to act in a manner inconsistent with the statement and, therefore, the shop may not have the practical ability to avoid the transfer of an economic resource, even if no defects have yet been reported. Again, the wording on the notion of an 'expected' outflow of economic benefits was removed from the definition of a liability to avoid the link with probability thresholds.

The definitions of income and expenses in the revised Conceptual Framework are based on those of assets and liabilities, but Jianqiao pointed out that information about income and expenses is just as important as information about assets and liabilities.

**Uncertainty is a key aspect of current financial accounting, and the IASB has made significant and productive progress on addressing this issue in the revised Conceptual Framework.**

### **RECOGNITION, DERECOGNITION AND MEASUREMENT**

Jianqiao stated that the revised Framework made some significant improvements to the recognition criteria. In order to recognise an item as an asset, a liability or equity, an item must meet both the definition of these elements and the recognition criteria. The revised version states that an asset or a liability is recognised only if such recognition provides users of financial statements with useful information, namely, information about that item that is relevant and provides a faithful representation of the asset or liability and of any resulting income, expenses or changes in equity. Jianqiao pointed out that one of the main contributions of the updated recognition criteria was that it clarified the role of existence uncertainty and measurement uncertainty in the recognition criteria.

Jianqiao also stated that new guidance on derecognition was added to the revised Conceptual Framework. It states that derecognition normally occurs when that item no longer meets the definition of an asset or a liability. Jianqiao mentioned that the Framework describes two aims of derecognition: faithfully representing both the assets and liabilities retained in a transaction and the change in the entity's assets and liabilities as a result of the transaction. Jianqiao clarified that an entity might need to continue to recognise a transferred component if derecognition was not sufficient to achieve the two aims.

The measurement part of the revised Framework, as Jianqiao explained, has been significantly improved because the previous version had little to say about it. The revised version categorises measurement bases into historical cost bases and current value bases. It also specifies the factors to be considered in selecting a measurement basis, including

relevance, which is affected by the characteristics of the asset or liability and how that asset or liability contributes to future cash flows, and faithful representation, which is affected by accounting mismatches and measurement uncertainty.

### **PRESENTATION OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME (OCI)**

Jianqiao stated that the revised Conceptual Framework emphasises that the statement of profit or loss is the primary source of information about an entity's financial performance. The revised version also emphasises that the statement of profit or loss is not the only source of information about financial performance. To understand an entity's financial performance, users need to consider all income and expenses, including those reported in OCI, which is a measure of income and expenses that have yet to be recognised in profit or loss in accordance with IFRS standards. Jianqiao explained that the IASB expected the use of OCI only in exceptional circumstances. Jianqiao emphasised that only the IASB could take decisions on whether an item should be included in OCI and whether the item in OCI should be reclassified (recycled) to profit or loss.

To summarise his presentation, Jianqiao highlighted that the revised Conceptual Framework contains many changes. The objective of financial reporting and the two fundamental qualitative characteristics of useful information (ie relevance and faithful representation) play a central role in the revised version. It is evidence of their close linkage with the concepts of recognition and measurement. Finally, Jianqiao mentioned that uncertainty is a key aspect of current financial accounting, and the IASB has made significant and productive progress on addressing this issue in the revised Conceptual Framework.

**In practice, if there is no active market available for the cryptocurrencies, it would be very difficult to find a valuation model to measure them at fair value or estimate their current value.**

## QUESTIONS AND ANSWERS

*Maryam Sutherland-Khan (Robert Gordon University)* asked how much consideration the IASB gave to concepts such as crypto-assets and cryptocurrencies in measurement and recognition.

Jianqiao Lu replied that the IASB and the IFRS Interpretation Committee had recently (starting in 2016) discussed the accounting issues arising from the cryptocurrencies, but he said that he did not think this specific issue was discussed when developing the Conceptual Framework. Jianqiao also mentioned that at the World Standard-setters meeting in October 2018, the IASB discussed with national standard setters how to apply the concepts in the revised Framework to transactions involving cryptocurrencies. Jianqiao's opinion is that, in most of the transactions, the cryptocurrencies held by an entity seem to meet the definition of an asset because the entity has the right to sell or exchange the cryptocurrencies, which have the potential to produce economic benefits. On the measurement of cryptocurrencies, if there is an active market for them, measuring at fair value might provide the most useful information to users. In practice, if there is no active market available for the cryptocurrencies, it would be very difficult to find a valuation model to measure them at fair value or estimate their current value. In addition, current value measurement may be very costly, or measurement uncertainty may be so high that the resulting estimation may not provide useful information to users. Jianqiao states that there is still a lot of research work to do in this area, especially about measurement uncertainty.

*Hesham Bassyouny (University of Portsmouth)* asked what value is added by the section on presentation and disclosure within the Conceptual Framework.

Jianqiao Lu replied that the section on presentation and disclosure in the revised version states the objective of presentation and disclosure and the principles of classification and aggregation of the items in the financial statements. Items that are economically similar can be aggregated, while dissimilar items should not be aggregated, as inappropriate aggregation could weaken the relevance of the information. In practice, some people may claim that the presentation and disclosure section of the revised Conceptual Framework might not provide enough guidance in this area. Jianqiao acknowledged that it only addressed basic concepts of presentation and disclosure; for detailed principles of presentation and disclosure, people would need to look at IAS 1, Presentation of Financial Statements. Jianqiao also noted that the IASB's current active project on 'Primary Financial Statements' focuses on how to improve the structure and content of the primary financial statements and the disclosures in the notes, especially the performance statement. The proposals in this project build on the concepts in the revised Conceptual Framework.

*Richard Slack (Durham University)* argued that, for assets' recognition, prudence actually impairs faithful representation, as it leads research and development (R&D) expenditures to be recognised as expenses rather than capitalised as assets. This is because preparers and auditors are both scared of future write-downs.

Jianqiao Lu replied that the accounting for R&D was addressed in IAS 38, Intangible Assets. Under the IAS 38, not all R&D expenditures are recognised as expenses. The development expenditures will be recognised as assets if they meet certain criteria. Nonetheless, Jianqiao



**The revised version states clearly that the exercise of prudence does not imply a need for asymmetry. Although some specific IFRS Standards might contain asymmetric requirements, they were intended to result in the most useful information.**

acknowledged that IAS 38 was developed many years ago and some elements of the Standard may need to be updated. He welcomes academic support and research on this topic, based on the revised Conceptual Framework, by exploring whether R&D expenditures or similar expenditures meet the definition of assets and recognition criteria and, if not, whether enhanced disclosures are needed.

*Omiros Georgiou (Manchester University)* stated that the IASB was worried about systematic asymmetry when it defined prudence in the new Framework. In its predecessor (1989), systematic asymmetry was not permitted and, therefore, Omiros wondered where the concept of systematic asymmetry comes from and whether it was a conceptual or practical issue for the IASB.

Jianqiao Lu replied that the revised version states clearly that the exercise of prudence does not imply a need for asymmetry. Although some specific IFRS Standards might contain asymmetric requirements, they were intended to result in the most useful information. He gave an example to illustrate the implications of this notion. He said that, during the 2007–8 global financial crisis, some regulators wanted to introduce systematic asymmetric accounting treatments in financial reporting in order to require companies to accrue more provisions (liabilities) and expenses, even though these amounts were not expected to occur. In Jianqiao's view, however, those sorts of asymmetry are not consistent with the objective of financial statements and the qualitative characteristics of useful information.



## The Conceptual Framework of Financial Reporting after the 2018 IASB Revisions

**Geoffrey Whittington, Emeritus Professor, University of Cambridge**

Building on his professional experience as a chartered accountant, consultant, member of the UK Accounting Standards Board and his academic career, Professor Geoffrey Whittington offered an overview of the revised International Accounting Standards Board (IASB) Conceptual Framework. Geoffrey provided a commentary which highlighted the positive elements of the Framework, pointed to some problematic issues and concluded with areas that need further development.

### **EASY CRITICISM: A CAMEL IS A HORSE DESIGNED BY A COMMITTEE**

This phrase was used by Geoffrey at the beginning of his presentation in an attempt to provide a first critique of the revised Conceptual Framework (IFRS 2018) and the work of IASB members. Following on Whittington's own study (2008a) and after an examination of the first chapters of the Framework on the Objectives and Qualitative characteristics, Geoffrey identified a heavy dependence of the chapters on the American revision of its own Framework by the FASB.

With regard to the very short, final chapter on Capital Maintenance, Geoffrey considered it to be a copy of the 1989 Framework published by the International Accounting Standard Committee (IASC). Geoffrey lamented that this lack of revision on the Capital Maintenance chapter is indicative of IASB's poor thinking over the previous 29 years.

The in-between chapters demonstrate a mixture of improvements in the sense that they include the systematic application of the concept of faithful representation on reliability, although Geoffrey did not regard that necessarily as improvement. They also include a new section on measurement, which Geoffrey called 'half-hearted innovation' as it does not provide adequate guidance, is neither complete nor thorough enough and does not meet the IASB's criteria for recognition in accounts. Geoffrey argued that Chapter 4,

with its clarification of the definition of assets and liabilities, is a real step forward in the revision of the Framework.

### **DEFENCE: A CAMEL IS VERY ADAPTED TO ITS ENVIRONMENT – IT MAY NOT BE PRETTY, BUT IT IS FUNCTIONAL**

Geoffrey then followed these criticisms of the revised Conceptual Framework with some supporting arguments. Although the updated Framework has not met its purpose, one cannot deny its functionality. Looking at the purpose of the Framework, it is clear that the IASB has tried to build a common language to create greater comparability and consistency in accounts when applied to the accounts of companies listed on stock markets. This allows the comparison of companies, particularly at an international context (Whittington 2008b).

The purpose of the Framework has been revised to aid the IASB primarily in standard setting. It is also quite useful for preparers and users of accounts who seek to understand the aims of the IASB. Geoffrey clarified that the purpose of the Framework is not to produce a set of assumptions from which one could deduce a single set of optimal standards. It is not a set of axioms that the IASB produces, he claimed. Rather, the Framework is designed to provide information for users that helps them make their decisions, such as deciding what a firm is worth or whether the management has acted wisely.

Measurement is another issue that has been added and is seen as one of the big improvements in the revised Conceptual Framework. Geoffrey stated that the IASB's retreat from fair value is a big step forward.

### HISTORICAL EVOLUTION OF THE FRAMEWORK

As Geoffrey explained, a constraint on the Framework is that it starts from an established position, embodied in existing standards. In his view, it is clear that the 'new' 2018 Framework is the old one with changes bolted on. Geoffrey then outlined the historical evolution of the Framework.

The IASB started off the Conceptual Framework in 1989 by summarising the FASB's position, which in the FASB Framework had a strong investor and future cash flow orientation but failed to resolve the issue of measurement.

In 2004 the FASB and IASB jointly started their review of the Conceptual Framework. The project was mainly staffed and driven by the FASB and resulted in the development of lengthy chapters such as the one on Objectives and Properties.

In 2010 the IASB and FASB decided to suspend their joint project and go their individual ways. The IASB resumed work independently in 2012 but demonstrated no intention of revisiting the FASB chapters. Instead, the IASB made some small alterations such as adding emphasis on stewardship. Nonetheless, the substance of the first two chapters has remained the same since the time of the collaboration with FASB.

In the following years, the IASB made some progress. In 2013 it produced a discussion paper followed by an Exposure Draft in 2015, and in 2018 it published the final version of the Conceptual Framework. Geoffrey deemed the effort as cobbled together, but he gave credit to the IASB for the progress made, given the constraints that the body is under.

### PATCHING-UP HISTORY

Geoffrey then discussed how the Conceptual Framework developed through the above process.

As he had mentioned earlier, before 2010 the Framework was primarily FASB dominated and led to the emergence of the 'Fair Value View' (Whittington 2008a). The Fair Value View assumed perfect and complete markets and assumed a

constantly accessible fair value with zero transaction costs. Fair value could then be used to produce a balance sheet to value the firm, if all assets and liabilities were included.

At that time, the concept of stewardship was ignored as it looked backward, related to accountability and, therefore, was not fundamental to investor decision making. That said, Geoffrey clarified that stewardship can be forward-looking but because of its confirmatory and less predictive nature is considered a conservative rather than a decision-useful concept. Stewardship was reinstated in Chapter 1 by the IASB and has a place in the 2018 Framework.

The concept of prudence is connected to stewardship. In the Framework of the joint project, prudence was rejected as it fostered an agency theory perspective which viewed accounting as an appraisal of past events and examined the performance of the firm, the actions of the management and the existence of incentives for managers to show themselves in a good light. Prudence has been reinstated but, choosing between the symmetrical and asymmetrical type, IASB has embraced symmetrical prudence. Although symmetrical prudence is generally rejected, it is still permitted when it serves the purposes of accounting. Geoffrey argued that despite the progress made in decision usefulness and predicting future cashflows, the IASB has adopted an unsupportive stance towards the concepts of stewardship and prudence.

Measurement is another issue that has been added and is seen as one of the big improvements in the revised Conceptual Framework. Geoffrey stated that the IASB's retreat from fair value is a big step forward. The updated Framework avoids the use of a unique measurement method; rather, it welcomes the use of mixed measurement methods that will be chosen on the basis of the facts and circumstances of the case and, in particular, the nature of the specific asset or liability.

Nevertheless, Geoffrey noted that the description of the alternative measurement methods is clumsy, inadequate, and incomplete. As he explained, the description does not

**Under the revised Framework, the omission of expected cash flows clearly signals the importance given to present assets and liabilities.**

discuss deprival value. Similarly, historical costs are described as incorporating impairment tests where lower market values are chosen. The description of current cost is not clear because the IASB describes replacement cost without providing further information about its actual definition and meaning. Geoffrey claimed that the IASB was ignorant of the theoretical literature on measurement and failed to improve the capital maintenance reporting that was superficially written in the 1989 IASC Framework.

Another problematic area in the Conceptual Framework was the concept of recognition. In Geoffrey's view, the new definitions of assets and liabilities have improved the concept. In particular, the new definition of an asset excludes the idea of the 'probable future economic benefit test'. The IASB has instead redefined the asset as a right, or more precisely, a present resource. Nevertheless, Geoffrey argued that the replacement of the reliable measurement test by the concept of faithful representation and the use of individual standards for the assessment of whether an asset could lead to important cashflows were issues of practical concern.

With regard to the notion of faithful representation, Geoffrey described it as a pervasive problem originating in Chapter 2 of the Conceptual Framework that was developed by FASB and IASB during the joint project (the 1989 version). Faithful representation should represent an economic phenomenon accurately. Nevertheless, the Framework fails to provide sufficient guidance of what an economic phenomenon represents. Geoffrey said that the notion of faithful representation was substituted for reliability, with added overtones of relevance that have minimised the effect of the trade-off between relevance and reliability.

## CONCLUSION

Geoffrey's overall conclusion was that the 2018 Conceptual Framework has improved to a large extent, especially if one takes into consideration that the definitions of assets and liabilities now tie in with the view of accounts as stewardship records. Moreover, under the revised Framework, the omission of expected cash flows clearly signals the importance given to present assets and liabilities.

Nonetheless, the updated version of the Framework is not without its faults. Geoffrey argued that there are many issues that are unfinished business for the IASB. These include matters such as the faithful representation concept, the rejection of asymmetric stewardship and the lack of proper discussion of measurement. Geoffrey recommended that more research needs to be done on fundamental areas that have fed back into the improvements of the Framework. One of these is the issue of probability and uncertainty and how these are captured in the accounts. Next, more research work could explore the entity approach as described in the Framework. Geoffrey explained that the Framework reports the adoption of an entity view; that is, accounting for the whole entity. Yet, he argued that the treatment of physical and financial capital maintenance is more closely related to the proprietary rather than entity approach. He suggested that future research on this topic could lead to the clarification of this complexity. Finally, an unsolved problem which could be an additional possible research avenue for academics is the issue of equity. Geoffrey encouraged researchers to explore the complicated phenomena of what the equity of a business is and how it can be disclosed in the accounts.



**In Geoffrey's view, there was an attempt to discredit reliability as he argued that the new concept was even more vague and complicated.**

### **QUESTIONS AND ANSWERS**

*At the end of the presentation, the audience had the chance to ask Geoffrey questions.*

*Paul Jennings (University of Winchester) asked Geoffrey whether he believed that people's confusion between a general concept of reliability and specific processes of reliable measurement was actually contributing to the debate between reliability and faithful representation.*

Geoffrey noted that it was an allegation made by the FASB which he did not support. In his view, there was an attempt to discredit reliability as he argued that the new concept was even more vague and complicated.

*Richard Martin (ACCA) wanted to know Geoffrey's opinion about the discrepancies in the definition of liability as found in the Conceptual Framework and the IASB's latest discussion paper on equity.*

Geoffrey answered that both the Framework and the project on equity were work in progress. He considered that the definition of liability in the Framework has undergone a satisfactory improvement. As he explained, if the equity project resulted in further improvements or research found inconsistencies in the Framework's definition, then the latter should be revised.



## 3. Discussion

### SUMMARY OF SPEAKERS' PRESENTATIONS

The five speakers presented a variety of diverse themes and ideas, although with some commonalities. There was a particular concentration on public sector accounting and the Conceptual Framework. A summary of their respective views is given below, followed by a brief synthesis of the themes.

#### Andreas Bergmann (Institute of Public Management)

*Andreas Bergmann spoke as chair of the IPSASB and a professor of public finance. In his presentation, he discussed the functioning of the IPSAS and the IPSASB work programme.*

Andreas started his presentation by illustrating the structure of IPSAS, the composition of the IPSASB and its role within public sector financial reporting. During his presentation, Andreas focused on IPSAS-based accrual accounting, which is part of a process that involves budgeting, accounting, auditing and governmental financial statistics. He pointed out that public sector accrual accounting implementation is expected to increase in countries adopting the accrual basis, while its use is expected to decrease in both countries adopting cash-based accounting and in those transitioning from cash to accruals.

Andreas illustrated the current IPSASB work programme, highlighting the convergences between public-sector-specific content and IFRS on non-exchange expenses, revenue and financial instruments. He pointed out that in some other areas, such as social benefit, public sector measurement, heritage, infrastructure assets and leases, conceptual frameworks specific to the public sector are still in place. Andreas then illustrated the new IPSAS 42 on social benefits. He explained that the new standard helps to solve a critical issue on social benefits: the identification of the moment in which liabilities related to social benefit should be recognised. In the new IPSAS 42, a liability must be recognised when the government has a legal obligation to transfer cash to an individual. Andreas then illustrated the work of IPSASB on non-exchange expenditures and revenues. He stressed how, at the time of the symposium, there were still no standards on expenditures, but only on revenues, even though this issue has been heavily debated in several consultation papers. He illustrated the standards on revenues and explained the differences between exchange and non-exchange revenues. Exchange revenues are constituted by enforceable agreements, with performance obligations for transferring goods or services to customers on commercial

terms, while non-exchange revenues do not involve performance obligations or stipulations. Andreas outlined that the difference between the two categories of revenues is not always clear, particularly when revenues come from enforceable agreements, with performance obligations or stipulations to use or consume resources in a specific way, or from agreements requiring resources to be used over a specified period. The IPSASB is analysing these cases through a public sector performance obligation approach, with the aim of changing the performance obligation approach used by IFRS15 to cover this 'shaded area'. Andreas discussed the project of achieving convergence with the IFRS15, noting that there will be no changes in the recognition and measurements for exchange revenues, but minimal changes on terminology to reflect more accurately the nature of the public sector. Andrew also explained how the public sector performance obligation (the 'shaded area') follows the five steps from IFRS 15:

1. identify the binding arrangement
2. identify all the performance obligations
3. determine the transaction price
4. allocate the price to the performance obligations, and
5. recognise revenue as the performance obligations are fulfilled.

Sheila started her presentation by highlighting that public sector accounting is moving towards an accrual basis even though it has historically been predominantly cash-based.

He highlighted the difficulties in implementing the first step (identifying the binding arrangement), which arise because in the public sector most obligations are not identified by binding arrangements but by laws. Despite this, and some difficulties on the second step (identifying performance obligations), no further issues exist in relation to the other three steps.

Andreas continued his presentation by discussing the aim and work of the EPSAS, an accrual basis accounting system aimed at improving the accounting and budgeting system of the EU Member States. He explained that the project is entering the so-called Phase 2, which aims at addressing the issue of comparability within and between the Member States in the medium to long term. This might not be an easy task to perform since no EPSAS standard has been yet issued and thus compatibility with IPSAS could not be assessed. Despite this, Andrew noted that because issued papers take IPSAS requirements as their main reference, it is quite likely that they are going to be very similar, but it is too early to know. He then discussed the differences between GFS and IPSAS, explaining that while GFS consolidates all levels of government but does not include their SOEs, IPSAS specify that governments consolidate what they control, such as SOEs.

Andreas concluded by arguing how academics admitted the lack of a theoretical basis for public sector accounting. He commented on the main theories used to inform the main studies on public sector accounting (eg accountability theory, new public management, critical theory, new institutional theory), arguing that they are either not very strong or not real accounting theories. He concluded by arguing the need to develop a theoretical basis for public sector accounting to help to draw more relevant results from future research.

### Sheila Ellwood (Professor at the University of Bristol)

*Sheila Ellwood is professor of financial reporting at the University of Bristol. Drawing on her research, she explained the importance of conceptual frameworks in public sector accounting.*

Sheila started her presentation by highlighting that public sector accounting is moving towards an accrual basis even though it has historically been predominantly cash-based. She questioned the transitional process that public sector accounting is going through. She criticised the EU transition toward EPSAS as it is happening extremely slowly with no EPSAS issued yet. She then commented on other countries such as New Zealand, which adopted IFRS on a sector-neutral basis across the private and public sectors; China, which is moving to an accrual basis with specific characteristics, and the US, which provides consistency across sectors at a transactional level. She also criticised the fact that developing countries have had sophisticated accounting practices imposed by international authorities but lack the culture, training and expertise to operate such practices. Sheila then illustrated the arguments for and against the adoption of accrual basis accounting in the public sector. On one hand, it provides useful information and allows effective measurement of goods and services consumed, income earned, and ownership capital. On the other hand, the accrual basis is costly to operate, introduces subjectivity and creativity into financial reporting and might be less effective than the alternative.

Sheila continued her presentation by illustrating the Conceptual Framework of IPSAS and its aims. She discussed the pros and cons of having a common framework rather than having a specific public sector framework. On the one hand, a common framework improves the similarity of treatment of transactions, creates comparability, and reduces scope for government manipulation. On the other hand, a common framework is difficult to implement because of the different character of financial reporting in the public sector from that in the

**Stakeholder empowerment is an issue as companies are expected to acknowledge the voice of stakeholders and address their concerns through their corporate reporting.**

private sector. The organisational purpose is not shareholder wealth maximisation but improving citizens' well-being. Sources of revenues are not predominantly market transactions based on consumer decisions, but taxation. Stakeholders are not concerned about profitability but on how money is spent. Sheila outlined that because of these differences, transferring a framework from the private sector may be unsuitable and may lead to manipulation and confusion. Sheila then discussed the differences in the aims and purposes of the Conceptual Framework provided by IASB and IPSASB and questioned whether the existence of such different purposes could generate different information needs. She supported her questioning by quoting previous academic studies in accounting that highlight the different needs for information for accountability/ stewardship purposes and for decision-making purposes.

Sheila then discussed the WGA for the UK for 2016–17, which had received a qualified audit report, as in every previous year. She then illustrated the issues arising from the audit report. Although IFRS has been adopted, the accounting boundary for the consolidated statements does not follow control as in IFRS10. This, Sheila argued, leads to the omission from the WGA consolidated statements of assets and liabilities of companies where the UK government is a major shareholder. In addition, the report points out the inclusion in the WGA of many bodies with different accounting regimes (not IFRS), different year ends and high levels of uncertainty. All these issues are the cause of huge problems in reporting for the whole UK public sector. Sheila also illustrated another issue arising from the WGA: the fact that the year deficit and net liabilities reported in the WGA do not correspond with the deficit and PSND used in UK budget documents from the statistically based National Accounts. This is because the PSND does not include non-financial assets and non-financial liabilities. She then illustrated the comparative net worth of 31 countries in a ranking prepared by the IMF, in which the UK was shown to be next to the bottom, ie in 30th place in net worth. She questioned the meaningfulness of such a study, because the assets and liabilities of

governments are not of a similar nature to those of commercial bodies. She warned that public sector net worth must be interpreted differently in different contexts.

Sheila concluded her presentation by arguing that accruals-based accounts are useful and informative, but they need to be applied by considering deeply the purpose of public sector accounting and how it serves the needs of its users. She pointed out that public sector accounting consists of many controversies and difficulties and IPSAS is playing an increasing role. She stressed how the IPSASB Conceptual Framework already acknowledges differences, but these are not reflected in the standards yet.

#### **Anne Kirkeby (Black Sun)**

*Anne Kirkeby spoke as lead corporate reporting consultant at Black Sun. In her presentation, she provided an overview of trends in narrative reporting in annual reports.*

She started her presentation by explaining the role of Black Sun, a stakeholder communications company which helps businesses to engage with their stakeholders. She then illustrated the issues that she believes are nowadays affecting corporate reporting. Firstly, stakeholder empowerment is an issue as companies are expected to acknowledge the voice of stakeholders and address their concerns through their corporate reporting. Secondly, a generalised lack of trust in company reporting has recently emerged, with CEOs and boards of directors getting closer to the bottom of the list of those trusted by the public. Anne believes that this is a problematic situation indicating that the messages delivered in corporate communications are not seen as trustworthy. Lastly, the demand for information goes beyond the financial statements, with investors looking for intangible information, including business culture and corporate engagement with stakeholders, that will help them to evaluate the riskiness and potential growth of a business. Anne outlined that factors such as brand, reputation and the ability of a company to grow substantially in the future are not evident in the financial statements of a business, even though they are becoming increasingly important for the valuation of



**The concept of Purpose has been described in annual reports for some time. Despite this, Anne believes that companies do not deem this concept to be the backbone of their current strategy and future growth and she urged that more attention be paid to it.**

a business. Anne also mentioned the proliferation of new regulations and reporting frameworks aimed at improving corporate reporting. She believes that the rise of such regulations and initiatives indicate a lack of transparency and a broader lack of trust in corporate reporting.

Anne continued her presentation by illustrating a report prepared by Black Sun to help its clients in developing best practice reporting. This report (Black Sun 2018) considers the Strategic Report and Corporate Governance sections of the annual reports of FTSE100 companies, evaluating their narrative sections to assess how they have changed over time and how companies have responded to already familiar but not established regulations. Using the results of this report, Anne discussed how companies have responded to recent regulatory changes. She first referred to the Companies (Miscellaneous Reporting) Regulation 2018, which requires companies to include a discussion of how they engaged with their stakeholders. The report shows that not all the companies studied clearly identified their key stakeholders, and only very few provided examples of how stakeholders were considered in their decision-making. She then analysed the responses to the updated Corporate Governance Code and guidance on producing the Strategic Report. The updated Code also requires companies to explain the role of diversity in their strategy and the board's evaluation of risks and opportunities. The report showed that only a little more than half the companies it covered discussed key resources and relationships in their business model and very few explained how diversity supports their strategy. The third regulatory change discussed by Anne was the Non-Financial Reporting Directive. Anne illustrated that, since the implementation of this Directive, almost all companies discussed issues of anti-bribery and corruption, while only a few more than half discussed due diligence processes and environmental policies.

Anne then presented six principles of trust, namely Purpose, Culture, Stakeholders, Diversity, Wider Value Creation, and Long-term Thinking, developed by Black Sun with the aim of

contributing to developing corporate trust. The first principle of trust is Purpose, a concept introduced by both the Corporate Governance Code and the guidance on the Strategic report. Black Sun suggests that its clients should discuss their purpose by communicating how they are part of the solution to societal challenges, rather than constituting the problem. The concept of Purpose has been described in annual reports for some time. Despite this, Anne believes that companies do not deem this concept to be the backbone of their current strategy and future growth and she urged that more attention be paid to it. The second principle of trust is Culture. The Black Sun team observed a steady state in culture reporting. Anne highlighted that companies need to identify what culture they need, depending on the nature of the industry in which they operate. They need to understand how the right culture can emerge and become established, design the appropriate systems and training to develop it, set the measures of success and find ways of encouraging its embodiment. The third principle of trust is the concept of Stakeholders, which in corporate reporting has seen an increasing interest, with almost all companies covered in the Black Sun report discussing their engagement with stakeholders, even though only a few companies discuss how stakeholder engagement is used to set their strategy. The fourth principle of trust is Diversity, which the Black Sun report claims has been discussed by very few companies. Companies with diverse boards and workforces that represent a wide range of stakeholder views are more informed and trusted. Diversity has been reported mainly as a moral issue, as a tool for controlling underused resources and as a concept that embraces different kinds of diversity in the workforce of companies. Anne supported the last of these as the approach to follow, because it will signal that the company's people are seen as a mirror of their wider stakeholders, whose needs and demands are of critical value for the sustainable future of the company. Wider Value Creation is the fifth principle of trust, requiring companies to report on their impact on the financial, human, natural and other kinds of capital.

**An asset is now defined as a present economic resource controlled by the entity as a result of past events. Economic resources are defined as rights that have the potential to produce economic benefits.**

Although, the concept of value creation is widely discussed in corporate reports, companies should also discuss how they create intangible value as this is a crucial element for long-term success. Anne concluded her presentation with the last principle of trust: Long-term Thinking. In discussing this concept, companies should explain how they are investing in areas such as technology, R&D, and human capital. Anne commented that many of her clients are nervous about the long-term story they need to present and think that long-term thinking should include financial metrics.

#### **Jianqiao Lu (IASB)**

*Jianqiao Lu spoke as a member of the IASB and formerly of the Chinese Ministry of Finance. Jianqiao's presentation focused on the main revisions of the new IFRS Conceptual Framework.*

Jianqiao started his presentation by discussing the purpose, history and status of the Conceptual Framework and then focused on its last revision, which took place in 2018. Jianqiao argued that the 2018 revised version has significantly improved on its predecessor. It has incorporated new concepts and guidance on measurement, derecognition and presentation and disclosure, not covered by the previous version. It has clarified important concepts (eg stewardship and prudence) that were unclear previously and has updated the definitions of assets and liabilities and recognition criteria that had become out of date. It has also clarified how the role of uncertainty should be considered in recognising assets and liabilities.

Jianqiao then illustrated the importance and implications of these improvements in the context of current digitalisation and the Big Data environment. He pointed out that the improvements made to the Conceptual Framework will be helpful in analysing whether the Big Data and the existing unrecognised intangible assets meet the updated definition of assets and recognition criteria or whether enhanced disclosures are needed to provide more relevant information for investors.

Jianqiao continued by illustrating the general purpose of financial reporting, which is to provide financial information useful to users in their decision making. He clarified that users' decisions are not limited to buying, holding or selling shares and providing or settling loans, but also include other decisions made while holding investments (eg voting at an AGM). To make these decisions, users need to assess management's stewardship of the entity's economic resources. Therefore, financial reporting should provide relevant information not only about economic resources, but also about risks inherent in those economic resources and how management has managed these risks.

Jianqiao then discussed the two fundamental qualitative characteristics of useful financial information: relevance and faithful representation. The revised Conceptual Framework does not change the definitions of the concepts of relevance and faithful representation, but three important aspects are clarified. Firstly, the revised Framework reintroduced the concept of prudence, which was removed in 2010, and clarifies its role. Secondly, it clarifies the role of substance over form. Thirdly, it clarifies the relationship between the concepts of reliability and faithful representation. Jianqiao also outlined that the revised Framework has not changed the meaning of the following qualitative characteristics that support the relevance and faithful representation: comparability, verifiability, timeliness and understandability.

Jianqiao illustrated the changes introduced to the definition of two elements of financial statements: assets and liabilities. An asset is now defined as a present economic resource controlled by the entity as a result of past events. Economic resources are defined as rights that have the potential to produce economic benefits. This new definition clarifies that an asset focuses on rights rather than flows of economic benefits or physical objects or legal ownership of a physical object. It clarifies that an asset is a right that has the potential to produce economic benefits. It does not need to be certain, or even likely, that there will

**Jianqiao outlined that the new definition of a liability emphasises that the obligation should lead to a potential transfer of economic resource, and, importantly, the entity had no practical ability to avoid the transfer.**

be a flow of economic benefits. The new definition of assets also clarifies that the inflows of economic benefits are no longer needed to be 'expected'. Based on the new revised definition, a 'right' can meet the definition of an asset even if the probability that it will produce economic benefits is low. A liability is now defined as a present obligation of the entity to transfer an economic resource as a result of past events. Jianqiao outlined that the new definition of a liability emphasises that the obligation should lead to a potential transfer of economic resource, and, importantly, the entity had no practical ability to avoid the transfer.

In the last part of this presentation, Jianqiao discussed the changes introduced in the revised Conceptual Framework to the concepts of recognition, derecognition and measurement. First, he illustrated the improvements to the recognition criteria. Assets or liabilities are recognised only if such recognition provides users of financial statements with useful information. Jianqiao pointed out that one of the main contributions of the updated recognition criteria was that they clarify the role of existence uncertainty and measurement uncertainty. Jianqiao then illustrated the new guidance on derecognition added to the revised Framework: derecognition occurs when an item no longer meets the definition of an asset or a liability. Finally, Jianqiao explained the improvements to the measurement concept, which he claimed was barely covered in the previous version. The revised Framework categorises measurement bases into historical cost bases and current value bases and specifies the factors to be considered in selecting a measurement basis.

Jianqiao concluded his presentation by illustrating the role of the profit or loss and the OCI in the revised Framework. The Profit or loss account is considered to be the primary source of information about an entity's financial performance, but not the only one. Users should also consider all income and expenses, including those reported in OCI. Jianqiao concluded by explaining that the IASB expected the use of OCI only in exceptional circumstances.

### **Geoffrey Whittington (UK Accounting Standards Board)**

*Geoffrey Whittington spoke as member of the UK Accounting Standards Board and as Emeritus professor of financial accounting. In his presentation, Geoffrey gave an overview of the revised IASB Conceptual Framework.*

Geoffrey's presentation started with a criticism of the revised Conceptual Framework. Geoffrey explained there was a heavy dependence on the revised chapters of the American revision of its Framework by the FASB. He criticised the lack of revision of the Capital Maintenance chapter, which he claims is a copy of the 1989 Framework and indicative of IASB's poor thinking during the previous 29 years. Geoffrey also criticised the new section on measurement, which he argues is incomplete, is not thorough enough, does not provide adequate guidance and does not meet the IASB's criteria for recognition of accounts. He recognised the attempts to develop the application of the concept of faithful representation on reliability although he did not regard this as necessarily an improvement. For Geoffrey, the main step forwards of the revised Framework is the clarification of the definition of assets and liabilities. Geoffrey then made some supporting arguments for the revised version. He believes that the IASB has built a common language to create greater comparability and consistency in accounts and that the revision of the purpose of the Framework will be useful for the IASB in standard-setting but also for preparers and users of accounts who seek to understand the aims of the IASB.

Geoffrey then illustrated the historical evolution of the Conceptual Framework, focusing, in particular, on the joint project of reviewing it, started in 2004 by the FASB and IASB. The project was mainly driven by the FASB and resulted in the development of lengthy chapters such as that on Objectives and Properties. The joint project was abandoned in 2010 after only the first phase had been finalised, when a revised Conceptual Framework was published that introduced into the existing framework the chapters on the objectives and financial statements.

**Geoffrey concluded that the 2018 Conceptual Framework has improved to a large extent, especially because of the definitions of assets and liabilities that now tie in with the view of accounts as stewardship records.**

The IASB and FASB then decided to follow individual paths. The IASB work was resumed independently in 2012, with no intention of revisiting the FASB chapters, which, except for the addition of emphasis on stewardship, have remained almost the same. Geoffrey explained that significant progress on the revision was done in the following years when a discussion paper followed by an Exposure Draft were produced, respectively in 2013 and 2015, with the final version of the Framework being published in 2018.

Geoffrey continued discussing how the Framework developed through the above process. He said that before 2010 the Framework was primarily FASB-dominated and this led to the emergence of the Fair Value View. He pointed out that at that time, the concept of stewardship, which was reinstated in 2018, was ignored as it looked backward, related to accountability and therefore was not fundamental to investor decision making. He then discussed the concept of prudence, which in the joint project on the Framework was rejected as it fostered an agency perspective that viewed accounting as an appraisal of past events and examined the past performance of the firm. 'Prudence' was then reinstated in 2018 but following a symmetrical concept. Geoffrey argued that despite the progress made in decision usefulness and predicting future cashflows, the IASB has adopted an unsupportive stance towards the concepts of stewardship and prudence. Geoffrey then discussed the issues relating to the concept of measurement. He believed that the IASB's retreat from fair value is a big step forward, as well as the fact that the revised Framework welcomes the use of mixed measurement methods, which will be chosen on the basis of the facts and circumstances of the case. Nonetheless, he criticised the fact that the description of the alternative measurement methods was clumsy, inadequate and incomplete. As he explained, the description does not discuss deprival value, description of current cost is not clear while historical costs are described as incorporating impairment tests where lower market values are chosen. Geoffrey claimed that

the IASB was ignorant of the theoretical literature on measurement and failed to improve the capital maintenance reporting which was superficially written in the 1989 IASC Framework. Geoffrey claimed that another problematic area in the Framework is the concept of recognition. He believes that the new definitions of assets and liabilities have improved the concept. Even so, the replacement of the reliable measurement test by the concept of faithful representation and the use of individual standards for the assessment of whether an asset could lead to important cashflows are, for him, issues of practical concern. He was also critical of the notion of faithful representation, which he described as a pervasive problem originating during the joint project. He believes that 'faithful representation' should mean representing an economic phenomenon accurately. Nevertheless, the Framework fails to provide sufficient guidance on what constitutes an 'economic phenomenon'.

Geoffrey concluded that the 2018 Conceptual Framework has improved to a large extent, especially because of the definitions of assets and liabilities that now tie in with the view of accounts as stewardship records. Nonetheless, the revised version has several weaknesses related to the faithful representation concept, the rejection of asymmetric stewardship and the lack of proper discussion of measurement. Geoffrey ended his presentation by recommending that more research can be done to feed back into the improvements made to the Framework. He argued that more research is needed in relation to the issue of probability and uncertainty and how they are captured in the accounts; the entity approach as described in the Framework; and the issue of equity.

## OVERVIEW

Three main central themes were discussed at the 2019 symposium: the revision of the Conceptual Framework; the evolution of narrative reporting; and controversies in, and development of, public sector accounting. An overview of these main themes is given in Table 3.1.

**TABLE 3.1:** Thematic overview of presentations

| THEME                                  | DISCUSSION   |
|--|--|
| Conceptual Framework                   | <p>The role of conceptual frameworks in accounting was widely covered during the Symposium. Jianqiao Lu and Geoffrey Whittington focused their presentations on the changes introduced by the revised IASB Conceptual Framework. Jianqiao provided a quite favourable analysis of the revised Framework. He claimed that the revised version has significantly improved, thanks to: a) the introduction of new concepts and guidance on measurement, derecognition and presentation and disclosure, which were missing in the previous version; b) the clarification of the stewardship and prudence concepts, which were unclear in the previous version; c) the updating of the definitions of assets and liabilities and recognition criteria, which were out of date in the previous version, and d) the clarification of how to consider the role of uncertainty in recognition of an asset or a liability. Jianqiao believes that these improvements are particularly important in the current digital and Big Data environment. On the other hand, Geoffrey has expressed a strong criticism of the revised Framework. Geoffrey sees the revised version as strongly influenced by the FASB as a result of the earlier joint revision project, started in 2004 and suspended in 2010, which was dominated by the FASB. He criticised the IASB for not having modified the chapters developed during the joint project. He also criticised the lack of revision of the Capital Maintenance chapter, which has remained the same since 1989, and the new section on measurement. In relation to the latter, he praised the retreat from fair value and the fact that the revised Framework welcomes the use of mixed measurement methods. Even so, he sees the description of the alternative measurement methods to be clumsy, inadequate and incomplete. He was also critical of the notion of faithful representation, which he argued should represent an economic phenomenon accurately, but the Framework fails to provide guidance on what constitutes an 'economic phenomenon'. The main step forward of the revised Framework, Geoffrey argued, are the new definitions of assets and liabilities that now tie in with the view of accounts as stewardship records. Conceptual frameworks were also covered by Sheila Ellwood in her presentation, when she discussed their role within public sector accounting. Sheila engaged with the debate on the creation of a common conceptual framework for private and public sectors, outlining pros and cons. Among the pros, the ability of the common framework to improve similarity of treatment and comparability of transactions and to reduce the scope for government manipulation. Among the cons are implementation issues due to the differences (eg organisational purpose, sources of revenues, stakeholders' concerns) that characterise financial reporting in public and private sectors. Sheila explained that, because of these differences, transferring a framework from the private to the public sector may be unsuitable and may lead to manipulation and confusion.</p> |
| Narratives in corporate annual reports | <p>Narratives in corporate reporting have evolved in recent years, following the issuance of new regulations and recommendations to guide companies on how to communicate with their stakeholders. This issue was well covered by the presentation of Anne Kirkeby.</p> <p>Anne discussed the three main issues that in her view nowadays affect corporate reporting: stakeholder empowerment; lack of trust in corporations and demands for information beyond financial statements. She outlined the proliferation of new regulations and reporting frameworks aimed at improving corporate reporting and discussed the results of a report prepared by Black Sun (2018) that assessed how narratives in the annual report have evolved to respond to already familiar but not established regulations, such as the 2018 Companies (Miscellaneous Reporting) Regulation, the 2018 Corporate Governance Code, the updated guidance on the Strategic Report and the EU Non-Financial Reporting Directive. Anne also illustrated the six principles of trust, namely Purpose, Culture, Stakeholders, Diversity, Wider Value Creation, and Long-term Thinking, developed by Black Sun, which companies should discuss in their annual report with the aim of contributing to corporate trust.</p>  |
| Accounting in the public sector        | <p>Public sector accounting has faced significant developments and areas of controversy in recent years. These issues were covered by Andreas Bergmann and Sheila Ellwood in their presentations. Andreas' presentation outlined the current development in public sector accounting. Andreas illustrated the current IPSASB work programme, which is aimed at promoting convergences between IPSAS and IFRS, focusing on the project of achieving convergence with the IFRS15 for revenue recognition. He also illustrated some of the new issued IPSAS, in particular the new IPSAS 42 on social benefits, which has provided a solution on the issue of identifying the moment in which a liability related to social benefit should be recognised. The aim and work of the EPSAS, an accrual-basis accounting system which is in the process of being developed within the EU Member States, were also discussed. The EPSAS is now entering its second phase, aimed at addressing the issue of comparability within and between the Member States in the medium to long term. Controversies and typical issues in public sector accounting were discussed in Sheila's presentation. Sheila questioned the transitional process that public sector accounting is going through and discussed the arguments for and against the adoption of accrual-basis accounting in the public sector. She also discussed the role played by conceptual frameworks in public accounting and particularly the pros and cons of having a common framework for private and public sectors rather than separate ones. The audit reports on the Whole of Government Accounts (WGA) for the UK was then used to illustrate some of the issues faced by public sector accounting. Accounting boundary, inconsistent policies, different year ends, and high uncertainty have emerged to be the causes of huge problems in reporting for the whole of the UK public sector.</p>  |





## 4. Conclusion

### **The January 2019 symposium was held at another interesting time of political, social and economic change, with continuing challenges to accounting and financial reporting.**

The political agenda in 2019 still has Brexit as its centre. The UK was expected to leave the EU by 29 March 2019, but the UK and the EU were unable to make a withdrawal agreement. As a result Brexit was pushed back to 31 October 2019. Meanwhile, Boris Johnson replaced Theresa May as prime minister, but it has not proved possible to negotiate a withdrawal agreement satisfactory to all parties, so the date of leaving has been put back again, to 31 January 2020. The negotiations between the US President Donald Trump and North Korean leader Kim Jong-un, aimed at dismantling Pyongyang's nuclear weapons and missile programmes, have also characterised the global political setting in 2019. Such negotiations have been stalled since the collapse of the second summit in Hanoi in February and any attempt to resume them has been unsuccessful at the time of writing. Environmental risks associated with climate changes, biodiversity losses and pollution of air, soil and water continue to be dominant among the risks globally faced (WEF 2019). Extreme weather is one of the risks of greatest concern, with the growing intensity of wildfires and their spread to new global corners during the 2019 summer (Amazonia, Siberia and Indonesia) raising fears that climate change is exacerbating such dangers.

The signs of economic recovery shown by most of the major economies between the end of 2016 and early 2018 now seem over, with the G7 economies expected to return by the end of the year to growth rates close to their long-run averages (IMF 2018a; PWC 2019). The persistence of economic growth without increased employment continues to raise challenges, mainly because of the disruptions caused by intensifying patterns of automation and digitalisation (WEF 2019). With unemployment rates failing to fall any further in several large economies (PWC 2019), this is becoming an increasingly serious area of concern.

As for accounting and financial reporting, there have been some important changes for both private and public sectors. In March 2018, the IASB finally issued the revised Conceptual Framework on which it had been working for some years. The revised Conceptual Framework will become effective from 1 January 2020, with early applications permitted. In 2019, the new IFRS 16 on leases became finally effective with a potential ability to end the practice of having leases off balance sheets. New research projects have been undertaken by the IASB recently, with the Management Commentary Practice Statement, primary financial statements

and the Rate-regulated Activities project being the most important. Within the public sector, the EPSAS initiative, which aims to provide harmonised accruals-based public sector accounting, is now ready to start its second phase. This phase will address comparability within and between the Member States in the implementation of EPSAS.

Three main central themes were discussed at the 2019 symposium: the role of the IASB's Conceptual Framework in accounting; the narratives in corporate reports; and accounting in the public sector. In late 2019 these issues remain fundamental questions and challenges to the future of financial reporting.

The role of conceptual frameworks in accounting has represented a highly debated topic among both academics and practitioners. The symposium addressed this topic by discussing the revision of the IASB's Conceptual Framework and the role that conceptual frameworks are playing within public sector accounting. The revision of the IASB's Conceptual Framework had been highly debated in the years leading up to its publication. The revised version incorporates important changes, such as the introduction of new concepts

**Conceptual frameworks were also discussed in relation to public sector accounting, where academics and practitioners are now debating the suitability of the conceptual frameworks common to private and public sectors.**

and guidance on measurement, derecognition, presentation and disclosure; the clarification of the stewardship and prudence concepts; the updating of the definitions of assets and liabilities; and the clarification of the role of uncertainty in recognising assets or liabilities. Nonetheless, areas of criticism have emerged relating to the faithful representation concept, the rejection of asymmetric stewardship and the lack of proper discussion of measurement. Conceptual frameworks were also discussed in relation to public sector accounting, where academics and practitioners are now debating the suitability of the conceptual frameworks common to private and public sectors. Despite the ability of such a framework to improve similarity and comparability and to reduce the scope for government manipulation, the symposium has shown that owing to the differences that characterise financial reporting in the public and private sectors, a common framework might be unsuitable and actually lead to manipulation and confusion.

Narratives in corporate reporting are increasingly important as they represent the main tool used by corporations to communicate with stakeholders. The symposium addressed this issue by showing how narratives in the annual report have evolved to respond to regulations and recommendations on narrative reporting that have proliferated in recent years. Speakers also discussed the key factors that nowadays affect corporate reporting: stakeholder

empowerment; lack of trust in corporations; and demands for information beyond the financial statements. Narratives on corporate purpose, culture, diversity, value creation and long-term thinking and on how companies engage with their stakeholders are considered to be pivotal in addressing these concerns, which are having an impact on corporate reporting.

Public sector accounting is nowadays facing significant changes, with several governments moving towards an accrual-based system and working on favouring convergence of accounting standards between public and private sectors and different countries. The IPSASB is working on promoting convergences between IPSAS and IFRS. The EPSAS project has been created within the EU with the aim of harmonising public sector accounting standards across the EU. The symposium also discussed the role played by conceptual frameworks in accounting and particularly the pros and cons for having a common framework for private and public sectors rather than separate ones.

The symposium discussed issues of key importance in accounting and financial reporting. These are long-lasting issues with no simple short-term solutions. The evolution of conceptual frameworks in accounting, the role of narratives in corporate annual reports and the evolution and controversies of accounting in the public sector are long-standing issues that are likely to continue to be debated in the future.

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