



**ADDRESS TO PAN ACCOUNTANCY PROFESSION LUNCH**

**MANSION HOUSE, LONDON**

**23 OCTOBER 2008**

**PAUL BOYLE**

**CHIEF EXECUTIVE, FINANCIAL REPORTING COUNCIL**

**Introduction**

Lord Mayor, Sheriff, Mr President, fellow professional accountants, ladies and gentlemen, it is a privilege to address you on the occasion of this pan accountancy profession lunch. It is nearly 25 years since I qualified as a member of the Institute of Chartered Accountants of Scotland and more than 30 years since I started studying for my degree in Accountancy at the University of Glasgow. I am proud to be a professional accountant and I expect that fellow professionals who have chosen to be here today are also proud of their profession.

It is a pleasure to recognise the presence today of professional accountants from many countries other than the UK, including Australia, France, India,

New Zealand and South Africa. Your presence signifies both that the accountancy profession is a global profession and that the City of London is an international financial centre.

The theme of this lunch is to recognise and celebrate the contribution of the accountancy profession to the success of the City of London and I was asked to base my speech on this theme. You will not be surprised to hear that this has proved to be a much more challenging speech to write than I expected it to be in the Spring when I accepted Ian Strange's invitation to address you.

### **Regulatory perspectives**

The invitation to address you was not a purely personal invitation but was in my capacity as Chief Executive of the Financial Reporting Council, the UK's independent regulator responsible for promoting confidence in corporate reporting and governance. This is too good an opportunity to pass up to give you a perspective on some of the preliminary lessons which we can learn from the current financial difficulties. As I do so from a regulatory perspective, I hope that I have not forgotten some of the perspectives learned during the other two thirds of my career as an auditor and as a commercial finance manager.

Oversight of the accountancy profession is one of the FRC's responsibilities but we have a broad range of responsibilities, including maintaining the Combined Code on Corporate Governance, monitoring compliance with the accounting and auditing requirements of the Companies Act and oversight of the actuarial profession. We have a broad range of stakeholders, including companies, investors and other users of corporate reports and the two professions and we try to take a balanced and independent view having listened carefully to all of them.

### **Corporate governance**

With respect to the FRC's responsibilities for Corporate Governance, it is the case that the current market difficulties have raised questions about corporate governance in the UK's banks and, perhaps, these questions will extend to other financial institutions. Our preliminary conclusion is that the primary questions should not be about the *standards* of corporate governance in these institutions but rather the *practice* of it.

Our view is that the standards set out in the FRC's Combined Code remain comprehensive and appropriately principles-based standards. For example, the Code states the role of a company's board is "to provide entrepreneurial

leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed.” It goes on to say that non-executive directors “should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible.” The Turnbull Guidance, which is annexed to the Code, provides some further guidance, but still in a principles-based way.

We expect that directors of banks and other financial institutions are already reviewing their governance and risk management practices. We, therefore, currently believe that the recent difficulties in the financial sector do not require a generalised tightening of governance standards across the UK corporate sector. The focus should be on whether the existing standards have been observed in practice.

### **Corporate Reporting**

Overall, I believe that accounting has held up well considering the extreme stresses in the financial system. Yes, there have been some criticisms and those will have to be carefully considered, but from my perspective the number of criticisms that the accounts of financial institutions have

understated the losses arising from the credit market problems is closely matched by the number of criticisms that they have overstated the losses.

I also note that some of the organisations which were most critical of accounting standards earlier in the year have turned out to be in need of substantial public sector financial support. Perhaps we have discovered a new regulatory risk indicator.

One of the characteristics of the growth of the financial services industry in recent years has been the extraordinary speed and range of innovation in products, services and indeed in organisational structures through which financial services are delivered. For some time innovation in financial services was regarded as being unquestionably a “good thing”. The credit crunch has led to this proposition being called into question.

There are questions about whether accounting techniques have been able to keep up with the rate of innovation. There have, for example, been questions about the boundaries of the organisation as reflected in consolidated financial statements: what degree of certainty is required before an asset or liability can properly be treated as off-balance sheet? There has

also been of great deal of heat generated by the debate on the appropriateness of fair value accounting. Notwithstanding the recent efforts of the IASB and FASB, questions remain about differences between various IFRS and US GAAP requirements relating to fair value accounting.

There are a wide range of sincerely held views about the merits of different accounting methods, and judgments have to be made as to which methods best meet the needs of the constituencies that have to apply them, audit them and make decisions based on them. We at the FRC believe that the most appropriate standards are likely to be developed if standard setters are able to exercise independent judgment, relying on their skills and experience. We support the IASB in its role as the setter of accounting standards to be used in this international financial centre and we welcome its recent announcements that it will continue to seek globally acceptable solutions to the accounting challenges of the day. Accounting standards must benefit from the input of all the constituencies and to this end, due process is critical.

## **Auditing**

So far, at least, auditing has had a good crisis. I have heard some criticism of the work of auditors but they have also been a mix of the “too lax” and “too strict” varieties of criticism. One of the challenges which critics of auditors need to meet is to be precise about their complaints. Suggestions, for example, that auditors should have intervened to encourage their financial services clients to constrain the rate of innovation and expansion of their businesses seem to me to be based on a fundamental mis-understanding of the relative roles of auditing on the one hand and on the other hand corporate governance and financial services supervision.

That said, the work of auditors is now coming under a much greater degree of scrutiny than has been the case in the past and in our role as independent regulators of the profession we are requiring auditors to demonstrate to a much greater extent that the judgements made in the course of their work are defensible.

## **The accountancy profession**

It is not the FRC’s responsibility to promote the success of the accountancy profession; that responsibility rests with the professional institutes. The

FRC independently oversees the work of the profession in the UK and has a limited range of powers to influence the way in which both individual accountants and their professional bodies go about their work. The era of total self-regulation of the accountancy profession by the professional bodies was brought to an end some years ago and it is unlikely to return.

We have explained the outcome which we would like to see in respect of the accountancy profession, in Outcome Five of the FRC's Strategic Framework which guides our thinking and our action. We would like it to be substantially the case that "clients and employers of professionally qualified accountants and accountancy firms can rely on them to act with integrity and competence, having regard to the public interest."

The primary responsibility for the achievement of the Strategic Outcome rests with individual accountants and with the senior management of the individual accountancy firms. It is at the level of individual responsibility that self-regulation needs to be alive and well even in the modern era.

I suspect that some accountants in the financial services industry are wondering whether the rate and complexity of innovation was matched by

adequate change in their own technical competence. Were all those involved in accounting for or designing internal controls for these innovative products, service and structures able to keep up with the pace of change?

And if, understandably, on occasions they were not able to do so did they have the courage to speak up about the consequential risks?

However, it is worth keeping the current position in perspective. The difficulties which we have experienced in the UK have also been widely experienced in other major financial centres around the world – and, for that matter, in some minor ones too. The sources of the City’s global competitive advantage remain substantially intact and I expect that they will allow the UK financial services industry to remain a world leader.

One of those sources of competitive advantage is the UK’s skills base and the accountancy is one of the leading skill sets in which the UK is a world leader. I have the honour to be the current Chairman of the International Forum of Independent Audit Regulators and in that capacity I travel extensively across the world and meet accountants, business people and regulators from many countries. I have not come across a country in which

accountants are more influential or held in higher esteem by decision-makers than is the case in the UK. We seem to have created a virtuous circle in the UK in which the quality of men and women attracted into the accountancy profession has led to the profession – collectively and individually – being respected and influential, which in turn helps attract some of the most talented graduates in the country into the profession today.

### **The toast**

Finally, it is my pleasure, Lord Mayor, to thank you on behalf of all of the guests here today for your support for the accountancy profession as demonstrated both by your generosity in making the Mansion House available to host this lunch and by your presence here today. Ladies and gentlemen, please join me in a toast to The Lord Mayor, the City of London Corporation and the Sheriffs.