Financial Reporting in the UK

A history of the financial accounting standards committee, 1969–90

Brian A. Rutherford

Routledge Historical Perspectives in Accounting

Financial Reporting in the UK

The UK accountancy profession's attempts to regulate financial reporting came under heavy attack in the late 1960s. Deficiencies in accounting methods were perceived as an important factor in causing several major financial scandals.

In this comprehensive volume, Brian Rutherford examines the history of the Accounting Standards Committee, the body responsible for developing financial accounting standards in the UK from 1969 to 1990, providing an account of the regulation of financial reporting during that period. *Financial Reporting in the UK* covers the formulation of standards on specific topics, the evolution of the institutional machinery of standard-setting, and a number of general themes including the politics of standard-setting, the theory of accounting standardisation and the emergence of a conceptual framework for financial reporting.

This book analyses the big 'set battles' between standard-setters and preparers of financial statements, over topics such as price change accounting, goodwill, leasing and foreign currency translation. It also gives attention to the stand-offs which delayed development in specific areas, as well as the smaller skirmishes which impeded the day-to-day work of improving financial reporting. Rutherford looks at the routine challenges facing those who attempt to prescribe accounting practice and examines the 'tradecraft' of standard construction.

Financial Reporting in the UK argues that the relationship between accounting standards and the 'scandals' they are often seen as responding to is more complex than is generally understood: in particular, although the committee was established to eliminate variety in accounting methods, such variety was implicated to only a limited degree in the scandals generally associated with its establishment. Another important theme running through the book is the difficulty the British accountancy profession – then, as now, divided between six different institutes – has in co-ordinating its activities in pursuit of the public good.

The concluding chapter of this volume examines the implications of the findings for accounting regulators.

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1 Profitability, Accounting Theory and Methodology
The Selected Essays of Geoffrey Whittington
Geoffrey Whittington

2 Financial Reporting in the UK
A History of the Accounting Standards Committee, 1969–1990
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For Lynne, as always, and for Jo and Steph

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Preface

This book is the outcome of a research project funded by the Institute of Chartered Accountants in England and Wales; I am very grateful to the Institute for providing the funding and for supporting the work in a variety of other ways. I am especially grateful to Professor Stephen Zeff for his help and encouragement at every stage of the project; to Peter Holgate, of PricewaterhouseCoopers, and Professor Richard Macve, who, with Professor Zeff, were members of the advisory group for the project; and to Anthony Carey, Director of the ICAEW's Centre for Business Performance at the time the funding was approved.

The book provides a historical narrative of the work and achievements of the Accounting Standards Committee from its establishment in December 1969 (when it was known as the Accounting Standards Steering Committee) until it was dissolved in July 1990. The work of standard-setters inevitably involves a degree of conflict with those whose interests are affected by their standards. This can sometimes result in spectacular set-piece battles; in the main, though, the ASC's preferred strategy was the war of attrition. I have endeavoured to capture the flavour of these – less spectacular but sometimes more effective – campaigns as well as the excitement of battle. I have also described something of the more routine work of the standard-setter's daily slog: seeking out useful if uncontentious improvements in financial reporting, keeping pronouncements up to date, and so on. One dimension of standard-setting that can get lost in accounts of the power struggles is its technical tradecraft – for example, the effectiveness with which those drafting a pronouncement cope with the sheer difficulty of capturing a complex accounting policy in suitable regulatory prose. I have attempted here to give proper attention to the relationship between the politics and the tradecraft of accounting standardisation.

The opening chapters of the book discuss the events leading up to the decision to attempt to 'narrow the areas of difference and variety in accounting practice', to borrow the wording of the 'Statement of Intent' published to announce the decision (chapter 1), and the construction of the machinery designed to carry that decision into effect (chapter 2). Thereafter, four chapters (3, 6, 8 and 10) set out the main, chronologically organised, narrative, each carrying the committee through a five- or six-year period. One hugely important

topic, accounting for changing prices, occupied the committee, on and off, for most of its life; to maintain continuity in the consideration of this topic it is dealt with outside the main narrative, in chapters 4 and 9. Various, slightly more abstract issues, including the 'conceptual framework' question, are dealt with in chapter 5. About half-way through its life, a major review of the purpose and constitution of the committee was undertaken. A number of significant reforms were implemented but one key recommendation was not taken up. The review and its outcome are described in chapter 7. Finally, the 'life and work' of the committee are analysed (chapter 11), looking at both the technical and political realms within which it operated; I was asked during the funding process to examine 'lessons for the future' to be drawn from the history of the ASC and I have endeavoured to deliver on this commitment here.

Various information is supplied in the appendices; the reader's attention is particularly drawn to appendices 7 and 8, which record the principal technical documents developed by the ASC – these provide a useful chronological pathway through the committee's history and may serve as a reminder of past events when a topic is addressed several times during the committee's life.

Since taking up the study of accounting history, I have read a good deal of postmodern historiography with great interest. In composing this history, I have endeavoured to set technical and political events in the context of emerging ideas of accounting standardization and its role in financial reporting, and to be sensitive to the way in which accounting standardization contributes to the social construction of the accounting world, as well as reflecting a world already taken for granted. Nonetheless, a combination of the job description agreed with the funding body and my own methodological and temperamental inclinations has led me to adopt the stance advocated by Richard Evans in his powerful manifesto, *In Defence of History*:

> It is right and proper that postmodernist theorists and critics should force historians to rethink the categories and assumptions with which they work, and to justify the manner in which they practise their discipline. But postmodernism is itself one group of theories among many, and as contestable as all the rest. For my own part, I remain optimistic that objective historical knowledge is both desirable and attainable. So when Patrick Joyce tells us that social history is dead, and Elizabeth Deeds Ermath declares that time is a fictional construct, and Roland Barthes announces that all the world's a text, and Hans Keller wants historians to stop behaving as if we were researching into things that actually happened, and Diane Purkiss says that we should just tell stories without bothering whether or not they are true, and Frank Ankersmit swears that we can never know anything at all about the past so we might as well confine ourselves to studying other historians, and Keith Jenkins proclaims that all history is just naked ideology designed to get historians power and money in big university institutions run by the bourgeoisie, I will look humbly at the past and say despite them all: it really happened, and we really can, if we are very scrupulous and careful and self-critical, find out how it

> happened and reach some tenable though always less than final conclusions about what it all meant.
>
> (R. Evans, *In Defence of History*, London: Granta, 1997, pp. 252–53).

During the course of the research I was able to interview every surviving chairman of the ASC and every secretary except one, as well as many others who played key roles in the work of the committee. Everyone was very generous in making their time available and helpful in the comments and suggestions they made; a number also took the trouble to comment on a draft of the manuscript. I am very grateful to the following individuals, all of whom agreed to be interviewed, or provided written comments, or both: Frederick Bleasdale, Derek Boothman, Anthony Carey, Ian Hay Davison, Peter Godfrey, the late Sir John Grenside, David Hobson, Peter Holgate, Christopher Morgan, Sir Douglas Morpeth, Roger Munson, Professor Christopher Nobes, Michael Renshall, Keith Robinson, Brian Singleton-Green, Stanley Thomson, Graham Ward, John Warne, Tom Watts, Chris Westwick, Robert Willott, Desmond Wright and Professor Stephen Zeff. I would particularly like to acknowledge Ian Hay Davison, Professor Christopher Nobes, Michael Renshall, Chris Westwick and Professor Stephen Zeff, who took the trouble to let me have long and detailed comments on various matters. Needless to say, responsibility for the final text remains entirely mine.

I should also like to thank the staff of the archives and libraries I consulted while conducting the research: the papers of the ASC are held in the special collections of the John Rylands University Library, University of Manchester; the papers of the Inflation Accounting Steering Group and Professor Harold Edey are held in the archives of the London School of Economics and Political Science; and papers of the ICAEW Council from the period are held at the Institute's offices in Milton Keynes. I also received assistance from staff of the British Library Newspaper Reading Rooms, the Department of Trade and Industry, the Library of the ICAEW, the National Archives and the University of London Library.

Finally, I am happy to thank Gillian Knight, of the ICAEW, for all her assistance during the course of the project.

B.A.R.

Series Editor's Foreword

In *Financial Reporting in the UK: A History of the Accounting Standards Committee, 1969–1990*, Brian Rutherford has written a valuable history of the United Kingdom's first experiment with setting accounting standards. He has searched the available archives, conducted interviews with the principals, and scoured the published literature as part of his exhaustive plan of research to document and explain the circumstances attending the formation, evolution and development, and eventually the concluding years of the Accounting Standards (Steering) Committee. He marshals evidence to trace provisions in the standards to the lobbying by companies and Government, which is an integral part of any undertaking to track the origin of accounting standards.

Rutherford appropriately devotes two chapters to the Committee's long 'struggle' to deal with the highly inflammatory problem of accounting for price changes, which consumed most of the 1970s and some of 1980s. No standard-setting body anywhere in the world invested more of its time and resources to finding a solution to this problem.

The Committee was in a very different position than its counterpart bodies in North America. In the United States, the Accounting Principles Board (1959–73) and the Financial Accounting Standards Board (since 1973) have set standards under the constant tutelage of the Securities and Exchange Commission (SEC), which intervened when it believed that it could not accept their recommendations, whether on recognition, measurement or disclosure. Moreover, the SEC rigorously enforced companies' compliance with the final standards. In Canada, beginning in 1972, the provincial securities commissions and then the companies acts formally declared that the Canadian Institute of Chartered Accountants' *Handbook* of releases promulgated by its standard-setting body constituted Generally Accepted Accounting Principles. In the UK, by contrast, no governmental body took official or even unofficial cognizance of the Committee. It was on its own to set the standards that would, in its view, be compatible with giving a "true and fair view." Indeed, the Committee's recommendations had to be endorsed by the governing Councils of its sponsoring accountancy bodies, both in the UK and Ireland, before they could be considered as final. It fell to the accountancy bodies themselves as well as to the London Stock Exchange to take actions to secure compliance with the standards, which proved to be an uncertain enterprise, at best, in self-regulation.

I commend this book to students of the accounting standard-setting process, and it is to be hoped that Rutherford's scholarship will inspire efforts to develop comparable histories of such bodies elsewhere.

Stephen Zeff
Rice University
February 2007

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The contents of Table 6.2 and the Council of the Institute of Chartered Accountants in England and Wales' *Statement of Intent on Accounting Standards in the 1970's* are reproduced by kind permission of the Institute of Chartered Accountants in England and Wales.

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List of Abbreviations

ACCA	Association of Certified and Corporate Accountants; Association of Certified Accountants; Chartered Association of Certified Accountants[a]
ACT	Advance Corporation Tax
AEI	Associated Electrical Industries Limited
AICPA	American Institute of Certified Public Accountants
AISG	Accountants' International Study Group
APB	Accounting Principles Board (USA)
APC	Auditing Practices Committee
ARB	Accounting Research Bulletin (USA)
ASB	Accounting Standards Board
ASC	Accounting Standards Committee
ASSC	Accounting Standards Steering Committee
BBA	British Bankers' Association
BPF	British Property Federation
CBI	Confederation of British Industry
CCA	Current cost accounting (system of accounting)
CCAB	Consultative Committee of Accountancy Bodies
CICA	Canadian Institute of Chartered Accountants
CIMA	Chartered Institute of Management Accountants[b]
CIPFA	Chartered Institute of Public Finance and Accountancy[b]
CPP	Current purchasing power (system of accounting)
CSI	Council for the Securities Industry
DoT	Department of Trade
DPP	Director of Public Prosecutions
DTI	Department of Trade and Industry
E	Exposure Draft (of an IAS)
ED	Exposure Draft
EEC	European Economic Community
EITF	Emerging Issues Task Force (USA)
ELA	Equipment Leasing Association
EPS	Earnings per Share
FAS	Statement of Financial Accounting Standards (USA)

FASB	Financial Accounting Standards Board (USA)
FHA	Finance Houses Association
FIFO	First in First out
FRED	Financial Reporting Exposure Draft
FRS	Financial Reporting Standard
GAAP	Generally Accepted Accounting Practice
GEC	General Electric Company Limited
IAS	International Accounting Standard
IASC	International Accounting Standards Committee
IASG	Inflation Accounting Steering Group
ICAEW	Institute of Chartered Accountants in England and Wales
ICAI	Institute of Chartered Accountants in Ireland
ICAS	Institute of Chartered Accountants of Scotland
ICI	Imperial Chemical Industries Limited/PLC (the company is generally known by its initials)
ICMA	Institute of Cost and Management Accountants[b]
ICWA	Institute of Cost and Works Accountants[b]
ILSC	International Learning Systems Corporation
IMTA	Institute of Municipal Treasurers and Accountants[b]
LBS	London Business School
LIFO	Last in first out
LOA	Life Offices' Association
LSCA	London Society of Chartered Accountants
MORI	Market and Opinion Research International
MSI	Maxwell Scientific Inc.
NRV	Net realisable value
P/E	Price-earnings ratio
PSC	Professional Standards Committee (of the ICAEW)
RDG	Regional Development Grant
RICS	Royal Institution of Chartered Surveyors
SEC	Securities and Exchange Commission (USA)
SME	Small or medium-sized enterprise
SOI	Statement of Intent
SORP	Statement of Recommended Practice
SSAP	Statement of Standard Accounting Practice
SUIT	Scottish and Universal Investments
TAC	Technical Advisory Committee (of the ICAEW)
UITF	Urgent Issues Task Force

Notes:
[a]For convenience, the body known by these various titles at different times during the period covered by this work is referred to using the initials it employed throughout the period. For further details, see note 121 to chapter 1. [b]See note 121 to chapter 1.

1 'Present Troubles, and More to Come'

The President of the Institute of Chartered Accountants in England and Wales in December 1969 was Ronald George Leach.[1] Leach trained with Peat, Marwick, Mitchell & Co., joining the firm at the suggestion of his father, who was a director of the Queen's coach builders, a client of Peat's. He qualified in 1932, coming fifth in the honours list, and was to remain with the firm all his working life. He joined the Council of the ICAEW in 1963 and became senior partner of the practice in 1966, the first from outside the Peat family. Together with Sir Henry Benson,[2] who beat him by one place in the honours list, Leach came to dominate British accountancy; he was considered 'a titan within the profession'[3] and on his death *Accountancy* mourned 'the last of the household names'.[4] Leach and Benson were strong and effective leaders, whose writ ran not only within their own firms but also in Moorgate Place, headquarters of the ICAEW; furthermore, they were accepted by government as speaking for the profession.[5]

On Thursday, 11 December 1969, six months into his term of office, Leach read a 'Statement of Intent on Accounting Standards in the 1970s' to the assembled members of the press. It had been prepared from a draft considered by the ICAEW Council on the Wednesday of the previous week.[6] The press, who had been summoned to the Institute's headquarters with little warning of the dramatic nature of the announcement,[7] heard the President say that it was his 'Council's intention to advance accounting standards . . . [by] narrowing the areas of difference and variety in accounting practice'.[8] The content of the statement, the speed with which it was prepared, and the manner of its announcement, foreshadowed a radical change in the Institute's stance on the regulation of technical matters. Why did this change come about, and why at this particular juncture?

Most writers describing the creation of the UK's first machinery for accounting standardization have taken the view that the Council was in the grip of a series of major scandals in the corporate sector, scandals which were exposing serious deficiencies in accounting methods and left little choice but to tighten up regulation in a substantial way. Writing in 1981, for example, Professor Michael Bromwich describes events thus:

> In the late 1960s a storm of criticism arose in the UK against the accounting profession's efforts to set guidelines. Accounting methods had been found

> wanting in a number of financial debacles that are still notorious today. These included the collapse of Rolls Razor Ltd, in 1964, just after publishing 'clean' accounts, and the vast difference between AEI's profit forecast for 1967 and the large loss reported after its takeover by GEC, partly resulting from the use of different accounting principles. Finally, there was the failure of the Leasco-Pergamon takeover, central to which was the use of different valuation bases for the same items by the two companies.[9]

Twenty years later, the consensus still holds. According to Professor Vivien Beattie, writing in 2002, 'pressure for reform in the UK came to a head with several public "accounting scandals", notably the GEC/AEI takeover in 1969'.[10]

Those directly involved offer similar accounts. Leach himself argued that 'it was in fact the development of the takeover bid which limelighted ... deficiencies of the system ... [T]he accounting bases adopted by the offeror and offeree could be strikingly different. Perhaps the most famous case was the AEI-GEC merger.'[11] Since they are so strongly associated with the emergence of accounting standards, it is worth investigating each of the debacles in some detail.

Accounting Scandals

On 28 September 1967, the General Electric Company Limited launched a bid to take over Associated Electrical Industries Limited.[12] This was resisted by the directors of AEI and, in the course of the acrimonious battle that ensued, the AEI Board issued a statement to the effect that the company would earn a profit, for the financial year ending 31 December 1967, of £10 million. Although this was technically a forecast, ten months of the financial year had already elapsed and it was reasonable to assume that there was little uncertainty associated with the figure. The forecast was very similar to the previous year's result, despite the outturn for the first half of 1967 having been much poorer than that in the equivalent period of 1966. AEI's optimism surprised outsiders; GEC attacked the forecast strongly and its credibility became a major issue in the closing stages of the contest, which was very close run. GEC's offer had to be raised twice, by more than 40 per cent in total, and favourable votes did not reach a majority until the opening of the post on the morning after the voting deadline.

GEC's financial year-end was 31 March and the company treated the whole of AEI's results for 1967 as pre-acquisition to the group. Nonetheless, GEC chose to put the AEI figures firmly in the spotlight: they were announced at the same time as the group's results and showed that AEI had made a loss of £4.5 million, a, now-famous, gap between forecast and outturn of £14.5 million – the equivalent at current prices would be in the order of £170 million.

GEC commissioned a report on the discrepancy from the joint auditors of AEI, Deloitte, Plender, Griffiths & Co. and Price Waterhouse & Co., and this

was published on the same date as the results, 29 July 1968.[13] The report began by pointing out that the size of the discrepancy had to be viewed in the context of a value for stock and unbilled balances of work in progress of some £100 million and continued:

> The appraisal of stocks, contracts and a number of other matters involve the exercise of judgement; they are not matters of precision. Broadly speaking, of the total shortfall of £14.5 million we would attribute roughly £5 million to adverse differences which are matters substantially of fact rather than of judgement and the balance of some £9.5 million to adjustments which remain matters substantially of judgement.[14]

The amount of the shortfall attributable to operating divisions was £13.8 million, 95 per cent of the total, and the report gave a breakdown of this figure by type of adjustment. Although the amounts do not line up exactly, the total for three items, additional provisions for stock obsolescence, losses on contracts in progress and completed, and bad debts, which would appear to qualify as matters of judgement, stands at £9.2 million and is fairly close to the figure attributed to judgement in the paragraph quoted above. Most of the remainder arose from the estimation of cost of sales in the forecast, which would be likely to involve matters substantially of fact.

Thus, on the basis of the public record at the time, it appears likely that the judgement involved related to future outcomes rather than the appropriateness of accounting methods. This interpretation has since been lent considerable support by the publication of extracts from the Price Waterhouse Partners' Newsletter in Edgar Jones' history of the firm: the issue of 6 August 1968 assured partners that the difference was not due to a change in 'method', but rather to 'the assessment of net realizable value in relation to substantial stocks and incomplete contracts, without any departure from the basic accounting principle'.[15]

Whether the two sets of judgements were reasonable in their different circumstances became a matter of heated dispute. Given the circumstances, it would not be unreasonable to assume a degree of optimism, not necessarily by any means reckless, in the AEI forecast. Equally, GEC would have been likely to take a pessimistic view; its approach to the routine estimation of provisions in its own financial statements was well known to be strongly conservative[16] and it had begun reorganizing AEI's business immediately after the takeover,[17] so that there would certainly have been some change in management intentions underlying the necessary judgements. Whatever the truth of the matter, no major issue of accounting method appears to have been involved.

Within eleven months of the disclosure of the AEI-GEC gap, events which were to result in a second scandal were set in train, again by a takeover bid. The Pergamon-Leasco affair was to become a much longer-running business and had all the complexity commonly associated with the activities of the late Robert Maxwell.[18] Maxwell had built up Pergamon Press Limited by applying aggressive

business techniques to the traditionally staid world of academic publishing. For example, he developed a stable of highly specialized scientific journals charging high prices for subscriptions, which would be taken out mainly by university libraries following the instructions of academics seeking to publish in the same journals.

Maxwell's success was greatly admired in the City and when he took the company onto the stock market, its shares proved popular.[19] However, by 1969, he was keen that Pergamon, in which he had retained a substantial stake, should be taken over. He approached the Leasco Data Processing Equipment Corporation of New York, in fact a conglomerate, headed by Saul Steinberg. After lengthy negotiations, it was agreed that Leasco would buy the entire share capital of Pergamon. Under the agreement, announced on 18 June 1969, independent shareholders were offered loan stock or cash and the Maxwell interests would accept stock for 25 per cent of Pergamon's capital and cash for their remaining 9 per cent. However, it transpired that Maxwell had not cleared the deal with the trustees of some of his family interests, who wanted cash for all their holdings, and further negotiations became necessary.[20]

During the delay, Touche, Ross, Bailey & Smart, called in by Leasco as investigating accountants after reaching the original agreement,[21] expressed doubts about the position of a Pergamon subsidiary, the International Learning Systems Corporation, and about trading relations between Pergamon and Maxwell Scientific Inc. (a Maxwell family company).[22] Leasco had been buying Pergamon shares on the open market at below the cash price agreed for the deal and on 20 August discovered that some of these had come from Maxwell family interests that it had been told were committed to the deal. It thus found that it had achieved a lower percentage of support than it had supposed and had been paying cash for shares it thought it was to obtain for stock.

The failure to disclose dealings by family interests breached the City Code on Takeovers and Mergers.[23] The following day, Leasco announced that it would not be proceeding further, giving as its reasons the doubts expressed by its investigating accountants and concerns about the published forecast earnings of Pergamon for 1969. Leasco was obliged to defend its withdrawal to the City Panel on Takeovers and Mergers, which accepted its explanation and referred the matter to the Board of Trade.[24] In September 1969, the Board of Trade appointed Companies Act inspectors to investigate; one of the two inspectors was Ronald Leach.[25]

A second inquiry, also established in September 1969, is of more interest here. Leasco agreed a new deal under which it would pay cash for all outstanding shares in Pergamon on the basis of a multiple of average earnings for 1968 and 1969. To determine earnings for the purpose of fixing the price, the Board of Pergamon appointed Price Waterhouse & Co. to review the company's financial statements, already published, for the year ended 31 December 1968, and the half year statements to be produced for the period to 30 June, 1969 – the latter period was subsequently extended to nine months.[26] The firm was to report 'any changes in accounting principles ... consider[ed] advisable', 'any substantial

adjustments ... consider[ed] appropriate', and 'what additional information might ... be given to ... shareholders'.[27]

As well as involving complex arrangements, the Pergamon-Leasco affair resembled other chapters of the Maxwell saga in the elaborate web of litigation that surrounded events. Maxwell appealed against the Takeover Panel's decision and successfully delayed the publication of the Board of Trade inspectors' report, taking the latter case to the House of Lords.[28] Leasco brought actions against MSI which, in turn, MSI used as a basis for refusing to disclose information to Price Waterhouse, despite Maxwell having confirmed in writing that he and his family trusts would cooperate with the inquiry unconditionally.[29]

Price Waterhouse conducted the bulk of their initial inquiries in November 1969[30] and provided an interim report, dealing only with the 1968 accounts, in March 1970. Their final report was published on 21 August 1970. Its length reflected the complexity of the affair: summaries occupied eight pages in *Accountancy*[31] and six in *The Accountant's Magazine*.[32] The recommended adjustments reduced trading profit for 1968 by £1.6 million (some £18 million at current prices and 76 per cent of the previously published figure). The company incorporated the recommendations in relation to the 1969 accounts in the published financial statements; as a result, trading profit for the first nine months of 1969 stood at a mere £29,000.

It will be recalled that Price Waterhouse was asked, among other things, 'to report any changes in accounting principles which [it] consider[ed] advisable',[33] and on this point its conclusion was unequivocal: 'we do not recommend any changes in the general accounting principles adopted by the group'.[34] The summary of the report in *The Accountant's Magazine* was particularly effective in anatomizing the reasons behind the recommended adjustments; time and again, the article concludes that they involve the correction of errors, alternative judgements about the future, incorporation of information possibly not available at the time of preparation of the accounts, or misapplication of accounting principles which were correct in themselves.

With the benefit of hindsight, and, in particular, the inspectors' reports and Maxwell's subsequent track record, it is easy to be confident that the 'errors' were contrived to flatter Pergamon's profits. Some involved dubious transactions with related parties, though these contributed substantially less than half of the total amount involved. It is possible that accounting standards actually issued many years after the establishment of the standard-setting machinery would have strengthened the hand of the auditors, Chalmers, Impey & Co., in dealing with these transactions.[35] However, it was never suggested that Pergamon had contended, let alone that the auditors had agreed, that it was an acceptable accounting policy to recognize transactions with a related party as if they would not reverse when it was known or expected, at the time of preparation of the financial statements, that they would in fact do so. Pergamon's treatment of related party transactions, like the other matters requiring adjustment, was based on (possibly implicit and probably mendacious) assertions that expectations about the future justified the application of what were, in themselves, acceptable practices.

The third scandal actually began well before the AEI-GEC and Pergamon affairs but was still running in 1969, though it always remained rather in the background. Rolls Razor Limited was primarily involved – despite its name – in manufacturing and distributing low-priced automatic washing machines, at that time something of a luxury good. The managing director was John Bloom and the chairman Richard Reader Harris, then MP for Heston and Isleworth. At first the company concentrated on direct selling of machines purchased from a Dutch manufacturer; it was able to under-cut other suppliers and was very successful. Rapid expansion, involving complex financial arrangements, was followed by a move into manufacturing when a rival business obtained a contract for the output of its Dutch supplier. The management proved unable to cope with the greater scale of operations or the demands of running a manufacturing business. In 1964, following a BBC programme highlighting its difficulties, the company collapsed.[36] In July of that year Board of Trade inspectors were appointed; the accountant in the team was Sir Henry Benson. *Accountancy*'s view at the time was that the company's shares had been hugely over-priced by excessively enthusiastic investors.[37] The financial statements were, in its view, innocent: 'the accounts of Rolls Razor Ltd. follow modern practice and are more informative than most'.[38]

In August 1965, a Private Office minute to the President of the Board of Trade discussed the imminent receipt of the inspectors' report:

> The report will criticize a number of accountants, merchant bankers and others who dealt with documents issued by the company and the inspectors think that their report will have a profound effect on the City and bring about changes in the way in which such documents are dealt with. Accordingly the inspectors consider that the report should be published immediately even if this means that criminal proceedings could not be instituted.[39]

The report was passed to the Board of Trade on 30 November 1965.[40] The inspectors' advice, quoted above, was not followed and it was announced that the matter had been referred to the Director of Public Prosecutions and police inquiries were in progress.[41] The Board of Trade decided that, in the meantime, the report could not be published because it might prejudice a fair trial.[42] In July 1967, the police report, 'so bulky that several men would be needed to hand it over',[43] was ready to be sent to the DPP. In 1969 the case was brought to trial and several directors indicted for fraud. The prosecution team, faced with the difficulty of bringing a complex case now five years old, and of finding witnesses able to give a reliable account of events, entered into plea bargaining with the defendants; as a result the more serious charges were dropped and Bloom himself received only a fine of £30,000.[44]

The Secretary of State for Trade and Industry then decided not to publish the inspectors' report, on the grounds that it would be improper to release a document, containing reflections on individuals, after the conclusion of criminal

proceedings in which related allegations had not been proved or had been withdrawn. This decision still stands.[45]

Benson's autobiography summarizes the inspectors' conclusions thus:

> The management was weak and inefficient, the company was under-capitalized, the accounts were unreliable, some of the stock valuations were suspect, and production problems had developed with the machinery and equipment incorporated in the washing machines which resulted in rejects and claims by dissatisfied customers which were continually increasing.[46]

Fortunately, the report has now become available under the Freedom of Information Act.[47] The chapter dealing with the financial statements concludes that, at 31 December 1963, the company's net assets were overstated by £1.8 million (£25 million at current prices – the actual position was a net liability of £0.5 million). Of the overstatement, 12 per cent was attributable to a failure to keep track of debtors arising in connection with the complex (but typical) arrangements for hire purchase finance; 38 per cent to under-provision for bad debts and repairs under guarantee; 25 per cent to overvaluation of stock; 12 per cent to a failure to write off an insolvent subsidiary; and the remainder to suppression of liabilities and a variety of minor discrepancies. The report makes it clear that the inaccuracies arose predominantly from incompetence and failure to acknowledge the circumstances prevailing at the time, rather than from poor accounting methods.[48] In one case, the under-provision for repairs under guarantee, the position was complicated by the introduction, late in the day – actually after the year-end, of what would now be called a quasi-subsidiary; it is possible that a pronouncement on this topic might have led the company to favour the level of provision identified by the inspectors, although the auditors were not aware of the ownership arrangements of the entity at the time.[49] The inspectors also commented on the insolvent subsidiary's failure, as a matter of accounting policy, to provide for losses under guarantee and under an instalment protection plan.[50] These are the only matters in which accounting principles were involved. In connection with some of the misstatements, the inspectors concluded that the auditors should have identified errors.[51]

The evidence is, then, that little of the scandalous behaviour associated with the cases of AEI-GEC, Pergamon and Rolls Razor involved serious differences within, or weaknesses of, financial reporting principles or methods. Furthermore, in the case of AEI-GEC, this was already at least reasonably clear from material in the public domain and was apparently entirely clear to Price Waterhouse, two of whose partners were members of the ICAEW Council.[52] In the case of Rolls Razor, an inquiry conducted by a member of the 1969 Council had long since been completed, though it remained unpublished. In Pergamon's case, two inquiries had begun: one involved a member of the 1969 Council and the other, relating specifically to accounting issues, was already well under way, so that its likely conclusions would have been apparent to (again) Price Waterhouse. The nature of some of the major areas of contention, related party

transactions, including their potential reversal, and the dubious profitability of ILSC, were a matter of public record as a result of the report of the Takeover Panel published in late August 1969[53] and Touche, Ross, Bailey & Smart, one of whose partners served on the Institute Council, would have known of these concerns in detail. How, then, did these scandals come to be implicated in the Institute's creation of radical and innovative machinery to narrow areas of difference in accounting practice, a problem, if such it was, apparently quite unconnected with the behaviour they exposed?

Professor Edward Stamp and the National Press

The more technical, and thus obscure, the operations of a profession, the more influential is the press in shaping the perceptions of its activities held by those outside the profession. In this instance, the press in general did not, at first, respond to events by asserting that the scandals exposed a need to narrow areas of difference in accounting practice. Two generalist publications can be taken as indicative: *The Times*, then still the 'newspaper of record', whose Business News section was an energetic source of investigative journalism, and *The Economist*, one of the leading voices critical of accountancy in an era when the professional press was predominantly loyal to the establishment.

The reaction of *The Times* to the AEI-GEC gap was given in an editorial published on 30 July 1968.[54] This left little doubt that, in its view, blame rested on weak legislation covering the preparation of forecasts, so that 'any board of directors can make nonsense of the whole business of mergers by uncautious [sic] forecasts'. The solution was for 'responsibility of a board for its forecasts [to be] written into the law to include the use of due diligence and care in interpreting all the facts available at the time of a takeover approach'. By contrast, *The Economist* focused on the amount attributable to judgement and concluded that,

> it is a fair guess that the bulk of the difference arose from the more precise and stringent accounting approach traditionally used by GEC management. In a complex and technically advanced group like AEI a more pessimistic approach to valuation of stocks and work in progress could produce a difference of this order, in the year the accounting approach changed.[55]

Though they might have winced at the use of the word 'precise', the partners of Price Waterhouse must have felt that the truth about the AEI-GEC gap was well understood at *The Economist*.[56]

Almost exactly a year later, the magazine carried a brief but wide-ranging article, entitled 'Auditing the auditor', criticizing the range of accounting methods employed in preparing financial statements but also the danger to auditors' independence from their relationship with management. It made no reference to a specific UK case and only one reference to a real-life case at all.[57]

Then the Pegamon-Leasco affair hit the headlines. The Takeover Panel's recommendation that Pergamon dealings should be suspended, effectively the

beginning of the public scandal, was reported in *The Times* on 22 August 1969.[58] Although the story referred to 'general accountancy principles' as one of a number of areas the Panel would need to investigate, this point was elaborated by discussion of matters such as bad debt provisions and the treatment of start-up costs, leaving open whether what was at issue was judgement or accounting policy. Much of the coverage dealt with the nature of transactions with related parties. Editorial coverage of 'questions for the panel' by the Financial Editor a few days later[59] did not refer to accounting methods and suggested that, 'perhaps the single most important issue', was transactions with related parties. On 26 August, a story described the statement by Leasco giving a fuller version of its reasons for abandoning the bid, which effectively put most of the facts described earlier into the public domain.[60]

The Economist's view of the affair was given in a major article published on 30 August and sarcastically entitled, 'A true and fair view'.[61] This referred to 'the possibility that profit forecasts may contain a wide margin of error and accounts a large measure – to be charitable – of eccentricity'. It concluded that 'the accountancy profession will seriously have to consider whether more of its own "best practice" rules should not be written into the Companies Act'. Significantly, the main text focused exclusively on Pergamon, commenting, incidentally, that 'a blow-up on this scale is mercifully rare'. Though the AEI-GEC gap was mentioned, it was referred to only in a table and in the context of forecasts that could be 'appallingly wide of the mark',[62] without any imputation that this was attributable to differences in accounting method.

Coverage of Rolls Razor was inevitably skimpy, given how few facts were emerging, and was confined largely to tracking the progress of the court case. It did not allude specifically to accounting practice.[63]

By late August 1969, then, the accountancy profession was receiving a good deal of flak from the national press, but much of it focused on audit issues; criticism of variety in accounting practice was limited and drew almost exclusively on only one concrete British case, Pergamon. It would not have been unreasonable to hope that, at least as far as accounting practice was concerned, the scandal would come to be seen as a 'one off', with very specific causes and potential solutions, and necessitating no wide-ranging action. If they did entertain this hope, the accountancy establishment reckoned without the attentions of Eddie Stamp.

Professor Edward Stamp was born in England in 1928 and obtained a First Class degree in science from Cambridge. He qualified as a chartered accountant in Toronto, becoming a naturalized Canadian. His first academic post was in New Zealand; he returned to the UK in 1968 to take up a chair at Edinburgh, later moving to Lancaster where he remained until his death in 1986.[64] Michael Mumford, a long-standing colleague and admirer of Stamp, points out that 'he became widely known to accountants world-wide, less for the originality of his ideas than for his robust campaigns to raise standards of corporate reporting, auditing, and open administration'.[65] He adds that Stamp's reputation was 'as an iconoclast, a maverick, very much a lone campaigner', and that 'even his closest colleagues would admit that he could be thoroughly difficult'.[66]

Stamp had already published, in Spring 1969, a vitriolic attack on the state of accounting practice. It appeared in the first issue of a new academic journal published from the University of Lancaster, the *Journal of Business Finance.* Ironically, it was not directed specifically at British accountancy and was, indeed, based on a lecture Stamp had delivered at the University of Sydney. Another irony, perhaps characteristic of the man, is that the attack on accounting practice was actually delivered as an aside. The meat of his article is a consideration of the relationship between auditors and stakeholders in entities subject to audit, but before embarking on his main theme, the author thought it 'worth considering for a moment . . . the under-pinnings of financial accounting theory and practice'[67] upon which an auditor's opinion is based:

> Many . . . so-called 'principles' are not principles at all but merely descriptions of current or, even worse, past practice; rules which in many cases are drawn up on an *ad hoc* basis to deal with the expediencies of a passing moment. Accounting principles are riddled with inconsistencies and illogicalities, and there are so many alternative 'generally accepted' ways of dealing with most accounting problems that it is almost true to say that practically anything is 'true and fair' to some accountant . . . What masquerades under the title 'generally accepted accounting principles' is a state of chaos. Can any other words describe aptly the situation where, as Chambers pointed out in a recent article, there are over a million combinations of mutually exclusive rules each giving a true and fair view of a company's state of affairs and its profits?[68]

The reference to a million combinations relates to an article published in 1965, coincidentally also in the first issue of a new academic periodical, this time the Australian *Abacus*, by Professor Raymond Chambers.[69] Chambers was a distinguished scholar of accounting but also, like Stamp, an accomplished polemicist. His calculation focused exclusively on the more fine-grained differences in accounting practice, such as stock flow assumptions, the grouping of stock items to apply the cost and market rule, and depreciation methods. Having identified a hundred thousand alternatives on this basis, he argued that 'alternatives implicit in some of the rules'[70] justified a further ten-fold increase in the count.

Significantly, the only concrete examples of problems with accounting practice offered by Stamp, in a ten page article, were an Australian case, the Reid Murray affair, dating from 1961,[71] and the AEI-GEC gap. He asserted that in the AEI-GEC affair, 'a substantial portion of the discrepancy between estimated and recorded profits was attributable to "differences of judgement" *over the choice of which accounting principles to use*',[72] and, in a footnote elucidating this comment, said of the 'adjustments which remain matters substantially of judgement' according to the joint auditors report, that they were, 'adjustments which it is believed related mainly to differences in the "principles" used in accounting for contracts'.[73] Even on the basis of what was on the public record at the time, this interpretation was surely, to say the least, tendentious.

Stamp's article had the effect of bringing him to the attention of the national press as a critic of the profession[74] and he became a preferred source for 'opinion' pieces. He contributed the unsigned article in *The Economist* of 9 August 1969, already referred to,[75] just before the Pergamon affair broke, which mentioned no British cases at all. When the dispute between Leasco and Maxwell hit the headlines, *The Times* invited him to contribute an article on the state of British accountancy. This appeared on 11 September,[76] and it marked a turning point in the battle for public opinion, or, at least, was perceived as such by leaders of the profession. The piece was introduced by a reference to Pergamon; though it asserted that this was 'not the first occasion on which warning signals [had] been run up', the only other concrete instance mentioned was the AEI-GEC gap. Stamp made a number of criticisms, 'expressed with his customary vigour':[77]

> In the first place there is the deceptive nature of the phrase 'accounting principles'. The word lends a spurious air of authority and accuracy to a situation which is in fact almost chaotic. As the Pergamon case has shown, accountants find it exceedingly difficult to agree upon or apply the 'principles' to be used in amortizing development expenditures, treating transactions between related members of a group of companies, valuing stocks, or determining at what point income can be said to have been earned. There are many other areas that are equally contentious.

Stamp again used Chambers' calculation of 'over a million different "true and fair views" of the same facts', attributing it to an anonymous 'authority'. This charge certainly struck home: at least one key figure in the events surrounding the establishment of standard-setting machinery, Sir Douglas Morpeth, remembers the reference to this day.[78] Stamp argued that the profession regarded 'principles' as being what was 'done in the best firms': 'this approach may be satisfactory in prescribing the "principles" of plumbing, or of wallpapering, or of carpentry. It is surely not good enough for a profession which believes itself to be the intellectual equal of the legal and medical professions.' Other criticisms related to the independence of auditors. His solutions to the problem of variety in accounting practice were a research programme to produce 'a set of rational, logical and self-consistent accounting principles' and, pending this outcome, disclosure, 'in great detail', of the particular principles chosen by a company, together with the highest and lowest income and balance sheet values that could be computed by the company using alternative acceptable principles.

The *Times* article brought further attention to Stamp's views. He appeared on BBC TV's *Money Programme*[79] and began writing a short book specifically on the need for reform of accounting principles, which appeared the following year.[80] Showing his characteristic courage, or belligerence, depending on one's view, he accepted an invitation to address a meeting of the Manchester Society of Chartered Accountants on 30 October. His talk was apparently followed by a 'lively discussion' in which 'a number of critical questions were put to Professor Stamp'.[81] The report in *The Accountant* implies that the principal line of criticism

was not that his views were wrong, but that he should air them within the profession rather than through the press, a theme taken up by the President of the Society in his closing remarks.

Government Pressure?

Two eminent establishment figures made criticisms to the ICAEW about deficiencies in accounting practice in the late 1960s. The first was Sir Frank (later Lord) Kearton, who was, at the time, chairman of both Courtaulds, a large public company, and the Industrial Reorganisation Corporation, a government agency established to assist in restructuring British industry. In June 1968, Kearton announced to the press that he had written to the President of the Institute, complaining about the problems caused in reconciling the financial statements of acquired companies with those of their new parent, and his announcement created a good deal of publicity.[82] It is sometimes suggested that he wrote as chairman of the Industrial Reorganisation Corporation, lending the weight of a public body to his concerns,[83] but the letterhead was in fact Courtauld's.[84] The President replied to Kearton, asking for further details, but received no response.[85]

The other figure was Lord Shawcross, who addressed the annual dinner of the Manchester Society of Chartered Accountants, on 20 November 1969, in his role as chairman of the Takeover Panel. In this capacity, he had, of course, been directly involved in the events surrounding the Pergamon-Leasco affair.[86] Leach was present at the dinner, and heard Shawcross say:

> I get the impression – although I am no expert in accountancy matters – that in the United States accountancy is regarded as something of an applied science and that in many matters very few options are open to the accountant: some particular practice is either right or wrong.
>
> In this country, on the other hand, accountancy is perhaps regarded as more of an art and it sometimes appears that many different views may be held about the proper way of dealing with the same matter . . . I cannot help feeling that it might be well if the Institute were perhaps to define more clearly what was the correct practice which has to be followed by all accountants in matters of this kind.[87]

Neither of these two critics was, of course, speaking on behalf of the government. Was there a real threat of government intervention, for example to expand the requirements of company law? At the 1971 annual meeting of the London Society of Chartered Accountants, Morpeth, then Vice-President of the ICAEW, had to reply to a fairly aggressive series of questions relating to the establishment of the machinery for accounting standardization, including whether this was 'the wish of the membership or the result of outside influence'.[88] He replied that, 'there had been serious risk that, if the Institute had not been prepared to take this matter in hand itself, then the initiative would have been

taken away from it by the Department of Trade and Industry'.[89] None of the key players interviewed for this book recalls any specific warning of government intervention and Professor Peter Bird pointed out in 1973 that, 'in fact, governments . . . seemed very reluctant to interfere with professional matters'.[90] On the other hand, of course, no government would be likely to stand by while the efficient working of the commercial sector was seriously undermined. In Michael Renshall's words:

> It was a nightmare that was produced, sometimes by leaders of the profession themselves; when they felt it was time to do something, they would produce this spectre and say, 'if you don't do this, you know what will happen', and everybody would say, 'oh, no, no, we'll do it your way'.[91]

The Institute's Response

As the state of accounting principles came under attack, leading members of the profession mounted a careful but robust defence. For example, following the publicity given to the AEI-GEC gap, Harold Edey, Professor of Accounting at the London School of Economics, who was to join the ICAEW Council in the following year, published an article in the *Financial Times*. In this he explained the role of judgement in making provisions for losses on inventory and long-term contracts and explained how, 'plans that Management A had devised and expected to carry through might be judged unprofitable by an alternative Management B'.[92]

This approach continued as the attack hotted up. In response to Stamp's article in *The Times*, Leach published probably the first 'official rebuttal' of a public attack on the profession,[93] also in *The Times*.[94] 'The real difficulty', Leach argued, was 'not the absence or multitude of accounting principles but applying them to the facts of a particular business'. This could be 'illustrated by considering what is involved in valuing stock and calculating depreciation, both of which are substantially dependent on the exercise of judgement'. In describing the potential causes of difference in valuing stock, Leach dwelt exclusively on the difficulty of establishing realizable value and on the possibility that a change in management might legitimately lead to a change in stock valuation:

> If a new management takes control – following a takeover – their general policy as it affects stock valuation may be quite different from their predecessor's. They may wish to discontinue or change product lines, alter the product range, or reduce drastically the volume of stock which is carried, with the result that some stocks immediately become redundant or obsolete. This does not in any way imply that the previous valuation was at fault at the time and in the circumstances in which it was made.

Although he does not identify AEI-GEC (as President of a professional body, he would no doubt have felt it improper to refer to specific cases), anyone familiar with events would recognise the connection.[95]

The defence continued into the following months. In October, Edey contributed an article to *The Accountant* which wearily began, 'it is clear from comment that the fundamental limitations of financial reports as guides to action are still underestimated in some quarters'.[96] Edey stressed again the role of judgement and the likely effect of changed management after a takeover but advocated the disclosure of 'the bases on which ... reports have been prepared' and the 'assumptions'[97] used, suggesting that, to avoid unduly lengthy annual reports, these could be given in a separate statement filed with the Company Registrar and available on request. In November, it appeared that the campaign was beginning to bear fruit. A feature article by Ian Davidson, of the *Financial Times*, pointed out that accountants were amongst the professions looked to as scapegoats when things go wrong and asked 'is this fair?' to which he gave the answer, 'no'.[98]

At the same time, however, a subtle change of line can be discerned in the ICAEW's public position. On 7 November, the President gave a speech at the South Eastern Society of Chartered Accountants' annual dinner[99] in which, while defending the profession against criticism in the press 'for financial debacles when there was no evidence of blame attaching to them', he argued that 'chartered accountants ... must change their attitude towards public relations'. He went on to say: 'Accountants should be much more informative as to the basis used in selecting accounting principles. If we recognised this it would do a lot to clear away criticism of our profession.'[100] On the same day, Morpeth, who was shortly to become Vice-President of the Institute, made a speech at the annual banquet of the Warwickshire Society of Chartered Accountants,[101] in which he conceded that 'some of the recent criticisms of the profession were ... justified', and suggested that 'the profession ought, perhaps, to go as far as giving a list of recommended best practice and disclose variations from it'.

These speeches no doubt reflect discussions at the ICAEW Council meeting two days earlier. As the first item of business, the meeting considered a special report from the President, setting out the profession's, 'present troubles, and more to come', and recommending that the Council should take steps to reduce the alternatives available in financial reporting, establish accounting standards and secure disclosure of departures from them, expose proposed standards to a wider audience, and police practice performance.[102] The Council agreed to set up a working party to prepare a draft Statement of Intent for consideration at the following month's meeting. At that meeting, on Wednesday 3 December, the Council agreed to issue its, now-famous, Statement of Intent. As Leach told the press, 'a new era for accounting was opening'.[103]

Causes and Contingencies

The general tendency for regulation to grow in extent and sophistication is well-documented[104] and studies by Professor Stephen Zeff[105] and others,[106] in many jurisdictions around the world, have shown that the prescription of financial reporting practice has developed along similar lines. The decline of the nineteenth

century *laisser faire* approach to the British commercial sector, and the expansion in the size of the sector, resulted in increasing political and legal pressures for better disclosure.[107] Thus it was almost inevitable that a greater degree of regulation in financial reporting would come about in the second half of the twentieth century; the issue, however, is why did a dramatic move towards prescription come about in 1969 and in the form in which it did?

It is instructive to compare the emergence of concern about, and machinery for addressing, variety of accounting practice in the UK and the USA. In the USA, concern first emerged in the early 1930s, in part as a result of the Great Crash of 1929, to which it was believed poor accounting had contributed.[108] The investment community, even at that early stage, regarded *variety* of practice as evidence of *poor* practice. For example, J. M. B. Hoxey, a member of staff of the New York Stock Exchange – not an accountant – pointed out to a meeting of investment regulators that the Exchange knew of eight different methods of accounting for periodic stock dividends which had received the approval of certified public accountants. In a, not entirely well-received, appearance at the American Institute of Certified Public Accountants' annual meeting four months later, he announced that a ninth method had been discovered.[109] Concern was translated into action and, by 1934, the American profession's attempts to limit practice by identifying accepted accounting principles were under way.[110] The structure was developed under the guidance of George O. May, who had a background in the British profession, yet pioneered a system radically different from the approach with which he was familiar. In the words of Reed Storey, a path-breaking historian of the development of accounting standardization in the USA:

> The U.S. business and financial community lacked the centralizing tendency which characterized that of the United Kingdom. The size of the British Isles and the class structure of her society contributed to the formation of a closely knit managerial and banking fraternity based on mutual acquaintanceship and respect. In the United States, on the other hand, regional rather than national groupings were the rule, and antitrust laws hampered co-operation both within and between industries.
>
> In addition, British practice with respect to corporate accounting was built upon a concept of the corporation not applicable in the U.S. The 'private company' was viewed essentially as an extension of the partnership . . . Hence the proposition followed easily that the owners, through their elected representatives, should be permitted to choose the methods of accounting which regulated interest among themselves, as long as creditors were protected. By 1930, however, corporate development in the U.S. had attained a degree of separation of ownership and management in which the interests of management were generally considered inimical to those of shareholders.[111]

Zeff argues that developments in the USA preceded those in the UK, 'because of its more developed securities market, the aggressiveness of its financial press,

and the accounting philosophy of the SEC'.[112] At least two of these factors, the first and the last, are linked fairly closely to Storey's more sociological model.

By the middle of the twentieth century the UK was catching up with the USA, both in the evolution of the modern business corporation[113] (including the separation of ownership and control, of which the contested takeover is a consequence) and in the relative decline of the closely-knit, class-based financial community observed by Storey in the 1930s.[114] Maxwell's social origins and attitudes, summarized in the title of Tom Bower's biography, *Maxwell: The Outsider*,[115] probably predisposed him against complying with the norms of the community of which he found himself part. The UK was also catching up in the aggressiveness of the press. The Business News section of *The Times*, which carried Stamp's attack, began life only on 11 April 1967, with its parent employing an additional thirty journalists to staff its pages.[116] Perhaps here, too, the old class loyalties were breaking down – in 1967, *The Times* was acquired by The Thomson Organisation, itself dominated by Lord Thomson of Fleet, 'a Canadian upstart', in Bernard Levin's words, who went through life 'collecting newspapers, with a satisfied chuckle, as another man might collect postage stamps or post-Impressionists'.[117]

By the late 1960s, the extent and apparent arbitrariness of differences in financial reporting practice were certainly being drawn to the attention of the profession from within. For example, *The Accountant* ran a series of articles by Michael Greener, starting in January 1968,[118] which anatomized variety in accounting practice. Several other articles on the subject appeared in the magazine in 1969 alone,[119] although the official journal of the ICAEW, *Accountancy*, was largely silent on the matter,[120] and *The Certified Accountants Journal*, the official journal of the Association of Certified and Corporate Accountants,[121] was wholly silent. *The Accountant* was obviously a little nervous about its daring in carrying Greener's material: one of the articles was preceded by editorial remarks concluding that 'his findings . . . will probably not be accepted by all our readers without question but they will undoubtedly stimulate thought – and, we hope, provoke further comment'.[122] In fact the articles provoked very little comment, at least in the correspondence columns of *The Accountant*. For example, the last three of Greener's articles appeared in consecutive weeks and the following issue, that of 11 October, contained just two letters on the subject,[123] advocating longer audit reports, payment of audit fees by a central levy, and 'more realistic . . . principles'[124] such as recognizing fixed assets at valuation.

So long as discussion is limited largely to the profession itself, the profession retains the initiative in deciding whether, and what, action is needed.[125] A number of developments were shaping the views of the profession's leaders during the 1960s, all of them pointing to the need for a reduction in variety. These need to be seen against the increasing importance which technical issues, and those responsible for managing them, were assuming within the profession:

> Technical partners . . . were just beginning to assume a position of power in the major firms. Before then, technical partners were just regarded as

> mechanics, but as life got more complicated all the firms realized that they needed to ... make sure that they had got a logical framework ... for the positions they were taking.[126]

An important influence was the increasing interaction between the UK and North America, fostered particularly by moves towards the creation of international firms, either as combinations of UK and US practices or by the creation of new offices.[127] Deloitte, Plender Griffiths & Co. merged with Haskins & Sells of the USA to form Deloitte, Plender, Haskins & Sells in 1952; Cooper Brothers & Co. merged with Lybrand, Ross Bros. & Montgomery, a US firm, to create Coopers & Lybrand in 1957; and George A. Touche & Co. merged with two American Touche practices to form Touche, Ross, Bailey & Smart in 1960.[128] Perhaps the most important single development in this area[129] was the creation of a London office by Arthur Andersen & Co., which took place in 1957.[130] The firm had a particularly rigorous approach to thinking through the issues underlying accounting practice.[131] UK and US partners in the same firm would be briefing each other on practice in their own country and, for UK partners, 'it was becoming harder and harder to explain why we didn't have a rule book'.[132]

The opening up of British practice to North American influence was accelerated by the creation of the Accountants International Study Group in 1966. The Group comprised representatives from Canada, the USA and the UK and included seeking 'a distillation of best practice'[133] among its objectives. Both Leach and Sir William Slimmings, the President of the Institute of Chartered Accountants of Scotland in 1969, were members and Slimmings felt that it was his experience in the Group that brought him to realize that the Scottish Institute should move away from its traditional antipathy towards the provision of technical guidance to members.[134]

Another influence was the beginning of a more aggressive approach by companies to financial reporting and what is now called earnings management. Although extraordinarily timid judged against contemporary activity, preparers were beginning to argue with their auditors about what was acceptable and,

> firms would feel fragile because they would say, 'we can't possibly accept that method' and the client would say, 'but X accepted it with Y'. That was one of the driving forces for having standards – that's why people were prepared to accept them more rapidly.[135]

The larger firms were also aware that, among some of the smaller firms, there was 'a distressing low standard', for example a willingness to accept recognition of stock at directors' valuation, and that 'things needed stiffening up'.[136]

There is evidence that some professional leaders, including Leach and Benson, had come to the view that action was necessary before 1969. It was Benson who had secured the increase in staffing for the Institute's technical work that saw Renshall's appointment to the secretariat in 1960. This was designed to support an expansion in the technical guidance given by the

ICAEW, though he was not at that time contemplating a change in its status from recommended practice.[137] Leach shared Benson's view and, 'as early as 1965 ... had publicly "lamented" the accounting profession's lack of leadership in improving the presentation of accounts'[138] – his comments were made at an ICAEW conference during a session on new Stock Exchange regulations.[139] He regretted that it should be the Exchange that was leading innovation in disclosure and drew attention to the more active role of the profession in the area in the USA. Such views were part of a 'new climate' at the Institute noted by Zeff, which embraced a reduction in the average age of Council members, the creation of the AISG in 1966 and a Professional Standards Committee in 1967, both Benson's initiatives, and the re-launch, at Leach's initiative, of a scholarly journal.[140]

Some of the hardest-hitting attacks on variety in accounting practice in the 1960s came from accounting academics, a group greatly increasing in number in several English-speaking countries, including the UK, during the period.[141] As practising accountants often point out, accounting scholars have no clients to appease and self-publicity rarely harms an academic career, while some are attracted or driven to an academic career by dissatisfaction with the practices they are asked to follow.

Although some leaders of the profession were conscious of a need to do something about variety in accounting practice, that is not to say that they wanted to go as far as the steps finally taken in 1970, or that they could have carried their colleagues with them if they did. At the annual general meeting of the ICAEW on 14 May 1969,[142] members raised a number of concerns, including simplification of the tax system, integration of the profession, the effect of high salaries offered in industry attracting staff from audit firms, the need for compensation to auditors for loss of office, the fate of the Institute's annual church service, professional development course charges, and (as always) subscription levels, but no mention was made of variety in accounting practice. Again, a meeting between Secretaries of District Societies of the ICAEW and the Institute secretariat, reported to the District Societies Committee on 1 July, gave no indication of concern on this topic.[143]

The seventeenth ICAS summer school, held on 20–24 June 1969,[144] took mergers and acquisitions as its theme and devoted the whole of Saturday to a discussion on a paper by W. C. C. Morrison, 'one of the Scottish Institute's younger members', on 'the need to promote the limitation of the range of accounting bases presently acceptable in framing accounts'. This 'drew support from summer school members', of whom there were 125, the best attendance ever. Morrison's solution, however, was not authoritative standards, but rather disclosure of the bases used, employing, 'greater clarity and uniformity of expression'[145] so as to 'reveal *over a period* which methods were finding general acceptance and tend to narrow the latitude of choice – especially among companies in the same line of business'.[146] In other words, narrowing the areas of difference by peer group pressure – a solution very much in keeping with the Scottish Institute's traditional approach to technical issues, which was to resist

the provision even of guidance, since this might undermine the individual professional's independent judgement.[147]

If they were aware of it at all, members of the public, the investment community, and the press seemed largely unperturbed by the phenomenon of similar circumstances yielding different accounting numbers, so long as this phenomenon was demonstrated only by logical derivation from the known variety of accounting methods (as in Chambers' million combinations) or empirical evidence of different methods being used by *different* companies (for example, the work of Greener).

The climate created by Rolls Razor, AEI-GEC and Pergamon undoubtedly had an effect here. Although variety in accounting method was implicated in these scandals only to a limited degree, and the profession's leaders knew that and were seeking to defend the profession along these lines, the scope for resistance was clearly significantly undermined by Stamp's contribution to *The Times*, an event recalled many years later with considerable feeling by some leaders of the time: Sir John Grenside, for example, described it in 2002 as 'a very offensive article'.[148] In this and other pieces Stamp displayed the skills of the spin doctor *avant la lettre*. Withering accounts of a million combinations are all very well, but what is needed to convince a lay audience, especially one hearing from the accounting establishment that differences in financial statements arise from the problem of applying accounting methods to complex business transactions, is evidence of real damage, in real cases. And actually, such evidence was difficult to find. Stamp handled this difficulty by deploying what would now be called 'smoke and mirrors': problems in the Pergamon case were described as straightforwardly resulting from differences in accounting *method* when in general they resulted from the abuse of accounting methods by the making of reckless and spurious claims of fact; differences in the AEI-GEC case were ascribed to '"differences of judgement" over the choice of which accounting principles to use',[149] when this is not how the report put it, not a fair précis of how the report put it, and not the case; his writings imply that a string of other cases exist when in fact there were very few.

Thus the scandals provided Stamp with material that he was able to build with considerable effectiveness into ammunition for his cause. The ICAEW held at the time two annual summer schools. The first to take place in 1969 came in early July.[150] It discussed communications, the business approach to the modern audit, tax planning, and decimalization. There is no evidence that variety in accounting practice was mentioned. The September school took place immediately after Stamp's diatribe in *The Times* and, although variety in accounting practice did not feature in the formal programme,[151] Stamp's article, and what *The Accountant* described as 'the whole series of events that led up to [it]', stimulated 'innumerable *ad hoc* huddles'.[152] There is, unfortunately, no record of any views about what should be done emerging from these huddles: did their members want standard-setting machinery or did they want Stamp shutting up and *The Times* writing about something else? Certainly members attending the annual meeting of the London and District Society of Chartered Accountants

sixteen months after the Statement of Intent was published made their views pretty clear; in the course of a fairly hostile session with the ICAEW Vice-President, a number of questions were asked about the new machinery. Members wanted to know 'whether the introduction of accounting standards was the wish of the membership', why they were not consulted before exposure drafts were issued, why standards were mandatory, and why standards were being issued before the question, 'what are accounts meant to do?' had been answered. It would appear that at least these members of the ICAEW had not been lobbying for something along the lines of what they actually got.[153]

By the last few months of 1969, Leach was being 'besieged by members demanding action from the Council to stem the mounting criticism of the profession in the press'.[154] As he put it in an interview for *Accountancy* shortly before he died, 'I was a bit disturbed. I had only just become President and I had people ringing me up and asking what I was going to do about it . . . I had to find something positive to do.'[155] The febrile mood in some quarters of the profession, the press and the financial establishment in the last few months of 1969 offered the profession's leaders both a threat and an opportunity. The threat, of course, was of a collapse in public confidence in financial reporting and in the integrity of the profession. Perhaps most worryingly from the profession's point of view, much press coverage also attacked deficiencies in auditing. For example, in October 1969, the City reporter of *The Guardian* wrote:

> On two separate occasions recently the accuracy of auditor's reports has been questioned in public. This is obviously a highly unsatisfactory situation, and . . . cannot be tolerated . . . [U]nless steps are taken to restore faith in our auditing firms by ensuring that they really do act as shareholders' watchdogs, a major row will break which will do the accounting profession lasting damage.[156]

The opportunity available to the profession's leaders was scope for taking action which might otherwise be resisted by a deeply conservative profession. At the centre of the storm, Leach was conscious of the weaknesses requiring attention and needed to take positive steps, both in the profession's interest and to respond to the calls being made on him personally, and he had the stature, appeal and skills necessary to carry forward an ambitious programme of change.

Storey notes that in the USA there had been three cycles of interest in accounting standardization by the 1960s:

> The second . . . began shortly after World War II and was largely a result of some serious criticism levelled at accounting and accountants . . . Some critics . . . concentrated on the fact that reported income and taxable income were not always the same amount or upon other similar irrelevancies. Criticisms of [this] type were symptomatic, for at the heart of much of the criticism was the basic ignorance of the public about financial statements and business operations in general. As a result of this ignorance,

> financial statements and the businessmen and accountants who prepared them were widely mistrusted. The matter was worsened by the lack of sophistication demonstrated by a number of commentators on the subject. There was, nevertheless, a beneficial result from this criticism. It led to substantial self-examination by accountants, and this, in turn, produced constructive steps toward the improvement of accounting practices and some improvement in public confidence in the results of accounting.[157]

The role played by Rolls Razor, AEI-GEC and Pergamon is perhaps best seen in the same way: criticism of accounting methods was to a large extent unjustified and misdirected but ultimately produced a constructive step towards improvement in accounting practice.

2 The Invention of the Accounting Standard

On 21 October 1969, the chairmen and vice-chairmen of the Parliamentary and Law and Technical Committees of the Institute of Chartered Accountants in England and Wales[1] met the President's Advisory Committee to discuss whether the ICAEW Council should 'take a stronger position on accounting and auditing standards'.[2] As a result of the discussions, the Advisory Committee, on the same day, decided that urgent action should be taken and authorized the President to bring forward tentative proposals.[3] By 27 October, the President's Special Report was complete, and it formed the first substantive item of business at the Ordinary Meeting of the Council held on the following Wednesday, 5 November.

Tentative Proposals

Perhaps unsurprisingly in view of the timescale in which it was prepared, the President's report was brief – three pages with a four page annex. Nevertheless, the report, entitled 'Tentative Proposals for Strengthening Accounting and Auditing Standards',[4] contained a series of quite detailed recommendations. At this stage most of the development work was being undertaken by Michael Renshall, the ICAEW's Technical Director, working closely with Ronald Leach himself.[5] Renshall read English Literature at Clare College, Cambridge. He qualified in 1957, having trained with a practice in Liverpool. He then worked for Pilkington Brothers, glass manufacturers, for four years, following which he joined the ICAEW secretariat. His command of technical issues and qualities as a draftsman were held in very high regard by leading members of the ICAEW Council.[6] He subsequently became a partner in Peat Marwick Mitchell in 1977 and a member of the ICAEW Council in 1986.[7]

Under the heading, 'Present Troubles, and More To Come', the President's report describes the accountancy profession as coming under 'what seems likely to be an increasing hail of criticism'.[8] It acknowledges that 'it may be argued that the criticisms being voiced are unjust and made out of ignorance and misunderstanding', but concludes, bleakly, that 'this is no comfort'.[9] The main criticism of the profession is identified as 'allegations that its standards display undue flexibility and its principles permit too many alternatives'. An explicit

parallel is drawn with events in the USA and the establishment of the Accounting Principles Board[10] and there is an approving reference to one of the Board's, 'declared primary aims [being] "to narrow the areas of difference and inconsistency in practice"'.[11]

The report's recommendations differed somewhat from the actions that were actually implemented. It was proposed that the ICAEW Council should, 'establish fundamental accounting and auditing standards' and 'recommend that all members should use their best endeavours to ensure that financial statements are prepared in accordance with established accounting standards'. Departures would be disclosed 'either in the statements themselves or, failing that, in auditors' reports'.[12] The 'fundamental accounting standards' would be a small core of basic principles. The 'established accounting standards' would, in the first instance, be constituted from among the existing Recommendations on Accounting Principles published by the Council and already in place[13] – in effect the selected pronouncements would become mandatory, so that an initial corpus of standards would be created overnight. Of course, the recommendations had not been drafted in the expectation of their becoming mandatory and many suggested alternative methods. For the future, the report recommended that the Council should 'resolve that its statements on best accounting and auditing practice will as far as possible be unambiguous and definitive'.[14] Major proposals on accounting and auditing standards would be given wider exposure in draft form than hitherto. The final recommendation was headed, 'Police Practice Performance' but, although the section began by pointing out that, 'strengthening of established standards will be ineffective unless members observe them', the remainder of its content was rather less fierce than its title:

> It is not proposed at this time that failure to observe the practice standards established by the Council should render members liable to disciplinary action, but it is proposed that means should be found to investigate and point the lessons of such failures for the benefit of all. This is a matter for the Professional Standards Committee not further considered here.[15]

Annexed to the report is a four page draft 'Statement of Fundamental Accounting and Auditing Standards'.[16] The fundamental accounting standards were:[17] (a) consistency; (b) continuity (that is, going concern); (c) conformity to recognized or justifiable accounting bases; (d) disclosure of sufficient information; and (e) disclosure of bases adopted in preparing financial statements where amounts are material and depend on judgement of value or future events or attribute amounts to other periods. The tests to be met in selecting accounting bases (point (c) above) and determining the required level of disclosure (point (d)) were conformity with: (a) legal and other formal established requirements; (b) standards laid down by the ICAEW Council; or, in the absence of these, (c) accepted business or trade practice or an approach justifiable on 'objective and reasonable grounds not calculated to favour a special interest or view'.[18] The draft included an appendix listing 11 of the Institute's recommendations

which would be 'declared to constitute standards requiring disclosure of departures'.[19] The list in fact contained all the extant recommendations applying to the accounts of companies, other than two relating to accounting for changing prices and one, covering retirement benefits, which dealt with both pension schemes and company accounts. The fundamental auditing standards included in the draft were (a) independence; (b) a proper standard of care; and (c) objective evidence.[20] The closing paragraphs of the draft propose that auditors be required to disclose departures from fundamental accounting standards (and thus, via the fundamental standard requiring that established standards be followed, departures from such standards) unless disclosed in the financial statements themselves.[21]

ICAEW Council minutes of the time did not include a record of points made in discussion or outcomes other than agreed actions. The action agreed in November was that a working party, nominated by the President and led by the chairman of the General Purposes and Finance Committee, Stanley Dixon, would 'prepare a draft statement of intent', for consideration by the Council at its next meeting.[22] We can infer from the document that was produced that the Council did not wish to proceed with the preparation of a statement of fundamental accounting standards, or to convert the previous series of recommendations to mandatory status, or with any action in connection with the establishment of fundamental auditing standards.

The range of topics covered by the recommendations proposed for mandatory status was quite wide and a sudden move to compulsion would no doubt have provoked considerable controversy. For example, depreciation of buildings would have become mandatory and depreciation on freehold buildings and all plant, machinery and equipment would have had to be computed on the straight-line basis;[23] cost of stock would have been required to include 'overhead expenditure . . . appropriately carried forward',[24] at a time when it was common practice for the amount of overheads included in the carrying amount of stock to be limited to factory costs or even variable factory costs;[25] and deferred taxation would have been required,[26] at a time when a third of major British companies were not disclosing a deferred taxation account in their balance sheets.[27] Although the intention had been to consult on the pronouncement setting out fundamental standards, and thus on the change in status of the recommendations, the complexity of the exercise, and the volume of the material on which comment would in effect have been sought, could be argued to go against the report's commitment to openness. Thus the decision to make a fresh start seems wise politically and also in keeping with the philosophy underlying the new approach. Although it was abandoned at the time, some of the structure and text of the draft statement on fundamental accounting standards was re-used, quite soon after, in the second proposed standard.[28] By contrast, the proposal to issue mandatory pronouncements on auditing was abandoned completely and no action was subsequently taken along these lines for another decade.[29] A sophisticated politician would be suspected of having inserted this plank into the platform simply to provide something that could be given up in the bargaining process.

The Statement of Intent

Dixon's working party completed its work on schedule, bringing the draft 'Statement of Intent on Accounting Standards in the 1970s', prepared 'following the general line . . . agreed', to the Council Meeting on 3 December. The minutes of that meeting contain only the final version of the statement, although amendments to the draft must have been required because it is minuted that they should be agreed between the President and Dixon.[30] The approach being recommended, even after the abandonment of some of the suggestions in the President's report, was a radical departure from the Institute's previous position, but there appears to have been very little dissent from members of Council. Professor Stephen Zeff's 1971 study, made when memories were still fresh, records that this was the case, apparently on the basis of an interview with at least one (anonymous) member of Council.[31] In an interview for this book, Sir John Grenside said that he did not recall anyone putting up any opposition to the proposal to issue accounting standards,[32] and this is of some significance because the minutes show that he was not present for the meeting of 3 December, so that his recollection would have been based on the November meeting, at which the general line was agreed. It certainly appears that Leach was confident, presumably in part on the basis of the November meeting, that he would secure agreement in December: the December minutes record that the press conference to mark the release of the statement had already been arranged and, as we have seen, Leach had in fact announced his intention to issue a statement at a public meeting, with members of the press present, some days before the Council meeting.[33] Renshall, who, being a member of the secretariat, was not present for either of the debates, remembers his reaction to finding out that the decision had gone so smoothly: 'I was surprised . . . Afterwards, I recall saying to Ronnie Leach, "was there any argument?" and he said "no, not really." I thought there would be blood on the floor.'[34]

Why was there so little dissent? In part, it was no doubt because, as the anonymous Council member interviewed by Zeff shortly after the event put it,

> The Council felt that something had to be done. There was truth in at least some of the accusations. The Recommendations have not really had sanctions, and they took a long time to prepare. A number of the more difficult problems have been skated over. As a result, some rather wishy-washy Recommendations have been approved.[35]

At the same time the importance of the standing of Leach and Benson[36] should not be underestimated. Leach played the leading role in this episode:

> Ronnie Leach was a great character and very persuasive . . . I think it went through without any serious opposition because [he] produced a fairly convincing argument as to why it should be done.[37]

> It was really Ronnie Leach – a diplomat and a brilliant persuader: if he would take an idea up it was almost certain he would sell it to the Council.[38]

But the position of Benson was also critical. Had he opposed the move, it would have been unlikely to succeed. However, it fell very much within his own way of thinking, so he supported it.[39] The presence of these two dominating characters at the heart of the Institute enabled it to provide the force and focus for a decisive act of professional leadership.[40]

The published statement[41] describes the Council's 'intention to advance accounting standards', and lists five lines of action to be taken:

1. 'Narrowing the areas of difference and variety in accounting practice' by 'publishing authoritative statements on best accounting practice which will wherever possible be definitive'.
2. Recommending that 'when accounts include significant items which depend substantially on judgements of value, or on the estimated outcome of future events or uncompleted transactions, rather than on ascertained amounts, the accounting bases adopted in arriving at their amount should be disclosed'.
3. Recommending that 'departures from definitive standards should be disclosed in company accounts or in the notes thereto'.
4. 'Wider exposure for major new proposals on accounting standards.'
5. A 'continuing programme for encouraging improved accounting standards in legal and regulatory measures', the latter including the City Code and Stock Exchange requirements.

The following, much briefer, paragraph is headed, 'Auditing' but in fact contains only the recommendation that, 'if disclosure of accounting bases or of departures from definitive accounting standards is not made in the accounts or in notes then appropriate reference should be made in auditors' reports'. The next paragraph asserts that 'The Council will do all in its power to assist and support members in the observance of established standards. To this end, it intends to strengthen its machinery for investigating and pointing the lessons of lapses from standards.' Readers are reminded that accounts are presented by directors, not auditors, and that the arbitrariness of the accounting period makes it inevitable that amounts shown depend on 'informed judgement exercised in accordance with accounting conventions' – a rare appearance of something sounding as potentially arbitrary as 'conventions', by contrast with self-evidently valuable and useful 'standards'. Finally, the Council announces that it will 'forthwith establish machinery for furthering [its] proposals'.

The proposed disclosure of accounting bases was carried over from the November report, where it appeared in the draft statement of fundamental standards. The term 'bases' (with the singular 'basis') had been in extensive use for many years: for example it is used in Recommendation N9 'Depreciation of Fixed Assets' as a synonym for 'method'.[42] The intention to recommend that departures from established accounting standards be disclosed in the financial

statements survived from the November report although the statement does not follow the report in explicitly indicating that Council will recommend that members use their best endeavours to ensure that standards are followed or departures disclosed.

The changes from the November report meant that there was nothing concrete to unveil in December 1969; in the event, the arrival of the first mandatory pronouncement was not greatly delayed. However, the adoption of mandatory pronouncements in some of the areas included in the series of accounting recommendations had to wait many years: for example a standard on foreign currency translation was not issued until 1983.[43]

The statement was generally welcomed in the press, despite the lack of concrete pronouncements, although a *Times* leader called for a tougher line.[44] The ICAEW circulated copies to a variety of interested parties, whose reaction was generally strongly favourable.[45] The President of the Board of Trade, Roy Mason, wrote:

> I welcome the steps which the Council is taking to advance accounting standards and to improve the comparability and usefulness of financial statements. I attach great importance to this work and hope that you will keep my department informed about the progress you are making.

There were favourable comments also from the President of the Confederation of British Industry, the Governor of the Bank of England, the chairman of the Issuing Houses Association and the Opposition spokesman on technology and trade, Sir Keith Joseph. Lord Shawcross, chairman of the Takeover Panel, who had criticised variety in accounting practice only a few days earlier,[46] said, 'I think this is an excellent statement and I was very glad to read it.'

What Sort of Standards?

One key problem facing accounting standard-setters was that there was no agreed framework of 'meta-methods' for determining which of two available accounting methods was the better – a difficulty alluded to in Professor Edward Stamp's *Times* article.[47] In the absence of such a framework, practitioners' thinking about how to account for events was strongly influenced by the classes into which items were marshalled for reporting purposes. Thus, there might be a call for a single method of accounting for, say, development expenditure, and it might be argued that the imposition of *any* method would yield some benefit, for example by reducing the time analysts spend on understanding an entity's financial statements, or increasing comparability, or simply eliminating criticism of the profession for allowing two methods. Yet, as Professor Edey pointed out in a contribution to *The Accountant* just as the ICAEW was pondering what to do about the problem of variety in accounting practice,[48] it is easy to demonstrate – in the abstract at least – that such an imposition, usually referred to by both its advocates and its opponents as *uniformity*, could easily

reduce the quality of information provided about the economic condition of an entity.

Suppose that three otherwise identical companies each undertake a given amount of development expenditure on a project; Companies A and B will recover the amount from the successful exploitation of their projects, but Company C's expenditure has proved fruitless. Suppose also that two methods of accounting for development expenditure are available: all such expenditure can be written off immediately or successful expenditure can be capitalized and amortized over the life of the project. Companies A and C follow the former method while Company B adopts the latter. As a consequence, Company A looks like Company C although in economic substance it is actually like Company B. Company C's balance sheet correctly reflects the substance of its project but users do not know this because they have no way on knowing whether the expenditure would have qualified for capitalization under the other method. This position is clearly unsatisfactory, but would the imposition of a uniform method help? The uniform imposition of immediate write-off (or capitalization) would make all three companies look the same, when they are not. It is not difficult to discern that what is needed is a regulation that, if expenditure will be recovered, it must be capitalized while, if it will not, it must be written off. On some definitions, though, this would not constitute uniform accounting because expenditure in the same *class* would be accounted for differently, according to a judgement – necessarily subjective – about its recoverability. More importantly, notice that we have been able to reach a firm conclusion about the best method in this instance only because of our initial assumption that it is possible to distinguish between successful and unsuccessful expenditure without difficulty. Once that assumption is relaxed, for example by suggesting that some expenditure might have a 50 per cent chance of being recoverable, or that it might not be known how likely recoverability is, the best accounting is less clear-cut.

As Professor Peter Bird pointed out in discussing the operation of the new system in 1977, there are, in ordinary language, two distinct uses of the term 'standard' of relevance to a programme of accounting regulation.[49] Performance-type standards, when expressed as targets, are *levels* of performance to be achieved, such as the minimum quantity of meat there must be in a pie before it can be described as a meat pie or the maximum number of trains a train operator is permitted to run late without suffering a penalty. Consistency-type standards are *norms*, compliance with which promotes compatibility, and thus efficiency of operation, such as railway gauges and schemes for specifying engineering components. Consistency-type standards promote better performance, for example avoiding the need to change trains every time a new line is encountered, or to manufacture a separate batch of bolts for each customer, but they do not specify quality. Performance-type standards can also be expressed as outturns, that is as actual levels of performance achieved; for example, when politicians talk of raising standards of health care they do not generally mean, or, at least, do not generally want to be understood as meaning, that *target* minimum performance will be changed without regard to whether the new

hurdle will in practice be cleared. What they want to be understood to mean is that they will make actual performance get better.

Whether intentionally or otherwise, in adopting the term 'accounting standard', the architects of the new system took on all the ambiguity reflected in the previous discussion. The word 'standard' (including the plural) appears no fewer than 17 times in the Statement of Intent's 646 words – actually only 502 words if we exclude the long section reminding readers of the underlying nature of accounts which, itself, does not use term. The preamble to the statement, and the opening sentence of the section covering accounting standards, both refer to the Council's commitment 'to advance accounting standards', which seems to imply raising actual performance, although the use of 'advance' rather than, say, 'improve', might be regarded as literally consistent with an intention simply to issue more consistency-type standards. The commitment to 'narrowing the areas of difference and variety in accounting practice' responds most directly to the concerns voiced in connection with the accounting scandals described earlier and, as Bird points out, it may not be a coincidence that this is the step that is given pride of place in the statement.[50] Since many of the public complaints related to there being *different* ways of doing the accounting rather than to the use of methods that were self-evidently inappropriate, it would appear at first sight that this is a classic opportunity for consistency-type standards and this is how Bird classifies this proposal. Curiously, the statement does not actually use the term 'standard' in this paragraph. It does indicate that the narrowing of variety is to be achieved by issuing definitive statements of *best* practice: yet if the practice has been identified as 'best' independently of its incorporation in the pronouncement, this suggests that the pronouncement is a performance-type standard. It may be that what is meant is that a single method, perhaps no better but, it is to be hoped, no worse than others, will be selected and that, once it is incorporated in the pronouncement, following this method will represent best practice because, if widely followed, it secures uniformity. This takes us back to a consistency-type standard, as argued by Bird, although it is not the normal interpretation of the phrase 'best practice'. Standardization is, indeed, a slippery notion.

The second line of action, disclosure of accounting bases, would, presumably, represent a qualitative advance on non-disclosure (leaving aside cost-benefit issues) and Bird classifies this as a performance-type standard, although again, the paragraph does not actually use the term 'standard'. The third line of action refers explicitly to 'established ... accounting standards', recommending that departures from standards should be disclosed. Since the previous paragraphs do not use 'standard' and the term is not defined elsewhere, we may feel that in principle we cannot be quite certain what the statement intends us to understand here but in practice it is obvious that the reference is to the pronouncements envisaged by the first, and perhaps the second, lines of action. The point is significant because this is the first use in the statement of the term 'accounting standard' to refer to the actual *pronouncements* specifying *accounting methods*. The fourth line of action also refers to accounting standards and, again, it seems certain that the reference is to the pronouncements developed under the first two.

Remaining references preserve the ambiguity. There is to be a programme for improving accounting standards in legal and regulatory measures; in Bird's view *improving* suggests performance-type standards,[51] though, if so, the meaning here differs from its use earlier in the statement. Alternatively, the statement could be interpreted as saying that where law or regulations require a choice to be made from a range of accounting methods, the programme will propose a reduction in this variety, as under the first line of action. Finally the section on the 'support and maintenance of standards' talks of assisting members [of the ICAEW] in 'observance' of standards, which perhaps leans towards a consistency-type interpretation ('observance' rather than, say, 'achievement') but of investigating 'lapses from standards' which surely leans towards a performance-type interpretation ('lapses' rather than 'departures').

From the perspective of those designing the new machinery, this analysis no doubt offers an overly academic approach: what they intended the machinery to do was to reduce – perhaps even eliminate – the variety of methods available for accounting for similar items. The pronouncements, and the machinery for producing them, could be seen as a development – perhaps even a natural evolutionary stage – from the series of Recommendations on Accounting Principles that the Council had been issuing since 1942.[52] The new pronouncements would be designed to overcome the drawbacks of the old: too many alternatives were allowed; documents were too long in development; the series carried too little authority.[53] Where it was possible to identify the best method, or a method better than some, this ought to be selected; otherwise another means of selection – consensus, voting, evidence of converging practice – would be needed. The reduction in variety would, it was no doubt hoped, itself yield some gain from consistency in financial statements. No more than this could reasonably have been expected in the circumstances of the time.

For the exercise on which the ICAEW had embarked, the emerging term 'standard', with its three-fold connotations – the potential for improving quality (performance standards as targets), the actuality of improving quality (performance standards as outturn), and utility derived from the imposition of – if necessary, relatively arbitrarily chosen – norms (consistency standards) – proved to be an inspired choice. For between these connotations lies a no-man's land of ambiguity into which a skilled politician can draw a good deal of wrangling about whether, for example, imposing a method that is not necessarily the best in all cases is nonetheless desirable – and then bury it. Whether intentionally or otherwise, the authors of the Statement of Intent, by skipping lightly between the various connotations, marshalled all the diplomatic potential of the term to the benefit of the new programme.

Building the Machinery

After publication of the Statement of Intent, the pace of events accelerated still further. On the day of its publication, Leach was signing a further Special Report, setting out arrangements for its implementation.[54] He began by stressing

that it was 'essential for the Council to press forward with its plans'.[55] The second paragraph read, somewhat starkly: 'To this end I propose that an ACCOUNTING STANDARDS STEERING COMMITTEE (ASSC) be established.'[56] The terms of reference proposed for the committee were 'to co-ordinate and expedite the Council's programme set out in the Statement of Intent of 12 December 1969 and to maintain liaison on behalf of the Council with representatives of industry, finance and commerce and with other accountancy bodies'.[57]

It was suggested that the initial membership of the ASSC should comprise the President himself, together with George Appleyard (Thorne, Lancaster & Co., London), Laurence Clark (Harmood Banner & Co., London), Stanley Dixon (chairman, The Midland Yorkshire Tar Distillers Ltd., Oldbury, Worcs.), Stanley Duncan (Price Waterhouse & Co., London), Stanley Harding (Financial Director, The Thomas Tilling Group, London), Stanley Kitchen (Foster & Stephens, Birmingham), Douglas Morpeth, (Touche, Ross, Bailey & Smart, London) and Kenneth Sharp (Armstrong, Watson, Milburn, Wyllie & Co., Carlisle). Although Leach was subsequently to claim that, 'care was taken to include on the ASSC leading members from commerce and industry as well as practising accountants',[58] in fact practising accountants dominated. London dominated the provinces and, including the chair, large firms outnumbered small firms.

Leach proposed that, 'initially', he should himself take the chair, 'in [his] capacity as President'.[59] Morpeth became vice-chairman. After training with a small practitioner, Morpeth had joined Touche Ross on qualification and became a partner in 1958. He joined the ICAEW Council in 1964, became Vice-President shortly after joining the ASSC and went on to become the Institute's youngest-ever President. He served as chairman and senior partner of Touche Ross and was knighted in the 1981 Birthday Honours list.[60]

The report recommended that the CBI, the Stock Exchange and the Take-over Panel 'should be among the first to be invited to nominate a liaison member who would attend appropriate meetings and receive papers',[61] and that, 'to establish a close working relationship with the other accountancy bodies', they should each be invited to appoint one observer.[62] The bodies concerned are identified as the Scottish and Irish Institutes, the Association of Certified and Corporate Accountants, the Institute of Municipal Treasurers and Accountants and the Institute of Cost and Works Accountants. The decision to involve the other accountancy bodies only peripherally was a deliberate strategy: 'originally the English Institute proposed to go it alone . . . because they knew it would be virtually impossible to get all those bodies to agree . . . [Leach] said, "if it goes well they will queue to join."'[63]

The report was considered by the General Purposes and Finance Committee on 17 December. The Committee added to the list of proposed members the name of Professor Harold Edey, recently elected to Council and occupant of a chair at the London School of Economics and Political Science; suggested that the Issuing Houses Association be included among the institutions to be invited to nominate the first batch of liaison members; and proposed that the ASSC

itself should be responsible for extending further invitations.[64] The Council considered the amended report on 7 January 1970, accepting its recommendations other than in one important particular. The Institute of Chartered Accountants of Scotland and the Institute of Chartered Accountants in Ireland, rather than being offered observer status, would 'together be invited to fill two seats on the Committee'.[65] In February it was reported to the Council[66] that the Scottish and Irish Institutes had been 'invited together to nominate two members' to the ASSC;[67] both had welcomed the invitation and 'it had been made clear on behalf of the Irish Institute that they would wish to have an Irish member sitting on the committee'. The Scottish Institute, however, 'wish[ed] to know the constitution and procedural rules of the committee' before deciding whether to accept.

Meanwhile, the ASSC itself had now met. The committee put forward to the Council a constitution which was approved, subject to minor amendments.[68] The objects clause in this first constitution read as follows:

> The Committee's objects shall be to propose for the Council's approval definitive standards of financial accounting and reporting. Its objects encompass (a) fundamentals of financial accounting; (b) definition of terms used; (c) application of fundamentals to specific classes of business; and (d) the form and content of financial statements, including presentation and disclosure.[69]

The Committee was to have authority to issue proposed standards, in the form of exposure drafts for comment, in its own name, making it clear that they did not have Council authority. After a suitable period for comment, the Committee would 'lay its proposals before the Council in final form for approval'.[70] In their covering report, the committee argue that this arrangement would speed up the process of drafting standards, 'relieve the Council of much paperwork and need for discussion of detail', and avoid awkwardness if a major change was needed after exposure because the Council would not be put in the 'possibly embarrassing position of having to retreat or change its mind in full public view'.[71]

The committee was to comprise not more than 15 members, including the President and Deputy President of the ICAEW *ex officio* and the two places reserved for the Irish and Scottish Institutes, with the remaining places filled by ICAEW members appointed by the Council; members of the Council were to make up a majority of the committee. The membership term was to be three years, renewable once only, with the cycle commencing in June 1971. Substitutes would not be allowed. The chairman and vice-chairman were to be appointed annually by the President of the ICAEW and could be re-appointed. The constitution stressed that members should 'not regard themselves as representing sectional interests but . . . be guided by the need to act in the general interest of the community and of the accountancy profession as a whole'.[72]

For the release of an exposure draft or submission of a proposed standard to Council, a majority of two-thirds of the whole membership was required, with

voting either by a show of hands or postal ballot. For other matters, a simple majority of those present and voting was sufficient, subject to a quorum of a majority of the membership. Another important clause set out the committee's 'operating policy':

> The Committee shall carry out its work in consultation with, and with the assistance of, the technical arm of the Council (that is, the Technical, Parliamentary and Law and Research Committees), which will continue to be responsible for the initial preparation of material. The Committee shall be free to settle its day to day operating procedures so long as they are consistent with this constitution.[73]

This approach was underlined by the next clause: 'The Committee shall be assisted by the staff of the Technical Department of the Institute of Chartered Accountants in England and Wales.'[74] The Council was told that a five-year work programme was being prepared and views on items to be included in the programme were sought.

The ICAS was not, apparently, consulted in advance about the initial suggestion of observer status or the offer of a seat and neither, presumably was the ICAI. Indeed, Sir William Slimmings records that the Scots learned of the decision to create the ASSC, 'at the beginning of February 1970, immediately after it had been taken.[75] In fact, of course, the decision had been taken on 7 January and the report of the ASSC meeting of 26 January implies that by this time the invitations had been issued and informal replies received: certainly this must have occurred by the Council meeting of 4 February. Precise dates here are of no importance: what is significant is that, however speedily the ICAEW was moving, the Scots and Irish seem to have been expected to move even faster. Given the timescale, it is difficult not to sympathize with the Scots' wish to know more about the proposals. In the event, they found no difficulty in forming a view. In Slimming's words:

> It did not take long to conclude that acceptance of these proposals would put the Scottish Institute into what I regarded as a quite impossible position. Whatever the English Institute did in publishing an accounting standard would be bound to affect the members of the Scottish Institute: the options open to the Scottish Institute would be to agree explicitly with an English Council statement, or to say nothing and be deemed to agree tacitly, or to disagree explicitly. The common thread running through the options was their unattractiveness.[76]

By now, the ICAEW's response to the problem of variety in accounting methods had appeared at the top of the Council's agenda for four consecutive meetings. In March, the pace slackened a little and the Council's attention could return to more routine matters: no mention of the ASSC and the first item on the agenda concerned the pricing policy for *Accountancy*. In the background, however, activity

was continuing. Early in the month, representatives of the ICAS, whose Council had now agreed that it must 'move away from its traditional attitude of opposition to the issue of standards; and that ... the move had to be whole-hearted and not grudging',[77] met their opposite numbers in Moorgate Place. The Scots asked for an 'opportunity for greater participation by them in the work of the committee:'[78] they wanted the ASSC to be be a joint committee of the ICAEW, the ICAS and the ICAI, with Scottish representation increased and final approval for standards resting with the individual institute Councils.[79]

The President's Advisory Committee of the ICAEW resisted the first proposal, 'having regard to the circumstances leading up to the committee's formation', and suggested instead that the ASSC 'be described as being "in association with" the Scottish and Irish Institutes'.[80] This was agreed by the Scots and Irish. The remaining proposals met with more sympathy.

The following month's Council meeting, too, passed without any ASSC business, although the Council heard that a survey of published accounts, prepared under the sponsorship of the Institute's Research Committee, would appear at the end of April 1970. It would concentrate on 'problem areas dealt with in the Institute's "Recommendations on Accounting Principles" or arising from the disclosure provisions of the Companies Act 1967', and the intention was that it would develop into a regular series.[81] The motivation behind the establishment of the survey included a conscious determination to improve compliance with recommendations and requirements by exposing poor practice[82] and the series was to provide an important source of information for standard-setters. Its appearance provoked some controversy, partly because it highlighted weaknesses in professional practice but also because it provided evidence for preparers who wished to challenge recommendations from their auditors.[83]

In May ASSC business reappeared on the Council's agenda – but now as a more routine item: it fell immediately after a recommendation that a club licence be sought for the restaurant and snack bar to be incorporated in the newly-enlarged Chartered Accountants' Hall.[84] The Council was informed that the initial five-year work programme had been prepared[85] and asked to approve revisions to the committee's constitution[86] following the changes in arrangements for participation by the Irish and Scottish Institutes. It was now recommended that three places be reserved for the ICAS, the additional two places being transferred from the ICAEW's quota. The revised constitution referred to the ICAEW as the ASSC's 'governing body' and to the Scottish and Irish Institutes as 'associated bodies'. Proposed accounting standards would now be submitted to the Councils of both the governing and the associated bodies for approval. The ICAEW would consider a proposed standard after the associated bodies and would receive 'formal statements reporting whether the Councils of the associated bodies [had] given the proposal their approval or whether they dissent[ed], giving reasons in the latter case,'[87] although neither the associated nor the governing bodies' decisions would bind other institutes.[88]

Amendments, not all minor, were made to the membership clauses following the increase in the Scottish quota. The *ex officio* places for the ICAEW President and Deputy President were dropped from the ICAEW quota and the number of ICAEW members to be drawn from the Council was lowered to six. Committee members were to be appointed annually, from 1 July, without an upper limit to their service. It was now explicitly stated that the chairman and vice-chairman of the committee would be members of the ICAEW. The Council approved the eleven ICAEW members of the ASSC for the year 1970–71 (presumably officially from 1 July, 1970, although internal secretariat documentation records June 1970 as the handover[89]). Appleyard and Dixon left the committee after a rather brief tour of duty. A new member from Council, John Frith (C. & J. Clark, Ltd., Somerset), joined, and two members, David Hobson (Cooper Brothers & Co., London) and Stanley Wilkins (Deloitte, Plender, Griffiths & Co., London), were co-opted. The same eleven members continued for the year from 1 July, 1971.[90]

The three places reserved for the ICAS had been taken up in May by Slimmings (Thomson McLintock & Co., London, immediate past-President of the ICAS), George Dewar (Peat, Marwick, Mitchell & Co., Glasgow, President of the ICAS), and Ian Morrow (London).[91] Slimmings had been the ICAS President at the time the new arrangements were being negotiated and Dewar had also been directly involved in the discussions.[92] The Irish place was also taken up in May, by William Lyster (Craig, Gardner & Co., Dublin).[93]

By June 1970, invitations from the ICAEW Council to appoint 'liaison members' of ASSC had been accepted by the Stock Exchange, the CBI, the Takeover Panel, the Issuing Houses Association and the Society of Investment Analysts.[94] Plans to bring in the three principal accountancy bodies not directly represented on the ASSC had not got very far, however. This may have been due to a combination of the distraction caused by changes in the arrangements for the Scots and Irish institutes together with uncertainty over the long-term position, because a major scheme for the integration of the entire profession in the UK was under discussion at the time.[95] On 1 July, the Council agreed to extend invitations to the ACCA, IMTA and ICWA to appoint 'liaison members to attend plenary meetings of ASSC as observers, in the same way as the five outside observers already appointed'.[96] It was, perhaps, unfortunate that the accountancy bodies received their invitations only after the 'outside observers' had been appointed, but the invitations were accepted and by April 1971 two meetings with the liaison members had been held, with a third scheduled for 10 May.[97]

In June 1970 the proposed scheme for the integration of the UK accountancy profession collapsed, following its rejection by the membership of the ICAEW.[98] In October, in an endeavour to maintain the 'spirit of co-operation which had been engendered between the six bodies over the past four years', the Council authorized the President to approach his fellow-office holders in the other five bodies to suggest regular meetings 'to discuss matters of mutual interest'.[99] These meetings were to lead, in 1974, to the formation of the Consultative

Committee of Accountancy Bodies, about which we will hear much more later.[100]

In the meantime, pressure for closer involvement of the ACCA, ICWA and IMTA in the work of the ASSC grew. In March 1971 *The Accountant* carried a letter from Desmond Goch, a member of the ACCA, calling for members of the three bodies to be co-opted onto working parties of the ASSC.[101] The journal's editorial columns in the following issue alluded to 'increasing criticism' of the limited involvement of the other bodies and indicated some sympathy with the view that at least the ACCA, as 'the second largest body of accountants in the UK', 'had some claim to be consulted – not merely informed'.[102] The column's measured conclusion was that some increase in representation would be acceptable – provided that the newcomers bore their share of the bill.

As on other occasions in the ASSC's early days, these demands met with a quick response. In October 1971, the ICAEW Council agreed that the ACCA and the ICWA should be admitted to 'associate membership' of the ASSC[103] on the terms set out in a memorandum from the President's Advisory Committee.[104] The ACCA and the ICWA were to have two seats each, with the ICAI increasing its representation to two seats. The two-thirds majority rule was retained and, to avoid any existing member having to give up a seat, it was agreed that total membership would rise from 15 to 21, with the membership of the ICAS remaining at three and the ICAEW block increased to 12.

The tone of the memorandum is somewhat grudging. It argues that 'the increase in numbers will without question slow the Committee's deliberations and add to organisational problems and costs, but seems unavoidable'.[105] It goes on to point out that the Scots and Irish are now over-represented in proportion to their memberships – the President's Advisory Committee evidently did not feel obliged to balance this point by mentioning that the Association and the ICWA were under-represented – and adds that, 'more important, the English Institute will no longer hold the balance of power in ASSC'.[106] This is to take a fairly demanding view of what constitutes the balance of power: ICAEW members could certainly stop proposals for exposure drafts and standards, and even minor recommendations needing only a simple majority; what they could no longer do was force through an exposure draft or proposed standard against the combined votes of all the members of every other body represented on the committee – ICAEW members would have required support from only one other body to achieve the required two-thirds majority. In any event, as the memorandum went on to point out, the constitution required members of the ASSC not to vote on a sectional basis. It added the further comfort that, 'the balance of power will remain with the Chartered Institutes' and that 'in any case, the rules of the ASSC will remain under the sole control of the Council of the English Institute'.[107] It did not draw attention to the fact that, since final standards were to be issued, not by the ASSC, but by the various professional bodies, the number of bodies with an individual veto over proposed standards would increase from three to five.

The recommendation was subject to the ASSC 'receiving satisfactory assurances from the Association and the ICWA: (a) to use their best endeavours to support accounting standards in common with the Institutes of Chartered Accountants; and (b) as to questions of finance and management'.[108] Satisfactory assurances were received and the change was announced in late October 1971.[109] The four members from the new associates on 1 July 1972 were Alan Nelson (Opass Billings Wilson & Honey, Sidcup) and Bertram Ogle (ICI, London) for the ACCA, and Arthur Fryer (also of ICI) and Henry Southall (Plessey, Ilford) for the ICWA.

Impelled by a belief that it needed to be seen to be responding to a crisis with swift and decisive action, the ICAEW Council, led by Leach and with Renshall's assistance, built the machinery for producing accounting standards, from a standing start, within six months. The achievement fully justifies Leach's claim that 'this was an occasion when the Council proved that it could act vigorously and quickly'.[110] The speed is impressive for *any* substantial initiative taken by a professional accountancy body, at least until the more commercially-minded approach of the 1990s, but the radical nature of the machinery's purpose, and the level of co-operation achieved with other accountancy bodies and with institutions beyond the profession, make it even more impressive.

Designing Accounting Standards

As we have seen, the Statement of Intent came close to giving the name 'accounting standards' to the actual pronouncements that would implement its objectives, but stopped just short of doing so. In the event, the pronouncements were officially christened 'Statements of Standard Accounting Practice', a phrase which arguably moves the meaning somewhat nearer to the connotation of consistency – standard practice, not standards of, or for, practice. However the more general term 'accounting standards' soon entered usage as the informal description, hardly surprising given the name of their source. Indeed, the constitution of the ASSC actually referred to 'definitive standards of financial accounting and reporting'[111] and an Explanatory Foreword, agreed in January 1971[112] introduced 'accounting standards' as the abbreviated version of the full title of the documents in the first line of the first paragraph. It became the designation of choice in other regimes: in 1973, the USA saw the demise of the APB, which had previously issued 'Opinions', to be replaced by the Financial Accounting Standards Board, which issued 'Statements of Financial Accounting Standards'.[113] Before then, *The Accountant* was referring to US pronouncements as standards: in April 1971 it headlined an article on US developments, 'Proposed new accounting standards' while, in the text, describing the documents as opinions.[114] Also in 1973, a new body established with global ambitions, as it happens by Benson, was given the name the International Accounting Standards Committee and set about developing International Accounting Standards.

Who was responsible for importing the term into UK accounting practice? Leach gives us a clear answer: '[the Statement of Intent] was the first time that

the term "Standards" was adopted in place of recommendations, opinions or practices, and credit must be given to Michael Renshall, who suggested it.'[115] But this answer relates specifically to the naming of the pronouncements and thus, given the range of connotations and usages explored earlier, represents only the last, albeit important, link in the chain. The earliest prominent use of the term in the USA[116] is in a 1940 American Accounting Association monograph by W. A. Paton and A. C. Littleton, who gave their work the title *An Introduction to Corporate Accounting Standards*.[117] The meaning they intend actually approaches that eventually adopted by UK standard-setters in one way, in that it refers to a prescription for the operations of accountancy (rather than outturn performance), but it is clear that they envisage something rather more like what has come to be referred to as a conceptual framework,[118] so that consistency-type pronouncements would hardly qualify:

> The term 'standards' is used advisedly. 'Principles' would generally suggest a universality and degree of permanence which cannot exist in a human-service institution such as accounting ... A statement of accounting standards should represent an integrated conception of the function of accounting as a means of expressing the financial facts of business in a significant manner ... [I]t must represent a practical tool of business and finance ... Standards should deal with fundamental conceptions and general approaches ... In essence, a scheme of accounting standards should consist simply of an explanation of what accounting attempts to tell the interested parties through the medium of reports of financial position and results of operations ... Although accounting standards are not in themselves procedures they point towards accounting procedures ... Standards ... should not prescribe procedures or rigidly confine practices; rather standards should serve as guideposts to the best in accounting reports.[119]

During the late 1940s and 1950s the AAA, principally then, as now, an academic organization, began to use the term 'standard' in connection with its proposals for financial reporting requirements, initially with the main connotation of a performance-type pronouncement but later with a more general meaning.[120] The use of the term 'principles' in the USA had, by the late 1960s, already attracted criticism because of the implication of greater force and universality than was appropriate for the pronouncements in issue.[121] In any event the term had been included in the title of the non-mandatory British series that the new pronouncements were to replace and so another term had to be found. The search involved 'quite severe philosophical contortions to arrive at a word that seemed appropriate'.[122]

The deployment of the term 'standard' in the UK, in the general context of the problem of variety in accounting methods, predates the publication of the Statement of Intent. The term was, indeed, in regular use in the pages of *The Accountant* during the discussion of the problem during 1969. The series of

articles by Greener in *The Accountant* has already been referred to,[123] and this used terms derived from the word 'standard' on more than one occasion; for example on 9 August he wrote: '[the] survey [reported in the article] emphasizes the fact that methods of reporting are so far from being standardised that any proper comparison of one company with another is often difficult and frequently impossible'.[124] Indeed, the three articles published in late September and early October 1969 actually ran under the general title 'Accounting standards'. References within these articles include:

> [U]nless members of the accounting profession recognise and accept common standards, both in the preparation of accounts and in auditing them, and apply such standards consistently, it is not surprising if the reports they produce tend to be confusing to the lay reader.[125]
>
> [I]t may be asked whether individual firms of auditors are consistent in the standards they apply to various clients.[126]
>
> Mr Fred Neumann, after some research into American practice, finds little evidence of agreement among accountants and suggests that this disagreement produces results that cannot in any way be considered satisfactory. He states, *inter alia*:
>
> > There is considerable discussion among accountants about the necessity of protecting the free exercise of the independent auditor's professional judgement. But can judgement based on a standard that permits such diverse results be defended?
>
> He notes the absence of any guidelines as to materiality and therefore the tendency for standards to be allowed to range rather widely and asks:
>
> > If the independent auditor may implement the standard within such wide boundaries, what can his audience reasonably expect?[127]

In October, Edey's article[128] also used the term 'standardisation', this time linking it to the dangers of seeking to impose uniformity on accounting methods relating to measurement, as distinguished from presentation:

> Like standardisation of spelling, uniformity in presentation can increase the speed of comprehension. It would, however, be a mistake to believe that it would be possible so to standardise accounting procedures that a unique figure of profit was always reported in given circumstances without detriment to the quality of the information.[129]

The one thing that is clear from these examples is that the term is not being used systematically with only one of its several meanings. It is Renshall who can claim the credit for the transition from the goal of improving performance to a name for the pronouncements designed to achieve this. Although the latter usage was challenged in some quarters, 'most people seemed happy enough with it'.[130]

The format for accounting standards was specified by Renshall in a 'Provisional Series Format and Style Directive' presented to the ASSC in March 1970.[131] Exposure Drafts and standards were to be in two parts, the first an 'explanatory memorandum' and the second the standard proper.[132] The explanatory memorandum was to be 'a self-contained report including such matters as: scope of study; problems examined; evidence and data; arguments for and against different practices. Its object is to explain the problem and the solution set out in the [standard section].'[133] The standard section itself 'should stand on its own without reference to the explanatory memorandum and should be: terse; clear; pointed; definitive; [and] unambiguous'.[134] The contents of the standard 'should be confined to one or more of the following: (a) matters of fundamental principle (or their application in particular cases); (b) definition of terms; (c) matters of form, content, presentation and disclosure'.[135] If reference to legal requirements was required, it should be dealt with in an appendix.[136] In drafting statements, 'every effort' was to be made to 'use plain English; keep sentences and paragraphs short; ensure technical terms are clearly defined; [and] avoid let-outs, weasel words and options'.[137]

Only minor changes were introduced into the proposed structure for the first exposure draft: the explanatory memorandum became an explanatory note; definitions were placed in a separate section; and the legal material was elevated to a section rather than an appendix. This basic structure survived to the final standards issued by the committee. Whether all its documents were clear, definitive and unambiguous, avoiding let-outs, weasel words and options, is a question we shall be examining further.

In 1983, the ICAEW Technical Advisory Committee recommended that the structure of standards be revised, to commence with the standard proper, followed by definitions and the explanatory note,[138] apparently so that the objective that the standard proper be self-explanatory would be tested by users reading it without the benefit of the explanation. The recommendation was not accepted, on the grounds that, by then, re-writing existing pronouncements would involve 'unjustifiable expense and disruption'.[139] The Technical Advisory Committee stood its ground, calling the response 'less than helpful', arguing that, 'as one of the most consistent responders to discussion papers and exposure drafts, [the Committee] believes that its unanimous recommendation should carry considerable weight', and pointing out that the restructuring could be carried out progressively as standards were revised.[140] As a consequence the matter was looked at again but the previous decision was confirmed, not least because no standard-setting body could be found anywhere in the English-speaking world that had adopted the structure advocated by the Technical Advisory Committee.[141]

Enforcement

The architects of accounting standardization were very conscious of the difficulties their new machinery would face in the area of enforcement. As we have

noted, the President's November Report foresaw that 'strengthening of established standards will be ineffective unless members observe them', and referred to the need to 'police practice performance',[142] while stopping well short of regarding non-compliance as a disciplinary matter. In the relevant paragraph of the report, quoted on page 23, we may observe the President wriggling on a hook. Compliance is important. It cannot readily be secured. There is the implied threat that failures may become a matter for disciplinary action at some unspecified time in the future. There is the possibility of failures being given a public airing for the mutual benefit of all – but, presumably, also the embarrassment of the perpetrators. Finally, he is off the hook: 'this is a matter for the Professional Standards Committee not further considered here'.[143]

The immediate route towards enforcement envisaged by the paper was actually set out earlier in the paragraph: the Council would,

> recommend that all members should use their best endeavours to ensure that financial statements are prepared in accordance with established accounting standards but that if they are not departures should be disclosed either in the statements themselves or, failing that, in auditors' reports.[144]

This two-pronged approach – preparers would be expected to comply, or disclose departures, or have it done for them in the audit report, while all professional accountants would use their 'best endeavours' to ensure that this was done – survived pretty well unaltered into the machinery built in 1970 and extended over the next few years. It was the result of careful deliberation by the architects of the system, pondering the fundamental problem of the weakness of professional discipline in relation to this sort of regulation. Here is Renshall's thinking:

> I realized we couldn't go to a binding rule because we didn't have the enforcement mechanism. Gradually the idea emerged – many people were consulted – that the rule will be, it is assumed you have followed the standards unless you say you have departed and if you depart you must give the reason . . . and be ready to answer questions – that was the big stick. It was a little bit of a bluff between you and me.[145]

Although the Statement of Intent did not employ the term 'police', it did refer to the Council's intention to 'strengthen its machinery for investigating and pointing the lessons of lapses from standards',[146] phrasing which hints, but is by no means clear, that lapses will not be a disciplinary matter.

The approach of requiring disclosure of departures in the financial statements or the audit report was similar to that employed at the time in the USA.[147] The American Institute of Certified Public Accountants was also stepping delicately in matters of enforcement: for example a failure to disclose a departure resulted

in referral to a committee of the Institute concerned with 'educating the reporting member and encouraging him to comply'.[148]

The formal position of the Councils of the three chartered institutes was set down in an 'Explanatory Foreword to Statements of Standard Accounting Practice', drafted by the ASSC, recommended unanimously to, and adopted by, the Council of the ICAEW in January 1971. Although the document was offered as a general explanation of accounting standards, in fact the 'vital part'[149] of it, occupying exactly half its length, was the description of enforcement arrangements. According to Leach, the Foreword was, 'by no means easy to draft'.[150] Paragraph 3 was headed, 'Obligation for chartered accountants to observe accounting standards or justify departures' and read:

> The Council expects members of the Institute who assume responsibilities in respect of financial accounts (signified by the association of their names with such accounts in the capacity of directors or other officers, auditors or reporting accountants) to observe accounting standards. The onus will be on them not only to ensure disclosure of significant departures but also, to the extent that their concurrence is stated or implied, to justify them. The Council, through its Professional Standards Committee, may inquire into apparent failures by members of the Institute to observe accounting standards or to disclose departures therefrom.[151]

The explicit position of the original Special Report, that failure to comply would not be a disciplinary matter, had apparently been abandoned. That this was, indeed, the intention was made clear in a Statement by the ICAEW Council issued at about the same time, in the wake of the failure of the integration scheme. A special meeting of Council on 4 November 1970, to consider the development policy of the Institute in the aftermath of the scheme's collapse[152] had requested the office-holders to draft an announcement to the membership explaining the 'very serious situation'[153] the Institute faced. This draft was received at the following month's meeting but judged to be too negative and a further draft, in 'brief and positive terms'[154] was requested. This was duly delivered to the January 1971 meeting and included a rather anodyne statement that,

> As best practice is progressively defined [by accounting and auditing standards] and announced, all members will be required to follow the code or disclose and justify departures. The possibility of giving positive support to members who take a stand on a matter of principle is being investigated.[155]

This paragraph was now thought to be too positive, and it was agreed that 'a clear indication be given to members of … the possibility that disciplinary action might be taken on departures from established accounting standards'.[156] This was done in the draft announcement agreed in principle at the February meeting, which included the following paragraphs:

> As best practice is progressively defined and announced, all members will be required to follow the code or disclose and justify departures. Failure to do so may render a member liable to disciplinary action.
>
> Means of giving positive support to members who take a stand on a matter of principle are being sought and studied.[157]

The draft also included a description of the programme of work for the ASSC,[158] an indication that 'a comparable programme on auditing standards will be undertaken as soon as resources permit', and a firm statement that, although in the past poor work had not been a disciplinary matter, 'Council [now considered] that more positive measures, which may include disciplinary action, will need to be taken in cases of unsatisfactory professional work.'[159] The text was to be incorporated in the President's Statement to the Annual Meeting and the President was authorized to rewrite it in an appropriate style.

Why the significant move, from the November Special Report's disinclination to propose disciplinary action to the Council's apparent determination in February to invoke disciplinary procedures? Accounting standardization seems here to have been caught up in the Council's general concern, in the wake of the failure of the integration, that 'it is doubtful whether the majority of members appreciate the full magnitude of the problems ahead, and the measures which are necessary to meet them',[160] to quote the December draft. The problems perceived by the Council included that 'accounting and auditing standards are under persistent attack from business and the press'[161] (they must here have meant outturn performance since no standards in the form of pronouncements yet existed), and some members of Council, at least, were concerned about 'the poor quality of the work of . . . the smaller firms' while at the same time recognizing the difficulty of making this point in public.[162] Hence the move to making unsatisfactory professional work, including failure to follow accounting standards, a disciplinary matter can be seen as an attempt both to improve professional performance in response to criticism and to shock a complacent membership into an appreciation that life could not go on as before. However, as we shall see, subsequent events suggest that Leach's preferred approach of November was the more realistic one.

Another feature of the draft's comments on compliance worth remarking on is the plan to provide support for those making a stand on principle, which becomes firmer as each draft emerges. In the event, of course, little was done about this and few, if any, cases arose of members taking a stand on principle over an accounting standard to the point at which Institute backing would have been needed.

Returning to the Explanatory Foreword, paragraphs 5 to 7, headed 'Exceptional and borderline cases', offered some guidance which, while certainly both necessary and appropriate in the light of the developmental stage at which accounting standardization then stood, were to be seized upon by the more sophisticated and creative in the years ahead. They are worth quoting in full:

> Accounting standards are not intended to be a comprehensive code of rigid rules. It would be impracticable to establish a code sufficiently elaborate to cater for all business situations and circumstances and every exceptional or marginal case. Nor could any code of rules provide in advance for innovations in business and financial practice.
>
> Moreover it must be recognised that there may be situations in which for justifiable reasons accounting standards are not strictly applicable because they are impracticable or, exceptionally, having regard to the circumstances, would be inappropriate or give a misleading view.
>
> In such cases modified or alternative treatments must be adopted and, as noted, departures from standard disclosed and explained. In judging exceptional or borderline cases it will be important to have regard to the spirit of accounting standards as well as to their precise terms, and to bear in mind the overriding requirement to give a true and fair view.[163]

The Scottish and Irish institutes issued similar documents and all three institutes held a joint press conference to announce publication.[164] The Foreword had to be slightly amended within a matter of months, to make it clear that SSAPs were not intended to apply to accounts prepared overseas for local purposes, though they did apply to the accounts of overseas subsidiaries incorporated in UK group accounts.[165]

At the Council meeting that agreed this revision, a draft statement on auditing, 'The Effect of Statements of Standard Accounting Practice on Auditors' Reports', prepared by the Technical Committee in consultation with the Scottish and Irish institutes, was approved in principle. The intention was that publication would follow as closely as possible the publication of the first Statement of Standard Accounting Practice.[166] In the event, SSAP1 was published in January 1971 and Statement on Auditing 17 in the following month. The audit Statement followed the Explanatory Foreword fairly closely in wording and 'fortified'[167] the latter's terms. All significant departures from accounting standards were to be referred to in the auditors' report, but if disclosure was 'fully explained' in the financial statements only a brief reference would be necessary; otherwise more detail would be required.[168] If a departure was not justified, and 'the true and fair view shown by the accounts ... thereby impaired', a qualified opinion would be required together with quantification of the extent of the departure 'unless ... impracticable', in which case the reasons were to be stated.[169] In the 'exceptional circumstances' in which departure was needed to achieve a true and fair view, the audit report would refer to the departure and confirm the auditors' concurrence but remain unqualified and without quantification of the departure.[170] Sharp drew attention to the significance of the Statement's requirement that, even where an auditor concurred with the departure, it was still necessary to refer to the departure in the audit report – the only case of this kind of which he was aware.[171]

On the surface, then, the initial irresolution about enforcement exhibited by the President's November Special Report seems to have been replaced by the steel of the Institute's disciplinary machinery. However, as we shall see, irresolution remained the order of the day. Why was the public banging of drums 'a little bit of a bluff'?[172] And why was discipline, even if it worked as described, to be limited to disclosure of departures? Why, in short, was a professional body that was perfectly willing – and capable – of preventing its members from advertising, or even mentioning their names when interviewed in the media, in such difficulties where accounting standards were concerned?

The problems were two-fold. As far as disciplining accountants as preparers of accounts was concerned, financial statements were, in law, the responsibility of the Board of Directors, which would be exceedingly unlikely to have a majority of qualified accountants. Though it was universally understood that, in almost all cases, Boards simply accepted what they were told by their finance director about how items should be treated in the accounts, it was easy enough for finance directors to assert, before their professional bodies' disciplinary machinery if necessary, that they had used their 'best endeavours' to persuade a cynical Board to follow standards but had, unhappily, failed. Could the Institute really discipline members for failing to persuade non-members to comply with accounting standards, especially if they were to claim to have been following their duty in law to seek out a true and fair view?[173] In 1975, the Explanatory Foreword was revised to reflect the addition of the Association and the ICWA as associate members. The opportunity was also taken to revise the paragraph on enforcement, which occasioned extensive correspondence between the parties involved.[174] The result was that the application of the paragraph to accountants who acted as directors was re-written to indicate only that they were expected to use their best endeavours to achieve compliance or disclosure of departures.[175]

In 1975 *Accountancy Age* carried a report about a threat by Patrick Edge-Partington, the chairman of Crown House, a quoted company, not to comply with a new standard.[176] The magazine had investigated the background:

> As yet there have been no cases of sanctions for failing to comply with standards. The policing is in the hands of the individual institutes and, of course, their power is only over their own members. Stanley Wilkins, a partner in Deloittes and a member of the ASSC, told *Accountancy Age* that the English ICA deals with cases through the professional standards committee. He stressed that not many had passed through its hands, partly because of lack of staff. 'The committee only deals with institute members,' he said. 'If a board member who is a chartered accountant has tried, but failed, to convince the rest of the board then he is off the hook.'[177]

In relation to auditors, the disciplinary machinery stood on somewhat more secure ground, since the firm had sole responsibility for its report. However, in the end the most that auditors could do was to issue a qualified opinion and give information about departures in their own report. In requiring them to do so,

the institutes were seeking to influence the sensitive relationship between auditors and their clients in a situation in which the scope of departures from standards to respond to 'exceptional and borderline cases' was built into the enforcement machinery.

One aspect of the developing structure that made enforcement a little easier was the involvement of the other professional bodies. The role of the Scottish institute was particularly important because of the number of finance directors and auditors throughout Great Britain who were included in its membership: without the ICAS on board, enforcement would have been impossible, first because Scottish finance directors and firms would have been able to ignore standards with impunity and secondly because English and Welsh accountants would then have insisted on the same freedom. Had the ICAEW resisted there might well have been a wholesale migration to the Scottish body.[178]

A potentially important source of support for the enforcement of accounting standards was the Stock Exchange, which had for some years imposed a series of detailed requirements on companies listed for quotation on the exchange. At the time of establishment of the ASSC, the organisation was known as the Federation of Stock Exchanges in Great Britain and Ireland and its conditions for quotation, set out in a booklet entitled *Admission of Securities to Quotation*,[179] included a requirement that companies sign a General Undertaking which specified a number of detailed disclosures for the annual accounts, in addition to those required by company law, but did not set down any general rules about the reliability of the financial statements or any provisions covering measurement.[180] The next edition was issued in June 1972; the organisation's title was now simply The Stock Exchange, the booklet was called *Admission of Securities to Listing*, and the document, the Listing Agreement.[181] A more significant change was that the list of requirements included:

> A statement by the directors as to the reasons for adopting an alternative basis of accounting in any case where the auditors have stated that the accounts are not drawn up in accordance with the standard accounting practices approved by the accountancy bodies.[182]

By way of explanation, a note indicated that:

> The Council [of the Stock Exchange] wish it to be known that they lend support to the policy of the Council of the Institute of Chartered Accountants in England and Wales (in association with the Councils of the Institute of Chartered Accountants of Scotland, the Institute of Chartered Accountants in Ireland, the Association of Certified Accountants and the Institute of Cost and Management Accountants) in formulating standard accounting practices. The Council will expect the accounts of listed companies to be drawn up in accordance with the standards approved by these accountancy bodies; any departure from these standards must be disclosed and explained.[183]

This level of support was achieved only after considerable effort by Leach and Morpeth.[184] As *Accountancy Age* pointed out at the time, though helpful, it effectively left companies free to depart from standards as they saw fit.[185] The report of Edge-Partington's unwillingness to comply with a new standard referred to earlier concluded that, 'the ultimate threat, as Edge-Partington admitted, is the Stock Exchange. As yet there is no movement of information between the two bodies.'[186] Even had there been an exchange of information, of course, the effect would have been to enforce disclosure of non-compliance rather than to enforce compliance.

The proposal of a move to disclosure of departures in the USA provoked significant opposition in the early 1960s[187] but in the UK 'virtually no perceptible controversy ensued'.[188] Zeff speculates that the difference was attributable to a combination of American 'rambunctiousness' and the willingness of British accountants to follow a precedent whereas, in the USA, there was none to follow.[189] It may also have been the case that British accountants employed by preparers observed the scope for creative compliance in the precise wording of the proposal and had confidence in the persuasive powers they could bring to bear on their auditors.

3 Honeymoon Period: 1970–1974

> The ASSC and its works had all the advantage of novelty and it was a honeymoon period for accounting standards.
>
> Sir Ronald Leach[1]

One of the ASSC's earliest actions, in consultation with the Technical, Parliamentary and Law, and Research Committees of the Institute of Chartered Accountants in England and Wales,[2] was to draw up a five-year programme of work encompassing twenty 'major items';[3] this was agreed by the committee on 5 May 1970 and reported to the ICAEW Council on the 12th of that month.[4] The programme is given in Table 3.1.

One of the items, number 18, 'fundamental objects and principles of periodic financial statements', was 'obviously a long-term research project' and the ASSC reported that the Research Committee had been asked to study 'the best means of mounting the work'.[5] Nonetheless a publication was envisaged within the five-year period covered by the programme. It was presumably intended that work on the remaining topics would yield regular standards. A 'planned release date' was given in the programme against each item; neither the programme itself nor the covering report indicates whether this is the date for an exposure draft or the standard but as four months of 1970 had already passed and six topics were scheduled for release in that year, including one on which work had yet to begin, the dates must surely refer to the publication of exposure drafts. The report itself pointed out that 'the programme was ambitious in scale and envisaged a rate of output substantially higher than that achieved hitherto by the [English and Welsh] Institute or the Accounting Principles Board of the American Institute of Certified Public Accountants'.[6] The rate of production of the ICAEW's Recommendations on Accounting Principles, to which the report refers, had been almost exactly one per year,[7] and that was without public consultation or attempting to eliminate all alternative treatments. The ASSC's programme thus envisaged a four-fold increase in rate of output combined with a more demanding product specification. Its target rate was approximately two and a half times that achieved by the Accounting Principles Board: 15 opinions in its first ten years.[8]

Table 3.1 The ASSC's initial five-year work programme

Ref. No.	Topic	Planned release date	Whether work in progress now
1	Disclosure of accounting bases	1970	Yes
2	Form and content of profit and loss account	1970	Yes
3	Form and content of balance sheet	1970	Yes
4	Treatment of investments in the accounts of trading companies and industrial holding companies	1970	Yes
5	Treatment of income of associated companies	1970	Yes
6	Fundamental principles of inventory valuation	1970	No
7	Treatment of extraordinary and prior year items	1971–72	Yes
8	Changes in accounting bases	1971–72	No
9	Fundamental principles, form and content of group accounts	1971–72	Yes
10	Accounting for mergers and acquisitions	1971–72	Yes
11	Accounting for contract work in progress	1971–72	Yes
12	Fundamental principles of depreciation	1971–72	Yes
13	Earnings per share	1971–72	Yes
14	Accounting for research and development	1971–72	No
15	Accounting treatment of pension funds in company accounts	1971–72	No
16	Form and content of pension fund accounts	1971–72	Yes
17	Accounting for changes in the purchasing power of money	1973–74	No
18	Fundamental objects and principles of periodic financial statements	1973–74	No
19	Accounting for goodwill	1973–74	No
20	Insurance company accounts	1973–74	No

Source: Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK.

The work programme was made public at a press conference to launch the ICAEW's new annual survey of published accounts[9] on 29 April, a few days before it was actually approved by the ASSC.[10] The conference was described by *Accountancy* as a 'welcome change for the press'.[11] Leach announced that the first paper would deal with associated companies and was expected to appear by the end of June. He accepted that, 'not all of the new recommendations would necessarily be popular, and that the testing time would come when industrialists and business generally had their first opportunity to comment on the exposure drafts'.[12]

In a speech given in February 1970, Leach said that, 'the formulation of new standards would provide the Council with an immense task over the next five years', but that, 'he thought the result would be that they would have the most comprehensive and definitive accounting standards of any country and the *maximum* disclosure of information necessary to interpret accounts'.[13] Professor Edward Stamp derided what he took to be hubris in the President's comment,

describing it as 'rather like making a declaration that Britain would soon be the most athletic nation in the world since we intended to win the Olympic Games in 1976'.[14]

The programme reflected a combination of the need to be seen to be responding to current problems, including those implicated in the call for standards, and a desire to provide a reasonably comprehensive framework of guidance. The problem areas,

> were real hot topics, they weren't just concoctions. Basically, they came out of the major technical problems the big firms were encountering at the time . . . Technical partners . . . were just beginning to assume a position of power in the major firms. Before, the technical partners were just regarded as mechanics, but as life got more complicated all the firms realised that they needed to consult internally, first of all to make sure all the partners were in line . . . and secondly to make sure that they had got a logical framework . . . for the positions they were taking. Gradually the technical partners . . . would meet with each other. So there would be reported back [to the ICAEW Technical Committee] a list of hot topics.[15]

Thus, from a very early stage, the work of the ASSC was intimately linked with the technical activities of the big firms.

Putting the Machinery to Work: Drafts, Meetings and Staff

As we have seen,[16] the constitution of the ASSC made it clear that the ICAEW's existing technical committees would continue to undertake the initial development work on pronouncements, as they had with Recommendations on Accounting Principles,[17] and that its own staff were to be the 'engine room'[18] of standardization. Indeed, the designation of so many topics on the initial programme – 12 out of the total of 20 – as active work in progress so soon after the creation of the committee results from the way in which it was cantilevered over the Institute's existing technical committees and staff. Work on new pronouncements for the existing series of Recommendations was under way within the existing machinery and this simply carried on, now targeted at the issue of standards.[19]

In June 1969, the technical secretariat of the ICAEW had been reorganized as a Department of Technical Activities under a full-time director. The reorganization was designed to co-ordinate the work of the various technical staff and the increased effectiveness thereby obtained was to be sorely needed. The new Technical Director was Michael Renshall, who had formerly been Secretary to the Parliamentary and Law Committee.[20] In the initial period of the ASSC's operations it had the half-time services of one member of the ICAEW secretariat together with the 'part-time services of Michael Renshall, who had responsibility for the full range of technical services at the Institute'.[21] The annual report of the ICAEW for 1970 in fact shows Renshall as secretary of the ASSC,

the Parliamentary and Law, the Technical, the Technical Advisory, the Research, the Accountants Joint Parliamentary, and the Chartered Accountants Joint Standing Committees. The other member of the secretariat assigned to the ASSC is J. D. Winters.[22]

This very modest level of resourcing was supplemented, with varying degrees of effectiveness, by work contributed by the big firms. Professor Stephen Zeff describes how this came about:

> In June, 1970, at the [English and Welsh] Institute's initiative, representatives of seven large accountancy firms met . . . the Chairman and Vice-Chairman of the Research Committee and the Institute's Technical Director. In response to a question about their internal research activities, most of the firms stated that while they [did] very little research in the broader academic sense, they deal[t] with many practical, technical questions on an ad hoc basis. During the meeting, the firms were invited to collaborate with the Institute in the preparation of background studies for the eventual drafting of pronouncements. While most of the firms were not enthusiastic about the prospect of such an assignment, they agreed to take on five of the most challenging topics (fundamental principles of inventory valuation; accounting for research and development; fundamental objects and principles of periodic financial statements; accounting for goodwill; and fundamental principles, form and content of group accounts). A sixth subject, accounting for leases, was assigned to another accounting firm some months later. The pressing urgency of the entire accounting standards programme was emphasised, and the firms were asked to move as fast as practicable. Once the papers were completed, they would be forwarded to working parties [of the ICAEW Technical Committee] as a basis for developing accounting standards. By the end of 1971, three of the original five studies had been completed.[23]

At this distance in time, we can only speculate as to why the firms were unenthusiastic about providing support for the standard-setting process – and, indeed, as to the identity of the single firm that resisted the ICAEW's invitation to do so. It seems unlikely that they were reluctant to provide resources for the Institute, especially since the work of its technical committees – including work on drafting standards – was being carried on largely by members of the same firms and also in the form of non-chargeable hours. Expertise in the nascent technical departments described by Renshall would have been in limited supply and there may have been some concern that younger staff might not be able to perform at the required level or that a complex problem would absorb more non-chargeable hours than the firms could spare. However, the most plausible explanation is that the firms recognized that, though the creation of the ASSC had been widely welcomed by the financial establishment, the process of standardization and the content of specific standards were likely to prove controversial with companies, making firms reluctant to

risk being associated too closely with pronouncements that their clients might not welcome.

Leach described the ASSC's working procedures in the first period of its life thus:

> The basic preparation of exposure drafts was done by sub-committees of members of the Institutes not by any means restricted to members of the ASSC, but including those with special knowledge of the subject, aided and guided by discussion by the main committee on two or three occasions as the draft progressed.

After comments and criticism had been received following publication of the exposure draft, a small committee considered and assessed the submissions and the draft was then finalised by the main committee with such amendments as proved necessary. The amendments were seldom numerous.[24]

In practice the 'sub-committees' were not committees of the ASSC but of the various committees making up the 'technical arm' of the ICAEW, predominantly the Technical Committee, augmented by members from the associated bodies.[25] At the time the ASSC was created, the ICAEW had both a Technical Advisory Committee, given this name in 1964 because the former name, the Taxation and Research Committee, could lead to confusion with the newly-created Research Committee, and a Technical Committee. The Technical Advisory Committee liaised with District Societies, each of which had its own Technical Advisory Committee. The Technical Committee was created in 1965 because of the growing workload of the Parliamentary and Law Committee and its initial role was to liaise between the Technical Advisory Committee and the Council on technical matters. From 1967 onwards, the work of drafting technical documents, including accounting recommendations, shifted from sub-committees of the Technical Advisory Committee, which included substantial representation from District Societies, to sub-committees of the Technical Committee, although the Parliamentary and Law Committee and the Research Committee might also undertake this work from time to time: all three of these committees were more clearly dominated by Council influence than the Technical Advisory Committee. Below the level of Council, a simple majority vote would usually prevail, although a close vote would be noted and reported upwards.[26]

Early in 1970, the Technical Committee divided its membership into two groups, 'so as to deal more effectively with the increased work arising out of the Council's Statement of Intent'.[27] Consideration of drafts was delegated to the two groups, meeting monthly, with the Technical Committee itself meeting in plenary session every other month. The committee's Progress Report for the year ended 30 November 1970, reported that as well as ED1, it had submitted to the ASSC proposed exposure drafts on 'Disclosure of Accounting Bases' and 'Accounting Treatment of Acquisitions and Mergers in Holding Company and Consolidated Accounts'.[28] In his review of the ASSC's first year of operations, Kenneth Sharp described the committee structure as 'rather cumbersome'[29] and

suggested that, at a minimum, the sub-committees of the Technical Committee drafting documents could report direct to the ASSC rather than via the Technical Committee itself.

The First Pronouncement: Associated Companies

The ASSC's choice of topic for its first pronouncement, the treatment of income from investments in associated companies, reflected its desire to be seen to be responding to current problem areas in financial reporting.[30] Traditionally, companies had made no distinction between 'trade investments' (holdings of small amounts of the investee's securities with the primary purpose of receiving dividends and the benefit of capital growth) and larger, more strategically important investments, sometimes held as one party in a consortium. As a result, the investor's income from the latter ('associated companies') would, like that from trade investments, be recognized on the basis of dividend income received and profits on disposal of holdings. An associated company might be a highly successful strategic investment, obtained at substantial cost. However, if it was currently paying low dividends, perhaps retaining profits to fund further, potentially highly profitable growth, little income would be recognized in the investor's profit and loss account and users of its financial statements might fail to appreciate the success of the investment. More problematically still, a consortium of three or four companies, investing together in the same investee, could jointly control its dividend policy and thereby manipulate their own incomes. Losses of an associate would not be recognized in the investor's profit and loss account, at any rate until a write-down in the investment became necessary, and a loss-making associate electing to pay a dividend would raise the investor's profits. During the 1960s, groups were acquiring increasing numbers of associates,[31] exacerbating the practical consequences of these problems.

Recommendation on Accounting Principles N20,[32] issued in November 1958, had dealt with associated companies, using this term. Its recommendation was that, if material, aggregate investment in associates should be stated separately.[33] The pronouncement explains the difficulty of appreciating the position where an associate has substantial undistributed reserves accumulated since acquisition by the investor and comments that, 'some explanation may . . . be needed in these exceptional circumstances to enable the accounts to show a fair view'.[34]

However, by 1969, some large companies had gone beyond the provision of additional information to use, as Leach puts it, 'what has subsequently been described as "equity accounting"'.[35] Under this method, the investor accounts for its full proportionate share in the profits and losses of its associated companies, regardless of the level of dividend paid. The method was developed in the USA somewhat before it appeared in the UK.[36] In August 1959, the AICPA's Accounting Research Bulletin no. 51 'Consolidated Financial Statements', expressed a preference for the use of the method to account for non-consolidated subsidiaries, while conceding that cost was the more commonly used method at the time and without giving it a name.[37] In December 1966, the

Accounting Principles Board's Opinion No. 10, recommended the method for domestic non-consolidated subsidiaries indicating that 'this practice is sometimes referred to as the "equity" method'.[38]

The ICAEW's survey of published accounts for 1968–69 identified nine cases of equity accounting among the 300 companies surveyed, including the General Electric Company, Lead Industries and Richard Costain. The principal areas of difference among the nine were in the definition of an associated company, unsurprising given the absence of guidance, and the balance sheet treatment. In five cases, post-acquisition profits retained by the associate were added to the investor's retained profits or revenue balances and to the carrying amount of the investment. In another, the profits were transferred to capital reserves, presumably to indicate that they were not available for distribution by the investor. In the remaining three cases, the profit retained by associates for the period was deducted from the investor's profit after tax, effectively reversing the inclusion of the undistributed element of profit in the pre-tax line, with the carrying amount in the balance sheet remaining at cost.[39]

According to Leach, 'some surprise was created by the first subject chosen being a highly controversial one . . . which opened up entirely new ground'.[40] It was in fact, politically, an astute choice, demonstrating that the ASSC was prepared to tackle 'hot topics'; indeed, there must have been some pressure to tackle one of the main areas apparently implicated in the scandals bringing about the establishment of the standard-setting machinery in the first place, and it was shortly to become apparent that the financial establishment was not content even with the speed at which the ASSC was moving.[41] The subject opened up new ground in that equity accounting was not yet widely used, so that a standard requiring it would be imposing a new method rather than adjudicating between two or more well-supported methods, each with its own advocates. While it might have turned out that preparers had previously considered using equity accounting and rejected it, in which case the ASSC would have found itself facing considerable opposition at the very beginning of its life, it must have seemed more likely that many companies were simply following the traditional method because they had not considered an alternative, so that they would not necessarily be inclined to resist the new approach. The technical character of equity accounting itself – for a profitable associate with a less than 100% pay-out ratio, the method increases rather than decreases the bottom line – must have made it seem likely to be reasonably popular. The technically straightforward nature of equity accounting was seen as another attraction of making it the first topic.[42] Although defining what should count as an associate was – and remains – a challenging problem, the only other area in which there was a diversity of practice among the users of equity accounting covered in the ICAEW survey of published accounts was the treatment of associates' retained profits in the balance sheet and here one of the two methods used is inconsistent with the treatment in the profit and loss account, so the choice seems reasonably straightforward. There was thus little scope for the debate to become bogged down in points of detail.

Another attraction of the topic was that it was already in the ICAEW's 'drafting pipeline', that is its technical committees and secretariat.[43] Work had begun in mid-1969[44] and a draft document was already at an advanced state.[45] The ASSC first considered a draft in March 1970 – the committee's third meeting – and was able to agree an exposure draft for publication three months later.[46] Leach's characterization of this as an 'amazingly short period'[47] somewhat underplays the amount of technical work undertaken before the subject reached the ASSC agenda, but is, overall, fair, given that the committee was itself feeling its way forward both technically and procedurally.

The ASSC's first proposed statement of standard accounting practice, 'Accounting for the Results of Associated Companies', was published on 26 June 1970, having been approved at a meeting of the committee held on 1 June.[48] In keeping with the committee's constitution, the document had not been considered by the ICAEW Council, or even, apparently, circulated to its members prior to publication. The Council meeting of 1 July 1970, received a report that the document had been published, and copies of the published version were circulated to members of Council, who were told that, 'it was hoped that members of the Council would express any comments they felt appropriate to the Technical Director'.[49]

Although the document was headed 'Exposure Draft', and described in the text as 'the first exposure draft issued for comment by the Accounting Standards Steering Committee',[50] neither on the document itself nor in the versions appearing in the press was it given a number. The printed version was on A4 stock and, with the exception of the front cover, reproduced text from typescript, giving the document an appropriately transitory air. The first page carried a letter from Leach,[51] addressed to 'persons concerned with financial reporting', explaining the role of the ASSC, the status of the draft, and the intention to move to requiring disclosure of departures from definitive standards. Responses were required by 25 August 1970, and it was emphasized that, 'it [would] be helpful to receive assenting . . . as well as dissenting views'. It was also explained that comments would be placed on the public record unless confidentiality was requested, beginning a practice which continued throughout the committee's life.

The structure of the document followed the prescribed format described in chapter 2.[52] It ran to 28 paragraphs plus two appendices giving examples of the layout of the profit and loss account. The explanatory note justified equity accounting (without using the term) as an extension of consolidation accounting to respond to the increasing trend towards strategic investment short of control. The extension was needed because of 'the importance which investors have come to attach to earnings (as distinct from dividends) and to the price/earnings ratio'.[53]

Part 2 of the draft – the definition section – contained only a single definition, of an associated company. Establishing this definition, and thus the investments to be accounted for by the equity method, had proved to be the principal problem in developing the document.[54] The definition reads as follows:

> A company is an associated company of the investing group or company if:
>
> (a) the investing group or company's interest in the associated company is essentially that of a partner in a joint venture; or,
> (b) the investing group or company's interest in the associated company is substantial (i.e. not less than approximately 20% of the equity voting rights) and, having regard to the disposition of the other shareholdings, the investing group or company is in a position to exercise a significant influence over it.
>
> In both cases it is essential that the investment should be for the long term and that the investing group or company participates (usually through representation on the board) in commercial and financial policy decisions including the distribution of profits.[55]

The core of the definition illustrates a fundamental dilemma that the ASSC (and other standard-setters) were to encounter time and time again: should the distinctions required to apply definitions and determine whether a particular transaction or event should be accounted for in one way or another be expressed in subjective or objective terms? In this context, objective tests are those set out in terms of quantified, independently verifiable, parameters, such as the percentage of equity voting rights referred to in the definition of an associated company. The advantages of objective tests – these days sometimes called 'bright line solutions' – are that it is easy to apply them, easy to audit the result, and easy to demonstrate to a third party – perhaps a court of law – that they have been applied correctly. The disadvantages are that, when they are applied in even slightly unusual contexts or in contexts not envisaged by their architects, they can produce outcomes that are of dubious validity; and that they encourage preparers to manipulate the underlying transactions and events to achieve the desired accounting method. ED1's definition is principally subjective – judgement is required to identify significant influence, whether a holding is for the long term, the level of participation, and so on – but it incorporates something approaching an objective test of a substantial holding, albeit that an element of subjectivity is introduced by way of the range of approximation surrounding the 20% test.

The proposed standard itself occupied 19 paragraphs and set out the equity accounting method in some detail. The balance sheet treatment to be used is recognition on the basis of attributable net assets adjusted for the investor's goodwill on acquisition.

Some 2,700 copies of the exposure draft were distributed[56] and the professional press' practice of publishing full versions, which has survived to the present day, began with this first document: it was printed in *The Accountant*,[57] *Accountancy*,[58] and *The Accountant's Magazine*.[59] The reception by the professional press was fairly low-key: *Accountancy*'s contents page described the document as 'a good start';[60] *The Accountant's Magazine* drew attention to the draft by a paragraph in its 'Notes

and Comments' section which gave details of three meetings arranged by local committees of the ICAS (one in London), designed to give members an opportunity to discuss the document;[61] *The Accountant* featured the draft in its lead editorial, describing its contents and background but offering only a limited degree of appraisal.[62] The financial press generally gave the draft substantial coverage; articles appeared, for example, in the *Financial Times*, *The Times*, *Investors Chronicle* and the *Sunday Times*.[63] It seems likely that this level of coverage was attributable at least as much to the novelty of the process as to the content of the particular draft.

The two-month exposure period fell at the height of summer; though the ASSC was keen to encourage submissions,[64] it presumably settled for this timetable to reflect the speed with which it wished to be seen to be taking action. Shortly after the exposure period ended, *The Accountant* published a compilation of views from a practitioner, a stock-broker, an institutional investor and an academic.[65] The practitioner rehearsed some practical problems with the proposal while the others broadly welcomed it; interestingly, no view from a preparer was sought.

Within the profession, there was a reasonably high level of interest. The first of the three discussion meetings organized by local societies of the ICAS took place in Edinburgh and the attendance, 'nearly 40'[66] was regarded by *The Accountant's Magazine* as indicating substantial interest. A large number of responses were received by the ASSC, 152 in all, with 51 coming from companies, 22 from practising firms, 26 from representative bodies (including accounting bodies), seven from academics and 46 from other individuals. The committee was not to know it, but this was actually the second-highest level of comment they would ever receive on drafts other than those relating to price-level accounting, and only one below the highest level.[67]

The submissions amounted in all to about 400 pages of material,[68] which were,

> ably reduced by the Secretariat to [a summary of] about 55 pages, but even then it was necessary for many of the comments, particularly those from persons who were opposed in principle to the proposals, to be reproduced in full and circulated to the Committee.[69]

As a consequence, the agenda for the October meeting of the ASSC ran to over 100 pages,[70] a harbinger of things to come. The submissions were 'predominantly favourable'.[71] There were, however, some trenchant criticisms of equity accounting from significant preparers. Following its consideration of the submissions, the ASSC made a number of minor revisions and, at its meeting on 2 December, unanimously agreed a text to be recommended to the English and Welsh, Scottish and Irish Councils.[72]

The area in which most changes were made was the definition of an associated company. This had been one of the most criticized features of the exposure draft (leaving aside the introduction of equity accounting itself), but the approach in the proposed standard remained the same. As Leach put it, 'we

could not better our original definition'.[73] There was, however, a good deal of tidying up: subsidiaries were explicitly excluded from its scope; the word 'essentially' in the section of the definition dealing with joint ventures was replaced by 'effectively', making it clearer that the intention was to test for substance; the qualification to the cut-off test for substantial interest – *approximately* 20%, rather than 20% – was dropped; and the two paragraphs in the draft were merged into one, making it clearer that participation was part of the definition rather than a gloss on 'significant influence'. The requirement that investment should be for the long term was moved into the section dealing with non-joint venture associates, so that even short-term joint ventures were caught. Finally, consortia were explicitly included with joint ventures in the first section of the definition. None of the changes made to ED1 were major, a tribute to the skills of those involved in the production of this 'first of its type' and something that became less common as the life of the ASSC continued.

The proposed standard was submitted to the ICAEW Council on 6 January 1971. The Council,

> resolved, on the unanimous recommendation of the Accounting Standards Steering Committee, that, subject to amendments in the light of discussion at this meeting, Statement of Standard Accounting Practice No. 1, 'Accounting for the Results of Associated Companies', be approved for publication.[74]

At the same meeting, the Explanatory Foreword was approved[75] and it was agreed that both documents would be released for publication in the press at the earliest opportunity, with each Institute free to publish and distribute copies as it wished. It was noted that the ICAEW would be including the Statement in the Members Handbook – SSAPs became Section M. The Council also approved in principle an Auditing Statement on 'The Effect of Statements of Standard Accounting Practice on Auditors' Reports'.[76]

It is possible to trace a number of minor changes between the version of the proposed standard recommended to the institute Councils and the published document. Although some may have been last minute amendments suggested by the ASSC itself, some presumably resulted from Council debate. Most are purely stylistic and extend to inserting or moving commas, even where the original version is not grammatically incorrect. One change was substantive, albeit minor: a sub-paragraph was added addressing the balance sheet treatment where the investor has no subsidiaries.[77]

The architects of the ASSC and SSAP1 must have breathed a sigh of relief as their first pronouncement reached the equivalent of the statute book only a few days over a year after the ICAEW announced its intention to 'advance accounting standards', having been successfully steered through public consultation and the institute Councils. The willingness of Council members to meddle in the detail, though without significant consequence on this occasion, may, however, have given them some concern.

As with the exposure draft that preceded it, SSAP1 was widely published in the professional press, again establishing a precedent followed throughout the committee's life. The standard appeared in *Accountancy* in February 1971 and as a loose-leaf insert in *The Accountant's Magazine* in the same month. *Accountancy* outlined the content of the standard in an article describing the progress of the ASSC under the headline, 'Accounting standards go forward'[78] (difficult to see what other direction they could have gone in at that stage), but did not offer any editorial comment. The text of the standard was reproduced (together with the Explanatory Foreword) under the headline, 'Accounting standards – A new era'.[79] Neither the article nor the text of the standard referred to the document as SSAP1 – rather it was described as 'the first Statement of Standard Accounting Practice'.[80]

Soon after the publication of SSAP1, the committee encountered an uncomfortable feature of life in the standard-setting arena which was to become only too regular: critical comment in the press, including intemperate language, continuing after the publication of a final document. On 1 March, ICI's Finance Director, Albert Frost, and Chief Accountant, Bertram Ogle, addressed a press conference called to unveil the company's financial statements for a period actually falling before the implementation date for SSAP1. Nonetheless they chose to make some remarks on the standard. Frost offered his 'personal view' that the standard was, 'liable to mislead stockholders rather than clarify the results of any company for them'.[81] Ogle explained that the company considered that many small shareholders relied on a calculation of dividend cover and that the inclusion of associate's retained earnings in the group's results would be likely to lead them to think they were available to pay a dividend: 'ICI feels quite strongly that it is more important to avoid misleading this sort of shareholder than it is to try to satisfy the more sophisticated shareholder'.[82] No decision had yet been made as to whether ICI would follow SSAP1. Ogle also pointed to technical problems, such as the difficulty of obtaining coterminous accounts under certain circumstances. Two themes here that would run through the life of the ASSC: dispute about whether standards should be designed for sophisticated users or avoid anything that could confuse 'widows and orphans'; and arguments about technical problems mounted by those who also happen to object to the required treatment in principle.

In the following month's edition, *Accountancy* carried a report under the headline, 'Accounting standards – Cunard's chairman lashes out'.[83] The subject was, again, associates: Cunard had voluntarily implemented SSAP1 and thus brought into its profit and loss account the *losses* incurred by a number of associates at the development stage of marketing container-ship capacity, with the consequence that its loss before taxation increased from £285,000 to £2 million. At the company AGM, the chairman, Sir Basil Smallpiece, 'put a brave face on things', referring darkly to accounting methods that, 'seem to have been used by others [in the industry]' which would have reduced the group's losses to the smaller figure.[84] He then apparently, 'lashed out':[85] 'Methods of accounting that produce such widely different figures as that cannot both be right – and the

unwitting stockholder is left to guess which gives the true and fair view.'[86] So then, Smallpiece supported the standardization project generally and SSAP1, the latter with such enthusiasm that he implemented it early. He in fact lashed out at his competitors' non-compliance, or strictly, failure voluntarily to comply early. At the ASSC, they must have hoped that *Accountancy*'s readers got past the headline.

In the weekly accountancy press, if finance directors do not 'lash out', they generally 'slam', and in February 1972, SSAP1 was, indeed, 'slammed'. According to *Accountancy Age*, 'another top British company [had] joined ICI in defying the ASSC's statement on associated companies': 'P&O's Finance Director, John Mitchell, slammed the ASSC's standard practice ... "I do not consider this is good accounting ... "'.[87] As the article pointed out, the accounts in which P&O were defying SSAP1, like those that were the subject of ICI's press conference, were for a period in which the standard had not yet come into force.

In fact ICI, whose financial year coincided with the calendar year, making them one of the first preparers to whom SSAP1 applied, fell in with the new standard in the first year in which compliance was required. The effect was to raise their earnings and some commentators felt they had observed the market failing to appreciate the impact of a change in accounting policy:

> The stock-market was caught nodding when the ICI preliminary results for 1971 first came over the tapes. Brokers and jobbers failed to take in the message that the profits were 'cum associated companies' and they misinterpreted the apparent jump in earnings as a sign of improved profitability, rather than the true situation of an actual decline.[88]

A review of the situation in June 1972 concluded that, 'a large majority of companies has adopted [the] proposals',[89] and in the annual survey of published accounts covering year-ends to 30 June 1974[90] (the second survey in which the standard applied to all companies), there were only three references to departures from SSAP1 in auditors' reports and in two of these cases the auditors concurred with the departure.

Although US standard-setters developed, and, notwithstanding Leach's comment, named, the equity method ahead of the British, at the time SSAP1 was being worked on no US pronouncement addressed accounting for associates. The pronouncement which did so, APB Opinion No. 18, was published in March 1971,[91] within two months of SSAP1. It extended the use of equity accounting to joint ventures and to other investees over which significant influence was exercised, though no name was given to such investments.[92] A number of similarities of approach can be identified, and, indeed, there are common or near-common phrases, including, 'significant influence' (both), 'representation on the board' (both), and 'participates ... in ... policy decisions' (UK) *versus* 'participation in policy making processes' (US).[93] The US pronouncement also adopted a 20% cut-off point although, anticipating a later revision to the UK

document, this is in the form of a rebuttable presumption.[94] The definitions are very similar.[95] According to a spokesman for the ICAEW, the AICPA, ‘acknowledged the great assistance which they received from a study of [ED1] in the preparation of their own paper’.[96] The year 1971 also saw the issue of Australia’s first exposure draft on accounting for associated companies, though this opted for an objective test for defining associates, eliminating the need to exercise judgement.[97] As an editorial in *Accountancy Age* put it, ‘the ASSC may well argue that the problem is not resolved by avoiding it’.[98] The International Accounting Standards Committee’s standard, IAS3 ‘Consolidated Financial Statements’, issued in 1976, followed the UK’s approach.[99] All in all, then, Leach, reflecting in 1981 on the ASSC’s first ten years, had some right to claim that,

> SSAP1 has proved workable and generally acceptable for ten years. More than that it has been the basis on which the international standard and comparable standards in overseas countries were founded.[100]

Disclosure of Accounting Policies

Wednesday, 20 January 1971, was a busy day at the ASSC. As well as the publication of the Explanatory Foreword[101] and the first accounting standard, it also saw the appearance of two exposure drafts, ED2 ‘Disclosure of Accounting Policies’, and ED3 ‘Accounting for Acquisitions and Mergers’. ED2 (which, unlike its predecessor, was given its number from the beginning of its life) actually covered two separate topics, one of which, the delineation of certain ‘fundamental accounting concepts’,[102] was ignored in its title; this aspect is discussed in chapter 5. The topic on which attention, and, indeed, the title, focused responded to the second line of action announced by the Statement of Intent’s programme to advance accounting standards, disclosure of accounting bases.[103]

The initial drafting work on ED2 was undertaken by Renshall, working largely alone – the small scale of the Technical Directorate in the early years of the ASSC has already been described[104] – with some input from Leach and other ASSC members, although this probably related more to the section on fundamental accounting concepts discussed later.[105] A pre-exposure version of the draft was circulated to six large companies for comment. The responses were mixed. British Petroleum drew attention to the difficulty of disclosing depreciation rates and methods in a large group in which choices were made locally and pointed out that the US Securities and Exchange Commission (SEC) did not require this, implying that the UK should not be seeking to leap-frog US requirements.[106] International Computers Limited wrote rather loftily that they were ‘not very impressed by the document, as it has tried to be all things to all men, and failed’.[107] Their letter raised fundamental questions about who standards were designed to help, the implication being that extensive disclosure of technical detail would confuse the lay user.

Despite these concerns, the ASSC continued with its drafting. A distinction was now introduced between bases generally and the particular bases employed by a given preparer, which were given the title, 'accounting policies'. The exposure draft again carried an introductory letter from Leach; though this was substantially shorter than that accompanying SSAP1 it continued to seek, 'assenting ... as well as dissenting views'.[108] The draft began by explaining that in the statement, 'distinction is made between *fundamental accounting concepts*, *accounting bases* and *accounting policies*'.[109] The structure adopted for accounting standards – explanatory note, then definitions of terms, then standard accounting practice – was already beginning to make for some difficulties of exposition: since the terms at the core of the document were all relatively novel its writers found themselves having to explain them – in a way that comes close to a definition – and then almost immediately repeat this material actually in the definition section.

Some 5,000 copies of the exposure draft were issued, up from the 2,700 copies of ED1.[110] Despite the objections raised by companies participating in the trial, the draft was 'largely non-controversial'.[111] Only 69 submissions were received, about half the number of responses to the first exposure draft, but, significantly, the number from companies was only 16, about a third of the number making a submission on ED1. The draft's emphasis on disclosures being, 'as brief as possible consistent with [its] objects' of clarity and fairness[112] may have gone some way to allay the concerns of companies like British Petroleum. Other factors may have included a postal strike which more or less coincided with the exposure period[113] and the publication on the same day of the more controversial third exposure draft.

A revised version of the draft was prepared and approved by the ASSC on 14 July 1971.[114] Though there were a number of stylistic changes, there were few alterations of any significance. The most important change was the abandonment of the requirement to disclose departures from accounting standards, which was thus left only in the Explanatory Foreword. The ED had included in a list of 'examples of matters which give rise to particular difficulty' in applying judgement about future events, 'the future benefits to be derived from fixed assets, the period of years over which these will be fruitful and the extent to which each year in that period will benefit,'[115] but in the proposed standard the last of these matters has been dropped. Had someone read Arthur Thomas's devastating critique of the theory of depreciation, published in 1969, which demonstrates that the choice of depreciation *method* is incorrigibly arbitrary and not a matter of judgement about future events?[116]

According to the definition section of SSAP2,

> Accounting policies are the specific accounting bases selected and consistently followed by a business enterprise as being, in the opinion of the management, appropriate to its circumstances and best suited to present fairly its results and financial position.[117]

The phrase 'present fairly its results and financial position' is not employed in the explanation of the term, which refers merely to policies being, 'most appropriate to [the] circumstances',[118] and, although it is used elsewhere in the explanatory section,[119] it is not glossed. The phrase must have been unfamiliar to many UK accountants (it was one of the US audit opinion criteria[120]) and its relationship to the familiar true and fair view is not obvious. The definition takes it for granted that the selection has been made according to identified criteria. While such an assumption may be partially justified by the requirements of the Companies Act then in force, there is a substantial gap between the legislation and the words used in the standard – not least the difference between fair presentation and the true and fair view. The consequence is that SSAP2 is, strictly speaking, a standard *solely* about disclosure of policies with no requirements about the selection of those policies. While this may well have helped in making the exposure draft largely uncontroversial it did miss an opportunity for a useful improvement in regulation.[121]

The proposed statement had to go as a recommendation jointly to the Councils of the ICAEW and the two associate members and was considered in meetings through September and October. Because its publication had to await approval at meetings of all three Councils, it was not published until November 1971, four months after the ASSC approved it, and it became the first case of implementation slippage, the target of 1 January 1971 in ED2 becoming 1 January 1972.[122] The involvement of three Councils yielded a rather convoluted entry for the ICAEW's minute book, pregnant with danger for future documents:

> It was resolved that Statement of Standard Accounting Practice No. 2 'Disclosure of Accounting Policies' be approved for publication, subject to certain amendments made at this meeting, to certain amendments proposed by the Scottish Institute and to any amendments which might be proposed by the Irish Institute.[123]

A close comparison of the version proposed by the ASSC[124] and that published suggests that the combined might of the Councils of the English and Welsh, Scottish and Irish Institutes made just three changes:

(a) A further case (warranties for products or services) was added to the list of examples of areas in which an accounting policy might be needed.
(b) Bracketed words pointing out that the relative importance of each of the four fundamental concepts would vary 'according to the circumstances of the particular case',[125] were added.
(c) At one point, the word 'directors' was changed to 'management',[126] reflecting the Explanatory Foreword's position that standards apply to 'all financial accounts intended to give a true and fair view of financial position and profit or loss'.[127]

An optimist would conclude that the brevity of this list demonstrates that the Councils appreciated that, if the standard-setting process was to function effectively, their role needed to be to accept (or reject), but not tinker with, the ASSC's recommendations. A pessimist might note that the very triviality of the changes suggests a willingness to tinker, even though there may not have been much dispute about the fundamentals in this particular case.

As with their first standard, the ASSC beat the USA in adopting a pronouncement on disclosure of accounting policies. A similar proposal had been discussed in the USA as long ago as 1932, but the Americans were only at the stage of working on a draft for exposure at the time SSAP2 was published.[128] The final document was adopted in April 1972,[129] although the APB had actually issued a pronouncement on *changes* in accounting policy somewhat earlier; in July 1971. This document did not use the term 'policy' (which was defined in the April 1972 Opinion), referring instead to 'principle'. Both jurisdictions made the same move in parallel, retaining the traditional term for the class of methods (in the US, principles, and in the UK, bases) but introducing the term accounting policy for the particular method chosen by an individual preparer.

The ICAEW survey of published accounts for 1973/74, the first year in which the standard was mandatory for all companies, recorded that, 'it [was] now very general practice ... for companies to present information on their principal accounting policies in a single summarised statement, though this ... is not specified in SSAP2 as standard'.[130] In that year, 87% of the companies surveyed provided such a statement and the remainder may well, of course, have given individual policies within the relevant note. Indeed, for those companies in the previous year's survey for which SSAP2 was mandatory (just over half), 88% had disclosed their depreciation policy and 94% their policy on deferred taxation. Further, in that year, among those companies for which SSAP2 was not mandatory, 64% had disclosed their policy on stock and 79% that on deferred taxation. Sharp's commentary on the ASSC's early years concluded that the early adoption of SSAP2 'illustrates [its] broad acceptability to industry'.[131] However, he goes on to suggest that there was 'some cause for concern that the phraseology being used in some cases is insufficiently specific'.[132] Disclosures in 1973/74 confirm that his concern was justified. Of the 266 companies disclosing a depreciation policy, only 106 gave rates for plant, though surely almost all must have had this category of fixed asset,[133] and among these, 'a range of rates was sometimes quoted'.[134] Again, of the 298 companies in the survey with material stocks, 93 (31%) gave no information about the treatment of overheads.[135] At least one only reported that its stock was stated, 'on bases and by methods of computation considered appropriate in the circumstances', down from 14 using this 'or similar wording' in 1968/69.[136] An academic survey of published accounting policies in the mid-1970s concluded that, 'from the point of view of users of accounts the extent of disclosure of accounting policies is unsatisfactory in a number of respects'.[137] Causes included, 'the non-specificity of SSAP2 in general [and] the reluctance of some

companies to disclose more than the minimum that can be construed as compliance with the standard.[138] The authors went on to say:

> The evidence ... suggests that in many cases the more critical aspect of an accounting policy is not disclosed ... In most cases there is no way of verifying whether non-disclosure of accounting policies is acceptable under SSAP2 in not being 'material or critical' other than relying on the auditor's opinion. A number of cases where the information included in the statements of accounting policy appeared to be inaccurate or misleading led us to question the value of some auditor's reports in this respect.[139]

The initial five-year work programme adopted by the ASSC listed changes in accounting bases (the term 'policies' not at that stage having been adopted) as a separate topic from the disclosure of accounting bases. A document was planned for 1971–72 but at the date of publication of the programme no work had been undertaken. By early 1971, it had been decided to include the topic with the treatment of extraordinary and prior year items.[140] Later that year the committee reverted to the original proposal and the exposure draft on extraordinary items issued in August 1971 announced that, 'the treatment of changes in accounting policies will be dealt with *in detail* in a separate Statement of Standard Accounting Practice'.[141] In September 1971 the ICAEW Technical Committee noted the exclusion and agreed that a separate standard would have to be produced as a matter of urgency.[142] The required sub-committee was established in November 1971, and in due course a draft ED was prepared. The Technical Committee, however, subsequently recommended that the topic should once again be combined with extraordinary items.[143] Although the revised version of the extraordinary items ED, issued in July 1972, still failed to address changes in accounting policy, the note explaining the ASSC's intention to issue a separate standard on the topic was dropped.[144] The SSAP on extraordinary items, SSAP6, issued in April 1974, did deal with changes in accounting policies but contained only a single, albeit lengthy, paragraph,[145] and one other reference,[146] in the explanatory note. As far as the standard proper is concerned, the extent of the treatment of changes in accounting policies is that they are defined as prior year adjustments[147] and, as such, required to be accounted for by restatement of prior years and disclosed.[148] The explanatory note states that, 'a change in accounting policy should ... not be made unless it can be justified on the ground that the new policy is preferable to the one it replaces because it will give a fairer presentation of the results and of the financial position of the business'.[149] This apparent rule is not established by the standard in which it is mentioned, since it appears only in the explanatory note, but, it is argued, derives from the fundamental accounting concept of consistency. The US pronouncement addressing changes in accounting principle, issued in July 1971, draws the line at requiring that the new basis be justified by the entity as 'preferable',[150] without indicating how this is to be established (though, as the ASSC were to do, it does explain that the adoption of a new standard always

justifies a required policy as being preferable). Poor regulation of changes in accounting policies was to form a regular feature of critical columns in the weekly accountancy press.[151]

There was a certain amount of agonizing over whether the nature of the material in SSAP2 meant that it ought to have carried the number '1' – Leach, for example, in reflecting on the ASSC's first ten years, goes out of his way to respond to the point that, 'this was a fundamental paper and should logically have been the first standard to be issued', justifying its actual number by referring back to the reasoning behind the decision to make the committee's 'debut with the controversial standard on associated companies'.[152] However, the IASC did ensure that its equivalent standard came first[153] and in 1979, when SSAP1 was being reviewed,[154] Christopher Morgan, then the ICAEW's Director of Accounting Standards, pursued the possibility of giving the revised standard on associated companies a new number at the end of the sequence, freeing up number '1', which could be reallocated to SSAP2:

> I thought, here's a chance to patch [the logic of the sequence] up a bit so I asked if the subject could be raised but they weren't interested and Tom [Watts, then chairman of the committee] said to me, 'they love their numbers'. It was all history: the people who had been there for SSAP1 didn't want [the number] changed.[155]

Mergers

So far, so good. But the first wobble was not long in coming. In tandem with ED2, the ASSC published ED3, which had the title 'Accounting for Acquisitions and Mergers' but was effectively aimed solely at establishing a new basis of accounting for mergers. Traditionally, all business combinations had been regarded as the acquisition by one entity of another, the owners of the first now owning both. However, in a merger, it is argued, one company does not take over another; rather two businesses pool their resources and operations and, crucially, the previously separate groups of owners now come together jointly to own the enlarged business. For this latter condition to be achieved it seems essential that the combination comes about largely by an exchange of shares rather than for cash. Under these circumstances certain features of acquisition accounting, including the recognition of goodwill, the revaluation of the assets of the entity treated as the acquiree, and the 'freezing' of its distributable reserves, can be argued to be inappropriate.

Since the 1950s, it had been common in the USA for such combinations to be accounted for by a method, known in the UK as merger accounting, which avoided these features.[156] The shares exchanged were accounted for at their nominal, rather than market, values, so that no share premium had to be recognized, both entities' assets remained at historical cost, no goodwill was recognized, and the profit and loss account in the period of the combination

included the whole of the results of both entities regardless of when in the period the combination actually occurred. In the UK, merger accounting remained rare (the ICAEW survey of published accounts for 1969/70 found only six instances[157]) but was employed in a number of high profile cases, including the brewery amalgamation of Bass and Charrington.[158] Other companies employing the method included British Leyland, ICL, Schweppes and Tarmac.[159]

Almost every aspect of merger accounting was, by this time, already highly controversial in the USA (where it is known as 'pooling of interests'). Whether true mergers of genuine equals ever occur was a matter of argument. One commentator at the time, Ray Hinton, put it like this: 'the merger method for amalgamations is based on the concept of continuity of ownership, which on examination is denied by the facts of any amalgamation of independent parties'.[160] In the USA, the method was effectively available as a matter of choice for virtually any combination.[161] Merger accounting can be abused by the dominant partner in an acquisition accounted for as a merger in a variety of ways. Avoiding the need to recognize (and therefore amortize or write off) goodwill is an attraction in itself. The assets of the subordinate entity, recognized at depreciated historical cost, can then be sold at market values, which in some cases (property, patents, media rights, licenses and so on) may exceed the carrying amount by a spectacularly large amount, giving the appearance that the managers of the dominant entity have revitalized their new partner's operations. Finally, because a full period's profit from the subordinate partner is recognized in the group's profit and loss account even if the agreement is arrived at very late in the period, there is ample scope for income management. By the late 1960s, these abuses were being mercilessly excoriated by 'the Ralph Nader of the accounting profession',[162] Professor Abraham Briloff, who coined the term, 'dirty pooling'[163] and wrote memorably about 'the APB and the "P" in the Pool'.[164] Other commentators nearer to the heart of the accounting establishment were also strongly critical of the abuses of merger accounting[165] and the UK press carried reports that the APB's difficulties in controlling abuses were raising doubts about its future.[166]

ED3 sought to meet the objections to merger accounting by providing a number of safeguards. First, there was a lengthy definition of a merger, which attempted to go to the economic substance of a genuine 'pooling of interests',[167] and the exposure draft insisted that merger and acquisition accounting were two alternative bases, each to be used for combinations satisfying the relevant definition, and not choices available for managers to apply as they wished. The definition attracted some criticism, both because it relied on objective, and thus inevitably arbitrary, cut-offs and on more technical grounds.[168] Other safeguards included a requirement that the comparative figures for the period immediately preceding the combination be restated as if it had taken place before the beginning of that period, and disclosure of the extent to which the results of the period included results of the new arrival prior to the date of the combination (somewhat reducing the impact of consolidating a full period's results in the period of

combination), together with a series of disclosures concerning the terms of the combination.[169] However, given the uncertain effectiveness of the enforcement mechanisms in the UK at the time, there remained concern that a standard would raise the credibility of the method itself while, as in the USA, the limits on its use would be eroded in practice.[170]

Though the method was controversial in the USA, it was, at least, lawful. In the UK the legality of merger accounting was a matter of doubt because company law required that, where shares were issued for consideration exceeding their nominal value, whether or not cash was involved, the premium should be recognized and capitalized. It also required that pre-acquisition profits be treated as non-distributable.[171] The exposure draft contained a note to the effect that 'there is legal opinion to support the propriety in law of the practice of recording in the books of a holding company, at the nominal value of the shares issued, shares received by the holding company in exchange for shares issued',[172] but gave no further details. One, in general not unfriendly, commentator described the assertion as 'not wholly convincing'.[173] *Accountancy*'s rather sarcastic comment was that, 'there is no doubt that certain leading counsel will proffer this advice'.[174] It had, indeed, carried articles supporting the position itself.[175] The general view, however, was that the legality of the method was, to say the least, 'not entirely clear'.[176]

But it was not only the legality of the method that was questioned. *The Accountant* invited three 'well-known commentators to express their respective views' in its issue of 8 April 1971.[177] Alan Hardcastle, a practitioner, concluded that, 'it is somewhat disappointing that the ... exposure draft appears to condone the present piecemeal and sometimes illogical approach';[178] Harry Norris, a company director, argued that 'the draft [was] attempting a differentiation which seems to have no validity';[179] and R. S. Allen, an analyst, 'would have preferred ... further restrictions on the scope for mergers'.[180] Apparently no one could be found who supported the draft – the previous issue also contained an article attacking it.[181] Others with strong feelings organized 'a one-day seminar and open forum ... to express the case against the ... exposure draft.[182] The *Accountant* presciently opined that, 'there appears little likelihood of a final decision on ED3 with any element of precipitate haste', attributing this to 'the importance of the subject matter' together with, 'the practical burdens of dealing with two drafts at the same time and the aftermath of [a] postal strike'.[183] The latter two factors seem unlikely to have contributed very much to the (eventual) delay of 14 years. Some 5,000 copies of the ED were distributed, the same as for ED2, and 88 submissions were received.

Given the general level of controversy surrounding merger accounting (the chairman of the ASSC regarded it as 'one of the most controversial subjects which could be chosen'[184]) and the uncertainty regarding its legality, why did the ASSC decide to embark on this topic so early in its life? Leach attributes the ASSC's choice, with some considerable insouciance, to 'its unlimited enthusiasm'.[185] Douglas Morpeth, the vice-chairman at the time, does not see it in quite this way: 'It was getting to the stage where we had to do something about

it.'[186] At the time Renshall personally suspected that merger accounting would prove 'problematic'[187] and also suspected that everybody else involved privately held much the same view. There was, though, a strong sense that something had to be done:

> The background to the dispute about merger accounting was this. Some time in the middle 1950s there was a huge public dispute between two major firms, Coopers and Turquand, Youngs. A major property company [City of London Real Property] wanted to adopt merger accounting. Turquand, Youngs, their auditors, said 'no'. Coopers were approached and agreed to accept it. [The ICAEW] Council issued a very strong statement about the circumstances in which it was acceptable for a firm to offer to adopt a treatment another firm had rejected: Council made a public statement virtually chiding one of its prominent members for offering to be flexible [over] accounting practices.
>
> [By the 1960s] Finance directors were beginning to emerge [as a force in business and some wanted to use merger accounting] . . . [They were] shouting and screaming because [accounting methods] had commercial consequences. ED3 was issued knowing that it would generate controversy. [It was] issued because there was the demand. Major firms wanted some orderly way of dealing with [the problem] but there wasn't consensus. We hoped it would 'go' but privately I didn't have much doubt [that it wouldn't]. Banning merger accounting wouldn't have run either.[188]

For the first, but not the last, time, the ASSC found itself in the grip of opposing, irreconcilable but irresistible forces. In October 1971, *Accountancy Age* carried a front-page story revealing that ED3 was to be withdrawn and a new draft issued later in the year. The draft would argue that the distinction between mergers and acquisitions was artificial and unacceptable in the UK.[189] Although the story did not say so in so many words, it was interpreted as indicating that the new draft would be 'likely [to] eschew the "merger" concept altogether'.[190] Sharp's March 1972 update on developments at the ASSC, while conceding that ED3 was, 'causing the Steering Committee some concern', reported that 'a basic decision has been made to proceed with the preparation of a standard acknowledging the distinction between acquisitions and mergers'.[191]

After a further eighteen months, *Accountancy* carried a story on ED3 under the headline, 'Sunk without trace?'[192] It asked Renshall, 'if there was any sense of embarrassment on the part of the ASSC that ED3 had lain on the table for so long, and whether ASSC felt it had egg on its face – that it had failed'.[193] His reply was:

> The ASSC is not happy about the situation and feels very dissatisfied. It had not foreseen – perhaps it should have – the nature of some of the objections on grounds of law, and it is now re-examining the possibility as to whether it cannot issue a further statement, at least to clarify its own position

> in the matter – and, hopefully, to try and settle the matter once and for all.[194]

Though the ASSC, *corporately*, may not have foreseen the difficulties, it seems likely that most of its members, individually, did. Did it issue the exposure draft deliberately to bring the difficulties into the foreground and demonstrate, for example, the need for clarification of the law? 'I don't think we were sophisticated enough for that', is Morpeth's view.[195]

In fact, the next document published on this topic was ED31, in October 1982, and SSAP 23 was adopted in April 1985, nearly fifteen years after the first exposure draft.[196]

Extraordinary Items

The idea that a company's profit and loss account might include items that are in some way 'abnormal', for example a transaction not usually undertaken by the business, or the outcome of a non-recurrent event, or an event of an exceptional nature, and that users of financial statements might need special information about such items, was not, in 1970, particularly startling or new. Indeed, the Companies Act 1948 contained provisions requiring that, if the profit and loss account was materially affected by any of the types of item listed above, this should be disclosed.[197] The legislation did not, however, indicate whether abnormal items should be included in the results for the period.

In October 1958, a Recommendation on Accounting Principles dealing with the 'Presentation of Balance Sheet and Profit and Loss Account'[198] sketched out two positions 'as to what should be included in the amount shown as the profit or loss of a year':

> Some consider that it should take into account . . . all profits or losses arising or ascertained within the year, including those items which . . . are the consequence, ascertained within the year, of transactions of earlier years. Others hold that the amount shown as the profit of the year should be restricted to the results of the operations of the year and that all other items . . . should be shown in the profit and loss account [i.e. as balance sheet movements].[199]

Characteristically of the series, their critics would say, the following paragraph began:

> Each of these opinions has arguments in its favour and it cannot be said that either of them is generally accepted to the exclusion of the other. Provided that the account is prepared in conformity with either of these opinions and is the result of the consistent application of recognised accounting principles it can properly be said to be true and fair.[200]

Consequently, the recommendation was that:

> Items of an exceptional or non-recurrent nature ... may be dealt with as follows:
>
> (a) where the items arise from ... trading operations ... they may be dealt with in arriving at the trading surplus or deficit and disclosed separately ...
> (b) they may be shown separately in the section of the account which includes other income and non-trading expenditure of the year.
> (c) they may be shown separately after the 'profit after taxation'.
> (d) they may in appropriate circumstances be ... taken direct to reserve.[201]

A position described by *Accountancy* as 'permissive in the extreme' and, even less politely, 'anything goes'.[202]

The first ICAEW survey of published accounts attempted to discern accounting policies for abnormal items. It concluded that,

> in a large proportion of cases no clear policy could be deduced, either because any exceptional items disclosed were insufficient to indicate policies or because items which might well appear in either profit and loss account or reserves were divided between the two.[203]

The compilers did identify 'a clear preference one way or the other'[204] for 113 companies, but 88 (78%) of these were treating items as movements on reserves. Further, there was cynical talk in the press of '"accident prone" companies [with] a genius for non-recurring expenditure recurring',[205] and the tendency for exceptional items to turn out to be, 'particularly losses, if we may suggest it'.[206]

Thus the ASSC was confronted by variety in treatments, at least potential inconsistency within an individual company's financial statements, and a favoured treatment which appears to deflect attention from abnormal items (which tend to be losses rather than gains). It set out to eliminate variety and took the bold decision that it would do so by requiring the treatment apparently preferred by less than a quarter of preparers, that is disclosure on the face of the profit and loss account. In adopting this approach it was, on this occasion, following the lead of the APB, whose Opinion No. 9 'Reporting the Results of Operations' was adopted in December 1966.[207] The UK exposure draft came 'the closest of any draft [issued up to that time] to an Opinion of the US Accounting Principles Board',[208] and this was noted by commentators at the time, with *Accountancy Age* arguing that the document was 'in many respects, a carbon copy of the relevant part of [the] US opinion'.[209] The Australian pronouncement, issued before ED5, had also followed the APB Opinion.[210]

ED5 'Extraordinary Items and Prior Year Adjustments' was published on 25 August 1971. It was the first exposure draft to be set typographically throughout (rather than reproducing typescript) but the layout adopted – three columns

with banner headlines across columns and an 'appendix' giving an illustrative Profit and Loss Account set within the text rather than at the end – made it look more like copy prepared for a magazine than the original of a draft regulatory instrument.[211] The draft distinguished 'items which arise from events or transactions outside the ordinary activities of the business',[212] which it named 'extraordinary items' and required to be disclosed on the face of the profit and loss account under a separate caption, 'after the results derived from ordinary activities'.[213] Items which were 'exceptional on account of size or incidence but . . . derived from the ordinary activities of the business' would be included in the normal calculation of profit before taxation but disclosed, giving their 'size and nature'.[214] The draft also dealt with 'prior year adjustments', which 'arise from events or transactions which occurred in a prior year, the accounting effects of which could not be ascertained or estimated with reasonable assurance at that time', and which would be 'adjusted against the opening balance of retained profits and thus excluded from the current year's profit and loss account'.[215]

The ED does not provide an explicit justification for the approach adopted beyond the statement in the introduction that 'accounting for extraordinary and prior period items through reserves or retained profits instead of through the profit and loss account can lead to anomalies in the reported annual results of a business and to disparities in the reported results of similar businesses'.[216] Presumably advocates of the alternative approach would argue that, although accumulated reserves over the life of the business will be higher or lower than the sum of individual year's profits, this is anomalous only if one holds that the two should be the same; even weaker is the argument from disparities, which could equally well have been rectified by adopting the other method. The bulk of the explanatory section actually comprises lengthy lists of examples of the various types of item.

ED5 was exposed for three months, unlike its predecessors, all of which gave only a two month period for comment.[217] Eighty-three responses were received, eighty-two in time to be included in the compilation for the committee. It is interesting to review the way in which these were reported to the committee now that this process was becoming fairly routine. Comments occupied about 170 pages and the committee received an edited compilation.[218] It included an analysis of comments from companies, representative bodies and practising firms, divided up by paragraph of the ED. Only the comments of representative bodies were also given in their original form. Comments from individuals, the Technical Advisory Committee and regional Technical Advisory Committees were not 'analysed in detail',[219] but where they contained 'observations which were not made elsewhere',[220] they were included in the analysis and separately attributed. Members of the committee were told that they could examine the original texts of comments 'at Moorgate Place on request',[221] hardly an invitation to delve deeply. Academics were treated as a separate category of respondent but no responses from this group were in fact received.

The paper also contained an analysis of responses between categories of respondent and the overall view taken. Of the 25 companies responding, nine apparently regarded the draft as 'generally acceptable', while another nine regarded it as not generally acceptable, so that preparers were split down the middle. The only other respondents finding the draft unacceptable were two (of ten) individuals. The overwhelming majority of other submissions were analysed as finding the draft acceptable, with 13 out of 14 representative bodies, 16 out of 17 practising firms and 15 out of 16 Technical Advisory Committees being thus classified. The remainder of these categories and one individual were classified as being in an intermediate position.

Submissions clearly reveal a tendency for respondents to base their positions on the effect of the proposal on their own individual positions rather than on the quality of financial reporting generally. A note against the figures for the number of companies analysed as regarding the draft as unacceptable, or taking an intermediate position, reads, 'many of these opponents based their objection on one specific item affecting their particular situation'.[222] Self-referential lobbying was to become a regular feature of the political economy of standard-setting.[223]

The respondent from the Committee of London Clearing Bankers wrote:

> The Clearing Banks have no particular comments on ED5 but I should be glad of your confirmation that the document does not prevent the Banks from continuing their existing practice of adopting accounting bases which defer the revenue effects of certain transactions, e.g. spreading profits and losses on sales of dated stocks through a suspense account.[224]

Another representative body went further, attempting to establish that their members would be exempt from this (and perhaps all) standards. The respondent from the Accepting Houses Committee, wrote that,

> Your paper ... has been looked at by two of the sub-committees of the Accepting Houses Committee, and I am asked to say that, as it is not in any way appropriate to Banking Companies, no specific comments on the content of the Paper would be appropriate from my Constituents.
>
> In order to avoid any future confusion or difficulty, it is suggested that the Paper should be clearly marked 'Not appropriate to Banking Companies', and I would be pleased to learn that your Technical Committee concur.[225]

Incidentally, the Stock Exchange reported that it had no comment to make on the ED[226] and at least two of the submissions cited so far in this paragraph must have been classified by ASSC staff as finding the draft generally acceptable. The submissions included one from an important source of support for the approach, The Society of Investment Analysts, whose principal objection to the draft was that it did not go far enough.[227]

Leach's account of the evolution of the standard suggests that it was not the issue of exceptional and extraordinary items that posed the major problem for the ASSC: 'the principal objective of the ASSC proposals was to outlaw "reserve accounting", as it was often called, and this was not too difficult; difficulty arose in dealing with prior-year items and the controversy over this necessitated [a] second exposure draft'.[228] ED7 was issued on 6 July 1972, again with a three-month comment period. In its foreword, Leach explained that,

> During the course of considering the comments received on [the] earlier Exposure Draft the Steering Committee came to the conclusion that certain fundamental changes were necessary to make the paper more consistent and acceptable. The principal change from the earlier Exposure Draft is the elimination of the proposals relating to the treatment of prior year adjustments which are now left to be dealt with in the profit and loss account [of the year in which they are recognised] either as extraordinary items or not, according to their nature.[229]

An editorial in *The Accountant* hints at the reason for the change when it points out that the above paragraph, 'is guarded, and may suggest as much a change of heart on the part of the ASSC itself as a prevailing weight of argument from other sources'. The issuing of a further ED postponed the target implementation date by a year (to 1 January 1973) but *The Accountant* supported a further draft rather than incorporating the change directly into an SSAP, not least because, 'attacks on the whole concept of mandatory accounting standards, as "dictation" by the ASSC in an area where legislation is silent, have not yet ceased and are best disarmed by allowing the maximum opportunity for the expression and harmonization of all interested views'.[230]

ED7 attracted marginally fewer responses than ED5, with reduced numbers in every category except individuals.[231] The resulting standard, SSAP6, issued in April 1974 with a further year's delay in implementation, reverted to the original proposed treatment of prior year items. There were two changes in the definition of extraordinary items, both of which had been signalled in ED7. It was now a requirement of such items that they should not be expected to recur 'frequently or regularly',[232] as opposed to merely frequently. The definition of extraordinary items in ED5 had contained an exclusion clause relating to exceptional items and this was carried over into SSAP6. However, these items were now, 'exceptional on account of size and incidence'[233] rather than 'exceptional or abnormal on account of size or incidence'.[234] The perplexing distinction between the exceptional and the abnormal was removed and items now have to be exceptional in size *and* incidence – though presumably a very large item occurring every four years might still be of interest to users. Weakness in definitions had been the principal criticism of ED5 offered on its publication by *Accountancy Age*, which pointed out that the APB had recently announced that it was to pursue further work in this area.[235] The minor adjustments in ED7, confirmed in SSAP6, do not go very far to overcome the

problem of establishing a clear distinction in an area where the incentives to manipulate are powerful and vagueness about the cut-off between extraordinary and other items was to prove one of the major difficulties with SSAP6.[236]

Stock and Long-Term Contracts

The ASSC's initial five-year work programme contained a project on fundamental principles of inventory valuation, on which work had not commenced at the adoption of the programme, but which had a planned release date of 1970. It also included a project on accounting for contract work in progress, with a planned release date of 1971–72, but on which work was already in progress. They were seen by those who drew up the programme as part of the drive to cover financial reporting in a reasonably comprehensive way rather than as dealing with pressing problems.[237] Nonetheless, the topics were an important part of the committee's technical agenda. Valuation of stock and long-term contracts had been implicated in the 'accounting scandals' to which the ASSC's formation was a response. The treatment of stock was a central concern of those who regarded the standards of small firms as unacceptably low;[238] some of the problems related directly to accounting methods (for example the inclusion of stock at directors' valuation) and, while others, strictly speaking, arose in connection with audit practice, it was going to be difficult to regulate the auditing more closely until it was clear what preparers should be doing.[239]

Both topics were covered by Recommendation on Accounting Principles N22,[240] which, however, permitted a wide range of methods; the ICAEW survey of published accounts for 1968/69[241] showed that preparers were taking full advantage of this flexibility. Many companies were using more than one basis, so that among the 295 companies with material stock and disclosing information about its measurement, 360 individual bases were to be found. Although almost two-thirds of these represented variants of the orthodox lower of cost and net realisable value rule, the remaining 129 drew from a wide range of alternatives, including cost without any test of recoverability (40 instances); cost or less with no indication of the reason for a reduction (10); lower of cost and replacement price (20); lower of cost, net realizable value and replacement price (20); base stock (5); sale value less normal margin (2); market value or forward selling price (1); standard cost (1); and other bases (16). In the remaining five cases, preparers merely indicated loftily that stock was recognized, 'on bases and by methods of computation considered appropriate in the circumstances of the business . . . or similar wording'.[242]

A second area of variety related to the treatment of overheads. The recommendation discussed alternative approaches here at some length but concluded only that, 'after weighing all relevant considerations it is necessary to decide whether and if so to what extent overhead expenditure should be included'.[243] Only 114 preparers gave sufficient information to discern the treatment of overheads and, of these, 75 stated that only a proportion of overheads were

included in the computation of stock, the most frequently included category being works overheads.

The preamble to N22 discussed long-term contracts and observed that 'it is often appropriate to spread over the period of the contracts, on a properly determined basis, the profits which are expected to be earned when the contracts are completed,'[244] though the recommendation itself simply stated that this 'may be appropriate'.[245] In the ICAEW survey, of the 62 cases in which the existence of long-term contract work in progress could be determined or inferred, 25 companies did spread profits, not necessarily on all contracts, 30 did not and seven did not disclose sufficient information: roughly half the preparers in each camp, then.

Work on the fundamental principles of inventory valuation got rapidly under way, with the initial background study being undertaken by one of the professional firms agreeing to collaborate on ASSC projects.[246] At first, the two topics were, as the initial work programme had envisaged, dealt with separately by the Technical Committee.[247] Subsequently, however, they were merged and by November 1971 a single document was in an 'advanced stage of drafting'.[248] In fact the exposure draft, ED6 'Stocks and Work in Progress', did not appear until 16 May 1972, meeting the initial target for long-term contacts but missing that for inventory, the first significant delay in the programme. There were two difficulties; the more serious involved discussions with the Inland Revenue of the implications of the pronouncement for company taxation, discussions which in fact continued after the draft appeared and contributed to further delays in the adoption of the standard.[249]

The other difficulty related to the format and structure of the pronouncement itself: the original draft produced by the sub-committee of Technical Committee was, 'a very detailed document, less clear on the principles', and the ASSC had to do a good deal of work on it.[250] The committee was certainly successful in eliminating distracting detail from the section of the draft setting out proposed standard accounting practice: the part addressing treatment (as opposed to disclosure) contained just a single paragraph:

> The amount at which stocks and work in progress are stated in periodic financial statements should be:
>
> (a) The lower of cost and net realisable value of the separate items of stock or of groups of similar stock items;
> (b) In the case of long term contract work in progress, cost plus attributable profit, less anticipated losses. If anticipated losses on individual contracts exceed cost incurred to date, such excesses should be separately shown as provisions.[251]

The term *attributable profit* was defined as 'that fraction of the total profit ... which fairly reflects the proportion appropriate to the work carried out at the accounting date'.[252] Thus the single paragraph in the ED effectively ruled out

the lower of cost and replacement value and the completed contracts basis of accounting for long-term contracts. The rationale offered for the elimination of the completed contracts basis was that, under it, the profit and loss account reflects the effect of contracts which have, 'by the accident of time, been completed by the year end'.[253] The underpinning rationale in N22, that profits are 'earned when ... contracts are completed', but 'spread over the period of the contracts',[254] was abandoned in favour of the view that profits are earned over the life of the contract.

The third reform to be introduced by ED6, a requirement to include in cost all attributable overheads, was established by providing a definition of cost which included 'costs of conversion'[255] plus a definition of cost of conversion that included production overheads and 'other overheads attributable ... to bringing the product or service to its present location and condition'.[256]

The explanatory section of the draft indicated that methods needed to be 'selected with a view to providing the fairest possible approximation to the expenditure actually incurred'[257] but said nothing to help in determining how to judge fairness if two or more methods are available. The standard was silent on choice of method (though it required the method chosen to be disclosed). An appendix discussing 'further practical considerations', but labelled as 'not form[ing] part of the proposed standard accounting practice',[258] accepted that, 'it is frequently not practical to relate expenditure to specific units of stocks and work in progress'. It also explained that, 'the ascertainment of the nearest approximation to cost gives rise to two problems', namely the choice of costing method (job, process, and so on) and the 'selection of an appropriate method for calculating the related cost where a number of identical items have been purchased or made at different times (e.g. unit cost, average cost or FIFO)'.[259] Note the reference to the nearest, rather than the fairest, approximation. The following paragraph, however, reverts to the previous criterion.

The wording suggests that the committee preferred the notion that for all items of inventory there is one 'true' cost, to which accounting methods are approximations, rather than a constitutive or constructed cost,[260] which accounting methods supply. The profoundly problematic nature of the notion of 'true cost' had been understood by some academic accountants since the 1930s, not least as a result of work undertaken at the London School of Economics.[261] As it happens, the member of the ASSC deliberately selected to 'represent ... academic interests',[262] Professor Harold Edey, was at the London School of Economics, and was very familiar with the debate. The inverted commas around the phrase, 'actual cost', were inserted specifically at his request, the remaining members of the committee being, apparently, entirely comfortable with the term.[263]

ED6 was the first exposure draft to be published after the Association and the ICWA joined the ASSC. It was also the first to affect the recognition of earnings in the financial statements of individual companies. Like ED1, its effect in the typical case, unless the required policies were already in place, would be to increase profits: some element of profit on long-term contracts would be now be

recognized and some element of overhead costs now deferred. However, because it applied to individual companies rather than only to consolidated statements, the change would potentially increase the tax payable for the period. The chairman's foreword explained that, 'the Steering committee realises that the adoption by companies of the standard practices proposed in [the] draft may . . . have taxation implications. It is proposed to hold consultations with the Inland Revenue to clarify the tax aspects before taking any steps to issue an accounting standard on the subject.'[264]

In fact the Revenue's position on inventory valuation had been widely publicized at the time of the adoption of Recommendation N22 and, as *The Accountant* predicted,[265] did not change.[266] On first adoption of the new policy, the Revenue allowed the new carrying amount of opening stock to be used in the computation of profits for the period (as it is in the financial statements) without re-opening the computation for the previous year, so that the uplift is untaxed. Hence, in a steady state, there is no change in the stream of taxable profits as a result of, for example, a switch to including overheads in inventory. However, if the level of activity, and thus stock-holding, expands, even if only in monetary terms, profit is recognized earlier in the financial statements, and thus for the purpose of calculating taxable profit, because of the increased value of overheads carried to inventory. The ASSC's discussions with the Revenue did not persuade them to extend their approach to long-term contracts, or to accept the completed contract method for tax purposes when the published financial statements recognized attributable profit, although it was prepared to allow existing contracts to run off on the old basis.[267] As a consequence, the adoption of the new policy would have direct economic consequences,[268] that is, change aggregate cash flows for the company, as it happens in an adverse direction. Although the outcome of the ASSC's discussions with the Revenue would not have been known on the publication of ED6, preparers were no doubt able to make a shrewd guess as to what it would be.

The Accountant commissioned a set of contributions commenting on the proposals. Patrick Edge-Partington, a chartered accountant and chairman of Crown House, whose activities included both manufacturing and long-term contracting, contributed first a letter[269] and then one of the commentaries, representing preparers. In his commentary, he suggests that, 'the accountant who favours a theoretical approach to the valuation of stocks and work in progress will find cause for satisfaction in ED6'. To no one's great surprise, it turned out that Edge-Partington himself preferred an 'approach based on simplicity and practical experience',[270] an approach, that is, like the one adopted by his own company, which recognized no profit on work in progress, even on long-term contracts, and wrote off all overheads other than factory and site expenses. This policy he commended on the grounds of certainty, simplicity and prudence. He refers to the 'profit estimates in work in progress' as being 'unrealised',[271] although the ASSC had carefully avoided giving that particular hostage to fortune, dropping the N22 notion of profit being earned on comple-

tion of the contract. ED6 makes no reference to the realization or otherwise of the profit but since SSAP2 had by then made it clear that prudence was a 'fundamental concept' under which, 'profits are not anticipated, but are recognised by inclusion in the profit and loss account only when realised',[272] it should, of course, have been apparent to Edge-Partington that in the ASSC's view, the profit *was* realized.

Edge-Partington's commentary mentions only in passing the concern that some were suggesting would be a major cause of controversy, namely, 'its likely effect on figures ... which have a direct impact upon liability to taxation',[273] as *The Accountant* put it in the introduction to its set of articles. Edge-Partington refers only to the increased capital needed to finance the business as a consequence: 'where estimates prove to be overstated, this could be very damaging'.[274] There was, he felt, also the additional problem of dividends potentially being paid out of overestimated profits. All in all, 'the requirements of ED6 in relation to accounting for long-term contracts would seem to be potentially dangerous'.[275]

The views expressed by Edge-Partington in his article were somewhat at variance with the position he had sketched out in his letter to the journal, published two months earlier.[276] There he had explained that the ED left him, 'in doubt as to its practical effect' as far as long-term contracts were concerned:

> The authors quite rightly have been unwilling to throw over the principle of prudence and only if it is prudent to do so expect profit on long-term contracts to be taken in advance of completion ... those who object to this procedure for practical reasons do so mainly on the grounds of prudence, and *there would appear to be nothing in ED6 to prevent them from continuing to exclude profits on uncompleted contracts for this reason*.[277]

In other words the accounting numbers could remain unchanged.

Paul Rutteman's contribution to the series in *The Accountant*, made as a practitioner, hints that auditors will not be able to challenge the approach suggested by Edge-Partington's letter: after listing a number of the uncertainties which attach to almost all long-term contracts, he concludes that, 'if a company in these circumstances claims that the outcome of a contract cannot reasonably be foreseen, are the auditors really in a position to disagree?'[278] As a result, 'those [preparers] which take a more conservative approach to the recognition of profits on long-term contracts by accounting for profit only when the contract has been completed may receive unqualified audit reports without really following the spirit of the standard'.[279]

This debate – must ED6 change the accounting numbers or can they remain the same? – reflects the tension, often apparent in standard-setting, between a shift in the principle to be followed (and hence the rationale underpinning an accounting policy) and the practical impact on the accounting numbers, in this case the question of how much profit on long-term contracts would have to be recognized earlier under ED6.[280]

Partly, no doubt, because its subject matter affected a wide range of companies, ED6 attracted a record number of submissions; indeed it was to retain the record for exposure drafts unconnected with price change accounting for the whole of the committee's life.[281] Although the figure for total submissions, 153, exceeds that for ED1 by only one, ED1 had the advantage of novelty and, moreover, ED1's total was inflated by a large number of submissions from individuals. Preparers' submissions on ED6, at 72, exceeded those on ED1 by a margin of 40%. Although it seems highly likely that *The Accountant*'s speculation that it would be the tax consequences of ED6 that would make it controversial was correct, this is not readily apparent from the submissions.[282]

It is true that some preparers' submissions comment quite openly about the tax position. Guest, Keen & Nettlefolds, for example, begin by stating that:

> Before listing our comments in detail, it is essential to preface these by saying that before any change in the basis of stock valuation could be contemplated, the taxation implications involved in such a change must be resolved so that the result is not disadvantageous to the tax payer.

The company goes on to object to the proposal on the grounds of prudence and a failure to make a case for change from the previous position. The Hawker Siddeley Group objected to the proposals for long-term contracts on the grounds of prudence but went on to say that:

> Unless special dispensation is obtained from the Inland Revenue Authorities, the increase in profits which would result from the proposals for work in progress valuation and profit-taking on long-term contracts will result in the timing of the charge to taxation being brought forward. This could have a serious effect on the cash flow position of industry, would increase costs due to the high level of cash utilisation arising, and . . . would not gain acceptance from responsible Boards or their financial advisers.

Again, ICI objected to the inclusion of overheads in stock on the grounds that no case for change had been made and it preferred marginal cost, but added, 'we would deplore paying any more tax as a result of this standard'.

However, these submissions were in a minority and, of course, made their principal objection on a basis other than tax consequences. Most respondents ignored the tax issue. Among the largest and best-known companies, Glacier Metal, GEC, British Insulated Callender's Cables, Taylor Woodrow and John Laing and Son all objected to taking profit on long-term contracts on the grounds of prudence or uncertainty (which amounts to the same thing), without mentioning taxation. Unilever objected to including overheads in stock on the grounds of prudence and technical difficulty, The Steetley Company preferred direct cost and British Oxygen preferred marginal cost, all without mentioning taxation.

Despite the level of objections, the ASSC persisted with the project and in May 1975, three years after the exposure draft, SSAP9 was issued. This was the longest gestation period of any standard issued in the 1970s – though of course a draft on merger accounting was awaiting finalization throughout the life of ED6 and well beyond it. The length of the gestation period did not reflect any need to undertake complex redrafting, for the final document contains no material changes and the textual improvements are small in number. One cause of delay was the need to pursue with the Inland Revenue a definitive statement of the tax consequences of the standard, already described. The principal causes seem, however, to have been the committee's need to steel itself for the reaction it was expecting, combined with the distraction of price change accounting.[283]

Improving Financial Reporting

Ironically, the Statement of Intent did not actually suggest that the programme of accounting standards would be used to secure improvements in financial reporting *generally*, that is beyond the specific and limited remit it set out. Perhaps the idea that the ICAEW would take the lead in promoting major new reporting initiatives was thought too controversial for the manifesto, but in practice the ASSC lost no time in moving into this area.

The committee's first such initiative, announced in its initial five-year programme, related to disclosure of earnings per share. The calculation of an EPS figure as a stage in the determination of price-earnings ratios had become relatively common among financial analysts by the late 1960s,[284] following a similar development a decade earlier in the USA.[285] However, it remained relatively uncommon for companies to assist them by providing their own figures: only about 20% of companies in the ICAEW survey of published accounts gave EPS in 1969/70.[286] Where a company did provide its EPS, it generally did so in a part of the annual report outside the scope of the audit and there was a tendency to use the period-end capitalization in the denominator rather than the average capital available during the period, and to ignore the dilutive effect of future dividend rights and outstanding share rights.[287]

The ICAEW's Technical Advisory Committee considered a draft standard on EPS in October 1970.[288] ED4, published on 22 March, 1971, 'followed the contours of an earlier Canadian Institute recommendation'.[289] Although EPS is simple in concept the document was in fact lengthy – 32 pages in all – largely as a result of the inclusion of worked examples dealing with more complex points. Responses were received from 66 parties although the number from companies, just nine, was one of the smallest in the ASSC's history. The responses were generally favourable.[290] *The Accountant's Magazine* did carry an article by Simon Keane[291] spelling out the misconceptions on which any view of EPS as 'an index of managerial performance'[292] foundered, including the problem that, 'the reinvestment of retained earnings may produce an apparently favourable, but illusory, trend in EPS'.[293] His battle had, however, already been lost. Having, as required by the ASSC's new constitution, first been approved by all

the other four bodies associated with the ASSC, SSAP3 was approved by the ICAEW Council on 2 February 1972.[294] It thus became the first standard approved by the Councils of the Association and the ICWA.

The standard followed the draft in establishing for the first time a limitation in the scope of the pronouncement, to quoted companies. It was revised in August 1974 – making it the first definitive pronouncement of the ASSC to be revised – as a consequence of the introduction of the imputation system of corporation tax and the resulting need to reflect, in the computation of EPS, irrecoverable advance corporation tax and unrelieved overseas tax arising on dividends. The revision was exposed in draft as part of an ED dealing with a related topic, ED12 'The Treatment of Taxation under the Imputation System in the Accounts of Companies Including the Effect on Earnings Per Share'.[295] The revised standard omitted the lengthy worked examples included in the original version. SSAP3 proved relatively uncontroversial[296] and by the edition of the ICAEW survey of published accounts for 1973/74, the first year in which all the accounts covered fell within the scope of the standard, all 300 companies in the survey published EPS figures.[297]

The second reform to the structure of financial reporting was the introduction into the UK of a statement of source and application of funds. Like the EPS requirement, it reflected a development pioneered in the USA, where such a statement was initially encouraged in 1963.[298] The US pronouncement was the first on the subject by a major standard-setter and its proposals proved popular with the financial community and relatively uncontentious among preparers. In 1970 a funds statement was adopted as an obligatory element of filings by the SEC,[299] and in the following year the APB made the funds statement mandatory.[300] Although almost unheard of in the UK until the late 1960s,[301] funds statements then started to become increasingly common, with the number of companies in the ICAEW survey of published accounts providing one increasing steadily year by year, from 41 (out of 300) in 1969/70 to 153 in 1973/74.[302]

The architecture of a funds statement follows from the definition of funds employed in it. ED13, issued in April 1974, did not provide a definition of funds, nor explicitly rule out a cash based concept, but its terminology, wording, structure and examples led unambiguously to a working capital based concept. The following paragraph is key:

> The funds statement will provide a link between the balance sheet at the beginning of the period, the profit and loss account for the period and the balance sheet at the end of the period ... The figures from which a funds statement is constructed should generally be identifiable in the profit and loss account, balance sheet and related notes.[303]

This wording survived into the standard, SSAP10, issued in July 1975, as did almost all the text. The standard introduced an exemption for entities with a turnover below £25,000 per annum – in effect an application of the cost-benefit criterion.

A criticism of ED13, and thus of SSAP10, is that its concept of funds, though ruling out cash, is actually rather confused[304] and this confusion was reflected in the subsequent variety of practices adopted by preparers.[305]

A difficulty for standard-setters on both sides of the Atlantic arose because this particular standard set out, not to regulate existing financial statements, but rather to bring a new one within the regulatory regime. How to require a new financial statement when the standard-setter does not have authority over financial reporting generally? In the UK, the ASSC employed phrasing to the effect that the standard applied to 'all financial accounts intended to give a true and fair view',[306] following the Explanatory Foreword, in an attempt to 'entrench ... the funds statement in generally accepted accounting practice'.[307] It was very largely successful in this endeavour: by the 1978/79 ICAEW survey of published accounts, only the second to be issued after SSAP10 became mandatory for all accounts covered by the survey, all 300 companies gave a funds statement, and by the following year these were all covered by the audit report, as required by the standard.[308] The status of the funds statement remained dubious, however, because the statutory requirements applying to company financial reporting and establishing the true and fair view doctrine did not include it among the prescribed statements. This ambiguity was considered by the ASC in 1984 (it also applied to certain types of current cost disclosures) and a working party reviewing SSAP10 was asked to determine whether a funds statement was in fact 'essential to a true and fair view'.[309] In the event the review led to no change. Preparers' willingness to provide a funds statement despite its ambiguous status may reflect ignorance of the opportunities thereby created, although when similar opportunities arose in relation to current cost accounting there was certainly greater interest in grasping them.[310] It seems more probable that the explanation is that the funds statement was not itself unpopular with preparers, especially given the flexibility available.

In 1973, the ASSC issued four exposure drafts dealing with topics not on its initial five-year programme. Three proved relatively uncontentious and reached standard status the following year. ED9 'The Accounting Treatment of Grants Under the Industry Act 1972' was issued in March and became SSAP4 'The Accounting Treatment of Government Grants' in April 1974. The trigger for the ED was the significant increase in capital-based industrial grants from government introduced by the Industry Act 1972, and the draft covered only this topic although the standard was extended in scope to cover all capital-based industrial grants from government (including those in the Republic of Ireland and Northern Ireland). ED10, issued in May 1973, dealt with the treatment of Value Added Tax, and became a standard the following April. The only significant criticism of the draft related to whether a standard was needed at all.[311] Another change in the tax regime, the introduction of the imputation system of company taxation in April 1973, yielded a further exposure draft. ED12 was issued in May 1973, but was preceded by a Discussion Paper, 'Notes on Accounting for Corporation Tax Under the Imputation System', in September 1972. This was the second occasion on which an 'official' discussion paper was

issued ahead of an exposure draft, the first having occurred in relation to changing prices.[312] The new tax system created a number of technical accounting problems, especially in the period of transition between the old regime and the new.[313] ED12 was described by *The Accountant* as 'the fruit of much thought and not a little contention'.[314] The draft proposed that dividends be shown in the financial statements at the cash amount distributed, with neither the advance corporation tax payable as a result of the distribution, nor the associated tax credit imputed to the recipient, included in the amount. This was on the basis that the ACT was part of the corporation tax charge and the credit a matter for the recipient, not the company. *The Accountant* thought that the credit was being funded by a higher rate of corporation tax on retentions, the substance of which should be reflected by allowing one or other to be included in the amount of dividend. The issue turns on how a complex economic reality is to be reduced to a simple accounting question: is the tax payment 'part' of the dividend or is it not? The standard was issued in August 1974 and in December 1977 an additional appendix was added setting out a separate standard applying to the Republic of Ireland.

The First Five Years

This account of the ASSC's first five years has strayed slightly over the five year mark to look at the adoption of SSAPs 9 and 10; it has, however, omitted the committee's work on deferred taxation, which fits better into the events described in chapter 6, and the development of a provisional standard on price change accounting, to which chapter 5 is devoted. If we look, for the moment, at the position strictly at the five-year mark, how has the ASSC performed against its initial programme?

Table 3.2 gives the state of play on the programme. The timetable proposed the publication of EDs on 20 topics: of these topics, six featured in EDs published on time, a further two in delayed EDs, and two more in EDs published shortly after the cut-off date: a 40 per cent outturn, then, or 50 per cent if we relax the timetable a little. Performance improves somewhat if we either deduct from the base topics withdrawn from the programme, which leaves only 13 topics to be covered, or include the five topics added to the programme within the first five years on which EDs were published within the period. As it happens, both measures yield approximately a 75 per cent outturn for EDs, not bad given that the initial target was a very demanding one.[315]

The position is almost as good if we turn to accounting standards. The initial programme did not specify a timetable for the transition from ED to standard but, given the pace assumed for EDs in the programme it does not seem unreasonable to expect the transition to take, on average, 24 months. After all, in his survey of the committee's first year, Sharp advocated 'an absolute maximum of six months' delay between the expiry of the exposure period and approval by the ... Councils'.[316] On this basis, 16 SSAPs would have been expected in the five years. In fact, five were issued on time, one covering two

Table 3.2 Initial five-year work programme and output

Topic	ED[a]			SSAP		Notes[a]
	No.	Date	Delay months	No.	Within 24 months?[c]	
Initial five-year work programme						
Disclosure of accounting bases	2	2/71	1	2	Yes	
Form and content of profit and loss account						Withdrawn from work programme after 5/71.[d]
Form and content of balance sheet						Withdrawn from work programme after 5/71.
Treatment of investments in the accounts of trading companies and industrial holding companies						Withdrawn from work programme after 5/71. ED55 issued 7/90.
Treatment of income of associated companies	1	7/70	On time	1	Yes	
Fundamental principles of inventory valuation	6	5/72	16			SSAP9 issued shortly after end of period.
Treatment of extraordinary and prior year items	5	9/71	On time	6	Yes	
Changes in accounting bases						Withdrawn from work programme after 5/71. [FRED21 issued 12/99].
Fundamental principles, form and content of group accounts						Remains on work programme. ED20 issued 7/77.
Accounting for mergers and acquisitions	3	1/71	On time			ED31 issued 10/82; SSAP23 issued 4/85.
Accounting for contract work in progress	6	5/72	On time			SSAP9 issued shortly after end of period.
Fundamental principles of depreciation						ED15 issued shortly after end of period.
Earnings per share	4	3/71	On time	3	Yes	
Accounting for research and development						ED14 issued shortly after end of period.
Accounting treatment of pension funds in company accounts						Withdrawn from work programme before 5/71. Subsequently restored before 12/74. ED39 issued 5/86.
Form and content of pension fund accounts						Withdrawn from work programme before 5/71. ED34 issued 4/84

Topic	ED[a]			SSAP		Notes[a]
	No.	Date	Delay months	No.	Within 24 months?[c]	
Accounting for changes in the purchasing power of money	8	1/83	On time	7[e]	Yes	
Fundamental objects and principles of periodic financial statements						Remains on work programme. Corporate Report issued 7/75.
Accounting for goodwill						Remains on work programme. ED30 issued 10/82.
Insurance company accounts						Withdrawn from work programme before 5/71.
Added to initial programme						
Accounting treatment of government grants	9	3/73	NA			
Accounting for value added tax	10	4/74	NA			
Accounting for deferred taxation	11	5/73	NA			
Treatment of taxation under the imputation system	12	5/73	NA			
Statement of source and application of funds	13	4/74	NA			
Accounting for diversified operations						
Accounting for leases						
Events occurring after the balance sheet date						
Accounting treatment of major changes in the sterling parity of overseas currencies						

Notes: [a]It is assumed that the planned release date refers to the exposure draft stage for the reasons given in the text (p. 48). [b]The work programme at the end of the five year period is taken from EDs 13 and 14. Withdrawals before 5/71 are identified from K. Sharp, 'Accounting standards after twelve months', *Accountancy*, May 1971. Documents released by the ASB are shown in square brackets. [c]Within 24 months of the end of the period planned for the release of the exposure draft. [d]Some material appeared in ED5/7.[e]Provisional.

topics was issued shortly after the end of the period, and three on new topics were issued during the period and one shortly after, making eleven topics covered, or 70 per cent. This rate of output would be even more remarkable for a body getting under way from scratch but, as we have seen, the ASSC was able to take over existing projects from, and benefit from the momentum behind, the ICAEW's existing technical machinery. On the other hand, the level of support that it had hoped would flow from professional firms did not fully materialize.

Of course, the method of measurement used here is reflecting quantity rather than (necessarily) quality or effectiveness. In particular, we should notice that seven topics were withdrawn from the programme, perhaps reflecting poor judgement in drawing it up but perhaps the difficulty of achieving standardization in some areas. Two of the withdrawals, the form and content of the profit and loss account and of the balance sheet, represent a move from a systematic, high-level treatment towards a more piecemeal approach, reflecting the realpolitik of standard-setting (there was a Recommendation on Accounting Principles covering these topics). Three of the withdrawn topics re-entered the programme later in the committee's life (one actually during the initial five years) and one was dealt with by the committee's successor, so it is not that they turned out to be areas in which standardization was unnecessary. In the case of the form and content of the profit and loss account and balance sheet and the treatment of investments, the subjects were dropped only after a draft pronouncement had been passed from the Technical Committee to the ASSC.[317]

Another feature of the table is that, of the small number of topics on which a pronouncement had yet to appear, several were to be subject to very substantial delays – mergers and acquisitions and goodwill being delayed by eight years, and pension costs (the topic that left and re-entered the programme) by eleven and a half. One topic that entered the work programme very early in the committee's life, accounting for diversified operations, was described as being 'in research stage' in May 1971,[318] yet became the subject of the committee's very last standard, issued only a month before the end of its life. Thus it would appear that the, apparently considerable, output in the first five years was achieved in part by dropping or avoiding some of the more difficult topics.

Some of the subjects standardized in the first five years plainly fall into the uncontentious category, including EPS and Value Added Tax. The standard on funds statements achieved uncontentiousness by allowing very considerable flexibility, contrary to the committee's mission to narrow areas of difference but defensible in the wider interest of improving financial reporting through innovation. The standard on accounting policies limited its contentiousness by addressing only disclosure, and that only in general terms, ducking the more difficult issue on the five-year programme of changes in policy. This is not to suggest that the ASSC avoided all controversy. Its first topic, associated companies, was an astute choice, since it demonstrated a willingness to deal with difficult topics while, for most preparers who were affected by it, actually improving the accounting numbers. Its second 'substantive' topic, mergers,

proved to be a most unhappy choice. The ASSC chairman's suggestion that 'it might have been wiser'[319] for the committee to stick to uncontroversial topics in its early years was probably offered tongue in cheek – it simply would not have been politically possible for the ASSC to avoid dealing with at least some 'hot topics'.

In some cases, the ASSC achieved standardization – or, better said, achieved a standard – with less controversy than they might have expected. Two such cases are extraordinary items and stock and long-term contracts. It may well be these topics that Leach had in mind when he spoke of the ASSC's honeymoon period. As we will see, it does appear that the limited opposition to these pronouncements demonstrated at the time of their adoption was attributable in no small degree to preparers' unfamiliarity with the standard-setting process, or at any rate, inability or unwillingness to engage with it on the standard-setters' timetable. Opposition grew after adoption rather than – as the process envisaged – during the exposure period.[320] This phenomenon was apparent, albeit to a limited degree, as early as SSAP1. Viewed as a political activity, the ASSC's 'advantage of novelty' meant that it could take the corporate sector by surprise. The ultimate effect was to store up trouble for the future.

Opinions on the ASSC's progress at the time were mixed. In October 1970, one of the profession's more prominent critics, Lord Shawcross, chairman of the Takeover Panel,[321] convened a meeting between representatives of the Panel and the accounting profession.[322] At this meeting he 'assured the ASSC of every possible support', but also, rather ominously, said that 'he hoped that the timetable already announced could be speeded up'. Such a suggestion, ignoring the already hugely demanding pace being set, suggests an unwillingness to contemplate what is involved in the development of accounting standards in the real world of financial reporting. Another of the profession's critics, Lord Kearton, interviewed in the middle of the following year, still less than 24 months into the ASSC's life, expressed a remarkably pessimistic view:

> As for accountancy practice, the accountancy profession, I would say, has taken far more on board than it can possibly cope with in a reasonable way and, therefore, the idea that you can hope to get any reform by giving accountants a bigger and bigger role, rather flies in the face of what the present accountancy profession, as it is manned and staffed, could hope to deal with. I have, therefore, come to the rather melancholy conclusion that there is nothing very much helpful in the short term. The best you might achieve is to have the problems more clearly recognised and over a period try to make improvements.[323]

In November 1970, the ICAEW Council was told that 'the Permanent Secretary of the Department of Trade and Industry had informally made it known that the Department was concerned about the situation and was keeping it under review'.[324] The initial welcome for the ASSC had worn off rather quickly; the committee were no doubt pleased when the profession's arch-enemy, Professor

Edward Stamp, defended the ASSC's early work, suggesting that it be given 'breathing space' to get on with its task.[325] He felt the need to deny that he was acting as 'poacher turned gamekeeper'.

The technical quality of individual pronouncements varied. Some contributed significantly to narrowing the areas of difference, including the first. Other major contributions in this respect included stock (eliminating some measurement methods and standardizing the treatment of overheads), long-term contracts and the treatment of extraordinary items. Some improved financial reporting by innovation, without necessarily addressing areas of difference: the clearest case here is the funds statement but the disclosure of accounting policies can also be included under this heading. Some had weaknesses: SSAP2 avoided dealing with changes in accounting policy and substantial flexibility was permitted in identifying extraordinary items, the treatment of government grants, and in both the identification of the funds concept and the format of the funds statement.

However, we need to be aware of the danger of judging the ASSC's 1970s efforts by the expectations of a later era. It is salutary to be reminded that one academic, now a prominent professor of accounting, was writing in a prize-winning essay in 1977, that,

> In its anxiety to narrow the areas of difference and variety in accounting practice, the Accounting Standards Committee has moved too far towards extreme rigidity, and future accounting standards must steer a middle course if they are to gain universal acceptance and respect ... It would be extremely undesirable to risk any action which would bring the whole concept of accounting standards into disrepute. Flexibility and communication should be the theme for the development of accounting standards in the years ahead.[326]

The ASSC's work reflected developments on the international scene in a variety of ways. Some of the issues to be addressed resulted from the arrival in the UK of commercial practices and accounting methods developed elsewhere, principally the USA. Examples include mergers and merger accounting and equity accounting for associated companies. In some areas, UK practice led (for example the 20 per cent cut-off for associated companies and the disclosure of accounting policy); in others it followed practice in the USA (extraordinary items, funds flow statements) or Canada (EPS). Despite the issues on which UK practice led, Leach was surely displaying uncharacteristic hubris if, as reported, he said that, 'the accounting profession in America and Canada ... is anxious to align itself with United Kingdom practice as closely as legal and taxation differences permit'.[327]

A number of the wider issues that were to be important in later periods were already becoming visible. In the technical domain, a number of discussions of 'conceptual' matters had arisen: who are the primary users of financial statements (raised in connection with ED1)? When is profit 'earned' or 'realized'

(equity accounting; long-term contracts)? Does treatment matter as long as information is disclosed (extraordinary items)? How should the balance be struck between the costs and benefits of improved disclosure (funds flow)? Do accounting methods approximate ascertainable amounts or construct their own reality (stock measurement)?

In the political arena, the Councils of the professional bodies showed signs that they expected to be able to influence the content of standards. Debate about the economic consequences of accounting standards became particularly sharply focussed with the ED on stock and long-term contracts because a direct cash flow – the timing of taxation payments – was involved. In another case, extraordinary items, submissions tended quite openly to advocate a particular approach on the basis that the standard should permit the respondent to continue its current practice, rather than on technical merit.

4 Accounting for Changing Prices: The Struggle Begins

Even the ASSC's honeymoon period was marred by what was to become its most serious and frustrating struggle. For a short while the committee thought it had found a neat solution, but eventually its inability to resolve the problem would play a significant part in destabilizing its work. The problem was inflation and the need to provide a reliable reflection of the impact of changing prices on the business entity in its financial statements.[1] At the heart of the problem, as far as accounting is concerned, is the dualistic nature of price changes. The prices of *specific* goods and services, including business inputs and outputs, rise and fall individually and, to some degree, independently. The overall impact of these movements yields a change in the *general* price level which, in turn, affects the purchasing power, and hence wealth, of those holding monetary assets and liabilities, including corporate debt, and the value of the unit of measurement (the currency) in which financial statements are prepared. While there is a tendency for prices to move together, individual prices can and do move out of line with the general price level, so that, for example, during a period of inflation a business might find its principal inputs or outputs falling in price.

A comprehensive system of accounting for price changes would reflect both specific and general price movements, but would, as an inevitable consequence, be complex.[2] In any event, at the beginning of the committee's life, thinking on the topic had not yet evolved to the point at which the need for such a comprehensive system was widely appreciated. Thus debate focused on the choice, in any proposed system, between using specific prices, such as replacement costs, and the general price level.

Interest in accounting for changing prices tends to vary with the rate of inflation, which largely also indicates the extensiveness of relatively substantial changes in specific prices. The three years immediately following the Second World War saw an inflationary burst caused by economic reconstruction and were followed by the publication of one of the Institute of Chartered Accountants in England and Wales' Recommendations on Accounting Principles, N12.[3] This rejected any form of systematic adjustment to the historical cost financial statements; any allowance to reflect inflation was to be carried out as a transfer between reserves. In 1951 and 1952 inflation ran at nearly 10 per cent per annum as a result of the Korean war and in the latter year both the Institute of

Cost and Works Accountants and the Association of Certified and Corporate Accountants published reports advocating systems based on specific prices (replacement cost).[4] Following publication of these reports, the ICAEW issued a further Recommendation.[5] Notwithstanding the proposals of the two other bodies, and the difficulty the Institute had found in arguing to government that an adjustment of profit to reflect inflation was appropriate for tax purposes while defending the position in its earlier Recommendation for financial reporting purposes, the new Recommendation reaffirmed its predecessor's resistance to the adjustment of financial statements. It conceded that historical cost information was deficient in the face of changing prices, but argued that the impact of inflation should be quantified in the directors' report, with an appropriate transfer between reserves. This position generated considerable controversy between the professional accountancy bodies,[6] but its conservatism was largely vindicated politically by the speed with which inflation was brought under control. In 1953 it fell to 3.1 per cent and in the following fifteen years averaged a little below 3.25, never reaching 5 per cent.[7]

In August 1968, a pamphlet entitled *Accounting for Stewardship in a Period of Inflation* was published by the ICAEW.[8] The event was unusual in two ways. The first is that official notice was apparently being taken of the problem of accounting for changing prices without the pressure of significant inflation. The second is that, although the pamphlet was described as having been 'prepared under the aegis of the Research Committee of the Institute of Chartered Accountants in England and Wales',[9] the leading role in its production had in fact been taken by the then President of the ICAEW, W. E. (later Sir Edmund) Parker. It is rare for a President in office to find the time, let alone have the desire, to contribute to the theoretical literature of her or his subject. Why the anonymity? At the time, Presidents of the ICAEW were very powerful figures and could get their way over most things, but not even as well-respected a figure as Parker could have insisted on the Council backing one particular method of accounting for changing prices.[10] However, his authorship rapidly became one of the most open secrets in the history of the British accountancy profession.[11]

The system advocated in *Accounting for Stewardship* was current purchasing power (CPP), a method which reflects changes in the general price level but not those in specific prices. Parker was a partner in Price Waterhouse's UK practice but had worked for a period in the US firm and was much more familiar with American financial reporting than most ICAEW Council members. His advocacy of CPP was partly influenced by his US experience; he had been interested in accounting for changing prices, and had made contributions to the debate on the subject, for more than a decade before *Accounting for Stewardship* appeared, and had supported CPP for some time.[12]

Accounting for Stewardship presents CPP as akin to foreign currency translation, a technical process much more familiar to most accountants than any form of accounting for changing prices. It is depicted as an evolutionary approach, building on Recommendation N15's acceptance of the deficiencies of historical cost. The pamphlet is brief – only 24 pages long – the method is well presented,

and there is a substantial worked example. All in all, its provenance, approach and style made the system set out in *Accounting for Stewardship* likely to be relatively palatable to practitioners.

Inflation Takes Off

In 1969 inflation breached 5 per cent for the first time since 1952. In March 1971, with inflation now running at nearly 9 per cent, Sir Henry Benson[13] wrote to the President of the ICAEW, Claude Croxton-Smith, suggesting that the Institute should, 'take the lead in the urgent consideration of the question of financial administration and accounting under inflationary conditions'.[14] Although his letter suggested an inquiry of wide scope, the Council effectively narrowed the debate by requesting the ASSC to initiate discussions with interested parties.[15]

It did so by holding a meeting which, following the confusing approach it had already adopted,[16] it described as a 'plenary meeting' of the committee.[17] On this occasion the meeting comprised the members of the ASSC, other 'standing' members of the Plenary Committee, plus a number of guests including representatives of the Bank of England, the Board of Inland Revenue and the Department of Trade and Industry, Benson, Parker and the chairman of the Accounting for Inflation sub-committee of the ICAEW Technical Committee.[18] This group first met on 10 May 1971. The press release issued before the meeting explained that it would investigate 'the possibility of establishing an accounting standard requiring financial statements to disclose the effects of changes in the purchasing power of money'.[19] The meeting was presented with two documents, a 'Factsheet' and a 'Discussion Paper', both carrying the title 'Accounting for Changes in the Purchasing Power of Money'.[20] The papers were written largely by Chris Westwick, who had joined the Institute's technical secretariat in April 1971, and had little time in which to prepare them.[21] Although described as a Discussion Paper, the document in fact gives a single 'suggested solution' for the inadequacy of historical cost accounting, a version of CPP, and uses this abbreviation. Because of their cover design, the two papers have come to be known as the 'Tombstone document'.[22] They were subsequently merged and published in *Accountancy*.[23]

David Tweedie and Professor Geoffrey Whittington argue that the final phrase in the press release quoted above shows that CPP was already the favoured solution before the first meeting of the Plenary Committee.[24] This conclusion is further underlined by the original title of the Tombstone document and by its contents. Indeed, it would appear that the presumption for CPP pre-dates the press release by at least twelve months: the initial work programme agreed by the committee on 5 May 1970[25] included a project on 'accounting for changes in the purchasing power of money' and the committee's progress report for the year ended 30 April 1971[26] indicates that a topic by this title is with a drafting sub-committee. The ICAEW Technical Committee confirmed to the Council that the approach taken in the Tombstone document was

consistent with the basis on which the drafting sub-committee was working and a working party of the Technical Committee was established to agree the final text of the Tombstone document.[27]

Sir Ronald Leach opened the meeting of the Plenary Committee by emphasizing that its purpose was not to 'arrive at any immediate decision'. He suggested that it 'should touch only lightly on technical problems, if necessary reference would be made to *Accounting for Stewardship*'. He explained that the papers before the meeting 'did not deal with replacement [cost] accounting but with price-level accounting'.[28] His introduction further underlines the fact that CPP was already the preferred option for a standard.

The representative from the Takeover Panel spoke next and supported CPP; he was joined by the representatives of the Issuing Houses Association and (albeit rather late in the debate) the Stock Exchange. Parker, not surprisingly, also supported CPP. The representative from the CBI was equivocal: he indicated that, 'it was difficult to forecast how his members would react [but] he was sure, however, that any reaction would be vigorous'.[29] In later interventions he argued (twice) for any recommendation to be voluntary.[30] His own suggestion was to 'concentrate on accounting for replacement of fixed assets'.[31]

The representative from the ICWA, H. P. Southall, spoke early in the debate and apparently 'said that his organisation was absolutely in favour of the idea of CPP accounts. The ICWA would support any move that required their publication. The ICWA had themselves published a book on the subject some time ago.' This is a puzzling comment, since the ICWA's 1952 publication in fact supported replacement cost accounting.[32] It is unlikely that he was confusing price-level and replacement cost accounting since he went on in the same speech to say that, 'the documents before the meeting were absolutely fine, they clarified the difference between price-level and replacement accounting'.[33]

Other representatives were less enthusiastic. David Damant, from the Society of Investment Analysts, was 'slightly worried that if CPP accounts were produced [alone] the analyst would be unable to undo them if he wished'.[34] Sir William Slimmings pointed out that if CPP was introduced alongside historical cost it would 'lead to triple accounting',[35] the third in the trio being tax accounting. The representatives from the ACCA and the Institute of Municipal Treasurers and Accountants spoke but without indicating a position on the main question.

Much of the time was taken up discussing a proposal by Benson that some sort of government inquiry should be set up. He argued that 'the government must take a hand'[36] because inflation presented problems not only for accountants but also for government itself, industry, the City and the unions. A variety of views on the proposal were offered, including support, opposition, concern that it would delay matters, and the need to consult more widely within the accountancy bodies. Ian Fraser, representing the Takeover Panel, presciently argued that an 'enquiry should not be allowed to fall into the hands of the government because they were too loath to admit that inflation exists'.[37] Representatives of the DTI, the Inland Revenue and the Bank of England all

undertook to take the views of the meeting to their departments and report back. Despite the title given to the meeting, 'Financial Management and Accounting Under Inflationary Conditions',[38] no discussion of the wider problems, other than Benson's intervention, took place.

Leach's recollection of the meeting, a decade later, was that, 'the paper was well received and in fact had the unanimous approval of the Plenary Committee, which had such a wide representative membership, including the Confederation of British Industry and government'.[39] This does seem rather a rosy assessment. The report of the meeting does not suggest that a vote of any kind was taken; while there were several favourable comments about the Tombstone document, some speakers (including the CBI representative) raised possible alternatives or mentioned disadvantages of the implied proposals and representatives of two accountancy bodies and all the representatives from government departments were careful to reserve their positions.

The report of the 10 May meeting was presented to the ICAEW Council on 7 July. The Council agreed to publish the Discussion Paper, 'edited as appropriate', and 'to seek a substantial degree of government involvement in the issue, by way of a government inquiry, or departmental inquiry, or attendance of departmental officials at relevant discussion'.[40] It also agreed, with some foresight, that if it proved impossible to secure government involvement, 'the Institute should seek some other means of giving the issue added status (perhaps by seeking Bank of England sponsorship) but in any event should take the lead in developing action'.[41]

An Exposure Draft Takes Shape

The system developed from *Accounting for Stewardship* and presented in the Tombstone document was effectively adopted by the ASSC for its first pronouncement on accounting for changing prices. Tweedie and Whittington examine the advantages for the system presented in the Tombstone document and conclude that it 'amounts to a rather weak case ... Each of the "advantages" listed ... is contentious.'[42] The document does not explicitly point out that the system is cheap to introduce and operate nor that it is easy to audit. However, claims for its evolutionary character, made in *Accounting for Stewardship*, hint at the former and its alleged objectivity – once the choice of price index has been made, and under the system proposed it would be made by the standard-setter, CPP is no less objective than historical cost – imply the latter.

The Plenary Committee met again in July 1971 but postponed drawing up a plan of action until it had heard back from the government departments who had been pressed to become involved.[43] The next meeting of the Plenary Committee, in December 1971, heard from the DTI representative, who explained, somewhat ominously, that, 'while not ruling out possible future action it was the Government's opinion that the accountants and other interested parties should be left to pursue the matter at this stage'.[44]

Meanwhile, the ICAEW's annual Cambridge summer conference in 1971 was devoted to the subject.[45] It was chaired by Parker, who gave a paper describing the Tombstone (that is, his) system, actually during the course of 'summing up' the conference.[46] Other speakers included several, for example H. Vermeulen of NV Philips and Eddie Weiss of Tube Investments, advocating replacement cost, some having had practical experience of the system. Nonetheless, *Accountancy*'s summary of the conference indicates that, while 'exponents of the various methods . . . spoke more or less convincingly, the consensus of opinion afterwards was that the price index system [i.e. CPP] was preferable to replacement cost accounting'.[47] To what extent the consensus had been influenced by Parker's role is difficult to judge. Although practitioners did not dominate numerically – they were outnumbered 98 to 87 by members from industry – this was a recent development (two years previously practitioners had a 6 to 1 majority)[48] and thus the 'regulars', more used, perhaps, to engaging in debate, would have been predominantly from practice.

In the new year of 1972, then, as the ASSC found itself without the government support it had judged important, and thus needing to proceed alone, it felt that it had substantial evidence that its preferred solution was acceptable: its Plenary Committee had not voiced objections and the summer conference had apparently reached a consensus in its favour. Whilst the evidence may have been somewhat tainted by the introduction of CPP as the favoured solution rather early in the consultation process, and by Parker's high profile, nothing had emerged to give serious pause for thought.

The sub-committee of the ICAEW Technical Committee responsible for drafting the ED was chaired by Gordon Hunter, of Dearden Lord Annan Morrish. Other members comprised four practitioners, four accountants from industry, an academic and one person in retirement,[49] so that it could scarcely be described as overwhelmed by practitioners. It was initially serviced by Kit Platt, who had been secretary of the Research Committee at the time *Accounting for Stewardship* was produced, and had done some of the drafting for it. He was allocated to the sub-committee partly because of this experience.[50] Westwick took over responsibility for servicing the committee on joining the ICAEW secretariat in April 1971. No specific projects were mentioned during his interview; on the day he joined, Renshall was out of the office, but had left a postcard on Westwick's desk, suggesting that he worked on several projects, including price change accounting, and Westwick was enthusiastic about this one because he had already appreciated the importance of the subject from his previous professional experience.[51] The urgency of developing a response increased as inflation climbed: in June 1971, the annual rate exceeded 10 per cent for the first time since June 1952.

The drafting sub-committee worked well together, co-operating to develop the document rather than adopting partisan positions. Nonetheless, the work went slowly, largely because the committee lacked of any sense of urgency. Meetings prior to Westwick's arrival in April 1971 had discussed principles rather than a draft pronouncement but, working from *Accounting for Stewardship*

and the normal template for accounting standards, Westwick was able to produce a first draft of the ED within a few days. The sub-committee then went over the draft line by line. There was only one technical problem: how to treat shareholders' capital, which was not specified in *Accounting for Stewardship*. Westwick suggested that its nature as a residual answered the question and the committee was relieved that the problem had been solved.[52]

The draft standard was approved by the Plenary Committee in November 1972 and published, as ED8 'Accounting for Changes in the Purchasing Power of Money', on 17 January 1973. It was open for comment until 31 July. Its contents followed closely not only *Accounting for Stewardship* but also US recommendations adopted in 1969.[53] CPP accounts would form a supplementary statement required only for listed companies. The lower of cost or market value test was to be applied to the restated amounts, obviating (provided the test is taken seriously) the danger of exaggerating the preparer's wealth if movements in the specific prices of its own assets fall behind the rate of inflation. A key issue is the treatment of the gain or loss arising on monetary items. For example, if an entity has borrowings of £1 million outstanding during a year in which inflation runs at 5 per cent the *opening* carrying amount will typically be adjusted to *closing* purchasing power and thus to £1,050,000 (as pounds at the end of the year are worth less than they were at the beginning, it will take more of them to buy the same volume of goods and services). Since the closing carrying amount remains £1 million, there is a gain of £50,000 to be accounted for. Under the ED, the gain on long-term borrowing was to be included in profit – it is often argued to be unrealized (because the assets financed by the borrowing have yet to be converted into cash) and its inclusion in profit is one of the most controversial aspects of CPP accounting:[54] the implication that gains on long-term liabilities could be used to support a dividend was regarded by many as evidence of recklessness and poor design.

CPP-adjusted carrying amounts for non-monetary items lack intuitive meaning for most non-accountants, and many accountants: they represent the actual price paid expressed in terms of today's general purchasing power rather than general purchasing power at the time of purchase. An alternative, hardly less obscure, interpretation is that they represent the outlay that would be incurred to purchase the asset today, had the price of the asset moved in line with prices generally. Preparers, finding that carrying amounts of their assets still differed markedly from the prices they would actually pay, or obtain, at the balance sheet date, tended to regard the results as unrealistic.

As well as working on the drafting of ED8, Westwick proposed and pioneered the development of two tools that were to become familiar parts of the standard-setter's armoury. The first was the field-testing of proposals. A group of preparers was recruited to check suggestions as they emerged, both for ambiguity in the construction of the requirement and for the practicability of the proposed method. The group gradually grew in size, and comments were judged by Westwick to be 'extremely useful'.[55] It was also, presumably, useful that the news that these volunteers were encountering little difficulty in applying

the system received publicity in the professional press.[56] The other tool was the guidance manual. Westwick worked on this alongside the drafting of the ED, sending sections to the field-testing group together with drafts of the ED, and it was published in 1973.

A third project, proposed and carried through by Westwick with Renshall's authorization, produced a more spectacular result. It sprang from Westwick's concern that CPP adjustments might not make any material difference to relative performance as measured by historical cost accounts: if all companies remained in station with each other, preparers and users might consider the exercise a waste of money. He approached a contact at Phillips & Drew and it was agreed that he and Richard Cutler, of that firm, would develop a method for estimating the effects of applying CPP. This was then employed on the firm's equity book, resulting in measurements for over 200 quoted companies. The exercise took a lot longer than was initially expected.[57] The results, given by name for 137 companies (representing about 75 per cent of the value of the UK equity market), were published in *Accountancy* in March 1973[58] – the issue in which ED8 itself appeared. Although a quarter of the companies registered an increase in profits (almost entirely as a result of the – controversial – gain on monetary items exceeding all other adjustments), the amounts involved were generally small. On the other hand, of the three-quarters of companies suffering a reduction in profit, 16 per cent exceeded a 50 per cent fall and seven companies found themselves making losses. Thirty-two companies were listed as having uncovered dividends. The final table indicated the possible effect of CPP on share prices, using historic P/E ratios applied to CPP profits, so that CPP loss-makers had imputed to them a zero share price.

It was all very well for the authors to counsel that 'the figures should . . . be treated with caution'.[59] As they might have guessed, they were in fact greeted with apoplexy in a number of Board Rooms, especially when a 'brief and somewhat sensational' summary appeared in *The Sunday Times*.[60] Cutler and Westwick were, indeed, orally threatened with law suits by a few finance directors.[61] Westwick's initial reaction was 'terror, followed by telling them to read the full article in *Accountancy*'.[62] No company did take legal action and the heat experienced by Cutler and Westwick is not apparent from the pages of *Accountancy*, which carried no letters on the subject in subsequent issues – it may well be that the companies most severely affected discovered that the estimates were broadly right and decided on a policy of least said, soonest mended. As Westwick somewhat laconically puts it, at least the article, 'contributed to achieving one of [his] aims – namely to get the subject of inflation accounting thought about by senior management and a wider public'.[63]

The ASSC received 113 responses to ED8, less than for its first ED and the draft on stock, and only a handful more than the average to date.[64] Given the enormous impact of the proposed changes, this level of response appears extremely low and should have provided a warning that the communities potentially affected did not understand that something momentous was under way. The responses were, as usual, analysed by the secretariat and summarized for the

ASSC. The analysis was carried out by Westwick.[65] There was an overwhelming majority in favour of some form of price change accounting (93 per cent) but the majority in favour of CPP was slim – only 56 per cent. Practising firms tended to support CPP (though only 12 responded and only 8 backed CPP) while two-thirds of companies favoured other methods.

Tweedie and Whittington[66] re-analysed the responses, classifying respondents according to their judgement of the depth of support shown, and found that, of those companies supporting ED8, nearly half did so with qualifications. Nearly two-thirds of the practising firms supporting ED8 qualified their support and the Technical Advisory Committees of the ICAEW, shown in Westwick's analysis as supporting ED8 almost unanimously, did so with qualifications in just over half the cases. In all, Tweedie and Whittington found 49 per cent of responses supported ED8, but 60 per cent of these provided only qualified support. The differences between Westwick's and Tweedie and Whittington's analyses need to be read, not as indicating that one or other is erroneous, still less that the true situation was hidden from the ASSC, but rather as evidence of the difficulty of judging levels and nature of commitment from submissions. As Tweedie and Whittington put it:

> Our own analysis convinced us of the difficulty of determining the view each respondent was attempting to communicate. Many responses were internally inconsistent; several (especially from committees or representative bodies) attempted to reconcile differing viewpoints with the result that the reader was left confused and uncertain as to the respondents' intentions.[67]

The response from the Society of Investment Analysts is of particular interest – it will be remembered that the Society's representative at the Plenary Committee Meeting of May 1971 was distinctly lukewarm about the Tombstone document. Its response[68] began positively enough: 'we very much welcome acceptance of the argument that company accounts based on historical cost accounting have become distorted by inflation'.[69] This enthusiasm was quickly overtaken by severe criticism, however: 'We do not in any way dispute the logic of your proposal, but we do question its relevance . . . we would prefer the use of specific indices, subjective though they may be, of the kind used by the proponents of replacement cost accounting.'[70]

While ED8 was under development, the CBI had established an inflation accounting committee under the chairmanship of Sir David Barran. The committee reported in 1973, supporting CPP.

The Government Decides that it is Time to Act

In the spring of 1973, as the exposure period of ED8 was drawing to a close, 'it seemed likely that a CPP accounting system would slip into effect almost without critical assessment by the vast majority of the UK's accountants'[71] – or, indeed, any other interested party. Events were, however, to take a turn which, though it

perhaps should have been expected, in fact came as 'a bolt from the blue'.[72] Shortly before the expiry of the comment period Morpeth, Renshall and Westwick were called to the DTI. They were given advance warning that the government was about to announce that it was setting up an independent committee of enquiry into the case for adjusting company accounts for the effects of inflation. The warning was delivered by the Minister of State, Lord Limerick, who was, as it happened, a chartered accountant: 'he looked very unhappy – he'd obviously been told what to do and he realized he was throwing a spanner in the works'.[73] The announcement was made on 25 July 1973 by the Secretary of State for Trade and Industry.

Despite the urgency of the problem (having dropped back a little in 1972, inflation was rising again; from April 1973 it hovered a fraction of a point below 10 per cent until November, when it exceeded that level, to remain above it for four years), the government's committee was established at a fairly leisurely pace. The initial announcement was made at the very end of the Parliamentary session which, suggested *The Accountant*, 'hardly indicates an appreciation of the sense of urgency which the accountancy profession and business interests have already displayed in their own approach to the problem of inflation'[74] (the government might, though, have pointed to the pace at which earlier development work was undertaken by the committee drafting ED8). The delay was attributed in part to difficulties caused by the 'intervening holiday season' but there were also rumours that, 'some potential candidates . . . expressed themselves reluctant to serve, and the appointment of a chairman [was] causing the Government particular difficulty'.[75] In the end a chairman, Francis (later Sir Francis) Sandilands, was appointed but the final composition of the committee, and its terms of reference, were not agreed until 21 January 1974.

We have seen that the ASSC's Plenary Committee urged the government to intervene in May 1971 but that it declined to do so in December, albeit warning that it might change its mind. Other approaches had been made prior to this but, although the profession was reminded that the government had a keen interest in seeing that the problem was tackled effectively, the ASSC had been told – in terms – that a suggestion that the government set up a committee of inquiry was unlikely to be favourably received.[76]

Why did the government intervene when it did? Tweedie and Whittington examine this question at some length, relying largely on what they were told by an old sparring partner of the ASSC, Professor Edward Stamp, who was at the time Chief Accounting Adviser to the Treasury.[77] The government and civil service had been monitoring developments throughout the exposure period of ED8. Their concerns were: (a) that at some stage government backing for a standard might be necessary (the ASSC had apparently already warned them of this) and it would then be necessary to demonstrate that appropriate steps had been taken to establish that CPP was what was needed to show a true and fair view; (b) that the method chosen should be acceptable to the financial community as a whole; and (c) the implications for government policy, especially counter-inflationary measures and taxation. On the second point, a majority of preparers

making submissions to the ASSC did not support CPP and it seems likely that the largest companies, who would have had the ear of senior politicians, would be lobbying to this effect. Peter Walker, who was by now Secretary of State for Trade and Industry did not (in 1984) recollect being lobbied, but Douglas Morpeth reported to Tweedie and Whittington that there were indications that large companies were lobbying government – perhaps via civil servants. The civil service were certainly aware of the strength of support – both theoretical and practical – for replacement cost accounting and of the availability of more sophisticated models for financial reporting such as current cost. They would also have been aware – not least through representation on the Plenary Committee – that very little work to explore alternative models had been undertaken by the ASSC. It is also likely that, of those civil servants who felt they had any technical insight into the problem at all, more would have been economists than accountants, and thus would perhaps be likely, in the context of individual companies, to think in terms of opportunity cost (and thus replacement cost) rather than the purchasing power deflator employed in national income calculations.[78]

On the third point, the government was attempting to control inflation by instruments which employed profit margins as a measure of the acceptability of price increases, and any method of accounting for changing prices would be likely to result in more rises passing the test, unless the target was recalibrated, which itself might look like moving the goal posts. The Inland Revenue was concerned that there would be pressure to move to taxing CPP rather than historical cost profits, thus lowering the take unless there was an increase in the rate which, again, could prove controversial. It was also concerned that accepting inflation-adjusted business profits for tax purposes would increase pressure to allow for inflation elsewhere in the system, for example by indexing personal allowances. By taking a step along the way to indexation, CPP accounting might make it easier to live with inflation and thus reduce pressure to control it; indeed it might create pressure for the extension of indexation to other areas of economic life and add to inflationary pressure. Any form of accounting for changing prices draws attention to these issues but CPP particularly highlights the process of indexation. Finally, and perhaps least nobly, the government itself, being a major borrower, was a primary beneficiary of the erosion of the real value of debt by inflation, a phenomenon explicitly revealed by CPP accounting.

All these points (except possibly the very last) are legitimate concerns and reflect the very wide range of parties affected by financial statements and the reporting model used. Though they were surely entitled to feel severely bruised by the government's dilatoriness in intervening, the ASSC should surely not have been surprised. The Tombstone document itself referred to the wide-ranging implications of the issue[79] and this theme was taken up again in Ken Sharp's March 1972 note on ASSC developments: 'the political implications of the proposals,' he wrote, 'particularly in relation to taxation and the nationalized industries, are considerable'.[80] Sharp was a member of the ASSC at the time. The President of the ICAEW, Arthur Walton, expressed the theme in even

stronger terms in his statement accompanying the Institute's Report and Accounts for 1971, presented at the annual general meeting on 10 May, 1972:

> There is still much to be done in the field of technical activities. Perhaps the greatest problem is that of securing acceptable recognition in accounts of the distortions caused by inflation, and any solution must be acceptable to business and to government (imperative for taxation purposes).[81]

Moreover, a DTI representative had apparently commented immediately prior to the issue of ED8 (presumably at the Plenary Committee meeting of November 1972), that the government was waiting to see what the reaction to the draft was.[82]

However, at least some of those involved do question the government's motives. Westwick notes that, the production of a standard having necessarily been delayed while ED8 was produced, it would now be delayed again while the Sandilands Committee deliberated, and offers the comment:

> It might be too cynical to suggest that, as the Treasury were the biggest beneficiary from inflation, in that the real cost of government borrowing was being eroded by inflation, they were the least keen to see this phenomenon quantified.[83]

David Hobson puts it like this, admittedly on the basis of comments made by a senior civil servant at a dinner party: 'It was quite clear that ED8 had left the government completely unprepared. Their solution, later, was to kick it into touch by appointing Sandilands.'[84] That the news came as a shock, and left standard-setters deeply cynical about the government's motives, is perhaps an indication of how 'financial reporting centred' those involved had become.

The ASSC Reacts

The government's announcement left the ASSC in a serious dilemma: although there was apparently majority support for CPP from respondents, one important constituency, preparers, preferred other methods, while the government itself had yet to reach a conclusion and there seemed a strong possibility that it would insist on replacement cost. If the ASSC did not develop a standard it was in danger of being accused of failing to provide guidance when the need was urgent. The profession's immediate reaction was to go on the offensive. The President of the ICAEW, now Kenneth Wright, was quoted as saying, 'I would very much regret if this inquiry caused unnecessary delay in the introduction of a standard approach to inflation accounting,'[85] while Morpeth, vice-chairman of the ASSC, 'rightly made it clear that the committee [had] no intention of abdicating its responsibility in this field'.[86]

One way forward was put to the committee by Westwick himself: to issue a standard requiring accounts which reflected the effect of changing prices but to

leave it to individual preparers to choose between CPP and replacement cost accounting.[87] This was rejected on two grounds: '(a) an accounting standard should lay down only one method; (b) CPP was a clearly described system (in ED8 and elsewhere) whilst replacement cost accounting was in fact a family of systems and poorly documented publicly.'[88] While the latter point was broadly correct, the situation was in no small part due to the ICAEW's and the ASSC's determination to favour CPP. The first point shows, perhaps, a degree of naivety on the part of the ASSC at this early stage in its history and, if so, it was trapped by the wording of the Statement of Intent.

In the event, the ASSC decided to convert ED8 into a standard but one with a new status (never to be used again): it was to be a Provisional SSAP. This proposal was discussed at a Plenary Committee meeting in September 1973 and received support from the CBI. The ASSC had received a warning from the DTI that to proceed with an orthodox standard would be regarded as a confrontation with government.[89] PSSAP7 'Accounting for Changes in the Purchasing Power of Money' was issued in May 1974. Its scope paragraph stated that it applied to listed companies (as proposed in the ED) but was recommended as good practice for all businesses.[90] This was somewhat undermined, however, by the 'note on the status of this statement',[91] which begins:

> The Statement which follows differs from conventional statements of standard accounting practice in that it is 'provisional': that is, it does not involve a binding obligation to disclose and explain in annual accounts departures from the procedures contained in it, nor does it oblige auditors to mention such departures in their report.

Actually, 'provisional' does not seem to be quite the word the ASSC needed: the Oxford English Dictionary defines the word as meaning, 'providing for immediate needs only; temporary' and while clearly PSSAP7 was expected to be temporary, its non-mandatory status does not follow from that expectation.

The statement's Foreword cited the support of the CBI and concluded, somewhat forlornly though also with considerable chutzpah:

> One of the bodies commenting on the Exposure Draft, namely the Society of Investment Analysts, has reservations, shared by a number of other commentators, on the method to be used, believing that, in many cases, a replacement cost approach would be preferable. The Society, however, confirms its support for the principle that company accounts should reflect the impact of inflation as an urgent requirement.[92]

The system remained as envisaged by the ED. CPP statements would be supplementary to the main historical cost accounts. Preparers were required to explain how the figures had been arrived at, and auditors were told that they should report on the statement, though what they should report is not prescribed In the UK, the general price index recommended was the Retail

Price Index, chosen because of the frequency and speed with which it was published and the absence of retrospective adjustments. This was the only significant change from ED8, which recommended the consumer price index.[93] The standard came into effect for periods beginning after 30 June 1974. The text contained several additions to ED8; an appendix explained the difference between CPP and replacement cost accounting, justified CPP on the basis that the reporting entity's capital was the purchasing power invested in the business by owners, and argued that replacement cost was a management tool. The controversial inclusion of gains on debt in profit was explicitly defended on the grounds that, 'monetary effects are real, as many small savers know to their cost' and that 'availability of liquidity is . . . a separate question from measurement of profitability'.[94] The appendix came closer to a 'basis for conclusions' than anything published in a standard hitherto.

In the month of the standard's publication, annual inflation ran at 16 per cent, up from 12 per cent in January.

Meanwhile, the announcement of the composition of the Sandilands committee in January 1974 suggested, at least to those who were familiar with its members, that CPP was, indeed, likely to be provisional in the orthodox sense of the term. As Hobson puts it, 'they packed [Sandilands] with people who believed in replacement cost'.[95] Lord Caldecote was the chairman of Delta Metal, one of the companies making a submission on ED8 favouring the alternative system; A. J. W. S. Leonard was Group Treasurer of Shell and was thus likely to have been exposed to replacement cost accounting in the Netherlands; and Michael Inwards was the financial controller of Pye Unicam, part of the Philips group, whose accounts had been produced on a replacement cost basis for a number of years. There were three accountants on a committee of twelve. Only one was in practice: Donald Chilvers, partner in Coopers & Lybrand. The other two were Inwards and the academic member, Walter Reid, Professor of Accounting and Financial Control at what was then the London Graduate School of Business Studies (now, London Business School). He was thought, at least by some of those involved at the ASSC, to favour replacement cost.[96] No member of the committee had been involved in the preparation of ED8.[97] As Tweedie and Whittington put it, 'the UK accountancy bodies . . . had lost control of the debate on inflation accounting'.[98]

A number of writers have drawn attention to the 'interesting and important question'[99] of when, and by whom, the decisions were taken to back only a single system, and to back CPP as that single system; none have so far answered the question. Westwick recalls that by the time he joined the ASSC secretariat in April 1971, the 'sub-committee [of the ICAEW Technical Committee drafting ED8] had agreed with its parent to follow the CPP method'.[100] The Tombstone document promoted CPP to the exclusion of other approaches. In principle, alternatives were 'closed off' at various points and it would be possible to identify moments in history at which persons or groups committed themselves, for example to putting CPP and only CPP in the first draft of the Tombstone document, to issuing the final version without altering this approach, and to an

outline of the approach to be adopted in ED8. To date however, no participant in the events has been able to recollect, and no documentary evidence had been identified to pinpoint, a 'defining moment' at which the process moved from significant openness about what method or methods would be recommended to a consensus around, or commitment to, CPP.[101]

It may be of some significance that neither of the 'giants' of the ICAEW at the time appears to have had a preference for a particular system of accounting for price changes. Although Benson was a prime mover in calling upon the Institute to take action, he was much more concerned that *some* action should be taken than that any particular system be introduced: 'he just wanted something done. He wasn't going to go into the details of this method or that. All he wanted was some effective method of accounting for inflation.'[102] Indeed, his biography does not mention the incidents described here at all, although he finds space to pass on a folk remedy for bed-wetting.[103] Sir John Grenside[104] believed that Leach would have been content with a more prescriptive version of the advice in earlier recommendations, that is, a transfer to reserves.[105]

It seems likely that this is one of history's 'A. J. P. Taylor moments', when systemic factors (constraints, inertia, a lack of incentives to take controversial decisions that would reverse its effect) result in a small initial cause having disproportionate consequences.[106] CPP emerged with accumulating momentum from *Accounting for Stewardship*, where it was presented in a particularly palatable way, appealed to all those close to the process because of its simplicity, cheapness, relative objectivity and auditability,[107] – plus, to standard-setters, because of the consequent speed with which a standard could be produced[108] – and was simply not opposed by any key opinion formers with a voice in the decision-making process. The decision by the Council of the ICAEW to remit the wider problems of financial management under inflation to the ASSC was a convenience at the time but probably the beginning of a natural trend to narrowing the discussion, in terms both of scope and the parties involved, that made the final debacle more or less inevitable.

This was a bruising chapter of events for the ASSC: it had been wrong-footed, had lost time that could have been spent on developing alternatives to CPP, and looked likely to be forced to move to a more complex and expensive system with no guarantee that those who backed it in preference to CPP would, in reality, embrace it enthusiastically. On the positive side, whatever emerged from Sandilands would be likely to be more popular with industry and give the ASSC some cover from government, though still with no guarantees that it would be officially approved or enforced.

5 The Holy Grail

> The search for a conceptual framework is a search for the Holy Grail.
>
> Tom Watts[1]

> We are still searching for the Holy Grail.
>
> Bryan Carsberg[2]

Ronald Leach accepted that there was a need for more research into financial reporting methods, to be conducted with the active participation of academics, in an interview given to *Accountancy* shortly before the announcement of the Statement of Intent[3] and, as we have seen, the initial membership of the ASSC included Professor Harold Edey, who was specifically chosen to 'represent ... academic interests'.[4] The ASSC's initial work programme included a study of the 'fundamental objects and principles of periodic financial statements'[5] and the Research Committee of the Institute of Chartered Accountants in England and Wales was asked to 'study the best means of mounting the work, including the extent to which accountants from the academic community could be invited to participate'.[6] In April 1970, Leach reported that the ICAEW was considering going further and 'setting up a working party, in parallel with its present investigation of accounting principles, to carry out fundamental research into the purpose of accounts. It would include representation from academic accountants.'[7] The message was backed up by his successor as President of the ICAEW, Claude Croxton-Smith, whose annual report to the membership in April 1971 stated that, 'much more time and effort must be devoted to fundamental research into the theory and practice of all aspects of accountancy'.[8]

The following month, *Accountancy Age* ran an editorial on the need for a better organized approach to the research input to accounting standards: 'the time must come when the academics and the practitioners sit down and thrash out just what type of research programme the profession requires, who is going to do it, and who is going to pay.'[9] Within days, it was announced that an International Centre for Research in Accounting was to be established at the University of Lancaster, with Professor Edward Stamp moving from Edinburgh to become its Director. Leach was to be chairman of the Board of Trustees and by the end of the year funding of £10,000 per annum for ten years had been

secured.[10] *Accountancy Age* welcomed the development, reporting that it had received 'a number of letters of support' following an earlier editorial on the need for a research centre. It was concerned that the Centre might over-emphasize basic research but regarded Leach's involvement as encouraging.[11] Douglas Morpeth also joined the Board, as did, among others,[12] Lords Kearton and Shawcross.[13] By the end of 1971, Professor Stephen Zeff was interpreting the lack of concrete steps by the ICAEW to implement its commitment to lead fundamental research in financial reporting, and the involvement of Leach in the establishment of the Centre at Lancaster, as meaning that the ICAEW 'was inclined to defer to the academic institutions as regards fundamental research, at least for the present'.[14]

Historically, the small number of accounting academics who could be found in England and Wales generally existed on the margins of the profession and their contributions to accounting policy making were treated with considerable suspicion.[15] Why, then, was the establishment of the ASSC accompanied by a change of attitude to fundamental research and to academic accountants? Three factors appear relevant. First, the forceful critique of financial reporting in the UK offered by Stamp in the run-up to the establishment of the ASSC included a campaign for fundamental research;[16] to the extent that Stamp's criticisms were instrumental in persuading the profession that change was needed, his remedies would be bound to have some attraction. Secondly, the US profession was showing increasing interest in more basic research. The Accounting Principles Board published its Statement No. 4 'Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises' in October 1970 and this covered, among other things, the objectives of financial statements. In April 1971, the American Institute of Certified Public Accountants established what became the Trueblood Study Group on the objectives of financial statements, with the explicit intention of developing APB Statement No. 4 to provide a conceptual underpinning to the work of standard-setters.[17] Finally, the prospect of a source of solutions to the issues of financial reporting that would be in some sense authoritative – and might thus eliminate the wrangling that had accompanied even some of the non-mandatory Recommendations on Accounting Principles[18] – must have been very attractive. Ironically, the profession's distance from any scholarly or intellectual analysis of its problems may well have robbed it of the scepticism that could have warned of the unlikelihood of this attractive outcome materializing.

The Corporate Report

In the event, little was done to study the fundamental objects and principles of periodic financial statements until, in October 1974, a working party of the ASSC was established with the following terms of reference:

> The purpose of this study is to re-examine the scope and aims of published financial reports in the light of modern needs and conditions.

> It will be concerned with the public accountability of economic entities of all kinds, but especially business enterprises. It will seek to establish a set of working concepts as a basis for financial reporting. Its aims will be to identify the persons or groups for whom published financial reports should be prepared, and the information appropriate to their interests.
>
> It will consider the most suitable means of measuring and reporting the economic position, performance and prospects of undertakings for the purposes and persons identified above. The conclusions of this study should be presented in summary or blueprint form not later than June 1975.[19]

The terms of reference embrace the scope of the 'fundamental principles' project included in the initial work programme but in a very wide-ranging way, particularly in referring to 'public accountability'. The context for this was the election of a Labour government in February 1974.[20] At the time of the election, the Labour Party had been preparing recommendations on the reform of company law which included a range of new disclosures and the establishment of a Companies Commission, to be involved in the setting of accounting standards. The report was published in May 1974.[21] In Michael Renshall's words,

> There was a period during the Wilson government when a group of thinking men – industrialists, economists, trade unionists – said capitalism has reached the stage where we can leave profit behind. Profit isn't really the thing that drives business – there's more to it than that. And . . . *The Corporate Report* was a response to a feeling that the social aspects needed to be recognised.[22]

It also appears that suspension of work on price change accounting, following the announcement of the Sandilands Committee in July 1973, left the technical resources of the Institute with capacity to take on a major new project[23] – no history of any regulatory process should overlook the internal dynamic of the permanent secretariat.

The working party was chaired by Derek Boothman, who had joined the ASSC in June 1974. Boothman, a partner in Binder Hamlyn, had not previously been involved in fundamental research; he agreed to chair the working party simply because Leach asked him to.[24] The working party included Stamp himself, and his International Centre for Research in Accounting was commissioned to provide research. The time available for the work precluded any original research, but the Centre carried out a literature survey, organized discussions within the professional bodies, and solicited the views of professors of accounting and the chairmen of 300 major companies; in addition a general invitation to submit comments was issued.[25] One hundred and seven individuals and organizations made submissions.[26]

The working party's deliberations fell somewhat short of a 'blueprint' but were concluded on time and published in July 1975. Their Discussion Paper, *The Cor-*

porate Report, opened with the statement that, 'our basic approach has been that corporate reports should seek to satisfy, as far as possible, the information needs of users: they should be useful.'[27] The group identified a range of potential users, including equity investors, loan creditors, employees, analysts and advisers, business contacts and the public,[28] and argued that 'the fundamental objective of corporate reports is to communicate economic measurements of and information about the resources and performance of the reporting entity useful to those having reasonable rights to such information.'[29] Unstartling as this proposition appears today, it was actually quite a radical development in the mid-1970s for a professional accountancy body – albeit at a distance – to countenance the notion that its principal product should be generally useful; indeed, when an inquiry in the USA reached similar conclusions in 1966, one distinguished American commentator announced that, 'this is a change in "world view" and is the stuff that revolutions are made of'.[30]

The report suggested a number of desirable characteristics for the information in financial reports, including relevance and reliability; the list was similar to that in the Trueblood report of 1973. A review of the present state of corporate reporting concluded that 'because neither business organisations nor the pubic regard the maximisation of owners' profit as the only legitimate aim of business, distributable profit can no longer be regarded as the sole or premier indicator of performance'.[31] Again, radical stuff. The working party identified six new statements to meet the expanded information needs: (a) a value added statement; (b) an employment report; (c) a statement of money exchanges with government; (d) a statement of transactions in foreign currency; (e) a statement of future prospects; and (f) a statement of corporate objectives.[32] It also recommended a 'practically-oriented programme of research and testing to develop a workable and standardised system of current value accounting capable of general application'.[33] In this respect their conclusions coincided with the – widely anticipated – recommendation of the Sandilands committee, signed off shortly before *The Corporate Report* came out but not actually published until September of that year.

Ten and a half thousand copies of *The Corporate Report* were sold.[34] In April 1976 Blackwood Hodge, by happy chance the world's largest distributor of earth-moving equipment, made the earth move by becoming the first company to publish an annual report including all the additional statements proposed by the working party.[35] Although no doubt gratified to have the feasibility of its proposals demonstrated, the working party may have been dismayed that the company's chairman disclosed that he was unconvinced that the information was really wanted and concerned about the additional cost of preparing it.[36]

In the same month, the ASSC (now renamed the Accounting Standards Committee[37]) got round to discussing the report.[38] After a three-hour debate, the committee agreed in principle to accept its broad conclusions and to initiate research into the proposed statements. This conclusion was by no means universally supported; members had concerns about some of the principles and some of the specific recommendations, in particular the statement of future

prospects. Indeed, *Accountants Weekly* reported that the decision was reached only thanks to what it described as the 'decisive chairmanship' of Leach,[39] together with the demonstration of feasibility provided by the accounts of Blackwood Hodge, which were circulated at the meeting. A draft press statement was to be prepared, initially for consideration at the May ASC meeting.[40] After further discussion the following month, the ASC actually issued the statement in July 1976, welcoming *The Corporate Report* as a major contribution to the development of thinking and accepting its main conclusions in general terms.[41] The statement was interpreted as a 'cautious welcome';[42] another publication headlined its report, 'ASC plays it cool'.[43]

The most popular of the new statements in practice was the statement of value added, which set out to report 'the wealth the reporting entity has been able to create by its own and its employees' efforts' and how this had been 'used to pay those contributing to its creation'.[44] Value added statements were included in published accounts by significant numbers of companies for several years; their underlying philosophy chimed with the ethos identified in the earlier comment by Renshall, although the more cynical also pointed out that by disclosing a much larger number than the profit figure, most of which was allocated to the workforce, value added might usefully distract attention from profits thought by workers to be excessively high and by shareholders to be too low.[45] The statement was the subject of not one but two official research studies.[46] Other studies were commissioned on the employment report, segmental analysis and simplified reporting.[47] Employment reports, in the sense in which the term was used in *The Corporate Report*, also enjoyed some popularity among preparers.

In July 1977, the government published a Green Paper endorsing a number of *The Corporate Report*'s proposals.[48] The President of the Institute of Chartered Accountants of Scotland, John Kirkpatrick, told his Institute's summer school that, 'most of us regret the paper ever having been issued . . . [it has] given the government ideas'.[49] However, May 1979 saw the election of a Conservative government with a very different philosophy. The impetus for further development of *The Corporate Report*'s proposals was lost and the ASC once again turned to consider price change accounting.[50] Publication of value added and employment statements fell away. Preparers and the rest of the accountancy profession simply lost interest: '*The Corporate Report* was a creature of its time . . . it's now forgotten and neglected.'[51]

A Conceptual Framework?

Although ED2's title, 'Disclosure of Accounting Policies', implies a concern *only* with the *disclosure* of accounting policies,[52] it accepted that such disclosure ought logically to take place within the context of a clear framework of broad general assumptions. Accordingly, the exposure draft and subsequent standard included four 'fundamental accounting concepts',[53] defined as 'the broad basic assumptions which underlie the periodic financial accounts of business enterprises',[54] namely going concern, accruals, consistency and prudence. Standard practice was to

assume that these had been followed unless the contrary was stated. The list of fundamental concepts was not regarded as complete, the standard merely stating that 'it is expedient to single out for special mention four [concepts] in particular'.[55]

The drafting of ED2's analysis of fundamental accounting concepts was chiefly the work of Renshall, consulting a rather small number of people at Moorgate Place with any interest in the philosophy of financial reporting, including Leach.[56] Renshall recalls undertaking a good deal of desk research, particularly focused on US texts. APB Statement No. 4 'Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises' was adopted in October 1970[57] and would have been a useful source (ED2 was published in January 1971). Previous US publications of relevance include Accounting Research Study No. 1 (identifying fourteen concepts)[58] and Accounting Research Study No. 7 (ten concepts).[59] SSAP2's treatment was a good deal more concise than any of these: APB Statement No. 4 identifies thirteen basic features of financial accounting; six pervasive measurement principles; three modifying conventions; seven principles of selection; seven principles of measurement; ten principles of the determination of the effects of events; and eleven principles of financial statement presentation.

A number of criticisms have been offered of the formulations of fundamental concepts provided in SSAP2, and particularly its approach to prudence and its statement that, where the accruals and prudence concepts are incompatible, the latter always prevails.[60] Nonetheless, they endured throughout the life of the ASC and, indeed, obtained a wider currency.[61]

As noted earlier, at the time of the establishment of the US FASB, the Trueblood Study Group on the objectives of financial statements was at work, and it delivered its report in October 1973. The FASB then embarked on a major – some would say monumental – study of the broad conceptual framework for financial reporting. This 'Conceptual Framework' project was the subject of a Discussion Memorandum issued in June 1974 and then of a series of working papers and formal pronouncements, initially culminating in December 1985, though further work on the project has since been undertaken.[62]

From time to time it was suggested that the ASC should give more attention to the fundamentals of financial reporting, perhaps even establishing a project parallel to the FASB's. During the course of a major review of the standard-setting process, initiated in 1978,[63] a consultative document argued that, 'if an "agreed conceptual framework" is equated with a single undisputed "model", then this is a luxury which evades us at the moment'.[64] Though the FASB intended to take the lead in securing agreement, the ASC seemed to feel that agreement must come about spontaneously within the profession at large. Many of the key submissions to that consultative paper called for a more proactive approach by the ASC. As David Tweedie points out, all six major accountancy bodies adopted this line, albeit with differing degrees of enthusiasm, as did fourteen of the twenty ICAEW Technical Advisory Committees and 'all nine of the "Top Ten" [professional accountancy] firms which included a section on the

conceptual framework in their submission'. Indeed, six of the latter 'explicitly stated that such research was a priority for the ASC'.[65]

There was, in fact, a degree of sympathy within the ASC for the view that an agreed conceptual framework would be useful[66] and it asked the ICAEW to commission research into the possibility of developing such a framework. The research, undertaken by Professor Richard Macve, consisted in a review of the existing state of work on the subject in other jurisdictions, predominantly the USA, to which Macve added some further reflections.[67] The report was published in 1981.[68] His principal conclusion was that,

> Once one starts to ask 'How is accounting useful and how can it be made more useful'? one is launched into what seems to be an endless series of further questions; and immediate clear answers are few and far between . . .
>
> It therefore seems idle to hope for an 'agreed conceptual framework' or general accounting theory of a type that will give explicit guidance on what is appropriate in preparing financial statements, or on what will improve accounting practice. The important thing is that the effort is made, and seen to be made, to ask the relevant questions with respect to users' needs; the methods that can satisfy these and their visible and hidden costs; and possible conflicts between needs . . . This view implies that all accounting research is potentially research into 'the conceptual framework of accounting'.[69]

The report was widely interpreted as concluding that the possibility of an agreed structure was distinctly slim[70] and the ASC did not in fact follow up the project. As a subsequent chairman of the ASC put it:

> We soft-pedalled work in the area of the conceptual framework. This is in danger of becoming the philosopher's stone of accounting: the mineral the discovery of which would achieve the alchemist's dream of a substance which would turn base metals into gold. Accounting is a language, the better it is understood the better it is at communicating information. There is no such thing as a perfect logical structure for a language, nor is there for accounting. I believe that the time and effort put by the Americans into the search for a conceptual framework and the lack of any comprehensive and conclusive progress, indicate that it was right for us to deny large resources to that search. Professor Macve's study carried out on behalf of the ASC confirms the correctness of this approach.[71]

This characterization of the framework as the philosopher's stone – Watts, Carsberg, Renshall and others preferred Holy Grail[72] – like Macve's conclusion, reflects in part the interpretation of the term, as in the consultative document quoted earlier, to mean a structure emerging in agreed form, spontaneously or consensually, from the profession at large. It also reflected the expectation that

the framework would provide direct answers to the technical questions the ASC faced: in effect turning the standard-setting process into a quasi-scientific endeavour. Although this conception of the framework was quite widespread at the time, it was not actually the specification the FASB was working to.[73] The goals of its conceptual project – which significantly did not use the term 'agreed' in its title – stated that it would, among other things, 'establish objectives and concepts that the Standards Board will use in developing standards ... [and] provide guidance in resolving problems'.[74]

A number of purposes for such a conceptual framework can be identified.[75] Some are political and may not be particularly honourable: for example in the period taken to develop a framework standard-setters have an ideal excuse not to issue substantive pronouncements, and other parties have ideal grounds for resisting their issuance. It may be that some of the popularity that the call for the development of a framework has had from time to time reflects such a possibility. Others are less reprehensible and include the potential value of the framework as a way of organizing standard-setters' thinking and subsequent debate; demonstrating the standard-setters' intentions to interested parties; and integrating the rationales behind specific substantive pronouncements. Though these purposes may be less attractive than the ultimate goal of scientific standard-setting, they have their attractions, and work on conceptual frameworks continued in other jurisdictions. In the mid-1980s, the IASC developed its own project, broadly along the line of the FASB's, and its framework was formally adopted in July 1989.[76] Also in 1989, the ICAEW published a set of *Guidelines For Financial Reporting Standards*, developed by Professor David Solomons under commission from the Institute's Research Committee and 'addressed to the ASC'.[77] The guidelines were, in effect, a conceptual framework,[78] broadly similar to those of the FASB and IASC. The chairman of the ASC at the time welcomed the publication of the draft Solomons Report, expressing his 'concern ... about the lack of "even an agreed definition of what constitutes an asset or a liability"'.[79] Very shortly before the end of its life, the ASC, 'agreed to recognise the [IASC's] Framework as a set of guidelines to assist in its work of developing proposals for new standards and revisions to existing standards'.[80]

The Role of Academic Research in UK Standard-Setting

Towards the end of the ASC's life, Anthony Carey, one of its under-secretaries, began a talk with the observation that 'on hearing that I was proposing to speak on the relationship between the Accounting Standards Committee and the academic community, more than one wag commented ... that my talk should not take very long to prepare'.[81] Though he went on to say that in his view, the jest was unfair, he may have had his audience in mind (it appears to have been composed of academics) in offering this opinion and his defence of his position is, to say the least, somewhat lame. He stresses the contribution individual academics had made as members of the ASC and its working parties, but, of course, although they may bring more scholarly attitudes to the table, academics

contributing in that capacity are essentially acting like any other member of their profession. He lists a small number of ICAEW research projects related to ASC topics but his text concentrates largely on projects with little or no involvement of academics. Even these can be welcomed only as background information or the like. No instance of a full-scale academic research study influencing an ASC pronouncement is recorded. He concedes that the number academic responses to the exposure drafts published in recent years is disappointing – the average was actually below two.

Although, as we shall see,[82] it was to make occasional and modest contributions to standard-setting debates, academic research *as such* conducted in the period played little role in the development of accounting standards. Why was this? Early optimism that fundamental research could provide a rigorous underpinning for the improvement of financial reporting rapidly dissolved. The impossibility of finding a universally agreed framework of concepts left individual academics developing their own preferred models for responding piecemeal to individual issues. The timescales of academia mesh poorly with the demands of standard-setters and the career challenges facing modern scholars encourage them to find academically interesting things to say rather than work on the most pressing problems on the standard-setting agenda. From the mid-1980s onwards, a grim dichotomy emerged. The sort of scholarly work that might feed straightforwardly into the standard-setting process would address accounting concepts and be normative and developmental; for example, Carey's speech called for help with questions such as, 'What is the nature of goodwill? What are its identifying characteristics? Does expenditure after acquisition maintain the value of existing goodwill or does it lead to the creation of new goodwill?'[83] Yet work of this sort ceased to be much valued by a community whose methods came to be dominated by essentially social scientific approaches, so that there was little incentive for academics to undertake it. On the other hand, the sorts of research that academics were doing was ill-suited to assist standard-setters, at least on the timescale they need to work on. For example, even individual large-scale econometric studies of phenomena such as the cash-flow consequences of a given accounting policy change are expensive, time consuming, and often difficult to design. Further, limitations of design and data availability often mean that the findings of the first few studies point in different directions and are thus, overall, inconclusive; reliable results emerge, if they emerge at all, as a significant number of studies accumulate, which will take even longer and be even more expensive.[84]

The Legal Framework

At the time of the establishment of the ASSC, company law impinged only lightly on the foundations and structure of financial reporting. It required that annual reports be published (and audited) and identified a relatively small number of specific information items to be included in them. The measurement and presentation of those and other items was left largely to the accountancy

profession. The transcendental legal requirement, that the accounts should show a 'true and fair view' of the preparer's affairs, troubled accountants, directors and auditors very little in practice and remained obscure in what it demanded.[85] The law did, however, allow preparers to depart from its other requirements in order to show this true and fair view.[86]

Over the life of the committee, financial reporting and company law were to draw closer together in two important respects. The degree of prescription of financial reporting procedures by company law greatly increased, largely as a result of the UK's entry into the European Economic Community in 1973. The Community had by then embarked on a programme of company law harmonization, which included financial reporting, as part of its objective of removing barriers to the movement of capital. The programme was implemented via EEC Directives, the contents of which member states were obliged to incorporate into national law.[87] Work on drafting the Fourth Directive, which regulated the accounts of individual companies, was under way at Britain's entry but was incomplete. Early drafts reflected, unsurprisingly, a continental European approach to the regulation of financial reporting, one involving a substantially higher degree of statutory prescription than the Anglo-American model.

British accountants managed to get the true and fair view doctrine inserted into the draft,[88] a move regarded in the UK at the time as a triumph.[89] They did not, however, succeed in getting the prescription taken out, with the result that the final Directive included extensive requirements relating to the basic concepts to be applied (which largely reflected SSAP2's fundamental accounting concepts), measurement rules, formats for the financial statements and terminology, as well as items to be disclosed. Further, the previously rather liberal approach to the true and fair view override was replaced by a structured set of tests; for example it was now clear that, only if there was no way of both complying with other requirements and showing a true and fair view, could the override be invoked. The Fourth Directive was implemented in the UK via the Companies Act 1981, which was then consolidated with all other extant company legislation in the 1985 Act. A Seventh Directive, among other things extending similar provisions to groups of companies, was implemented via the Companies Act 1989. The more prescriptive approach embodied in the new legislation was to impact upon UK standard-setting in a variety of ways, as we will discover in later chapters.

The second way in which the law and accounting standards drew closer was an attempt by standard-setters to enhance the status of standards, mainly with the intention of securing improved compliance and easier enforcement.[90] In 1983 Counsels' opinion was obtained on the role of accounting standards in relation to the true and fair view requirement. The ASC was pleased with the outcome.[91] Weaving through a fairly lengthy text, we find that:

> In the end ... the question of whether accounts give a true and fair view ... must be decided by a judge. But the courts look for guidance on this question to the ordinary practices of professional accountants ... The courts will

> treat compliance with accepted accounting principles as prima facie evidence that the accounts are true and fair ... Thus the value of a SSAP to a court ... is two-fold. First, it represents an important statement of professional opinion about the standards which readers may reasonably expect in accounts ... Secondly, because accountants are professionally obliged to comply with a SSAP, it creates in the readers an expectation that the accounts will be in conformity with the prescribed standards.[92]

Helpful as it may have been, for example in emphasizing that accounting practice could evolve through time,[93] it left a number of loopholes. It pointed out that if a given SSAP did not achieve widespread support, did not, that is, enter the 'ordinary practices of professional accountants', it would not become part of 'accepted accounting principles' and thus compliance would not be necessary. This, in effect, gave preparers an incentive to rebel in crowds rather than individually.[94] Nor did the opinion resolve the paradox that, although in the generality of cases it might be necessary to comply with standards to show a true and fair view, in any particular case it might be essential to depart from such standards with the same objective, yet preparers and others are given no criterion by which to judge into which category an individual set of circumstances falls.[95] Perhaps unsurprisingly, there is little evidence that the opinion was of great assistance to the ASC in practice in securing compliance.

The Political Economy of Standard-Setting

In the early days of standard-setting in the UK, accounting standards were thought of predominantly as technical instruments – as tools to improve the functioning of the financial reporting machine.[96] This view is implicit, in some cases explicit, not only in the way in which the profession engaged in the process but also in the writings of commentators at the time. An example is the analysis of standardization offered by Professor Peter Bird, which we examined in chapter 2. Since accountancy is a technology, the view of standards as technical devices was, and remains, an important dimension in the debate.

In the UK, as in other countries, the attempt to shape financial reporting with pronouncements carrying at least some mandatory force rapidly exposed what have come to be called the *economic consequences* of changing accounting policies.[97] Although the term has been defined in a variety of ways,[98] in its broadest sense it refers to changes in the distribution of wealth that result from, or are perceived to result from, changes in accounting policy via their effect on the accounting numbers disclosed in financial statements. One classification of economic consequences[99] distinguishes between compliance and analysis costs, mechanistic consequences and judgmental consequences.

One accounting policy may simply cost more to comply with than another, especially if it involves disclosing substantially more information. The ASSC began quite early to respond to the argument that the cost-benefit calculation might differ between categories of preparer, for example excluding small

companies from the scope of SSAP10,[100] though the calculation of the balance of benefit is inevitably very impressionistic.

Mechanistic consequences arise when accounting numbers are directly linked to decisions, whether as a result of regulatory structures (including the tax system) or by contractual arrangement. SSAP6's changes to the recognition of stock and long-term contracts were, as we have seen, controversial in part because of the tax implications of the changes.[101] Contractual consequences arise, for example, if debt covenants include a gearing restriction based on the financial statements.

Judgmental consequences are those that arise as a result of changes in the way users and other parties perceive the reporting entity and thus the judgements and decisions they make about it. Classically, at the micro-level, investors may sell shares because of a perception that profitability has fallen when in fact the reduction is a result of the application of a different accounting policy with no implication for the underlying situation of the entity. This may cause the entity's share price to fall, reducing the wealth of other investors and endangering the position (and therefore wealth) of management and others. Although there is now considerable evidence to suggest that the market does not respond naively to such 'cosmetic' changes in accounting numbers by assuming that they are entirely attributable to underlying events, this mainly dates from after 1970 and, in any event, the balance of evidence remains today compatible with scepticism about investors' capacity to discriminate fully between cosmetic and meaningful differences in accounting numbers in all cases.[102] The demand for, and resistance to, merger accounting encountered by the ASSC was linked in part to beliefs about how users would react to the changes in accounting numbers that would ensue.[103] As well as micro-level consequences, changes in accounting policies may have macro-level effects because 'a range of users are influenced in a way that affects the political, economic and social climate'.[104]

Where there are economic consequences, there will be significant and systematic 'political' activity; activity, that is, by parties to the standard-setting process (such as preparers) with vested interests and apparently designed to further those interests rather than to remedy technical defects in financial reporting or proposed standards. Of course, the positions taken by those pursuing their own interests are often defended in technical terms but, for a variety of reasons, it does not always seem plausible that the disinterested pursuit of higher quality financial reporting is the motivating force behind the positions taken. Such behaviour was to be observed even in the honeymoon period of the ASSC: examples include self-referential lobbying on accounting for extraordinary items and positions taken on overheads on stock and the recognition of long-term contracts.

Few technical processes of any significance are entirely exempt from political influence. Engineers designing a bridge, for example, take decisions about the type, quality and quantity of materials to use based on data from the physical sciences about strength, loadings, tolerances and so on, but they are also likely to be influenced by questions such as the acceptability of the design to the local

population, the willingness of paymasters to fund the cost and social attitudes to risk. It is possible, at least in principle, to separate out these two kinds of influence on the decision, and thus retain a purity about the engineering specification. In practice, though, there may be areas (for example a forecast of the way a new material may react to long-term exposure to climatic conditions) where it is difficult to take a decision, or at least to demonstrate that it has been taken, wholly on the basis of disinterested technical considerations.

One reaction to the intrusion of political activity into the standard-setting process is to demand that it be reversed: to seek a renewal of the purity of the standard-setting technology. This approach underlies Solomons' famous call for financial reporting to be like cartography:

> Accounting is financial mapmaking. The better the map, the more completely it represents the complex phenomena that are being mapped. We do not judge a map by the . . . effects it produces. The distribution of natural wealth or rainfall shown on a map may lead to population shifts or changes in industrial location which the government may like or dislike. That should be no concern of the cartographer. We judge his map by how well it represents the facts. People can then react to it as they will.[105]

As Peter Taylor and Stuart Turley point out, focusing on the potential for standard-setting to be a purely or at least predominantly technical process has advantages (political advantages, it has to be said) for a self-regulatory body acting within the accountancy profession. If the process comes to be seen as concerned with mediating between the conflicting interests of a variety of parties, many of them not accountants, the argument for it to be carried out by a political body with a more credible claim to be able to balance such a range of interests, is considerably strengthened.[106] Where the regulatory authority has weak powers of enforcement, it can ignore political pressures only by running the risk that technically superior pronouncements will not in fact be followed, and if it does so, its credibility is simply undermined from a different direction.

Academic investigation of the standard-setting process came to raise a profound question about the relationship between the political and the technical, namely whether, even in principle, the two could be separated. What may be easy in principle, and feasible within limits, in dealing with an activity, such as bridge-building, that takes place in the physical world, may not be possible for an activity that seems to be located in the mental world of individuals and the social space of their interactions. Some have argued that the political and the technical are inseparable because of the practicalities of financial reporting. In response to Solomons' advocacy of financial cartography, for example, David Tonkin[107] pointed out that only one chart per entity per period is produced, inevitably meaning that choice has to be made about what aspects of the financial 'ground' should be plotted: such choice ought to reflect an appropriate adjudication between users' needs, which can only be arrived at by political means.

A more radical view, pioneered by Professor Ruth Hines, Professor Tony Tinker and others, is that accounting is concerned not to find the means of *reflecting* some underlying set of brute facts which, however complex, can with sufficiently powerful technology be successfully charted, but to construct or constitute the reality of the financial reporting world.[108] On this view, for example, the issue is not whether overheads *are* costs of the period or of inventory, or whether certain sorts of outflows *are* a component of periodic profit or a reduction in capital, but how the financial reporting world is constituted to make them one or the other (or to retain the flexibility for them to be both). Another such issue arose in connection with the apparently rather obscure question of the treatment of ACT on dividends.[109] For Hines and Tinker, standard-setters are engaged in an irredeemably social (and therefore political) process and some, including Hines, have argued that any attempt to reduce the process to the technical, for example by devising a conceptual framework like the one discussed earlier in this chapter, is doomed to fail.[110]

The present volume is a work of history and does not seek to resolve the competing positions of the various parties to this particular debate; in interpreting events in the life of the UK's standard-setting machinery, however, it is useful to be able to view them through a number of different lenses.

6 The Going Gets Tougher: 1975–1979

In February 1976 the ASSC's constitution was significantly amended. The Chartered Institute of Public Finance and Accountancy joined the committee, which now embraced all six senior UK accountancy bodies. The six were given, at least formally, equal status as 'governing bodies'. They had set up a Consultative Committee of Accountancy Bodies in 1974, to co-ordinate activities in matters of mutual interest, and the ASSC now became a joint committee of the CCAB. The Institute of Chartered Accountants in England and Wales still held a brute majority of places on the committee, twelve out of twenty-three, with the Institute of Chartered Accountants of Scotland having three places and the remaining bodies two each. From now on the drafting of pronouncements would be undertaken by sub-committees of the ASC itself rather than within the committee framework of the professional bodies (and mainly the ICAEW).[1] Finally, the word 'steering' was dropped from the committee's title, so that it became the Accounting Standards Committee (ASC).[2]

The reason for dropping the word 'steering' is nowhere officially recorded. The term 'steering committee' was in fashion at the ICAEW at the time of the ASSC's creation and its use in this case might have been intended to reassure members of the ICAEW Council that they would remain in control.[3] It does seem to have been the shift in responsibility for initial drafting work from the professional bodies' technical machinery to the ASC itself that triggered the renaming although the change can be characterized alternatively as a 'coming of age'[4] or a descent from being an 'Olympian force', guiding the inhabitants of the professional bodies' technical communities.[5]

The new constitution, like the old, made it clear that, 'the Committee shall be assisted by the staff of the Technical Directorate of the ICAEW.'[6] Staffing levels within the directorate were increasing significantly. In 1970, there were 14 staff costing £140,000; by 1976 the number had risen to 28 and the cost to £300,000, although two-thirds of this was now covered by contributions from other CCAB bodies and sales of publications.[7] By 1978, there were two professional staff within the directorate working full-time for the ASC.[8] Michael Renshall left the staff of the ICAEW in 1977 to take up a partnership in Peat Marwick Mitchell & Co. and James Carty became secretary of the ASC.

At the end of June 1976, the ASC's founder chairman, Sir Ronald Leach, stepped down. He had served six and a half years, a record that would never be beaten. His replacement, Sir William Slimmings, was a member of the ICAS; his appointment recognized the enhanced involvement of the other CCAB bodies (there would never be another chairman from outside the ICAEW) and also his role in bringing the Scots into the community of accounting standard-setters at the inception of the committee's work. He came from a working-class background, becoming an apprentice to A. C. Phillip and Company in 1929, winning a prize in his finals, and joining Thomson McLintock & Co. on qualifying, apparently because, alone of all the firms he approached, they offered to pay his interview expenses. He became a partner in 1946 and went on to become senior partner.[9] Douglas Morpeth continued as vice-chairman of the ASC.

Slimmings served his two-year term and was replaced by Thomas (universally known as Tom) Watts, technical partner at Price Waterhouse. Watts had begun training in 1934, when his father took him into the firm's offices, answered the questions on his behalf, 'put down the 500 guineas and that was that'.[10] He became a partner (and the firm's first technical partner) in 1963 and joined the ICAEW Council in 1974. As a consequence of the 1976 restructuring, Watts' appointment was subject to approval by the CCAB, and this was agreed at its January 1978 meeting.[11] He was already a member of the ASC and well known and widely respected for his technical expertise. He was also regarded as 'the UK profession's leading representative in European and EEC affairs',[12] an important area for the committee's work. *Accountancy Age* heralded his appointment as the conclusion of a 'search for a forthright personality to steer the profession's ASC through a period of mounting criticism'.[13] Though a man who knew his own mind, Watts had a reputation for diplomacy and consensus building and was to demonstrate these skills in abundance during his term of office.[14]

When Slimmings retired, his place as a representative of the ICAS was taken by James McKinnon, finance director of the Imperial Group. This brought the number of members of the committee from outside public practice to a majority for the first time: 12 to 11.[15]

Another change was the expansion of the consultative machinery. The Plenary Committee structure was abandoned in favour of a separately-constituted Consultative Group, whose membership rose in 1976 from ten to twenty-one organizations, and now included the Trades Union Congress, the Confederation of Small Businesses and representatives of the pension funds sector.[16] By 1978, a further three bodies had joined.[17]

At the time Watts' appointment as chairman was announced, it was disclosed that he would lead 'an urgent review of the entire standard-setting process'.[18] Although it was originally intended that Watts would take over at the end of March, at the same time as Slimmings retired from practice,[19] in the event Slimmings stayed until 30 June (which became the normal 'hand-over' point for the chair) to allow Watts to devote himself to the review.[20] It led to extensive

changes in the structure and operation of the ASC, which are described in chapter 7.

In June 1973, accountancy bodies from nine countries, including the UK, established the International Accounting Standards Committee (IASC) under the chairmanship of Sir Henry Benson.[21] The objectives of the IASC were 'to formulate and publish in the public interest, basic standards to be observed in the presentation of audited accounts and financial statements and to promote their world-wide acceptance and observance'.[22] The accountancy bodies subscribing to the agreement accepted a responsibility to 'use their best endeavours' to obtain acceptance of its standards.[23] The IASC recognized that, given the nature of its task, it would be important to 'confine [its standards] to essentials' and 'not . . . make them so complex that they cannot be applied effectively on a world-wide basis'.[24] Many UK accountants assumed that, since the IASC's standards were to be 'basic', they would have no impact in the UK, with its much more sophisticated approach. They were rapidly proved wrong: in March 1976 the IASC approved a standard on consolidated financial statements, on which there was no UK equivalent.[25]

The Business Community Stirs

By 1975, the ASSC's honeymoon was over. Two standards were giving particular difficulty, SSAP6 'Extraordinary Items and Prior Year Adjustments' (which had an implementation date of 1 January 1974) and SSAP9 'Stock and work in progress' (1 January 1976).

In May 1975, a special report in *Accountancy Age* began:

> SSAP6, for all its good intentions, has succeeded in creating extraordinary confusion. The first annual reports to fall under the rule of the sixth standard are flooding off the presses and are gathering almost more qualifications on this one standard than on the other seven put together. On top of that, there are a wealth of items which are being treated as extraordinary items here, taken direct to profit and loss there and falling under capital reserves somewhere else.[26]

In addition, a number of technical problems with the standard emerged and, though relatively minor, caused adverse publicity. The first was raised by the insurance sector, which claimed that the disclosure requirements purported to override the sector's Companies Act exemptions with respect to 'inner reserves'. The ASSC responded by proposing an amendment to the Explanatory Foreword indicating that in any conflict between the law and standards, the law prevailed.[27] The second concerned investment trust companies, who argued that, as they were not permitted by their constitutions to distribute profits on the sale of investments, it would be misleading to include those profits above dividends in the profit and loss account. This point had been made to the ASSC at the exposure stage but the ASSC's conclusion was that non-distributability did

not affect a surplus' status as profit, so that the appropriate response would be to make a transfer between reserves. This did not satisfy the sector, which renewed its lobbying after the standard was published. The ASSC then reversed its position, agreeing, in December 1974, to an amendment exempting investment trusts. The Association of Investment Trusts was permitted to inform its members that an exemption was on the way. Unfortunately, the amendment then had to be approved separately by the councils of five accountancy bodies, a process that inevitably took several months. Approval by the ICAEW Council, always the last in the chain under the ASSC's pre-1976 constitution, took place in April 1975 and the revised version of SSAP6 carries this date although it was not published until July, apparently because the printing was tied into the production of SSAPs 9 and 10. As a result of the cumulative delay, several investment trusts found themselves receiving qualifications although an exception was being recommended by the ASSC.[28]

When SSAP6 was originally issued it explained that the ASSC intended to develop a separate standard for foreign currency translation. In the event, the treatment of surpluses and deficits on translation was probably the area in which the greatest variety of practice was exposed. The May 1975 special report in *Accountancy Age* carried a table setting out the treatments adopted by 29 companies, almost all of them household names, including ICI, Tube Investments and Esso. Ten different policies can be identified among the 29 preparers and the most popular is followed by only a quarter of the sample. Another area in which several policies, each with considerable support, were being followed was the treatment of gains and losses on the revaluation and sale of fixed assets. In September 1975 the ASSC issued ED16 'Supplement to "Extraordinary Items and Prior Year Adjustments"', addressing these issues. Publication came only four months after the approval of revisions to SSAP6, which itself came only a year after the original pronouncement. The standard section of ED16 ran to only five paragraphs; those dealing with revaluations and realizations of fixed assets had not been taken any further at the time of the review of SSAP6 in 1983,[29] while those addressing foreign currency translation were superseded by ED21, which itself was overtaken by ED27.[30]

The principal areas of controversy arising in connection with stock were the use of base stock and LIFO, the inclusion of overheads and the write-down to market value. Base stock was used mainly by primary commodity processors: the level of stock deemed to be that required for 'normal' operations is maintained in the balance sheet at the price for which it was initially purchased, so that gains from stock-holding in a period of rising prices are excluded from profit. Proponents argued that, 'by maintaining this constant valuation ... the true operating results of the company are reflected'.[31] There was also concern that abandonment of the method would have tax (and thus economic) consequences. The method had not been permitted for tax purposes for some years; in the mid-1970s, however, in response to the rapid inflation then being experienced, the tax regime had been altered – on a temporary basis – to provide a measure of relief on stock profits.[32] Some companies were apparently intending, at the point

at which the government contemplated ending this system, to argue for the reintroduction of base stock for tax purposes and thought that its withdrawal from financial statements would undermine the argument.[33] Lead Industries continued to employ base stock after the implementation of SSAP9 and provided a 400-word justification for its use.[34] Its auditors supported the decision and, accordingly, did not qualify the accounts. Tate & Lyle also continued its use of base stock for periods after SSAP9 applied, with its auditors indicating that they concurred with the basis of valuation.[35]

Several major companies, including BOC and Tootal, continued to employ LIFO in consolidating the results of US associates, apparently for fear of the tax consequences of abandoning the method. LIFO was permitted in the USA for tax purposes, provided that it was also employed in the financial statements.[36] Tootal apparently believed that, to move to an acceptable method for the UK consolidation, it would have to adjust the carrying amount in the US subsidiaries' statements. The group declined even to disclose the amount of the departure in the UK, for fear that, if it was also disclosed by the US subsidiary, this would jeopardise its tax position, while if it was not so disclosed, the SEC would take action.[37] Companies declining to include overheads in stock included Wedgwood, Dowding & Mills and Steetley,[38] the first two receiving audit qualifications as a result.

SSAP9 also covered long-term contracts, the carrying amount of which had normally to include attributable profit – the percentage of completion method.[39] This had direct economic consequences for preparers because the uplift in carrying amount, at least for new contracts, would become chargeable to tax earlier than under the completed contracts basis.[40] The finance director of Crown House, Peter Edge-Partington, stated in the company's 1975 accounts that the method was 'not only imprudent but bad accountancy';[41] it was not, of course, obliged to adopt the method for those accounts and did not do so. A year later Edge-Partington appealed to the ASC to defer implementation of the standard and was turned down. He was supported by the finance director of Wimpey, Harry Norris, who had been due to take a seat on the committee but subsequently declined to do so: 'I approached the Institute on the same lines and got a dusty reaction.'[42] Edge-Partington took up a full page in the 1976 accounts (SSAP9 still did not apply) to protest about the new method.

However, opposition was rapidly crumbling and, in September, a representative of the ASC claimed that only two construction companies were still refusing to adopt the percentage of completion method.[43] Indeed, in April 1977, Norris himself said that 'the flexibility of the standard should allow most contracting firms a way of complying'.[44] Two months' later, a survey of construction company accounts in *Accountants Weekly* found that,

> among the large contractors who have just turned over to the new procedure are George Wimpey, John Laing and Taylor Woodrow ... Full blooded opposition ... does continue in some quarters. Tysons (Contractors) is one company that has refused point blank to adopt the standard.[45]

In fact Tysons did include some attributable profit but recognized only two-thirds of the total, on the grounds of prudence. This departure resulted in a qualified opinion from 1976 to 1978. In the following year, the company complied with SSAP9 while refusing to comment on reasons for the change.[46]

Despite its well-publicized conservative approach to contract valuation,[47] one company that did not contribute to the public debate was GEC. In its accounts for the year ended 31 March 1976, the last year before SSAP9 applied, the company used the completed contracts basis[48] but in the following year its policy was described as follows:

> Profit on long term contracts is taken when the outcome of the contract can be assessed with reasonable accuracy; due to the nature of contracts undertaken this usually occurs when contracts are completed or part deliveries are made and invoiced to customers.[49]

No restatement of the preceding period's figures was necessary and the audit report was unqualified. It can thus be inferred that the auditors accepted as reasonable the statement that the outcome of contracts could only be assessed with reasonable certainty at their completion or on part-delivery.

Thus most objectors found, in Norris' words, 'a way of complying', and even the small number of high profile opponents who published their first financial statements after the introduction of the standard without complying, such as Tysons, moved to apparent compliance within a few years. It has been argued[50] that these events are consistent with a degree of 'creative compliance', that is, using regulations to escape regulatory control without actually violating the regulations.[51] The tactic, appreciated more rapidly by some preparers than others, would have consisted in pushing the scope for applying genuine caution in determining the point at which the outcome of the contract can be 'assessed with reasonable certainty'[52] so far that the profit recognition profile approached that under the completed contracts method.

Press reports of audit qualifications and defiant rhetoric were by no means limited to SSAPs 6 and 9. For example, on 30 April 1976, *Accountants Weekly* carried a story under the headline, 'Bowater Group rejects SSAP8',[53] and a fortnight later the same magazine reported that Guest, Keen and Nettlefolds had decided to 'launch a powerful attack on current accounting standards in a foreword printed on the inside cover of its annual report'.[54] Readers of *Accountancy Age* and *Accountants Weekly* encountered stories of major companies flouting standards and receiving qualifications on a regular basis. Regardless of the generality of company behaviour, these high-profile cases were bound to have some effect on perceptions of the impact and success of the standard-setting process. Of course, these magazines were a recent innovation in the UK – the first to arrive on the scene, *Accountancy Age*, began to appear on 5 December 1969, just days before the publication of the Statement of Intent – and needed to attract their readers' attention to build up circulation. Further, non-compliance sometimes lasted only for a year or two and sometimes, indeed, was only *prospective*:

companies threatened to defy a newly-published standard but actually complied when the implementation date arrived.

So what was the true position? An obvious source of information is the ICAEW's annual survey of published accounts. Unfortunately, in many instances it is not apparent from the published information whether standards have been followed in detail. The information that can be gleaned from the survey suggests that there was a moderate degree of non-compliance. For example, as far as the basis of stock valuation is concerned, the volume for 1977/78, the first year in which SSAP9 applied to all accounts in the survey,[55] reveals that, of 320 instances (some companies in the 300 used more than one basis), cost is used 19 times, cost or under/cost less amounts written off, 4 times (non-compliance unless the write-down is to net realizable value, in which case, why not say so?), lower of cost and replacement price, 4 times, bases 'considered appropriate', twice (presumably not lower of cost and NRV or, again, why not say so?), and 'miscellaneous bases', twice. It would appear, then, that almost 10 per cent of the instances involve a breach of the standard. The survey also shows that there is some continuing use of LIFO for US subsidiaries (14 per cent of instances) and base stock (6 per cent).

An alternative approach is to look at audit qualifications for non-compliance, although this has its own difficulties. It assumes, of course, that unjustified non-compliance always results in a qualification. Further, in the mid-1970s the format of auditor's reports was less tightly regulated than now, sometimes making it difficult to determine if a report had been qualified.[56] Nonetheless, by January 1976 *Accountancy Age* had accumulated a list which showed that more than 100 quoted companies and nationalized industries had had their accounts qualified in the previous year; what's more, the list 'show[ed] that many – including Barclays Bank, Wimpey and ICI – departed from the ASSC's standards'.[57] The widely-publicized departures of ICI (concerning SSAP4) and Barclays (SSAP6), unjustified in the sense that they resulted in qualifications, were not followed by appearances before the professional disciplinary machinery of the accountancy bodies. Indeed, Barclays was apparently 'astonished' when the press enquired about whether such an appearance had been proposed.[58]

In February 1976, the president of the ICAEW, John (later Sir John) Grenside, let it be known that Touche Ross had agreed to second a member of staff to the ICAEW to, as *Accountancy Age* put it, 'monitor company accounts'.[59] The article began, 'a clamp-down on breaches of accounting standards is to be carried out by the English ICA'. However Grenside put it rather differently:

> I am concerned with how best to monitor the application of accounting standards, especially since some of the more recently agreed standards are not easy to implement . . . [T]his [is] not a spying exercise. It is to enable us to see whether the lack of implementation indicates a defect in the standard itself.[60]

In parallel with the study, the ICAEW sought information from the big accountancy firms about their routine monitoring of compliance with accounting

standards. Their replies indicated that this monitoring was carried out on quite a substantial basis.[61]

In the event the exercise became a review, not of compliance or of accounting standards, but of audit qualifications. The final version was circulated to members of the ASC and the secretaries of the CCAB bodies in November 1977.[62] The report examined in detail the 300 companies in the 1976 ICAEW survey of published accounts, a random sample of 100 companies listed on the Stock Exchange and all references to qualifications appearing in the press. The number of qualifications identified was 146, of which 39 related to non-compliance with accounting standards or generally accepted accounting practices. Renshall (by then at Peat Marwick Mitchell) welcomed the report because, 'it demolishe[d] the myth that qualifications on account of departures from SSAPs have become so numerous as to devalue audit reports'.[63] Nonetheless, it remained unpublished.

The rather more limited information that was published, at somewhat greater distance from the ICAEW, via the annual survey, continued to appear. As Table 6.1 shows, it revealed a fairly uniform rate of qualifications, a little below 5 per cent, despite the rising number of standards in force. Special comments also ran at about the 5 per cent level. A situation in which one in twenty companies, some among the largest and best-known in the country, are failing to comply with at least one standard, and without any justification that satisfies their auditors, is surely unsatisfactory; at the same time it is far from the catastrophic rebellion readers of the weekly press might have imagined was taking place.

One concern for the profession was that significant numbers of qualifications for non-compliance with standards, especially when the detail of the departure is difficult to follow and the non-compliance is robustly defended by preparers, would reduce the impact of qualification itself. Such qualifications can be characterized by preparers as of little or no importance – the phrase, 'technical qualification' tends to be deployed – and if so-called technical qualifications became too widespread the credibility of the audit more widely may suffer.[64] If

Table 6.1 Qualifications and special comments on non-compliance with SSAPs and GAAP

	Qualifications		Comments	
	No.	Per cent	No.	Per cent
1975/76	10	3.3	6	2.0
1976/77	10	3.3	14	4.7
1977/78	6	2.0	13	4.3
1978/79	11	3.7	13	4.3
1979/80	13	4.3	15	5.0

Source: Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1977*, London: ICAEW, 1978, and Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1980*, London: ICAEW, 1980.

it becomes accepted that qualifications are technical, this in turn leads to the argument that standards are at fault for causing them:

> Howard Macdonald, Group Controller of Royal Dutch Shell . . . came down heavily against 'technical' qualifications in auditors' reports . . . These were meaningless and served only to devalue the audit report . . . There should be more willingness to amend standards. They should be drawn up with sufficient flexibility for people from industry to be able to pursue their judgement when preparing accounts.[65]

Where departure from a standard does not result in a qualification, the challenge to standard-setting and the profession is different, but no less problematic. It suggests that there are deficiencies in the financial reporting process – either the standard or the audit is defective. Where auditors are not censured, the implication is that the standard is in some way deficient.

As we saw in chapter 2,[66] the Stock Exchange's listing agreement offered only limited support for standards, and the Exchange was apparently keen to make this clear:

> The Stock Exchange this week denied that it has any obligation to compel listed companies to comply with accounting standards. Chartered accountant Jeffrey Knight, deputy head of the quotations department which has responsibility for the accounts of listed companies, stated that the only requirement is that a company should disclose where it has departed from a standard.[67]

At least, surely, undisclosed non-compliance would be caught by the Exchange? Here is Knight again:

> We feel that we are in the second line and we don't attempt to do a critical survey of the accounts of every company to see if they have been complying. We just aren't capable of that. We lend our weight in principle.[68]

Deferred Taxation

The ASSC was now beginning to approach some of the less tractable problems on its technical agenda. One was the question of how financial statements should reflect timing differences between the recognition of expenses in the financial statements and their availability as a deduction from taxable profit. The classic case is the cost of using plant and machinery, which is spread over its expected useful life in the profit and loss account via depreciation charges but may be allowed against taxable profit on a much more rapid basis – even 100 per cent in the year of acquisition – for example as an incentive to industrial investment. In a period of particularly heavy investment, the tax to be paid will

be substantially out of line with accounting profit. If no adjustment is made, naive users of the financial statements may think that the high level of profit after tax reported for the period can be repeated in future years, whereas, if investment, and therefore allowances, drop substantially, post-tax profit will also fall. Although more sophisticated users may be aware of the general problem, they will be unable to make any detailed calculation of the likely impact of this reversal.

When methods of adjusting for the impact of timing differences first came into use, the system was typically referred to as 'tax equalization', a description that gives a clear indication of what at that time was taken to be its objective.[69] The first formal use of the term 'deferred taxation' came in ICAEW Recommendation on Accounting Principles N27,[70] issued following the passage of the Companies Act 1967, which itself explicitly permitted the use of methods to avoid undue fluctuations in taxation charges. N27 recommended that deferred taxation should be accounted for on all originating differences (that is, full provision), with the balance maintained at current tax rates (the liability method). Full provision was argued to be appropriate, even though further originating differences (for example new capital expenditure) might postpone any actual payment of tax for the foreseeable future: 'the fact that as elements of [the] liability mature they are replaced by new deferments does not alter the character of the balance.'[71] The liability method was preferred to the alternative, deferral method, which treats the initial transfer as an effort to equalize the charge, with any error emerging as the transfer is reversed, because:

> The deferred taxation account is intended to provide for a future liability ... [and], as changes in the rate of corporation tax take place, it should be recognised that the basis on which past provision has been made has become out of date.[72]

Deferred taxation was on the ASSC's initial work programme and SSAP2 listed the topic as an area in which different accounting bases – the liability method and, disregarding N27, the deferral method – were used. According to the 1971/72 ICAEW survey of published accounts, 249 of the 300 companies surveyed provided for deferred taxation, and in the following year, still before any ASSC pronouncement had been issued, the figure had risen to 265 (in only four cases, however, was it apparent that no provision was necessary).[73] Although the survey was not able to distinguish the method employed in all cases, 'descriptions ... imply the use of the "liability" system is much more commonly than the "deferral" system'.[74]

In May 1973 the ASSC published ED11 'Accounting for Deferred Taxation'. The draft had been under development for some time: David Hobson reported to a conference in June 1972 that an exposure draft on the subject would be published 'within the next few weeks'.[75] It followed Recommendation N27 in proposing full provisioning but switched from the liability to the deferral method. Two reasons for preferring deferral were given. The 'major argument

against the liability method is that the adjustment required to then existing deferred taxation balances when there is a change in the rate of tax may have a significant but misleading effect on the profit or loss and earnings per share for that year.'[76] At the time of publication of ED11, the government was in the process of introducing a new system of company taxation (the imputation system) which was expected to result in a substantial increase in the rate of corporation tax, from 40 per cent to about 50 per cent;[77] it was also predicted in some quarters that the rate would fluctuate much more widely than hitherto.[78] While it is clear that a change in the tax rate may have a *significant* effect, whether this is *misleading* depends in part on whether one considers that the amount of a liability has changed. The other argument was, 'the conclusions reached by the Accountants' International Study Group in 1971 and the approach adopted in the majority of countries where this subject has been studied.'[79] The deferral method was specified in the USA by APB Opinion No 11 'Accounting for Income Taxes', adopted in 1967.[80]

The summary of responses to ED11 prepared for members of the ASSC[81] showed that 120 submissions were received. Forty six companies responded, of which 18 were identified as definitely supporting some system of deferred taxation and eight as opposing such a system. Of those companies explicitly expressing a preference, twenty-five favoured the liability method and only one deferral; submissions from preparers thus reflected the system most widely used in practice. Support for the liability method was also very substantial among representative bodies (six favoured the liability method and none deferral) and practising firms (fourteen favoured the liability method and two deferral). A major source of criticism was the weakness of the rationale for moving away from the most common system then in use; respondents tended to favour allowing alternatives rather than ruling out deferral.[82]

Some criticism was also levelled at the requirement for full provisioning when a combination of inflation and the system of tax allowances made it unlikely that there would be substantial net reversing differences – the deferred tax balance would simply go on growing. An editorial in *The Accountant* reported 'transatlantic experience showing that the drawdown from published deferment provisions might be of the order of 2 per cent'[83] and raised the possibility of discounting the future liability. The magazine reported the publication of the accounts of Courtauld, in which their auditors gave 'what must be regarded as tacit support', by not qualifying the accounts, for a decision not to provide for further deferred tax. It also quoted Eric Frye, Finance Director of Plessey, as saying that 'tax equalisation not only negates part of the Government's incentive intentions on accelerated capital allowances, but also creates an artificial accounting reporting position which cannot be wholly in the interests of current shareholders'.[84] It is argued that full provisioning is not in the interests of shareholders because they will misinterpret balances as short-term liabilities, and thus undervalue the company, possibly selling their shares too cheaply. If true, this would constitute an economic consequence of an accounting policy.[85]

Another criticism of the draft was its complexity: it ran to 24 pages, of which half were taken up by appendices containing a series of worked examples. An article in *The Accountant* summarized complaints about complexity made in the national press including one suggestion that the draft was, 'a theoretical document completely divorced from the practicalities of commerce'.[86] The article also suggested that, because of its complexity, ED11 was undermining the standard-setting process in general.

The ASSC's response to resistance to the deferral method was to permit either the liability or the deferral methods to be used – a step backward from its mission to narrow areas of difference. However, the danger that the need for large adjustments under the new tax regime would make the liability method less popular than it had been, the need to assist companies affected by US pronouncements, and the political difficulty of carrying out a complete reversal in direction increased the attractiveness of permitting choice of method. The arguments nonetheless delayed the production of the standard, SSAP11 'Accounting for Deferred Taxation', which appeared in August 1975. Full provisioning continued to be required. The number of examples was substantially reduced, despite the doubling in the number of methods permitted.

The new standard was to come into effect for periods beginning on or after 1 January 1976. Although its gestation had been prolonged, the vote at the ASSC was unanimous[87] and some members of the committee, at least, did not expect that the standard itself would cause substantial difficulties.[88] Unfortunately, events were to prove them wrong. Ironically, the potential problem that the ASSC went to such lengths to avoid, the impact of adjustments caused by tax rate changes under the liability method, would not in fact have arisen: the corporation tax rate introduced under the new system, actually 52 per cent, had not changed by 1982.[89] What did happen was that originating differences continued to outstrip reversing differences, so that deferred tax balances went on increasing for many companies. The first year tax allowance for plant and machinery had been set at 100 per cent in 1972 to provide fiscal incentives for industrial investment. By 1974, annual inflation was running in double digits and in May 1975 it reached 25 per cent, so that a constant real level of investment in plant generated ever larger allowances. In 1974, a government under considerable pressure to relieve industrial companies of the burden of taxation that they were suffering as a consequence of the use of historical cost amounts in tax computations, granted 'stock appreciation relief' on the rising value of their stocks.[90] The impact of these factors caused deferred taxation (originally referred to, let us recall, as tax *equalization*) to mushroom – from less than 5 per cent of shareholders' funds in 1971 to about 20 per cent five years later.[91] Furthermore, the impact varied between industries so that, in the construction sector (which was a particular beneficiary of first year allowances), the deferred tax balance had reached almost exactly one-third of shareholders' funds by 1976, and, for wholesale distribution (which benefited from stock relief), the figures were almost as large.[92]

Industrial opposition to SSAP11 was led by the Confederation of British Industry, which let it be known[93] that a working party of members of its taxation committee, chaired by Reginald Pickerill, president of the Institute of Taxation, was drafting a statement calling for the standard to be reconsidered. Pickerill was a well-known opponent of deferred taxation, having published in the professional press a response to ED11 under the headline, 'Hocus-pocus'.[94] He was also Taxation Manager of Plessey, whose opposition to deferred taxation we have already encountered.[95] The ASC responded by revealing that it would be 'discussing the principles underlying the deferred tax standard in the near future, possibly at its June meeting'.[96] This was insufficient to derail the CBI's campaign, however, and their statement was despatched to the committee in mid-June.[97] It offered two arguments against providing for deferred taxation in the circumstances of the time.[98] The first was the economic consequences argument already advanced by Plessey, namely that it was inequitable to current shareholders.[99] The second was that the standard showed

> an unnecessary emphasis on mathematical symmetry, which results in serious distortions for the vast majority of companies . . . and results in a misleading after-tax return on the capital employed, which does not have a proper regard to commercial and economic realities.[100]

Bankers, insurers and some large accountancy firms also advocated a change of direction.[101] It was feared that the change in the apparent relationship between debt and equity would affect industry's borrowing capacity, both mechanically, via the terms of debt covenants using financial statement measures of gearing, and through its effect on lenders' perceptions of risk.[102] Indeed, there were fears that rising deferred tax balances might force companies into default of their borrowing powers as a result of the effect on their financial statement gearing.[103] There were also macro-political fears in play:

> The CBI spoke for industry and said . . . 'we see this as a threat because we are fearful that one day, whatever they say now . . . a Labour government will say, "oh, we see in your balance sheet, we own at least half your assets, so we are going to take them."' It seems far-fetched now, but it was . . . put forward as a genuine fear and seriously argued against that treatment – that it was backdoor nationalisation. That was a political dimension and it was a new one for us.[104]

Whether genuine or not, these fears were encouraged by some politicians. *The Accountant* reported that David Howell MP had said that

> the proponents of state intervention could see the accumulating tax liabilities on company balance sheets and observe: "These things are coming our way: we see real reasons, if these companies carry such huge liabilities, why they should come under state ownership".[105]

Ironically, the Labour government's preferences actually coincided with industry's. According to David Hobson, chairman of the ASSC's working party on deferred taxation,

> The government became worried because, while they were saving companies a lot of money by improving cash flow with free depreciation on fixed assets [ie. First Year Allowances] and stock relief, when you applied [SSAP11] you didn't improve the very moderate performance of these companies shown in their annual accounts. It was affecting companies' borrowing powers . . . And so there was pressure to do something about this . . . including not to go ahead with full deferred tax accounting . . . That was at the Treasury's request . . . Yes there was pressure – there were suggestions, I wouldn't put it stronger than that . . . I was made aware of a desire to have the problem dealt with if possible.[106]

That there was Treasury pressure for a move towards partial provisioning was conceded a little later by a government minister, when a new standard permitting it was published:

> Support for the latest accounting standard on deferred tax came from Joel Barnett, Chief Secretary to the Treasury, last week. In the current financial year there has been a reduction of £4.3 billion in corporation tax payable because of fiscal reliefs. While the government gave tax reliefs, accountants appeared to be taking them [away] with their original deferred tax standard SSAP11. There was concern in industry and government that SSAP11 reduced the willingness of institutions to lend, said Mr Barnett . . . But SSAP15 takes a more pragmatic view, he said. Although the government is prepared to let the profession 'blaze the trail' on standard-setting the Accounting Standards Committee is aware of the government view through Ken Sharp, Head of the Government Accountancy Service, who is a member of that committee.[107]

In October 1976 the Councils of the ASC governing bodies agreed to an amendment to SSAP11, suspending its operation by deleting the paragraph dealing with its starting date. The announcement envisaged this as a postponement and gave, as the reason, the need to consider changes in the economic climate and tax regulations. The bodies nonetheless strongly recommended that companies that had previously provided for deferred taxation should continue to do so.[108] Thus SSAP11 was suspended only a little over a year after it had been issued and before its implementation date would affect any financial statements. The accounting bodies' strong recommendation to continue to provide for deferred taxation was ignored by a number of well-known companies, including Westland Aircraft and Tate & Lyle, although an expected stampede to change policy ahead of a new draft did not materialize.[109]

During 1976 the ASC was also struggling with its response to a government enquiry calling for current cost accounting.[110] During that year its Inflation Accounting Steering Group prepared for the ASC a number of reports, including one on deferred taxation. This included a recommendation that under current cost accounting, SSAP11 should be modified 'to give more recognition to the substances of the allowances and reliefs ... broadly speaking provisions for deferred taxation should not be required where the potential claw-back is not reasonably foreseeable'.[111] The approach treated deferred taxation as a liability and hence the liability method would be required. When the first exposure draft relating to current cost accounting (ED18) appeared, it contained a discussion of deferred taxation reflecting the report quoted above.[112] Thus the discussion of deferred taxation in the context of current cost accounting opened up the debate about economic substance and saw the introduction into the debate of terms like 'reasonably foreseeable' and 'reasonably probable'.[113] It provided both the conceptual rationale for a move towards partial provisioning and some of the technical tools needed to operate it. As Hobson says of the pressure to move away from full provisioning: the Treasury's view 'wouldn't have affected things if I hadn't believed that it was right'.[114] It is clear that he believed that the change in regime made a change in accounting appropriate.

The ASC's review resulted in the publication of ED19 'Accounting for Deferred Taxation' in May 1977 (SSAP11 remained extant). The draft reversed many of the provisions of SSAP11 and the influence of the thinking behind ED18 is readily apparent. Deferred taxation was to be accounted for other than on 'any tax reduction which can be demonstrated with reasonable probability to continue for the foreseeable future'.[115] The liability method was to be used. The potential amount of deferred tax for all timing differences was to be disclosed in a note, showing the amounts involved for each principal category. The sole explanation for the use of partial provisioning is that, 'so far as the balance sheet is concerned, provision of amounts for deferred taxation which can be demonstrated with reasonable probability not to be needed may distort the relationship between funds provided by shareholders and other sources of finance.'[116] There is no explanation for the requirement to use the liability method other than that implicit in the definition of the method, which indicates that it is 'a procedure whereby the taxation effects of timing differences are regarded as liabilities for taxes payable in the future [which are] subject to future adjustment if taxation rates change.'[117] Despite the need to explain and justify the abandonment of SSAP11, the entire document runs to only thirty-three paragraphs, including four addressing the situation in the Republic of Ireland. Once the exposure draft was published, 'the rush for companies to switch accounting policies ... [was] on in earnest'.[118]

Of the 115 responses to the draft, 29 were from companies. The reduction of nearly 40 per cent in the number of responses from companies, compared to submissions on ED11, suggests a reduction in the level of opposition and this was confirmed by an analysis of the responses (25 of the 29 could be categorized as broadly supporting the draft[119]) and a sample survey undertaken by the ASC

of the views of 100 randomly selected listed companies.[120] That the ASC had undertaken such an exercise indicates a degree of sensitivity about the position and awareness of the danger that opponents are more likely than supporters to make a submission. The response from professional firms was more evenly divided:

> generally speaking, the large professional firms either supported ED19 on the grounds that it represented a realistic practical approach to the ... problem ... or they disagreed strongly on the grounds that it traded off theoretical rigour for pure expediency.[121]

A number of submissions from professional firms argued that 'the degree of subjectivity inherent in the ED19 approach was inconsistent with a basic *raison d'être* of the ASC – the standardisation and comparability of accounts.'[122] Many responses from firms alluded to the problems of auditing ED19:

> The determination of the amount of [deferred taxation] will cause considerable difficulties. It will be necessary to prepare and review forecasts of profits, cash, capital expenditure and stocks for some years ahead and, apart from the normal 'internal' assumptions, management and auditors must predict events which are outside the company's control.[123]

In such responses we see the tension between reporting economic substance and the challenges presented to auditors by the judgements such reporting requires.

There was a delay of several months while banks checked with their auditors that they would not be required to disclose their general bad debt provisions as part of the breakdown of the deferred taxation balance by category. Under the regime established when banks gave up exemptions from some company law accounting disclosure requirements, they were permitted flexibility in calculating general bad debt provisions, but these were not tax deductible.[124] It was agreed that the provisions would be treated as permanent differences.[125] The draft standard went out to ballot by members of the ASC in May 1978.[126] In October, two years after SSAP11 was suspended, the accountancy bodies simultaneously withdrew SSAP11 and adopted SSAP15.

The requirements of ED19 were changed in two principal ways. First, the bare statement in ED19 that to qualify for non-recognition, it had to be possible to demonstrate 'with reasonable probability' that a reduction would 'continue for the foreseeable future'[127] was glossed across a further four paragraphs.[128] There had to be 'reasonable evidence', covering at least three years, that no liability was likely to arise; and 'no indication' that the situation was likely to change thereafter.[129] Further, the position was to be reviewed annually and 'regard [was to be] had to the past pattern of capital expenditure and stock levels and whether forecasts made in the past [had] proved reliable.'[130] The standard then indicated that, 'where the criteria ... are satisfied ... the deferred tax provision ... can [not *must*] be eliminated'.[131] Was this a drafting slip,

understandable since the pressures for a change to SSAP11 must have made the ASC think it unnecessary to worry about outlawing full provisioning, or a deliberate attempt to introduce free choice? In his press conference announcing the publication of SSAP15, Watts, now chairman of the committee, made it plain that in his view, 'companies insisting on providing full tax deferral [might] in future find their audit reports being qualified'.[132] This suggests that the committee read the pronouncement as requiring partial provisioning and that is how it was widely interpreted.[133] However, even on this interpretation, it was possible for a company 'to remain fully provided, simply by failing to produce, or pleading an inability to produce, future plans or projections.'[134]

The second change from ED19 was that nowhere in the standard were the liability and deferral methods mentioned and thus, implicitly, both methods were permitted. The reasoning behind this was given in a single paragraph towards the end of the ASC's statement accompanying the publications of SSAP15. This explained that,

> ASC recognises that for most companies the liability method of calculation will be appropriate. For some companies which need to provide fully for deferred tax on all or a given class of assets the deferral method may be equally or more convenient. SSAP15 does not therefore interfere with the freedom to choose the appropriate method for calculating deferred tax balances.[135]

There is no explanation of what makes the liability method appropriate for 'most' companies, nor for why the criterion applied by the others is to be convenience. Nor is there any indication of whether companies might 'need' to provide fully because they had no qualifying reductions or because they were taking advantage of the implicit freedom to follow full provisioning. The somewhat emotive phrase that SSAP15 'does not interfere with the freedom [of companies] to choose the appropriate method' ignores the statement's acceptance that convenience will do as a basis for choice, and, indeed, the ASC's mission to narrow areas of difference. In fact the need to allow flexibility was related largely to considerations of international harmonization – in the USA the deferral method was required and UK companies with US listings would thus otherwise have had to make parallel computations.[136] In addition, the IASC appeared likely to favour full provisioning, permitting partial provision only under more restrictive conditions than the ASC.[137]

An academic survey of compliance with SSAP15 found that,

> companies ... rapidly adopted those parts of SSAP 15 which increase reported profits and produce a more healthy looking balance sheet. This in turn may have been used to justify increases in dividends and in borrowing that would have been more difficult under SSAP 11 There has, however, been considerable reluctance to follow SSAP 15 in detail.[138]

Research and Development

Although the ASSC was born in the heat generated by several accounting *causes célèbres*, its research and development project was the first to be carried out in the immediate aftermath of a scandal actually centring on the topic concerned.

Serious doubts about the financial stability of Rolls-Royce Limited emerged early in 1970.[139] Prior to this, in the words of an *Accountancy* leader, its reputation had been as 'a great company . . . Its main board included men who would have adorned any boardroom . . . It enjoyed the confidence of its bankers and of Her Majesty's government. It was respected by its competitors. Its products had an enviable reputation.'[140]

The size and prestige of the company meant that its difficulties would have significant consequences for the wider industrial sector and, on 6 November 1970, the government appointed Cooper Brothers to investigate the position. Benson was put in charge of the assignment[141] and had not been long at the task when the crisis deepened.[142] He reported, on 25 January 1971, to the Permanent Secretary at the Ministry of Aviation Supply (in the absence abroad of the Minister) and thence to the Prime Minister, Edward (later Sir Edward) Heath and the Governor of the Bank of England.[143] It is a measure of the seriousness of the crisis that his meeting with the Prime Minister was organized for 9 p.m. on the day he informed the Permanent Secretary of the position. Benson also attended a cabinet meeting, at which he recommended manoeuvring the company into receivership; the cabinet fell in with his proposal and the Board of Rolls-Royce agreed to the appointment of receivers on 4 February 1971.[144]

In April 1971 a DTI investigation was established. One of the inspectors was Peter Godfrey, who, some years later, was to become chairman of the ASC.[145] Thanks to their report,[146] we have a very clear picture of the problems at Rolls-Royce. In 1967, the company established a programme to develop a new aero-engine, the RB211–22; early in the following year it signed a contract to supply the engine to Lockheed, for a new aircraft to enter service in 1971. The company embarked on the project without a full-scale evaluation of the level of investment required, or the extent of the risk, and the development challenges posed by the project were very badly underestimated; as Godfrey puts it, in rather less formal language than employed in the report, 'they designed an engine and then found they needed to invent new material because the existing material melted in their new engine.'[147] It had been widely suggested that the company's accountants, and their methods, were to blame for the collapse but the report stated firmly that, 'once the contract was signed, no system of financial control could have significantly influenced the course of events.'[148]

In 1961 Rolls-Royce had altered its policy on research and development expenditure, from writing it all off as incurred to capitalizing some outlays. This had been done because technical problems on another project, the Spey, were necessitating expenditure which, had it been written off, would have yielded losses: 'but for this change . . . the 1961 accounts would have shown a loss, and

in two of the six remaining years prior to the signing of the Lockheed contract the annual profit would not have covered the dividends paid.'[149] Development expenditure on the RB 211–22 was capitalized from the inception of the project. At 31 December 1968,[150] the amount involved (before deferred taxation) was £5.6 million, representing approximately £60 million at 2006 prices. This was about a quarter of the total development expenditure carried forward, which itself represented only a little over 5 per cent of the company's net assets.

During 1969, net expenditure of another £5.3 million was added to the carrying amount of the RB211–22 and other projects increased by a small amount. However, an early paragraph in the Directors' Report warned of the risks attaching to the project and announced that:

> In view of these uncertainties the directors consider it prudent to make a special provision of £20 million against the risk of non-recovery of total development costs. Your directors are conscious that the final outturn of the RB211–22 project may significantly affect the financial position of the company.

The auditors' report drew attention to the paragraph in the directors' report quoted above, and to the provision, but was unqualified. The firm involved was Touche Ross & Co. and Morpeth, then vice-chairman of the ASSC, was familiar with the audit. Although some £3.5 million of capitalized development expenditure remained on the balance sheet at the end of 1969, none of this related to the RB211–22, and the very substantial write-down had been carried out at the insistence of the auditors as a consequence of their doubts about the viability of the projects concerned – in particular the RB211–22. Expenditure capitalized prior to the inception of the RB211–22 had been reviewed by the auditors for viability.[151]

Rolls-Royce provided the backdrop to the ASSC's discussion of accounting for research and development. The 'hawks' on the drafting committee – those favouring immediate write-off – had their hand considerably strengthened by the argument that Rolls-Royce demonstrated that you could never be certain of getting your money back from development activity and that write-off avoided embarrassment.[152] Benson strongly supported immediate write-off and was believed to have advised Heath, during that hastily arranged evening meeting, that the company should not have capitalized development expenditure, with the implication that its accounting policy had encouraged it to behave as it did.[153]

Research and development was included in the ASSC's initial five-year work programme,[154] the problems at Rolls-Royce becoming apparent as it was being drawn up. It was one of the topics that professional firms agreed to take on; in this case the volunteer was Deloitte & Co.[155] The drafting committee for the project, a sub-committee of the Financial and Management Accounting Committee of the Institute of Cost and Works Accountants (including, of course, representatives of the other governing bodies), was appointed in January 1972, with Rupert Nicholson, receiver to Rolls-Royce, as a member.[156] However

ED14 'Accounting for Research and Development' did not surface until January 1975. One reason for the delay was that the sub-committee favoured an approach under which preparers would have a measure of choice in their treatment of some expenditure but the ASC's determination to resist alternatives made this approach unacceptable to the committee.[157]

As a result of this wrangling, the argumentation of the ED sits oddly with its conclusion; on the surface, bad tradecraft – in reality a reflection of the tensions between the expensing hawks and the capitalizing doves. The draft offers a careful classification of expenditure between pure research, applied research, and development, arguing that the benefit of pure and applied research cannot be traced to individual periods, so that expenditure should always be written off as incurred.[158] Readers must surely have taken this as signalling that development expenditure was going to be treated differently, and the next four paragraphs appeared to confirm that expectation. The first pointed out that:

> The development of new and improved products is . . . distinguishable from pure and applied research. Expenditure on such development is normally undertaken with a reasonable expectation of specific commercial success and of future benefits arising from the work, either from increased revenue and related profits or from reduced costs. On these grounds it may be argued that such expenditure should be deferred to be matched against the future revenue.[159]

The next three carefully set out the criteria on which deferral could be justified for individual projects: essentially that they are distinguishable from the rest of the business, technically feasible, commercially viable and expected to be profitable, and that they can be completed with the company's available resources.[160] The following paragraph points out that 'the elements of uncertainty inherent in the considerations set out in [the previous] paragraphs are considerable',[161] but might be no more than a prelude to emphasizing caution in deferral. However, in the next paragraph, it turns out that:

> If these uncertainties are viewed in the context of the concept of prudence, few development projects would be likely to be judged to have sufficient certainty of producing future benefits to justify carrying them forward. While it cannot be denied that there is a theoretical case for carrying forward development expenditure in these few cases, it is nevertheless considered that the combination of rarity of occurrence and considerable uncertainties make such a case an insecure foundation for a practical standard. Accordingly, it is proposed to regard as standard accounting practice that research and development expenditure should be written off in the year in which it is incurred.[162]

Sixty-six responses to ED14 were received, including 15 from professional firms and the same number from companies. Submissions need to be understood in

the context of the levels of research and development undertaken by industry. In 1975 about 70 per cent of industrial expenditure on research and development was undertaken in just three sectors: aerospace, chemicals and electrical engineering (including electronics and telecommunications).[163] Spending was of varying importance in relation to size: in chemicals it represented only 2 per cent of turnover, in electrical engineering 9 per cent, and in aerospace 19 per cent. Although basic research is vital and, being speculative, in some sense wasteful, it is also cheap, taking up only 3 per cent of all expenditure on research and development. At the other end of the chain, development accounts for three-quarters of expenditure. Government assistance was important: it provided about half of the finance for research and development in electrical engineering and 82 per cent for aerospace.

Tony Hope and Rob Gray[164] re-analysed submissions according to the interest group concerned; thus, for example, bodies representing the corporate sector are included with individual companies. They classify thirteen corporate sector bodies as firmly indicating a position on the treatment of research and development; of these eight support ED14. This corresponds to the trend in reporting practice: the percentage of companies writing off all research and development in the ICAEW annual survey rose from 64 per cent in 1969/70 to 93 per cent in 1973/74,[165] a significant shift, attributed by some commentators to 'the Rolls-Royce debacle [having] petrified auditing firms'.[166] However, the five corporate sector bodies advocating some deferral represented significant players: the British Aircraft Corporation, Hawkers, Westland Aircraft, Rediffusion and the Society of British Aerospace Companies. The four respondents from the aerospace industry explicitly phrased their advocacy in terms of adverse economic consequences arising directly in cash flow terms. Hope and Gray cite the Westland response as typical:

> . . . the treatment of [product development] expenditure in the . . . accounts is of great significance, because it has considerable influence on the profit percentage allowed in government contracts. This percentage is calculated by adding an agreed annual profit percentage on capital employed to the cost of the products. The calculation of capital employed is thus of great importance and it is agreed by HM Government and the CBI that capital employed includes product development expenditure only if it is included in the company's balance sheet . . . the loss of profit could be as much as 40 to 50 per cent of the development cost if all the company's business is for HM Government.[167]

As the Society of British Aerospace Companies put it, 'compliance with the exposure draft would . . . lead directors to impose a financial penalty on their shareholders, which does not appear justifiable.'[168]

Coincidentally, the number of accounting firms identified by Hope and Gray as taking a clear position on accounting treatment is also thirteen; four advocated some deferral. The submissions also 'reveal a single unifying theme', but this

time it is 'the importance of the matching principle'.[169] The example cited by Hope and Gray is the response from Ernst & Whinney:

> A disservice will be provided to industry if the profession insists that development costs would be written off as incurred for reasons of accounting convenience and expediency. The matching concept is an important one and we do not believe that this should be surpassed [sic] by the prudence concept merely because of difficulties in obtaining a fair valuation for development costs.[170]

About half the corporate respondents and a third of the firms were opposed to ED14's disclosure requirements, preferring that only information about individual projects be provided. Reasons given included problems of definition, lack of comparability, materiality, competitive advantage and that old standby, the danger that users would become over-excited:

> Disclosure . . . may cause the reader to believe that material hidden benefits exist. This could be misleading since a more efficient and innovative company with a lower level of R&D may be in a significantly better prospective trading position.[171]

The ASC mulled over the submissions it had received and, in April 1976, produced a second exposure draft, ED17 'Accounting for Research and Development (Revised)'. The preface explained the reason for the new draft:

> A considerable body of opinion has emerged during the exposure period to the effect that in certain industries (particularly aerospace and electronics) many projects are in hand at any one time in respect of which the theoretical case . . . for carrying forward the expenditure could be evidenced. In these circumstances, the Accounting Standards Committee is persuaded that a standard accounting practice which requires all development expenditure to be written off as incurred would be too rigid.[172]

In the revised draft, the four paragraphs from ED14 addressing the circumstances in which matching would be appropriate were repeated word for word.[173] The next paragraph (on uncertainty), and the first sentence of the following one ('If these uncertainties . . . '), which in ED14 signalled the turn towards prudence, were also repeated word for word. But now, the remainder of this paragraph tells us that:

> Nevertheless, in certain industries it is considered that there are numbers of major development projects that satisfy the stringent criteria set out [in the previous paragraph]. Accordingly, where expenditure on development projects is judged on a prudent view of available evidence to satisfy these criteria, it should be carried forward and amortized over the period expected to benefit.[174]

Thus preparers were *required* to defer expenditure meeting the specified criteria 'to the extent that its recoverability can reasonably be regarded as assured'.[175] Only opening and closing balances and the movements in the period on deferred development expenditure were required to be disclosed.[176] The draft explained that the change had been made because of 'considerable problems of definition'.[177]

The argument now flowed much better, unsurprisingly since it had been drafted to lead towards the possibility of deferral, but the use of so much common text enabled critics to assert that 'the ASC issued two exposure drafts . . . on the same topic, each of which, by using almost identical arguments, came to very different conclusions.'[178] Actually the change in conclusion appears to reflect a revision in an empirical judgement about the number of cases that could be evidenced as satisfying the criteria, not a matter of logical argument. A more accurate criticism would be that the preface did not reflect the real reason for the change in conclusion, it being related more to the economic consequences of the policy than to any demonstration that the initial factual judgement was wrong.[179]

There were only forty-nine responses to the draft, including only eight from companies. There was general agreement with the new proposals from industry and auditors, although several companies argued that the provisions for deferral of development expenditure should be permissive. Only two respondents objected to the withdrawal of the requirement to disclose research and development expenditure, one firm and the Department of Trade and Industry.[180] Some respondents, including Westland and Plessey, argued for a further liberalization so that expenditure written off could be written back again if the uncertainties causing it to have been written off no longer applied.[181]

SSAP13 'Accounting for Research and Development' was published in December 1977, more than 18 months after the second ED, although the changes from that draft were, in technical terms, small. As requested by some respondents, the deferral of development expenditure satisfying the specified criteria became optional. Thus, between the first draft and the standard, a single uniform method had been relaxed, first to two alternative methods for different categories of event, without choice, and then to free choice between the two methods. Tight disclosure requirements had been abandoned.

There are a number of paradoxes about the way in which the consultation process apparently operated. Although the revised draft pointed to 'a considerable body of opinion' having 'emerged [from the] aerospace and electronics [industries]',[182] only one submission was in fact made from the electronics industry, from Rediffusion Ltd, a company which surely 'may only be classed very loosely as an "electronics" firm'.[183] The electronics industry was, as we have seen, likely to be affected by the proposal in much the same way, though perhaps not to the same extent, as aerospace. Yet Hope and Gray found no evidence of lobbying through the press,[184] common enough in other areas, and the summary of submissions prepared for members of the ASC contains no suggestion that responses from the industry were received with requests for confidentiality.[185] Indeed, several electronics companies, including Plessey and EMI, were prepared to

write to Christopher Nobes setting out their objections to ED14, presumably aware that the correspondence was likely to be published, as indeed it was, in *Accountancy*.[186] Their objections to Nobes, however, were expressed in terms of the write-off being 'misleading' (Plessey) or causing 'distortion' (EMI).[187] Did they lobby members of the drafting working party, the ASC and its secretariat informally, the explanation favoured by Hope and Gray,[188] or was the industry named gratuitously by the ASC to add apparent breadth to the lobby for deferral?

Another paradox is that, although the ASC claimed that a considerable 'body of opinion' had emerged that 'the theoretical case . . . for carrying the expenditure forward could be evidenced', in fact submissions say little about *evidence*, focusing rather on adverse cash flow consequences. Indeed, the British Aircraft Corporation argues for non-competitive government contracts to be excluded from the scope of the standard.[189]

The third is that the chairman of the Review Board for Government Contracts, the body which oversaw the government funding formula that caused such difficulty, was at the time, Slimmings, who was also chairman of the ASC. Hope and Gray suggest that, 'this dual role may [have been] crucial'[190] in the context of the exercise of influence but an alternative perspective is to ask why Slimmings' expertise in the area was not brought to bear on the issue sooner.

Finally, given its preference for comprehensive write-off, why did the ASC not suggest that pro forma accounts be used for determining the appropriate profit calculation on government contracts?[191] Slimmings could presumably have mediated between the Review Board and the ASC; if auditors believed they could audit compliance with ED17, they could have prepared a separate report on the pro forma accounts (presumably at no greater cost for the main and the pro forma audit report together than for auditing financial statements prepared on the basis of ED17). Perhaps some of the 'regulatory side' parties (the ASC, auditors and the Review Board) believed strongly in the existence of an additional blessing conferred by incorporation in the published financial statements, or perhaps the ASC did not feel it could open up this issue, for fear of antagonizing the government when it was struggling with the problems of price change accounting.

Would SSAP13 have prevented the Rolls-Royce debacle? In other words, although hindsight clearly shows that the RB211–22 was not commercially viable, would it have been judged unreasonable, at 31 December 1968, to capitalize about £4 million against a balance sheet total of some £227 million, using the criteria developed in SSAP13? To justify the deferral, the company would have asserted to its auditors that the expenditure was recoverable, as indeed it did in the 1969 accounts. At the ICAEW's Summer Conference in 1979, Ian Irvine and Tom Watts argued that the scandals of GEC-AEI and Pergamon would not have been prevented by applying the accounting standards existing in 1979. They took the same view of Rolls-Royce.[192] Of course, a policy of writing off all development expenditure immediately would have avoided any embarrassment to the accounting profession but there is no reason to be confident that the reduced profits thereby reported by Rolls-Royce in earlier years

would have constituted better information from a user's perspective or would have saved the company.

The Long March towards Depreciation of Property Begins[193]

One topic on the ASSC's initial work programme was described as 'the fundamental principles of depreciation'.[194] In practical terms, significant problems were occurring in only one area, property. Paul Rutteman, writing in 1975, explained that:

> Depreciation is generally considered to be an allocation of the cost of an asset over its economic life rather than a measure of the change in value of that asset. In 1920 the Colwyn Commission argued that depreciation of buildings may be offset by appreciation of their site. Today accounting textbooks say that this confuses a possible capital gain . . . and the expense representing the allocation of the cost of a building over its life.[195]

Notwithstanding what the textbooks said, the ambivalence about the nature of depreciation exhibited by the Colwyn Commission remained readily apparent in the treatment of property at the time of the ASSC's establishment. The 1968/69 ICAEW survey identified 142 companies (out of the total of 300) from whose accounts it was 'apparent that no depreciation was provided on some category of fixed assets'.[196] The large majority of instances concerned property: there were 91 cases of non-depreciation of freehold land and buildings and 43 cases of non-depreciation of leasehold property. The survey reported that 'in many cases, it was stated or appeared probable that the non-depreciation . . . was because of a revaluation or the existence of valuations in excess of book values.'[197] The number of cases rose steadily and by the 1972/73 volume the compilers were reporting that 'an increasing number of companies do not provide depreciation on certain categories of fixed assets . . . Where a reason for non-depreciation was given it was generally because the asset was held in the books at less than the current valuation.'[198]

By 1973/74, the number of companies failing to depreciate one or more classes of fixed assets stood at 240, four-fifths of the total.[199] The increasing incidence of non-depreciation of property coincided with rising inflation and there is no reason to doubt the validity of claims that property values exceeded historical cost.

ED15 'Accounting for Depreciation' was issued in January 1975. Some degree of ambivalence is apparent in its definition of depreciation as 'the measure of the wearing out, consumption *or other loss of value* of a fixed asset whether arising from use, effluxion of time or obsolescence through technology and market changes.'[200] The standard section's requirement to charge depreciation looks more firmly in the direction of allocation, while continuing the implication of the definition that depreciation reflects some observable

phenomenon: 'Provision for depreciation of fixed assets having a finite useful life should be made by allocating the cost less estimated residual values of the assets as fairly as possible to the periods expected to benefit from their use.'[201]

The phrase 'as fairly as possible' has echoes of the true and fair view doctrine but there is nothing in ED15 to indicate unambiguously what is meant by fairness (equity? clarity?[202]) or how it should or could be measured, though it is stated that this 'involves the exercise of judgement by management'.[203] The explanatory section indicates that, 'depreciation should be allocated to accounting periods so as to charge a fair proportion to each accounting period during the expected life of the asset',[204] which suggests equity. However, this section also says that, 'a change from one method of providing depreciation to another is permissible only on the grounds that the new method will give a fairer presentation of the results and of the financial position',[205] which restores the ambiguity. What appears on the surface to be rather sloppy drafting is, of course, not poor tradecraft but rather a symptom of a deeper failure to come to terms with the essentially arbitrary nature of accounting depreciation.[206]

The draft was clearer about the need for depreciation of property:

> It is not appropriate to omit charging depreciation of a fixed asset on the grounds that its market value is greater than its net book value ... All buildings ... have a limited life which may be materially affected by technological and environmental changes and they should be depreciated on the basis of their useful life to the business.[207]

This 'explanation' occupies four out of a total of thirteen paragraphs in the explanatory section. None of its content, however, is carried through into the standard section.

The main impact of ED15 was recognized from the beginning as being to require that freehold buildings be depreciated.[208] This is not without its technical problems. It is necessary to estimate the useful economic life of the building, which, with adequate maintenance, may be very long indeed, and its residual value. After a revaluation, it is necessary for the revalued amount to be split between land and buildings, an exercise which, in a 'highly critical' submission on ED15, the Royal Institution of Chartered Surveyors argued was 'logically sound but unrealistic'.[209] Whatever the – real or purported – technical problems, depreciation of property did not generally materially affect industrial concerns. It did, however, seriously affect property companies (which fell within the scope of ED15) and other sectors with major property holdings such as retail store groups. During the exposure period, opposition came mainly from property companies. The British Property Federation launched a 'stinging attack' on the draft.[210] Their submission pointed out that the impact of the proposal on Brixton Estate's profit after depreciation would be a reduction of 75 per cent, while for Land Securities a profit of £425,000 was turned into a loss of £5.5 million.

While submissions were being considered by the ASC, the IASC moved to adopt IAS4 'Depreciation Accounting', approved in July for publication in October 1976. The standard section required that depreciation be charged on all long-lived assets with limited useful economic lives. The explanatory section indicated that buildings are depreciable assets[211] and though, as in ED15, there was no repetition of this point in the standard section, property was not exempted in the standard section. The UK's preface to IAS4 drew attention, 'in an unusually blunt way',[212] to the difference in status between the non-mandatory explanation and the standard section. Nonetheless the lead shown in IAS4 put added pressure on the ASC.

In February 1977, the ASC considered the final draft of a proposed standard. Although most submissions related to property, the draft followed ED15 very closely in this, as in all other, areas.[213] The pronouncement was agreed by the ASC and despatched to the six governing bodies for endorsement. As usual, the ICAEW ran up the rear. The first five bodies to consider the draft approved it but, for the first time, the ICAEW exercised its veto. Property companies had apparently been indicating to their auditors that they would accept qualified audit reports rather than comply[214] and the ICAEW Council proposed an exemption for them. The ASC did not agree to the exemption but suggested instead that investment properties be excluded from the scope of the standard, initially for one year, while further discussions with property companies were held. This was acceptable to all six governing bodies and SSAP12 was published in December 1977.

The adoption of the standard galvanized opposition in other quarters; in June 1978, it emerged that,

> A group of finance directors from the brewing industry has proposed to the Accounting Standards Committee that public house freeholds should not be depreciated under SSAP12. At the moment brewing companies do not depreciate freehold buildings in the licensed estate, on the grounds that maintenance gives the property an almost indefinite life . . . Allied Breweries finance director John Clemes told [*Accountants Weekly*]: ' . . . We have no quarrel with SSAP12 as such, but we want to achieve a mutual understanding with the ASC on the special problems of the brewing industry. The ASC now has the matter under review.'[215]

The same article revealed the results of a stockbroker's report that depreciating pubs 'could cost the brewing companies between 4% and 9% of their reported profits'. The brewers' initiative was rather curious since, if the expected economic life of licensed freeholds was so long as to make a depreciation charge immaterial, no depreciation would be required under SSAP12 and thus there would have been no need to approach, let alone achieve a mutual understanding with, the ASC and no need for the committee to take the matter under review. Of course, the stock-brokers report would also have been erroneous.

A number of companies outside the brewing industry also conducted a high-profile campaign against the standard[216] but the adoption of SSAP12 actually had a quite dramatic impact in this area. Unfortunately, changes in the format of the data in the ICAEW's annual surveys make it impossible to plot this precisely. In 1979/80, the first year in which SSAP12 applied to all financial statements in the survey, there were 40 companies shown in a single category as failing to depreciate freehold buildings or leasehold property.[217] In 1977/78, the final year before SSAP12 applied to any of the companies in the survey, there had been 122 instances of non-depreciation of freehold buildings and 79 instances of non-depreciation of leasehold property.[218] Hence, even if all companies failing to depreciate freehold property were also failing to depreciate leaseholds, the figure of 122 may be compared with the 40 companies not depreciating freehold or leasehold property immediately after the implementation of SSAP12; if the overlap was not complete, the comparable figure for 1977/78 would be higher.

The survey breaks down the reasons given for failing to comply with SSAP12 in 1979/80 and this information is reproduced in Table 6.2. The survey explains that:

> the 22 companies classified under 'Depreciation provision would not be material' are mainly companies who state that as certain property has such a high residual value and such a long life any resulting annual depreciation charge will be immaterial. The high residual value of the property is usually said to be due to good maintenance. Brewery companies are particularly

Table 6.2 Reasons given for not depreciating freehold buildings or long leasehold property 1979-80

	All companies	Companies disclosing non-compliance with SSAP12
Depreciation provision would not be material	22	11
Residual value exceeds book value	4	2
Market value exceeds book value	4	2
Frequent revaluations made	2	2
SSAP12 to be complied with in following period	2	2
Value of the asset to the company maintained by maintenance	1	0
Depreciation based on book values is meaningless	1	1
No reason given	4	2
Total	40	22

Source: Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1980*, London: ICAEW, 1980, Table 4.4.

> noticeable in advancing this reason in respect of licenced [sic] freehold and leasehold property. None of the companies in this classification, except one, give immateriality as the reason simply because the value of the property in question is insignificant.[219]

Thus 26 companies, more than half those failing to depreciate property, appear to be doing so on the grounds of a combination of high residual values and long lives. Normal historical cost depreciation procedures applied to such assets could indeed yield nil or immaterial depreciation. Nothing in the *mandatory* section of SSAP12, as issued in 1977, contradicts this position. There was, for example, no explicit statement that residual values had to be measured in prices prevailing at date of purchase or subsequent revaluation, so that it remained an open question whether subsequent changes in price-level could be taken into account.[220] The explanatory section asserted only that buildings should be depreciated 'having regard to the same criteria as . . . other . . . assets'.[221] Yet exactly half the 26 companies actually disclosed non-compliance with SSAP12. The survey refers to this paradox, pointing out that,

> where . . . reasons are advanced for not depreciating property, sometimes they are accompanied by a statement that SSAP12 has not been complied with, and sometimes they are not . . . [C]omparison of the individual accounts in question reveals no marked differences between them which could cause this variation in disclosure practice.[222]

Somewhat enigmatically, it adds that,

> it is necessary to bear in mind that whatever is reported or stated in the accounts has met the considered judgement of auditors based upon full knowledge of the facts and circumstances, and that these facts and circumstances are not necessarily matters for complete disclosure.[223]

The opportunity for interpreting the standard to mean that high residual values and long lives justified non-depreciation had clearly been seized by some preparers; others apparently missed this point, unless, of course, the survey was hinting that the reasons they were advancing were at odds with the underlying circumstances.

The ASC returned to the fray, attempting to make depreciation of property universal practice several times over the coming years.[224]

Some Minor Improvements

ED20 'Group Accounts' was issued in July 1977. Its introduction explained that 'the practice of preparing group accounts . . . has become well established in the United Kingdom and Ireland since 1948 and there has therefore been no urgent need for an accounting standard on the subject.'[225] Why then was a

standard to be issued? In March 1976 the IASC had approved IAS3 'Consolidated Financial Statements', its first standard addressing an area on which there was no UK equivalent.[226] This presented something of an embarrassment for the ASC. Although a project on group accounts appeared on its initial work programme, with work apparently already in progress, nothing had been published. In their preface to the UK edition of the IAS, the UK accountancy bodies undertook to issue an SSAP, implementing the international standard, before 31 December 1977.

As one observer put it, commenting on the draft's claim that methods of consolidation accounting were well understood in the United Kingdom,[227] 'there is, of course, a world of difference between universal understanding and universal application of accounting principles.'[228] A number of low-key but potentially significant areas would now be standardized. The option, implicitly permitted by company law, to produce group accounts in a form other than consolidated accounts was closed off. The back-dating of acquisitions to permit the inclusion of a whole year's profits, or of disposals of loss-making subsidiaries, were ruled out.[229] A few small changes were made in the text and SSAP14 appeared in September 1978, only nine months later than promised.

Standards in two closely-related areas, post balance sheet events and contingencies, were also prompted by the work of the IASC. IAS10 'Contingencies and Events Occurring After the Balance Sheet Date' was approved in June 1978 for publication in October, following an exposure draft in June 1977.[230] Though a Recommendation on Accounting Principles (N17) had covered post balance sheet events in 1957,[231] and an ICAEW research report had been published in August 1976,[232] there was, as yet, no UK standard. ED22, issued in February 1978, adopted an approach similar to IAS10's, which itself was compatible with N17, and the draft was converted to a standard, SSAP17 'Accounting for Post Balance Sheet Events', in August 1980.

A significant change from the ED was the inclusion of a reference to window dressing, although the term is used only in the explanatory section. A spokesman told *Accountancy Age* that it had not originally been intended to deal with window dressing in SSAP17:

> 'The Department of Trade report on Ashbourne Investments and the London and County case made window dressing a major issue when SSAP17 was being discussed', he said. 'We felt that we could go some way towards solving the problem within the framework of SSAP17 since most window dressing relates to post balance sheet events. We are not saying in the published standard that we have succeeded in defining window dressing and are now going to put a stop to it – we're saying that we can expose some window dressing by getting companies to disclose the real purpose of such transactions. We're aiming to put the world on notice, as it were,' he said.[233]

Ashbourne Investments had been taking in additional short-term deposits at the year end to improve their balance sheet position. This practice was explicitly

condemned by the inspectors who drew attention to the absence of clear accounting standards relating to window dressing.[234] SSAP17 required disclosure, as a non-adjusting event, of a material post balance sheet event which was, 'the reversal or maturity after the year end of a transaction entered into before the year end, the substance of which was primarily to alter the appearance of the company's balance sheet.'[235] Apparently, 'the London and County case also stimulated the ASC into "background discussion with the Bank of England and other interested parties on the more far-reaching aspects of window dressing."'[236] The problems of financial engineering were to loom large in the later years of the ASC's life.[237]

An exposure draft on contingencies, ED23, was issued somewhat after ED22, in November 1978. It was one of the ASC's briefest, with the standard section running to only four paragraphs, of which one concerns the implementation date and one requires the disclosure of the date of approval of the financial statements, a provision actually incorporated in SSAP17. The most controversial aspect of the draft was the requirement to disclose contingent gains, which went beyond the Companies Acts and was criticized by some respondents as seeking to extend company law.[238] SSAP18 'Accounting for Contingencies' was published in August 1980.

Towards Maturity

In addition to dealing with the topics discussed in this chapter, the ASC was devoting a good deal of energy to the struggle with price change accounting, described in chapter 9. It also issued exposure drafts on foreign currency translation and associated companies, the latter a revision of SSAP1; these are described, together with the standards that emerged from them, in chapter 8. Further, the committee began a major review of its own functioning, described in the following chapter. Its rate of output of finished standards declined a little against the first five years. Eight standards were published in the first five years, plus three shortly after the end of the period (thus reflecting the work of the period); for the second five years, the figures are seven published in the period, deduct the three attributable to the work of the previous period, add three published shortly after the end of the period, making seven against the earlier output of eleven. Arguably, though, some allowance should be made for the 'work in progress' within the technical machinery of the ICAEW at the start of the ASSC's life. Overall, the committee was keeping up a good pace. Three topics on the initial five year programme remained live but unfinished after ten years: mergers (the subject of ED3, on which no progress has been made) and pension costs and goodwill, yet to feature even in an exposure draft. However, that initial programme had been very ambitious.

In its second five years we can see the ASC approaching maturity: maturity as a technical standard-setter and maturity in the wider political environment within which its standards were developed and followed – or, perhaps, not followed. Perhaps the most obvious characteristic of this maturity is complexity – of the business

issues for which standards had to be developed; of the technical solutions canvassed; of the political environment itself; and of the way in which the various parties concerned, including the standard-setters, perceived and understood the process in which they were engaged.

Deferred taxation is a complex conceptual and technical issue – there is even doubt about its existence, which is challenged by proponents of flow-through.[239] The technical issues interact; resolving the deferral v. liability question has implications for full v. partial provisioning, for example. In practice, the urgency of coping with a particular topic, the effort justified in seeking out the best solution to particular issues, and, of course, the political resistance to technically sound solutions, vary according to the probable circumstances in which the standard will be applied. When these change – in the case of deferred taxation, changes in the tax regime – new pressure points emerge. Naturally, those parties most severely affected by applying the 'standard for the old times' are most vociferous in clamouring for a standard for the new times.

Even the apparently simple technical issues disposed of in the first five years were proving more complex in application. The treatment of extraordinary items can be seen as a classic example of standardization: at a minimum it is a consistency standard,[240] improving financial reporting because users know where particular types of event will appear; if the method also achieves a better appreciation of financial performance, perhaps by promoting forecasting capability, it will also represent a performance standard. The committee's approach to defining extraordinary items, relying on a judgement-based rather than a 'bright line' solution, should have improved financial reporting but actually permitted a range of interpretations which itself undermined the efficacy and credibility of the pronouncement. Creative compliance also emerged in the case of the stock standard, particularly in connection with its provisions on the recognition of profit on long-term contracts. A further, apparently simple, topic with rapidly-emerging complexities, interaction between the political and technical dimensions, and scope for creative compliance, was the depreciation of property.

Another issue in the tradecraft of standard-setting with which the committee found itself grappling was the inclusion of alternative treatments in pronouncements. Research and development threw into sharp relief the difference between a scheme containing several treatments corresponding to alternative underlying circumstances, which thus narrows the field to a single identified treatment for a particular set of circumstances, and 'free choice' pronouncements allowing more than one treatment, regardless of the underlying circumstances. For development expenditure satisfying the relevant criteria, ED 17 provided a systematic scheme of alternatives; SSAP13 allowed free choice.

The committee encountered a good deal of political activity, of increasing sophistication, from other parties in the wider standard-setting arena. Clear examples of preparers lobbying for vested interests arose in connection with both deferred taxation and research and development. In both cases the committee made the changes sought. This certainly exposed the committee to charges that it was capitulating to vested interests.[241] Yet the motivation of

preparers (and others) in lobbying for change does not necessarily mean that *standard-setters* are motivated other than by a belief that the method lobbied for is superior on technical grounds, perhaps as a consequence of changing circumstances, or on some other defensible grounds such as cost-benefit. Ironically, this defence is particularly plausible in the case of the research and development standard, where the *rationale* for the new position was already built into the text of the pronouncement setting out the old position.

Much political activity was, or was claimed to be, motivated by concerns about the economic consequences of proposed standards. Again the situation was complicated. In the case of development expenditure, some preparers faced unambiguous and permanent reductions in cash flow from government contracts. In other cases the issues were more subtle: the cash flow consequences of the build-up of deferred taxation balances were either indirect and a result of incorrect perceptions of users (such as higher borrowing costs) or long-term threats that might or might not materialize (such as government seizure of balances as equity investment). Some of the more immediate concerns were, as with extraordinary items, related to the non-cash impact on the accounting numbers, and particularly on key lines in the profit and loss account. The technical and political issues here are profoundly problematic. It may be that users can or should be able to discern the total absence of significance of non-cash effects, in the sense that they carry no connotations about the underlying events and circumstances which generated the numbers. If so, preparers did not understand or accept that this was so: it was argued that rising deferred taxation balances, for example, would be taken to signal lower proportions of capital employed attributable to equity and thus result in lower share prices. Here we see how accounting numbers, and hence the standards that affect them, can contribute to the social construction of the world of business, and not simply reflect its already-existing features.[242]

We can begin to discern in the political arena the emergence of relatively sophisticated manoeuvres. An example would be high-profile opposition to a standard during the pre-compulsory period after publication, creating an impression of widespread resistance, without necessarily any 'follow through' once the date for implementation arrives. The diminution of resistance over time is itself a complex phenomenon combining both tactical retreat from what may always have been intended to be a short-term position and increasing awareness of the possibilities for creative compliance – for finding a 'way to comply' – as seems to have occurred with long-term contracts. The weakness of enforcement, and the increasing public acknowledgement of this weakness, added to problems of the ASC.

Another example of the raised level of political sophistication was the more artful character of some submissions to the ASC, such as the deployment by auditors of fundamental accounting concepts to debate the appropriate treatment of development expenditure, in preference to the economic consequences case put by preparers. In another context this artfulness has been referred to as a 'market for excuses'.[243]

Whether a conceptual framework would have helped the ASC at this stage in its work remains a matter of conjecture. Tony Hope and John Briggs[244] argue that it would not have done so in the case of deferred taxation. The committee's efforts to identify an appropriate treatment of development expenditure can be characterized as groping towards a conceptual framework; in particular, the criteria on which capitalization would be justified can be seen as a step on the path to establishing recognition criteria based on measurability. Conceptual frameworks have had limited success in identifying solutions to the problems of accountancy but can be helpful in structuring the thinking of standard-setters and in justifying and explaining positions. The ASC's change in position on development expenditure could certainly have been presented as a more careful application of the sort of conceptual framework since adopted by standard-setters.

As well as the political activity of others in the wider arena, the ASC found itself dealing with interference – albeit constitutionally sound interference – from its own governing bodies, in the shape of the ICAEW Council's exercise of its veto to prevent deprecation of property companies' properties. The committee was also beginning to experience pressure from another standard-setter, the IASC.

7 Reforming the System

In 1978 the ASC had been in existence for nearly a decade, so a review of structure and procedures seemed a sensible step. However, the decision to undertake such a review was more than merely a routine piece of housekeeping: it was a response to increasing criticism of the committee, which was coming to be directed not only at individual standards but also at its role and approach.

In July 1975, Albert Frost, Finance Director of ICI, addressed the summer conference of the Institute of Chartered Accountants in England and Wales on the subject of accounting standards, arguing that the thinking of the ASSC was 'dominated more by theory than by practice'.[1] Standards were too strict and left insufficient room for the characteristics of individual businesses. He objected to the need to quantify departures from standards and considered that, if the directors 'believe[d] it to be right to depart from an accounting standard . . . the auditor's certificate should be a clean one'.[2] In August, *Accountancy Age* carried a follow-up article reporting that Frost had received 'considerable support from accountants in industry'.[3] In May 1976, Guest, Keen and Nettlefolds used its annual accounts to attack the programme of accounting standards, claiming, like Frost, that they were too rigid and 'theoretical' and led to audit qualifications as a result of technical breaches.[4] Later in the month it was reported that representatives of construction companies were meeting on an '*ad hoc* and unofficial basis to talk over common accounting problems and present a unified opinion to their auditors and the accountancy policy-makers in general'.[5] In October, the President of the Institute of Cost and Management Accountants, Ronald Frank, warned that, although his institute was currently approving standards emerging from the Committee, there was what the article described as 'a danger that too-high standards might hamper management.'[6]

As the months passed, the critical voices of key individuals and important companies were joined by influential representative bodies. In the first few days of 1978 calls for a change in the approach to standard-setting were made by finance directors' groups based in Scotland and in the Midlands[7] and by the Law Society.[8] The Society argued that leaving problems to be dealt with by the ASC was 'profoundly unsatisfactory' and suggested that the Department of Trade and Industry establish an advisory panel to ensure that all interest groups were properly represented in the standard-setting process. In April it emerged

that there was increasing pressure for the 100 Group of Finance Directors to adopt a tougher stance in its dealings with the ASC.[9]

The Watts Review

In the face of the mounting tide of public criticism, Sir William Slimmings suggested that an urgent and wide-ranging review be conducted.[10] The proposal was discussed by the Consultative Committee of Accountancy Bodies as well as the ASC. Some members of the CCAB wanted it to be conducted by a 'top-level panel' with a majority of members drawn from outside the profession,[11] in part as a response to the calls being made by bodies like the Law Society. In the event, the group appointed to conduct the review, chaired by the incoming ASC chairman, Tom Watts, consisted entirely of ASC members. Arrangements were announced in January 1978, in the same week that Watts' appointment as chairman-elect was made public. The other members of the group were David Hobson (senior partner of Coopers & Lybrand), Burton Johnson (Electricity Council), Leslie Miller (Whinney Murray), Bertie Ogle (ICI), Ken Sharp (Head of the Government Accountancy Service), Dennis Sherriff (Turquands Barton Mayhew) and Geoffrey Wilson (Delta Metal). Meetings were attended by the ICAEW Technical Director, Chris Westwick.[12] Including the chairman, there were four members from the audit side of the profession and three from industry.

A few days after the review was announced, the London Society of Chartered Accountants launched its own examination of the standard-setting process.[13] It soon became clear that the LSCA project would rival the ASC's in scope.[14] The press was uncertain whether the LSCA operation would provide 'a large measure of assistance'[15] or create 'conflict'.[16] Ever the diplomat, Watts, 'was at pains to stress [that] both parties shared "a mutual interest" in the success of the accounting standards programme', but added: 'Our intention is to produce a public document which [will] be wider in scope, more informed and more authoritative.'[17]

The ASC group pursued its task, as intended, as a matter of urgency. Its first meeting took place on 18 January, only days after its formation was announced.[18] It met six times in all; the last meeting, on 16 May, agreeing the report to go to the ASC. The group was clearly aware that its findings would be of considerable interest; arrangements for dealing with press inquiries were made at its first meeting.[19]

At the second meeting, members reported back on their contact with various interested parties, including the Confederation of British Industry, the Society of Investment Analysts, the 100 Group, the Law Society, the Association of Pension Funds and the Midland Group of Finance Directors. Many organizations would be submitting papers; members of the group would be meeting others.[20] The chairman had spoken to the Department of Trade, 'who had indicated that [the Department] did not wish to be involved in the work of the Review Group *at present*'.[21] If, by any remote chance, Watts was unaware that this was exactly the stance taken by government in the early days of price change accounting, the Technical Director would certainly have been able to remind him.[22]

The second meeting also received a draft synopsis of the report. The group confirmed the status of pronouncements as mandatory standards and raised questions about whether a conceptual framework was desirable and whether information overload might be being reached. However, the main focus was on resourcing and on concerns about consultation in advance of exposure and 'the secrecy surrounding the standard-setting process.'[23] The third meeting continued its discussion of the synopsis but also agreed to seek advice from Counsel on the legal status of accounting standards. This decision was taken because Crown House – a well-known opponent of the standard-setting programme[24] – had obtained Counsel's opinion that standards had little status in law; the ICAEW's legal advisers felt that it would be possible to obtain an opinion to the contrary.[25] By the following meeting drafts of parts of the report were available. They did not contain firm recommendations for action, which was a 'serious deficiency ... it was felt essential that the Review Group indicate what it felt ought to be done'.[26] The group agreed to recommend that ASC members should continue to serve unpaid; that arrangements for consultation should be formalized and extended; and that there should be 'significant strengthening of the secretariat'.[27] The remaining meetings were devoted to polishing the draft.[28]

A draft report was submitted for the May meeting of the ASC,[29] and a second was seen by the committee the following month.[30] Although the ASC had been empowered to issue the paper on its own authority, it was shown 'as a matter of courtesy' to the CCAB in July. The CCAB decided not to take a position, leaving it to individual bodies to respond.[31] Meanwhile, in June, the LDSA report was published.[32] It concluded that early standards had been of good quality but 'recent exposure drafts [had] lacked the quality which earns respect and ready compliance'.[33] Standards should specify a single treatment and this 'would be facilitated by an agreed conceptual framework'.[34] Audit reports should be qualified only if auditors were 'not satisfied about [a] departure'[35] and the accountancy bodies and the Stock Exchange should make more effort to ensure compliance. The report urged that there should be more openness in both operating procedures and thought processes. The ASC should have more representatives from industry and users, including non-accountants, and needed a full-time chief executive and a larger, high calibre, secretariat.

Notwithstanding that the Watts group's draft was originally shown to the CCAB only as a matter of courtesy, the position now evolved into a need for all six governing bodies to give permission for its publication.[36] Discussions at several Council meetings saw demands for the content to be 'watered down'.[37] The Scots Institute raised a number of objections and 'discussion of staffing levels and finance' was also 'seen by some to be undesirable'.[38] This area also concerned David Richards, Deputy President of the ICAEW, who wrote to Watts on 21 July:

> I read through your Review Report with an eye to the political aspects and there were two points that struck me. The first was that your Group was putting rather a lot of emphasis on the lack of resources ... and secondly that

> there is a tendency throughout the document to offer the ASC's control and responsibilities to others.
>
> I am sure that you would agree that the last thing we want to do is to lose control over the accounting standards field, and I believe that we should not make too much of our restricted resources or our willingness to hand over the control to others.[39]

Following further tweaking and approval from each of the six bodies, *Setting Accounting Standards: A Consultative Document* appeared in late September 1978. The report ran to 28 pages and made 16 recommendations, intended to 'stimulate discussion and in no way inhibit comment'.[40] Some recommendations advocated continuation of the status quo:

> Accounting standards ... will continue to be necessary. One of their main aims should be to narrow the choice of accounting treatment ... SSAPs should continue to be used as definitive principles ... and not merely as a benchmark against which deviations can be measured. A material departure from an SSAP should continue to be allowed only in those exceptional circumstances where to adhere would fail to give 'a true and fair view' in a particular case, or because to follow the SSAP would be demonstrably inappropriate ... The audit report should refer to material departures and breaches. It is a matter for consideration whether reference to a material departure need be made in the audit report in a case in which the auditor concurs and an explanation of the departure is given sufficient prominence in the financial statements.[41]

Two changes in relation to the application and enforcement of standards were recommended. The first was that 'supplementary standards for individual industries should, where necessary, be developed in close consultation with the industry concerned and specialist users'.[42] The second was that, 'the possibility of the Stock Exchange, or the Council for the Securities Industry (as it develops), taking a more active role in enforcement should be explored.'[43] The CSI was in the course of being established as the Watts group deliberated; it was set up at the instigation of the Bank of England and City institutions to co-ordinate existing regulatory mechanisms.[44] Other enforcement methods were considered but it was thought unlikely that statutory backing for standards set by a private body could be secured and incorporation of standards into law would cause drafting difficulties and delay. The creation of an equivalent to the USA's Securities and Exchange Commission, 'for the sole or primary purpose of enforcing SSAPs', would be 'an excessive step'.[45]

As far as the standard-setting process was concerned, the report made a number of modest proposals, mainly designed to improve communication:

> Consultative procedures should continue to be extended as resources permit. Informal discussions with the press should be held. The ASC should be

> prepared to hold public hearings in exceptional cases. The ASC should publish a periodical news-sheet. So far as resources permit, the ASC should publish explanatory booklets. The ASC staff should continue to give oral guidance. The ASC should have the power to issue formal Recommendations and Interpretations although it is to be expected that such documents would rarely be issued.[46]

Open meetings of the committee were not supported. The recommendations on public hearings and a news-sheet include references to practices of the US standard-setting body, the Financial Accounting Standards Board and an appendix describes FASB procedures.

The report examined alternative constitutional arrangements for the standard-setting body, including independence from the profession (paralleling the FASB) and giving a greater role, and possibly a veto, to the consultative group. However, 'failing any clear reasons and consensus for a change', it recommended 'retention of broadly the existing structure, devoting considerably more resources to the consultative process'.[47] Several recommendations, like this one, refer to the importance of finding additional resources, and the report also pointed out that even without changes from the status quo, 'it is reasonable to foresee ... growing complexity of the issues under discussion and growing demands for advice and guidance' so that 'it must be expected that the cost of standard setting will grow substantially.'[48] This perhaps makes the report's final recommendation more or less inevitable: 'CCAB should carefully consider the best means of providing finance in the longer term for the setting of accounting standards in the UK and Ireland.'[49] A final chapter considered the possibility of an agreed conceptual framework but concluded that, 'if an "agreed conceptual framework" is equated with a single undisputed "model", then this is a luxury which evades us at the moment.'[50]

It was natural to look to the FASB as a source of ideas in any review of standard-setting. Members of the FASB are appointed full-time on substantial salaries and relinquish other paid employment. This arrangement obviously increases the time commitment they make to their role but also serves to promote independence from interest groups. The membership of the FASB was considerably smaller than that of the ASC but its support staffing is very much larger: numbers vary but during the period described here were generally in the order of 40 to 50.[51] At the time of the Watts review the FASB's annual budget stood at around $5 million; by contrast, the ASC's stood at £90,000 – and this assumed an expansion in professional staffing during the year from two to four.[52] This budget was borne by the governing bodies in proportion to their representation on the ASC. For comparability with the FASB, and to obtain an estimate of the level of resourcing going into standard-setting in the UK, it is, of course, necessary to add the value of the efforts of those serving unremunerated on the ASC and its working parties, which the Watts group put at approximately £500,000 per annum.[53] Watts visited the FASB in November 1978, with Douglas Morpeth.[54] Did 'the Price Waterhouse technical supremo' learn

anything on communications from the Americans? 'No, I don't think so. I have plenty of ideas – it's just that I lack the resources to put them into practice'.[55]

Shortly after the publication of the report, Watts gave an interview to *Accountants Weekly*.[56] He emphasized the need to 'polish up' the standard-setting process by ensuring that the governing bodies would 'have a more effective say at an earlier stage'.[57] On resourcing and the FASB he had this to say:

> There is a distinction, isn't there, between the British way of doing things and the American. The Americans always want to get it 100 per cent right and that take 100 hours. We try to get it 80 per cent right, and that takes one hour. With our relative lack of resources we have to live on our wits without trying to turn every stone and get everything perfect first run.[58]

It was put to him that, 'the Stock Exchange has not been too keen in the past to take a more active role in helping the profession enforce standards' and he was asked how he would persuade them to change their minds. His reply was that the CSI 'might conceivably wish to take a more active role' but he conceded that he had not yet had any indication that this was so.[59]

Early in 1979, a decision was taken to implement one of the report's recommendations by holding public hearings – on its own proposals. The hearings were to take place in July and those taking part would have ten minutes to make their case and then be examined by the ASC panel.[60]

In March the ICAEW, acting on behalf of the ASC, held a forum of 'representatives from the profession . . . users of accounts, industrial representatives and members of the ASC'.[61] Those attending 'queued to tell the ASC how essential it [was] that a "conceptual framework" for accounting be agreed'.[62] Speakers making this point included Ian Tegner, of Bowater, David Smith, a partner in Arthur Young, Chris Evans of the National Enterprise Board, John Barber, chairman of the Scottish Finance Directors' Group and Henry Gold, Head of Accounting Research at Shell.[63] Despite this apparent blow for the report's conclusion on conceptual frameworks, Watts 'said he was well pleased with the first open meeting'.[64]

Responses to the consultative document were received from 97 organisations and representative groups and 34 individuals. The number of submissions on EDs had stabilized at about 80 to 120[65] (ignoring price change accounting which attracted vastly greater interest), so it would appear that the standard-setting process itself attracted scarcely more interest than any individual topic. Unusually, the submissions were published by the ASC.[66]

Given their key roles, the responses from the ICAEW and the Stock Exchange are of particular interest (the CSI did not make a submission). The ICAEW recommended that:

(a) The ASC should be in the nature of a Council, acting as a forum for the debate of matters of principle rather than technical detail (i.e. it should be 'senatorial' in character) and should give consideration to including in its membership several prominent persons drawn from organisations other

than the accountancy bodies, being persons who are either preparers or users of accounts;

(b) The staff of ASC should be strengthened in size and quality.[67]

The reference to a senatorial ASC was picked up in the headlines[68] and was to find widespread use in the debates that followed. Avoiding technical detail would be important if representatives of preparers were to be of senior status (since finance directors and others of equivalent rank are, understandably, less likely to be motivated to interest themselves in the minutia of accounting technique than technical partners), and if users were to make a full contribution. The second recommendation followed, in part, from the first, since technical detail would now have to be developed at staff level. The ICAEW suggested that there was a need for 'a very senior executive with substantial technical and management experience'[69] and total qualified staffing in the region of 8–10, nearly tripling current expenditure. It favoured retaining the governing bodies' individual power of veto – necessary, it thought, because without the authority of the Councils, the power of professional bodies to discipline members for breaches 'may have no force'[70] – but was prepared to let the ASC 'settle the final wording'.[71] It thought that the profession would have to pick up the majority of the financial burden of enhancing the ASC's secretariat and consultative processes. On enforcement, the ICAEW backed the report's proposal that the Stock Exchange or the CSI should take on a more active role.

The Stock Exchange's submission discussed enforcement generally and its own role in particular – on the latter there is a separate section running to over a page. For the Exchange, 'it would seem that the most appropriate way of dealing with non-compliance is to require full disclosure and full explanation of the fact in the audit report',[72] a view at variance with Watts' recommendation that 'SSAPs should *continue* to be used as definitive principles . . . and not merely as a benchmark against which deviations can be measured.'[73] As a result of its position, the Exchange considered 'the question of enforcement irrelevant and even misleading'.[74]

Adequately disclosed departures from standards left the Exchange untroubled because the market was fully informed and dealing could continue; the draconian nature of suspension of listing as a penalty, and the damage it does to shareholders, was emphasized.

The programme of public hearings got under way in Glasgow on Thursday, 5 July. There was initially some concern that the numbers seeking to appear at the hearings were rather low[75] but the ASC was later able to announce that the hearings were 'fully booked',[76] an outcome which appears to have been achieved by limiting the length of the hearing to half a day rather than finding more speakers.[77] Hearings also took place in Dublin, on 11 July, and in London, at Moorgate Place, on 19–20 July. Many presentations came from organizations that had already submitted evidence and added little to the written submissions. The hearings did, however, enable members of the ASC present, mainly Watts himself, to submit respondents to 'gentle probing of their ideas'.[78] The hearings were

sparsely attended and a photograph of one session shows the floor almost empty.[79] Professor Edward Stamp, who had been so deeply implicated in the campaign to establish the ASC, attended to argue for legal backing for the standard-setting process. The photograph shows him at the front of the audience, presumably waiting to give his evidence, slumped in a pose of utter boredom.

The Final Report

The hearings completed, Watts turned to drafting his final report. A good deal of work had been going on in the background on one of the recommendations, the involvement of the Stock Exchange and the CSI in enforcement. The CSI's initial reaction to the Watts proposals had been unenthusiastic[80] but it was subsequently reported that it had agreed to further discussions,[81] and by the end of April 1979 the ICAEW was sounding bullish:

> Despite previous lack of enthusiasm on the part of the Stock Exchange and the new Council for the Securities Industry to lend a hand . . . there is no reason to suppose they will not consider new specific proposals, says English Institute technical director Bob Willott.[82]

Negotiations were on a knife-edge. In late May, the chairman of the CSI told a press conference that he favoured involvement;[83] a month later, the CSI decided to await publication of Watts' final report before taking a decision.[84]

Discussions with the Stock Exchange continued through the autumn[85] and, just before Christmas, the Stock Exchange Council announced that it was 'looking forward to working with the accountants'.[86]

On 1 February 1980, *Accountants Weekly* carried an apparently authoritatively-sourced account of the latest position.[87] Following a meeting with the Exchange in late January, Watts felt it was 'clear the two sides have the same sort of mechanism in mind. This looks set to materialize as a monitoring panel manned by representatives of the Stock Exchange, the Council for the Securities Industry and the Accountancy Bodies.' In the middle of February, the CSI agreed to join the ASC and the Stock Exchange.[88] A draft agreement was reported to the CCAB at its March meeting which, in turn, referred it on to its constituent bodies.[89] The hardest nut of all appeared to have been cracked. Understandably, Watts saw this as a significant advance, referring to it in his presentation to the ICAEW Centenary Conference in May,[90] and again when briefing the press about the completion of the first draft of his final report in July.[91]

The finalisation of the report was not, however, proceeding smoothly. Watts had outlined his thoughts to the March CCAB meeting, but 'met with rather more criticism than expected'.[92] His thinking included provision for five outsiders on the ASC, nominated by the Stock Exchange and the CSI, and a degree of independence for the ASC along the lines of the US system. Ronald Spencer, Vice-President of the Association of Certified Accountants was quoted

as saying that 'the feedback was such that one would expect the views to be borne in mind when the final report was being produced.'[93] The March CCAB meeting also discussed complaints from the ACCA that too much was being done in the name of the CCAB without proper consultation, or by the ICAEW unilaterally, including an appointment to a government review of company law and changes in the rules on professional ethics.[94] The complaint extended to the negotiations concerning enforcement of accounting standards. In April, the CCAB suggested that the proposed enforcement scheme be separated out from the main review; Watts declined.[95]

In July, Watts gave a further presentation on his thinking to the CCAB.[96] Before that meeting, William Hyde, the President of the ICMA, was quoted as saying that he had 'grave doubts' about the move to introduce externally nominated members.[97] The CSI had now indicated its view on the standard-setting process generally.[98] It was unwilling to see it remain the exclusive preserve of the accounting profession. Authority to approve standards, determine policy and manage enforcement should pass to an Accounting Standards Board, with the CCAB bodies giving up any involvement. The Board would have about a dozen members, with a chair nominated by the Bank of England and other members chosen by a broad spectrum of organizations representing preparers and users; there would be one representative of the accounting bodies. Watts thought this unlikely to be acceptable – an easy guess given the earlier feedback – and was continuing to pursue an extension in membership of the ASC to embrace non-accountants, to be nominated by the chairs of the ASC, the CSI and the Stock Exchange. He was also continuing to pursue a measure of independence for the ASC.[99] According to *Accountancy Age*, the meeting, 'identified these points as the key issues and brought the CCAB's lack of unanimity out into the open ... it [was] thought unlikely that the differences [would] be resolved speedily and happily.'[100] The disagreements were causing lengthy delays in the production of the final report and undermining the likelihood of its being a credible influence for change when it appeared.[101] One news story specifically mentions the damage likely to be done to the proposal for a joint review body.[102]

In September, a revived panel began meeting to assist Watts in the production of an 'acceptable' version of his report.[103] This had some members in common with the original group but now also included Morpeth.[104] Its meetings were difficult, with Ogle challenging the assumption that there was a continuing need for the ASC at all, since the programme of standards was, in his view, nearing completion.[105] Later that month, the ICAEW Council considered another outline of Watts' conclusions.[106] Although intended to be confidential, the outline was in fact leaked to the press in considerable detail.[107] Outside membership and the joint review panel continued to feature in the recommendations but the CCAB would maintain its constitutional power over the committee. The costs of the operation were estimated to be likely to rise from the current budget of £180,000 to around £440,000 as a result of increased staffing and the cost of the proposed monitoring and enforcement arrangements. The possibility of

securing outside funding, via a foundation on the US model, was mooted. The meeting did not reach a decision on the paper but warned that the Council was unlikely to look favourably on the level of additional funding needed (despite the position taken in the Institute's submission) and that other CCAB bodies would be likely to take a similar view.[108] The paper then went to the other CCAB Councils before appearing on the ASC's agenda at the end of October.[109] The principal remaining problems in this, the third, draft of the final report were the proposal for outsider membership and the cost.[110] A fourth draft was considered at the following month's ASC meeting; the meeting was poorly attended but sent for a fifth draft – 'fifth and final', according to the headlines.[111] In the event the fifth draft did not quite satisfy the committee and a sixth had to be prepared to go for the postal ballot stage in December. It was approved and proceeded, in its tortuous way, to the Councils of the member bodies and the CCAB itself.[112]

Perhaps unsurprisingly, the report remained 'bogged down in procedural difficulties'.[113] The ACCA Council decided that it would not oppose publication of the report but did not agree with its findings. It objected strongly to the allocation of more money to the ASC, especially as the committee was so strongly associated with the ICAEW.[114] The ACCA was in favour of some outside membership but this point was the subject of objections by the ICAS. The ICMA and the Chartered Institute of Public Finance and Accountancy also had reservations.[115] Meanwhile, some ASC members were revealing that they regarded themselves as having voted only for the report to be passed to the CCAB and not for its publication.[116] The CCAB meeting decided to refer the report back to the Councils again, seeking 'general approval' of its conclusions and approval to publish without further amendment, but not full support of the recommendations.[117] It also recommended that the Councils request that the ASC continue to give consideration to the composition of the committee and the plans for policing non-compliance after the report was published.[118] Even these recommendations proved controversial; the ACCA remained initially unwilling to support publication at all and, while the ICMA and CIPFA agreed to the CCAB proposal, they also let it be known that they remained opposed to the increase in funding and, in the ICMA's case, the policing arrangements.[119] Eventually all Councils agreed to the publication of the report,[120] which 'limped into full public view'[121] in early May, 1981.[122] The accompanying press release indicated that the CCAB had authorized publication of the report but, in case there was anyone left who did not appreciate how weak this endorsement was intended to be, added that it had asked the ASC to give 'early consideration' to three of its recommendations – the composition of the committee, the policing mechanism and funding.[123] It had been suggested that the report would be accompanied by a letter explicitly stating that the recommendations did not have the support of a majority of CCAB bodies[124] but, in the event, a slightly less combative tone was adopted.[125] Difficulties in agreeing the text of the release resulted in a further delay to the publication of the report.[126]

The report's summary of conclusions and recommendations is reproduced in Appendix 3. Many appear unexceptionable; for example, 'accounting standards are necessary and will continue to be necessary.'[127] Others might appear unexceptionable now but were more controversial at the time; for example, 'the tasks of the standard setting body will continue as far ahead as can be foreseen.'[128] Departures from standards would be permitted only when necessary to give a true and fair view, but the detail of departures would not have to be disclosed because the costs of so doing were considered to outweigh the benefits. Some standards might be limited to large enterprises and specific industry standards should be used to deal with problems unique to major sectors.[129] The standard-setting body would continue to consist primarily of accountants but 'the wider public interest and the needs of users should be more clearly recognised in the membership of the ASC',[130] with appointment of non-accountants as appropriate. Four or five additional members were envisaged, appointed by the chairman of the CCAB on the recommendation of the Stock Exchange or the CSI or both.[131] Power to issue standards would remain with the CCAB bodies but procedures should be reviewed, 'to ensure there is adequate consultation at the formative stages with the intention of avoiding conflict with the findings of the standards body arrived at after due processes of consultation and debate.'[132] This rather enigmatic phrasing was intended to mean that if a CCAB body was contemplating the exercise of its veto, it should say so before the draft was agreed by the ASC, not after.[133]

On policing, the proposals remained largely as they had been sketched out earlier. The CCAB and the CSI were recommended to adopt proposals, already approved in principle by the Stock Exchange, to establish a joint panel to review non-compliance with accounting standards by listed companies.[134] This was 'a matter of considerable importance'[135] – the only recommendation to have particular emphasis attached to it. The objective and procedures for the joint panel were set out in the report in some detail and expanded on in an appendix to the report, reproduced here in Appendix 3.

Development of standards would involve wide consultation and debate and this would include discussion papers issued prior to exposure drafts; more use of the Consultative Group; regular progress reports; and issuance of non-mandatory guidance.[136] On resourcing, 'substantial technical staff support for the ASC' was needed and this should include the appointment of a Director of Accounting Standards. It might be necessary to provide for remuneration of a chairman, since the duties had become 'almost full-time'.[137] The Director of Accounting Standards should be 'a person of a calibre somewhat equivalent to that of a technical partner in a major practising firm in the profession or the equivalent in industry or commerce.'[138] The cost of the operation as envisaged would be a minimum of £263,000 per annum, with the likelihood of it rising to £400,000 in due course. This compared to the current budget of £200,000.[139]

The ASC's member bodies continued to distance themselves from the review's recommendations. Four of the six revealed to the press that they had not supported the recommendations. The most vociferous was the ACCA,

whose President, Edmund Gibbs, reminded *Accountancy Age* readers that his Council's members had 'had serious reservations on the original draft' and now reported that they were 'not very happy about the escalation of costs it still envisages'.[140] Apparently, a move had been made to outflank the ACCA by getting the other five bodies to issue a statement supportive of the report, but this did not find favour with the ICAS or the ICMA.[141] The street fighting deteriorated further in the following month, when the ACCA published a critique of the recommendations including new points that it had not focused on in discussions of the draft, causing 'anger' at the ICAEW.[142] The critique reiterated the ACCA's earlier points, including an attack on the proposed joint panel and argued that the staff of the ASC should be independent from the ICAEW.[143]

Implementing Watts

The ASC's next move was to set up another working party, chaired by Morpeth, to undertake the reconsideration of the most controversial proposals urged by the CCAB – Morpeth's appointment was interpreted as a signal that he was likely to be the next chairman.[144] The ICAEW's next move was to jump the gun. While the Watts Report's organizational recommendations were being wrangled over in public, posts were being discussed in private. The Institute was keen to establish the Directorship of Accounting Standards envisaged in the (at that stage yet to be published) Watts Report – to function separately from its own Technical Director, possibly as a prelude to widening the gap between the ASC and the CCAB. Robert Willott, the incumbent ICAEW Technical Director, was offered his choice of the new Directorship and the attenuated ICAEW Technical Directorship but, believing that the proposed new structure would further undermine the public credibility of the profession's technical work, and the ICAEW in particular, declined both posts and left to join Spicer and Pegler.[145] James Carty, secretary to the ASC, left to establish his own practice. 'It is a pity from the point of view of continuity that Carty is leaving,' but 'it is not fatal', Watts told *Accountancy Age*.[146]

Following these departures, the ICAEW combined the existing ASC secretary post and the ICAEW Technical Directorship to create the new Directorship of Accounting Standards, achieving the staff leadership it wanted for standard-setting while leaving open the option of a later move to split the roles. By late April, the ICAEW was 'putting out feelers to find a suitable candidate'.[147] In June, it was announced that the new post had been filled by Christopher Morgan, a Deloitte Haskins & Sells partner, who would occupy it on a secondment to last for three years.[148] Morgan had been a partner since 1973 and had an audit, rather than a technical, background,[149] despite the reference to a technical partner in the 'job description' included in the Watts Report[150] and the Institute's well publicized search of technical departments in major firms.[151] This, together with the use of secondment, suggests that the Institute had some difficulty in filling the post.

Morgan's appointment infuriated the ACCA, whose response to the final Watts Report, published a week after it was announced, said of the creation of the post that it was 'unnecessary and cannot be justified'.[152] The Association also objected to the manner in which the decision to proceed had been taken (apparently on the basis of 'informal talks' with CCAB presidents, rather than formally at a CCAB meeting, and certainly in advance of mature debate on Watts' final recommendations[153]) and to the title. By merging two posts, a cost saving was achieved compared to the original proposal and the financial implications of the appointment had been reflected in a budget approved by the CCAB.[154] Further, since the appointment was to the ICAEW's staff, it was presumably constitutionally proper for the ICAEW to make it – and to give the post-holder whatever title it wished. It was not a happy start for Morgan, however.

A New Chairman

Watts had been indicating for some time that he did not necessarily want to complete his second term.[155] Morpeth, vice-chairman of the committee since its inception, had been tipped in the press as successor to Watts since at least early 1980, the time at which Watts' second term was under discussion,[156] and by July 1981 this had hardened into an expectation.[157] However, the press was also predicting that problems would arise over the succession, not least because of difficulties within the CCAB caused by disagreement between the bodies, and particularly between the ICAEW and the ACCA.[158] By convention at least, the choice of chairman needed unanimous approval by the CCAB bodies.[159] In the event, Morpeth was invited to take over the chair shortly after this prediction was made but turned the offer down.[160] This news was given to the August meeting of the ASC. Morpeth, who had been knighted in the Birthday honours list, explained:

> I've spent an awful lot of time involved with accounting standards and institute work over the last ten years . . . I thought I would be able to contain the ASC job, but I realised it will be almost a full-time task in the next two years. I now intend to spend more time on Touche Ross business.[161]

Morgan was upbeat about the search for a replacement: 'feelers have been put out for a successor . . . We hope there will be a decision fairly soon, perhaps in the next two weeks.'[162] Names canvassed in the press included Ogle, Richard Wilkes and Jim McKinnon.[163] One CCAB president confirmed to the press that several candidates had been approached.[164]

In fact the search took several months, but, in early January 1982, the CCAB was able to announce that Ian Hay Davison would take over the chairmanship from 1 July 1982.[165] Davison was a member of the ICAEW Council, which he joined in 1975, and had played a leading role in the Inflation Accounting Steering Group,[166] but had never been a member of the ASC. He studied at the

London School of Economics and Political Science and the University of Michigan and became managing partner of Arthur Andersen's UK practice in 1966. He had overseen the growth of the practice from five partners and 146 staff, dependent largely on business referred from the USA, to 85 partners and 2,000 staff. He gave up his role as managing partner on appointment to the ASC but continued as senior partner of the UK practice.[167]

A profile of Davison marking the announcement of his chairmanship of the ASC described the appointment as a paradox, because 'relief to have someone accept the job' was contrasted with concern that 'such a forceful character may rebound upon the conservative centre of the profession'.[168] Despite Watts having done the job more or less full-time and Morpeth having turned it down because it was almost a full-time commitment, Davison would be undertaking the role on a part-time basis.[169]

Davison himself acknowledges that, 'to some I was a surprising choice: although a Council member of the ICAEW for some six years I had not been noted for moderation in the expression of unorthodox views.'[170] Indeed, those whom the choice surprised included Davison himself.[171] His own speculation is that Harry Singer, the President of the ICAEW at the time, asked him to do the job because 'he must have been desperate'.[172] It does seem likely that something like this, combined with the knowledge that Davison was striving to build up Andersen's profile in the UK – so that he 'happily grabbed anything that came [his] way',[173] and was thus likely to accept the posting – was one element in the picture.

However, to suggest that this is the full story is to understate both Davison's strengths (he had been managing partner of Arthur Andersen & Co. for sixteen years and had chaired the ICAEW's Technical and Research Committee for three[174]) and Singer's insight. Davison was acquiring a reputation as an effective political operator.[175] As he puts it: 'I was unquestionably someone who was a pragmatist and who would seek political solutions to problems rather than theoretical solutions . . . and wouldn't go on head-banging in search of the theoretical answer which would never be capable of achievement.'[176] Such a characteristic must have been attractive to those who were anxious to get the ASC through the next phase in its development, including Eddie Ray, Deputy President, and David Currie, Vice-President of the ICAEW at the time of Davison's appointment. Currie worked in industry – a relatively unusual background for someone on the Presidential escalator – and had a formidable reputation for innovation and getting things moving.[177] To this group, Davison would have had many attractions beyond mere willingness to serve.

Davison was an enthusiastic supporter of the 'senatorial' model for the ASC.[178] Well before taking up the chair, he began fashioning from the Watts recommendations a composition for the ASC that would reflect his ambitions for the way it would work. Proposals, about which he had 'already talked extensively with senior members of all the CCAB bodies',[179] and with the Government, the CBI and the Governor of the Bank of England, Gordon Richardson,[180] were accepted by the ASC at its May meeting[181] and Davison

then toured the CCAB member bodies to present his ideas ahead of the CCAB vote. At the ACCA he 'said he had made it clear he was chairman of a CCAB committee and not an English Institute committee. "The roots of the ASC lie deep in the English Institute but times are changing."'[182] His political skills were functioning well.

Davison was proposing that appointments to the ASC would be made by a committee consisting of one senior member from each of the CCAB bodies. The quota of places for each governing body would be abolished and appointments made on merit. The ASC would be reduced slightly in size and a balance between practice, industry and the public sector observed, with at least one member of each governing body invited to serve. Five places would be filled by eminent figures from industry and the City, who could be non-accountants.[183] Members would serve a three-year term, renewable once, and there would be an expectation that they would attend regularly, a proposal designed to 'remedy poor attendance, which [had] dogged the ASC in recent years'.[184] The committee would be encouraged to work on the senatorial model. Two government observers would be invited to attend. It was suggested that costs be shared in proportion to the membership of the respective parent bodies.[185] It was not, however, intended that the secretariat would change from their present status as employees of the ICAEW, based at Moorgate Place. *Accountancy* pointed out that the ICAEW might baulk at losing its built-in majority but shrewdly added that the proposed constitution would still be likely to result in the committee including 'a high proportion of its own members'.[186] All the CCAB Councils accepted the proposals.[187]

The new nominating committee met for the first time on 4 August, in the expectation that the 'reconstituted ASC' – some of the press preferred 'revamped',[188] while Watts charmingly referred to the 'reconditioned'[189] committee – would meet for the first time on 26 September.[190] This timetable was achieved.[191]

A Reconstituted Committee

The reconstituted committee looked very different. It had seven members from practice and five from industry, five users, two members from the non-trading public sector, and one academic, making twenty in all.[192] Only eight had served on the old ASC and four of those had joined only in January 1982. The longest-serving members were Sharp, who had been a founder-member and re-joined as Head of the Government Accounting Service in June 1975, and McKinnon, who joined in July 1978. There were two non-accountants. Professional body loyalties among the eighteen qualified members are difficult to calibrate precisely because no fewer than seven held multiple qualifications.[193] Most of these, however, were current or former members of the Council of only one body, and using this to identify their main allegiance, it would appear that the ICAEW held nine places, the ICAS, the ACCA and the CIPFA two each, and the ICAI and the ICMA one each, with one person – not a member of the ICAEW –

having no clear single allegiance. On this basis, the ICAEW's grip had fallen from 12 out of 23 to 9 out of 20 – no longer a brute majority, but not a bad position. The average age of the committee was a little less than 51, Davison's own age.[194] The 'user members' were Ronald Artus, of the Prudential Corporation, an investment analyst; Jeffrey Knight, chief executive of the Stock Exchange; Michael Mallett, a director of James Neil Holdings; Derek Palmar, chairman and chief executive of Bass; and John Quinton, Barclays Bank. It is not entirely clear what role Mallett and Palmar, both of whom were qualified accountants, held that made them users rather than preparers of accounts.

Changes in the committee's methods of operation followed rapidly. The first meeting agreed to give six topics priority: leasing, pension costs, pension scheme accounts, acquisitions and mergers, goodwill and foreign currency translation. Work on six topics, related parties, the reviews of SSAPs 9 and 10, materiality, interim accounting, and segmental reporting was suspended.[195] The development of a conceptual framework was put 'firmly in the second division'[196] and work on implementing international accounting standards was suspended indefinitely.[197] Some users disagreed with the lowered priorities – for example brokers felt that work on interims and funds flow should continue.[198] Later in the month, the President of the ICAEW had to give assurances to the chairman of the International Accounting Standards Committee that the UK bodies were still committed to their pledge to use their 'best endeavours' to secure adoption of international standards.[199] Press Conferences were held following each meeting.[200]

The style of the committee's procedures also changed considerably:

> We obtained the commitment of our eminent members by some simple rules. We would never meet more than once a month and never for more than two hours at a sitting. Anyone who wished could bring an aide or adviser ... Although some ASC members served with distinction on subcommittees and working parties it was clearly understood that this was not an obligation of membership. Finally, there was to be no drafting in committee.[201]

Davison established four standing committees.[202] There was a four-person Planning Committee, chaired by Davison and including the chairs of the other three standing committees.[203] All ASC staff participated in the meetings. The committee shaped the agenda for ASC meetings, chose members for its working parties and dealt with general tactical issues. It met monthly, like the ASC, and enabled Davison to keep the agenda for the main committee down mainly to substantial debates of policy issues.[204] The other committees dealt with international affairs (chaired by McKinnon, finance director of Imperial and vice-chairman of the ASC), inflation accounting (chaired by Stanley Thomson, finance director of Ford) and the public sector (chaired by Derek Fowler, deputy chairman of British Rail). Observers from government departments, the CCAB Auditing Practices Committee and the IASC were appointed[205] and 'played an

active part at ASC meetings'.[206] The Law Society was persuaded to appoint a legal adviser[207] and Professor Bryan Carsberg, Research Director at the ICAEW attended meetings and 'made noteworthy and influential contributions'.[208]

Although Watts had recommended increasing the role of the Consultative Group, Davison, allowed it to become 'moribund'.[209] The senatorial model itself meant that the ASC's 'lines were open to the power centres among preparers, users and auditors'.[210] Beyond this, Davison preferred a less formal approach to consultation:

> I went further and initiated an extensive programme of consultative meetings with users such as the Hundred Group, the Midlands Industrial Group and the Scottish Group of Finance Directors. I also met the relevant subcommittee of the CBI, a group of investment analysts hosted by Ron Artus of the Prudential, and the senior partners of the larger, and smaller, auditing firms. In addition, I tried to meet regularly with the Councils, or Technical Committees, of the six CCAB bodies. Some of these meetings (and I must have held at least 50) were very useful in clarifying the needs and perceptions of our customers; they were essentially market research.[211]

This approach occupied a good deal of the chairman's time; Davison's appointment as chief executive of Lloyd's, in 1983, 'meant a reduced commitment of time to the ASC and it was the programme of consultative meetings that suffered most'.[212] The programme of public hearings was not judged a success and was discontinued.[213]

A working party was established to look once again at the standard-setting process. Although it was initially chaired by Davison, he passed the role on to McKinnon after taking up his position at Lloyd's and its final recommendations became known as the McKinnon Report, which appeared in May 1983.[214] The working party concluded that 'the essential characteristics of future accounting standards' would include that 'they deal only with matters of major and fundamental importance affecting the generality of companies, and will therefore be few in number.'[215] In order to cater for the needs of users while limiting standards to matters of fundamental importance, a new category of final pronouncement, the Statement of Recommended Practice (SORP), would be introduced.[216]

Within the new category, there were to be 'franked SORPs':

> These will generally relate to topics of limited application, for example, a specific industry. The work on franked SORPs will generally be undertaken by a working party drawn mainly from the industry concerned, but its work will be overseen by and subject to review by the ASC. The final approved document will be published by the industry concerned.[217]

To further lighten the load, the ASC would consider, case by case and employing a cost-benefit criterion, whether exemptions from standards for particular categories of preparer should be permitted.[218]

A new form of consultative document, the Statement of Intent would be introduced.[219] Interpretations would not be issued,[220] for fear of producing a 'cookbook' of detailed rules.[221] The report emphasized the importance of consultation with the CCAB bodies 'from an early stage and regularly thereafter' as each project evolved.[222]

One aspect of the Watts recommendations which remained unimplemented was the joint panel to review non-compliance: 'Davison, launching the [McKinnon] report last night, said: "The report is silent on enforcement changes. We have taken off the jackboots."'[223] When he looked back on his time as chairman in 1985, Davison had this to say on the matter:

> In three important respects we have deviated from the proposals in Tom Watts' report. First and most important, after considerable discussion and negotiation we decided to do nothing in the area of enforcement. It must be clearly understood that it is the task of the ASC to propose to the six institutes standards for adoption by their Councils. Enforcement of standards upon the membership is a matter for the disciplinary processes of the professional bodies.[224]

Resources

A key resource for the ASC is the time of its chairman. Morpeth had expected that the job would be 'almost a full-time task'[225] and, when Davison was asked to take the role on, it was assumed that he would need to devote himself full time to the ASC. He declined to accept the job on that basis, agreeing instead to make it 50 per cent of his workload.[226] Even this level of commitment was not to last long:

> In December 1982, after less than six months in office, I was approached by Gordon Richardson, then Governor of the Bank of England, to go to Lloyd's as Chief Executive to assist with urgent regulatory matters there. As a result I had drastically to curtail my time commitment to the ASC. Two and a half days a week became less than a day a week for the remaining 18 months of the two-year term which I had agreed with Harry Singer to serve.[227]

Davison himself believes that this very substantial reduction in his own time commitment – even more substantial when compared with that of his predecessor – did not much affect the performance of the ASC[228] and it probably is the case that the refocusing of the ASC's own activity, from the senior technical and drafting group to a senatorial body, meant that a 'non-executive' chairman became a possibility.

In parallel with the discussion of the amount of time that Davison would commit to the chairmanship, his firm agreed to provide and fund a personal

assistant to Davison in his role as chairman.[229] Peter Rawlins, a senior audit manager with Arthur Andersen, took on this job, effectively being seconded to the ASC more or less full-time but remaining physically based at Andersen's. Rawlins took a very active part in supporting Davison's chairmanship, for example writing substantial numbers of reports and policy memoranda.[230] The arrangement was potentially quite hazardous, with the danger of further complicating lines of authority and communication in an already complex situation, there being, by then, a Director of Accounting Standards (combining his role with the Technical Directorship of the ICAEW) and a secretary of the ASC (dedicated full-time to ASC work but employed by the ICAEW). In practice, it worked well, causing little friction with the secretariat of the ASC, perhaps because Rawlins's contribution was directed to the constitutional and organizational side of the ASC's operations, with which the secretariat had always had limited contact, leaving the secretariat to deal with the technical agenda.[231]

Another uncosted resource is the time of the members of the ASC and its sub-committees and of other staff employed by their organizations providing support to the members – mainly technical staff of audit firms. In 1980, there were 13 meetings of the ASC, 83 meetings of sub-committees, one meeting of the Consultative Group and one public hearing.[232] As we saw, the Watts Consultative Document estimated the value of the 'voluntary effort' put in by 'members of the ASC and their own support staff' at about £500,000 per annum.[233] Work by support staff in audit firms included the preparation of research studies as well as informal advice to members.[234] Other such studies were financed from research funds of the ICAEW.[235]

By 1980, the ASC was beginning to attract some public criticism for, among other things, lack of new blood and poor attendance,[236] and the situation did not remedy itself in 1981. A gossip column in *Financial Weekly* pointed out that, at one meeting, only six members of the committee were present and that at another, of the nine voting, two came from the same company, and a company with a well-known position on the subject of the vote.[237] The Davison reforms attracted substantial new blood on to the committee and the changes in its working practices improved attendance. Of course, the amount of time these new members donated was substantially lower than hitherto because of the new working practices. The new, senatorial, philosophy meant that the technical quality of the output depended even more heavily than hitherto on the drafting working parties.[238]

The principal costed resource employed by the ASC was its secretariat. By 1977, the secretariat was composed of two technically qualified members and a secretary and cost £34,000, including £10,000 for premises and office services.[239] In 1978 the budget was raised to permit the employment of two additional qualified staff and another secretary. It was estimated that the full year cost at the new staffing level would be £110,000.[240] At that stage the budget was borne by the six governing bodies in proportion to their representation on the committee.[241] By 1980 the budget had risen to £180,000[242] and in 1981 it stood at 'almost £200,000'.[243] A further increase in staffing had become

necessary when the IASG, the cost of which had been paid for from other funds, was wound up in March 1980,[244] leaving work on price change accounting to be carried out by the ASC secretariat. Whatever the budget, there were difficulties in filling vacancies – for example the Progress Report for the year ended 30 November 1980, indicated that,

> at the year end there were two vacancies for under-secretaries to the committee which it had not been possible to fill. For most of the year the secretariat was below establishment and this situation will continue at least for the first part of 1981.[245]

Drafts of the final Watts report prepared in late 1980 suggested a funding level for the new machinery of some £440,000, including £40,000 for the proposed panel on enforcement.[246] However, this suggestion encountered a good deal of opposition[247] and the final version states that,

> The ASC believes that the minimum cost (at present prices) of operating the standards setting body would be £263,000 in its first full year. It would, however, be wise to contemplate that the cost could increase over a period of time to some £400,000 a year (at present prices).[248]

Within a few weeks of the appearance of the final Watts report, the CCAB was contemplating its 1982 budget, which would have included only a fraction of the proposed increase in full-year funding for the ASC. The total proposed budget for 1982 for all CCAB activities was £834,000,[249] representing an increase of 17 per cent on projected expenditure for 1981. It is in the nature of budget-financed activity, especially where costs are dominated by staffing, that actual expenditure will almost invariably fall below budget because any vacancy during the year will yield a cost saving. Although not all CCAB activity falls into this category, most, including the ASC itself, does. It is thus difficult meaningfully to compare previous actual expenditure with proposed budgets but since projected inflation at the time would probably be estimated at around 12.5 per cent,[250] the expansion in overall activity envisaged by the proposed budget seems small. Despite this, the CCAB meeting in July 1981 referred the budget back to the ICAEW.[251] Apparently, a spokesman for the ICAEW made it clear that the row that had developed over Morgan's appointment 'did not form part of the member bodies' reaction'.[252] This 'pre-emptive rebuttal' must be read in the usual way: it would be surprising if this particular incident[253] had had no effect on Councils' reactions.

In 1982, at the time of the reconstitution of the ASC, it was reported that 'the costs of the ASC [were] now believed to be approaching £250,000 a year.'[254] The change in the distribution of the budget doubled the ACCA's contribution (from £22,000 to £42,000) and raised that from the ICMA by two-thirds.[255] We know from Davison's memoir that, 'far from doubling the budget of the ASC [he] managed to keep its costs more or less stationery despite inflation during

[his] period in office'.[256] This was on the basis of technical staffing, paid for from the ASC budget, which never exceeded five in number, although an additional technical staff member, Peter Vass, was made available by CIPFA to support the work of the Public Sector Liaison Group.[257]

CCAB wrangling over the ASC budget became a recurrent theme. In January 1984, with ASC costs still not reaching the quarter million pound mark, a cost-cutting review of the CCAB budget by the ICAEW secretary and the president of CIPFA identified substantial savings by cutting back ASC operations.[258] In the event, the CCAB did not accept the recommendation and the levels of resourcing remained unchanged.[259] By 1989, the last full year of the ASC's operation, the budget was £440,000.[260] The increase in price levels between 1982 and 1989 was 39 per cent, implying a real increase of £92,500, although secretariat salaries probably beat inflation by some margin over the period. A combination of budgetary constraints and difficulties in filling vacancies[261] kept the secretariat small; for example in early 1986, the secretariat consisted of Peter Holgate (secretary), Susan Baker, Paul Ebling and Philip Pawson, with Vass still servicing the Public Sector Liaison Group.[262] Even this small staff remained vulnerable to budgetary pressure: when Susan Baker tendered her resignation in April 1986, Peter Holgate was warned that the post was likely to be frozen because the CCAB was looking for economies.[263]

At about the time of her resignation, Baker was spending about 40 per cent of her time on international work (staff support for IASC Board members, including attendance at three three-day meetings per year; review of IASC documents; support for the ASC International Committee; equivalent work for the Groupe d'Etudes; staff responsibility for UN and OECD groups, including assistance to the DTI; liaison with the FASB and other standard-setters) and also dealing with projects on pension costs, fixed assets and depreciation, and related party transactions. Ebling was working on changing prices; pension scheme accounts; a review of SSAP2 – which included at that stage both off-balance sheet financing and profit realization; accounting by charities; and fair value. Pawson's portfolio included segmental reporting; a review of SSAP9; and materiality. Holgate was working on changing prices and a review of SSAP6 as well as managing the staff and servicing the business of the ASC itself, including the Planning Committee.[264]

A further problem with the establishment was the rapidity of turnover, which affected both senior and junior staff. ASC secretary Keith Robinson left after two and a half years to take up an offer from Davison to become secretary of the Rules Committee at Lloyd's.[265] His successor, Brian Singleton-Green, was offered a better-paid post at the ICAEW just twelve months after being appointed.[266] In general, junior staff (under-secretaries, in the quasi Civil Service jargon of the ICAEW) also served only for brief periods: 'It is difficult to see a lifetime career as a member of the ASC staff.'[267]

Although the secretariat remained small in size, it is universally agreed that it was of excellent quality.[268] Even given their high quality, were there enough staff? Davison thought so:

> I believe that our high calibre young staff were fully capable of producing the work that the position of the ASC required and that a higher budget would not have been reflected in more effective output or greater progress given the temper of the times.[269]

Morgan agrees: 'We were tiny compared to the FASB, but all the better for it . . . The more people we had, the more prolific we would have been and that would have been a mistake.'[270] So does Holgate: 'We had a view of what we were supposed to be doing and we had the staff for it.'[271]

In judging this view, the role of the ASC's technical staff must be understood. While the nature of their contribution would, naturally, vary from project to project, in the main, by the time of the Watts review, the technical development of a document would be driven by the working party members and, particularly, its chairman. This approach significantly reduced the staffing required to support a project and also limited the problem of turnover; continuity was provided by the working party chairman and members if not by the secretariat.[272] It is also as well to remember that the structure and format of documents remained, by comparison with the output of the FASB and modern UK pronouncements, relatively simple:

> SSAPs were thin by today's standards but they were supposed to be; that was what was wanted. FASB had more resources and wrote long impenetrable documents and we didn't want to be like them. [The view at the time was that] they were wrong rather than [offering] something to be aspired to . . . The long and detailed basis for conclusions hadn't been invented.[273]

Of course, working party chairmen were volunteers with many other demands on their time and, at least potentially, vested interests. Could working party members be relied on to test ideas and phrasing in a detailed, rigorous, inevitably time-consuming way?

Opportunities Lost

The various enquiries, reports, schemes, proposals and debates which followed from the January 1987 decision to review the standard-setting process occupied well over five years – the original intention was that the review would be 'urgent'[274] – and absorbed a good deal of time and energy. Some outcomes were unequivocally for the better: embracing non-accountants and explicitly recognizing users, improving consultation and due process, provision for SORPs and Guidance Notes were among these.

Some outcomes were probably improvements and arguably did no harm. The famous move to make the ASC a more senatorial body facilitated widening of the committee's membership, raised its status and its members' commitment, and enabled it better to cope with increasingly complex and controversial topics. Some outcomes were unsuccessful but did no harm – for example public

hearings – and demonstrated that the profession was trying to improve things. Some outcomes were probably going to happen anyway, for example the (modest) increase in staffing.

Some outcomes, however unsatisfactory, were probably inevitable given the realpolitik of the day: the failure to make the ASC an independent body or even escape the multiple CCAB member vetoes, falls into this category. The problems caused by CCAB politics were not to go away, however, so we should score these as opportunities lost by the profession's unwillingness to recognize the consequences of its actions. A degree of separation, valuable at least as a symbol, could have been achieved by establishing an independent secretariat but the level of squabbling within the CCAB over budgets creates doubt about how well funded this group would have been.

One outcome might well have been within the grasp of the profession and would have added enormously to the effectiveness, status, strength and, probably, longevity of the standard-setting machinery it controlled: the adoption of a compliance monitoring and enforcement scheme operated jointly with City institutions including the Stock Exchange. Whatever the final result of the negotiations might have been,[275] the opportunity to put the scheme to the test was lost – thrown away – by internal wrangling within the CCAB. Perhaps more could have been done by Watts during the evolving discussions to keep the CCAB bodies on side, but one is bound to feel sympathetic over the pressures on a voluntary and supposedly part-time chairman, finding himself negotiating not only with City institutions but with his sponsors too.[276] Perhaps the other CCAB bodies – principally the ACCA – could have forced themselves to overcome their pique at their treatment by the ICAEW. But, however one apportions the blame among the CCAB bodies, it was an opportunity thrown away and some consider that, 'in one decision, they destroyed self-regulation of accounting in this country. It was a very, very important decision . . . fundamentally important.'[277]

8 The Art of the Possible: 1980–1984

> The way in which Tom [Watts] went about his role was to adopt a pretty consultative approach. I remember him saying very early on, 'standard setting is more a matter of politics than technical accounting, and, like any political exercise, it is a question of the art of the possible.'
>
> Graham Ward[1]

> Accounting standardisation is the art of the possible.
>
> Ian Hay Davison[2]

At the beginning of 1980, Tom Watts was about half way through his four years as chairman of the ASC. As we have seen, his review of the standard-setting process was becoming mired in political difficulties within the Consultative Committee of Accountancy Bodies, but at least in early 1980 there was a reasonable prospect that the co-operation of the City in an enforcement scheme could be obtained. The first quarter of 1980 saw the publication of a standard on current cost accounting, the new, essentially replacement cost-based system, designed in response to a collapse in support for the current purchasing power system. The standard had been hard-won after the profession's mangling at the hands of the government over its preferred CPP system. It was impossible, at that stage, to imagine the difficulties over CCA that still lay in store, and which we will examine in chapter 9. In the New Year of 1980, then, there were grounds for cautious optimism.

By the end of 1984, Watts' successor, Ian Hay Davison had completed his single, two-year, term and his own successor, Peter Godfrey was in place. Compliance remained a problem, following the abandonment of attempts to implement the scheme negotiated by Watts, and the ASC was struggling to find something to replace the new CCA standard. Meanwhile, attempts to narrow the areas of difference within historical cost accounting went on. The process had become 'the art of the possible'.

Foreign Currency Translation

When the ASSC's initial five-year work programme was drawn up, the ICAEW's Recommendation N25 'The Accounting Treatment of Major Changes in the

Sterling Parity of Overseas Currencies'[3] was less than two years old. After a major devaluation in November 1967, the UK appeared to be settling down to a new 'pegged' exchange rate of $2.40. Foreign currency translation was thus insufficiently urgent to appear on the work programme. The $2.40 rate survived until the collapse of Bretton Woods in 1971; thereafter the UK adopted a floating rate and the pound weakened against other leading currencies by an average of 7.3 per cent a year for the remainder of the decade, with the biggest single fall, 15.3 per cent, occurring in 1976.[4]

Recommendation N25 dealt with occasional major devaluations and made no formal recommendation on methods of translation under floating rates. However, a note described two methods for use under these circumstances, which it called 'closing rate' and 'historic rate'. Under the closing rate method all amounts are translated at the rate prevailing at the date of the financial statements. Under the historic rate method, fixed assets are generally translated at the rate at acquisition or later revaluation, long-term liabilities at the rate ruling when they were incurred, and current monetary items at closing rates. For stock, the rate should be that at acquisition but closing rate was also permitted. The note indicated that the two methods were 'equally acceptable in practice',[5] but pointed out that the historic rate method 'was evolved in the context of overseas branches and subsidiaries largely financed and stocked from the United Kingdom', whereas the closing rate method, which was becoming more popular, 'recognises overseas branches and subsidiaries as viable units existing apart from their parent, and by no means necessarily relying on their parent for finance or stocks'.[6]

In 1972 an Accounting Research Study published by the American Institute of Certified Public Accountants,[7] seeking a more logical approach than the various pragmatic methods recommended in previous US pronouncements, argued for the 'temporal' method. Under this method amounts are translated at the rate deemed appropriate to the date at which the amount is measured: historical cost amounts are translated at the historical rate and amounts measured at the closing date (including all monetary items and stock carried at market value) are translated at the closing rate. This was advocated on the grounds that, if the purpose of consolidation accounting is to present the financial statements of the group as if it were a single entity, foreign transactions should be recognized as if they had resulted from transactions of the parent.[8] The method may involve translating carrying amounts of fixed assets purchased years before at rates wildly out of line with current rates but, the argument goes, this is a consequence of adopting the historical cost basis of accounting, not an error in translation method.[9] The proposal was adopted in FAS8 'Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements', issued in 1975 as one of the Financial Accounting Standards Board's earliest statements.[10] Gains and losses were required to be taken to the profit and loss account in full in the period in which they arose.

The US standard attracted heavy criticism.[11] Under the temporal method, if a fixed asset is financed by a loan, the asset will continue to be translated at the

rate applying on its purchase date while the loan reflects subsequent changes in rate. The US dollar depreciated by 15 per cent between 1977 and 1979;[12] however strong the technical rationale underpinning the temporal method, if the parent currency is weakening, it looks to practical people as if funding the asset locally has covered the currency risk involved in holding it, so that recognizing a loss on the loan is artificial.

The ASSC's first attempt to grapple with the problem of changing exchange rates came in ED16 'Supplement to "Extraordinary Items and Prior Year Adjustments"', issued in September 1975.[13] This dealt only with the treatment of gains and losses on translation but reported that translation generally was 'under study'.[14] ED16's treatment of gains and losses dealt separately with those on fixed assets, which were generally to be carried to reserves as unrealized revaluation surpluses or deficits.[15] Where borrowing and the acquisition of a fixed asset were linked, a cover method, offsetting a gain on the asset against a loss on the borrowing would be permitted.[16] Although the draft provided fairly clear directions on the treatment of gains and losses, a year after its publication practice continued to exhibit considerable variety.[17] The ICAEW annual survey for 1976/77 showed that, of 41 companies disclosing their policy for gains and losses on net current assets, 24 took these to the profit and loss account and 17 direct to reserves.[18] There was, however, near unanimity on the choice of translation method: 94 per cent of the 253 companies disclosing their translation method used closing rate.[19] Prospects for a 'no choice' standard were, however, not as great as this statistic implies, because the remainder included some very substantial companies using the temporal method to comply with US requirements.

The ASSC's attempts to develop a price change accounting standard responding to the Sandilands report[20] were causing a certain amount of 'planning blight' elsewhere in its technical agenda and, as late as mid-February 1977, it was being reported that the development of a pronouncement on foreign currency translation was 'on ice' until the implementation of current cost accounting.[21] The pound's continuing decline, however, made this position increasingly difficult to defend and, by the end of the month, the ASC had appointed a panel to draft a pronouncement 'as a matter of top priority'.[22] The panel, chaired by Bertie Ogle, Deputy Treasurer of ICI,[23] was asked to produce a draft in time for consideration by the ASC on 28 March, a timetable described by Ogle, with some understatement, as 'extremely tight'.[24]

In April, Ogle briefed the press to the effect that he did not 'expect [the new ED] to differ very much from the existing ED16'. A provisional draft had been considered on 28 March, and there had been 'general support for it'. It had subsequently been discussed with a sample of major UK firms, a meeting that had been 'a great success'. The draft would return to the April ASC meeting, where he hoped that 'differences [would] be ironed out swiftly'.[25] However the same article reported James Carty, secretary of the ASC, as insisting that 'a compromise to allow for the US requirements [had] still to be thrashed out. "Many international firms are using the US 'temporal' method and it would be difficult to disregard it," he said.' The differences

between Ogle and Carty extended to appropriate procedures and the necessary exposure period:

> The confusion over the progress of the exposure draft on translation of foreign currency has brought a call from ICI's Bertie Ogle to change the way that the Accounting Standards Committee brings its wares to the public. Ogle was originally hoping to have his draft out by the end of May this year. Instead the secretary of the ASC, Jim Carty, is now expecting publication on 28 September ... Carty then sees a six month exposure period until April next year even though the last two drafts from the ASC were given three months. Ogle, who told *Accountancy Age* that he 'very much regretted the delay', believes that a three month exposure period would be long enough. He claimed that much of the delay so far was because the draft has been frequently going back to the ASC for 'relatively minor amendments'.[26]

ED21 'Accounting for Foreign Currency Transactions' appeared on 29 September and with a six month exposure period. It stated explicitly that it dealt only with historical cost financial statements[27] and permitted either the closing or the temporal method to be used, offering extremely brief explanations of the rationales underlying the two methods which essentially follow the characterizations of the methods included in N25.[28] A list of four advantages of the closing rate method is given without any compensating disadvantages or comment on possible advantages of the temporal method. Listed advantages of the closing rate method include the empirical claim that 'results are easily understood by users of accounts', though no evidence is given.[29]

The rationales offered for the two methods would have enabled the pronouncement to require a single method under specified circumstances but ED21 in fact permits free choice between the two methods. Treatment of exchange differences is unaltered from ED16. Although the press was quite clear that the draft 'allows the temporal method to be used to fit in with US requirements',[30] no explanation of the reason for allowing free choice is in fact given in the document.

Commentators were quick to point out that ED21 was 'a highly pragmatic text ... the first time that a UK exposure draft provides options which meet differing national requirements.'[31] A notable feature of the criticism was the attack on the tradecraft of the standard: 'ED21 is lightweight – light on standards, light in logic, light in explanations', said Cyril Shaw, BP's manager of group accounting research at an ICAEW conference to publicize the document.[32] The limited explanation of the rationales underlying the two methods was contrasted with FAS8.

Of the 44 submissions from preparers on the public record,[33] only 10 explicitly supported the free choice between temporal and closing rate methods although 20 gave no clear view, with many supporting the draft in general terms and thus, perhaps, by implication, accepting choice. The number explicitly supporting

free choice was just exceeded by the 12 respondents arguing that only one method should be permitted, in every single case this being closing rate. One submission sought freedom for an individual preparer to use a mixture of the temporal and closing methods. Only one respondent followed up the rationales offered for the two methods in the draft by suggesting that,

> Because the problems of accounting for foreign exchange gains and losses are complex and the circumstances of different groups diverse, it is unlikely that one set of rules can be found with general relevance to all companies. For this reason, our preferred approach would be for a draft Standard containing a far more rigorous analysis of the problems involved, leading to a rationale supporting each of a number of possible alternative solutions. By this means the suitability of the particular solution opted by an individual group could be tested both by the auditors and, assuming adequate disclosure, by the public at large.[34]

This submission was from Unilever; although he was not the signatory of the covering letter, the internal document reference suggests that its author may have been Allan Cook, of whom more later.

There was considerable opposition to the splitting of exchange differences. Only one preparer explicitly supported it and 26 explicitly opposed the draft on this point, with 20 advocating taking all differences to reserves, four to the profit and loss account, one to either, and one indicating no preference. Several preparers advocated policies they themselves used, with little or no technical defence other than the implication that their use of the method demonstrated its virtues. One company (British Leyland) simply analysed the differences between its own policy and ED21, making no explicit recommendation but presumably implying that the draft needed to be aligned to its own policy. Dowty concluded their submission as follows:

> I enclose a copy of my company's accounts for the last year and would draw your attention to the treatment of the translation of foreign subsidiaries' accounts . . . We regard this as a model of simplicity and would not easily be persuaded that any change from this method would be more informative to our shareholders.[35]

Again, Steel Brothers began by quoting their policy and continued, 'consequently we are able to accept some of the Exposure Draft's proposals'.[36]

Why was there such sharp criticism of a draft which allowed not only the method adopted by 94 per cent of preparers[37] but also the next most favoured alternative? Lobbying on standards was moving away from being a straightforward, 'single-issue at a time' exercise to involve more sophisticated manoeuvres addressing a range of technical subjects combined with attitudes towards standard-setting itself. For preparers who did not need the temporal method to be available, criticizing free choice became an opportunity to attack standard-setting

generally. Another issue in play at the time was accounting for research and development expenditure,[38] for which a revised exposure draft *requiring* capitalization of development expenditure meeting certain criteria was in the course of conversion to a standard. BP's Shaw pointed out that,

> when we were debating ED17 on research and development, some of us wanted the standard to say that research [actually, development] should be written off but in certain circumstances may be capitalised. We were told quite emphatically that a standard could not give an option and that research must be capitalised if it fell within the regulations.[39]

Shortly afterwards, SSAP13 was issued, permitting exactly this choice.

In some cases, opposition to the free choice in ED21 seems to be almost retaliation for loss of choice on earlier subjects:

> We find the latitude allowed in this instance in total contrast to the rigid attitude adopted in SSAP9 on Stocks and Work in Progress where prohibitions were placed on the use of such techniques as LIFO and Base Stock which, in our opinion, should have been permissible options.[40]

Another set of reasons relates to the desire of preparers to insinuate further options into the document. Shaw argued as follows:

> In my view, [ED21] fails because it is based far too heavily on pure theory, almost totally unsupported by the dirty practical experiences of reality. It envisages groups with almost independent subsidiaries with a full internal financing structure. It has not taken into account the reality of life in many groups where there is a tremendous volume of inter-company trading and a significant element of financing undertaken via current accounts.[41]

Yet BP's policy was to use the closing rate method and the 'pure theory' attacked by Shaw was designed to underpin this method. However, BP's treatment of exchange differences did not follow ED21, with substantially more categories of difference, including all differences on the re-translation of overseas subsidiaries, taken direct to reserves.[42] Thus a standard even more flexible than ED21 would have benefited BP.

In December 1977, the IASC issued E11 'Accounting for Foreign Transactions and Translation of Foreign Financial Statements', which permitted both the closing and temporal methods and, in addition, permitted gains and losses on long-term monetary items to be deferred and written off over the remaining life of the item.

By May 1978, the exposure period was completed; Ogle was quoted as saying that he hoped the adverse comments would not delay the production of a standard. 'I think the six months exposure period was too long', he was still complaining, 'now we have got to get down to work.'[43] The ASC appointed a

panel to review the comments and make recommendations. Ogle chaired the panel and its other members were Norman Berman of National Westminster Bank, Henry Gold, of Shell and M. E. G. Graham, of Unilever.[44] Shell was vehemently opposed to the use of the temporal method in the USA; it reported using US practice and was regularly suffering the effects of FAS8.[45]

Five months later, Ogle was apparently still reviewing the comments received and was predicting that the next document would not appear until spring 1979, nearly a year after the end of the, he thought excessively long, exposure period: 'at this stage I believe the proposed changes will be significant enough for the ASC to insist on a further exposure draft.'[46] He declined to be drawn on what changes were likely; 'there had been little common theme in the comments received.'[47] In fact, the revised exposure draft arrived not in spring 1979 or even spring 1980 but in the autumn of that year. Delays were due in no small degree to developments in the USA.

During the course of 1979, the FASB had been slowly agreeing a version of the closing rate method. In April it agreed that stock should be translated at closing rate; in June that the closing rate was generally preferable; and in October that gains and losses on current assets and liabilities should be taken to profit and those on long term items amortized over the life of the related item. The stance that all gains and losses should pass through the profit and loss account sooner or later was related to the Board's view that the purpose of consolidation was to present the financial statements of the group as if they were the accounts of a single entity.[48] In August, Canadian, UK and US standard-setters had met at the FASB in an attempt to co-ordinate their national standards.[49] The Canadians had suspended the relevant section of the Members' Handbook, adopted in 1978, which required the temporal method and amortization of gains and losses on fixed assets and long-term liabilities, on the announcement that FAS8 was being reviewed.[50] The meeting took place at their initiative. The UK delegation consisted of Robert Willott, ICAEW Technical Director, Carty and an ASC member, Stanley Wilkins. After their return, Wilkins was quoted as saying: 'We don't see any method which is better at meeting the problems than that suggested in ED21, but we keep an open mind. And we might be willing to give a bit in the cause of international conformity.'[51]

Although international opinion now seemed to be converging on the closing rate method, there remained plenty of scope for disagreement about the treatment of exchange differences. In the UK, the ASC was working on a 'net investment concept/situational approach', which had been considered, and rejected, by the FASB in the course of developing FAS8.[52] A note from the ASC secretariat explained:

> Exchange differences arising in the local currency accounts by the translation of any items denominated in a currency other than the local currency are fundamentally different to exchange differences which arise on consolidation. The former represent interim estimates of value of operational assets/liabilities that will be payable/receivable in the future and should be

> reflected in the profit and loss account. The latter arise on restatement of local currency net assets that are not expected to be converted to the group currency in the foreseeable future. As such they are considered to be similar to a revaluation of fixed assets which should be taken to reserves rather than to the profit and loss account.[53]

The note pointed out advantages of the method – it preserves the ratios from the original financial statements and avoids differences in the numbers occurring depending on the route by which inter-company lending is passed between subsidiaries – but, importantly, also drew attention to some problems:

> The balance sheet values that arise as a result of using this approach for non-monetary items may be difficult to interpret without segmented information or local revaluations . . . Use of the net investment concept conflicts with the traditional accounting approach of preparing consolidated accounts as if the parent company and its subsidiaries were a single entity.[54]

The September meeting of the ASC was told that the intention was to wait until the FASB had finalized its pronouncement, at that stage due later in 1979. If the text was acceptable, the ASC would follow its approach.[55] Attempts to co-ordinate development continued, with a further meeting of the British, Canadian and US standard-setters taking place in February 1980, again at the FASB. Carty was appointed an observer member of the FASB taskforce preparing its pronouncement.[56] One difficulty was that the FASB was itself divided about how to proceed, so that knowing the outcome of the vote at any one meeting did not mean the ASC could be confident of the final decision.[57]

In April Carty returned from a meeting, confident that the Americans would be adopting the net investment approach. The press was briefed:

> 'ASC has spent a year persuading the FASB that closing price should be the one used in translating foreign currency transactions', an ASC spokesman said. 'We have to continue to tread carefully because although the Americans have agreed with us on the main principles, when it comes down to the detailed working-out there may be differences. And it is because we do not want to pre-empt anything that they might do that we are opting for a discussion paper and not an exposure draft', he said.[58]

That they had got there under persuasion from the British, rather than as a response to pressures in the USA, might have come as a surprise to the FASB. The following week, the ASC met. Once again, the secretariat and the chairman of the working party were at odds. Before the meeting, it had been intended that the next stage would be a discussion paper. However, after a 'strong effort' by Ogle, the ASC agreed to issue an exposure draft.[59] One justification for a discussion paper would have been that the net investment concept was a new system, unlike any embraced by ED21.

Once again, Ogle was set a tight timetable: the May meeting of the ASC considered the panel's proposed revisions[60] and called for a further draft by the end of June. Release of the pronouncement was to be timed to coincide with the FASB exposure draft.[61] In August 1980, the FASB's exposure draft was issued, having been approved by four votes to three, the three dissenters preferring to retain FAS8's approach on grounds of conceptual rigour.[62] Press reports after the decision indicated that the UK draft would be published in August with an exposure period lasting until the end of November.[63] By late August, the ASC was issuing a press release describing the US document as, 'similar in all material respects to an exposure draft prepared by the ASC [which] is likely to be published toward the end of September'.[64] The release explained that the delay was a result of the pronouncement going through the ASC's balloting procedure, 'which takes more time than the comparable process of the FASB'.[65] Watts described the US exposure draft as a 'joint effort'[66] and explained that similar efforts were being made on price change accounting and pension costs. Interestingly, some press comment referred to 'the net investment or "Unilever" method'.[67] ED27 'Accounting for Foreign Currency Translations' in fact appeared on 27 October 1980.[68]

Watts announced the new draft with the words, 'Thank God we've solved it.'[69] He described the new draft as 'more stringent'[70] than ED21, although of course, it was more stringent chiefly in ruling out a method used by almost no preparer in the UK and now not needed by British preparers with a US listing. The change in treatment of exchange differences meant that more now went to reserves, the approach favoured by the majority of preparer respondents to ED21. ED27 was nearer to US practice in more than one respect: it was a good deal longer than ED21 – 38 pages against 10. Nonetheless ED27 was substantially shorter than the FASB's document and Watts asserted that the ASC 'takes credit for saying the same thing in one tenth of the space'.[71]

ED27 adopted what it called the 'closing rate/net investment method' except that, 'in those circumstances where the trade of the subsidiary is a direct extension of the trade of the holding company',[72] the temporal method would be used. This characterization of the approach differed from the American. The FASB's depiction of its chosen method starts by requiring that all assets, liabilities and operations of foreign entities be measured in their 'functional currency'. For entities which are an extension of the parent, the functional currency is that of their parent, so that if their books are maintained in local currency, a re-measurement process, intended to yield the same result as if the underlying books of record had been maintained in the functional currency, is needed. Once this has been done the items are stated in the reporting currency and no *translation* is needed. Thus translation is only needed where foreign operations are relatively self-contained, so that their functional currency is the local currency. As a result of this neat logic, the pronouncement is able to say that *all* translation should take place at closing rates.[73] For the USA, therefore, there are not two methods, to be used under different circumstances, but a single method. The Preface to ED27 refers to the US terminology of a 'functional currency' but the draft proper does not employ the term.

One issue not previously referred to is the rate at which the profit and loss account should be translated under the closing rate method. Although the use of the closing rate for this purpose appears consistent with that employed for the balance sheet and the underlying rationale for the method – for example it leaves ratios of profit and loss account to balance sheet items undisturbed – an alternative is to use the average rate over the period. ED21 permitted either approach. The Preface to ED27 explained that the average rate was now to be required on three grounds:

> (a) it more fairly reflects the profits and cash flows which arise throughout an accounting period;
> (b) the profits disclosed in quarterly statements do not have to be restated if the exchange rate is different at the year end from the rates prevailing during the year;
> (c) the FASB exposure draft makes the use of an average rate mandatory. In view of the extent of international harmonisation achieved in this whole area the method of translation of the profit and loss account would not appear to be of such importance that it was necessary for there to be a difference between the standards.[74]

This was a late change in the ASC's draft revised ED, which at one stage, like ED21, permitted either method.[75] It is revealing that paragraph (b) refers to quarterly reporting – the US requirement – and not to interims generally, or half-yearly figures – the UK requirement – to which the argument applies equally strongly. There was really only one consideration – the desire to be consistent with the USA.

The cover 'concept' employed in ED21 did not entirely disappear. A parent or UK subsidiary taking out a foreign currency loan to finance an equity investment in a subsidiary or associate overseas would, if ED27's general method was strictly applied, be required to take gains or losses on the loan through its own profit and loss account, and thus through the group profit and loss account, while the changes in the value of its underlying investment brought into the consolidation passed through reserves. ED27 permitted the two to be offset against each other under prescribed circumstances.[76]

ED27 omitted some of the arguments in favour of the closing rate method offered in ED21. Arguments that the method is easy to use and its results easy to understand were dropped. As Christopher Nobes said of the latter argument:

> It may be easy to *think* that one understands the results, but real understanding is almost impossible. This is because the closing rate method involves, for example, the translation of a US subsidiary's asset balance in 1960 dollars using the exchange rate for dollars ruling in 1980.[77]

Another omission from ED27 was discussion of the difficulty of reconciling the closing rate/net investment method with the objective of consolidation as being

to 'present the information contained in the separate financial statements of the holding company and its subsidiaries as if they were the financial statements of a single entity',[78] a problem alluded to in the ASC's briefing notes of November 1979.[79] For good or ill, the FASB's much longer document addressed rather than ignored such issues.

The level of co-operation that had taken place in the development of the British and US exposure drafts became the subject of conflict with continental Europe. The IASC, whose secretariat was now led by Allan Cook, had developed a draft exposure draft which closely followed the British, US and Canadian documents. There was, however, doubt about whether it would be issued because, although countries including Germany, France and the Netherlands did not necessarily dispute the merits of the approach adopted, and the closing rate method was popular in continental Europe,[80] they were reluctant to appear to be simply following the British and US lead, a move which would reinforce what was already a widespread perception of International Accounting Standards.[81] An IASC meeting in November requested that future meetings to co-ordinate national standard-setting should include an IASC presence.[82] It also agreed to publish the document that had been developed, but as a discussion paper rather than an ED.[83]

At its November meeting, the ASC agreed a timetable for consultations on ED27 including public hearings and a meeting with finance directors.[84] Meanwhile, towards the end of December, the FASB's public hearings took place. There was near universal agreement on the use of closing rates but numerous disputes on the detail; 'naked self interest was the only consistent position that emerged', according to Lee Seidler, an analyst with Bear Stearns.[85] Most worrying, from the British point of view, was that the level of objections made it likely that a second US exposure draft would be needed, with further delay and the possibility of a third UK draft.[86] Further international meetings of standard-setters were taking place, now also involving the IASC.[87] The meeting between the ASC and finance directors was relatively supportive, the major objection raised being to the requirement to use average rates in the profit and loss account.[88]

The UK public hearings were poorly attended. The first day began with an audience of sixteen, some of whom were queuing to make a presentation. After lunch, the session got under way with an audience of only nine, rising to twelve when the next speaker appeared with two colleagues.[89] The most common theme, at least among preparers, was a preference for closing rates in the profit and loss account, or free choice.[90] The Unilever representative approved of the overall approach but preferred closing rates in the profit and loss account.[91] The Price Waterhouse representative argued for disclosure of a geographical breakdown of foreign assets and liabilities, something else suggested in the earlier ASC briefing note on the net investment method.[92] This proposal was 'met with horror'[93] by the Unilever representative – remember that Unilever was getting pretty well the accounting treatment it wanted; indeed, it was getting 'the "Unilever" approach'.[94] Notwithstanding the poor turnout, Watts professed himself convinced of the usefulness of the occasion.[95]

In April it was announced that the FASB would be issuing a second exposure draft.[96] The draft was issued at the end of June. Again, the vote was four to three; the chairman, Donald Kirk, was among the dissenters.[97] The changes brought the pronouncement even nearer to ED27; according to the FASB there were now no major differences.[98] In November the FASB agreed a new standard, FAS52 'Foreign Currency Translation',[99] which was issued in the following month for adoption for periods beginning on or after 15 December 1982; note that preparers got twelve months' notice prior to the beginning of the period in which the pronouncement had to be applied. Yet again, the vote was four to three, with the dissenters including the chairman.

By March 1981, the ASC had received the submissions on ED27, 107 in all, with 46 from companies.[100] The total was down a little on ED21 but the number of companies was almost exactly the same.[101] Of the companies submitting on ED27, 22 had previously made representations on ED21. Most submissions now supported the principles set out in the draft; the most common objection was to the requirement for average rates to be used in the profit and loss account, with commentators more or less evenly divided between average and closing rates. Another common request was a relaxation of the terms for the application of the 'cover' method.

In September, Watts explained that ASC members would comment on a draft standard in October and that the working party would then follow their points up.[102] Ever the optimist, Ogle, in the USA to observe the FASB agree its new standard, said that he expected to finalize the UK proposal by the end of November. The draft standard now allowed closing rate in the profit and loss account, whereas the US standard, like the previous exposure draft, required the average rate.[103] Despite having yet actually to *adopt* a standard, the British remained gung-ho about winning the race; they would pip the Americans at the post because SSAPs gave little or no notice prior to the beginning of the period of mandatory implementation. The November meeting of the ASC would consider the latest draft of the standard: 'I hope a new standard would be effective for January 1982 – not 1981 financial statements', said Watts.[104]

The ASC did indeed consider a draft standard in November. Its problems of poor attendance affected the meeting and a gossip columnist was able to point out that only nine members of the committee were present and, of these, two, Ogle himself and Jeffrey Pearcy, were ICI men – though Ogle had by now retired – and 'ICI has rather particular ... views on the subject.'[105] As the columnist concluded, 'it's hardly the ideal way to hammer out accounting standards, is it?'

The final stages in the development of the standard were to be very far from straightforward. The first difficulty to emerge with the November draft concerned what had hitherto been regarded as an uncontroversial matter: the inclusion of exchange gains on monetary items held by individual companies in the profit and loss account of the company concerned. The EEC Fourth Directive had by now been incorporated into British law by the 1981 Companies Act.[106] It required that profits should be included in the profit and loss account only

when realized.[107] When the detailed implementation of the Directive in UK law had been under discussion, the CCAB had recommended that realized profits be defined by reference to generally accepted accounting principles, and the acceptance of this recommendation 'was regarded as a triumph'.[108] The Department of Trade now made it clear, however, that what constituted generally accepted accounting principles was, as with any other legal expression, a matter for interpretation by the courts; use of the phrase did not pass the initiative back to individual accountants or bodies of accountants. The ASC had previously believed that, even if there was doubt about a standard complying with generally accepted accounting principles, companies would be able to invoke a further provision of the 1981 Act which allowed directors to depart from the requirement where it appeared to them that there were 'special reasons' to do so.[109] The Department, however, was reluctant to accept that special reasons could arise as widely as would be needed in this case.[110]

The DoT's views were confirmed to the ASC by letter on 9 December 1981.[111] A meeting to discuss the problem took place on 21 December between ASC members and staff and officials from the Department's Accountancy Services and Companies Divisions and its Solicitors' Department.[112] The Department's view was that gains on monetary items denominated in foreign currency were not realized because the exchange rate could move in future in the other direction.[113] Arguments that gains were already realized in money terms, albeit foreign money 'would not comply with the intent of the Fourth Directive and might not be acceptable to other EEC countries'.[114] The particular intent of the Directive referred to was the prudence concept, now embodied in the Act.[115] It was, apparently,

> no secret that certain of those concerned with the relevant Directives in the Commission and elsewhere in the Community do have difficulty with what they understand to be the way in which the concept of realisation is to be applied by the ASC in the foreign currency translation context.[116]

Although the 1981 Act defined realization in the terms already described, this was an attempt to comply with the Fourth Directive and, if it were shown in the European Court that it failed to do so, the Act would have to be amended. Further,

> the effect of [the definition of realisation] is not that if a standard states that in particular circumstances a profit falls to be treated as realised, then the profit is necessarily realised. The effect is rather that a profit is realised if it falls to be treated as realised in accordance with generally accepted principles whether or not that treatment is prescribed by a standard. In other words, accounting principles do not become generally accepted simply by virtue of being embodied in a standard. It is not inconceivable that a standard may embody principles which are not generally accepted (but on which, for example, the profession considers it right to give a lead). Of course, once

> embodied in a standard, a principle may thereby rapidly become generally accepted because of the authority carried by a standard on accounting matters: there is therefore no doubt that accounting standards will carry very considerable weight in this context.[117]

This consideration is described by the writer as 'somewhat nuancé'.[118] It suggests that, if the ASC did wish to 'give a lead', it would have to issue a standard asserting that an item *is* realized and *should be* included in the profit and loss account but adding a note to the effect that, since the assertion is not yet generally accepted by accountants, the item is, in law, *not* realized for companies and *should not be* included in the profit and loss account, until such time as the assertion is generally accepted by accountants, which acceptance they cannot signal by treating the item as realized, since no one accountant knows at any moment the judgement of their colleagues. Not quite the triumph the CCAB had supposed.

The meeting on 21 December started the attempt to make sense of all this. The DoT accepted that, if a satisfactory definition could be found, gains on short-term items could be regarded as realized[119] and suggested that the realization of long term gains 'should be considered in conjunction with the prudence concept'.[120] One gambit the ASC tried was to include gains in the profit and loss account and then transfer them out again immediately to a non-distributable reserve, but this was unsuccessful.[121] Eventually the approach settled on was to emphasize the need to employ prudence in recognizing gains on long-term monetary items and thereafter to resort to the 'special reasons' provision, the special reason in this case being the need to show a true and fair view.

In May 1982 the ASC let it be known that a revised draft had been approved by ASC members in a ballot.[122] One report continued: 'It now only remains for the councils of the bodies in the CCAB to give final approval for the standard to be released. The standard should appear by the end of July.'[123] The prediction was to prove, yet again, very optimistic.

The proposed standard was approved by the Councils of five of the six CCAB bodies and it was at first expected that it would be published on 2 August.[124] The Association of Certified Accountants' Technical and Research Committee considered the draft ahead of Council, apparently in an attempt to speed progress[125] because of the tight timetable imposed by the ASC. However, the committee declined to recommend adoption.[126] When the draft was considered by the ACCA Council, Frederick Bleasdale, Vice-President of the Association and an assistant general manager at Midland Bank International, persuaded his colleagues to veto the draft because of difficulties he believed it would cause for the banking sector. The problem concerned the application of the cover concept, which was restricted to consolidated financial statements. Banks that held overseas investments directly and used foreign borrowings to finance them, thereby hedging the exchange rate risk, would not be able to reflect the hedge in their own financial statements.[127] The issue had featured in the ASC's discussions with the DoT in February and the draft reflected what the ASC had been

able to persuade the Department to accept as within company law.[128] Ogle, himself a certified accountant, said of the ACCA's late intervention, 'I am absolutely disgusted, mainly because they have waited so long.'[129] Christopher Morgan, Director of Accounting Standards, 'was also surprised at the timing of the rejection. "This point was extensively debated and was settled in March," he said. "We had no comeback then."'[130] The ICAEW President contacted his counterpart at the ACCA but was unable to persuade him to change the Association's position.[131]

Talks took place between the ASC, the DoT and the ACCA but were inconclusive.[132] Indeed, a second problem emerged: the way the draft addressed the realization of gains and losses on short-term monetary items was felt to imply that banks would be required to exclude their exchange dealing profits from operating profit.[133] The ACCA had previously been persuaded to allow this to be dealt with in the Technical Release accompanying publication of the standard (supposing that this event might ever occur), but the DoT now felt that it was so important that it should be addressed in the standard.[134] Further talks took place with the British Bankers' Association.[135] The bankers' preference was to be exempt from the standard; Bleasdale was quoted in *Accountancy Age* as saying, 'We want the banks to be excluded. The law relating to banks is developing at a slower pace than other company law and this gives a perfectly valid reason for the exemption.'[136] By now whether his 'we' referred to the ACCA or the banks was unclear. At one stage is seemed likely that an exemption would be needed to get the standard on the books;[137] the ASC was unwilling to grant such a concession[138] but, so long as the bankers' influence extended to persuading the ACCA to exercise its veto, such a course might have to be contemplated. Once the extent of the problem emerged, it was clear that the new draft would have to do the rounds of the CCAB Councils again. It was, nonetheless, hoped that a compromise might be found that would enable the September meeting of the ASC to approve the changes.[139] The bankers, however, played a long game, a spokesman reporting at the end of that month that, 'the banks are still considering the changes which they would like to see made.'[140] Meanwhile, the continued scrutiny the document was receiving provoked the DoT to raise a further series of queries.[141]

BBA and ASC representatives met in October and a revised draft was developed. There were further delays when the ASC's legal adviser reviewed the draft and felt that there were still problems relating to realization and the distribution of gains.[142] At long last, the January 1983 meeting of the ASC was able to approve a draft and despatch it to the CCAB bodies.[143]

This time the draft cleared all the hurdles. In April 1983 – seven years after ED16, five years after ED21, and 29 long months after ED27 – the new standard, SSAP20 'Foreign Currency Translation', was issued. In an interview to mark the publication of the standard, Ogle made one final prediction about foreign currency standardization in the UK, warning that SSAP20 would 'probably only be good for a few years'.[144] Like all the others, his final forecast proved to be wrong. SSAP20 unquestionably stood the test of time: it remained

extant, unamended, until the adoption of the international accounting standards regime in 2005.

The principal change from ED27, so far as most preparers were concerned, was that the profit and loss account could now be prepared using either average or closing rates, the change most frequently called for by commentators on the draft.[145] In addition, the application of the 'cover' concept was relaxed, both within the consolidated accounts and by extending it to the accounts of the investing company. It remained permissive. The standard's note on legal requirements,[146] and an uncharacteristically lengthy accompanying Technical Release,[147] explained the approach that had been taken to address the problem of the application of the realization test to gains on long term monetary items. Such gains were to be included in the profit and loss account on the grounds that the need for symmetrical treatment of gains and losses, in order to show a true and fair view, constituted a special reason for departure from the realization principle, in accordance with paragraph 15 of the relevant Schedule to the Companies Act.[148] Symmetrical treatment was required because gains can be determined no less objectively than losses and differential treatment would 'be illogical . . . [and] inhibit fair measurement of the performance of the enterprise'.[149] The ASC considered it 'more appropriate' to invoke paragraph 15 than the true and fair view override itself,[150] although the distinction between the need to show a true and fair view constituting a special reason for departure from the realization principle and a ground for overriding the principle must have struck some readers as fairly subtle. A further section of the Technical Release dealt with questions of whether some gains and losses under the standard might need to be treated differently for the purpose of determining distributable profits under new company legislation.[151]

The issues raised by the banks were reflected at a number of points in the standard and the Technical Release. Disclosure exemptions within company law for financial institutions were emphasized and the definition of a foreign branch was extended to include a group of assets and liabilities accounted for in a foreign currency.[152] One section of the Technical Release listed the principal differences between the UK and US standards.[153] In the large majority of cases it would be possible for a company to design an accounting policy for foreign currency translation that was compatible with both the UK and US standards.

Leases

The traditional method of accounting for plant and equipment leased by an entity, in the UK as elsewhere, was to treat the annual payments as hire charges, with no recognition in the financial statements of commitments to make payments in future years.[154] Footnote disclosure of forward commitments was regarded as best practice rather than obligatory. This approach caused little practical difficulty while the volume of leasing transactions was small; a Recommendation on Accounting Principles, issued in 1964, was concerned only with the accounts of finance companies, as lessors, and dealerships.[155]

Three inter-related factors raised the profile of lease accounting. The first was a major expansion in the volume of leasing, largely triggered by changes in the tax system rather than any change in the fundamental pattern of demand for finance. The increasing generosity of tax allowances on industrial plant[156] meant that many companies did not have sufficient taxable profit to claim the full amount of the allowance as it became available, so that the cash flow benefit of the reduction in tax was postponed. Banks, which need little industrial plant for their own operations, had substantial taxable profits and limited tax allowances, and from this imbalance a lucrative business opportunity was created.[157] The banks, via their finance house and leasing company subsidiaries, purchased eligible assets and leased them to customers, claiming the allowances against their banking profits and passing some of the benefits, perhaps around 80 per cent,[158] on to the lessee. Banks had no alternative use for the plant they were purchasing and were keen to avoid having it returned by customers who had no further use for it or could no longer afford the lease payments. Hence most agreements were, or came very close to, so-called 'full payout leases', under which the lease term represents the whole useful life of the asset and the payment stream covers the initial purchase price together with the cost of financing the arrangement and the lessor's profit margin.[159] For tax reasons, residual rights could not be sold by the lessor to the lessee, so any value of the asset at the end of the lease term was passed to the lessee by other routes, for example by the lessee being entitled to continue the lease at a peppercorn rent.

The result was an explosion in leasing activity, from £288 million in 1973 to £2,894 million in 1983,[160] of which only a little over a third was attributable to inflation. It was not long before managers began to appreciate that the new form of finance, combined with the old way of accounting for leases, had cosmetic advantages and leasing became one of the first forms of 'off-balance sheet financing':[161] the lessee had the full use of the asset over its economic life but it did not appear on the balance sheet and neither did the commitment to a stream of future payments. Compared to a competitor purchasing equivalent assets and borrowing to finance the purchase, the company using leasing would have a lower gearing ratio and thus lower apparent risk and greater freedom to borrow further.

The second factor to raise the profile of lease accounting was perhaps an inevitable consequence of the first: a high profile financial collapse associated with previously undisclosed lease commitments.[162] Court Line was a diversified group with many operations in the leisure industry, including a package holiday business using leased aircraft. It collapsed in August 1974. Why did the company fail? In the words of the subsequent DTI Inspectors' Report:

> The short answer is that there was no single reason for the collapse, which was caused by a number of contributory factors. Court Line expanded rapidly in many directions, some of which were both logical and justifiable, others not. The overall management was throughout inadequate, and it was in any event never supported by the necessary financial control. This meant

> that, as Court Line expanded, it became progressively vulnerable to any substantial setback in any of its areas of activity.[163]

Within this gloomy picture, the holiday airline business had been in many ways quite successful,

> but its one failure, the acquisition of the Tristars [ie. the aircraft obtained on lease], was a major one . . . Whilst the acquisition of the aircraft was a bold decision, it was in [the Inspectors'] opinion quite certainly a wrong one. Many . . . subsequent problems . . . were a direct result of the acquisition of the Tristars, since this took them outside the philosophy of their business as expounded to us by Mr Young [the managing director] that the aviation business should be conducted like their shipping business, as charters and not operators.[164]

In September 1973, the group had non-cancellable leasing obligations totalling around £40 million while shareholders' funds in the group balance sheet at the same date amounted to approximately £18 million.[165] In accordance with permitted practice at the time, the leasing obligations were not disclosed although, in the Inspectors' view, they should have been.[166] To make matters worse, the non-disclosure took place in a context in which, the Inspectors concluded,

> it appears to us that whenever there was a doubt about the possible methods of application of accounting practices, Court Line chose the method which reacted most favourably on profit for the year. We do not believe that this happened by accident. We believe it to be a deliberate decision of management.[167]

In the absence of an accounting standard or recommendation, both the directors and the auditors were able to tell the Inspectors that they would have had no objection to disclosing the amount of leasing obligations, 'but nobody made the suggestion'.[168] Although the full facts of the Court Line scandal did not become known until the publication of the Inspectors' Report in 1978, the underlying problems were apparent in 1974 and an interim report was published in 1975.[169] One of the DTI Inspectors was Douglas Morpeth, vice-chairman of the ASSC.

The third factor was the decision by the FASB to develop a standard on leasing. A Discussion Memorandum was issued in July 1974 and FAS13 appeared in November 1976.[170] Prior to this, US practice was similar to that in the UK.[171] The FASB approach divided leases into two categories. A 'capital lease'[172] is one that, in essence, 'transfers substantially all of the benefits and risks incident to the ownership of property'[173] to the lessee and is 'accounted for as the acquisition of an asset and the incurrence of an obligation by the lessee'.[174] At the time the lease is entered into, the value of the asset is brought onto the balance sheet together with the liability created by the obligation to

make the stream of future payments, discounted to reflect the benefit of making those payments over time. As time passes, the carrying amount of the asset is reduced by depreciation and payments under the lease are apportioned between repayments of the borrowing and finance charges. The FAS also contains provisions relating to the treatment of a capital lease in the financial statements of the lessor, designed to record it as a 'sale or financing',[175] depending on whether the transaction has the character of a dealer's sale or a financial arrangement, with the lessor's asset being its claim on the lessee rather than physical property.[176]

In December 1974 the press carried news that 'a new exposure draft on lease accounting [would] be published next summer following the setting up of an ASSC working party.'[177] As the first stage of work on the project, the ASSC had commissioned a research report from Arthur Young, McClelland, Moores & Co. and the chairman of the working party was Paul Rutteman, a partner in the firm. By February 1975, before the ASSC working party had even met, the project was already embroiled in controversy. One subtle but important complexity arising for lessor accounting concerns the pattern of profit recognition; given that a method should be found which yields a constant rate of return on cash invested in the lease, what profile of cash flows should be incorporated in the calculation? Approaches can be broadly classified between pre-tax and after-tax methods. After-tax methods, such as 'the investment period method', treat the receipt of the tax allowance in cash as a recovery of cash invested in the lease. Since that receipt occurs early in the life of the lease, and thereby reduces the amount of the cash investment to which the constant rate of return is applied, such methods recognize most of the profit early in the life of the lease.[178] With a speed rare among those making representations to the ASSC, the industrial body representing leasing companies, the Equipment Leasing Association had already made a submission advocating the investment period method.[179] Stockbrokers Greene and Co. responded with a report containing 'a hard-hitting attack on the investment period method' and advocating more conservative methods.[180] Press leaks in February suggested that the Arthur Young report would be likely to 'set the working party on the road to an investment period-based exposure draft'.[181] In June, with the banking industry (specifically the Committee of London Clearing Banks) about to issue a report expected to back the investment period method, the leaks were suggesting that, though the working party's views were 'in flux, it [was] not likely to accept investment period accounting'.[182] Meanwhile, the ELA's annual report explained that it had nominated two members of the ASSC working party[183] including Leslie Christmas.[184]

By July 1976, the working party had arrived at preliminary recommendations along the lines of US thinking, that is that lessees acquiring substantially all the risks and rewards of ownership (in the UK the term being used was 'finance leases') should include the underlying physical property in their balance sheets while the lessors treated their asset as the stream of future lease payments. Discussions of the proposals with consultative groups encountered 'strong opposition'.[185] The Inflation Accounting Steering Group[186] was also addressing

the issue of which party held the tangible asset, to be adjusted by reference to the prices of physical assets, and which the financial asset, to be valued by reference to future cash flows.[187] ED18, published at the end of November, followed the approach envisaged by the leasing working party, setting out very brief recommendations occupying less than two pages.[188]

Opposition by lessors to the proposed lessor accounting varied according to the precise methods the working party was thought likely to recommend. The ELA supported the investment period method, which, as we have seen, tends to recognize profit relatively early in the life of the lease, as being a more 'accurate',[189] and a 'truer and fairer'[190] method. Objections to the capitalization of leases in the accounts of lessees made in public included the fear that putting leased assets on lessees' balance sheets would somehow undermine lessors' legal title to them[191] and, more importantly, encourage government to give the investment allowance to lessees rather than lessors.[192] Lessees would then have to wait much longer before the benefits crystallized in cash and accordingly would suffer in economic terms. Less frequently publicised were two other considerations. The first was that this shift would also undermine, and perhaps completely erode, the incentive to lease rather than purchase with loan funding. Even if the reduction or elimination of cash benefits from tax allowances did not remove the incentive to lease, bringing the finance onto the balance sheet might nonetheless do so. Either effect would, in turn, cause severe damage to, and possibly even the demise of, the leasing industry.[193]

In December 1976, on the news that the FASB had adopted its standard, the secretary of the ASC told the press that the UK exposure draft on leasing would be with the ASC by the following March.[194] Another year passed and it was decided that two separate exposure drafts would be prepared, one for lessees and one for lessors.[195] In February 1978, meetings were held (separately) with about 35 representatives of leasing companies and another 35 from lessees.[196] Two controversial areas remained: sale and leaseback agreements and whether hire-purchase transactions should be included in the scope of the documents. The Finance Houses Association argued that no standard on hire-purchase or credit instalment transactions was needed because existing accounting methods were not causing problems. Recommendation N23 did indeed deal with the area in a way that was regarded by the ASC as adequate but it was not, of course, mandatory.[197]

At the meeting with lessors, the working party heard that they now accepted capitalization in the accounts of lessees,[198] a position that may have been connected with the working party's, now stabilizing, preference for after-tax methods of revenue recognition for lessors. By June, the ELA was, indeed, briefing the press that it was 'getting fed up waiting for the exposure draft':

> Leslie Christmas, chairman of the association's taxation and accounting sub-committee said this week: 'We're frustrated by this. In particular, the association wants a draft which sets down the investment period method of accounting as a standard for lessors. We've been waiting for over two years now so that our members can use it and have it accepted by the public.'[199]

Some firms were already using the method, of course, but the ELA wanted official backing for a method which front-loaded profit. The ASC secretary was now quoted as saying, 'we hope to publish in October, November time.'[200]

However, the following month the ELA's stance changed. Its incoming chairman, Tom Clark, led it into opposing the draft's proposals on lessee accounting. It now preferred disclosure of the obligation only by way of a note. The ELA's objections reflected the view that inclusion of an asset in the balance sheet should be based on legal title and that the proposed method could lead the government to move the tax allowance to the lessee. It denied that the probable consequential damage to the leasing industry was a motivating factor.[201] By October, the press was suggesting that 'a sustained campaign against the draft is . . . a distinct possibility,'[202] despite the fact that the ASC was letting it be known that the Inland Revenue had indicated that it was unlikely to seek any fundamental change in tax laws in the area.[203] Government economic departments had access to many sources of information about the funding flows arising from capital allowances, not least the tax returns of leasing companies. It surely would not take the publication of an exposure draft to tip the Revenue off, and it seems unlikely that it would have felt that an accounting standard was necessary to provide backing for a change in the treatment of tax allowances had the government wanted to make one.[204] If the ELA's fear was not the damage from a change in the allocation of tax allowances, it seems likely that it was concern about losing the incentive of off-balance sheet financing.[205]

As predicted by the press, the leasing industry continued to campaign against capitalization. In *Accountancy Age*, John West, a director of Williams and Glyn's leasing operations, suggested that, 'if put to the vote by the Institute, a proposal for capitalisation would be substantially defeated', a reference to the rejection of mandatory current cost accounting in this manner some 15 months earlier.[206] As far as the US precedent was concerned, he claimed that 'a great many people in this country object to the blind acceptance of American influence when we are European.'[207]

In March 1979, the IASC considered a draft pronouncement prepared by a working party chaired by Rutteman, largely paralleling the UK proposals.[208] It agreed only to circulate the proposals to member bodies.[209]

The ASC considered the subject in July but took no firm decisions; a final document was scheduled for the September meeting, with publication in November.[210] The ELA was now reported to be 'really quite relaxed'[211] about the danger of allowances being switched to lessees; the 'official ELA view' was that its concern was 'purely technical and prompted by the belief that capitalisation would confuse users'.[212] The September meeting confirmed that finance leases should be capitalized in the lessee's balance sheet, making an ED by November 'likely'.[213] In October, the ASC received formal confirmation from the Inland Revenue that adoption of a standard imposing capitalization would not lead it to seek a change in tax law or practice.[214] The British press was now carrying coverage of problems with the US standard.[215] In the first three years of its life, it had been amended four times and six interpretations had been

released. The cause of the problems was perceived to be, not the principle of capitalization, but the volume of detailed prescription, which now covered 121 pages. The ASC indicated that it was aiming to avoid the problem by issuing 'a very short standard which deals with major principles, plus a set of guidelines'.[216] In November, the ASC considered a full draft of the proposed ED and the guidance notes. Further revisions were agreed and it was decided that the documents would then be ready for balloting. The contents of the proposal were carried in the accountancy press in considerable detail;[217] finance leases would be capitalized and the net investment period method used by lessors. A publication date of February 1980 was suggested.[218]

In January 1980 the ICAEW held a conference to explain the ASC's proposals.[219] Clark threatened that there 'could, and perhaps should, be the same grassroots resistance as we saw in the case of ED18',[220] another reference to the ICAEW membership's rejection of mandatory current cost accounting. Apparently, 'Clark's speech was only one of a number which prophesied trouble ahead for the exposure draft on leasing.'[221] The ELA now had three objections to capitalization: that it ignored the legal position; that its complexity would discourage small and medium-sized enterprises from using a valuable source of finance; and that it represented a slippery slope towards capitalizing all sorts of long-term obligations.[222] It explicitly denied any concern about changes in the tax system.[223] On lessor accounting, the ELA 'believe[d] that the ASC's current proposals [were] an important step in the right direction' but that there should be 'flexibility in the method chosen by leasing companies to allocate estimated net profit'.[224]

In May, the ASC was still meeting leasing industry representatives.[225] *Accountants Weekly* reported that there was 'evidence of some behind-the-scenes lobbying of auditors by ELA member companies'.[226] Come October and there was still no UK draft although at the end of that month the IASC published its proposal, E19 'Accounting for Leases', requiring capitalization.[227] Again, the IASC had overtaken the British standard-setters. Even South Africa had published an exposure draft.[228]

December's issue of *Accountancy* carried the news that an exposure draft on leasing, which it referred to as ED28, was in 'its final stages of preparation for publication' and added, 'it may even make our Christmas stockings.'[229] But it was not to be. In February 1981, the expected publication date given to the press was May.[230] An attempt was made to respond to the ELA's criticism that the proposed methods were too complex by including a section setting out a simple, straight-line, basis for recognizing cost.[231] In April, the expected publication date given to the press was June.[232] In June, the document, now numbered ED29, was 'expected to be made public before August'.[233] In fact August saw the ballot stage of voting on the proposed draft but the ballot resulted in 'a substantial number of objections'.[234]

Watts attributed the scale of objections to newly emerging concerns about the economic consequences of the proposed treatment; the UK economy was now in recession and 'there was a substantial lobby which felt that capitalisation of

finance leases, and the consequent balance sheet liabilities disclosure, might inhibit industrial re-equipment programmes.'[235] As a result of the objections, it was decided to reconsider the document at the ASC meeting on 16 September.[236] The draft was now accompanied by a lengthy Preface setting out the case for the proposed treatments, but was otherwise largely unaltered.[237] The meeting approved the document but excluded the Republic of Ireland from its scope. This exclusion, the first territorial restriction, reflected the different tax system in Ireland. There, capital allowances were given to the business bearing the burden of wear and tear and it was thought that capitalization, with the consequent depreciation charges for lessees, might 'encourage individual inspectors to disallow capital allowances to lessors'.[238]

This time, there were no further hiccups and ED29 'Accounting for Leases and Hire Purchase Contracts' was published on 14 October 1981, a little over five years after the working party first agreed to recommend the methods which survived largely intact in the final document. Given its subject, the document is not particularly long: the ED proper occupies 58 paragraphs against, for example, 20 in ED22 on post balance sheet events. FAS13, the basic US pronouncement on leasing actually takes up fewer paragraphs (51 in all) but they are much longer. Perhaps the best measure of the terseness of the British standard is that FAS13 runs to approximately 11,000 words (excluding background information, the basis for conclusions, numerical appendices and a dissenting position) while ED29 uses 3,750 (excluding the Preface, which covers the same ground as the FASB's background information and basis for conclusions, and the Guidance Notes, which are the equivalent of the numerical appendices; no dissenting opinion was published in the UK). Does this differential entirely justify Carty's comment?

> We think that the British accountant has rather more intelligence than FASB thinks US accountants have. We are aiming for a very short standard which deals with major principles, plus a set of guidelines. The US approach in contrast has been to say, 'we must define everything'.[239]

In fact, the Guidance Notes are rather longer than FAS13's numerical appendices, suggesting that the ASC actually felt that British accountants needed more guidance – but not prescription.

The Preface occupied slightly more than half the length of the ED and justified the methods used on the basis of substance over form.[240] The objection that capitalization would cause companies to breach debt covenants is rejected on the grounds that legal advice had been received that the construction of a lease would mean either that it constituted borrowing regardless of the accounting or, more usually, that it would not constitute borrowing in law. A lengthy section sets out the arguments about possible economic consequences[241] of capitalization and invites comments. It is written in an almost sarcastic tone. The first possibility is the 'breach of covenant' argument: the earlier response is reiterated but the paragraph allows that 'the general advice may not be applicable in every

case'. It is pointed out that, 'no specific case has so far been brought to the ASC's notice', but, nonetheless, the 'ASC particularly requests submissions from any persons or companies who believe that their particular position might be affected in their own specific circumstances.'[242] Next,

> there is the more general and less tangible argument that the requirement to capitalise finance leases might inhibit some companies from entering into finance leases in the future . . . Or, to put it more baldly: that while some companies are prepared to use 'off-balance sheet' finance for the acquisition of productive assets, they would not acquire the assets if the finance came into the open and 'on-balance sheet'.

This paragraph concludes by echoing its predecessor: 'No cases have so far been brought to the ASC's notice, but again ASC invites submissions from any companies who believe they would find themselves in this position.'[243] The third possibility is the loss of tax benefits. The Revenue's undertaking is repeated and it is pointed out that the government would presumably take into account any economic consequences in deciding on a change in the system.[244] The section concludes by inviting 'commentators who submit reasoned opinions that there would be an unacceptable danger of adverse economic consequences'[245] to suggest an alternative approach, given that non-disclosure of material facts cannot be condoned.

The ELA's comments on the ED were published at the end of November. The Association called for the withdrawal of ED29, on the grounds that it ignored three matters 'of prime importance' and that because 'ED29 neither highlights these matters as discussion issues nor offers guidance on them', this 'remov[ed] much of its authority'.[246] The three issues were the danger of losing tax benefits (returning to a theme previously discarded by the ELA); the interaction between the financial evaluations of projects carried out by management and the financial reporting; and the basis for treating Regional Development Grants (RDGs). Of these, the most important was now thought by the ELA to be the treatment of RDGs,[247] non-taxable government grants designed to encourage investment in deprived areas. The grant would be reflected in the lease payments set, so that contracts might yield a pre-tax loss, offset by a taxation recovery based on the larger taxable loss resulting from ignoring the value of the grant in determining the tax allowance, to leave an after-tax profit. Some lessors were grossing up the value of the grant to show a 'normal' profit margin before tax but this was prohibited by the ED.[248] The Guidance Notes explained that this was 'not appropriate because it introduces into the financial statements an artificial transaction which falsifies the real position'.[249] The ELA considered that, regardless of the post-tax profit, the appearance of a pre-tax loss would discourage lessors from entering into contracts and thwart the government's intentions on regional development policy.

As far as the ASC – or, at least, Rutteman – was concerned, the treatment of RDGs was a side-issue: 'more a question of accounting for tax-free grants than

for leases'.[250] The ELA submission reads rather oddly – for example, given the outcome of the correspondence with the Inland Revenue on the subject, it is very difficult to substantiate the claim that the ASC *ignored* the argument about the potential loss of tax benefits. Some commentators suggested that, 'in many ways the response . . . is a confusing document. It is difficult to avoid the feeling that it [was] prepared as a rationale for a decision made long ago to reject the draft standard.'[251]

In March, public hearings on ED29 took place; turnout made the hearings on foreign exchange translation look positively overcrowded. Only five groups expressed an interest in appearing and the second day was cut.[252] The British Property Federation's concerns had already received a public airing;[253] the ELA reiterated its well-known points about capitalization and grossing up of RDGs and the FHA maintained its line on hire purchase accounting.[254] It is difficult not to sympathize with *Accountancy*'s headline: 'Were they worth the bother?'[255] Shortly afterwards, the IASC adopted its own standard on leasing, IAS17 'Accounting for Leases', which was to become operative for periods beginning on or after 1 January 1984, but with a four-year transitional period.[256] The terms of the standard were similar in outline to ED29.

In September 1982, the submissions on ED29 were made public. There were 137 in all – the highest number on any topic other than price change accounting since ED6 on stock. However, this outcome has to be understood in the context of a steady pattern of responses at a fairly modest level, numbering between 80 and 110,[257] so that the level of 'extra' interest was only in the order of 30 or so responses. Submissions ran to 456 pages with a 'lack of clear consensus'; needless to say the ELA's response criticized the capitalization proposal.[258] The following month, the ASC announced that it would be proceeding with the adoption of a standard 'broadly following the proposals in ED29'.[259] In view of the concerns about the implementation of the capitalization proposal, it would be phased in over a three-year transitional period, with disclosure as an acceptable alternative in the transitional phase. This approach mirrored the new IAS and the target implementation date would also correspond to that in the IAS, 1 January 1984, with the SSAP being issued in late 1983.[260]

Continuing negotiations with interested parties further protracted the redrafting. The draft standard considered by the ASC in July 1983 made a critical concession to the ELA; as Rutteman put it, 'The ELA were concerned about the treatment of RDGs. We have given them a compromise . . . allowing them to gross them up.'[261] It is difficult to see how this was a compromise, since the ELA got exactly what it wanted. The proposed standard also 'appeased' the BPF – *Accountancy Age*'s word, not Rutteman's – by including text which, in Rutteman's words, 'made it clearer that property leases would normally be operating leases'.[262]

In September, the Irish tax problem surfaced again. The fear that, under the Irish tax system, allowances would be switched to lessors remained[263] and the government was now conducting an inquiry into the tax treatment of the leasing industry, with its conclusions due to be announced in February 1984.[264] In the

light of this situation, the Institute of Chartered Accountants in Ireland sought a six-month delay in the adoption of the standard.[265]

No doubt bearing in mind that the tax authorities presumably knew what the economic and legal realities of the situation were without needing to have them unveiled by an accounting standard, the ASC Planning Committee recommended that the ASC should agree the proposed standard and send it to the CCAB bodies for adoption.[266] The ICAI then petitioned the CCAB itself for postponement.[267] The November meeting of the CCAB rejected the petition, having considered an exemption for Ireland but turning this down, partly because of concern about confusion caused by differences between the jurisdictions of the UK and the Republic of Ireland.[268]

Because the standard required the approval of the Councils of all six CCAB bodies the ICAI was in a position to insist on a delay of six months in the adoption of what had by now been given the number SSAP21, and this it effectively did. There were hopes that the Irish government would offer a definitive statement on the tax position by the new year but it failed to do so and the January 1984 meeting of the Irish Council again refused to approve the pronouncement. Hopes were then pinned on the government's budget announcement on 25 January, but the Irish Institute president, Margaret Downes, subsequently told the press that, although this had 'gone a long way to clear the position ... it [was] not definitive'.[269] The February Council meeting reaffirmed the veto, although by now other CCAB bodies were becoming impatient.[270] The Irish budget in fact removed the tax benefits of leasing, a result held by some in the Irish business community to have resulted from the accounting profession's rehearsal of the arguments for a substance-based accounting treatment and its representations to the Irish government not to allow this to affect taxation, thereby drawing attention to the arguments.[271]

In March 1984, the British Chancellor of the Exchequer announced the abolition of the 100 per cent First Year Allowances that had fuelled the expansion in finance-based leasing in the first place, together with a compensating reduction in the rate of Corporation Tax.[272] Some, at least, suspected that leasing would lose its popularity: 'the initial reaction was, "that's the end of the leasing industry." So, SSAP21 was coming out as a historical document explaining how the accounting should have been done.'[273] Nonetheless, the ASC announced that the standard would be issued, 'unaltered as planned in June'.[274] It wasn't, of course. Christmas, now immediate past president of the ELA, called for the standard to be shelved for two years while the leasing industry reorganized itself in the aftermath of the budget.[275] SSAP21 'Accounting for Leases and Hire Purchase Contracts' was published on 16 August 1984.[276]

Business Combinations and Goodwill

We last encountered the topic of mergers and acquisitions in November 1973: ED3 had been issued nearly three years earlier; no progress towards a standard had been made; and Michael Renshall was reporting that the ASC

was 're-examining the possibility as to whether it cannot issue a further statement, at least to clarify its own position in the matter – and, hopefully, to try and settle the problem once and for all'.[277] In December 1975, Sir Ronald Leach admitted that it had been 'lunacy' to try to formulate a pronouncement on the subject so early in the life of the committee,[278] but revealed that it was his ambition to see the project through to a standard before he retired as chairman of the ASC the following year.[279] However, Leach's and Renshall's optimism proved unfounded. Apart from any doubts there may have been about other aspects of merger accounting, the problem about the legality of recording shares issued as consideration for an acquisition at nominal rather than market value remained unresolved.[280] On his retirement in 1976, Leach described the failure to make progress on ED3 as his biggest disappointment.[281]

Leach's December 1975 comments suggest that he was also hoping to see progress on goodwill, another topic that appeared on the ASSC's initial five-year programme, with a target release date for a draft of 1973–74.[282] The committee did discuss the topic in 1974, initially favouring amortization on the US pattern. It called for an exposure draft following this method to be prepared by the ICAEW Technical Advisory Committee but the committee refused; prefiguring the next quarter of a century in the history of goodwill accounting, two working parties were established, one to pursue the case for amortization over 40 years, the other, immediate write-off to reserves.[283] Papers advocating each position were written by the chairmen of the working parties – that pressing for immediate write-off was prepared by Ian Hay Davison. Both papers were subsequently published in the technical press under their authors' names, with, bizarrely, each author described as 'chairman of an English ICA sub-committee drafting a proposed standard on goodwill'.[284] The ASSC considered issuing a discussion document setting out the two alternatives[285] but in the event published nothing. Leach disclosed that, 'there [had been] indications of a compromise on this issue but these optimistic signs evaporated when the formal agreement stage was reached.'[286] The matter was then left, 'in abeyance'.[287]

In the late 1970s, practice remained highly varied; a little over half the companies with a discernible accounting policy on goodwill wrote it off immediately and the remainder divided more or less evenly between amortization and permanent capitalization, though the former was becoming increasingly popular.[288]

When Leach came to hand over the chair in June 1976, goodwill was described as 'one of the ASC's notable failures'[289] – but he explained that the ASC was now waiting for an EEC directive. Developments in company law, introduced in response to the EEC company law harmonization programme, created both an opportunity and the need for the ASC to move forward in the twin areas of merger accounting and goodwill. Drafts of the Fourth Directive, covering individual company accounts, indicated that it was likely to outlaw permanent capitalization of goodwill and make amortization either mandatory or, at least, difficult to avoid. Although this would not apply to goodwill on consolidation, it suggested that the subsequent Seventh Directive on group accounts would be likely to follow suit and thus ban an accounting policy still

fairly popular in the UK. The ASC would need to respond to these developments, not only to reflect the new legal position in accounting standards but also to advise the DoT on its negotiations on the Seventh Directive and on the implementation of the directives, including the use of options and derogations. Accordingly, the ASC set up a panel under Renshall's chairmanship to report on possible courses of action. The panel reported in December 1979 and its report was published in the following year as a Discussion Paper.[290]

At the time the Discussion Paper was issued, the Fourth Directive had been adopted and was due to be incorporated into national legislation by the end of 1980, for implementation within a further 18 months.[291] It required goodwill to be written off over a period not exceeding five years, with a member state option to permit systematic write-off over a longer period not to exceed useful economic life. The layouts specified for the balance sheet presented goodwill as a fixed asset and implicitly precluded its being shown as a current asset or an asset neither fixed nor current; a restriction on offsetting assets and liabilities also implicitly ruled out the 'dangling debit' approach.[292] This procedure, often associated with Davison,[293] had risen from relative obscurity in the early 1970s to adoption by about a quarter of companies in the late 1970s.[294] By showing goodwill as a separately identified debit balance, carried forward from period to period but presented as a deduction from reserves, the approach appears on the surface to enable companies to avoid all three 'orthodox' treatments.

Much more significantly for British companies, the current draft of the Seventh Directive adopted the same approach as the Fourth, though at this stage it remained a matter for further negotiation.[295] In addition, it was, at least to a British eye, unclear whether the Fourth Directive, strictly interpreted, required that the write-off be carried out through the profit and loss account,[296] leaving open the possibility that immediate write-off to reserves, the approach then most popular in the UK, would in fact be acceptable as what mathematicians would call 'the limiting case' of systematic amortization.

The Discussion Paper concluded that there was no significant difference between purchased goodwill in the accounts of individual companies and those of groups.[297] In a section entitled 'theoretical background'[298] it examined the nature of goodwill and concluded that,

> although goodwill is intangible, it is a reality; it exists, can be quantified and can be purchased (albeit only in conjunction with an acquisition of a business). It is an asset, although different in quality and character from other assets.[299]

Accordingly, although goodwill does not last indefinitely, and must therefore not be permanently capitalized,[300] to treat it as a 'once only expense associated with the purchase of a business' would not be consistent with its 'asset characteristic'. Rather, 'capital has been expended in exchange for the right to a number of years future distributable earnings' and the asset 'should be amortised against the profits generated or affected by that item in the same way as for any other

capital assets'.[301] The paper suggested, 'as one possible measure which could be used as an upper limit for the assessment of the economic life', a figure of two and a half times the price-earnings ratio at which the acquisition took place, with a maximum of 40 years.[302] This, apparently rather precise, formulation was derived mathematically and depended on a number of simplifying assumptions;[303] it was subsequently quietly forgotten. A *requirement* to amortize goodwill over its useful life was, however, inconsistent with the Fourth Directive, which, as we have seen, permitted member states to allow, but not require, this policy as an alternative to writing off over an – implicitly arbitrary – period of not more than five years.[304]

There were over 80 submissions in response to the Discussion Paper, but, as Renshall put it,

> the only plain fact to emerge was that there is a great diversity of views. It is very difficult to see a clear indication of a solution. Most people favoured the idea of writing goodwill off against reserves on acquisition but there was no clear majority. The question now is what form the exposure draft should take. If we assume that the elimination of goodwill is made a standard then there are at least three ways forward for the draft. You could amortise against profits, you could write off against reserves on acquisition or you could have a draft which says do one or the other. The problem with the last course is that leaving an option doesn't seem to me to be a standard.[305]

The following week the ASC agreed that the Panel should be asked to prepare an exposure draft under which goodwill would be 'written off immediately on acquisition directly against distributable reserves'.[306] A new working party, again under Renshall's chairmanship, began drafting. By February 1981, he was expressing the hope that a draft might be available 'around the middle of the year' but cautioning that there was still some way to go: 'there are still severe problems to be overcome'.[307] He was right to be cautious: in December, the ASC was letting it be known that it hoped that an exposure draft on goodwill would be issued before June 1982.[308]

Goodwill and merger accounting were now being dealt with by the ASC in tandem.[309] The legal uncertainty surrounding merger accounting was finally resolved in the early 1980s. The first stage in the resolution was a 1980 tax case, Shearer v. Bercain, which upheld the taxpayer's case that it was obliged by law to record a share premium and freeze pre-acquisition reserves.[310] The draft of the Seventh Directive current at the time of Shearer v. Bercain appeared also to have the effect of outlawing merger accounting but the DoT had already accepted that this would cause problems and had issued a consultative paper seeking views on the desirability of seeking an amendment to the Directive.[311] The problems stemmed partly from those high profile cases where reputable companies had already used a method of accounting that appeared to have at least some support in the accountancy community, witness its inclusion in ED3, and partly from its widespread but more low profile use for internal reorganization

of groups, where it was employed to avoid arbitrarily 'freezing' reserves as a result of restructuring. In 1981, a joint working party of the CBI, the CCAB and the Law Society issued a memorandum advising the government on a legal framework for permitting merger accounting and suggesting that accounting standards should be left to prescribe the method. The memorandum explicitly argued that the government should leave open the possibility that the standard could allow merger accounting on more tightly constrained grounds than the law.[312]

A 'last-minute scramble'[313] succeeded in getting provisions giving relief from recording a share premium, so as to permit merger accounting, included in the 1981 Companies Act.[314] In a debate on the bill, the government indicated that it would 'be for a future accounting standard to prescribe the accounting treatment to be adopted in circumstances that fall within the scope of [the provision]',[315] thereby effectively leaving the detailed design of merger accounting to the ASC. The July 1981 meeting of the ASC established a working party, chaired by Christopher Stronge (a partner in Deloitte Haskins & Sells), to produce an exposure draft.[316] An ASC spokesman, perhaps with tongue more firmly in cheek than usual, pointed out that the working party would be drawing on the comments received on ED3, which was 'still valid as a starting point'.[317] In September 1981, the IASC issued E22 'Accounting for Business Combinations', permitting merger accounting and requiring goodwill to be amortized.[318]

The old and new committees appeared to agree that, to qualify as a merger, substantially the same body of shareholders as owned the various pre-merger entities separately must remain for the post-merger entity. However, although ED3 may have been the starting point for the new working party's deliberations, the end point was dramatically different. ED3's approach reflected an organizational model of merger: two entities merge if they come together without one dominating the other. As a consequence, the substance of the main businesses of the constituent entities had to continue and there was a size test – albeit a generous one – to avoid the larger overwhelming the smaller.[319] The new working party viewed a merger more in terms of the confluence of economic interests – the US terminology was, after all, 'pooling of interests'. Hence the key test was that 'the combination of businesses is brought about ... without significant resources leaving the combining companies.'[320] Tests beyond those applying to the share transaction itself, and shareholders' consent to it, were abandoned. A further reason given for abandoning the size test was that it was 'too arbitrary a consideration on which to base an accounting standard'.[321] To ensure that significant resources did not leave the business, not less than 90 per cent of the value of consideration given had to be in the form of shares. The method of merger accounting set out in the exposure draft was essentially the same as that in ED3; like ED3, where the definition of a merger was satisfied, merger accounting was compulsory.

Two exposure drafts, ED30 'Accounting for Goodwill' and ED31 'Accounting for Acquisitions and Mergers', were issued on 28 October 1982.[322] ED30 had been voted on by the ASC membership as at 30 June 1982, apparently to avoid

delays while new members read themselves in but also, perhaps, in case those not a party to earlier decisions wanted to reopen them. All voted in favour except for one member whose paper was not returned. Some minor comments on technical matters were added to the voting papers and one member voting in favour annotated his paper, 'I do not necessarily agree with its contents.'[323]

ED30 permitted free choice between amortization and immediate write-off. Whichever policy was selected was to be applied to all goodwill. In justification for free choice it was explained that,

> The majority practice is to write off goodwill immediately to reserves but a significant minority of companies amortise goodwill. ASC considers that a single accounting treatment for purchased goodwill could only be laid down as standard if that treatment could be justified by sound argument, and, further if sound argument could be advanced against the alternative treatments. Since both ways of looking at goodwill are thought by ASC to have validity, it has concluded that . . . it should allow companies an option.[324]

As Nobes has pointed out, 'the discussion paper *had claimed* to make the necessary sound arguments; and the ASC's objectives *included* that it should try to narrow the variations in accounting practices even if a whole range was acceptable in principle.'[325] Indeed, the argument offered in the exposure draft in support of amortization follows the Discussion Paper almost word for word[326] but is now accompanied by a statement that, 'one view is that goodwill is not an asset in the normal sense of the word because it is not independently realisable',[327] supported by argument which follows almost word for word that included in an appendix to the Discussion Paper containing an 'outline of alternative treatments and arguments rejected by the panel'.[328]

Ninety-seven submissions on ED30 were received. Some idea of the diversity of opinions can be obtained by examining the positions of the largest accountancy firms:[329]

Arthur Andersen – Immediate write-off.
Arthur Young, McClelland, Moores – Free choice applied consistently.
Coopers & Lybrand – Free choice transaction by transaction.
Deloitte Haskins & Sells – Amortization.
Ernst & Whinney – Free choice applied consistently.
Peat, Marwick, Mitchell – Would prefer permanent capitalization to be permitted in addition to other choices but accept that EEC directives make this impracticable.
Price Waterhouse – Immediate write-off.
Thomson McLintoch – Issue guidance only – favouring the dangling debit approach.
Touche Ross – Issue only an amendment to SSAP14 banning unacceptable methods such as dangling debit and permanent capitalization.

Faced with such widespread divergence of views, the working party had little prospect of tightening its position. A proposed standard was approved in principle in March 1984[330] and passed to the CCAB bodies. It attempted to steer preparers to immediate write-off but permitted amortization, effectively as a free choice. ED30's limitation of 20 years on the amortization period was abandoned, Renshall explaining that, 'the truth of the matter is that everyone knew 20 years was purely arbitrary.'[331] This explanation is consistent with the view he took when the limitation was proposed, although his conclusion then was rather different: 'The ASC is currently thinking of 20 years. You cannot rationalise five, 20 or 40 years but tend to say that 20 years is about right.'[332] He did then go on to say that, 'twenty years is only a proposal at the moment for the public to see if they like it.' Evidently they didn't.

SSAP22 'Accounting for Goodwill' was issued in December 1984. It stated that 'purchased goodwill ... should normally be eliminated from the accounts immediately on acquisition against reserves' but that it 'may be eliminated from the accounts by amortisation through the profit and loss account in arriving at profit or loss on ordinary activities on a systematic basis over its useful economic life'.[333] In a significant retreat from ED30, the pronouncement indicated that, 'nothing in this standard precludes a company from using both the immediate write-off treatment and the amortization treatment in respect of the goodwill which relates to different acquisitions.'[334] One commentator, no doubt essaying Swiftian irony, suggested that the ASC should have gone the whole hog and permitted goodwill on a single acquisition to be accounted for by a combination of write-off and amortization.[335]

The British position, as embodied in SSAP22, was adopted in the final version of the Seventh Directive and thus in the UK by the 1989 Companies Act.[336] In practice almost all – but not all – preparers aligned themselves behind the ASC's preference for immediate write-off.[337] The IASC abandoned the amortization method of E22 and allowed free choice in IAS22 'Accounting for Business Combinations', issued in 1983.[338]

ED31 had not been long issued when it came under attack. In December 1982, Don Hanson, the managing partner of Arthur Andersen, called for greater flexibility in the application of the definition; he felt that the recent combination of Argyll Foods and Allied Suppliers, in which shares amounted to only 80 per cent of the consideration, ought to be considered a merger.[339] From the other direction, criticism was levelled at the 'pooling' approach, on the argument that, as Robert Willott, the former ICAEW Technical Director put it, 'there is plenty of evidence to show that an exchange of shares is often a deliberate ploy to achieve particular financial ends.'[340] An ASC spokesman conceded that many submissions had made this point and suggested that a size test might be restored to the pronouncement.[341]

In April 1984, the ASC approved a Statement of Intent on merger accounting. It would be relaxing the definition of a merger; the limit on share consideration would now be, as Hanson had proposed, 80 per cent, a move which Stronge described as 'more consistent with market practice'.[342] No size test was mentioned.

The ploys involved in share for share exchanges included so-called 'vendor placings' and 'vendor rights'.[343] Vendor placings had been in use for some time to leave the shareholders of the target with cash but apparently satisfy the 'continuity of ownership' criterion for merger accounting. Shareholders were invited to exchange their shares in the target for shares in the acquiring company but with an accompanying offer from institutional shareholders in the acquirer to purchase the newly-obtained shares for cash at a stated price. Because this method prevented smaller shareholders in the acquirer from increasing their holdings it was of limited popularity. Shortly before the adoption of the standard a new tool, vendor rights, was invented by Samuel Montagu. This involved an offer from a financial institution to purchase the newly-obtained shares for cash and these were then offered to all the original shareholders in the acquirer.

Some commentators regarded these devices as permitting straightforward evasion of the proposed standard: 'they have found a way of getting a takeover treated as a merger',[344] according to Rutteman. Indeed the ASC's new chairman, Peter Godfrey, was reported as indicating that,

> speaking personally, he was concerned that in two seemingly identical situations there could be two different accounting treatments. He said the ASC was 'looking at this matter to see what [it] might do'. The problem was that the issue had arisen mid-way through the standard's adoption process. ASC secretary, Peter Holgate, said he though it unlikely the standard would be amended, but said that the accompanying Technical Release could urge companies not to make use of this loophole.[345]

At the time of these comments five of the six CCAB bodies had approved the standard,[346] the ICAEW by a slim majority.[347] The following month the ICAI gave its approval and SSAP23 was on the books.[348] The ASC's position on 'vendor' ploys was now somewhat different: according to Godfrey, 'we're quite happy to allow vendor placings and rights',[349] and an article in *Accountancy* by Professor Harold Edey, a former member of the ASC explained that 'SSAP23 adopts a different conceptual basis [from ED3], namely that there should be no substantial release of resources as consideration for the transfer of ownership.'[350] These explanations left the critics unsatisfied: 'I don't believe the standard should have been adopted',[351] was the view of Michael Lickiss, chairman of the ICAEW Technical Review Committee.

Investment Properties

A first glance at the chronology of SSAP19 'Accounting for Investment Properties' suggests an uncontroversial pronouncement: only one exposure draft; from ED to standard in 14 months, a record never bettered after the ASSC's honeymoon period; and an outcome that survived for ten years without amendment until international accounting standards displaced the domestic variety in 2005. Keith

Robinson serviced the panel developing the pronouncement and confirms that it was a straightforward process:

> It had a relatively easy time. We obviously had to take a lot of notice of what the property industry said but they worked with us ... It was unarguable that accounting for a property you held for investment purposes was different to accounting for one you used in your business. It was a nice project, I enjoyed doing it. The British Property Federation were extremely interested and involved but by no means hostile. They were a good group to deal with. I think they had some technical problems with it at times but they were good people to work with.[352]

We need to remind ourselves, though, that a separate pronouncement covering investment properties was required only because of difficulties with the standard addressing depreciation generally.[353] After the standard had been approved by five CCAB Councils, the ICAEW applied its veto, apparently in the face of widespread threats by property companies not to comply with the standard. To secure the passage of the standard, the ASC agreed that investment *properties* should be excluded from its scope for twelve months while further discussions were held. The exclusion initially lasted until 1 January 1979,[354] but was extended for a further year.[355]

The property sector's arguments against depreciation fell into two categories. The first related to the nature of its assets which, it was suggested, had lives so long that periodic depreciation charges would be immaterial.[356] Further, with rising property values, 'why charge depreciation ... on assets which might well be worth more money at the end of the year than they were at the beginning?'[357] These arguments can, of course, apply to any property and were, indeed, being used by industrial concerns such as the brewing industry.[358] They could scarcely provide a rationale for dealing with the property sector differently from others. The second category of argument concerned the nature of the sector itself. As the BPF put it, a property investment company,

> regards its properties in a similar way to that in which an investment trust regards its share portfolio. Their value to the company depends on the stream of present and future income and on their capital growth potential. If future income or capital growth can be enhanced by a change in the investment portfolio then an appropriate sale or purchase will be made. Depreciation and obsolescence are not significant factors.[359]

Here, at least, was some basis for distinguishing between property companies and others, though, as one commentator pointed out, the explanation for non-depreciation by investment trusts is that, 'share certificates seldom wear out, and if they do, don't exactly cost a fortune to replace.'[360]

An important consideration for at least some property companies was the likely effect of charging depreciation on their dividends. Many property companies

were established with a Memorandum and Articles of Association which proscribed the payment of dividends from profits on the disposal of properties, largely to reinforce a case to the Inland Revenue that the company was not trading in property and thus should not be taxed on the proceeds as trading profits.[361] Companies with only rental income available to cover dividends might find depreciation substantially eroding that profit and thus dividend capacity.[362] The BPF went as far as to suggest that 'adoption of depreciation ... would be inflationary, since it would oblige property owners to seek to maintain the current level of ... post-tax profits, after providing for depreciation.'[363] One difficulty for the BPF (and the ASC) was that depreciation of investment property was common practice in North America[364] and continental Europe.[365] As a result it had been incorporated without difficulty into IAS4,[366] whose adoption had precipitated the development of SSAP12 in the first place, and the Fourth Directive. The BPF's explanation for the unusual position of the UK was that the UK has a more sophisticated property valuation profession[367] and that there were differences in the construction of leases and the relative contribution of land values compared to the rest of the world.[368]

The BPF held a series of meetings with the ASC panel. The first, held in July 1978, was described by the BPF Director-General as 'a good start ... Our paper was received in a friendly atmosphere.'[369] In October 1979, the ASC suggested an amendment to SSAP12, defining investment properties (undefined in the original standard) and allowing annual revaluation as an alternative to depreciation.[370] The CCAB bodies were consulted but the Scottish and Irish Institutes objected on the grounds that a preparer adopting the more prudent approach, leaving a property at historical cost in a period of rising values, would suffer a depreciation charge while a less prudent preparer would not.[371] In January 1980, the formal exemption from SSAP12 ran out but no other arrangements were in place (and no proposal had been publicly exposed), so that financial statements for periods commencing after that date would have had to include depreciation on investment property.

In June 1980 the ASC considered a secretariat paper advising against renewing the exemption, on the grounds that the lack of a definition of investment property allowed too much latitude and that the implementation of the Fourth Directive would in any event supersede it.[372] It also advised against allowing preparers a free choice between historical cost and current cost (with the possibility of requiring historical cost to be undepreciated, thereby meeting the earlier Scottish and Irish objections), on the grounds that this, too, would be superseded by the Fourth Directive. What was left was to require defined investment properties to be carried at an annual valuation. The paper argued that this approach could be squared with the Fourth Directive because, since only one treatment was permitted, it could be argued that the treatment was necessary to show a true and fair view and thus justified a departure from the rule requiring depreciation. The paper was accompanied by a draft ED following these lines. Revaluations could be carried out by employees of the preparers; there was no requirement that they should be qualified valuers, but their names

or qualifications had to be disclosed, together with the fact of their employment, if this applied, and the basis of the valuation. Revaluations were to be carried to a reserve (unless there was an overall deficit, which would be charged to the profit and loss account) and changes in the reserve were to be displayed prominently in the financial statements.

Also in June, the ASC received a note of a meeting with the Life Offices' Association (the trade body for life insurance companies),[373] one of a series with interested parties. By the time this meeting was held – late May, 1980 – the ASC had effectively agreed that investment companies should not be required to depreciate investment properties, leaving only the task of finding a means to a secure this outcome which would satisfy the Fourth Directive. Was the LOA happy? No:

> Mr Davis [LOA] explained that the LOA did not consider it appropriate to depreciate head office buildings which were used for administrative purposes. Such buildings were considered as part of the fund and were held primarily for investment purposes.

The proposed exposure draft was discussed by the ASC in June 1980. Following discussions with the DoT and circulation of a pre-ballot draft, it was agreed in a ballot and issued, without substantial amendment from the June version, in September 1980. ED26 'Accounting for Investment Properties – An Addition to SSAP12 "Accounting for Depreciation"' is a proposed amendment to SSAP12, adding Part 5 to that pronouncement. Included within the document is a 'Statement by the ASC on Publication of ED26 "Accounting for Investment Properties"', effectively a 'basis for conclusions'. This explains that:

> It is not, and never has been, the general practice in the UK and Ireland to provide for annual depreciation of investment properties . . . The reason that annual depreciation is not provided on such properties is largely instinctive and has not been clearly rationalised. Subject to consideration of submissions on this exposure draft, the ASC believes that this instinctive practice has a sound foundation . . . The argument . . . proceeds: (a) the financial statements of enterprises holding investments are more helpful to users of financial statements if the investments are accounted for at current values rather than on the basis of a cost or valuation established some time in the past; and (b) depreciation is only one element which enters into the annual change in the value of a property and as the use of a current value places the prime emphasis on the value of the assets, it is not generally useful to attempt to distinguish, estimate and account separately for the element of depreciation; and (c) depreciation, although not separately identified, will be taken into account in dealing with changes in current values.[374]

Thus the ASC did the property company accountants' work for them. The statement went on to point out that this rationale suggested that all investments

should be accounted for at current valuation and indicated that this would 'require further study'.[375]

The exposure draft was welcomed by the BPF, whose director wrote to its members urging them to back the draft.[376] As the press explained, 'the federation's fears appear to be that if there is not strong support for the annual revaluation requirement . . . the Government . . . may be forced back into requiring such property to be depreciated'.[377] Since the ED could not be converted to a standard in time for 1980 financial statements and property companies were reporting that, however much they supported the principles, they would not have time to revalue their investment properties[378] – somewhat oddly, perhaps, since according to the ASC the rationale for the proposed treatment was the instinctively-understood superior usefulness of current values – the application of SSAP12 to investment properties was once again deferred for a year, to 1 January 1981.[379]

The ASC received 107 submissions on the exposure draft,[380] a large number for such a specialist area. Some large accountancy firms were uncomfortable about the draft[381] but most submissions were supportive.[382] In May 1981, the ASC considered a proposed standard involving no change of substance from ED26 but cast now as a separate standard rather than an amendment to SSAP12.[383] The draft was sent for ballot and agreed.[384] In July it was sent to the CCAB bodies. The ICAS approved only in return for a promise of a review of SSAP12.[385] The other bodies also approved the proposed standard and it was issued in November 1981 as SSAP19 'Accounting for Investment Properties'. At the same time SSAP12 was amended permanently to exclude investment properties from its scope.

Leasehold properties with an unexpired term of 20 years or less are excluded from the scope of SSAP19 and must be depreciated in the ordinary way. ED26 explained the problem:

> A property held on a lease with an unexpired term of 20 years or less may not be treated as an investment property. This is necessary to avoid a position in which a property company could purchase a short leasehold and amortise the premium paid to acquire the short leasehold against the investment property revaluation reserve whilst taking the rentals received to the profit and loss account. A pragmatic view was taken in setting 20 years as the life of an investment property. Two options were available to ASC on this matter, either to set a figure on a pragmatic basis or to deal with the problem in more general terms. On balance ASC decided it would be more helpful to state a figure for the life of an investment property.[386]

Peter Holgate succeeded Robinson, quoted at the beginning of this section, as secretary of the ASC. His comments on the pronouncement are:

> The project was largely complete before I arrived. The thing that was notable was the immense organisational and lobbying ability of the British

> Property Federation. They got what they wanted after putting that effort in. Even to the point that – this is a second hand story but it's probably true – Tom Watts asked a senior RICS person who they had been working with about when it is that a leasehold property starts to lose value so that non-depreciation no longer makes sense. 'Oh', he said, 'when there are 20 years remaining'. So that went in SSAP19. I merely report the rumour. [SSAP19 was seen in the secretariat] as a case of successful lobbying but as an answer, not a bad answer. Intuitively it felt about right, but with the worry that surely buildings fall down eventually . . . So [the BPF] got an answer that was better than they deserved [but] you didn't get users of accounts arguing against it.[387]

Reviewing Standards

At the end of its first decade, the ASC adopted a systematic policy of reviewing existing standards.[388] The first standard to be reviewed under this policy was, logically enough, SSAP1 'Accounting for the Results of Associated Companies', issued in January 1971. The standard had not proved particularly controversial on issue and was, on the whole, followed adequately by preparers.[389] Minor amendments were incorporated into the standard in August 1974.[390]

Over the years, it became clear that some preparers were taking advantage of limitations in the standard's prescription of procedures for equity accounting in areas such as the treatment of intra-group transactions,[391] use of non-uniform accounting policies[392] and the application of the grounds for excluding an associate from equity accounting.[393] However, the most serious problem concerned the definition of associated companies and specifically the cut-off point between associates and trade investments. Leaving aside joint ventures, SSAP1 defined an associated company such that:

> the investing group or company's interest in the associated company is for the long term and is substantial (i.e., not less than 20 per cent of the equity voting rights), and, having regard to the disposition of the other shareholdings, the investing group or company is in a position to exercise a significant influence over the associated company . . . it is essential that the investing group or company participates (usually through representation on the board) in commercial and financial policy decisions of the associated company, including the distribution of profits.[394]

Thus there were four requirements, all of which had to be met. Much of the attention fell on the 20 per cent rule, the ASC's first attempt at what is now called a 'bright line' solution, that is one that clearly delineates between two categories without the need for judgement or estimation, and is thus highly auditable. Some groups failed to apply equity accounting even to investees held at levels substantially above 20 per cent, including cases where holdings ran to

49 per cent. Although it is possible that in such cases one or more of the other elements of the test had been failed, commentators expressed some scepticism that this was always the case.[395]

More controversially, some groups applied equity accounting to investees where their holding was less than 20 per cent. In 1977, the accounts of the Midland Bank were qualified for non-compliance with SSAP1 because the group equity accounted for its 16 per cent holding in Standard Chartered Bank, although it had used the same method in the previous year without qualification.[396] Midland persisted in using equity accounting, on the grounds that 'having regard to the size and long-term nature of the investment' it was of the opinion that it did constitute an associate,[397] although, of course, on a strict interpretation of SSAP1's definition it simply *could not* constitute an associate. Midland sought to rely on the spirit of the standard.[398] Some commentators sympathized with Midland – *Accountants Weekly*, not normally prone to giving preparers the benefit of the doubt, described the audit qualification as 'a fit of excessive zealotry'[399] – but there was little or no sympathy for another preparer using equity accounting at below 20 per cent, Lonrho.

Lonrho already had a reputation for the limited quality of its financial disclosure[400] and was 'often treated by institutional investors as something of a maverick'.[401] Its unaudited interim results for the first half of 1978 showed pre-tax profits of £42 million, up from £39 million in the previous first half, but only because of the inclusion of £5 million of profits from House of Fraser, treated for the first time as an associated company.[402] Lonrho and its subsidiaries held only 19 per cent of the shares of House of Fraser but another associate, Scottish and Universal Investments, of which Lonrho owned 30 per cent, held a further ten per cent of House of Fraser's shares. Lonrho were apparently calculating their holding of House of Fraser to include 30 per cent of SUIT's 10 per cent, tipping the balance over the 20 per cent level. However, Lonrho clearly did not control SUIT and therefore did not control its shares in House of Fraser. The market apparently viewed the upward trend in Lonrho's profit achieved in this way with some suspicion and its share price fell sharply.[403] Under pressure from the Stock Exchange, Lonrho announced that its treatment had the support of its joint auditors', though apparently on the grounds that 19 per cent was near enough to 20 per cent, rather than that the SUIT shares could be counted.[404] The manoeuvre became known in some quarters as 'the Lonrho loophole'.[405]

Pressure for the review of SSAP1 to be brought forward was now coming from two sources: controversial approaches to the cut-off in the definition and the need to consider the contents of IAS3 'Consolidated Financial Statements', released in 1976.[406] The definition in IAS3 did not provide a prescriptive numerical cut-off but included a 'one-way' rebuttable presumption that a holding of below 20 per cent should not qualify unless significant influence could be clearly demonstrated.[407] A panel under the chairmanship of Martin Gibbs, of stockbrokers Phillips & Drew, was established and comments on the working of the standard called for.[408] Responses indicated that in most areas the standard

was working adequately but many called for changes in the definition of an associate. Preparers typically called for a relaxation in the definition, moving to a cut-off based on influence (and hence requiring a judgement) while audit firms sought a tightening of the approach, based on shareholding.[409] Going against this tendency, however, both the joint auditors of Lonrho called for a move to a broader definition.[410]

A revised version of SSAP1 was exposed by ED25 'Accounting for the Results of Associated Companies', published in October 1979. The principal change was the adoption of a subjective definition of an associate, based on 'significant influence' and including a 'two-way' rebuttable presumption that a holding of 20 per cent or more represented significant influence. This approach followed Accounting Principles Board Opinion No. 18 'The Equity Method of Accounting for Investments in Common Stock',[411] which was itself issued shortly after SSAP1.[412] The ED indicated that, 'for the purposes of establishing whether or not significant influence is presumed to exist', the holdings to be counted included those of the investing company and its subsidiaries but not its associates.[413] Press reports suggested that, 'this would have ruled out the Lonrho treatment',[414] but, of course, at 19 per cent, Lonrho might have been able to rebut the rebuttable presumption.

Public hearings were held in April 1980 but only two submissions were received.[415] The revised standard was issued in April 1982 and followed ED25 closely while allowing equity accounting in the financial statements of a parent company without subsidiaries[416] – a cause strongly pursued by Shell at the public hearings.[417] This was a requirement of the SEC and affected Shell, which had some 600 associates but no subsidiaries.[418] It had thus taken two years to get from the closure of the exposure period to the revised standard without any significant change occurring. As it happened, by the time ED25 was published SUIT had become a subsidiary of Lonrho and Midland Bank had sold its holding in Standard Chartered Bank.[419]

The other standard coming under review in the period was SSAP15 on deferred taxation. Two factors prompted the review. The Finance Act 1981 largely removed the clawback of stock relief, effectively making relief permanent.[420] Hence companies that had previously been providing for deferred tax on stock relief as a timing difference needed to release the provision. The ICAEW issued interim guidance on the treatment of the release, recommending that it did not constitute an extraordinary item but should be included in the tax charge for the year and separately disclosed.[421] This treatment is consistent with SSAP6's approach, since the original provisions were made as an ordinary charge to the profit and loss account and the entry is simply an adjustment to the amount originally provided. However the effect was, in some cases, spectacular. *Accountancy* recorded one case in which pre-tax profits fell by 65 per cent but earnings per share rose by 78 per cent. Although the company disclosed the effect of the release this was done only in note 9.[422]

The other factor was the diversity of treatments adopted generally under SSAP15.[423] The CCAB requested that the ASC review SSAP15, both to produce

short-term guidance on the treatment of stock relief – to replace the ICAEW statement – and to revisit the requirements of the standard generally.[424] As far as the former was concerned, the issue was whether the abandonment of clawback constituted:[425] (a) a change in the effective rate of taxation, to be treated under SSAP15 as part of the ordinary tax charge;[426] or (b) a change in the basis of taxation arising outside the ordinary activities of the business and thus an extraordinary item under SSAP6.[427]

The ASC's non-mandatory guidance note, issued without clearance through the CCAB bodies, appeared in November 1981[428] and was reproduced in the following month's *Accountancy*.[429] It contained some uncontroversial recommendations on the treatment of continuing relief. In respect of the reversal of earlier provisions, so much time had passed that the guidance was able merely to note that most companies would already have reported the release, using one or other of the methods described in the previous paragraph. This was nonetheless interpreted as permitting either approach, and, as such, regarded as controversial.[430]

By 1982, SSAP15 had been in operation for three years but appeared to be either seriously misunderstood or subject to widespread evasion.[431] As the authors of the ICAEW survey of published accounts covering 1981/82 put it:

> Of the 282 companies which based their policy on SSAP 15, 119 (1980–81: 117) stated that deferred taxation is accounted for on those timing differences expected to reverse in the future. Whilst in practice such an accounting policy might be in accordance with SSAP 15, if applied literally it will almost certainly not be: accounting for deferred taxation only on timing differences which are expected to reverse is less prudent than accounting for all timing differences except those which it can be shown with reasonable probability will continue in the future. Ten companies indicated that in assessing their future circumstances regard was paid only to the following 3 years, which is the minimum period laid down in paragraph 28(a) of SSAP 15, but made no reference to the criterion set out in paragraph 28(b) regarding the likelihood of the liability crystallizing after the 3-year period. Eight companies used various descriptions which are not strictly in accordance with the requirement of SSAP 15 to have regard to the foreseeable future: for example, several companies stated the provision is made 'where necessary'.[432]

In March 1982 a panel was established by the ASC under the chairmanship of Richard Allen, of Peat, Marwick, Mitchell.[433] Comments on the working of SSAP15 were called for but there were few responses.[434] ED33 'Accounting for Deferred Tax' was published in June 1983. The principal effect of the draft was 'a change in emphasis, from "do provide unless . . . " to "provide to the extent that it is probable that a liability will crystallise and do not provide to the extent that it is probable that a liability will not crystallise".'[435] The effect of this change was to bring the pronouncement into line with the practice apparently

adopted by the substantial minority of preparers regarded by the annual survey as not complying with SSAP15.

In March 1984, the Chancellor of the Exchequer announced a new company tax regime under which First Year Allowances would be progressively eliminated, leaving only the normal annual rates, and the rate of corporation tax substantially reduced. This would bring tax allowances much more closely into line with depreciation but require deferred tax to be provided for during the transitional period because future relief could no longer be expected.[436] On 28 March the ASC approved a press statement[437] reiterating that, though undergoing review, SSAP15 remained in force and that, under the standard, companies expecting the crystallization of liabilities as a consequence of the changed regime should provide for them immediately, either as part of the normal tax charge or as an extraordinary item under SSAP6. However, the statement went on to say, somewhat enigmatically,

> There may be instances where companies feel that applying SSAP15 and SSAP6 does not enable their accounts to give a true and fair view . . . Full disclosure of the treatment is essential, particularly by companies departing from standard accounting practice in order to give a true and fair view.[438]

The principal sufferers from applying SSAP15 would be banks, which would lose the allowances from their leasing business. The provisions necessary were estimated to amount to approximately a full year's profit.[439]

The draft press statement seen by the ASC included manuscript revisions reflecting the impact of the Budget.[440] The paragraph dealing with departures in order to show a true and fair view was preceded by a clause indicating that such departures would be rare,[441] but this had been deleted: 'Had it not been struck out, it would have been clear that the "true and fair" override would only apply in *exceptional* cases. This, however, was not what the ASC's banking fraternity was looking for.'[442] Some members of the committee apparently agreed the statement unaware that the clause had been dropped.[443]

The statement agreed on 28 March was intended for release at a press conference on the following day but was leaked overnight.[444] It was widely interpreted as permitting the banks to invoke the true and fair override to spread the necessary provisions over several periods: 'as a result share prices of the London clearers rose dramatically: National Westminster by 17p; Barclays by 15p; Lloyds by 13p; and Midland by 8p.'[445] *Accountancy* takes up the story:

> By the time of the press conference, Ian Hay Davison knew of the interpretation being put on the ASC statement, and the market reaction to it. Notwithstanding intense and searching questions from members of the accountancy press at the conference, he refused to clarify the ASC's position, repeatedly contending that the ASC was a legislative body, not an interpretive one: reading the statement should be sufficient to understand it. It was pointed out by the press (but not accepted by Mr Davison) that [the

relevant paragraphs] were nothing if not ambiguous. The rest of the statement told us nothing new, so why was it being published at all, unless [the paragraphs] were indeed to be interpreted as paving the way for the banks to take a softer line? No comment was offered.[446]

This line was widely seen as encouraging an 'anything goes' interpretation[447] and there was considerable pressure, particularly from audit firms, for it to be reversed.[448] The following month, a Statement of Intent was published, indicating that a revised standard would be issued and would differ little from ED33.[449] The Statement made it clear that 'companies that foresee deferred tax liabilities crystallising should provide immediately for those liabilities at the rates at which they are expected to crystallise', and that 'all significant adjustments to the deferred tax account arising from changes in the basis of tax will be required to be treated as extraordinary items'[450] and thus charged against profit in the period. Comments on whether the Budget should affect the pronouncement were sought; commentators generally agreed that it did not affect the principles of deferred taxation.[451]

The revised SSAP15 was published in May 1985. As foreshadowed by the Statement of Intent, it largely followed ED33. However, although ED33 had indicated that 'the liability method . . . is the method consistent with the aim of partial provision',[452] it had, like the original SSAP15, not actually specified that this method should be used in preference to the deferral method. The revised standard now specified the liability method, apparently at the request of some commentators.[453] The accompanying technical release implied that this followed a proposed change in international accounting standards,[454] but Allan, the chair of the deferred tax working party, was probably more accurate in saying, 'it is only because of the US being wedded to the deferral method that we have held off for so long. Now the FASB . . . is making tentative moves towards the liability method.'[455]

A Mature Standard-Setter

As well as the work reviewed in this chapter, the ASC: completed the development of SSAPs 17 and 18 (covered in chapter 6); published an exposure draft on accounting for pension costs (ED32) and reviews of SSAPs 6 and 12 (covered in chapter 10); published exposure drafts on accounting for Petroleum Revenue Tax (ED28) and pension funds (ED34) and a discussion paper on accounting by charities; and continued the pursuit of a method of current cost accounting (dealt with in chapter 9), publishing one exposure draft (ED35) on the subject. The ASC's output of new standards over the five years was thus six (SSAPs17–22), with two of these largely completed before the period began and one other (SSAP23) appearing shortly after the end of the period; thus five standards reflect work undertaken substantially during the period against seven in the second half-decade and eleven in the first. The deceleration continues but is not dramatic and is balanced by other work not undertaken in earlier periods, such

as the substantial reviews of earlier standards and development of discussion papers.

Some of the most important pronouncements are, however, now taking a very long time to emerge: SSAP20 on foreign transactions took more than five years to develop from ED21; SSAP21 on leasing nearly five years from ED29, which itself occupied the working party for over five years; and SSAP23 saw 'closure' of a topic first exposed by ED3 in 1971. Though the period between exposure draft and standard for goodwill was not particularly long, the ASC had been struggling with the topic, off and on, since 1974. Although the rate of output was largely keeping up with earlier periods, the speed of production was declining.

Both the modest decrease in rate and the lengthening gestation period reflect, of course, the increasing technical difficulty, and political sensitivity, of the topics addressed. Significant as the political issues surrounding, say research and development, were, the technical dimension was relatively straightforward, the central argument clear, the parties affected few in number, and the problem capable of resolution in a local (ie. UK) context. In grappling with foreign currency translation, the ASC found itself addressing complex technical issues, affecting large numbers of preparers in different ways, and with significant international ramifications. In some cases, for example leasing and investment properties, it was now running up against highly-organized interest groups with well-articulated views.

A tribute to Watts on his retirement recorded that,

> his tactic of slowly persevering towards his goal infuriated many . . . 'The whole game is saleability,' he will say . . . With the system that we have you must make a judgement on what salesmanship, or education, if you want to call it by its other name, can achieve.

He regarded leasing as a prime example of his method: 'Leasing has been a problem that we have had around for six years. And it has only gone through relatively painlessly because we have taken the time to sell it.'[456] His comment here relates to the ED; the standard on leasing was in fact another two years off. It was, indeed, a slow haul.

The increasing importance of the international dimension was a key feature of the period. In some areas the ASC found itself under pressure to keep up with pronouncements from the IASC whilst the need to co-ordinate developments with standard setters in other national regimes, largely driven by multinationals with multiple quotations, was a key feature of work on foreign transactions. Another important pressure was the increasing impact of the legal framework following the EEC company law harmonization programme.

Arguments about economic consequences continued to rage and played an important part in the debate on leasing. Direct cash flow effects from the proposed changes were hard to discern yet preparers claimed that indirect consequences would be significant, though without providing evidence to back up

their claims. In some instances, the claims seem almost ludicrously lightweight, for example the fear that capitalizing leases would somehow alert the government to the volume of leasing activity or provide cover for a change in the tax system it desired but would otherwise lack the nerve to bring off.

The standard on leasing was a highly significant step in advancing the doctrine of substance over form (and the associated technique of discounting); indeed it was the first major change in accounting in the UK secured by a standard relying on the doctrine.[457] At the beginning of the development work there was only 'quite a small band of believers'[458] to carry the flag for capitalization, led by Rutteman and greatly assisted by the collapse of Court Line, but, perhaps because the standard 'had been so long in gestation[,] . . . it received a reasonable acceptance from a resigned public'[459] – Davison's more insouciant but fundamentally similar reading to that offered in the tribute to Watts quoted a little earlier. The small band changed the way leasing agreements came to be perceived in the financial reporting world and moved the British accountancy profession to the point at which 'the basic "substance over form" arguments in respect of leasing are by now very familiar';[460] familiar and, whether from education or exhaustion, accepted. Of course, as Holgate puts it: 'The ELA continued to object to [capitalization] throughout the three years of my involvement and no doubt still would, if asked.'[461]

Davison, under whose chairmanship the exposure draft was steered towards a standard, described the pronouncement as 'pushing forward the frontiers of disclosure' and suggested at the time that it marked 'the end of an era' because 'the ASC will not be permitted to do this again.'[462] Those who distinguish sharply between disclosure and measurement might note that Davison sees the crucial issue here as disclosing the amount of the commitment rather than measuring leasing liabilities in the balance sheet.[463]

The determination of substance is not always easy; in the case of foreign currency, though measurement at current rates may appear a better reflection of economic substance, the rationale for the net investment method can be argued to conflict with the substance-based rationale for consolidation itself. Nor is the regulation of substance unproblematic. As we shall see, the standard on leasing included a cut-off test for finance leases that was to prove easy meat for an avoidance industry.[464] Imperfect as it was, the ASC's pioneering drive towards substance over form in accounting for leases had, in itself, a major impact on perceptions of the balance sheet and also paved the way for a number of similar developments in later years.

One very significant concession to free choice made by the ASC during the period was in the treatment of goodwill. The standard on goodwill could scarcely be described as a major advance in standard-setting:

> It was a considerable failure in retrospect, obviously. It was an interesting example . . . of an unprincipled approach. We had no notion of what assets were, what goodwill was, whether it was an asset. It was an entirely pragmatic discussion – who does what? Everyone writes it off, but surely its

> worth something, but to insist on amortisation is inconsistent with internally generated goodwill . . . You can think of two or three reasons for any position in this area and we did – we wrote them all down. It was a very, very pragmatic discussion leading to what was in retrospect – or even at the time, frankly – an unsatisfactory standard . . . It wasn't that members [of the ASC] generally wanted to be firm but were afraid to do so, they accepted that there were two ways to do it . . . Michael Renshall chaired the goodwill working party. Michael had no strong personal notion of whether goodwill was an asset . . . He was looking for a political compromise that would look like an accounting standard and look like progress and get rid of the more extreme things but not really hurt companies or make things more difficult for auditors – well, maybe just a bit because that's what we're here for.[465]

In defence of the ASC it should be pointed out that whether goodwill is an asset remains a matter of contention – even at the conceptual level and between standard-setters using similar conceptual frameworks.[466] The technical case for narrowing the areas of difference had now become deeply embroiled in an environment of economic consequences and political interests.

The ASC did manage to rescue standardized choice – alternative treatments for alternative circumstances – in one important respect during the period, by adopting 'the Unilever method' of foreign currency translation. Even here, though, free choice prevailed in the profit and loss account.

A – surely unwise – feature of the tradecraft of standardization during the period was the continual announcement of grossly optimistic forecasts of the future timetable. It is difficult to believe that those involved could possibly have thought that work was going to proceed on the timescale they were claiming; each new claim flew in the face of previous experience. Though no great damage may be done in the world at large by announcing and missing deadlines, the impression created by the constant, unrelieved, news of slippage was of an organization losing its grip: 'the delays and the extent of the rewriting have become notorious.'[467]

Several of the ASC's working parties included members from – some, at least, clearly saw themselves as representing – organizations with well-known positions on the subject. In some cases they were associated with industry groups. In others, individual preparers with direct interests were central to the development effort. In the case of foreign currency, the involvement of Unilever, Shell, Cook and Gold was particularly significant, with Cook, indeed, moving from Unilever to the IASC, whose support for 'the Unilever method' eased its passage into the standard, and thence to Shell. Gold appeared at the public hearing for ED27 on behalf of Shell to explain that, 'the terms of the exposure draft are strongly supported',[468] when he was a member of the panel that had produced it. He also attended the FASB public hearings,[469] but would not have been allowed to play any part in the production of the US standard. Such preparers bring a fund of technical expertise and operational experience to standard-setting and this is

particularly valuable when the secretariat has limited resources. Their preferred methods may well be appropriate and even superior to others. Given the political environment within which the ASC was operating, they also brought influence of value in securing the acceptance and implementation of pronouncements. There is, though, a danger that a standard-setter can be seen as becoming too close to the interest groups whose interests they are supposed to regulate.

Finally, the ASC's difficulties with its member bodies were now producing delays in the adoption of standards that were both embarrassing in themselves and embarrassing because they drew attention to the constitutional structure that caused them.

9 Accounting for Changing Prices: The Struggle Continues – and Ends Badly

We left the problem of price change accounting in 1974, with the profession's preferred solution, current purchasing power accounting, forming the basis for a provisional standard. Only a provisional standard could be issued because, in mid-1973, the government pulled the rug out from under the profession by establishing a committee of inquiry on the subject.[1] We now pick up the story.

The Sandilands Report

The Sandilands Committee began meeting in January 1974 and signed its report[2] on 25 June 1975. During this period there was a change of government but the incoming Labour administration asked the committee to continue its work under the same terms of reference.[3] As expected, the report recommended a system drawing heavily on the replacement cost model. David Tweedie and Professor Geoffrey Whittington show how this outcome may have been shaped, not only by the background of the members,[4] but also by the committee's terms of reference (it was required to consider matters such as management decision-making, for which the ASC had never claimed CPP was appropriate); by its visits to other countries (it was particularly impressed by the use of replacement cost in the Netherlands); by criticism of CPP from industry and from the Society of Investment Analysts; and by the rather unusual nature of the inflation occurring in the UK at the time. In 1973, the normal broad equivalence between movements in raw material and retail prices collapsed:[5] a dramatic change in oil prices, following the Middle East War, caused industrial raw material prices to rise by 32 per cent while retail prices (which would be used under CPP) rose by only 9 per cent; in the following year the figures were 48 per cent and 16 per cent. The resulting profit squeeze provoked a massive industrial crisis which the application of the retail price index simply did not capture and this undoubtedly increased the unpopularity of CPP within industry. A particular concern was the treatment of stock for tax purposes.

Chris Westwick, still working on price change accounting for the ASSC, was appointed technical liaison officer to the Sandilands committee. The ASSC made four submissions to Sandilands: 'the main thrust of the ASSC's argument was naturally in favour of CPP accounting ... Our arguments however seemed

to have been of little avail.'[6] Westwick believes that his appointment was intended as an olive branch to the profession – Francis Sandilands was a man of old-fashioned courtesy and got on well with Sir Ronald Leach. At first Westwick received the papers prepared for the Sandilands Committee but after a while they stopped coming and he was told they were confidential.[7]

Sandilands recommended a measurement method known as 'value to the business'.[8] Although in practice this normally yields a carrying amount measured at replacement cost, the system is rather more complex because it is designed to deal with abnormal cases in which replacement cost would not be appropriate.[9] The new system was to be used in the main accounts and not merely to provide supplementary information[10] and was to be referred to as 'current cost accounting'.[11]

Sandilands was flatly dismissive of CPP accounting, questioning even the usefulness of the concept of general inflation.[12] Consonant with this dismissal, there would, in the proposed system, be no recognition of gains and losses on the holding of monetary items and no move to establish a constant unit of measurement. Two adjustments would be made in the profit and loss account: a cost of sales adjustment to reflect the difference between historical cost and value to the business of stock sold; and a depreciation adjustment to reflect the effect of charging depreciation on value to the business. Holding gains were to be carried to reserves. The balance sheet would be in current costs.[13]

The committee recommended that 'a Steering Group should be set up under the aegis of the ASSC to oversee the introduction of current cost accounting in consultation with the ASSC and the professional accounting bodies.'[14] The target implementation date for listed and other large companies and the nationalized industries was 24 December 1977.[15] A number of detailed recommendations on the functioning of the Steering Group were made, including that the members should be paid.[16]

In policy terms, the Sandilands Report represented 'a formidable piece of work, prepared under great time pressure with slender resources.'[17] Its 364 pages include a 60-page appendix giving a fully-worked example.[18] A brand new system of accounting had been produced in substantially less time than the ASSC were by then taking to get out a standard on many individual topics – for example research and development or depreciation.[19] Nonetheless, the report fell short of providing a complete system and there was a good deal of work left for the Steering Group to do.

The Sandilands report was published in September 1975 and the government sought a reaction from the accountancy profession before the new Parliamentary session began in November. A response on behalf of the CCAB, prepared by a committee of the ASSC chaired by Sir William Slimmings and serviced by Westwick, was submitted at the end of October.[20] In view of the speed with which it was required, the submission focused on the central recommendations of the report. It welcomed the report's conclusions as a major step towards more relevant and informative reporting and accepted that, provided appropriate indices were made available, the system was practicable. However, it disputed

the committee's claim that the proposed system was comprehensive, pointing out that it did not account for the impact of price level movements on monetary assets and liabilities or the effect of changes in the unit of measurement on comparability through time and the measurement of proprietors' interest. The short-term recommendation for responding to this problem was to combine CCA with a CPP-based calculation, to show the amount necessary to maintain the proprietors' interest in purchasing power terms, in a separate statement after the Sandilands figures. Even this suggestion did not prove acceptable to the government. The Secretary of State for Trade made a statement to the House of Commons at the end of November, endorsing Sandilands' recommendations; the profession, 'having virtually been ordered by the government to produce a current cost solution to the problem of accounting for inflation',[21] set to work.

The Inflation Accounting Steering Group and ED18

The Inflation Accounting Steering Group was established in January 1976. It was constituted as a sub-committee of the ASC but was separately funded, one-third by government and two-thirds by major firms and companies. The private sector funding effort was co-ordinated by Leach; in total, undertakings to finance an operation costing around £125,000 per annum for three years were received. The group was chaired by Douglas Morpeth, 'an energetic chairman . . . able to devote a substantial amount of time, energy and thought to the work'.[22] The group was composed of three accountants from practice and five from industry and commerce, two civil servants (one an accountant), one academic accountant and one stockbroker. Members included Ian Hay Davison, Professor Harold Edey, Jeffrey Pearcy (of ICI), Kenneth Sharp and Stanley Thomson (of Ford UK). A secretariat of qualified staff was recruited on secondment, with Chris Westwick as secretary.

The terms of reference of the IASG were agreed with the government. The group was to draft a standard implementing the Sandilands report, taking into account responses to the report and especially that from the CCAB; further study those areas identified as needing such study by Sandilands and undertake any other research considered necessary; and test the practicability of the proposed scheme by field testing.[23]

An initial decision by the IASG was significantly to shape its output:

> At the start of the work . . . we decided that we would endeavour as far as possible to cover all the practical problems raised by the introduction of current cost accounting. We felt that if we did not do so we should be open to the legitimate criticism that we were putting forward something which was not practicable. It was most important that the methods of CCA should be fully explained if CCA was to replace historical cost counting.[24]

To that end six working parties were established and a list of 25 problem areas allocated among the working parties and various outside experts. Some idea of

the range of problems faced by the IASG can be obtained from a partial selection of the topics on the list:

> Distributable profit – need to define? Valuation of liabilities; Associates; Subsidiaries; Overseas assets and operations; Goodwill and other intangibles; Comparative figures; Publication of interim statements; Calculation of deferred tax; Treatment of realised holding gains; Audit implications; Compatibility with draft Fourth Directive, IASC, other overseas standards and legislation, and stock exchange requirements in the UK and overseas; impact of CCA on other ASC standards.[25]

In examining this list, it is important to bear in mind that, at the time, there were no standards covering depreciation, group accounts, overseas operations, or goodwill and other intangibles. Although there was a standard on deferred taxation it was running rapidly into trouble.[26]

During 1976 the IASG submitted 14 interim reports on different aspects of CCA to the ASC. The report on goodwill gives some idea of the problems the IASG faced as a result of its determination to produce a comprehensive system. No doubt written tongue in cheek, it politely asked the ASC to make up its mind on the fundamentals of the problem:

> The Steering Group would find it of great assistance if the ASC, having considered this paper, could advise the appropriate treatment of goodwill under Historic Cost Accounting, so that the Exposure Draft on CCA can be based on the ASC's recommended method.[27]

Equally polite, but in no mood to be browbeaten by a mere working party, the ASC responded:

> It was agreed that IASG should be asked to recommend an appropriate treatment of goodwill under the CCA system and to include this treatment in the Exposure Draft. The committee was of the opinion that the Exposure Draft should contain a single treatment and not recommend alternative treatments.[28]

And this from the committee that was not to bring itself to recommend a single treatment of goodwill, under historical cost accounting, for another decade.

The working party dealing with legal implications argued against making the use of CCA a legal requirement. Instead, in order to ensure flexibility, it was suggested that reliance be placed on an orthodox accounting standard and Stock Exchange sanctions. The majority of the working party supported an interpretation of the true and fair view doctrine that meant that no amendment to company law would be needed to introduce CCA: this interpretation amounted essentially to the proposition that nothing known about the court's interpretation of true and fair conflicted with CCA.[29]

The IASG's determination to construct a fully worked-out system of CCA involved it in a huge volume of work. In the last two months before its recommendations were finalized, the Steering Group was meeting weekly. Tweedie and Whittington devote very nearly 100 pages to the British debate on price change accounting from 1973 to 1983 but find that, 'given the comprehensive nature of [the resulting draft], it would be impossible to deal ... with all the problems tackled by the IASG during 1976' in the space they have available.[30] The ASC were unwilling to allow the IASG to publish discussion papers, so it had to rely on field testing and limited consultation with particular interest groups. Their work was shadowed by a government committee set up to liaise with the IASG.

The major theoretical issue faced by the IASG was the need to identify a capital maintenance model. This encapsulated the clash between Sandilands and the CCAB response on the treatment of monetary items and proprietors' capital. The group considered a variety of approaches before arriving back at the suggestion in the CCAB response. In relation to the capital maintenance model to be used in the main accounts and the treatment of holding gains, the group fell back on permitting a wide range of discretion: the net surplus on the revaluation of assets was to be appropriated to a revaluation reserve but directors could transfer more or less than this amount to reflect, among other things: (a) the maintenance of monetary, in addition to physical, assets; (b) maintenance of equity in purchasing power terms; and (c) the release of holding gains on assets financed from borrowing.[31] The exposure draft was candid about admitting that this was an 'interim solution which will almost certainly require modification in the light of experience'.[32]

This approach was settled on very late in the development of the document. One member of the ASC, Frank Barrett,[33] provided for colleagues in his firm a full account of the committee's discussions over the weekend of 2 and 3 October:

> These meetings represented the second and third days of a series of five or six organised by the ASC to review and, hopefully, approve the IASG draft ... The version ... which we used in our discussion was draft 9 which became available the day before our meeting. About 17 members of the ASC attended on both days [out of 21] ... Th[e] debate [on capital maintenance and holding gains] took the entire [Sunday[34]] afternoon and the result was that the Steering Group was told, in effect, to go back to the drawing board. There was considerable divergence of views among the Committee members and, after a very full airing, it was not possible to reach any reasonable measure of agreement. If I interpret correctly the consensus of the meeting in so far as any consensus was discernible, a majority was in favour of splitting the presently unified profit and loss account into two parts, the second of which [is] to be treated as an appropriation account. Even though they will be working along these lines I am not at all sure that what they produce will be agreed at the next meeting.[35]

The split account first appeared in draft 10, dated 18 October. The shadow government committee 'was not keen on going beyond Sandilands on the question of monetary items and in the event was only just able to accept the appropriation account proposals'.[36] Fortunately the proposals were also acceptable to the ASC.

Both the IASG and the ASC were aware, as they debated successive versions of the CCA draft, that it was unlikely to be universally welcomed. Guest Keen & Nettleford had been generally supportive of the IASG's work but, on 1 September, Paddy Custis, its finance director, wrote to Douglas Morpeth, 'to voice [his] disquiet on the way the work of the Steering Group [was] developing'.[37] Barrett's account of the ASC weekend quoted above concludes that: 'the draft is fraught with problems and imperfections'.[38] Nonetheless, the key players felt impelled to go forward with the draft, in part because of an acute awareness of how much time had already been taken up in working on a solution. One source of encouragement was the largely favourable responses to initial field testing. Westwick was struck by how feedback from field-testers reflected 'attitude of mind' rather than objective conditions: 'one company gave it to one of the young lads who polished it off in an afternoon, while another gave it to one of their senior staff, who came back a month later and said, "this is impossible."'[39] However, as Westwick himself has pointed out, companies agreeing to participate in the field testing programme were likely to be favourably inclined to the system – or, at least, neutral and open to fresh ideas – and to have an above average level of technical resource.[40]

The ASC's consideration of the document, though lengthy and time-consuming, nonetheless concentrated on its 'cardinal features',[41] an approach agreed by the committee itself in advance.[42] The final vote was twenty to two for publication, comfortably above the two-thirds majority required.[43] ED18 'Current Cost Accounting' was published on 30 November 1976, less than twelve months after the IASG was established. It ran to 332 paragraphs plus an introduction and five appendices – nearly 100 pages in all. The IASG also produced a brief guide,[44] a guidance manual[45] and a volume of background papers,[46] which constituted, in effect, a basis for conclusions. The guidance manual contained nearly 300 pages, excluding the ED itself and a Royal Institution of Chartered Surveyors guidance note on valuation, which appeared as appendices. It was produced by a working party led by Davison, who himself applied a great deal of thought and energy to its production; it also occupied one of the secretariat full time.[47] A guidance manual of this size was another consequence of the decision to construct the most comprehensive system attainable within the time and resources available.[48]

The overall impression given by the documentation was certainly of comprehensiveness – the objective the IASG had set out to achieve – but also of a system likely to be cumbersome, difficult, time-consuming and expensive to implement, as Barrett, Custis and others feared. One consequence of presenting a fully-worked out system was that it was perceived by some as an attempt to steamroller the system through unchanged, whereas, in fact,

> the Steering Group was determined that they would consider all informed comments with open minds and accepted that there would be a need for changes in the preparation of the standard. This was said during the exposure period loud and clear, by many members of the Steering Group. It is a great pity that this was not sufficiently accepted at its face value by more people.[49]

The likely length and complexity of the ED – and the effect this would probably have on its readership – dawned on the IASG only as its various working parties contributed their sections to the finished product; indeed, it seems likely that length and complexity were in part a result of the distribution of the drafting work between a variety of working parties. The group was concerned about the issue and its decision to produce a 'brief guide' was a response to this concern.

The basic principles of ED18, as described by Westwick, one of its main architects, were:

(a) the non-monetary assets of the business should be shown in the balance sheet at their value to the business at the balance sheet date. Value to the business would normally be replacement cost but in exceptional circumstances could be the higher of net realisable value and economic value (discounted present value) if both were lower than replacement cost.
(b) revenue should be charged with the depreciation of fixed assets calculated on their value to the business, and with the cost of stock consumed valued at its replacement cost at the date of sale.
(c) revaluation surpluses should be credited in the first instance to the appropriation account. Revaluation surpluses would arise mainly from the revaluation of fixed assets and from the difference between the replacement cost and historical cost of stock consumed.
(d) directors should appropriate out of the revaluation surpluses and, if necessary, out of current cost profit, an amount based on their assessment of the needs of the business including provisions for the effect of inflation on monetary items, gearing and backlog depreciation.[50]

The draft made it clear that it was intended that the system would apply to all financial statements designed to give a true and fair view.[51] However, in order to 'spread the workload on those concerned in its introduction',[52] it was to be introduced in four phases, starting with listed and large non-listed companies, then proceeding through three remaining tiers by size. The first tier would produce CCA accounts from July 1978, and the next two after a further six and eighteen months respectively, but there was no implementation date for the smallest category. This was for companies with turnover and assets of below £100,000. It was further said, of this last category, that a method appropriate to

it would be devised by the ASC and ample warning of the commencement date given; in other words – don't worry yet awhile.[53]

ED18 yielded a massive response: 746 submissions in all, three times as many as the next largest response, also to a draft on CCA, and nearly five times as many as the largest response to an ED not on CCA. There were in fact only 666 letters of comment but to these were added questionnaires returned by those field-testing the system, perhaps to avoid focusing on the number 666. Tweedie and Whittington carried out an extensive analysis of a sample of 133 responses, drawn to include both the most important key opinion formers and a random selection of others.[54] Their findings correspond to the internal analyses carried out by the IASG at the time.[55] Only 5 per cent of respondents supported the draft unamended, or with only a few, minor, amendments, and more than half of these were users. The most common objection to the draft was its complexity, criticized by 59 per cent.[56] The next most common criticisms, all expressed by almost exactly 40 per cent of respondents were subjectivity; speed of implementation; cost of the system; abandonment of historical cost; the approach to the valuation of fixed assets; the appropriation account; and treatment of monetary items.[57] Had the group done anything right?

Of course, contributors to the debate were not motivated solely by pursuit of technical excellence:

> Taking an overview of the objections to ED18, it could be said that, in many ways, self interest lay behind many of the criticisms of the Exposure Draft's proposals. The desire of practising accountants for objectivity and a precise definition of income in current cost accounts, in addition to their reluctance to abandon historical cost accounts, reflected their concern with the difficulties of auditing the proposed ... financial statements. On the other hand, perhaps not unnaturally, preparers of accounts did not appear to be as worried as auditors about either the prospect of the increased element of judgement involved in the preparation of their accounts or the greater discretion given to directors in the determination of income. The expense of implementation was of more relative importance to this group.[58]

Furthermore:

> Banks did not like the absence of a monetary adjustment before the appropriation stage, since they believe[d] they should be entitled to tax relief on amounts set aside to maintain their capital base. Equipment leasing interests did not like the capitalisation of leased equipment in the accounts of the lessee.[59]

And the list goes on: government contractors working on fixed-price contracts did not like the treatment of work in progress as a monetary item, thereby precluding the application of a cost of sales adjustment that would have yielded a lower profit margin and, they hoped, justify a higher price.[60] Companies with

substantial 'cash mountains' were unwilling to show the damage inflation was causing to their investments.[61] A simple objection was that 'many company managements did not like the effect of the proposals on reported profit.'[62] Against this level of opposition, it might be counted a considerable feat to have got an exposure draft out at all.

In the subsequent debate, particular heat came from small and medium-sized entities and small practitioners. The burden of CCA was likely to be proportionately large for smaller entities, since learning and system redesign costs would be relatively fixed, and small practitioners felt that better management accounting and cash management procedures represented a higher priority for smaller business than CCA.[63] The ASC realized early in the exposure period that the threshold for inclusion in the timetabled phases had been set too low, at least in political terms, and Morpeth made a public statement to the effect that it would be 'increased considerably'.[64] Other changes that the IASG announced that it would be pursuing included: simplifying the proposals; delaying the switch to CCA for the main statements; and improving the treatment of monetary items.[65]

These efforts were, however, too late to save ED18. Two previously low-profile members of the ICAEW, David Keymer and Martin Haslam, requisitioned a special meeting of the Institute to consider the resolution, 'that the members of the ICAEW do not wish any system of current cost accounting to be made compulsory'.[66] The meeting took place on Wednesday, 6 July 1977. In the run-up to the meeting, *The Economist* published a highly critical article under the headline 'Accountants funk inflation': 'Is the British accountant capable of advising on the finances of a whelk-stall? Not in a period of inflation, judging by his response to the most important single issue that the British accountancy profession has faced since the war.'[67] Statements were sent to the membership from Council and the President putting the case for CCA. Neither the Institute's leadership nor *The Economist*'s criticism could deflect the critics, however, and the resolution was carried by 15,512 votes to 13,148, a margin of about 10 per cent of the total votes cast.[68] Just under half the membership voted – a record turnout.[69]

Westwick has offered his impressions of the motivations of those who voted against ED18.[70] Some, he felt, doubted the establishment's willingness to amend the draft; some preferred CPP; some rejected price change accounting altogether; and some were using the opportunity to protest about other aspects of the profession's leadership, including its remoteness from small practitioners and those in industry – for whom the potentially universal imposition of CCA represented a focus for this wider concern.

The ICAEW Council immediately re-affirmed its view 'that the introduction of an acceptable system of accounting in the face of inflation [was] urgently needed' but recognized 'that there should be a reappraisal of the approach to the introduction of accounting in the face of inflation', stating that, 'with this aim in view it intend[ed] to urge the Accounting Standards Committee to hold further consultations with representatives of finance, commerce, industry and the government.'[71] The ASC did not have to wait long for the government's

reaction. On 8 July, the Under Secretary of State at the Department of Trade welcomed the Institute's call for a reappraisal of approach but re-affirmed its support for the early introduction of CCA.[72] Now almost everyone was speaking with forked tongue: pity the poor IASG.

Shortly after the general meeting, representatives of the Confederation of British Industry and the Stock Exchange met the chairmen of the ASC and IASG and 'expressed concern that momentum should not be lost' in the development of CCA.[73] Since 97 per cent of preparers and 95 per cent of bodies representing preparers who had responded to ED18 had either expressed outright opposition to CCA or called for substantial amendments,[74] the membership of the CBI must have been heavily implicated in the disturbance of its momentum; we must presume, though, that the urbane Slimmings[75] resisted the temptation to point this out. The Stock Exchange felt justified irritation in finding itself having supported a pronouncement that the ASC itself now apparently intended substantially to revise. One consequence of the revolt was that the changes the IASG had already announced tended to be seen as a consequence of 'direct action'.

In order to try to keep the momentum up, the ASC issued a Statement of Intent later in July. It announced that, in the short term, it was proposing that the IASG develop simple guidelines for supplementing historical cost accounts with CCA information about depreciation and cost of sales. In addition, an adjustment to take account of gearing would be included in the statement. The aim was to produce guidance in time for application for the year ending 31 December 1977. Although inflation was falling from the peak of 24 per cent in 1975, it remained in double figures. The annualized rate for May 1976, the latest figure that would have been available for the ICAEW special meeting, was 15 per cent and it fluctuated between 13 and 18 per cent for the next eighteen months.[76]

The idea of a gearing adjustment had been under consideration by the IASG for some weeks – it lay behind the inclusion in the May 1977 statement of the proposal to seek an improvement in the treatment of monetary items. The shift was influenced by Stanley Thomson, finance director of Ford UK and a member of the IASG. Ford was at that stage considering making an adjustment in the appropriation account in their 1976 CCA financial statements to retain in the revaluation reserve only that part of the revaluation surplus for the year attributable to the proportion of assets financed by equity (and it did, indeed, do so). Ford was a front-runner in the development of CCA, in part because the company accepted that, in conducting what were often difficult negotiations with its trade unions, it could scarcely claim that there was no money to meet high wage claims while reporting substantial historical cost profits to its shareholders.[77]

The Hyde Guidelines and ED24

A fresh committee, chaired by William Hyde, a member of the ASC, and containing three members of the IASG, got down to work. All the major decisions

had been taken: the Statement of Intent gave the skeleton and the flesh had simply to be transplanted from Sandilands, ED18 and work already done on the Ford gearing adjustment. The committee conducted all its work by post and telephone. The secretariat was now headed by John Foyle, a member since its inception, on secondment from Price Waterhouse; Westwick had moved to become Technical Director of the ICAEW, following Renshall's departure. The resulting pronouncement, universally referred to as the Hyde Guidelines,[78] was issued in November 1977. Published in the name of the ASC, it had in fact been cleared by the CCAB bodies. The Institute of Chartered Accountants of Scotland was concerned that companies might want to use methods of calculating a gearing adjustment other than that suggested and the pronouncement was amended to permit this.

The depreciation and cost of sales adjustments had proved relatively uncontroversial in ED18 and were incorporated into Hyde. The gearing adjustment essentially followed the Ford model except (and importantly) that only realized revaluations for the period (in the form of the cost of sales and depreciation adjustments) entered into the calculation of the adjustment, a more conservative approach. The effect of the gearing adjustment was to abate the other CCA adjustments by adding back to profit the extent to which the relevant assets had been financed by borrowing. If monetary assets exceeded liabilities, a gearing adjustment to reflect the additional capital needed to maintain the operating capacity of the business, analogous to the cost of sales adjustment for inventory, was to be made. It was thought that this would be popular with the banks. There was no CCA balance sheet.

The Hyde guidelines stood in contradistinction to ED18: voluntary, limited in scope to listed companies, simple, short. Indeed, almost vanishingly short: 24 paragraphs, including the introduction explaining the background, plus three one-page appendices. Commentators have generally regarded the Hyde guidelines as 'accepted reasonably well by industry',[79] and so they were, up to a point. The ICAEW survey of published accounts for 1978/79, the first full year after the recommended implementation date, shows that 47 per cent of the companies surveyed provided supplementary information following the guidelines, with another 9 per cent using other methods to provide price change accounting information. All the companies in the survey were listed on the Stock Exchange and therefore fell within the scope of the recommendations. Thus 44 per cent of companies to whom the Hyde guidelines were addressed ignored them; a substantial improvement on the reaction to ED18, but hardly universal support.[80]

It is also true that with Hyde, 'the emotional climate surrounding the introduction of CCA was changed'.[81] Tempers cooled; workloads lessened; flexibility was introduced. The gearing adjustment offered a real prospect of moving both the conceptual debate, and the practice of price change accounting, on from the intellectually, politically and practically impoverished position in which Sandilands had left it. Westwick is right to remind us, though, that one factor affecting attitudes in 1977 was surely, 'the cumulative effect of the debate so far'.[82]

Work on developing a new standard proceeded in parallel with the production of the Hyde guidelines. As well as technical development, there was 'considerable debate on the political desirability and timing of another exposure draft'.[83] A further Statement of Intent was published in July 1978, announcing that a new ED would be produced and that it would be evolutionary from Hyde. Three features announced at this stage were intended to defuse major objections to ED18. The new standard would apply only to listed and large companies, with simpler methods available to other companies on a voluntary basis. The information would be supplementary to the historical cost accounts and would be provided by adjustment to historical cost profit rather than, like ED18, 'starting again'. Finally the standard would be confined to principles, with non-mandatory guidance notes offering technical infilling, and thus be relatively simple and short. Two of these three key features thus directly contradicted explicit recommendations of Sandilands, while the third certainly contradicted its spirit; since Sandilands itself contains no fewer than 199 recommendations, it is difficult to see how they could be accommodated in a simple, short standard.

The resulting exposure draft, ED24 'Current Cost Accounting', was issued in April 1979. It largely kept the promises of the Statement of Intent. It was certainly shorter: 50 paragraphs against ED18's 332. A number of features go beyond the Statement of Intent, to meet criticisms of ED18, and ED24 was built around a more intellectually coherent model. There is a clearly defined concept of income: 'the surplus after allowing for the impact of price changes on the funds needed to continue the existing business and maintain its operating capability.'[84] Value to the business was retained as the measurement method but was now described in rather more practical terms. The current cost balance sheet was reinstated, but with much greater emphasis on flexibility and the use of indices.

ED24 moved the approach to monetary items on a stage from Hyde. There were now to be two adjustments: monetary working capital was subject to an adjustment paralleling the cost of sales adjustment while long-term borrowing entered into a gearing adjustment similar in approach to Hyde's. The preface helpfully showed how the monetary working capital adjustment would work for a supermarket, a manufacturing company and a bank – in the latter case substantially reducing historical cost profit. This approach had been considered by the IASG during its deliberations on ED18 but discarded. The draft's approach to monetary items was its most controversial aspect.

The ASC and the ICAEW secretariat undertook a public relations campaign, promoting the virtues of ED24 to large companies and auditors.[85] In general, ED24 was well received. Tweedie and Whittington analysed a sample of the 248 submissions made on the draft and found that 83 per cent 'broadly supported' the ED; 78 per cent of the sampled companies in the top 100 of The Times 1000 and eight of the top ten accounting firms were supportive, as were all five of the 'influential representative bodies' sampled, the CBI, the three major finance directors' groups and the Society of Investment Analysts.[86] All six

CCAB bodies expressed full or qualified support.[87] The way was now clear for the publication of a standard.

SSAP16 'Current Cost Accounting' was issued in March 1980, nearly a decade after work started on ED8. Including Sandilands, a different proposal on price change accounting was unveiled every year between 1973 and 1980 with the single exception of 1978.[88] As well as the standard there were guidance notes,[89] and a manual to assist smaller businesses adopting CCA voluntarily, published under the unforgettable title, *CCA The Easy Way*.[90] SSAP16 did not differ materially from its predecessor exposure draft; although a number of minor changes were made in method, scope and presentation.

At the time ED24 was published, the UK had just enjoyed its sixteenth month of single-digit annual inflation. In the month of its publication (April 1979) inflation climbed back above the 10 per cent level and, by the publication of SSAP16, it was running at 20 per cent. The Statement by the ASC on the publication of SSAP16 indicated that,

> the ASC believes that there is now a need for a period of stability. It is the intention of the ASC, as far as possible, to make no change to SSAP 16 for three years so as to enable producers and users to gain experience in dealing with practical problems and interpreting the information. The ASC will maintain a standing sub-committee to monitor the ways in which SSAP 16 is being implemented and the changes that may ultimately be needed.[91]

Unfortunately, as we shall see, these rather innocent comments were to create further difficulties for the committee.

The Short Life of SSAP16

As Tweedie and Whittington put it, with the publication of SSAP16, 'the debate in the UK rested.'[92] However, at around the same time, a number of critical features of the environment surrounding price change accounting altered dramatically. May 1979 saw the election of a Conservative administration with a fundamentally different philosophy underpinning the battle against inflation: attempts to control prices and incomes directly were replaced by restrictive monetary policy. Whether for this reason or otherwise,[93] inflation dropped; after peaking in May 1980 (two months after the publication of SSAP16) at 22 per cent, the annualized rate fell for 32 successive months with only four minor blips, none raising the rate by a full point. At the beginning of 1983 the rate fell below 5 per cent for the first time in over a decade. Whatever the impact on the reliability of historical cost information of inflation at these levels,[94] the impression was clearly that the problem was now firmly under control.

The shift from prices and incomes policy substantially reduced one of the attractions of CCA to preparers. While at the Price Commission during the late 1970s, Davison had been instrumental in persuading it to base its calculations of acceptable levels of profits on accounting data adjusted for price changes.[95]

Thus there was a powerful incentive for large companies to use CCA to persuade the Commission that high historical cost profits did not represent grounds for refusal to approve price increases. There is, indeed, statistical evidence that regulatory influences affected compliance with SSAP16.[96] The abolition of the Commission and its price control regime in 1980 removed this incentive.

A potential incentive to move to CCA, never in fact becoming available, was its use in the corporate tax system. From the beginning, the relationship between price change accounting and the tax system had been a significant factor in the development of the former.[97] Positions taken up towards particular aspects of the methodology were certainly consistent with the pursuit of advantage from a CCA-based tax system, for example positions towards the treatment of holding gains. Successive Chancellors of the Exchequer, of both political colours, had indicated that it might be possible to use price change accounting to provide tax relief for inflation provided that a suitable system could be designed; the first to do so was Denis Healy, on introducing stock relief in 1974. It has been suggested that the publication of the Green Paper on reform of Corporation Tax in January 1982[98] marked a turning point in the debate by signalling the government's unwillingness to move to CCA for the corporate tax base.[99] However, the situation is rather more complex than this. The Green Paper certainly signals considerable concern about practical issues arising from the use of SSAP16 profits for taxation, for example the subjectivity of asset lives and the chosen revaluation basis for depreciable fixed assets.[100] However its main focus was on the feasibility of using current costs for taxation rather than specifically the system adopted by an accounting standard and its comments were much friendlier towards the possibility of using standardized lives and official price indices by broad categories of asset.[101] Such an approach would parallel traditional methods of dealing with fixed assets for tax purposes; while it would not necessarily involve companies switching to SSAP16, a move to current costs for financial reporting would be consistent with their use for tax purposes and might encourage the Inland Revenue in that direction.

The Green Paper offers an insight into one possible motivation for industry to back-peddle on CCA-based taxation. It makes it clear that any change to the system will be designed to be revenue-neutral, that is, the rate of tax will be changed to yield the same total revenue from the newly-defined base.[102] Using past data, it estimates that, at the time of publication of the paper, the move would have left the tax rate broadly as it was, largely because of the extent to which the system of allowances had already been adapted to provide relief for the effects of inflation.[103] There would, however, have been substantial redistributive effects, including a dramatic increase in the burden on manufacturing and distribution and a similar reduction in that on the financial sector, almost entirely due to the introduction of monetary adjustments into the system.[104] So the message to the manufacturing and distribution sectors was not, 'you can't have CCA taxation', but rather, 'don't think you can ramp up your allowances and, by the way, you'll pay more tax, because of the relief you want us to give to the banks.'

The ASC honoured its promise to 'maintain a standing sub-committee to monitor the ways in which SSAP 16 is being implemented and the changes that may ultimately be needed',[105] and in abundance. Initially the sub-committee was chaired by Morpeth; at the end of 1981 it had six working parties.[106] One, set up in November 1980, and chaired at the beginning by Custis, dealt with monitoring and publicity. When the reconstituted ASC took over in September 1982, it created a new Inflation Accounting Sub-Committee, chaired by Thomson.[107] This had twelve members, with six coming from listed companies and five from public practice, and an observer from the Inland Revenue. It had five working parties with members drawn largely from outside the sub-committee. Tom Neville, finance director of Vickers, took over as chairman of the monitoring group and its reports appeared under his name. While the announcement that the standard was to be kept under review was probably politically useful in securing initial acceptance, the decision, and especially the speed and comprehensiveness of its implementation, undoubtedly contributed towards the development of an expectation of impermanence.

In 1980/81, the first year in which SSAP16 applied, 78 per cent of the listed companies covered by the ICAEW's annual survey published CCA information, though with a small number still complying only with the Hyde guidelines. In the following year, 95 per cent of companies did so, all following SSAP16. In the main, preparers followed the detailed requirements of the standard. Only 10 per cent of accounts included explicit adverse comment on CCA accounting, with a quarter of these coming from companies that failed to produce CCA information. The most common comment was doubt about the utility of the system.[108] It was, apparently, 'noticeable that expressions of dissatisfaction were more moderately stated' than in the previous year.[109]

In mid-1982 the instigators of the ICAEW general meeting which rejected ED18, Keymer and Haslem, requisitioned a further meeting to call for the immediate withdrawal of SSAP16. An intensive lobbying campaign was conducted; members of the ASC secretariat telephoned contacts of Council members and others, chiefly in an attempt to persuade them to write letters for publication in the quality dailies, and particularly the *Financial Times*, supporting CCA. There were a number of successes.[110]

At the meeting, held on 29 July, the resolution was defeated by 15,745 votes to 14,812 – like the earlier debate, a very close result – with 41 per cent of the membership voting.[111] As with the 1979 vote, at least some of those voting for the resolution appear to have been motivated by factors other than a concern with the technical niceties of price change accounting, and allegations along these lines were certainly made during the debate. Although the vote represented a victory for the ICAEW Council and CCA, the narrowness of the margin, after such intense lobbying, appears to have shaken confidence, as indeed, arguably, it should have done.

Within weeks of the special meeting, Davison took over the chairmanship of the ASC.[112] His track record of astute political manoeuvring no doubt improved the prospects of a settled outcome but also encouraged the various interested

parties to pursue their political positions, if any encouragement was needed. A profile of Davison appeared in one specialist newsletter, suggesting that 'the trial period for SSAP16 will be ended at the earliest possible date'[113] and speculating that it would be replaced by a simple, non-mandatory pronouncement addressed only to large companies. This caused Morpeth to write to the President of the ICAEW, protesting at the comments and querying whether a decision to ditch SSAP16 was indeed the current position of the ICAEW.[114] By now there was an increasing perception, reflected in the profile quoted above, that the initial years of SSAP16 were in 'in some sense experimental'.[115] This was not the intention of the ASC at the time of its publication; the accompanying statement[116] was designed to secure a period of stability before the standard was adapted, not until it was abandoned.[117]

Morpeth's letter went on to comment waspishly on the profile's apparent revelation that Davison 'has much more respect for David Keymer and Martin Haslam than many others in the accounting establishment, believing that their actions have changed the climate on inflation accounting, if not standards as a whole, very dramatically'.[118] Certainly, Davison took Keymer and Haslem seriously, travelling to Haywards Heath to meet them on 11 November 1982.[119] They explained that the correspondence they had received opposing SSAP16 came from larger companies falling within its scope – a surprise to the ASC, which had assumed that they were speaking for small practitioners who might be reassured by a promise to leave them permanently outside the scope of the system. Keymer and Haslem were willing to make the correspondence available to the Neville group, but not the ASC, and only after they had 'filter[ed] some of the more trenchant letters', suggesting that they must have been quite vitriolic. There is no evidence that Davison had a particular respect for Keymer and Haslem's technical or policy views but clearly his visit confirms, as we would expect from a political pragmatist, that he respected their clout – how else should a political pragmatist view a force that had once stopped the ASC in its tracks and been only narrowly prevented from doing the same thing again a few weeks before?

Another blow came in December 1982, when the Stock Exchange announced that it would no longer require interim accounts to include CCA figures, although SSAP16 would still apply to annual statements. The ASC issued a joint statement with the Stock Exchange,[120] regretting the decision and expressing the hope that those companies that continued to issue interim CCA statements would follow its draft guidance notes, which had been published only a few months earlier.[121]

The monitoring group consulted a wide range of preparers, users and auditors, 169 in all. It published an interim report in April 1983, concluding that, although there was substantial agreement that historical cost accounting was unsatisfactory at a time of significant price change, few preparers or auditors believed that SSAP16 should be left substantially unamended. Although users were happy to leave SSAP16 alone, most made little use of the information it yielded. The cost of sales and depreciation adjustments were more acceptable

than the monetary adjustments. Providing two sets of statements was regarded as confusing and likely to bring the profession into disrepute, but also as unavoidable. The CCA balance sheet was thought misleading. Small businesses almost unanimously opposed the extension in scope of SSAP16 to include them. Depressingly, although there was significant agreement on a number of negatives there was no consensus on a way forward. The ASC considered the interim report and put forward three points for general discussion: that material inflation meant that historical cost accounts did not give a true and fair view; that a standard should offer alternative methods; and that the standard should be universal but subject to a cost-benefit test.[122]

The final report appeared in September 1983. Neville's recommendations were that the new standard should apply to all financial statements intended to give a true and fair view; that it should require statements to show the effects of changing prices where material; that alternative methods should be allowed; that a balance sheet should not be required; and that where trend information was given, it should be adjusted by the Retail Price Index.[123] The universality principal was particularly controversial, and, indeed, surprising, given the working party's conclusions about the unpopularity of CCA with small businesses and the careful reference in the ASC's 'discussion points' to a cost-benefit criterion.

As the Neville report was hitting the streets, the ASC secretariat was busy preparing a press release in response to a story that had appeared in *Accountancy Age*.[124] Davison had spoken to the District Societies conference of the ACCA, revealing some of the conclusions shortly to appear in the report.[125] The *Age* ran its account of the occasion under the headline 'Davison confirms the scrapping of SSAP16',[126] as, indeed, he did, in the sense that he confirmed that it was highly likely that in due course it would be replaced by something else. Other journalists searched his remarks in vain for the justification of quite such a startling way of putting it, and, predictably, the headline 'caused near-jamming of the Institute's switchboard by calls to the ASC',[127] no doubt seeking the precise date on which CCA was to be abandoned. The press release confirmed that SSAP16 continued in place until a successor was issued, but the 'legs' the story developed were another sign of the weakness of the ASC's position.

In parallel with the Neville working party, the ICAEW commissioned fifteen academic studies of the costs and benefits of CCA, under the leadership of its Director of Research, Professor Bryan Carsberg. The work was undertaken between January and September 1983; a draft of Carsberg's summary of findings became available in September and the Carsberg Report proper was circulated in November.[128] Carsberg's summary[129] suggested that the studies showed a more optimistic view of the usefulness of CCA information, and a less pessimistic view of the costs, than the Neville report. His policy prescriptions also somewhat cut across Neville; perhaps unsurprisingly, given that the programme of research was focused on costs and benefits, Carsberg recommended differential reporting on cost-benefit grounds. Again, not unsurprisingly given the attention to users, he recommended that choices of method should not be permitted, so as to promote comparability. Thomson, the chairman of the

Inflation Accounting Sub-Committee, commented to the press that the Carsberg report findings added little to what was already well-known, namely that there was no consensus on the way forward.

Towards the end of 1983, the ASC received comments from the Department of Trade and Industry on the Neville recommendations; it was not enthusiastic. The Department reminded the ASC that it had welcomed SSAP16; explained that it regarded allowing choice of methods as a regressive step, because it undermined comparability and permitted manipulation; expressed scepticism about the need for CCA to be extended to smaller entities; and pointed out that since materiality was given considerable weight in the recommendations, it would be necessary for some criteria of materiality to be developed.[130] In effect, this put the DTI in opposition to all the principal Neville recommendations.

As part of its monitoring exercise, the ASC was receiving monthly statistics from the Stock Exchange. Non-compliance with SSAP16 dominated the picture: for example, between January and March 1983, 20 companies received qualifications for failing to comply with all other standards put together while 61 failed to publish CCA statements, a further 7 failed to have them audited and 1 received a qualification on its CCA statements.[131] Further, non-compliance increased markedly towards the end of 1983: from 22 per cent in the second quarter to 48 per cent in the last.

The Inflation Accounting Sub-Committee elected to make its recommendations in the form of a draft new exposure draft. The text was actually prepared by a group of two auditors and two industrial accountants, reporting to the sub-committee. The debate became focused on the tension between a universal requirement, with, it was argued, a concomitant need to permit flexibility of method (the approach recommended by the Neville report), and differential reporting, with CCA limited to larger entities and the potential for a restrictive line on choice (as advocated by Carsberg). The sub-committee favoured universality[132] and early drafts reflected this approach. In December 1983, however, the ASC decided to focus primarily on large companies and in the following month it agreed the outlines of a further Statement of Intent which would limit the application of the new standard to large and listed companies but propose fairly prescriptive requirements. Wide publicity was given to these decisions;[133] one article describing the ASC as having 'agreed a decisive route forward'.[134]

Then, at the following month's Planning Sub-Committee, Thomson persuaded his colleagues to restore universality, with immediate application to large and listed companies and an indication that an appropriate methodology would be developed to cover the rest of the sector later. A new draft statement along these lines was prepared for the February ASC meeting, and, again, given wide publicity.[135] *Accountancy* described Davison, who had been briefing the press on the ASC's rapidly changing intentions, as 'quixotic'.[136] The February ASC meeting then rejected the Planning Sub-Committee's approach in favour of limiting the scope of the standard, although the majority by which this was agreed would have been insufficient to authorize release of an exposure draft.[137]

It has been suggested that the difference between the sub-committee and the ASC on this point is attributable to the greater representation on the latter committee of auditors and users as compared to preparers, who had half the places on the former.[138] Those favouring prescription (and therefore restricted scope) argued that a 'standard' allowing a wide degree of flexibility could scarcely be described as a standard at all – or as 'narrowing the areas of difference' – and thus would be likely to bring the standard-setting machinery into disrepute.[139] Those favouring universalism (and therefore flexibility) were able to argue that differential reporting would bring the true and fair doctrine into disrepute. The issue of whether differential reporting was compatible with the true and fair doctrine was certainly a problem for the ASC.[140] In March 1984, it sought a supplementary counsels' opinion from Leonard Hoffman and Mary Arden on whether cost-benefit criteria could be operated to introduce differential reporting in CCA terms and the opinion it obtained supported this view.

Following receipt of the supplementary opinion, the ASC agreed to issue a Statement of Intent. It set out the lines it would be taking on the development of a standard: mandatory CCA disclosure would be limited to public companies but, for these, would be essential for a true and fair view; the four profit and loss account adjustments from SSAP16 would be required, though with alternative methods of calculating the gearing adjustment permitted; some simplification of the determination of current costs would be allowed. The Auditing Practices Committee confirmed that the resulting information would be auditable. These conclusions were carried through into ED35 'Accounting for the Effects of Changing Prices', issued in July 1984. Where the main financial statements were prepared under historical cost, companies would show the required disclosures in a note; perhaps to emphasize the modest nature of its requirements, the specimen formats appended to the draft were firmly labelled 'Note 23'.[141]

By now the technical merits of any particular version of CCA were entirely subordinate to the political imperative of achieving consensus. Davison made this clear in his reflections on his chairmanship: 'I don't propose to discuss the pro's and con's of ED35 . . . The important point to recognise is that it reflected the sole basis upon which it was possible to find unanimity among the members of the ASC.'[142] Or as the secretary of the ASC at the time, Brian Singleton-Green puts it, 'what we ended up with was something that nobody agreed individually but was the only solution that everybody seemed to be willing to put their names to. So the technical content of the work came second.'[143]

July 1984 also marked the hand-over from Davison to Peter Godfrey, who describes his appointment as being 'handed a poisoned chalice', the poison being price change accounting. At least he knew the chalice was poisoned because by now the deadly substance was foaming over the brim.[144] The topic took up about half his time as chairman, most of that being devoted to 'selling' rather than production.[145]

There were 125 submissions on ED35 – a very much smaller number than for ED18. According to Christopher Pong and Professor Geoffrey Whittington,[146] only eight respondents fully supported the draft and of these the only two

preparers were nationalized industries with particular regulatory concerns. No CCAB body expressed full or qualified support. Two, the ACCA and ICMA, announced publicly, before the end of the exposure period, that they would veto any attempt to adopt a standard based on ED35,[147] a move that Davison suggested was 'to exhibit arrogance bordering on the preposterous'[148] and akin to the House of Lords announcing that they would reject an appeal before the lower court had convicted. At least one big firm was threatening privately to cease qualifying its audit reports for the lack of CCA statements.[149]

The ASC was now in an extremely difficult position. Most of its member bodies remained of the view that something should be done but there were highly divergent views about even what form the next pronouncement should take. Consultations in March 1985 showed that the ICMA favoured a standard, the ACCA and the Institute of Chartered Accountants in Ireland a SORP, and the ICAEW and the ICAS a revised exposure draft. The Stock Exchange indicated that it would not be able to enforce compliance if a significant proportion of companies rebelled. The DTI was approached to see if it would support some form of statutory backing, a question initially pursued by the ICMA and then taken up by the ASC. The DTI's response is a masterpiece of Sir Humphreydom.[150] Spanning six pages, it carefully rehearses four alternative approaches before concluding that 'all the routes have different disadvantages.'[151]

In March 1985, ED35 was withdrawn[152] and a working party headed by Renshall began the attempt to find a more popular successor.[153] In June, following the agreement of the CCAB bodies, the status of SSAP16 was changed to make it non-mandatory.[154] Such a move was not envisaged in the constitution of the ASC and required a somewhat convoluted procedure: the ASC announced that paragraphs 2–6 of the Explanatory Forward (relating to the disclosure of significant departures from standards and the obligation of members of the governing bodies to observe standards or justify departure from them) would no longer apply to SSAP16. At the same time, the CCAB bodies suspended paragraph 13 of the auditing guideline *Auditors' Reports and SSAP16*, relieving auditors of the duty to refer to any absence of CCA accounts.[155] The announcement of the change in *Accountancy* referred to rumours that compliance with SSAP16 had fallen below 20 per cent.[156]

At the same time the ASC had been working on its next attempt at a standard. Provisionally numbered ED38[157] and entitled 'Reporting the Effects of Changing Prices on Earnings',[158] it was considered by the ASC in June. The exposure draft applied only to listed companies, reducing the number of companies within its scope by about 50 per cent compared to SSAP16. It required disclosures only if material, allowed the choice of capital maintenance concept and whether to make monetary working capital and gearing adjustments, and did not include a balance sheet.[159] Some commentators argued that the wording was loose enough to permit CPP, although this was denied by Renshall.[160] The ASC agreed to a ballot on the text, but with publication delayed until the committee was sure of 'a reasonable degree of support'.[161] As a result, Godfrey embarked on (yet another) wide-ranging consultation exercise. Meetings were

held with the Stock Exchange, the Bank of England, the Treasury, various groups of finance directors and the CBI and copies of the provisional draft sent to major accountancy firms and about 50 companies.[162]

The result of the paper-based consultation has a delicious irony to it: exactly half those responding expressed full or qualified support for the draft and exactly half were opposed, fully or with qualifications. There was no distinction between auditors and preparers: both split 50/50 to within a single vote. However, there was more unqualified opposition than unqualified support. This result scarcely constituted 'a reasonable degree of support', especially for so flexible a pronouncement, and attention focused again on the possibility of securing legislative backing. Yet again, there was little consensus: the ACCA and ICMA supported seeking such backing, the Chartered Institute of Public Finance and Accountancy and the ICAI opposed it, while the ICAEW felt that CCA accounting should not be pursued further. The Stock Exchange indicated that it was unwilling to enforce a requirement.

On 23 October, Godfrey met Michael Howard, Secretary of State for Trade and Industry.[163] He emphasized that the ASC felt that CCA information was useful but explained that it had been unable to persuade business of this. Compliance was now down to 15 per cent. Howard thanked Godfrey for his 'gloomy but comprehensive' introduction. He reminded his audience that his predecessors had not been enthusiastic about legal backing and indicated that he shared their viewpoint. Godfrey was asked what the ASC proposed to do next. He explained that he felt that issuing a standard would be counter-productive and that a SORP would simply be ignored, as was happening in Australia. The third alternative was to 'bring together previous work and put it on the shelf for later use [if inflation took off again]. For example, this could be in the form of guidance notes prefaced by a commentary with an exhortation to companies.' It is evident from the remainder of the note that the Minister found this third alternative attractive.

Following discussion of the feedback from all these sources, the ASC issued a statement in December 1985, setting out its intended policy.[164] The statement began by listing the 'principal limitations of historical cost accounting' which it described as 'well understood'. It reaffirmed its view that where historical cost information is materially affected, information about the impact of changing prices is necessary and that CCA was the best system for providing such information. Listed companies were 'urged' to disclose information. The committee proposed that SSAP16 should be withdrawn, 'to free the way for innovation and development', but considered that its 'general principles and methodology remain[ed] sound'. The standard, with supplementary material, would form the basis for a Handbook, to be prepared by the ASC. It had become clear that 'if a general practice of even modest minimum disclosure is to be established, it is presently beyond the accounting profession alone.' The ASC would consult with the CCAB about how disclosure provisions might be developed and whether statutory support should be sought. CCAB bodies were urged to retain the subject on examination syllabuses. Finally, the committee warned that 'historically the cycle of inflation always returns'.

The proposal to withdraw SSAP16 and seek legal backing for current cost disclosures was first put to the CCAB in February 1986.[165] Of course, given what was already known about the government's position, a request for statutory backing must be seen more as a move to allocate blame than an attempt to secure the publication of CCA information. In any event, the CCAB presidents decided not to approach the government.[166] It may have been a coincidence that the ICAEW and the Scottish and Irish institutes were at the time planning to seek government support for limiting professional liability,[167] but it clearly would not have been a good time to put the DTI on the spot over CCA.

At least the withdrawal of SSAP16 would have been a useful means of burying the evidence of the profession's inability to secure the disclosure it still thought important. Yet the CCAB could not bring off even this simple manoeuvre with speed or dignity. Initially, only the ICAEW supported a policy of withdrawal with no further action; the Irish and Scottish institutes wanted some action, though stopping short of a standard, while the remaining members of CCAB wanted a 'one-line' standard or SORP, perhaps modelled on the never-issued ED38. The president of the ACCA, Peter Hobkinson, apparently 'felt particularly strongly on this issue',[168] although he was not known for his passion for CCA. The vice-president in that year was Thomson, who had played a major role in the development of CCA and pioneered the system at Fords.[169]

The ASC nonetheless went ahead and, in April, formally sought CCAB approval for the withdrawal of SSAP16 and a statement of support for the new Handbook. Notwithstanding their previous positions, put on the spot, five of the six CCAB bodies agreed. The ACCA Council followed its officers and declined to fall in with the majority. In August, the ACCA issued a statement calling on the rest of the CCAB to join it in instructing the ASC to develop a new standard.[170] They found no support and, in October, a statement was issued in the names of 'the presidents of five of the leading accountancy bodies',[171] welcoming the publication of the Handbook, calling on companies to report the effects of changing prices where material, and reporting that their bodies had proposed that SSAP16 should be withdrawn. No explanation of the reason why this proposal was not actually being implemented was given, although a politically astute visitor from another planet could have gained a clue by comparing the full list of CCAB members, included in the Handbook because they were the governing bodies of the ASC, with the five bodies named in the withdrawal statement. The ASC did what it was empowered to do on its own initiative and withdrew the guidance notes on SSAP16.[172]

The ASC discussed CCA further at its meetings in November and December 1986 and on the second occasion agreed to revisit the issue in September 1987.[173] In February 1987, the ACCA wrote to the Secretary of the ASC, offering to undertake and fund research into attitudes to price change accounting and stating that if the offer was accepted, it 'would be prepared to withdraw its opposition to the withdrawal of SSAP16'.[174] The ASC's Planning Sub-Committee accepted the offer and the Association commissioned Market and Opinion Research International to conduct the investigation.[175] It was intended

that the results be available in time to inform the September discussion but in the event the survey was not published until November and the ASC's revisitation was postponed until March 1988. The results[176] provided some support for the ACCA's position: for example, at then-current levels of inflation (a little short of 5 per cent), 68 per cent of financial statement users thought it very or fairly important for companies to indicate the effects of increasing prices on their operations. Among preparers, the figure was lower, still reasonably high at 46 per cent, but not a majority. Unfortunately, the results provided little help for a standard-setter deciding what to do about the concern felt: thirty-nine per cent of respondents favoured a mandatory standard while 49 per cent preferred that it be optional.

The Planning Sub-Committee concluded that the MORI survey showed that the target of creating a climate of opinion in which a successor to SSAP16 would be acceptable had not yet been achieved and recommended that the ACCA be asked to consent to the withdrawal of SSAP16. The paper was passed on to the secretariat of the Association so that they could 'forewarn appropriate people of its content'.[177] The March ASC meeting agreed the Planning Sub-Committee's recommendations and, on 15 April, Renshall, now chairman of the ASC, wrote to the president of the ACCA – by a quirk of fate, Thomson – enquiring if the Association would be prepared to support the withdrawal of SSAP16.[178] The reply was short but its contents surely sweet. It came, not from Thomson, but from the Association's secretary, Andrew Sansom. It read, in full, 'I am writing in response to your letter, reference 12-100-18 of 15 April 1988, to my President and to confirm that the Chartered Association's Council has agreed to the withdrawal of SSAP 16 "Current Cost Accounting".'[179] In the same month, SSAP 16, and with it the CCA system, was formally withdrawn – if not forever, at least until the present. The standard's life was certainly, as Hobbes has it, nasty and brutish, but it was not quite as short as it should have been.

An Unhappy Chapter

The struggle to establish a system of price change accounting was long, arduous, convoluted, highly politically charged, ill-tempered at times,[180] and ultimately unsuccessful.[181] The momentum behind the work, such as it was, was destroyed by the fall in inflation, though whether this fatally undermined the profession or, fortuitously, rescued it, depends on one's point of view. Those involved in the technical development of the system faced huge difficulties in squaring ultimately irreconcilable positions: on the methods to be used, the treatment of particular items, universality, prescription, comprehensiveness. The initial decision to produce a comprehensive system, which both multiplied the length and complexity of the documentation and necessitated resolving technical problems unsolved for historical cost accounting, derailed the first exposure draft but may well have facilitated such acceptance as subsequent, simpler, systems in fact achieved. Thereafter, the technical development of CCA was largely submerged

as those seeking solutions were buffeted by one political storm after another. The sheer speed with which severely complex technical issues had to be addressed overwhelmed the structures and resources available to address them and made it difficult for those attempting to manage the project to stand back and take cool political judgements. The rate at which pragmatic technical fixes for challenging problems were 'knocked out' in the CCA workshop should not be overlooked merely because the overall development process became extremely protracted.

Few groups, other than those struggling to solve the technical issues, emerge with much credit from the struggle. Government willed the end, interfered in the process, but denied the means to achieve a resolution, though without any apparent desire to scupper the system or the profession. CCAB politics complicated the technical development and promotion of the system, confounded orderly policy-making, and severely disrupted the retreat. All in all, it was a sorry chapter in the history of the ASC and for most of the individuals involved. Whether it had wider consequences, we will discuss in the final chapter.

Why did the ASC persist in its attempts to design a price change accounting system for as long as it did? Given the government's position, it would clearly have been almost impossible for the profession to abandon the attempt completely until very clear evidence had emerged that there was opposition from preparers to any version that could be devised, and no strong support from potential users, and inflation had been brought largely under control. Combined with this, the issue had become politically sensitive both for the CCAB bodies and for the ASC. The CCAB bodies, especially the ICAEW, after its bruising encounters with Keymer and Haslam, were unwilling to allow the ASC to manage the price change accounting project without interference – although they were equally unwilling, or unable, to lay down a clear policy line, let alone stick to one. For the ASC, price change accounting became bound up with the wider issue of whether it had the capacity to move forward in a controversial area and make the resulting pronouncement stick.[182]

10 Losing Steam? 1985–1990

> The Accounting Standards Committee was set up (as the ASSC) in 1969. Historians may well note critically . . . a visible 'loss of steam' in the 1980s (whether as a result of self-satisfaction or lethargy)
>
> Geoffrey Holmes[1]

During the last five years of its existence, the ASC worked against the backdrop of an increasingly active takeover market triggered by the October 1986 'Big Bang' reform of the Stock Exchange; aggressive earnings management greatly increased and companies invented ever more ingenious, 'financially engineered', schemes designed to achieve misleading results when accounted for using traditional methods. A new branch of business literature emerged, excoriating the extent of these abuses[2] and thereby added to the pressures on the ASC to halt them. Other pressures were the effects of increased competition within auditing and growing calls for international harmonization.[3]

Ian Davison's term of office as chairman ended in mid-1984; the search to find a successor began a few months before then. Jeffery Bowman, who had been a member of the committee since 1982, was approached. He insisted that he would accept only if the Consultative Committee of Accountancy Bodies adopted the original recommendation of the Watts report that a full-time, senior-ranking Director of Accounting Standards be appointed.[4] In June 1981, Christopher Morgan had been seconded for three years to a job that combined this post with the technical directorship of the Institute of Chartered Accountants in England and Wales but the appointment proved controversial with other CCAB bodies.[5] Although relationships warmed somewhat as time passed, Davison's appointment as chairman had a major impact on the job Morgan found himself doing.[6] Davison interpreted his role as chairman to include the management of standard-setting strategy, and he received technical support in this role from his own firm.[7] In the light of these changes, Morgan decided to end his secondment early and returned to his firm towards the end of 1982.[8] On his departure, the combined role was not retained. The CCAB refused to accede to Bowman's conditions.[9] Fortunately, by the time the news of Bowman's refusal leaked to the press,[10] another approach, to Peter Godfrey, member of the committee since 1983, had been successful.

Godfrey was born in 1924 and served in the army before completing his training with a small City firm. He joined Ernst & Whinney on qualifying in 1949 and became a partner in 1959, deputy senior partner in 1978 and senior partner in 1980.[11] His appointment was regarded as marking a change in style, from what *Accountancy Age* described as Davison's 'autocratic' and 'abrasive' manner[12] to a more 'conciliatory approach': 'I do not see myself as the super-technician . . . I am more a chairman who will persuade, both within the committee and within the business community.'[13] He estimated that he would be spending about a quarter of his time on the chairmanship,[14] a considerable burden for someone who was also a senior partner.

Meanwhile the annual round to find new members had abandoned the nominating committee structure, introduced by Davison to neutralize CCAB politics and secure the highest quality membership.[15] A 'special meeting' of CCAB presidents took place (on a Saturday morning) to discuss the role and budget of the ASC; according to the press, the intention was to 'curb the power of the ASC[,] . . . downgrade [its] standing and, if possible, limit its role to simply issuing standards while passing the job of issuing non-mandatory guidance back to the individual accounting bodies'.[16] In the event the suggested limitation in powers came to nothing; the CCAB's budgetary wrangles have already been described.[17]

In September 1986, Michael Renshall[18] took over as chairman from Godfrey, who retired both from the ASC and from Ernst & Whinney.[19] *Accountancy* pointed out that Renshall arrived just as the ASC was 'shelving . . . the once seemingly interminable current cost accounting debate'.[20] Listing the controversial topics he would have to deal with, the journal speculated that by the time his term of office ended, he might be pining for the days of inflation accounting.

In July 1985, Godfrey had written to the chairman of the CCAB (the ICAEW's president), arguing that, with the demise of SSAP16, the time was right for the CCAB to return to the issue of monitoring and compliance with accounting standards generally.[21] The CCAB chairman's reply reminded Godfrey that 'enforcement is, of course, essentially a matter for individual member bodies of CCAB', but conceded that he could 'see benefit in a discussion of the issues within CCAB'.[22] He suggested that they return to the question 'after the holiday period'. Later in 1985, members of the ICAEW Technical Directorate conducted a pilot study to test the feasibility of monitoring published financial statements against a checklist of requirements, concluding that such monitoring was feasible. The results 'did not reveal any significant problem of non-compliance with standards by listed companies' but found 'evidence to suggest that there could be widespread and serious non-compliance by smaller companies'.[23] The report conceded that looking only at the published statements would not necessarily identify all cases of non-compliance.

A meeting between the ASC and ICAEW technical staff held in September 1985 established that, as far as the ICAEW was concerned,

> the Professional Standards Committee saw its role as being to help and advise. It acted on complaints and its brief was not to look for trouble, although it monitored the professional and financial press . . . the PSC can only persuade – it has no powers to do anything as such.[24]

This despite the ICAEW president's view that enforcement was a matter for individual CCAB member bodies.

When Renshall took over the chairmanship he continued to pursue the issue and it was discussed by the CCAB in November 1986.[25] The President of the Institute of Chartered Accountants of Scotland reported that his institute strongly 'supported the introduction of monitoring and looked to the CCAB to make a declaration of principle'. The other five bodies prevaricated: the ICAEW could not take a position until the outcome of current consultations with members about self-regulation generally was known; the Institute of Chartered Accountants in Ireland thought that more work should be done on the possible shape of the machinery before a decision was reached; and the Institute of Cost and Management Accountants was concerned about innocent finance directors overwhelmed by non-accountants on the board. The Chartered Association of Certified Accountants had not one but four concerns:[26] that some instances of non-compliance might be overlooked and then emerge later, so that 'the entire profession would be accused of incompetence or worse'; that some instances successfully identified would be trivial but the bodies would not be able to ignore them for fear of being 'accused of complacency, or protecting their own by taking no punitive action'; that the bodies would inevitably lean towards harshness, so that 'injustice would be the likely result'; and the cost of the exercise. An ASC file note records that 'the ICAS are fairly exasperated by the other bodies' position, which they take to be that monitoring will never happen.'[27]

In December, the ASC discussed the issue and Jeffrey Knight, chief executive of the Stock Exchange and a member of the ASC, reiterated that the Exchange 'remained sympathetic in principle to the idea of establishing a joint panel',[28] as originally negotiated by Tom Watts.[29] In February 1987 a paper setting out detailed proposals for the panel was circulated under the name of the chairman of the ASC.[30] As the ICAS feared, nothing came of it.

Renshall's appointment became a case of the wheel turning full circle – and then stopping. In November 1987, the CCAB appointed a Review Committee with an external chairman, Sir Ron Dearing, to examine standard-setting in the UK. Less than a year later, in September 1988, it reported, recommending a new, independent standard-setting structure.[31] Only a further six months was required for the CCAB to reach the stage of accepting substantially all the report's recommendations.[32] The new machinery took over from the ASC on 1 August 1990. Thus, for the second half of the period described in this chapter, the members of the ASC were aware, with increasing certainty, that the life of the committee was coming to an end; this knowledge, as we shall see, almost certainly affected their attitude towards their role.

Pension Costs

Accounting for pension costs featured in the ASC's initial five-year work programme, was dropped from the technical agenda shortly afterwards, and reappeared before the initial five-year period had elapsed.[33] Sir Ronald Leach, addressing an audience of chartered accountants in November 1975, emphasized the importance of the subject and indicated that he would like to see a standard emerging soon.[34] Presciently, however, he added that 'it is obviously going to be a difficult one.'

Pension costs had been covered by a Recommendation on Accounting Principles, issued in February 1960,[35] which made clear that 'the full extent of an employer's contractual obligations for payment of retirement benefits to employees needs to be reflected in the employer's accounts'[36] and emphasized that recognizing only payments made to insurers or into a separate scheme was unacceptable. In the mid-1970s, most companies made few disclosures about their pension arrangements, so that little was known about the accounting methods used.[37] What was known suggested that accounting methods were inconsistent and, in some cases, severely deficient.

Many UK pension schemes were defined benefit schemes, under which the employer makes a commitment to pay pensions based on conditions yet to crystallize, such as the employee's final salary and her or his length of service; the risk that past funding may be insufficient to support payments at this level is borne by the company. It is these schemes that present most accounting difficulties. It is possible for the company to account on a 'pay-as-you-go' basis, because no cash flows are required until pensions fall payable, though such an approach is clearly contrary to the matching concept, no matter how widely stretched. For a variety of reasons, including the tax advantages available, most UK schemes were funded by contributions paid in advance of the need to cover pension payments. Funding methods included initial funding, under which the year's payment was intended to cover pensions for staff taken on in the year, and terminal funding, under which the payment covered pensions for staff retiring in the year. Neither of these would reflect the cost of pensions to be paid in respect of work done during the year in question, but it seems likely that they were being used by some companies to recognize costs in the financial statements.[38] Further, pay-as-you-go arrangements were more common elsewhere, for example in much of the rest of Europe[39] and it seems likely that some UK groups were reporting these schemes as recognized in the subsidiaries' statement in the consolidated accounts.[40]

Most UK schemes were funded using 'actuarial' methods designed to calculate systematic annual contributions over an employee's working life that would, together with investment income, cover the ultimate cost of her or his pension. There was a substantial number of such methods,[41] the most common in the UK, the 'aggregate cost' method, being designed to keep contributions level, as a percentage, in the medium term.[42] Once a method has been selected, payments depend on benefits offered, the number and age profile of current staff

and pensioners, assumptions (to be made by the actuary) about life expectancy, staff leaving before retirement, changes in benefits and the characteristics of the workforce, rates of investment income, and future pay rises. Although all actuarial methods spread the cost of the pension promise over the working life of the employee, and thus correspond in some broad way to the matching concept, they can produce significantly different figures for the same workforce and actuarial assumptions. Further, the assumptions made in the actuarial calculations will inevitably turn out to be wrong. As a result, the fund will be larger or smaller than now needed. This difference is referred to as an 'experience surplus or deficiency'. Based on past experience, or for other reasons, the actuary may also need to change the assumptions made in respect of future periods. The employer may decide to improve the value of benefits offered to employees or current pensioners, or to change conditions of membership, and to make these changes retrospective (producing 'back service costs').

The urgency of ensuring appropriate treatment of pension costs was increasing during the 1960s and 1970s because of quite dramatic changes in the provision of pensions in the UK. Partly because of government encouragement, the proportion of the working population covered by occupational pensions schemes increased significantly after the second world war.[43] Arrangements were moving very rapidly towards 'final salary' schemes, promising a pension based on earnings at or near retirement: between 1963 and 1971, the proportion of such schemes in the profit-seeking sector rose from 13 per cent to nearly 50 per cent.

Less than a year after Leach had expressed the hope that a standard would emerge rapidly, the ICAEW published a working paper on the subject produced by staff at Unilever.[44] This recommended that the accounting measure should be based on an 'estimate of the continuing cost to the company of operating its pension scheme',[45] effectively allowing most actuarial methods used for funding to be used also for recognition in the financial statements: thus recognition could correspond to cash payments into the scheme. Back service costs, experience surpluses and deficiencies, and the effect of changes in actuarial assumptions would be spread forward over the average expected working life of current employees, the period over which, according to the report, 'the liabilities will emerge.'[46] Although the report conceded that there were arguments for charging back service costs, the effects of changed actuarial assumptions and experience deficiencies immediately on the grounds of prudence and, in the case of experience deficiencies, also on the grounds that they are straightforward misestimates of past costs, it argued that 'prudence must be given a somewhat different interpretation in the context of the very long-term estimates associated with pension costs.'[47] Back service costs arose from the employer's decision to seek to buy a future commitment from its staff which would benefit future periods. The potentially quite wide range of methods and assumptions to be allowed would result in significant differences in the resulting figures, a problem which would be addressed by requiring consistency of approach through time and demanding extensive disclosure.

On publication of the working paper in November 1976, the ASC announced that it would form the input for a draft accounting standard.[48] Nine months later, such a draft, following the lines of the working paper, was circulated to the technical committees.[49] After a further nine months, the CCAB made a submission to a long-term inquiry being undertaken by the Occupational Pensions Board[50] in which it emphasized its belief that better disclosure of pension commitments was required in UK accounts and reported that an exposure draft would be ready later in the year (i.e. in 1978). It urged the government not to act precipitately.

In July 1978, a further draft was despatched to technical committees.[51] The delay in publishing an exposure draft was attributed to the launching of the Auditing Standards Committee and the pressure of dealing with price change accounting. Members of the working party expressed anger that the draft in circulation contained significant changes from the version they had approved. Its broad structure, however, still reflected the recommendations of the Unilever report.[52]

In November, the ASC itself devoted most of its meeting to considering a draft.[53] The principal objections came from an ACCA representative, Alan Nelson, although the ACCA itself conceded that none of its four points was 'earth shattering'.[54] Publication was due in February 1979.[55] In February the ASC was actually considering another draft. Pension costs were still required to be spread, the draft requiring that 'a reasonably stable future pension cost relative to future pensionable payroll' be achieved.[56] Now the ICAS was reported to be unhappy with the disclosure requirements.[57] Further, there was difficulty with the treatment of lump sum payments to the scheme, for example to cover experience deficiencies or back service costs. It had been proposed that these should be written off – *Accountants Weekly* suggested that this might have been in response to the consideration that such write-offs would be allowable as deductions from profit in data given to the Price Commission to justify price increases under counter-inflation regulations.[58] The ICMA and others had opposed this treatment and February's draft merely emphasized the difference between funding and accounting, implying that the amounts should be spread forward.[59] This was unacceptable to some members of the committee and the February debate was inconclusive.[60] It was announced that further consideration of the topic would now be postponed until after the latest price change proposals had been agreed.[61]

In May 1979, the ASC considered another draft (allowing lump sum payments to be written off) and it was agreed that this should go to a ballot.[62] The ballot was inconclusive and, in November, the ASC announced that it had abandoned the attempt to arrive at detailed rules after discussion at five meetings of the committee, and would propose instead a more flexible approach, combined with extensive disclosure.[63] This draft, too, fell. Although the technical problems of pension accounting are undoubtedly complex – 'the field . . . attracts complications like a magnet attracts iron filings', was how Watts put it[64] – and some are controversial, the ASC's difficulties at this stage were caused

in part not by complexity and controversy as such but by the consequences of these factors for the dynamics of the committee. Attendance at the meetings could be poor and, 'with a membership of about 20, and six or seven absent, then you get a six/eight split one month and then eight/six at the following meeting.'[65]

Further, the members of the committee were not pension specialists. Graham Ward, at the time Tom Watts' personal assistant on ASC affairs, recalls an attempt to focus minds:

> It was something of a challenge to get the members of the committee to get their thoughts around this one. It was a real task to get it accepted that you should take a longer look. We got Allan Cook who was then working in the pensions division of Unilever to help us. We put together what Tom described as a test paper; it wasn't quite a test paper but it was a series of questions to assist the committee in forming their views – I think I did the theoretical section and Allan did the practical section and we sent it round to all the members of the committee. [Then] we came to the session of the committee where the results were to be announced and Tom said, 'well gentlemen, I've had your test papers in and I've had Harold Edey moderate the marking and I'm sorry to say that you've all failed. The good news is that at least you were honest and filled them in yourselves.' This was preliminary work to get people thinking. So Tom said, 'I suggest we move on to something more straightforward.' The next item on the agenda was CCA.[66]

In 1981 the pressure for the development of a standard increased, mainly as a result of new companies legislation implementing the Fourth Directive and requiring disclosure of pension commitments.[67] The absence of professional guidance on the subject was referred to in a parliamentary debate on the legislation, the Labour opposition threatening to establish regulatory machinery to improve the standard-setting process.[68] In addition, the International Accounting Standards Committee was now working on the subject.[69] A new working party was established, under the leadership of Jeffrey Pearcy, of ICI.[70] It was reported that it would draw on research commissioned by the ASC from Christopher Napier, an academic at the London School of Economics and Political Science.[71]

An interim report from Napier was published in February 1982.[72] It was described in the press as taking 'the revolutionary view that the cash paid each year to provide the funding is different from the actual costs',[73] although, of course, this point had been made in the 1960 Recommendation and the Unilever report of 1975 and underlay all the draft EDs considered by the ASC since then. The publication of the report enabled the ASC to solicit views on the proposals without identifying its own position. The report gave Napier as author and invited respondents to send their submission to him by name, albeit care of the ASC. The report did not nominate a particular method for reporting normal cost, contenting itself with ruling out methods that fail to allocate charges over the

working life of the employee (such as pay-as-you-go) or ignore future pay increases (discontinuance methods). It implied that abnormal costs should be spread forward and recommended a range of disclosures. Its overall approach was very similar to that taken by the Unilever report.

By the middle of 1982, the IASC had adopted a standard on pension costs, requiring recognition on the basis of an actuarial computation, adding to the pressure in the UK to adopt a standard.[74] 1983 saw the publication of the final version of Napier's study.[75] It followed the interim study in allowing any actuarial method that took into account future pay increases and sought to ensure that 'the amounts to be contributed accrue systematically over each employee's working life'.[76] Experience deficiencies, however, were to be provided for as they arose, as corrections of routine estimates and not extraordinary items or prior year adjustments. Back service costs were to be spread forward. Fund surpluses were not to be taken into the employer's financial statements unless the intention was to reduce contributions below the level of the actuarial computation in the short term.[77]

Also in 1983, the ASC announced its intention of dealing with pension accounting in stages; there would first be a pronouncement addressing only disclosure but this would be followed by one dealing with treatment.[78] The first exposure draft, ED32 'Disclosure of Pension Information in Company Accounts', was issued in May 1983. It created little controversy, although some commentators were disappointed at how little it advanced beyond legal requirements. There were also suggestions that it should be issued as a (non-mandatory) SORP rather than an SSAP.[79]

In early 1984 Pearcy's working party was finalizing a Statement of Intent setting out how the ASC proposed to deal with the second stage. There was little new. The 'accounting objective' was to charge the cost of pensions 'on a systematic basis over the employees' working lives', on a basis that would 'produce a substantially level percentage of the current and expected future pensionable payroll'; any actuarial method achieving this objective would be acceptable. Variations from normal cost would be 'spread over the period during which the benefit . . . is prudently expected to arise – not exceeding the employees' average working lives'. The emphasis was on the income statement charge, with the balance sheet liability reflecting unfunded costs.[80] The SOI was reported in March to be likely to be agreed by the ASC in April, with an exposure draft emerging during the autumn. It was hoped that the measurement phase would thus catch up with disclosure to form a single standard.[81]

Meanwhile the Financial Accounting Standards Board was developing its own exposure draft. The FASB's preliminary views, exposed for public comment, amounted to 'a radical change in thinking' from the previous US pronouncement, which allowed considerable latitude;[82] the actuarial obligation, measuring the extent to which accumulated promises had yet to be funded, would be recognized as a liability on the employer's balance sheet. Only one actuarial method of measuring the pension liability, the projected unit credit method, would be permitted. This method is one of a class of 'accrued expectations

liability' methods which Napier had come close to suggesting represented the ideal cost measurement basis.[83] According to one actuary,

> Projected unit credit funding aims to have enough money in the fund at any time to provide the benefits based on service to date and salaries projected to the employees' retirement date. In other words, if no further contributions were paid into the scheme and future service earned no pension rights, there would be enough money to pay employees accrued pensions based on their expected salary at retirement. It is widely agreed that . . . projected unit credit is the theoretically correct accounting measure.[84]

Accrued expectations liability methods were unpopular in the UK because they do not necessarily produce a level profile of funding requirements.[85]

Whether or not one actuarial profile is a reasonable approximation to another will depend, in part, on the characteristics of the population for which pensions are being provided. Studies of this question are rare but Napier quotes one, using realistic data, which produced initial rates for contributions (or costs, if used for accounting purposes) of 14.4 per cent for the projected unit credit method and 16.5 per cent for the aggregate method. The discontinuance target method, another popular UK approach, resulted in a rate of 10.1 per cent.[86] It is sometimes suggested that differences between measurements do not greatly matter because pension provision takes place over the long term and 'the company will be given plenty of time to build up the necessary provision without having to suffer dramatic fluctuations in year-by-year costs.'[87] Of course, for many companies the purchase of, say, fuel, takes place over the long term but accountants do not customarily allow the company to select its own profile for recognizing the relevant costs. Further, material differences between the value of funds and the employer's pension obligations can be significant in the short term, for example during the course of takeovers. A bidder may be aware that a company's pension scheme is overfunded; if existing shareholders are unaware of this 'hidden' asset, because it is not recognized in their company's accounts, they make accept a lower price.

The SOI promised for April was eventually approved in September.[88] It was given the slightly curious status of a *consultative* statement of intent. It followed the draft previously leaked in March.[89] Disclosure requirements were carried over from ED32, which the SOI indicated would not now be adopted as a separate standard. Responses focused on arguments for exempting overseas subsidiaries and small companies; the burden of the disclosure requirement, especially where large numbers of separate schemes were involved; and the treatment of ex gratia payments.[90]

Until the early 1980s, much of the debate about pension accounting had addressed the problem of coping with scheme deficiencies. By the mid-1980s, however, the position had reversed, largely as a result of unexpectedly high investment returns and significant levels of redundancy, and many companies had large surpluses. Indeed, it was estimated that UK companies had surpluses

amounting to £50 billion, 30 per cent of their schemes' assets.[91] One argument against including a fund surplus as an asset in the employer's accounts was that it was in practice unlikely that the employer would benefit from that surplus, which would remain in the fund and be used either to pay improved benefits or offset subsequent shortfalls in contributions. However, companies with surpluses were in practice taking 'contributions holidays', that is ceasing to make further contributions over a period, thereby, in effect, receiving a benefit by running down the scheme surplus,[92] somewhat undermining this argument. In December 1985, it was announced that the Inland Revenue had agreed that Redfearn National Glass could obtain a refund from its scheme on the grounds that it was so overfunded that even a five-year contributions holiday would not eliminate the surplus.[93]

In December 1985, the FASB adopted FAS 87 'Employers' Accounting for Pensions'.[94] It permitted an averaging method in the income statement to dampen fluctuations arising from changes in the fair values of scheme assets and reduced disclosure requirements by comparison with the ED. However cost measurement remained based on the projected unit credit method.[95]

ED39 'Accounting for Pension Costs' finally appeared in May 1986. It followed the SOI on major issues while tightening up a number of areas.[96] After a further two years, in May 1988, SSAP24 'Accounting for Pension Costs' was finally adopted.[97] It largely followed the ED, the SOI, the recommendations of Napier and, indeed, those of the Unilever report issued more than 12 years before. A year after its publication, Ward, by then a partner in Price Waterhouse, contributed an article to *Accountancy* headlined, 'When is a Standard not a Standard?' to which he gave the answer, 'when it's SSAP24.'[98] The reason was that companies were exploiting some of the fine detail in the drafting to, in Ward's view, abuse the standard:

> an employee's regular pension cost should be a substantially level percentage of his pensionable pay during his expected service with the company ... However, the use of employees', rather than employee's, in paragraph 77 [of the standard] and the use of the words 'in the scheme' in paragraph 79 have led some to follow [an] approach where the aim is to keep the cost of the scheme itself as a substantially level percentage of expected future payroll. Account is taken of expected changes to the scheme such as new entrants and changes in the members' contributions in respect of those new entrants. This leads to a current year cost based on current and expected future circumstances and in practice to recognising the benefits of reducing average age of scheme members now rather than when the reduction happens. In my view, this takes pension cost away from measuring the costs of employees which the company has this year to measuring the average costs of the employees which it has this year and might have in the future ... The differences can be material: indeed, according to circumstances, more than 100 per cent[.]

Desmond Wright, who took over as secretary of the ASC between ED39 and SSAP24, puts it like this: 'SSAP24 was not the greatest standard ever written ...

We knew there were flaws in the standard but we didn't feel terribly defensive about it. We just wanted to get it out there and move on.'[99] Professor Christopher Nobes, who became a member of the ASC between ED39 and SSAP24 is less kind:

> I don't think I really understood SSAP24 at the time. I now realise why: it cannot be understood – it's basically mumbo jumbo. People were talking as though it made sense and they understood it, and when one has recently arrived on a committee . . . one feels a little nervous about saying, 'hang on a minute, none of this makes any sense.' SSAP24 is a remarkably strange document. For example, there is not a single sentence telling you how to choose the numbers to put on the balance sheet.[100]

Off-Balance Sheet Finance

Margaret Thatcher may have rid the ASC of its most troublesome project from the early 1980s – by eliminating inflation – but her deregulatory zeal contributed to its most troublesome project of the late 1980s, by freeing up the banking sector to lend in newer and ever more ingenious ways. That problem became known as 'off-balance sheet finance'. This is easy to define: 'The funding or refinancing of a company's operations in such a way that, under legal requirements and existing accounting conventions, some or all of the finance may not be shown on its balance sheet.'[101] But it is much more difficult definitively to identify *incorrectly treated* off-balance sheet finance, that is, off-balance sheet finance that ought to be on-balance sheet.[102]

Increasingly aggressive management of financial institutions, and increasingly aggressive financial engineering by companies, combined to produce a huge increase in the use of off-balance sheet finance in the late 1980s.[103] Two, relatively straightforward, examples are sale and repurchase agreements, widely known as a 'repos', and so-called 'grey leases'. A repo would suit a manufacturer, such as a whisky distiller,[104] obliged to hold stock for substantial periods before sale but needing to pay staff and purchase raw materials in the meantime. A finance house would purchase the stock at an early stage, settling in cash, but grant the distiller an option to repurchase it, at a price fixed in advance, close to maturity. The price for the repurchase would be fixed to cover the original sales proceeds plus appropriate interest. The distiller is unlikely to fail to exercise its option, given the profit available on the subsequent sale of the matured whisky through normal trade channels. The transaction has the character of a loan, repayable with accumulated interest, but was being accounted for as a sale followed by the separate purchase of the matured whisky.

In chapter 8, we left accounting for leases at the point at which substance had apparently triumphed over form.[105] The standard defined finance leases as follows:

> A finance lease is a lease that transfers substantially all the risks and rewards of ownership of an asset to the lessee. It should be presumed that such a transfer of risks and rewards occurs if at the inception of a lease the present value of the minimum lease payments, including any initial payment, amounts to substantially all (normally 90 per cent or more) of the fair value of the leased asset.[106]

At the time, the 90 per cent test seemed appropriate: financial institutions were deeply reluctant to take on any residual risk on a lease and there was clear water between the full payout leases they wrote and short-term hiring agreements.[107] However, during the 1980s, companies looking for off-balance sheet financing were keen to enter into leases written to fall just below the 90 per cent limit, and financial institutions became increasingly sophisticated in the products they were prepared to offer.[108]

In July 1987, just as the mandatory application of SSAP21 was taking effect, the ICAEW issued a Technical Release[109] reminding preparers that SSAP 21 'does not . . . provide a strict mathematical definition of a finance lease. Such a narrow interpretation would be contrary to the spirit of SSAP21 and SSAPs generally.'[110] But it was too late – the genie was out of the bottle[111] and the grey lease had been invented.

Motives for employing off-balance sheet finance were varied and complex but included misleading users of the financial statements, for example by reporting lower gearing or higher profits in early years; signalling management's intentions, for example signalling the intention to reduce gearing in future by taking it off the balance sheet now; improving borrowing power, for example where it is limited by an agreement expressed in terms of financial statement gearing; risk-sharing with the financial institution involved; manipulating reported income for legal or tax purposes, which might, of course, be in the shareholders' interest; and manipulating reported income for the benefit of management, for example in the case of a profit-related bonus scheme.[112]

Concern first surfaced in the UK from the Bank of England and from the viewpoint of banking regulation and the risks being taken on by financial institutions,[113] rather than among financial statement users. It did not, however, take long for alarm to become more widespread, and, as often happens, a corporate failure served to focus attention on the problem. The 1984 financial statements of Burnett and Hallamshire Holdings disclosed a number of contingent liabilities but concluded that no material loss would ensue should any of the contingencies arise. However,

> The true nature of some of these contingent liabilities was revealed . . . when the company almost collapsed and a rescue package was put together. One commentator noted that the company's overall borrowings at 31 March 1984 were £154 million, of which £83 million were off balance sheet.[114]

The rapidity with which the Bank of England was expecting a pronouncement to be developed was inconsistent with the timetable required by the ASC's due process and it was agreed that the ICAEW Technical Committee would produce initial guidance in the form of a Technical Release. The ASC was less than happy about the ICAEW encroaching into its field, but recognized the need to respond on something like the timescale the Bank was demanding. In any event, the problem was at the time (early 1985) perceived within the ASC to be much smaller in scale than later became apparent.[115] A working party, chaired by Ken Wild, a partner in Touche Ross, was established and, in December 1985, only six months or so after work began, the ICAEW Technical Committee issued TR603 'Off-balance Sheet Finance and Window Dressing'.[116] The content reflected the speed with which it was produced. The release calls on the ASC to provide guidance and, in the meantime, argues that 'in financial statements which are intended to give a true and fair view the economic substance of [potentially off-balance sheet] transactions should be considered rather than their mere legal form when determining their true nature and thus the appropriate accounting treatment.'[117] It triggered a response from the Law Society, condemning the 'wish expressed by the Release to substitute substance for form' as 'dangerous and undesirable',[118] on the grounds that it would replace the certainty and objectivity of legal form with uncertainty and subjectivity, and that it was illegal.[119]

In February 1987, the 1986 volume of the ICAEW annual survey was published. It contained a chapter, written by Price Waterhouse partner Ian Brindle, on off-balance sheet finance, listing a variety of types of scheme and giving examples of each type drawn from well-known companies.[120] Its contents, and particularly its conclusion that 'the ASC remains silent on the matter; meanwhile billions of pounds are being invested in off-balance sheet schemes',[121] were widely reported.[122] Fortunately, an ASC working party, led by Allan Cook, had been developing an exposure draft and Renshall was able to respond in rather Churchillian terms: 'we shall not remain silent for long.'[123]

The working party had originally been established to review SSAP2[124] and it was at first thought that it would be possible to deal with off-balance sheet finance as part of the review by invoking substance over form as a fundamental accounting concept.[125] The working party proposed some 'general principles', which the ASC, in March 1987, asked it to work up into an exposure draft. These included:

(a) The need to account for transactions and arrangements in accordance with their substance is central to the concept of 'true and fair' . . .
(b) In order to account for transactions and arrangements in accordance with their substance, it is necessary to ensure that their accounting effect is consistent with their economic effect, in particular:
(i) the transaction's or arrangement's effect on the company's rights to the use or enjoyment of an asset; and
(ii) the transaction's or arrangement's effect on the liabilities of the company.
(c) All entities which are effectively controlled by the reporting company should be consolidated in its consolidated accounts.[126]

In April, the ASC announced that an exposure draft would be 'prepared by June' with a standard 'being ready by early next year.'[127] Within a week, *Accountancy Age* was reporting threats that companies following the proposed line would be taken to court by solicitors as test cases.[128] It was suggested that the motivation behind the Law Society's memorandum was tactical:

> The treasurer of a top plc said: 'The counsel and solicitors I've spoken to say they were caught by surprise over leasing and now they probably couldn't win in the courts. But on this one they have been forewarned and they won't let it go without a fight.'[129]

After another week, a partner in a 'top City firm' was suggesting that auditors who qualified financial statements on the grounds that they did not consolidate controlled non-subsidiaries, a form of off-balance sheet finance,[130] could find themselves being sued by their clients for defamation.[131] In fact, it was by then known that a new approach to defining subsidiaries was to be embodied in UK law by the Seventh Directive, with the effect that, at least in many cases, the ASC's approach and the law would coincide; however, this was not expected to occur for another eighteen months or so.[132]

A major problem for the ASC's proposed approach was the absence of any authoritatively-agreed definitions of assets and liabilities in the UK, all pursuit of the 'holy grail' of a conceptual framework having been abandoned.[133] In June, Renshall revealed that the ASC's latest thinking was to employ the definitions adopted by the FASB, in its Statements of Financial Accounting Concepts, in 1980.[134] At this stage, the UK draft was, indeed, entitled 'Assets and Liabilities'.[135] According to the US definition, 'assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events',[136] and there is a symmetrically opposite definition of liabilities. It was accepted that such an approach would place a considerable burden on auditors and methods of coping with this were being examined, including, apparently, a 'hotline' to the ICAEW.[137] By now, the ED was due in early September, with a standard to be fully in force within a year.[138]

Towards the end of July 1987 some more 'latest thinking' was revealed.[139] Corporate annual reports would include two sets of financial statements, one in accordance with current rules and one including all assets and liabilities, as defined. Both sets would be essential for a true and fair view. The definitions of assets and liabilities were to be 'improved'. The fourth draft was now being further redrafted. The ASC staff member in charge of the drafting was described as 'soon to depart' and as feeling that the published timetable was 'naive'.[140]

In fact the July meeting of the ASC called for a radical rethink in the face of the lawyers' objections to the two major planks of the proposals, consolidation of controlled non-subsidiaries and an economic definition of assets and liabilities. Initially the Department of Trade and Industry had accepted that assets and liabilities could be defined differently for accounting and legal purposes but, having consulted its own lawyers, it was now taking a different view.[141] In

October, it was revealed that the latest proposals had been sent for counsel's opinion, which was not expected until November, after which the DTI and the legal profession would be consulted again, making it unlikely that an ED would surface until the new year.[142] In November, the DTI confirmed its intention to implement the Seventh Directive in a way that would support the consolidation of controlled non-subsidiaries, aiding the ASC in moving forward on that front.[143] That month's ASC meeting heard that counsel's opinion had been favourable.[144] It was presented with a new draft, substantially rewritten to simplify the arguments.

ED42 finally appeared in March 1988. Its title was now, 'Accounting for Special Purpose Transactions', and was derided in the press as euphemistic.[145] The use of the term 'special purpose' to mean something like 'unscrupulous purpose' (what would a *general purpose* business transaction actually look like?) was introduced from the USA, where the Emerging Issues Task Force had referred to special-purpose borrowing and special-purpose entities in pronouncements issued in 1984.[146] Mealy-mouthed as the term may be, the ASC's difficulty in naming the class of transactions it was seeking to regulate is obvious: if the ASC was successful, much off-balance sheet finance would come onto the balance sheet.

The argument in the exposure draft may have been expressed more simply than in previous versions but it remained somewhat gnomic in places; it is open to doubt whether an otherwise well-informed accountant, unaware of the problem it was designed to solve, would actually grasp its intention. The definitions section contained no definition of assets or liabilities, though the 'characteristics' of an asset and of a liability are discussed at length in the explanatory section. There is a definition of a special purpose transaction, namely,

> one which combines or divides up the benefits and obligations flowing from it in such a way that they fall to be accounted for differently or in different periods depending on whether the elements are taken step by step or whether the transaction is viewed as a whole.[147]

There is no explanation of why, say, a household's purchase of a pint of milk from the milk van, to be paid for at the end of the week, is not a special purpose transaction, on the grounds that if its two elements are viewed separately they become a gift of milk *from* the dairy on the day of delivery and a cash grant *to* the dairy on Saturday.

Any obscurity in the definition of the term in the title of the pronouncement was of limited importance because the standard proper is devoted mainly to identifying the substance of 'a transaction',[148] by implication any transaction, and accounting for the ensuing assets and liabilities. Special purpose transactions are referred to only in terms of additional disclosure. The focus on special purpose transactions – such focus as there was – was adopted to emphasize that these would be no change in the accounting for 'normal' transactions.[149] Four pages of the explanatory section were devoted to exploring 'applications of the

characteristics of assets and liabilities' to specific cases, including factoring, repurchase schemes, leaseback, goods on consignment, securitized receivables and sub-participations.[150]

The number of responses to ED42 was, perhaps surprisingly in view of the importance and controversial nature of the topic, rather small: there were 56 submissions in total, only 13 from companies. The draft was not well received. Many responses managed to combine a welcome for the conceptual approach of the document with a call for more detail and prescription.[151]

Towards the end of the year the results of a study commissioned by the ICAEW into a conceptual framework for financial reporting became available.[152] This was undertaken by Professor David Solomons, a British academic long resident in the USA, who had contributed to the FASB conceptual project. Renshall told *Accountancy Age* that his experience of wrestling with the problems of off-balance sheet finance had turned him from a cynic about the value of conceptual frameworks to something of an enthusiast for a more philosophical approach: 'the problems are not as simple as 20 years ago.'[153] The Solomons report took an approach to the definition of assets and liabilities very like that of the FASB, and thus of ED42. It had no authoritative status but served to move the UK profession a little nearer to the idea of deriving rules from concepts. A further, and even more useful, step was taken in April 1989, when the ASC agreed to embrace the IASC's new framework (whose definitions of assets and liabilities were also very similar to the FASB's) as a benchmark against which to 'test' new standards as they were developed.[154]

The March 1989 meeting of the ASC considered the working party's comments on the submissions on ED42.[155] The working party stressed that it did not feel that it was its job to develop a conceptual framework, which, of course, made it difficult to respond to commentators' requests for more guidance in areas such as recognition criteria. It did, however, recommend that it should develop a set of detailed notes to illustrate the application of the principles and this was agreed by the ASC, which proposed that these notes should have the status of standard practice rather than the guidance notes issued with, for example, the leasing standard. The focus on special purpose transactions, having served its purpose of avoiding frightening the horses, was to be dropped in favour of the substance of assets and liabilities. A new draft was expected in the autumn.[156]

As usual, the predicted timetable proved optimistic. ED42's successor, ED49 'Reflecting the Substance of Transactions in Assets and Liabilities' appeared in May 1990, in the closing months of the ASC's existence. There were detailed application notes, running to some 27 pages – more than half the length of the document – which the Preface explained should be regarded as standard practice,[157] a status achieved by their inclusion in the standard section as specific recognition tests.[158] The under-secretary for the project described the draft as making, 'certain refinements to the conceptual discussions' which the ASC did not think warranted re-exposure in themselves; the new draft had been issued to obtain comment on the application notes.[159] While the import of the pronouncement

did indeed change very little, its content and structure were certainly different from its predecessor; there were now definitions of assets and liabilities (referred to, rather curiously, as definitions of 'the essential characteristics' of assets and liabilities); there were general recognition criteria in the standard section (following the IASC's); there was a definition of control to help in identifying what were now called quasi-subsidiaries; references to special purpose transactions were dropped; the rather arch explication of 'form through substance' was abandoned.[160] In short, the availability of a conceptual framework with at least some credibility enabled the pronouncement to be developed with a much clearer and more logically-structured approach.

Debates at the ASC as ED49 moved towards completion apparently reflected a mood liberated by the knowledge that responsibility for nurturing the document would soon be passed on to others in a better position to adopt it as a standard because of the expected arrangements under the new regime.[161] It remained a highly controversial document, not just with the lawyers but among some members of the committee, particularly the preparers. The majority of the ASC, though, thought that the approach was the right one and, fortified by the knowledge that they would be out of the way by the time the flak came over, so they voted.

When the ASC's successor issued a further exposure draft on the topic in February 1993, it 'carried through the general principles set out in ED49 with only two major changes'[162] and the resulting standard was arguably the UK's most distinctive contribution to world-wide standard-setting.[163] The detailed application notes survived: there were further refinements to the conceptual discussion and the concept of the 'reasonable accounting analogy', employed in ED42 and retained in ED49, was abandoned.[164]

Group Accounting and Intangibles

Towards the end of its life, the ASC returned to a number of the topics related to group accounting with which it had had difficulty over the years – Renshall felt 'a terrible sense of *déjà vu*'[165] – and produced documents at a prolific rate.

SSAP22 'Accounting for Goodwill', issued in December 1984, permitted free choice between amortization and immediate write-off. The importance of the goodwill 'problem' was increasing in a bull market: in 1985 the value of completed acquisitions and mergers was £6.3 billion, nearly 50 per cent more than the previous year,[166] and the average ratio of goodwill to bidder's net worth, approximately 3 per cent between 1967 and 1983, rose to over 40 per cent from 1984 to 1987.[167] Under these circumstances, immediate write-off produces lower net assets for the group than for the parent, and even negative net assets, in groups trading perfectly successfully – a counter-intuitive outcome. The more extreme results are particularly common in service industries with few tangible assets.[168]

Although there is no recorded instance of a company seeking to use a combination of the two treatments permitted by SSAP22 for goodwill derived

from a single acquisition,[169] variety in practice stopped only a little short of this.[170] Different methods could be used for different acquisitions. Companies started out using one method and then switched to the other.[171] Further, companies writing off goodwill immediately were using a wide range of reserves to do so.[172] Some companies were creating a new 'goodwill write-off reserve' with a nil carrying amount, then writing off goodwill to it, thereby establishing a debit balance not unlike the 'dangling debit' treatment that it was thought company law harmonization directives had eliminated. Companies amortizing goodwill were choosing a wide range of lives – from 40 years to less than 10 – with little apparent connection to the economics of the underlying businesses.[173]

Further difficulties arose in the calculation of goodwill, especially in connection with provisions. In arriving at the fair value of the assets obtained, acquirers were entitled – some commentators suggested they were positively encouraged[174] – to make provisions for 'items that were taken into account in arriving at the purchase price'.[175] Such items included not only liabilities and provisions at the date of the combination not shown in the accounts of the acquiree, but also, more problematically, costs of future reorganizations that the acquirer intended – or said it intended – to carry out after the combination, together with future trading losses it expected the acquiree to suffer as a result of the reorganization. Provisions increased the amount of goodwill and could thus be written off directly to reserves. Clearly, profits after the acquisition were that much higher because they did not have to carry the costs provided for. Even more controversially, if it emerged that an excessively prudent view had been taken and part of the provision was no longer needed, some preparers were reversing amounts back to the profit and loss account, thereby effectively recycling profits. Instances occurred of provisions for future trading losses by acquirees currently trading profitably and with no record of recent losses. In the opposite case, where costs and losses occurred in the acquiree which had not been anticipated at the time of the combination, these were sometimes included in a retrospective adjustment of goodwill, even two or more years after the combination. Some acquirers made provision for reorganization of the acquirer as well as the acquiree.[176]

As if all this was not enough, companies, especially those in the service sector for whom goodwill was often a highly significant item, were also taking advantage of what appeared to be another invitation in SSAP22[177] to separate out from goodwill amounts for 'identifiable intangibles' not previously recognized in the acquiree's accounts, and, indeed, not previously much recognized by anybody at all. Examples given in SSAP22 were publishing titles, franchise rights and customer lists. The standard indicated that the list was 'not intended to be comprehensive' and preparers certainly made sure that it wasn't: other examples included the value of milk rounds to a dairy and retail outlets in the news agency business.[178]

SSAP23, on business combinations, proved equally controversial. The definition of a merger made it relatively easy to structure a combination to satisfy the definition, for example by the use of vendor rights and vendor placings.[179]

The rule that immediately prior to the offer, the offeror should not hold more than 20 per cent of the shares of the offeree, or shares carrying more than 20 per cent of the votes, could easily be circumvented by selling the excess to a friendly third party and re-acquiring them as part of the general offer.[180] Thus the form could be varied to move a business combination between acquisition and merger, while in the case of combinations clearly mergers in substance, the use of merger accounting was optional.

In July 1987, the ASC announced that it was to undertake a 'major review' of SSAPs 1, 14, 22 and 23 (the last two had been in effect only since the beginning of 1985).[181] The official reason given was the implementation of the Seventh Directive, although this would have no effect on SSAPs 22 and 23, which had been drafted taking it into account. The circumstances, however, offered an opportunity to respond to the controversy surrounding the standards. Shortly after the announcement, the Confederation of British Industry issued what it called a Consultation Paper on merger and acquisition accounting.[182] This contained a clear attack on the current state of accounting in the area – *Accountancy* headlined its report, 'CBI paper slams SSAPs'.[183] The ASC responded by conceding that there was little in the paper it would disagree with other than its 'blinkered approach' in 'not accepting that there are counter arguments which are fairly strong'.[184]

Controversy continued to grow, fuelled, among other things, by combative chapters in the ICAEW annual survey.[185] In March 1988, *Accountancy* reported that the ASC had 'bowed to pressure and announced that it is to set up a major review of SSAPs 22 and 23'.[186] In fact the *ASC Report* made it clear that this was actually an increase in the scale of the 'major review' already announced the previous summer.[187] According to the *Report*, the exercise was now a 'major root-and-branch review' and was 'bound to take many months'.[188] In the meantime, limited proposals for increased disclosure were to be considered. These materialized in ED44 'Accounting for Goodwill – Additional Disclosures' in September 1988, which was hailed as 'still too weak, still too flexible' by one commentator.[189] The provisions of the exposure draft were subsequently incorporated into a revised SSAP22 in July 1989. The extensions to disclosure were intended to provide users with enough information to enable them to adjust the treatment adopted in a company's financial statements from merger to acquisition accounting or vice versa.[190]

In June 1988 the ASC published a substantial Discussion Paper on 'Fair Value in the Context of Acquisition Accounting'.[191] This set out proposals to regulate the calculation of fair values of various classes of assets and liabilities; to limit the period during which 'hindsight adjustments' could be made; and to prohibit provisions for future trading losses of continuing operations, though not for losses arising on closures of material and separable identifiable components of the business or for reorganizations. At the same time, the government announced its intention to introduce into the next Companies Bill provisions to increase disclosures relating to goodwill and to ban charging goodwill to the revaluation reserve.[192] Even the limited proposal to ban writing off goodwill to

the revaluation reserve was opposed by major and reputable companies such as Grand Metropolitan and Whitbread.[193]

A working party to develop a successor to SSAP22 was established in 1988, under the chairmanship of Roger Munson, a Coopers & Lybrand partner.[194] A feature of its, and the ASC's, discussions, occupying considerable time, was conceptual debate about the nature of goodwill: was it an asset and should it be recognized?[195] In this respect, discussions paralleled those relating to off-balance sheet financing. The committee and its working parties were increasingly aware that they were framing standards in a conceptual vacuum. One of the committee's weekend retreats was devoted to discussing the conceptual framework and the ultimate outcome of this concern was the committee's decision to embrace the IASC framework – albeit only as a benchmark. This was more than just a polite nod to the ASC's commitment to the IASC however; the committee might have gone further but for nervousness about what full adoption might have meant for extant standards not complying with the framework.[196]

The outcome of the conceptual discussion was the conclusion that purchased goodwill did constitute an asset, as defined by the FASB or the IASC, and did satisfy the recognition criteria in those frameworks. Equally important, non-purchased goodwill did *not* satisfy the recognition criteria because it could not be measured with reasonable reliability.[197] This would enable the former to be capitalized without any implication for the latter. Confidence in considering radical change may have been increased by Renshall's own stance towards SSAP22, the outcome of a working party he had chaired. This was made public on occasions such as his response to the CBI attack; he believed that SSAP22 was flawed from its inception.[198] There emerged a consensus – the ASC secretary at the time, Desmond Wright, calls it a 'Rousseauesque general will' – that writing off goodwill against reserves was unacceptable.[199] The consensus emerged in part because members of the committee listened to, and, more importantly, allowed themselves to be swayed by, the arguments.[200]

If goodwill is to be capitalized, how should it be treated subsequently? The Companies Act 1989 amended the 1985 Act to implement the Seventh Directive and made it clear that, if goodwill was treated as an asset, it had to be 'reduced by provisions for depreciation calculated to write off [the total] systematically over a period chosen by the directors of the company . . . not [to] exceed the useful economic life of the goodwill in question'.[201] The ASC obtained counsel's opinion to the effect that the life of goodwill could not be taken to be infinite, an interpretation already put to it strongly by the DTI.[202] However, systematic depreciation methods could be argued, by analogy with usage-based machine depreciation, to include charging amounts on the basis of periodic impairment reviews with proper criteria. As when SSAP22 was being developed, there was also doubt about the period of amortization. An arbitrary one and if so how long? Or economic life? What about changes in economic life?

Goodwill was discussed by the ASC itself in outline at least three times in 1988 and 1989.[203] Although a consensus for capitalization had emerged, there was less agreement about how goodwill should be amortized. The working party

put up a draft favouring amortization by formula, rather than impairment; this was debated at ASC meetings in December 1989 and January 1990.[204] There was unanimous support for capitalization and, although the decision about the alternative ways of amortizing the asset was more contentious, the majority of speakers were, on balance, in favour of the draft's approach.[205] The subsequent secret ballot on the draft saw nineteen members of the ASC supporting it, one voting against and one abstaining.[206] This level of unanimity around a pronouncement that seemed likely to prove highly controversial may be attributable, in part, to members of the committee viewing the ED as 'flying a kite' rather than representing a 'preliminary version' of a final standard.[207] A related, but not identical, explanation would involve members knowing that they would not be around to take the draft on to a standard.[208]

ED47 was published in February, 1990. It required capitalization of goodwill, which was then to be amortized over its economic life on a straight line basis, or one more conservative than straight line provided that the alternative was systematic and 'considered to give a more realistic allocation'.[209] The amortization period was to be determined 'by identifying and evaluating as far as possible the factors that gave rise to the goodwill'.[210] These factors were to be reviewed annually and the period shortened or lengthened if appropriate, though it was emphasized that the period should not be lengthened because 'new' goodwill was replacing the original. Useful life was not to exceed 20 years except in those 'rare circumstances'[211] where it could be demonstrated that it did – an attempt to establish by rule what can only be an empirical observation. The period was never to exceed 40 years. There would be an annual review for impairment, with write-offs through the profit and loss account, but no upwards revaluations.

The ED contained a 16 page appendix setting out 'the basis of the proposed treatment of goodwill'.[212] The rationale for its capitalization was that it satisfies the definition and recognition criteria of an asset in the IASC Framework and other similar pronouncements. The shift from SSAP22 was justified because 'the ASC regards it as more important that purchased goodwill should be treated consistently with other purchased intangible and tangible fixed assets than that purchased and non-purchased goodwill should be treated consistently [the justification offered for SSAP22's approach].'[213] Publication of the appendix was voted on separately and one member supporting publication of the ED voted against publishing the appendix, on the grounds that its attempt at a 'pre-emptive rebuttal' of the arguments for some alternative methods had not been fully debated: if the appendix was to be published, it should be described as a secretariat text.[214]

Debate on the ED began in the press before its publication, with a number of articles appearing in the *Financial Times* in December 1989 and January 1990,[215] including a piece in favour by Nobes, a member of the goodwill working party, and another opposing systematic amortization, by Graham Stacy and David Tweedie (the former a member of the ASC but not of the working party[216]). Submissions ran very heavily against the proposals, especially in relation to formulaic amortization. Companies were 'uniformly opposed' to this, as were

the CBI and the 100 Group of finance directors.[217] This same position was taken by audit firms, with all of the six largest firms opposed to ED47.[218] That auditors should take this position appears at first sight curious, since writing down by impairment reviews is the least 'bright line' method and involves regular appraisal of essentially subjective judgements. Nobes points out that auditors had earlier been generally comfortable with the proposals of ED30 and SSAP22 and argues that their new-found public enthusiasm for the impairment model was 'consistent with the [now] clearly revealed strong preferences of their clients and potential clients'.[219]

The political force behind the resistance to formulaic amortization was sufficient, as Nobes has confirmed, to result in personal pressure on members of the ASC and its goodwill working party, from colleagues and clients, to resist ED47:

> One of the partners of the Big Eight . . . said, 'I will probably have to resign because I have been part of issuing this exposure draft and now large companies are complaining to my boss that this will devastate their earnings and why is someone from this accounting firm involved in preparing this outrageous exposure draft?' And the finance directors, sitting there over coffee, would say, 'irrespective of whether this is the right answer I cannot be seen to be voting for it because I will go back home and the chairman will say, "how did the vote go this morning on this outrageous goodwill suggestion?" and I will not be able to say – I cannot put myself in the position of having to say – "I voted for it".' So, since the majority of the ASC were finance directors or technical partners, it was an appalling example of lack of independence.[220]

Stanley Thomson recalls some preparers 'looking over their shoulder' during the debates on the document that became ED30.[221]

Such was the pressure against ED47 that, as Nobes puts it, 'few members of ASC could be found to admit to voting in its favour.'[222] Certainly the finance director of Fisons claimed, after the publication of ED47, that he had found only two members of the ASC that supported regular amortization, the chairman and one other (Nobes, perhaps?).[223] However, the record shows that 19 out of 21 *did* vote for it, and thus began to shape up for a rebuttal of the hypothesis that all members of the accountancy profession are mere handmaidens to business as it purses its vested interests.

Responses to the exposure draft were not due until 30 July, shortly after the last meeting of the ASC, but Renshall was able to tell that meeting that 'an overwhelming number' of the 100 or so responses received by then were 'fiercely opposed' to the capitalization/amortization method.[224] 'We suggested amortisation as the best course,' Renshall commented, 'knowing full well that it would be rejected.'[225] The ICAEW Technical Committee's response did not come to a conclusion on the substantive issue but was sure of one thing: the profession could not afford 'to put forward a position it is unable to implement'.[226] Its solution, two decades after the topic first appeared on the ASC's technical

agenda? 'Further research is needed into the nature of goodwill, value statements and an overall conceptual framework for accounting.'[227] The Law Society certainly did not like the ED, but their submission suggests that, after 20 years, they still hadn't quite grasped the point of the ASC: '[the pronouncement] is not so much a statement of practice as an attempt to impose a standard.'[228] Quite so.

The invitation in SSAP22 to seek out and recognize the intangibles of an acquiree was being taken up with ever-increasing enthusiasm, and by late 1988 the ASC was coming under considerable pressure to take action. A particular favourite was brands. There was a highly acrimonious takeover battle for the confectionery manufacturer Rowntree, featuring two bidders, both Swiss, Nestlé and Jacobs Suchard. Before the first bid, Rowntree's shares were trading at 477p; the outcome of the battle was a victory for Nestlé, who ultimately paid 1075p. It was widely suggested that the gap between what the UK equity market apparently thought Rowntree was worth and its value to Nestlé was attributable mainly to the value of Rowntree's brands, which included Kit-Kat, Quality Street, Polo, After Eight and Yorkie, undisclosed on its balance sheet and therefore, it was argued, undervalued by UK analysts. It was claimed that non-recognition of brands was resulting in the systematic undervaluation of UK companies and, perhaps, even their acquisition on the cheap by overseas predators.[229]

In the wake of the Rowntree affair, Grand Metropolitan announced that it would be recording brands purchased during the course of acquisitions in its balance sheet from the year ending 30 September 1988. The policy would be applied retrospectively for acquisitions in the previous three years and was expected to add over £500 million to the balance sheet.[230] Although this policy was still rare, the company was by no means alone, and the policy was supported by its auditors.[231] A much more radical step was taken by Ranks Hovis McDougall, who announced in November 1988 that it was going to include all brands, including 'home grown' brands, on its balance sheet. The carrying amount thereby recognized, £678 million, reduced the group's gearing from 42 per cent to 13 per cent. The measurement method was described as current cost (provisions of the Companies Act 1985 made it doubtful that a market valuation would be lawful) and was arrived at with assistance from a well-known brand valuation consultancy, Interbrand.[232]

The December meeting of the ASC was devoted largely to the topic of intangibles. Renshall reported wearily to the press that the committee had 'noted for the umpteenth time that there was plenty of evidence that markets were not misled by attempts to adjust the balance sheet by reference to matters that have no real economic significance', but added that if companies wished to value intangibles the ASC would not try to stop them.[233] At the same meeting it was agreed that an interim statement would be issued on accounting for intangibles.[234] This appeared within days – it was reported in March's *Accountancy* – something of a record. It urged companies that were not already recognizing intangibles to refrain from doing so until the ASC's full guidance was available. While disclosure was encouraged where useful, assets should be recognized only when separately identifiable and measurable with reasonable certainty. If companies

were recognizing intangibles they should adopt and disclose an accounting policy covering depreciation and impairment; there was a rebuttable presumption that intangibles, including brands, have a limited useful life. Revaluations should be carried out only as part of a consistent policy of revaluation of intangibles and should comply with the Companies Act alternative accounting rules (covering current cost).[235] An exposure draft was due in the summer.[236] The same issue of *Accountancy* carried news that Lonrho was to begin recognizing newspaper titles; Hodgson Holdings, funeral directors, were to do the same for the trade names of undertakers acquired in the previous eight years, and would not be providing for regular amortization; WPP were contemplating recognizing acquiree's names.[237] It also carried the news that the Stock Exchange had agreed to allow intangibles included without audit qualification in company balance sheets to be included in its size tests.[238]

Accountancy cheerfully said of the interim guidance that it 'could prove to be as unpopular as current cost accounting'.[239] It certainly generated further controversy, including a public statement from the CBI about the 'great danger that we only value the things we can measure precisely'.[240] In July, a research report, commissioned by the ICAEW from the London Business School, was published. It argued that the market was not fooled by the absence of brands from the balance sheet and that in general brands would not be separable or measurable with sufficient reliability for recognition.[241] It suggested that the 'solution' to the 'problem' of equity depletion caused by writing off goodwill was capitalization of goodwill, though, of course, this would involve regular amortization, to which the brand 'hawks' were opposed. The hawks within the 100 Group attempted to persuade the group to send a letter to the ASC attacking the LBS report in advance of the committee's consideration of it and suggesting that any standard preventing the recognition of brands would be ignored. The draft was leaked to *Accountancy Age* and disowned by the group's chairman, Ian Tegner.[242] Meanwhile the range of intangibles recognized in the balance sheet grew ever wider: December's *Accountancy* carried reports that Tottenham Hotspur was to become the first football club to recognize the cost of players purchased on the transfer market[243] and Aberdeen Steak Houses was to recognize 'pre-trade outlay', that is start-up costs, of new branches.[244] At least in these cases there was to be regular amortization.

February 1990 was a busy month as far as the standardization of group accounting was concerned. Apart from ED47 on goodwill, the ASC issued a further statement on intangibles, TR780 'Accounting for Intangible Fixed Assets',[245] and an exposure draft on acquisitions and mergers. TR780 pushed the ASC's thinking a little further. At one stage the ASC had considered banning the recognition of brands and the preparer community had been celebrating leaked news that it had changed its mind – somewhat prematurely, as it turned out.[246] In fact TR780 did something rather more subtle. It required that,

> An intangible fixed asset should be recognised in the balance sheet as a fixed asset in its own right if and only if:

- either the historical costs incurred in creating it are known or it can be clearly demonstrated that they are readily ascertainable; and
- its characteristics can be clearly distinguished from those of goodwill and other assets; and
- its cost can be measured independently of goodwill, of other assets and of the earnings of the relevant business or business segment.[247]

Amortization requirements would correspond to those in ED47 for goodwill. Revaluations were to be permitted only if based on depreciated replacement cost and this figure could be measured with reasonable certainty.

The consequences of this ingenious piece of tradecraft were as follows. For most brands and similar intangibles, value is built up over the years in ways which make it difficult to relate that value to the efforts, and thus the transactions, designed to create it; few are purchased in separate transactions. Companies would, therefore, find it very difficult to identify historical cost for internally generated brands. Further, after an acquisition, the acquirer would not be able to include any intangible at fair value that the acquiree could not have included in its own balance sheet because it could not identify the historical costs that had given rise to it. An alternative valuation basis would not overcome this problem because the historical costs would still have to be demonstrably available. This provision, in itself, would be enough to prevent most brands being recognized after a takeover.

But the ASC also argued that

> the characteristics of some intangible fixed assets such as brands are thought to be so closely associated with those of the business as a whole that they cannot be recognized separately from goodwill and so should be subsumed within it and accounted for accordingly.[248]

Thus brands also failed the second recognition criterion. As a consequence the value of brands would be included in the carrying amount of goodwill and, under ED47, have to be amortized. Even if, by some combination of fluke, ingenuity and generosity on the part of the auditor, a brand was held to have passed the recognition criteria for intangibles, it would still have to be amortized under the same principles as goodwill, although a potential loophole would be opened up in that the economic life and outcomes of impairment reviews might differ as between the two categories.

ED48 'Accounting for Acquisitions and Mergers' responded to criticisms of SSAP23 by introducing a substance based definition of a merger. This was backed up by a page and a half of instructions, in the standard section of the pronouncement, about how to interpret the definition, and a requirement that mergers should be accounted for as mergers, rather than leaving preparers with free choice between merger and acquisition accounting.

The new release on intangibles added to the fury directed against ED47 – the combination led to the accusation that the ASC was 'putting accounting back a

hundred years'.[249] Undaunted, the ASC published ED52 'Accounting for Intangible Fixed Assets' in May 1990, co-ordinating publication with a new ED on fixed assets and revaluations (considered later). Its contents remained substantially as in TR780. Because its content was very close to the release, it was not put to a fresh postal ballot, a decision to which a number of members of the ASC objected.[250]

In June, ED50 'Consolidated Accounts' was issued (the haste with which documents were now being produced upset the chronological numbering). This largely reflected modifications in company law following the implementation of the Seventh Directive. The document also provided a rationale for the treatments proposed and was thus 'considerably longer than the sum of the two it replace[d]' (SSAPs 1 and 14).[251] 'A sign of things to come', critics of the length of modern standards can, retrospectively, harrumph. Finally, in July 1990, the last month of the ASC's life, ED53 'Fair Value in the Context of Acquisition Accounting' was issued. It appeared two years after the Discussion Paper and made a number of minor technical changes to its content.

Now, like goodwill, mergers, brands and fair value were all someone else's problem.

Segmental Reporting

Though not in the initial five-year work programme, segmental reporting had been added to the ASC's technical agenda by the end of its first five years. In July 1975, Coopers & Lybrand were commissioned by the ICAEW to carry out a research study on the subject and this was delivered in April 1976[252] and published the following year.[253] The need for standardization in the area came about because the Companies Act 1967 required disclosure of an analysis of turnover and profit by class of business and the Stock Exchange Listing Agreement required a similar analysis by geographical area. These provisions were being interpreted in a variety of ways, both in defining classes of business and geographical areas and in the treatment of such items as inter-company sales and common costs. One survey referred to a 'yawning gap in accounting rules'.[254] The FASB issued an exposure draft on the subject in September 1975. This draft is referred to extensively in the Coopers & Lybrand report and, indeed, appended to it. The report recommends that, subject only to some 'minor modifications',[255] the UK should follow the FASB approach.

By 1982, pressure for a pronouncement had increased because there was now an International Accounting Standard on the topic and companies' legislation had been extended to include a geographical analysis.[256] A working party had been established, chaired by the author of the Coopers & Lybrand study, Adrian Lamb.[257] The pressure for a standard was still not perceived by the ASC as 'a big political imperative' and there were significant concerns among preparers about the danger, as they saw it, of being required to release commercially sensitive information.[258] The alleged commercial sensitivity of segmental disclosures had also resulted in UK companies legislation exempting a preparer from disclosure

when this would be 'seriously prejudicial' to its interests.[259] Many involved in the technical committees of the CCAB bodies – and some in the ASC – believed that, if company legislation explicitly permitted something, accounting standards could not, or should not, ban it.[260] Failure to incorporate an exemption would offend against this principle but failure to require disclosure would undermine the force of a standard. After the reconstitution of the ASC under Davison, work on segmental reporting and, indeed, on the implementation of IASs generally, was suspended.[261]

The ASC eventually resumed work on the topic and ED45 'Segmental Reporting' was published in November 1988. It permitted exemption on the grounds of serious prejudice and the requirements going beyond legislation were limited in scope to public limited companies and other large entities. Its requirements were similar to the IAS, except in allowing the exemption. Its approach and language followed UK legislation closely.[262]

The ASC subsequently approved a draft standard with little amendment and preserving the exemption. Those who favoured the argument that standards should not take practice beyond legal requirements prevailed: 'even at the end of the life of the committee, it still felt pretty weak about that sort of thing.'[263] Once again, the CCAB veto disturbed the progress of a document. The Technical Committee of the ICAS considered that there was no evidence that segmental information was needed (somewhat against the run of international events and academic research) and its Council declined to support publication. After some months it was 'embarrassed' into changing its position and SSAP25 'Segmental Reporting' was published in June 1990.[264] As *Accountancy* put it, 'the last SSAP before the end'.[265]

Related Party Transactions

In January 1982, it was reported that a project on related parties would be established during the course of the year;[266] the IASC was developing its own pronouncement – E25 'Disclosure of Related Party Transactions' was issued in March 1983 – and the subject was covered by a hodge-podge of legislative requirements (many dealing with directors' interests and having resulted over the years from scandals exposed by DTI Inspectors' Reports) and Stock Exchange rules.[267] It was a 'quite touchy' issue[268] and there was a reluctance to go beyond the legal position[269] but occasional scandals surfaced, frequently as a result of a company doing business with its directors,[270] and there was a need for better regulation. The topic had more than usually strong implications for audit, and attempts to co-ordinate with the Auditing Practices Committee were made.[271]

Work on the project was suspended in the wake of the reconstitution of the ASC. When it resumed, things proceeded at a relaxed pace, the ASC, according to one of its members, recognizing that the profession was not yet ready for a pronouncement on the topic.[272] In 1984 work was suspended again because a new statutory instrument on the issue was felt to be ambiguous and it was

assumed – wrongly – that a revised version would be issued. In September 1985 the project was picked up for a third time;[273] an exposure draft, provisionally numbered ED40, was prepared by the working party in 1986 but not approved by the ASC.[274] A further draft was approved and published, as ED46 'Disclosure of Related Party Transactions', in April 1989. The final draft was not substantially different from the earlier ED, or indeed, outline proposals considered by the ASC in 1980; however, at least sixteen separate drafts were prepared by the working party and unsuccessful submissions to the ASC made on three occasions.[275] According to Renshall, the subject 'proved much hotter than I thought it would – I was being naive . . . For small and medium sized companies, related party transactions are not uncommon and not necessarily improper. They thought, "Hello, these fellows are accusing us of something."'[276] It would be misleading, though, to suggest that there were no technical problems to be resolved: the definition of a related party created genuine drafting difficulties and a decision to require disclosure only of abnormal transactions with related parties, contrary to the IAS requirement and that in the USA, made it necessary to define abnormality.[277]

Thirty-nine responses to ED46 were received, not a particularly high number for a draft which appeared controversial; perhaps potential respondents suspected that they would get a second crack of the whip from the new standard-setting machinery.[278] The definition of a related party was generally acceptable. The recommendation for disclosure only of abnormal transactions was welcomed by preparers but greeted more equivocally by others; five of the six CCAB bodies argued that the distinction was unacceptable as did half the professional firms. Respondents argued that there was a need to conform to the IAS and that the distinction was unauditable. A proposal to disclose any economic dependence of the entity on another party was objected to by three-quarters of respondents commenting on the issue, and four-fifths of those commenting, including all the CCAB bodies, opposed the suggested exemption of small companies, arguing that the proposed disclosures were at least as important for small companies as for large. However, the DTI supported the exemption on the grounds of the burden to preparers.

In January 1990, the ASC was reported as 'determined to push ahead with a standard',[279] but, in the event, it ran out of time.

The Revision Programme

The ASC's programme of reviews of its standards yielded a number of exposure drafts in the last five years of its life. Extraordinary items proved a difficult subject when the original standard, SSAP6, was under development. In the early years of its operation, preparers showed a very marked tendency to use any loopholes in its definitions to work credits in the profit and loss account upwards towards operating results and debits downwards as far as possible away from that line – indeed, efforts of this kind were sometimes apparent even when there was no ambiguity in the standard. This behaviour continued as the years passed.[280]

In January 1983 a Discussion Paper was issued asking for comment on a number of issues, including the 'considerable inconsistency between the treatment of apparently similar items in the financial statements of different companies'.[281] The working party proposed to deal with this by supplementing their definitions with lists of items 'normally to be treated as an undisclosed credit or charge, an exceptional item, an extraordinary item or a reserve movement'.[282] The Discussion Paper drew attention to the apparent inconsistency between SSAP6's definition of extraordinary items, which included a requirement that they should not recur frequently or regularly, and the way companies were reporting such items in practice, which sometimes involved individual companies reporting the same category of extraordinary item period after period. It repeated the proposal in ED16 that the result on the sale of a revalued asset should be calculated by reference to book value and not depreciated original cost.[283]

ED36 'Extraordinary Items and Prior Year Adjustments' was issued in January 1985. A change to the definition of extraordinary items, to remove the test of frequency and regularity, suggested by the Discussion paper because of the problem of recurring extraordinary items, was abandoned as a result of the comments; a definition of ordinary activities was added in an attempt to widen the scope of the ordinary, and thus narrow that of the extraordinary. A list of examples of extraordinary items was provided in the explanatory section of the pronouncement. Extraordinary items were to be included between the result from ordinary activities and the total profit or loss for the year, the latter being struck before dividends. This would prevent the practice of bringing in profit brought forward before deducting extraordinary losses.

Exceptional items were defined (in SSAP6 the definition was implicit) and required to be distinguishable as such, whether shown on the face of the profit and loss account or in a note. Again, a list of examples was provided. The exposure draft reversed the Discussion Paper's recommendation on the measurement of the result on sale of fixed assets, requiring it to be calculated by reference to depreciated original cost. This was justified on the grounds that the whole of the difference between sales proceeds and original cost would now pass through the profit and loss account. Termination of activities would be treated as extraordinary only where a business segment was closed.

Eighty-three submissions were received on ED36, which proved largely uncontroversial except in its recommendations on the sale of revalued assets. The Technical Release accompanying the revised standard[284] explained that,

> The ASC has concluded, based on comments received, that opinion on the matter does not at present allow one method to be laid down as standard to the exclusion of the other, and that the matter requires further study. Accordingly, the matter is not dealt with in the revised SSAP6 but will be considered in a new project on fixed assets and revaluations . . . Similarly, ED 36 contained proposals for the accounting treatment of unrealised surpluses and deficits on the revaluation of fixed assets, but no requirement appears in the revised standard.[285]

ED16 appeared in 1975, so that this rather straightforward technical issue had apparently been under study for more than ten years; this was an unfortunate position for a standard-setter, committed to narrowing areas of difference, to find itself in.

Apart from these changes, the revised SSAP6 'Extraordinary Items and Prior Year Adjustments', adopted in July 1986, followed the preceding exposure draft closely. It had only moderate success in improving the situation.[286] Terry Smith's famous denunciation of the camouflage in corporate financial reports, published in 1992 ('the book they tried to ban'),[287] devoted an early chapter to extraordinary items. The post-ASC standard-setting machinery issued its first exposure draft, its second Urgent Issues Task Force abstract, and its first 'home grown' standard to the subject.[288]

At the time of its adoption, the most controversial aspect of SSAP12 'Accounting for Depreciation' was its attempt to achieve depreciation of property. The number of companies failing to depreciate property fell sharply after its introduction but a sizeable and vocal minority of non-depreciators remained.[289] After its adoption, several other problems emerged, largely as a consequence of the application of current cost accounting. A particularly controversial issue was the use of 'split depreciation'. A company revaluing its property would be expected to calculate depreciation by reference to the newly-established carrying amount; however, the wording of the company law requirements implementing the Fourth Directive, though ambiguous, appeared to allow the charge in the profit and loss account to continue to be based on historical cost, with the additional amount charged to the revaluation reserve to which the original uplift was credited.[290] This practice was adopted by a number of companies, most famously Woolworths.[291] Arguments in favour of split depreciation included consistency between companies revaluing and those not revaluing their assets; avoiding the charge to the profit and loss account becoming a matter at the discretion of management; and keeping the charge in the profit and loss account consistent with historical cost accounting.

A less controversial approach was to charge 'supplementary' depreciation to reflect the impact of rising prices, thus in effect putting the depreciation charge on a revalued basis while retaining historical cost in the balance sheet. Another device achieving something of the same effect was artificially to shorten the life of assets in the historical cost accounts, a wheeze which came to light when companies were required to publish current cost accounts alongside the historical cost statements; if they kept the same lives they would further reduce their current cost profits, while if they used realistic lives in the current cost accounts, they would be employing different estimates of useful life for the same assets in the two sets of financial statements.

A review of SSAP12 to address these issues commenced in early 1982 under a working party chaired by Jeffery Bowman.[292] The re-prioritization of the work programme on Davison's arrival as chairman resulted in lowering the urgency attached to the work but a Discussion Paper was nonetheless issued in December of that year.[293] The Discussion Paper proposed that split depreciation should be

banned, without giving a reason but merely asserting that it contradicted SSAP12 and the Companies Act. This claim was easily disputed;[294] the relevant paragraph of the standard is silent about where the period's provision should be charged.[295] As Nobes says,[296] split depreciation may be contrary to the spirit of SSAP12 but it can hardly be said to breach its letter. The working party recommended consistency in the estimation of asset lives between the historical and the current cost accounts and banning supplementary depreciation. Calculation of profit or loss on the sale of assets should be carried out by reference to book value, the method proposed in ED16 and also supported by the Discussion Paper on extraordinary items published the following month.[297] Non-depreciation on the grounds of very long life with residual value being maintained was permitted but the rarity of the cases in which it would be appropriate was emphasized.[298]

If the working party's assertions that its recommendations merely echoed the existing version of SSAP12 and company law are accepted, it is easy to sympathize with Davison's view that the exercise did not merit continuing with the project.[299] The reality, of course, was that some of its recommendations would change preparers' options. Perhaps for this reason, the Discussion Paper generated much the same volume of comment as other pronouncements – 88 submissions, very much in line with the two exposure drafts issued in 1982, ED30 on goodwill (97) and ED31 on mergers (86).[300]

Commentators requested that the revision of SSAP12 should be linked to the development of current cost accounting and, hence, work on the review was suspended until July 1984, when ED35 was published.[301] Thereafter work proceeded fairly rapidly, with an SOI, setting out the proposed changes in outline, issued in September 1984[302] and ED37 'Accounting for Depreciation' published in March 1985. Calculation of the result on the disposal of a revalued asset was dropped, being now dealt with in ED36. Guidance on revaluation itself, referred to only very briefly in the Discussion Paper was also dropped, on the basis that it was being dealt with in the context of current cost accounting. With these exceptions the ED followed the earlier documents.

The ED largely retained the original definition of depreciation, preserving the reference to loss of value (but adding the word 'permanent'), thereby retaining some ambiguity about whether depreciation was an allocation or a measure of loss of value.[303] In response to the problem of non-depreciation of property, the draft proposed that residual value be measured in prices at time of acquisition or subsequent revaluation and not of disposal. The point that 'buildings have a limited life' and should thus 'be depreciated having regard to the same criteria' as other assets,[304] which appeared only in the explanatory section in the 1977 version of SSAP12, was moved to the standard section.[305] The standard section dealt explicitly with 'very long life' assets along the same lines as the Discussion Paper, except that long life and residual value at or above net book value were now alternatives rather than both being required. The rarity of such cases was again emphasized.[306]

Eighty-nine comments on ED37 were received. Some submissions raised the issue of the ambiguity caused by the reference to loss of value in the definition of

depreciation and in the standard this was replaced by a reference to 'reduction in ... useful economic life'.[307] ED37 had indicated in the explanatory section that, where a policy of revaluing assets was adopted, valuations should be kept up to date, but this requirement was not carried through into the standard section. Commentators asked for more guidance but the ASC in fact dropped the topic from the scope of the project, referring it to a new project on fixed assets and revaluations. Although objections to the banning of split depreciation were received, the ASC stuck to its guns, on the grounds of consistency between the profit and loss account and the balance sheet. In response to the argument that company law permitted it, the ASC responded that the position was ambiguous, but even if it did, the treatment was undesirable and should not be incorporated in a standard.[308]

SSAP12 (Revised) 'Accounting for Depreciation' was published in January 1987, nearly two years after the ED. Its definition of residual value was carried over from the ED, thus maintaining the block on the 'high residual value' route to non-depreciation. However, the reference to very long-lived assets was dropped completely. The statement accompanying the publication of the revised standard indicated that,

> a significant number of commentators expressed concern that the proposal could be open to misinterpretation or misuse. It was believed that it might represent a loophole ... The ASC acknowledges the potential problems associated with the proposal and has not retained it in the standard. It will be necessary to consider in individual cases whether a provision for depreciation under the standard is required. In doing so, the general principle of SSAP12 ... should be applied. This means that the ASC recognises that there could be circumstances, such as those outlined [in ED37], in which it might not be appropriate to charge depreciation.[309]

This change of position led *Accountancy* to describe the development of the revised SSAP as a 'sorry tale': 'The ASC's apparent inability to make up its mind has caused dismay. "This can only lead to a further crisis of confidence in the standard setting process," one large firm technical partner said.'[310]

The working party had completed its work on amending the standard at the beginning of 1986 and a draft revised standard was considered by the ASC in February of that year and, following further revision, approved by ballot in March.[311] It was then approved by the Institute of Chartered Accountants in Ireland, the Chartered Institute of Management Accountants and the ACCA. The ICAEW raised objections and the ICAS therefore deferred consideration of the draft.[312] Most of the ICAEW's objections were resolved without amendment to the draft, but two changes were made, amplifying requirements relating to the revision of estimated asset lives and permanent diminutions of value. The new text was approved by the ASC in July and resubmitted to the CCAB bodies.[313]

This time round, the ACCA had a number of reservations. A meeting with a member of the ASC secretariat resolved all but one of these; the ACCA

continued to object to the revised wording on re-lifing that had been agreed in order to satisfy the ICAEW, arguing for the reinstatement of a requirement to disclose the amount written off where the whole of the adjustment was made in the first year.[314] The secretariat took the view that in deleting this requirement, it had not been envisaged that the amount would not be disclosed, merely that it would inevitably constitute an exceptional or extraordinary item and thus fall to be disclosed under SSAP6; it was thus agreed that, as 'a useful concession which can only create goodwill'[315] with the ACCA, the change would be made and notified to the CCAB bodies as a drafting alteration not requiring their approval.[316]

This left the ICAS, whose Council considered the document for the first time in October. It now objected on the grounds that the document appeared too restrictive in dealing with the non-depreciation of property.[317] Its first preference was the reinstatement of the paragraph in the ED acknowledging that there would be circumstances under which non-depreciation would be appropriate but it was accepted that its reinstatement would necessitate a further round of CCAB body consideration. As a concession, it was prepared to accept a change in the definition of residual value, dropping the reference to realizable value being based on prices prevailing at the date of acquisition or revaluation. It claimed that, because these words were 'not explained elsewhere' and did 'not seem to be of particular help to the reader', dropping them would 'provide a better link between [the relevant paragraphs]'.[318] The result would, of course, have been to reopen the 'high residual value' route away from depreciation. As the ASC well understood, this was not a minor matter and would also have required re-submission, with no great likelihood that the other CCAB bodies would approve it.[319] The secretariat's 'inside information' was that it was individuals on the ICAS Council, with no support from its Technical Committee, who were raising the objection. The ASC held its nerve and the ICAS settled for the clarification in the accompanying Technical Release, already quoted.

This was, of course, precisely the wording complained of by *Accountancy* and the anonymous technical partner. While describing the outcome of the review as likely to provoke a crisis of confidence in the ASC may have been more than a little intemperate, there was a point to be made. Although the changes actually agreed during the two rounds of CCAB body deliberation were minor – even trivial – and the major change called for by individuals on the ICAS Council successfully resisted, and although the cumulative delay was not great by the standards of some of the ASC's fresh pronouncements, the system's inability to carry even the outcome of a review of an existing standard through the CCAB bodies without alarms and excursions underlined the problems associated with the ASC's constitution.

The review did little to narrow areas of difference beyond heading off the limited forces backing split depreciation. Around a quarter of companies in the ICAEW annual survey continued to leave some buildings undepreciated.[320] In 1990 *Accountancy* reported that, 'when SSAP12 (revised) . . . came out in January 1987 it was thought that the brewers might wish to change their pub depreciation

policies, but they merely appear to have altered the reasons given for non-depreciation.'[321]

The ASC's one attempt to open up variety – in choice of depreciation method – also apparently failed. This was designed to achieve standardized, not free, choice, by requiring the use of the method 'most appropriate'[322] to the asset and its use. Carey[323] shows that in 1990/91, in 86 per cent of instances in which a depreciation method for a class of assets was disclosed by companies in the ICAEW survey, the method used was straight line. As he points out it is difficult to judge the extent of change from earlier years because the data was aggregated in different ways in different years, but, 'clearly . . . any change has not been substantial in spite of the [changes made] in the last revision to SSAP12'.[324]

The review of SSAP9 represented a triumph of the standard-setters' tradecraft. When originally issued, the standard on stock and long-term contracts provoked a good deal of controversy but this abated as time passed.[325] A small number of building and engineering companies continued to use the completed contract method in defiance of the standard; some received audit qualifications, others escaped.[326] The IASC issued an exposure draft permitting either completed contract or percentage of completion and then adopted a standard placing such tight restrictions on the use of percentage of completion as to make its application effectively voluntary, a response to claims that it was open to abuse. Advocates of the completed contract basis were pleased with the exposure draft and ecstatic about the standard.[327]

Non-compliance for trading stock also continued, with companies failing to include attributable overheads,[328] or using unacceptable methods such as base stock.[329] Not all these departures resulted in disclosure of non-compliance or audit qualifications. *Accountants Weekly* concluded that,

> If consistency be the measure of the effectiveness of an accounting standard, then as we have discovered in recent weeks [as a result of reading its surveys of published accounts] SSAP9 on accounting for stocks must lie fairly low down the value for money league table.[330]

A further difficulty was that the 1981 Companies Act, implementing the Fourth Directive, permitted last-in-first-out, opening up (again) the argument that what was explicitly allowed by law should not be banned by the ASC.[331] The ASC first reviewed the operation of the standard in 1982, under a working party chaired by Stanley Thomson and tasked specifically with investigating the use of LIFO.[332] The working party got as far as preparing a report for the main committee's consideration in September[333] but the review then fell as a result of the re-prioritization carried out by Davison.[334] Most of the problems, other than the LIFO question, were, in any event, issues of compliance.

The standard returned to the agenda rather more quickly than had been expected as a result of change introduced by the 1981 Act. The problem that resulted was to test the standard-setter's tradecraft to the limit. It illustrates very

well the technical difficulties posed for standard-setters by the importation of the continental European, prescriptive, approach to legislating for financial reporting that resulted from the Fourth and Seventh Directives.

The 1981 Act introduced two provisions relevant to SSAP9's treatment of long-term contracts. The first required that only realized profit be included in the profit and loss account.[335] It was argued by some that SSAP9's treatment of long-term contracts was in conflict with this provision, because attributable profit was unrealized, but this objection was disposed of easily because the Act left the determination of realized profit to generally accepted accounting principles[336] and SSAP9 itself therefore provided grounds for arguing that the profit was realized. This interpretation was incorporated in a Technical Release issued by the CCAB bodies and approved by counsel.[337] The release indicated that the DTI did not dissent from this approach.[338]

The second provision was more troublesome. The Act required that current assets (including stock, and therefore long-term work in progress under SSAP9) should be stated at the lower of net realizable value and purchase price or production cost.[339] The definition of purchase price was expressed in terms of the consideration given for the asset,[340] thereby allowing debtors to be included at recoverable amount, on the grounds that the goods or services supplied constituted the consideration given for the debtor balance received.[341] The inclusion of attributable profit in long-term work in progress clearly contradicted this requirement. Two routes to achieving compliance with the Act (other than by abandoning the percentage of completion method) appeared open.[342] One would involve a change in the way attributable profit was determined, so that only work charged to the customer via progress payments would be eligible for inclusion in the calculation. But this would be difficult to justify: why should there be no attributable profit merely because the progress payment had yet to be charged and why should two companies with similar projects recognize different profits simply because the contracts scheduled progress payments differently?

The other involved invoking the true and fair override provisions in the legislation. These had themselves grown more complex as a result of the company law harmonization directives. The override was only available where there were 'special circumstances in the case of any company',[343] so that its systematic use in all cases was in some doubt and was certainly not favoured by the DTI.[344] More problematically for preparers, if the override was invoked, particulars had to be given of the departure, the reasons for it, and its effect,[345] thereby revealing the profit on work in progress at the balance sheet date. This was a matter of considerable concern to preparers; a company with a small number of projects, or a special corporate vehicle set up to manage a single project, might find itself disclosing commercially sensitive information.

There was also a technical issue about measuring the effect. If the appropriate treatment without invoking the override would be to recognize no attributable profit, the effect of the departure would be the total amount of attributable profit. This was the interpretation favoured by the DTI.[346] If, however, it is considered that the profit attributable to the element of the work subject to

progress payments would properly be recognized without the override, on the basis of the rules for measuring cash and debtors, then total attributable profit must be apportioned between progress payments and net work in progress. As Peter Holgate, then an under-secretary at the ASC, put it: 'Unfortunately (or fortunately, depending on your point of view), it is far from clear how much profit is included in [net work in progress].'[347] This was the interpretation favoured by preparers.[348] In the ICAEW annual survey for 1983/84, 76 companies disclosed the existence of long-term work in progress. All followed SSAP9 in including attributable profit in the amount but, of the 60 companies following the 1981 Act format, 32 disclosed only the application of the true and fair override and not its effect and 20 failed to disclose even the application of the override. Of those companies disclosing the application of the override but not its effect, 23 stated that this was because they were unable to apportion profit between progress payments and work in progress and the remainder gave no reason.[349]

In the April 1983 issue of *Accountancy*, a member of the ASC secretariat confirmed that the committee was developing guidance.[350] The following month's issue indicated that there was not to be a comprehensive review but that the specific problem would be resolved urgently, 'say within six months', according to Davison.[351] In rather less time than that, however, the ASC reversed its position. After discussions with the DTI and the construction industry, it decided to remain silent, so silent, in fact, that it announced this decision only in a letter to construction companies; recipients were invited to take their own legal advice.[352] *Accountancy* speculated that the ASC had received legal advice to the effect that the disclosure should relate to the gross amount of work in progress, supporting the DTI rather than preparers.[353]

And there the matter rested for a further twelve months. Then the DTI wrote to the ASC, reminding them of the unfinished business and reporting their concern that so many companies were invoking the override but failing to disclose its effect.[354] As a result, the ASC decided to review all accounting standards in the light of the new companies' legislation, but to start with SSAP9.[355] A working party was established under the chairmanship of Christopher Nunn.

Yet how was the ASC to resolve the matter? The answer, when it finally arrived, was blindingly simple: balances relating to long-term contracts on which attributable profit was to be recognized were not, after all, stock, but debtors. Specifically they were 'amounts recoverable on contracts'[356] and, as such, would be shown within debtors and could thus, of course, include a profit element without departure from the detailed provisions of companies' legislation. Job done. Now all that was necessary was to persuade the world that it made sense for an item that had for years been stock to be reborn as debt, preferably without at the same time conceding that financial reporting had embraced the post-modern culture 'characterised by a loss of belief in an objective world and an incredulity toward meta-narratives of legitimation'[357] such, perhaps as the corpus of generally accepted accounting principles.

A convenient source of cover was available in the shape of IAS11 'Accounting for Construction Contracts',[358] and this was, indeed, given in internal ASC

documentation as the only source for the proposed method.[359] It had, however, been clear from the start of the working party's operations that the principal, if not the sole, reason for the review, at least as far as long-term contracts were concerned, was to address the conflict between company law and the standard. For example, the paper setting out the proposals for change considered by the working party on 3 April 1986, begins:

> SSAP9 was published in May 1975 and remains in force. In most respects the standard appears to be well-accepted. However, problems have arisen with regard to the balance sheet carrying value of long-term contract work in progress; as a result of changes in company law in 1981, the method put forward in SSAP9 now conflicts with the Companies Act.[360]

No other reason for a change is given.

Yet this was not how the need for change was explained in early drafts of the ED, a point which worried the DTI. A letter from the Department dated 4 July, 1986, commented on various drafts:

> Turning to the first draft of the Exposure Draft, from our standpoint the most important point in the preface is that the revision has overcome the conflict between the present SSAP9 and Schedule 4 of the Companies Act 1985. Indeed we thought this was the main reason for the ASC undertaking the revision. We therefore think this should have the major emphasis in the preface, instead of (as at present) [the provision of] a consistent and integrated financial statement which accords with international practice. I appreciate there may be some sensitivity about highlighting compliance with UK law as I suggest. If the ASC is concerned about this, then perhaps it could be given as another (but equally important) reason for the revision.[361]

The DTI's compromise proposal was adopted in the published version of ED40 'Stocks and Long-term Contracts', which appeared in November 1986. The preface said that the new approach 'accord[ed] with international practice,[362] without referring directly to IAS11, because of the inconvenient fact that IAS11 did not actually specify any particular balance sheet treatment. The rationale for the debtor classification is IAS11's profit and loss account treatment, which involves recognizing turnover and cost of sales, rather than merely introducing the attributable profit itself, as under the original SSAP9. The approach is described in the explanatory section of the IAS[363] but not carried through into the standard. This obviously made it difficult to argue that the method in ED40 was essential to comply with IAS11, a point made to the working party in May 1986 by Renshall, who was at that stage about to take over as ASC chairman, and who concluded that, 'it may therefore not be possible to place too much reliance on the IAS in putting forward this approach.'[364]

Where, then, did the idea come from and who had the brainwave? Unfortunately, no evidence of a 'Eureka moment' survives in the ASC archive. It is

possible, of course, that the imperative to square the treatment with paragraph 90 was sufficient inspiration in itself. Another possible source is the USA;[365] the ASC secretariat had access to considerable experience of American practice, for example from Christopher Morgan. In the USA, both completed contracts and percentage of completion were permitted[366] and no balance sheet treatment was specified; US practice included treating unbilled costs variously as inventory, as a separate category within current assets, and as receivables.[367]

The construction sector, particularly smaller companies, opposed the new approach, in part because of a concern that classifying completed work as turnover and thus debtors might raise tax difficulties, such as challenges to provisions against the value of this work. One building company accountant wrote that if the new approach was implemented, 'I must warn ASC that NON-COMPLIANCE WILL BE MASSIVE.'[368] The industry preferred to press for the legislative provisions permitting the inclusion of a profit element in current assets to be interpreted as applying to work in progress. This point was taken up with the DTI, who replied that, in its view, this was not possible.[369] In October 1986, on the eve of publication of ED40, the ASC obtained counsel's opinion that their proposed treatment in the balance sheet was acceptable.[370] A year later, still under pressure to find a way of retaining the approach in the original SSAP9, they went back to counsel to ask whether paragraph 89 (now paragraph 90 in the 1985 Act) could be applied to stock and received the answer they were expecting: no.[371]

In April 1988 the draft standard began the rounds of the CCAB bodies.[372] In June the ICAS Council declined to approve it because some members objected to the approach to the recognition of turnover in the document. If a contract was at an early stage such that no profit was to be recognized, this would be achieved by recognizing turnover equal to cost of sales. The ICAS objected on two grounds: that this would mean profit was not matched to turnover and that it conflicted with IAS11. A spokesman for the ASC conceded: 'we're not able to say that the proposed standard is entirely consistent with IAS11'.[373] Amendments proposed by the ICAS were incorporated into the document and the revised standard, SSAP9 (Revised) 'Stocks and Long-term Contracts', was issued in September 1988. The effect of the amendments was to leave the relevant question open, with a reference to the possibility that it 'may be appropriate'[374] to recognize turnover and costs of equal amount for early-stage contracts.

Two other standards reviewed in the period had actually caused very little difficulty. SSAP13, on research and development costs, had caused problems in its gestation, but not since. A requirement to disclose research and development expenditure for the period appeared in ED14 but was subsequently abandoned, apparently because of definitional difficulties.[375] It had been highly controversial during the exposure of ED14 although it was supported by the DTI.[376] Political pressure for disclosure of the level of activity recurred intermittently, principally on the grounds that research and development are good things and disclosure might embarrass industry into doing more of them.

A working party on SSAP13 was established as part of the ASC's post-1981 Companies Act programme of reviews and soon found itself subject to such

pressure; a House of Lords select committee called for disclosure and the chairman of the ASC working party, Professor Michael Bromwich, visited the DTI to learn how it proposed to respond, since legislation requiring disclosure would obviously make inclusion of detailed rules in a standard relatively straightforward.[377] Some time later, a visit by Godfrey (then chairman of the ASC) to see the Secretary of State for Trade and Industry about other matters was dominated by the minister's determined advocacy that disclosure should be achieved by a change in the standard rather than by legislation.[378]

It was to be June 1987 before these concerns met a response in a proposed revision of SSAP13. ED41 'Accounting for Research and Development' required separate disclosure of research and development expenditure written off and any amortization of capitalized development expenditure.[379] The preface implied that the change was proposed principally to secure compliance with IAS9 and various overseas standards but also reported that the ASC 'believes that this disclosure would provide useful information to users of accounts'.[380] The draft made no proposal to change accounting treatment, which would thus remain, for qualifying development expenditure, a free choice between capitalization and immediate write-off.

According to one analysis,[381] the proportion of respondents to ED41 opposing disclosure was similar to that in the case of ED14, the earlier exposure draft on the subject. Objections included commercial sensitivity and difficulties of definition. Although the arguments were very similar to those offered against ED14, the ASC did not offer any evaluation of them, or explanation of why it should now be possible to overcome problems thought insurmountable in 1977,[382] merely reasserting that the information would be useful and referring to an IAS, when there was little evidence that such pronouncements usually had the ASC jumping to obey. The ASC did accept the argument that difficulties in applying the requirements would make the costs of disclosure outweigh the benefits for smaller companies, and the revised SSAP13 'Accounting for Research and Development Expenditure', issued in January 1989, exempted companies not considered by the ASC to be 'publicly accountable'.[383]

The final topic to be reviewed was government grants. A working party was established in February 1987, following representations from the ICAS that there were difficulties in applying the standard because of the changing nature of government grants, which were now less often linked to specific expenditure and more likely to be expressed in terms of targets and objectives.[384] ED43 'The Accounting Treatment of Government Grants', published in June 1988, provided more generalized guidance and also eliminated the free choice alternative of recognizing grants towards fixed assets in the balance sheet by deduction from cost, a treatment arguably already outlawed by companies legislation requiring assets to be shown at purchase cost,[385] and also banning the off-setting of assets and liabilities.

Even this modest narrowing of areas of difference caused considerable objection among respondents to the draft. As a result of the objections,[386] the working party proposed an amended treatment, preferring deferred credit but

permitting deduction from cost. The DTI objected, challenging the legality of the deduction from cost method.[387] Proponents of deduction argued that the credit was not, generally, a liability (unless it was still subject to repayment pending completion of outstanding conditions) and it could thus be deducted from the gross amount without breaching the rule about offsetting, and arguably should be deducted from purchase cost, representing a kind of discount thereon.[388]

The ASC took counsel's opinion and were told that the deduction from cost method was, indeed, against the law. Nonetheless, the force of argument in favour of the method, the possibility that its counsel might be wrong, and the availability of the method for entities not covered by the relevant legislation, led the ASC, in July 1989, to issue a revised SSAP4 'Accounting for Government Grants', preserving free choice between deduction from cost and deferred credit.[389] Another opportunity to narrow an area of difference lost, in the very last month of the Committee's existence.

Judged by their final outcomes, it is possible to be sympathetic to Davison's comments on the review process – he had presided over the initial stages of the reviews of SSAPs 6 and 12: 'Experience of reviewing accounting standards leads me to wonder whether the effort is worthwhile. Rarely do the resultant amendments match in consequence the time, money and resources spent on the consultative process of the review.'[390] Nonetheless, a regulator has a duty to keep the regulations up to date even in minor particulars and the ASC was discharging this role. In doing so, it simply encountered its bigger problems writ small: the impact of the new approach to companies legislation (almost all the topics discussed here); the absence of effective enforcement making it difficult to eliminate methods with significant political support (the depreciation of property); interference by CCAB bodies, with positions that might be legitimate but should have been sorted out before the proposed standard was circulated (depreciation, long-term contracts); pressure by government unwilling to legislate (research and development); absent users (research and development); and the lack of a conceptual framework (government grants, sale of revalued assets).

A Final Flurry

In the last three months of its existence, the ASC issued seven exposure drafts, of which four (EDs 49, 50, 52 and 53) have already been described. In May, ED51 'Accounting for Fixed Assets and Revaluations' was published. This project was designed to pick up some hot potatoes dropped by the reviews of SSAPs 6 and 12 and to fill in the gaps left by the pronouncements on goodwill and intangibles.[391] Some principles, adopted by the ASC to guide the working party in early 1989 were announced in its May *Report*.[392] The most important of these related to revaluations. Where companies used valuations, these were to be 'kept up to date'[393] and, for large companies, independently reviewed every five years. Permanent diminutions in value and profit or loss on disposal would be determined by reference to the revalued carrying amount. In addition there were

some uncontroversial principles about the determination of cost, a proposal that capitalization of interest (permitted by IAS23) be optional, and rules for the use of the revaluation reserve. The requirement to base profit or loss on disposal on carrying amount was a reversion to the treatment proposed in ED16 (in 1975) and the Discussion Papers on extraordinary items and depreciation, abandoning the alternative, depreciated original cost, preferred by ED36. It was coming to be known as the 'new cost'[394] approach, and was implicit in the banning of split depreciation by now implemented in SSAP12 (Revised).

A particularly complex feature of accounting for fixed assets, introduced (like so many other complexities with which the ASC had to struggle) by the detail of the new approach to financial reporting in companies legislation, was the subtle – even elusive – difference between downward revaluations and provisions for permanent diminutions in value:

> The law permits downwards revaluations to be taken to reserves to the extent that a previous revaluation surplus on the asset exists . . . Provisions for permanent diminutions in value must, on the other hand, always be charged against profit. So the name of the game here is to try to protect your profit figures by making a downwards revaluation three seconds before you are forced to provide for a permanent diminution. This is totally absurd of course – the ideal solution would be to amend the law so that provisions and downwards revaluations are treated alike and both debited to reserves if an appropriate surplus exists. This is the approach which appears to be adopted most often in practice, though usually without any acknowledgement that it is a departure from the detailed provisions of the Act.[395]

Actually, those who believe that current market value is the best estimate of future value might argue that the ideal solution is to abolish the artificial distinction between downwards revaluations and provisions for permanent diminutions in value.[396]

ED51 followed the principles unveiled earlier closely, but was timed to coincide with the publication of ED52 on intangibles. The document contained recognition criteria, derived from the IASC framework recently recognized by the ASC, and lengthy guidance on cost measurement which essentially followed generally accepted practice.[397] Capitalization of borrowing costs was optional, the arguments for and against being apparently 'finely balanced',[398] but a single policy had to be followed for all eligible assets. To prevent preparers employing the manoeuvre described above to avoid charging a permanent diminution against profit, a permanent diminution in an accounting period was to be deemed to have occurred prior to any downwards revaluation. Valuations were optional but, if employed, had to be carried out for the whole class of assets and follow rules on basis, frequency, and qualification of valuer. The revaluation reserve was to be kept 'in step' with the valuations of assets currently in use by transfers between the reserve and the profit and loss account. The ASC project

got no further and a new standard covering tangible fixed assets was issued by its successor only after nearly another decade and the publication of a further Discussion Paper and exposure draft.

In July, the ASC issued ED54 'Cash Flow Statements', proposing that the statement of source and application of funds, introduced by SSAP10 in July 1975, should be replaced by a cash flow statement, reflecting, among other things, developments in the USA and Australia.[399] This shift had been hinted at when a working party to review the standard was first established in 1983[400] but had to wait until the ASC's successor issued its first standard in September 1991.

The ASC's last exposure draft (last, that is in numbered sequence; two others were issued simultaneously) was ED55 'Accounting for Investments'. This project was added to the ASC's work programme in November 1988, following concerns expressed by a member of the ASC in September 1987.[401] In the aftermath of the deregulation of the financial services industry, market making and investment dealing activities, previously undertaken by entities not subject to companies legislation, were now being taken over by companies and, as a consequence, needed to be accounted for in accordance with the accounting rules in company law. It was a widespread practice within the sector to carry investments at current market value and to include changes in such value in profit, a method known as 'marking to market.' This seemed to make a good deal of sense in the context: valuations for publicly traded securities are readily ascertainable; though not received in cash, profits are 'there for the taking'; to use historical costs would enable management to manipulate the profit and loss for the period within very wide limits;[402] and if several deals in the same security have taken place at different purchase prices, the matching of actual shares bought and sold would be artificial and require new stock control systems where none were previously needed.

Unfortunately, the method fell foul of companies' legislation, possibly in two respects. The easier problem to address concerned the requirement that only realized profit be included in the profit and loss account for the period.[403] Since realized profit is defined in terms of generally accepted accounting principles,[404] what was needed was evidence that the method was indeed part of generally accepted accounting principles, evidence such as an accounting standard. The less tractable problem was that including investments at a valuation in the balance sheet was possible only under the alternative accounting rules, designed for current cost accounting, and these required gains resulting from revaluation to be carried directly to reserves (paragraph 34 in the Companies Act 1985).

The working party tackled the first problem by drawing on the argument that *realization* should be treated as an issue of reliability of measurement, so that traditional concerns with an exchange for cash or near cash[405] are best viewed as a proxy for reliability rather than constituting a separate test. Conveniently, a suggestion along these lines had recently been made in a research report for the ICAEW.[406]

Two possible approaches to overcoming the more serious barrier of paragraph 34 were explored. The first was certainly ingenious: profits would initially

be carried directly to reserves, then immediately released to the profit and loss account of the period, on the argument that the relevant paragraph allowed amounts to be released in this way where they represented realized profits. Unfortunately, the DTI were unwilling to accept that this device was lawful,[407] the department's lawyer arguing that the construction of the paragraph was such that it had to be interpreted by imputing an intention of Parliament that a second set of factors, beyond those resulting in the original accounting entry, would be needed to trigger the second.

That left the true and fair override. But this could be applied only in special circumstances. The DTI appeared willing to accept this manoeuvre as applied to the activities for which the problem actually arose, that is, market makers and investment dealers, but was not prepared to see it extended 'wholesale' to all entities with readily marketable securities.[408] Yet the ASC could see no defensible distinction between readily marketable securities held as current assets by investment dealers and similar holdings of other entities.[409] Further, the approach it was taking was, in the words of the ED, 'consistent with the object of the ASC to narrow the differences of financial accounting and reporting treatment between enterprises'.[410]

It was originally intended that the working party's final exposure draft would be considered by the ASC in May 1990, but pressure of business prevented this.[411] It was considered briefly in June and again during the final meeting in July. The drafts under consideration continued to bring readily marketable investments held as current assets by any entity to which SSAPs applied within the scope of the requirement to mark to market. The DTI representative at the meeting continued to suggest that the scope of the requirement be limited to dealers.[412] Eventually it was agreed that, in the words of the note of the meeting, 'given that the proposals are *merely* to be issued as an exposure draft, it would be sufficient to refer to the DTI's reservations in the Preface.'[413] Lest it be thought that demob fever made the ASC's last meeting irresponsible, it should be pointed out that the note records no fewer than 54 points of detail on the draft made by members and observers.

The ED was hailed by one commentator as containing 'an underlying conceptual rationale . . . that could be developed into a viable and practical general framework for financial reporting'.[414] The ASC's successor did not, however, pick up the subject, perhaps because of the legal minefield associated with it.[415] The practice of marking to market continued to be used, but mainly by dealers, often without disclosure of the use of the true and fair override. As one commentary puts it, 'this appears to have been industry practice for many years, but remains an unresolved and potentially contentious issue.'[416]

The End

The last meeting of the ASC was held on 25 July 1990. The meeting 'took note' of the CCAB's resolution to retire the committee with effect from 1 August.[417] Renshall admitted to 'shedding a tear'[418] in an interview with *Accountancy*, a

disclosure which the journal apparently viewed with some scepticism: borrowing a technique from *Private Eye*, it ran a photograph captioned 'Renshall: "Shed a tear"' but in fact showing Michael grinning from ear to ear, eyes twinkling. This mood, *Accountancy* attributed to the committee being able to pass the subject of goodwill, 'the hottest issue since inflation accounting', on to its successor, which met for the first time on 24 August.[419]

In each of the first four half-decades of the ASC's life, it issued between 10 and 13 exposure drafts;[420] in the last year of its existence, it issued a further 9, quadrupling its previous rate of output. This torrent was unleashed in part by the ASC's knowing that it would not be around to convert the drafts into standards; as Renshall said of ED47, 'we suggested amortisation ... knowing full well that it would be rejected.'[421] The circumstances do argue, however, that, at least as far as quantity is concerned, the constraint on the ASC's output in the previous twenty years was not its technical resources but rather its judgement about what was acceptable to its constituents.

The discussion papers, statements of intent, exposure drafts and standards produced in the final years were not the ASC's only output. Following the Watts reconstitution, the range of its pronouncements widened. A new series of Statements of Recommended Practice, as envisaged by the 1983 McKinnon Report,[422] was inaugurated in May 1986, with an Explanatory Foreword and two pronouncements, SORP1 'Pension Scheme Accounts' (following ED34 of April 1984), and SORP2, 'Accounting by Charities' (following ED38 of November 1985). It is not clear that these pronouncements, each of which deals with a special 'non-corporate' sector but applies universally within that sector, are quite what the working party had in mind; its report implies that SORPs would address specific topics relevant to the corporate sector but of limited significance.[423] The question of who should have the authority to issue SORPs, the ASC, the CCAB, or the individual CCAB bodies, became itself a matter of some dispute between the various parties.[424] Professor Edward Stamp[425] was unenthusiastic about the new documents: 'if this is a way of pigeon-holing a problem and allowing it to gather dust for years then this is a big step backwards.'[426] The series did not prosper and no further ASC SORPs, or exposure drafts of ASC SORPs, were issued.

Davison's belief that SORPs had an important role to play in accounting regulation[427] was better vindicated by the output of 'franked SORPs', that is pronouncements developed by working parties within an industrial sector and subsequently endorsed by the ASC, confirming that due process had been followed. From 1986 onwards, franked SORPs were produced by the oil and gas industry, the banking sector, the insurance sector, local authorities and universities.[428] A variety of approaches was taken: the university SORP provided comprehensive guidance on financial reporting for the sector; the local authority SORPs provided guidance on the application of SSAPs within the sector; and the profit-seeking sector SORPs gave guidance on individual industry-specific topics. ASC work on the public sector SORPs was undertaken by the Public Sector Liaison Group established in September 1983.[429]

August 1986 saw the publication of a revised version of the Explanatory Foreword to Accounting Standards, the result of a project undertaken by the ICAS on the ASC's behalf.[430] The revised Foreword,[431] which was circulated to the CCAB bodies but not exposed for public comment,[432] incorporated a number of amendments including a statement that standards were developed 'in the public interest'; an emphasis on the importance of 'having regard to the spirit of and reasoning behind' standards; and an explanation of the relationship between SSAPs and IASs.[433]

A working party under Hugh Aldous was set up in October 1986 to examine the application of standards to small businesses.[434] It concluded that 'there [was] neither reason nor demand to exempt small companies from applying existing standards while the present legal requirements for companies to produce meaningful accounts for shareholders continue.'[435] The ASC endorsed this conclusion but indicated that it would continue to examine the arguments for an exclusion for small companies on a case by case basis.[436] It established the criteria it would use in this examination in July 1988.[437] The methodology established in this release resulted in exclusions for small companies during the review of SSAP13 and the development of SSAP25.

Another general issue reviewed in the period was the treatment of taxation across the corpus of standards. This was undertaken jointly by the Chartered Institute of Management Accountants and the Institute of Taxation[438] because of, in the words of an ASC under-secretary, 'the old story of the ASC's lack of resources'.[439]

Last of all, the ASC issued its Final Report and Recommendation.[440] Most of the report is taken up by lists of ASC publications. The sole recommendation was that the ASC's records and files 'be made available to the Accounting Standards Board for its assistance in the continuing development of accounting standards'.[441] The report concludes: 'ASC welcomes the establishment of the Financial Reporting Council, the Accounting Standards Board and the Review panel and confidently entrusts the maintenance and development of accounting standards to the new bodies.'[442]

The title of this chapter poses a question; we will consider the answer in the next chapter, as part of a wider examination of the performance of the committee, the problems it faced, its responses to those problems, and the reasons for its demise.

11 Setting Accounting Standards 1969–1990: Technical and Political Realms

In his 1985 Julian Hodge Lecture, reflecting on his time as chairman of the ASC, Ian Hay Davison expressed his 'fear that continuing point-scoring between the six CCAB bodies will not only undermine the standing of the profession, as it has clearly done, but also undermine the work of the ASC'.[1] He described a particular dispute relating to the price change accounting debate,[2] but went on to say that 'such a regrettable attitude was all too prevalent during [his] period of office'.[3] He also recorded his regret that the arrangements for selecting members of the ASC introduced after the Watts report, involving the Bank of England and the Confederation of British Industry and designed to secure appointments made on merit rather than as a result of power brokerage within the Consultative Committee of Accountancy Bodies, had been abandoned.[4] Their abandonment, of course, re-opened another venue for point-scoring within the CCAB. Davison suggested that 'the solution to the problem may lie in giving the ASC the power to promulgate standards on its own authority like the FASB in the United States', but concluded, balefully, that he could 'see no likelihood of such a step being supported unanimously by our six professional bodies'.[5]

The following year, a commentary on the work of the ASC appeared in *Accountancy* under Peter Godfrey's name. The article was published in the September issue, Godfrey having retired as chairman of the ASC in the previous month.[6] He complained of the 'labyrinthine complexity' of the committees within the CCAB bodies which needed to approve standards: 'the nearest they get to synchronization is that they all take their holidays in August.' He explained that this caused, at best, delay, while 'the difficulties that arise if one or more committees or Councils tries to change a document while it is undergoing its tortuous process can easily be imagined.' He offered the parenthetical comment that, 'although the naive observer might expect the professional bodies to co-operate with each other, too often the relationships are adversarial and joint programmes such as accounting standards suffer as a result.' His solution? 'I believe that a strong case for allowing the ASC to issue accounting standards on its own authority can be made.' His proposal was designed not only to promote efficiency but also to make it easier to attract high-calibre members of the committee by demonstrating trust in its work.

Within the next twelve months, Michael Renshall became the third chairman of the ASC in succession to argue in public that the post-Watts structure was not working effectively and the first to do so while still in post. Speaking at the Institute of Chartered Accountants in England and Wales' 1987 annual conference,[7] Renshall focused on three issues: resourcing, inadequate enforcement, and the governance of the ASC – what he privately calls, 'the impossibility of managing six governing bodies'.[8] Publicly, he put it thus:

> The ASC should be empowered to issue binding standards on its own authority. This would remove an unnecessary and unfruitful delaying stage in the process. Now that the ASC is in its 18th year and has more than proved itself, its parent bodies should acknowledge that it has attained its majority.[9]

In fact, Renshall had already triggered drastic action. The ASC's recent budget submission to the CCAB had called for rather more than double the current level of resourcing, in order to increase technical staffing from four to eight. He asked for the extra money, 'without any illusion that the CCAB would provide it'.[10] On 6 July, in the closing days of Derek Boothman's presidency of the ICAEW, and therefore chairmanship of the CCAB, Renshall found himself in a taxi with Boothman, on their way to a meeting of the CCAB to present the ASC's report and budget. Boothman told him that the officers of the ICAEW and the ICAEW's secretary-general, John Warne, had decided to call for a major and independent review of the ASC; his budgetary demands had made this inevitable. Though the logic behind Renshall's call for additional resources was accepted, it was thought unlikely that the CCAB Councils would agree to it – and even more unlikely that, should they agree to it, they would be able to persuade their memberships that the additional funding was justified.[11] The recommendation had already been supported by an informal meeting of the office-holders and chief executives of the Institute of Chartered Accountants of Scotland, the Institute of Chartered Accountants in Ireland and the ICAEW and was accepted by the CCAB and announced immediately.[12]

The existing secretariat was over-stretched and, although the ASC was able to recruit high-quality staff, it remained difficult to attract and retain even the numbers funded in the existing budget. In addition, the complexity of the off-balance sheet financing project made some increase in staffing highly desirable.[13] However, the increased resourcing sought was based, not on any detailed analysis of forward workload,[14] but on a more strategic view:

> Extra funds would ... have allowed the secretariat more time for research and planning. 'We are always racing against time at the moment,' said one secretariat member. 'As a result we have to rely quite heavily on the six bodies to spot technical inconsistencies. If we had more time, we could rely on the bodies less, which might enable us perhaps to move out from under the CCAB's wing. It would also enable us to do a little more strategic

> forward planning so that we could see things coming and we wouldn't always have to work hand to mouth.'[15]

The bid enabled the ASC to confront the CCAB without complaining directly about its interference in the standard-setting process.

After some initial difficulty in finding a suitable chairman for the independent inquiry,[16] Sir Ron Dearing, the recently-retired chairman and chief executive of the Post Office, agreed to serve[17] and the committee was appointed in November 1987. Thus, as we have seen, for the last three years of its life, the ASC was operating in the knowledge that it was likely – eventually that it was certain – that that life would not last much longer. This knowledge actually had little effect on the commitment and morale of staff and working party members, who felt that they still had an important job of work to do and, on the whole, got on with it.[18] It does seem likely, however, that it affected how committee members were prepared to vote on the various documents issued during the period.[19]

Was the ASC's Demise Inevitable?

Accounting historians of the *longue durée* have demonstrated the more or less inexorable emergence, at least within Anglo-American-style market economies, of the key features of standard-setting machinery ushered in by the Dearing reforms – features such as independence from professional bodies, enforcement mechanisms with teeth, and substantial technical resources under the standard-setter's own control.[20] Tom Watts himself did not expect that the reforms he offered the CCAB would preserve the life of the ASC indefinitely; a profile on his retirement reported that 'his views on the long-term effectiveness of self-regulation keeping government control at bay are somewhat gloom[y]. "In any event, by the year 2000 we are going to be regulated by someone else," he prophesies.'[21] But whatever its long-term inevitability, was the radical reform of the standard-setting machinery heralded by the Dearing report bound to take place in the late 1980s?

Brian Singleton-Green's review of the life of the ASC,[22] published to mark its demise, argued that 'the accountancy bodies were swept along by forces that they were unable to resist',[23] attributing the fall of the ASC to its loss of self-confidence as a result of the price change accounting debacles; the adoption of free-choice standards, and in particular SSAP22 in December 1984 ('the beginning of the end for ASC');[24] an accumulating backlog of unresolved and complex topics, including pension costs, off-balance sheet finance and fixed asset accounting; and, finally, widespread abuse, and the publicity it was receiving in the emerging literature of denunciation.[25] Professor Geoffrey Whittington's review of standard-setting in the UK, published the previous year, took a similar view:

> The ... withdrawal of SSAP16, following substantial non-compliance ... resulted in a serious loss of confidence by and in ASC. This must raise doubts as to ASC's ability to deal adequately with such pressing matters as off-balance sheet financing ... Moreover, on a number of other issues, ASC

> has either failed to act or has seemed to be very anxious to avoid controversy by accommodating the needs of pressure groups. ASC's central problem is lack of authority, and some would add to that a lack of direction.[26]

Geoffrey Holmes, former editor of *Accountancy*, also commenting in 1989, spoke of 'a visible "loss of steam" in the 1980s'.[27] Indeed, in November of the previous year, an article had appeared in the *Financial Times* accusing the ASC of grinding to a halt.[28]

The ASC's failures in the area of price change accounting can scarcely have done its reputation or self-confidence any good.[29] In the later years of the saga, the continuing search for a standard seems to have been driven predominantly by historical momentum rather than any strategic calculation:

> It was the most important thing on its agenda, not because it was the issue at the forefront of people's minds in 1983, but because it had been the big issue in 1975 and it was just part of the ASC's historical inheritance ... [The committee] had this major project, inflation accounting, which was top of the agenda ... As long as there was a remnant of that project there, it had to be the most important one we had got.[30]

The ASC might be criticized for failing to seek out a more elegant escape route, although an alternative view is that its persistence provides 'evidence of the ASC's independence and desire to lead rather than follow popular opinion'.[31] But, whatever view is taken of the ASC's determination to solve the price change accounting problem, both the development process and the demolition work would have been a good deal more straightforward without CCAB politics.

Of greater significance in any evaluation of the ASC's performance in this area, however, is the consideration that its inability to maintain in place a standard on price change accounting simply placed it in the same category as all other major standard-setters world-wide; in other words, its record was merely unexceptional. There is no evidence of a long-term impact on the self-confidence of members of the ASC; as Desmond Wright puts it, they did not become 'gun shy' as a result of price change accounting,[32] not least because turnover on the committee brought in new members not directly affected by the debacles.[33] Members of the secretariat worked on their individual projects and their motivation was geared mainly to those projects; staff working on the price change project itself often enjoyed the technical and political challenges regardless of the outcome.[34] An indirect long-term effect of the price change accounting debate, of significance for the ASC, was to raise awareness of the possibility of resistance to standards, in terms both of accepting audit qualifications[35] and of calling general meetings of the professional bodies.[36] These factors are, of course, themselves related to enforcement and to the relationship between the ASC and the professional bodies.

The loss of nerve that resulted in the more notorious free-choice standards – most notably SSAP22 on goodwill – probably undermined both the ASC's

public credibility and its own self-confidence substantially more than the failure of price change accounting,[37] not least because here other standard-setters were able to hold a stronger line.[38] The speed with which members of the committee moved to show which choices they would like to remove, once it had become clear that the responsibility for doing so would not be theirs, argues for some sort of 'collective consciousness' that the previous documents were flawed.

The ASC's unwillingness to attempt to narrow areas of difference on some topics, such as goodwill, was directly related to the problem of enforcement:[39]

> With regard to the content of standards, a widespread criticism is that the ASC has, because of its weak enforcement powers, had to take a consensus view and has frequently changed its mind or made concessions to placate pressure groups. Examples of such cases have occurred in relation to the treatment of research and development expenditure, deferred taxation and investment properties.[40]

Unwillingness to adopt 'dramatically unenforceable' standards was so embedded in the culture of the ASC that it rarely surfaced as a subject of extensive debate; the constraint was accepted silently.[41] It is, of course, a sound principle of regulation that there is little point in adopting radically unenforceable rules, but such a principle inevitably constrains the shape of the rules to fit within what can be enforced; repeated failure to secure effective enforcement left the ASC badly exposed. The ASC's members (all acting voluntarily and thus employed elsewhere) were certainly susceptible to pressure from preparers – particularly those preparers who employed them or were clients of their firms.[42] Such pressure may have made ASC members even keener to accept the constraint of enforceability, and thus embrace free choice over goodwill, for example, than a rational analysis of the enforceability problem alone would have done. Put simply, it spared them difficult conversations back at the office.[43]

It would be possible to criticize the ASC for failing to engage more seriously with the problem of enforcement. Although the view that it was 'someone else's problem' was constitutionally correct – and a highly attractive one considered in the context of the 'art of the possible' – it overlooked the intimate link between enforcement, effective standardization and the credibility of the ASC. It seems unlikely, however, that by attending even more seriously to the problem, the ASC could have achieved a great deal by itself. Watts had come close to crafting an effective enforcement mechanism in 1981. Whether the proposed joint panel would ultimately have come to fruition cannot be known; any chance of finding out was destroyed by internal CCAB squabbling.[44] Davison did not pursue the issue further, judging it to be 'part of the CCAB problem'.[45] Subsequent efforts by Godfrey and Renshall were pursued by means of 'quiet diplomacy' within the CCAB. Would a more public strategy have been more successful – or should we view the last campaigns as part of the argument for the more radical step the outcome of which was the Dearing committee?

Although the ASC's budget was undoubtedly kept tight by the CCAB, the level of staffing in the late 1980s was not about to cause a major breakdown in the technical work programme – witness the final flurry of documents – and there was always work to be done at the monthly meetings of the committee.[46] Resourcing for a full-time chairman might have improved the quality of the production process and enabled the ASC to focus more clearly on 'higher order' issues such as enforcement, liaison with interested parties, recruitment to the committee and the promotion of the standard-setting programme generally, but it is difficult to demonstrate that the outcome would have been substantially different, given, among other things, the difficulty in bringing the CCAB bodies into line behind the committee's actions. A major expansion in the budget might, however, have had two beneficial effects beyond those listed by the secretariat member quoted earlier.

While the staff of the secretariat were technically very able they were also young and had limited experience of the business environment surrounding the problems they were addressing. Any deficiencies in their experience and insight were counterbalanced by the input of the volunteer members of the technical working parties and, in particular, the working party chairmen. This was usually of very strong technical merit and based on extensive and relevant experience but the resulting power for the working party members greatly increased the potential and perceived opportunities for working party members to pursue interests which might cut across the professional and public responsibilities of the ASC. There is little evidence of the pursuit of naked and direct self-interest in practice. Although, for example, it could be argued that a working party's willingness to countenance free choice might have been a function of its members' sense of self-preservation in the face of the strong demands of their employers and clients, there is, again, no evidence that a working party with a strong conviction towards narrowing areas of difference could have driven through the main committee a document with fewer free choices than those actually adopted. However, a better-paid full-time secretariat, with at least the potential for recruiting more mature and experienced staff, might have either actually secured a reduction in free choice or, at any rate, demonstrated that the problems in doing so were insurmountable within the constitutional framework of the ASC. An alternative is that such a secretariat might, by raising the profile of the issues involved, without solving them, have undermined the political credibility of the ASC sooner and more thoroughly. Paid staff time is also, of course, easier to manage, so that the pace of projects would have been less vulnerable to the exigencies of the working party chairman's work commitments – although, again, there is little evidence of major problems here.

A second benefit of a larger staff might have been to make it easier to justify separating the secretariat from the ICAEW, thereby perhaps improving relations with other CCAB bodies and raising the morale of those who saw themselves as involved in an unnecessary tug-of-war. Of course, the larger budget would itself, no doubt, have imposed additional strains on CCAB relations.[47]

Though the independence of the post-Dearing machinery has undoubtedly been useful in demonstrating that its output is less susceptible to the pursuit of the vested interests of the profession, there was actually little criticism prior to Dearing that the profession was exploiting its position in this way. It was not often suggested, for example, that the profession was using its powers of veto to secure accounting policies that satisfied its own interests rather than those of other constituents, or that resources for the ASC were deliberately restricted to undermine its capacity to develop standards that might conflict with the profession's interests. As we have seen, three successive chairmen of the ASC urged that it be given independent authority to issue standards simply in order to avoid the debilitating effects of continual CCAB squabbling.

The catalogue of problems caused by the inability of the CCAB bodies to agree among themselves seems almost endless. Disputes over staffing, the budget, enforcement, constitutional arrangements, and the technical programme, have formed a major theme in this book. In the closing years of the ASC's life, the Department of Trade and Industry and the Bank of England were signalling concerns about the committee's work,[48] and the exclusion of outside parties, including the Bank of England, from the committee nominating members of the ASC cannot have helped. There were disputes about membership of the committee and, on one occasion, the Chartered Association of Certified Accountants held up approval of two candidates to fill unexpected vacancies on the grounds that its President and Vice-President were out of the country, although it was able to hold a Council meeting, chaired by the Deputy President. As a secretariat note waspishly put it, '[the Deputy President] and [secretary] between them have sufficient authority to hold the Council meeting, but apparently have insufficient authority to approve two nominations to ASC.'[49]

When Godfrey was appointed chairman of the ASC he was also made a member of the ICAEW Council in his role as chairman of the ASC – a move he came to regret as signalling too intimate a relationship between the ASC and the ICAEW.[50] As well as affecting staffing levels, CCAB politics affected key appointments, including the decision to appoint a Director of Accounting Standards which itself poured petrol on the flames of CCAB relations,[51] while the decision to recruit Singleton-Green back to the ICAEW secretariat at the point at which a new chairman was playing himself in was unfortunate – at least as far as the new chairman was concerned.[52] Even rooming became a matter of CCAB politics – one of the most contentious decisions taken by Davison was to move meetings of the ASC to Lincoln's Inn Fields, the headquarters of the ACCA, because it had a meeting room more suitable for the size of the ASC and the style of its deliberations.[53] Their perceived domination by the ICAEW affected the morale of some ASC staff.[54] Keith Robinson recalls that it made it very difficult for him as the secretary of the ASC to know who he was answerable to.[55] There were even spats about the logo to be used in staff advertisements[56] and whether the cost of printing was being borne equitably.[57]

If the accounting profession was in the grip of irresistible forces, then, they were not pressing in on it from outside – rather they sprang from its utter inability to control its own internal feuding. As Davison puts it:

> We were a committee of the CCAB, which was an unwieldy body in many ways and consisted of the [English] Institute 'lording it' and all the other five bodies sniping – that's really what it consisted of. The Institute was very inefficient at lording, so they didn't in fact score many points to their own advantage and the others measured their progress largely by the spots they could knock off the Institute.[58]

Some of those involved see this internecine warfare as part of the long shadow of the failure of the 1970 integration scheme, lost by the vote of members of the ICAEW: 'the motto of the five smaller bodies [then became] the reverse of the conventional nostrum, "if you can't beat them, join them".'[59] However, this failure can itself be seen simply as another example of professional body rivalry:[60] only after 1970 did the interlopers develop the muscle to stand up to the ICAEW, and when they did, they exercised it. If there is cause for optimism about professional relations to be derived from the history of the ASC, it is in the remarkably cordial, co-operative and productive relationships between members of the different CCAB bodies that predominated in the technical work of the ASC itself and especially its working parties; it was only the other things that got bogged down in the rivalry, but those other things were vital to the standard-setting process.

One measure of the consequences of CCAB politics is the extent to which the Dearing reforms were pre-figured in the Watts recommendations: greater involvement by outside institutions in appointments; better (some) enforcement mechanisms; better resourcing and a remunerated chairman; exploration of the potential for a conceptual framework.[61] Had the CCAB bodies been able to implement Watts' (implicit) recommendation that they manage their veto by objecting before, rather than after, a draft standard was ready for approval, a good deal of subsequent trouble might have been avoided. But the CCAB bodies were unable to stomach the prescriptions Watts offered without the sugar coating of an independent review, and, perhaps, the powerful motive of outside funding.

It is surely inappropriate to characterize the ASC, its members, secretariat and working parties as losing steam. To the end, they had the appetite to do the work, the capacity to produce the documents, and the insight to say what was needed to narrow areas of difference – even if, arguably for lack of an enforcement mechanism, they did not always have the will to put their names to pronouncements that would carry this into effect. When Whittington referred to the ASC's 'lack of direction',[62] he apparently meant a lack of agreed technical objectives and of coherence in and between pronouncements, since the remedy he examined was the Solomons Report,[63] which proposed guidelines for reporting standards related to the conceptual frameworks of the FASB and other standard-

setters. In fact the ASC was beginning, in the very last months of its life, to edge towards acquiring a conceptual framework, via its recognition of the IASC version,[64] and to use a conceptual approach in tackling off-balance sheet financing[65] and explaining its proposed change in the treatment of goodwill.[66]

If we carry through the railway metaphor, what the ASC was losing, and losing in a serious way, was not power but traction: it was losing its grip on the increasingly steep track it was attempting to climb. Partly as a result of changes in the business and economic environment,[67] the problems that the ASC faced were becoming technically much more complex and politically more controversial – off-balance sheet financing being the most obvious example.

The connection between financial reporting and company law was creating further complexities,[68] hardly imaginable at the time the ASC was created; as one commentator discussing the new legislation put it at the beginning of the 1980s, 'the ASC [is] in chains: whither self-regulation now?'[69] Further, as company law grew more prescriptive, it opened up new ground for argument, for example it became possible to argue that what the law permitted, such as last-in-first-out, the ASC could not ban.[70] The problem of the lack of an effective enforcement mechanism may not have been getting worse but, as the ASC faced difficult issues it could no longer duck (such as goodwill), as well as the increasing ingenuity of preparers and organized lobbying (such as that from the Equipment Leasing Association), the difficulties caused by weak enforcement become more and more visible.

Additional pressure on standard-setters arose from structural changes in the audit profession.[71] The ever-increasing size of the firms dominating the profession created greater demand for systematic procedures – to co-ordinate teams; to ensure consistent treatment of clients and thereby avoid complaints from those dealt with less 'generously'; to defend actions before the courts. Individual firm 'rule books' can be developed more easily where few judgement-based decisions are required. As competition in the market for professional services grew fiercer, firms increasingly felt that if they were to resist the demands of a client, it would be necessary to show a specific rule that precluded the treatment the client desired. These pressures created a demand not only for greater provision of detailed rules in standards, but for standards of more comprehensive scope, dealing with all possible situations. At the same time, competitive pressures were weakening the coherence of the profession, and thus the professional bodies' ability to secure consensus on major issues such as accounting standardization or the increased funding necessary to expand activities.[72]

A further source of 'technical pressure' was the globalization of industry, increasing demands for co-ordination between key national and international standard-setters.[73] Though the arguments for such co-ordination are strong, its achievement is usually technically and politically demanding and resource-hungry, as we saw in the case of foreign currency translation.

One countervailing force was the increasing sophistication of the technical branch of the profession (technical partners and staff in audit firms and a – still

very small – number of specialists within industry), manifesting itself, among other ways, in some highly technically literate members of the ASC. But this development in itself had only limited potential to offset the technical, organisational and political challenges confronting the committee.

At the end, when the CCAB bodies should have been providing extra locomotion to cope with the increasing gradient, they just could not bring themselves to pull together. The timing of the CCAB's initiative in establishing an external inquiry reflects the dawning of an awareness that standard-setting now needed more support – financial and institutional – than the CCAB bodies collectively could be persuaded to provide, together, perhaps, with an impatience with the organizational effort needed to keep the show on the road in the face of CCAB politics. External forces provided the context but not the immediate impetus. Had the CCAB bodies brought themselves to give one more shove to the old machinery – more resources, more (some?) discipline about the exercise of the veto – they might well have retained their role in UK standard-setting for a few years more.

How Effective was the ASC?

One would have to be a very determined advocate of unregulated markets in financial information[74] to argue that the ASC's work, over the twenty-one years of its life, did not significantly raise the quality of British corporate annual reports. In view of the potential for improvement in 1969, the pressures on the accountancy profession to do something, the precedents available from elsewhere (predominantly the USA), the resources the profession devoted to the task (including volunteers' time), and the timescale over which the machinery operated, it would have been a quite extraordinary outcome if the ASC had not managed to secure substantial improvement. The more difficult question is how the degree of improvement actually secured compares to what could reasonably have been expected, given the structures and resources the ASC was working with and the constraints imposed upon it. Some constraints were imposed from outside the profession – for example, the approach to financial reporting introduced by the company law harmonization directives and the unwillingness of the government to respond to calls for standards to be given legal backing. Some constraints were imposed by the profession itself, most notably the CCAB body vetoes, but, whatever view one takes of the profession's role in imposing such constraints, we can scarcely blame the ASC itself.

By the ASC's own yardstick, its *volume* of output appears disappointing. The initial work programme envisaged exposure drafts on 20 subjects in five years, which should have yielded 20 standards within about seven years: three per annum. Had the committee been able to keep this pace up (and had there been sufficient topics available), it would have produced some 60 standards by the end of its life. In practice it produced only 25, about 1.2 per annum, not substantially different from the rate of output of the earlier series of recommendations.[75] The ASC's performance was, however, approximately in line with a

more realistic yardstick, the US Accounting Principles Board's average work rate at the time the ASC was established, 1.5 per annum.[76]

But what of the quality of the ASC's pronouncements? The original Statement of Intent contained only one objective referring specifically to the results to be achieved by the generality of accounting standards: 'narrowing the areas of difference and variety in accounting practice'.[77] Neither the objects clause nor the terms of reference in the ASC's constitution enlarged on this goal.[78] Interpreted strictly, then, the committee's objective did not require it to seek out *better* accounting methods, nor even the best currently in use – it merely had to endorse fewer methods than it found in use in any particular area, and preferably only one. Viewed from this perspective, the criticism sometimes made that the ASC merely sought out the most popular method and adopted it would be misconceived: that is what it was charged with doing. The only other objective in the Statement of Intent referring to the results to be achieved by standards was to secure disclosure of accounting policies. This was done by SSAP2, which certainly secured a 'significant and permanent change'[79] for the better, though the degree of change can be criticized.[80]

The provisions of SSAP9 relating to stock might be regarded as a classic example of the 'narrowing areas of difference' approach: the more *outré* variants – base stock, cost untested for recoverability – are outlawed, leaving all the more popular policies available. In defence of the ASC, it must be pointed out that other standard-setters have found themselves similarly unable to eliminate all difference in this area. The provision requiring inclusion of overheads in the carrying amount of stock did adopt the most popular approach then used, at any rate by large companies, but nearly a third of preparers had not previously followed this policy and this aspect of the standard proved controversial.[81] In its requirements relating to long-term contracts, SSAP9 did not simply fall back on permitting all methods used by a significant proportion of preparers; it would appear that companies split about half and half between the percentage of completion and the completed contract methods[82] and the ASC came down on the side of the better method, as judged by standard-setters around the world. Again, the provision proved controversial. The ASC was willing, even very early in its life, to confront significant proportions of preparers in order to pursue what it saw as improvements in quality. Indeed, the very first standard actually adopted a method that was used by only a small number of the largest companies.[83] SSAP9 also secured significant improvements in the volume of detailed information disclosed.[84]

In some areas, improvements were secured by innovative measures, such as the disclosure of earnings per share and the funds statement, though in the latter case the degree of flexibility permitted probably led to an increase in discord where previously silence had prevailed. In some cases, areas of difference were narrowed whilst leaving scope for considerable variety to remain, as with accounting for pension costs and the treatment of extraordinary items. In some cases, as with segmental disclosure, reporting was pushed beyond previous practice while, again, leaving scope for variety. Sometimes, as in the case of

extraordinary items and, perhaps, depreciation of property, some remaining variety was a consequence of real technical difficulties in grappling with slippery concepts rather than a failure induced by the politics of the process.

Over its lifetime, the ASC issued a number of standards embodying free choice at a fairly fundamental level. The reasons behind the decision to tolerate free choice differed from case to case. SSAP11 on deferred taxation permitted both the liability method (the most popular) and the deferral method, apparently in the interests of consistency with US practice, which required the latter.[85] SSAP13 permitted qualifying development expenditure to be capitalized or written off, the former being quite possibly the better policy but one without a great deal of support outside specific sectors, where its attraction was that it offered cash benefits rather than that it represented better reporting.[86] The most egregious instance of free choice permitted by the ASC was undoubtedly the treatment of goodwill; the optional use of merger accounting would probably have received less criticism if it had not been so closely linked, chronologically and functionally, to the goodwill decision. In this case the motive seems to have been a mutually reinforcing combination of (arguably quite proper) concerns about radical unenforceability, and its effect on the credibility of the process, together with (rather less proper, but perhaps understandable) personal failures of nerve caused by an awareness of the political interests of ASC members' employers and clients; which of these considerations predominated is probably unknown even to those who voted. In defence of the ASC, it must be pointed out that these topics caused enormous difficulty and controversy elsewhere; it was these topics, more than any other, that were responsible for the demise of the APB in the USA.[87] What purpose would have been served by the adoption of a standard that was widely ignored? It might, perhaps, have brought about reform of the standard-setting regime a little earlier than in fact occurred, but it is debatable whether it was the ASC's job to achieve this.

The standards dealing with goodwill and merger accounting also included provisions which supported, apparently deliberately, what might be called *engineered choice*. In the case of goodwill, companies were offered the opportunity to identify intangibles separately and apply policies different to that used for goodwill.[88] The merger standard defined a merger in terms of the flow of funds rather than the substance of the enlarged entity and effectively enabled combining companies to structure the financing of a combination to qualify as a merger, when operationally it was an acquisition.[89] By thus appearing actually to support creative accounting, the ASC damaged the credibility of its commitment to improving financial reporting.

The standard on leasing revolutionized financial reporting in the UK, both in the way in which leases themselves are accounted for and also, much more widely, by introducing innovative, substance-based, accounting methods generally. It is possible to criticize both the time it took to adopt the standard and aspects of its detailed content, including, most significantly, the 90 per cent rule. It is also possible to argue that, in the context of the nature of the issue, the scandal prompting its consideration, and parallel developments in the USA, the

ASC deserves only limited credit for standing its ground, simply because it could do nothing else. But this is an ungenerous view; the standard was both an important technical achievement and a triumph of the resistance of political lobbying – albeit one won by a war of attrition rather than glorious battle.

In its work on developing substance over form via the leasing standard, and its crafting of recognition criteria for development expenditure in SSAP13,[90] the ASC can be seen as groping towards the conceptual framework that the committee was so reluctant explicitly to seek out. Some of the more abstract argumentation in the later stages of its work on goodwill also served to assist in the explication of fundamental terms, though with little consequence for the ASC's own standards. This work, and particularly the leasing standard, must have had a major influence on the way the parties to the financial reporting process came to view the transactions being undertaken – that is, on the social construction of the financial accounting world. Other standards, such as those on funds flow and segmental reporting, must also have significantly influenced the way users (and, perhaps, preparers) of financial reports think about the entities with which they are concerned.

One major advance which the ASC was not, ultimately, able to bring off was the secure adoption of current cost accounting. Some criticism can be made of the committee for a false start and for various tactical blunders along the way, notably the attempt to launch the system in comprehensive, detailed and elaborate form, with the threat of universal application from the outset. In most of the mistaken moves, others besides the ASC were also implicated. The attempt to build a comprehensive system from the outset, for example, was heavily influenced by the recommendations of the Sandilands committee.

Did the ASC bow unacceptably to external pressure from preparers and others? Two quite clear-cut cases of the success of 'political interest' lobbying are research and development expenditure[91] and the 'sudden *volte-face* on deferred tax'.[92] Such lobbying violates due process and a powerful case can be made for a standard-setter's duty to ignore all activity of this sort, although we must beware of imposing today's expectations of good governance on the ASC of the 1970s. In defence of the ASC, it can be said that in both cases there were well-founded technical rationales for the moves: the nature of the tax regime to be accounted for had changed and capitalizing qualifying development expenditure has come to be seen as the superior policy. In neither case was the outcome egregiously 'bad accounting', unlike a number of chapters in the history of standard-setting in the USA, including those dealing with investment credits,[93] marketable securities[94] and stock options.[95] The ASC might, certainly, have moved to its final positions with more elegance, and thereby avoided some of the criticism it attracted because it 'reacted to pressure by changing the whole tenor of particular exposure drafts and standards',[96] though, again there is a defence that it was still learning its tradecraft.

In other areas, the ASC was able to resist the pressure of vested interests, at least on the larger questions, or to manage them so as to limit the damage they caused. Capitalization of leases was won in the teeth of lobbying by the Equipment

Leasing Association, although minor concessions to the representatives of the ELA were made in the development of the standard[97] and the method of lessor accounting selected from the inception of the project was the one favoured by the ELA.[98] Interaction between the political and technical dimensions of standard-setting sometimes made it difficult to respond effectively to vested interests; it was one thing to know that preparers were behaving inappropriately in resisting charging depreciation on property, but another to craft the standard that would overcome this resistance without catching inappropriate cases, and do so under the enforcement regime then in operation.[99] Political pressures on the development of the foreign currency translation standard certainly impeded its progress and resulted in concessions in areas such as the rate to be used in the profit and loss account and the application of the cover concept.[100] Arguably, delays in the adoption of the pronouncement, caused in part by political manoeuvring, resulted in better fundamentals, avoiding at least overt free choice, in an area in which determining the conceptually strongest method remains highly problematic.

A major advantage for the ASC was the substantial impetus built up in its early years, not least by the astute political and technical management of Sir Ronald Leach and Renshall, who themselves had the major tactical advantage of surprise – of getting the machinery, and some pronouncements, in place before many in the community knew quite what to expect. The personal efforts of the volunteers who bore the heat of both technical development and political manoeuvring, principally working party chairmen, went a considerable way to overcoming the limitations of the formal budget. The committee was able to attract very able young technical staff to a novel form of professional activity, though recruitment and retention were always precarious.

Whether by astute succession management or good luck, the ASC was remarkably well served by its chairmen, each of whom brought to the job the combination of skills and personality needed at the time of their appointment: Sir Ronald Leach, with his enormous professional stature and political acumen to launch, if not a revolution, then at least a radical programme of change; Sir William Slimmings to continue in the same vein and provide, if only on a limited scale and for a limited period, a sense of co-operation across the profession; Tom Watts when technical mastery of complex issues, a consensual approach, and huge patience were needed; Ian Hay Davison to drive through what limited change the profession could bring itself to contemplate with energy, imagination and considerable forcefulness; Peter Godfrey to return to consensus-building and keep things ticking over during an unpropitious period; and, finally, Michael Renshall to keep the show on the road in the face of very considerable challenges on all sides, and to maintain staff morale and volunteers' commitment in the shadow of Dearing, which he did with patience, modesty, technical and diplomatic skill and benign good humour.

Viewed from the perspective of the political economy of the accountancy profession, Leach's radical experiment in institutional co-operation and interference with professional freedoms postponed the end of the self-regulation of

financial reporting methods beyond the point in time at which the government's patience would otherwise have worn out. This was regarded as an important goal by many members of the profession, though some may well have regarded regulation by the ASC as little better. It is ironic, since Leach's original scheme included a programme of auditing standards, resisted by the ICAEW Council,[101] that the reform may also have assisted in postponing the end of self-regulation of auditing.

The professional bodies willed the ends (in terms both of improved financial reporting and of professional self-discipline) but were reluctant to will the means, providing minimal levels of resources, exhibiting little sympathy for a rational and rigorous, conceptually-driven, approach to the specification of accounting standards, and rarely resisting the temptation to interfere even when little of fundamental importance was at stake.

Within the constraints of its constitutional position and resourcing, and necessarily working within British professional traditions of conservatism, pluralism, pragmatism, incremental change, voluntary service, 'professional generalism', back-room dealing and distrust of the abstract, the ASC punched well above its weight for most of its life, contributing more to the improvement of UK financial reporting than the profession that supported it, pretty grudgingly most of the time, was entitled to expect. In doing so, it went well beyond its original remit to narrow areas of difference, in addition seeking out better methods and innovative disclosures.

The outcome of its endeavours fell well short of perfection for a number of reasons, of which the technical difficulties of determining which is the most useful accounting method in any particular context should never be overlooked – though the ASC's disinclination to arm itself with even the limited power of a conceptual framework did not help. One of the most important lessons that a detailed study of the history of the ASC has to offer is that the underlying events to be reflected in financial statements, combined with technical limitations of the financial reporting process imposed by its very fundamentals,[102] make the financial reporting world sometimes difficult to get a grip on, so that failure to do so effectively does not necessarily always result from technical short-sightedness or political weakness. Gross defects in the enforcement regime presented a choice for the ASC between setting demanding standards that would be widely ignored or moderate standards that would be likely to be followed; the former make heroes of standard-setters but the latter may achieve greater improvements in financial reporting.

Lessons for the Future?

A. J. P. Taylor famously argued that, since history does not repeat itself, there are no lessons to be learnt from its study, the only point of which is 'fun'. This level of scepticism is not widely shared by historians and, indeed, was not consistently adhered to by Taylor;[103] a more balanced view is expressed by Professor Richard Evans, who argues that, although,

> history cannot create laws with predictive power[,] an understanding of the past might help in the present insofar as it broadens our knowledge of human nature, provides us with an inspiration – or a warning – or suggests plausible, though always fallible, arguments about the likely possibilities of certain things happening under certain conditions.[104]

Professors Gary Previts, Lee Parker and Edward Coffman put the point this way: 'in accounting, as in other fields, knowledge of the past provides a prologue to understanding contemporary matters.'[105]

Accounting standard-setting for the UK now takes place within an institutional framework quite different from that within which the ASC operated. The post-Dearing regime was funded on a different scale and was much further removed from the direct influence of professional accountancy bodies; even more importantly, standards were recognized in law and much more effective enforcement mechanisms were available. This regime, however, itself lasted only 15 years or so and the machinery has once again undergone radical transformation. Since 1 January 2005, quoted groups of companies have been required to follow, not the British Financial Reporting Standards developed by the post-Dearing regime, but International Financial Reporting Standards developed by the International Accounting Standards Board (at the time of the handover, ten pronouncements, a third of the then-extant total, survived from the ASC's output).[106]

These changes in the context of UK financial reporting, together with even mild scepticism towards the repetitiveness of historical events, argue for considerable caution in attempting to read the lessons of the ASC's history across to the work of accounting standard-setters in the second decade of the twenty-first century. It might also be though to be something of an impertinence to doubt that those who operated the post-Dearing machinery, many of whom had had experience of the ASC's work, were fully aware of the lessons to be gleaned from the earlier period and, indeed, passed them on. Nonetheless, one lesson of history is that, as time passes, the lessons of history may be forgotten, especially if they are not sufficiently well recorded. In this spirit, this final section offers some suggestions about the implications of the ASC's experience for future standard-setters.

I begin with lessons relating to the technical construction of standards. As far as is reasonably practicable, standards should function acceptably under all reasonably foreseeable conditions, and standard-setters should put in some effort, during the construction process, to predict what alternative circumstances are likely to occur, and to test draft pronouncements against those circumstances. Such 'proving' might have avoided, for example, the difficulties associated with the *volte-face* on deferred taxation and the 90 per cent rule in accounting for leases.[107] This prescription is to be distinguished from an attempt to deal comprehensively with a wide range of related issues, such as that which contributed to the ASC's difficulties over price change accounting.

The second lesson, which is linked to the first, is to beware of the temptations of 'bright line' solutions. These will be attractive to auditors,[108] who are a vocal

pressure group and, in a volunteer-based system, an essential source of technical support, but generally store up trouble, as with the definition of an associate, the 90 per cent rule for finance leases, and the first ED on research and development. This is the sort of lesson which deserves to be set down explicitly because, as standard-setters rely increasingly on conceptual frameworks which lead naturally to judgement-based tests, the difficulties caused in the past by bright line solutions may be forgotten, making it likely that they may be tempted to react to a particular difficulty by reaching again for such a tool.

Thirdly, beware of allowing technical content to be driven by a knee-jerk reaction to a past scandal. Writing off all development expenditure was an over-reaction to the Rolls-Royce case (even leaving aside the mitigating circumstances of that case). Capitalization of leases, on the other hand, was an appropriate technical prescription regardless of Court Line.

Fourthly, standard-setters should avoid the temptation to provide ingenious escape routes such as the engineered choices in SSAPs 22 and 23; they do their craft no credit and will surely come back to haunt them.

Fifthly, as far as possible, an exposure draft should test the detail, not, as with ED14 on research and development expenditure, the principle. A change of direction may be a logically justified outcome of exposure but it is unlikely to be seen as reflecting well on the standard-setter, except, for the wrong reasons, by those whom the change favours. This is probably true whether or not the change is itself technically sound or an improvement; the exclusion of investment properties from the scope of the depreciation standard was a move which, if it was going to be done at all, would have been better done early. That this lesson has been well-learned is evident by the use of preliminary Discussion Papers even in the later period of the ASC.

Would the ASC's technical performance (or life) have been improved if it had moved with greater speed towards embracing a conceptual framework? It is difficult to demonstrate that the frameworks available at the beginning of the third millennium would, even had they been available in 1970, have led the ASC easily to widely accepted and enduring standards for some of the less tractable technical problems it faced, such as deferred taxation[109] or goodwill.[110] On the other hand, a conceptual framework would have clarified arguments, for example about whether items were not to be recognized because they were not assets (or liabilities) or because they could not be measured reliably, and thus enabled the ASC to move with greater confidence, and provide a stronger technical rationale in cases such as qualifying development expenditure and goodwill. Had a conceptual framework been adopted earlier, and with more enthusiasm, the ASC's attempts to deal with off-balance sheet financing by resorting to fundamental definitions would have carried rather more weight. Equally, the capitalization of leases could have been justified by reference to the framework's definition of an asset rather than leaving its advocates to begin the defence by arguing for their version of the definition of an asset. Indeed, economic substance might have been embraced more widely by the ASC had a conceptual framework been in place. It would also have helped the ASC to

develop standards that were consistent with each other and to demonstrate that consistency or provide good technical reasons for any apparent inconsistency.[111] Again, a conceptual framework might have enabled the ASC to explain to the world, and especially to its critics, what it was doing in ways that were defensible in technical terms and looked less like ducking and weaving.

The temptation towards frivolousness is difficult to resist. Lessons for the young standard-setter: 1. Get in early, while there are still simple problems to be solved; 2. Avoid working during periods of inflation; 3. Compose and motivate your committee so as to avoid swing voting leading to technically arbitrary reversals in decisions;[112] 4. Put off dealing with goodwill and mergers for as long as possible. Actually, even these points, though they appear flippant, perhaps carry weight. Certainly, Leach and Renshall made excellent use of the honeymoon period. Subsequent standard-setters will, and have, encountered more knowing constituents, and it would be wrong to conclude that the lesson is to use the honeymoon to speed through as many pronouncements as can be developed. It may be better to use the period to solve a small number of profound problems or develop and adopt a conceptual framework; the lesson is to use the combination of goodwill (in the non-technical sense) and ignorance to maximum effect before they evaporate.

The lesson from ED3 (merger accounting), SSAP22 (goodwill), and SSAP24 (pensions) – documents that span the committee's life – is to avoid issuing a pronouncement before you are confident of its quality just because there is pressure to do something. As Storey puts it, 'Accountants who cry for action – any action, so long as it is action – are endangering future progress as much as those who cling tenaciously to the status quo.'[113]

Some forceful and, in their own terms, persuasive attempts have been made to glean lessons from particular chapters in the price change accounting debate; a good example is Chris Westwick's analysis of the period to 1980, which is, indeed, specifically designed for this purpose.[114] However, the comprehensive failure of all the different approaches attempted by the ASC and fellow standard-setters around the world makes it difficult to be confident quite what lessons can be learned. For example, Westwick includes in his list of lessons: acting too slowly; failure to study company and overseas practice; the attempt to provide a comprehensive solution; failure to educate and persuade constituents; insufficient research; inflexibility; and failure to provide explicit reasoning for positions. Subsequent phases in the ASC's search for an acceptable pronouncement surely learnt these lessons, at least to some degree, yet were hardly more successful. (Of course, it is always possible to argue that, for example, with yet more education, constituents would have been more positive.)

The remaining items on Westwick's list are: lack of clearly articulated demand from users; failure of government backing; lack of a defined goal (conceptual framework); and need for more resources. Although all subsequent pronouncements were developed with fewer resources than available for the period about which Westwick was writing, the cumulative effect of technical development work must go some way to offset this problem. It is difficult to believe that a better-

resourced secretariat, working with an explicitly adopted conceptual framework, could have overcome the level of opposition subsequently encountered by the ASC. But Westwick's list surely contains at least this fundamental truth: price change accounting is most likely to be adopted in stable form when influential users demand it and the government of the day backs it.

Operationally, the quality and size of the technical secretariat is certainly important, but perhaps the best advice that can be offered is that the constitution and budgetary arrangements for the standard-setter should be structured so that staffing matches current technical demands, neither undermining progress by shortages or poor quality, nor leaving an over-sized 'permanent staff', under-employed or justifying their existence by producing excessive regulation. It must be emphasized that at no time in the history of the ASC did the latter occur, but, if the secretariat was short-staffed, this was in part because of a fear, justified or otherwise, that it might come about. Achieving this balance is not easy; in particular, the superficially attractive device of using young staff on short-term appointments and secondments may limit the secretariat's 'craft skills', technical and political insight, folk memory, and commitment to the quality of the process. And, of course, a young, 'unseasoned' secretariat will not be able to provide a counterbalance to the political and time pressures on a part-time, voluntary committee and working party members.

One observation from the history of the ASC so nearly constant that it is tempting to offer it in rebuttal of the assertion that history cannot identify laws with predictive power is that standards take longer to develop than standard-setters expect. From this it follows that, despite the temptation to win applause by announcing stretching targets, standard-setters who wish to avoid derision[115] should propose realistically pessimistic work programmes.

As will be apparent to all readers of this volume, if the members and staff of a standard-setting body maintain a frank and open relationship with the press, it is of enormous benefit to the accounting historian, and, for this reason, I make the following suggestion with some regret. The degree of candour exhibited by the members of the ASC and its staff at times certainly suggested, perhaps revealed, and perhaps, indeed, contributed to, a sense of loss of pace and direction.[116] A more circumspect approach might have produced better public relations.[117]

A key feature of the regime within which the ASC operated was weakness in powers of enforcement. In the face of widespread non-compliance, or threats of non-compliance, the ASC delayed, modified or withdrew some of its standards and sometimes apparently sought to avoid non-compliance by permitting free or engineered choice. Did this appeasement of preparers damage its credibility more than the non-compliance thereby avoided, as some critics have argued?[118] Certainly, chapters in the history of the ASC show that appeasement damages standard-setters' credibility. The widespread abuses of the late 1980s, referred to by Singleton-Green and documented by Ian Griffiths and others,[119] suggest that appeasement over some standards does not blunt preparers' appetites for creative accounting or achieve cooperation on other topics. This evidence does not, though, provide support for the proposition that the ASC, or any other standard-setting

body operating within a regime of weak enforcement, should not engage in appeasement; we simply do not know whether appeasement or non-compliance do more to damage the credibility of the regime.

What the history of the ASC does underline is the strong link in practice between standard-setting quality and enforcement. Standard-setters should attend to the care and maintenance of enforcement regimes and are probably right to err on the side of relative heavy-handedness in policing enforcement (for example in insisting on full compliance with minor provisions), the better to discourage the opening up of debate about borderlines and the vicious circle of weakness inviting further abuse.

Little has been said in this history about the users of financial statements, although these surely constitute, in principle, a constituency of outstanding importance. Little has been said simply because little *was* said, or done, by users, despite the ASC's efforts to involve the constituency in working parties and the committee itself, and in making submissions. Users did not form a separate category in the ASC's own analysis of submissions, but, as Appendix 9 shows,[120] submissions from auditors, companies and representative bodies of accountants usually hugely outweighed submissions from other representative bodies, and the latter category in any event included preparers and other parties as well as users. The theme of 'the absent user'[121] recurs throughout attempts to learn lessons from the history of the ASC, not least in relation to price change accounting.[122] Unfortunately, the experience of the ASC tells us little about how such involvement may successfully be achieved, only that it will be difficult. Another potentially important constituency is, of course, government. Maintaining good relations with government is important but should never delude a standard-setter into thinking that, on the day, government decisions will be taken on anything other than broad political considerations.

Technical proposals will inevitably meet, from time to time, with 'political' responses, that is responses pursuing the vested interests of the parties making the response. Such responses are not necessarily, in themselves, morally unjustified or, indeed, technically unsound. There were technical merits in the arguments for changing the standard on deferred taxation in 1977, and the cash flow consequences of writing off development expenditure, even where the prospects of its recovery were good, provided an economic incentive, and arguably not an unethical one, for government contractors to lobby for capitalization.[123] Whatever the arguments of principle that a standard-setter should not accede to pressures manifesting themselves outside 'due process', the practical reality is that it is exceedingly difficult to resist cases which have technical merit and widespread support. It would seem that the best a standard-setter can do is to maintain an active policy of 'scanning the horizon', identifying political issues early, reacting decisively, and explaining changes openly. The design of due process should, within a setting of transparency, accountability and good governance, be designed to facilitate rather than hinder these factors.

The ASC began its life thinking and planning in terms of a technical agenda containing a list of topics to be addressed (the initial five-year work programme).

This was certainly understandable given the circumstances of its birth. Partly, perhaps, for this reason and partly, no doubt, because the principal reason for having a standard-setter, and the dominant aspect of its daily life, is the production of technical pronouncements, little attention was given to strategy in a wider sense. Davison created structures to focus on organizational issues, managing the technical agenda, relations with constituents, and so on, but at the time these were necessarily concerned chiefly with getting the reconstituted committee off to a successful start. Latterly, there were annual conferences but these were concerned more with technical than wider strategy – for example with whether a conceptual framework was needed and what it should look like.[124] Issues such as enforcement were seen as someone else's problem – and, constitutionally, correctly so. Although at times of crisis a good deal of effort would be put into 'selling' a particular document, there were few systematic efforts to educate the public about the character of financial reporting and the role of standards, or to promote the corpus of standards generally or the work of the machinery for setting them. Again, according to the strict terms of its constitution, the committee was right to think that these were not part of its job, although, compared to the issue of enforcement, it was much less clear quite who was supposed to be doing these things.

The ASC's management of its technical agenda was dominated by fire-fighting and progress-chasing, which were in the foreground at the time of its birth. When changes in timing were announced, for example to await legal developments or co-ordinate with another pronouncement or standard-setter, this sometimes looked as much like an excuse for delay as genuine planning. A more strategic view might have enabled the ASC better to manage the conflicts between technical quality, political acceptability and organizational momentum. It might also have gone some way to avoid the charge of loss of steam in its final period, which, however unfair, did do some damage to its reputation.

A further advantage of a strategic approach to the management of the technical agenda is that it enables more research to be undertaken during the period in which a topic is rising up the agenda, rather than once a topic is in the drafting stage, when it may have to be done under severe time pressure. Professor Stephen Zeff's masterly survey of the state of standard-setting across five countries at the beginning of the 1970s, which reported the very beginning of the ASC's life, concluded with a 'plea to the profession':

> Throughout the research, this writer was impressed with the many instances in which the profession has postponed or ignored consideration of an issue until the need for a solution had become imminent, either as a result of outside pressures or other circumstances beyond the control of the profession. At times the profession has confronted problems so late that the decision was virtually taken from its hands . . . Programmes aimed at dealing with current problems must be complemented by a continuing, active search for new knowledge, new directions, new challenges.[125]

Such research can be more thorough and, perhaps, more creative – in the best sense of the word. Could early research have identified preparers' predisposition towards replacement cost rather than current purchasing power and avoided the lengthy and costly dead-end of PSSAP7?[126] Could the transmutation from the, strictly, free choice of ED21 (foreign currency) to the relatively logical structure of ED27 have been achieved by back-room research and announced in the ASC's first (and thus only) ED, rather than having to emerge in the glare of revision, and thereby saved the damaging consequences for the committee's credibility?[127] Sadly, the ASC was so rarely able to undertake such research, which requires more than a background study by a single academic or practitioner, that no conclusions can be drawn from its history. However the cost, in money and credibility, of the alternative is sometimes high, so that some experimentation seems justified.

If the first iron law of standard-setting history is that standards take longer to agree than standard-setters expect, it might be thought that the second is that standard-setters will be continuously buffeted by accounting scandals. Although this proposition is largely true, a more interesting truth is revealed by the history of the ASC. At the technical level, the relationship between scandals and standards is, though not quite random (take Court Line, for example), only very loose; many accounting scandals are not caused by the absence of accounting standards and are thus equally not avoidable by faster or more extensive development of accounting standards.[128] It follows that, while standard-setters must learn to cope, politically and technically, with the after-effects of scandals, and perhaps try to manage their impact strategically, they should beware of the pressure to respond *technically* by drafting the standard that would have avoided the most recent scandal with the greatest certainty – for it is unlikely that that standard will avoid the next scandal.

The prescription has some force at the political level also but, of course, there is a need to be seen to respond to what are perceived by opinion formers as accounting problems. While a programme of education may go some way to address this issue (and those who established the ASC certainly expressed their regrets that more had not been done to educate the public about the nature of financial statements), it has to be admitted that the public has a limited appetite for information about the constraints imposed on financial reporting by the nature of the world to be reported.[129] Nonetheless, standard-setters should analyse the accounting scandals arising on their watch carefully and ensure, as far as possible, that the 'politics of scandalization' do not deflect the standardization programme from a technically sound course.

The final lesson in the list is perhaps the most obvious and profound, but I have left it to last because it is not a lesson for standard-setters but for the UK accountancy profession as a whole: though we like to think that our multipartite institutional structure enables us to compete where appropriate and co-operate as necessary, in practice competitive urges, both commercial and social, overwhelm such co-operative spirit as we can muster and damage our capacity to act, and to be seen to act, responsibly and for the public good.

Notes

1 'Present Troubles, and More to Come'

1 For further biographical details, see S. Grey, 'The last of the household names?' *Accountancy*, October 1994. Leach was knighted in the Birthday Honours List, 1970. For the source of the quotation used as the chapter title, see below, note 102.

2 Later Lord Benson; for biographical details, see chapter 2, note 36.

3 'Accountancy: DTI report fails to highlight integrity', *The Times*, 5 April 2001, p. 32.

4 'Exit the last of the household names', *Accountancy*, October 1996, p. 16.

5 Interviews with Sir John Grenside, 27 March 2002, and Robert Willott, 10 June 2002.

6 S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and an Analysis of Trends*, Champaign, Illinois: Stipes, 1972, p. 38.

7 Zeff reports that the conference was called 'without warning' (*Forging Accounting Principles in Five Countries*, p. 38), but Leach had in fact announced that the ICAEW was 'shortly to issue a "statement of intent" about its policies . . . on accounting standards and principles', at a luncheon meeting of the London and District Society of Chartered Accountants held in the week before the Council meeting. This was reported in *The Accountant* on 4 December, so the more widely-read members of the press would have had some intimation of what they were to hear ('Institute's intentions on accounting standards', *The Accountant*, 4 December 1969, pp. 758–59; at p. 758).

8 The statement was printed almost verbatim in *The Times*, 12 December 1969, p. 24, and verbatim in a number of professional journals, including *The Accountant*, 18 December 1969, pp. 842–43, *Accountancy*, January 1970, pp. 2–3, and *The Accountant's Magazine*, January 1970, pp. 11–12. It is reproduced in Appendix 2.

9 M. Bromwich, 'The setting of accounting standards: The contribution of research', in M. Bromwich and A. G. Hopwood (eds), *Essays in British Accounting Research*, London: Pitman, 1981, p. 38. For other sources describing events in similar terms, see B. A. Rutherford, 'The AEI-GEC gap revisited', *Accounting, Business and Financial History*, 1996, 6:2.

10 V. Beattie, 'Traditions of research in financial accounting', in R. Ryan, R. W. Scapens and M. Theobald (eds), *Research Method and Methodology in Finance and Accounting*, London: Thomson, 2002, p. 98.

11 Sir Ronald Leach, 'The birth of British accounting standards', in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards: The First Ten Years*, Cambridge: Woodhead-Faulkener, 1981, p. 4.

12 For a fuller analysis of the accounting issues involved in this case, see Rutherford, 'The AEI-GEC gap revisited'.

13 Tom Watts, who was in due course to become chairman of the committee set up to produce accounting standards, was 'closely involved' in the preparation of the

report (T. Watts, *The Role of the Accounting Standards Committee* (Deloitte, Haskins and Sells Lecture, 3 March 1983), Cardiff: University College, Cardiff, 1983, p. 4). He refers to 'a series of accounting "scandals" (as seen in public eyes)' (p. 3).

14 Deloitte Plender Griffiths & Co. and Price Waterhouse & Co., Letter to Lord Aldington, Chairman of GEC, 29 July 1968, paragraph 6.

15 Price Waterhouse Partners' Newsletter, 6 August 1968, 3:20, quoted in E. Jones, *True and Fair: A History of Price Waterhouse*, London: Hamish Hamilton, 1995, p. 278. The interpretation given here was also confirmed to the author by Tom Watts in correspondence, 6 July 1995.

16 'Matters of fact and judgement', *The Economist*, 3 August 1968, p. 68.

17 General Electric Company Limited, Annual Report and Accounts, 1968, p. 4.

18 See, for example, J. Haines, *Maxwell*, London: Macdonald, 1988, T. Bower, *Maxwell: The Outsider*, London: Arum Press, 1991, and T. Clarke, 'Case study: Robert Maxwell: Master of corporate malfeasance', *Corporate Governance*, 1993, 1:3.

19 Clarke, 'Robert Maxwell', p. 142.

20 J. Graham, 'Robert Maxwell's Chinese cracker', *Accountancy*, October 1969.

21 Interview with Sir Douglas Morpeth, 3 July 2002. Touche, Ross, Bailey and Smart was re-named Touche, Ross and Co. later in 1969.

22 Graham, 'Robert Maxwell's Chinese cracker', and G. Holmes, 'The Pergamon story', *Accountancy*, October 1970.

23 Graham, 'Robert Maxwell's Chinese cracker', pp. 754–55. The City Panel on Takeovers and Mergers was established in 1968 by major groups in the City of London to protect the interests of shareholders during contested takeovers. It had no formal power but considerable influence among financial institutions. It operated under the City Code on Takeovers and Mergers, itself developed from earlier guidance. See E. Stamp and C. Marley, *Accounting Principles and the City Code: The Case for Reform*, London: Butterworths, 1970, chapters 3–6, and Zeff, *Forging Accounting Principles in Five Countries*, pp. 34 and 59–61.

24 Holmes, 'The Pergamon Story', p. 697.

25 The inspectors produced three reports. The first famously concluded that, 'Mr Maxwell . . . is not in our opinion a person who can be relied on to exercise proper stewardship of a publicly quoted company' (see Clarke, 'Robert Maxwell', p. 142).

26 Anonymous, 'Pergamon: Thoughts on the Price Waterhouse Report', *The Accountant's Magazine*, October 1970, p. 480, and Graham, 'Robert Maxwell's Chinese cracker', p. 755.

27 Quoted in Holmes, 'The Pergamon story', p. 698.

28 Holmes, 'The Pergamon story', p. 698, and Clarke, 'Robert Maxwell', p. 143.

29 Jones, *True and Fair*, p. 279. The firm agreed to the assignment only after receiving this commitment.

30 Ibid.

31 Holmes, 'The Pergamon story'.

32 Anonymous, 'Pergamon'.

33 Quoted in Holmes, 'The Pergamon story', p. 698.

34 Quoted in Anonymous, 'Pergamon', p. 485, and Holmes, 'The Pergamon story', p. 699.

35 Specifically SSAP17 'Accounting for Post Balance Sheet Events', August 1980, Accounting Standards Board, FRS5 'Reporting the Substance of Transactions', April 1994, and Accounting Standards Board, FRS8 'Related Party Disclosures', October 1995. Certainly FRS8 would have led to wide-ranging disclosures.

36 Lord Benson, *Accounting for Life*, London: Kogan Page, 1989, pp. 142–44.

37 'Points from published accounts: Rolls Razor – No lack of information', *Accountancy*, August 1964, pp. 727–29.

38 Ibid. p. 729.

39 Minute to the President [of the Board of Trade] and Prime Minister from G. F. Morris, 25 August 1965, NA, File No. BT 299/139.
40 'In Parliament', *The Accountant*, 18 December 1965, p. 830.
41 'In Parliament', *The Accountant*, 13 May 1967, p. 637.
42 Benson, *Accounting for Life*, p. 143.
43 'John Bloom report is ready', *The Times*, 2 August 1967, p. 1.
44 Benson, *Accounting for Life*, p. 143, and 'John Bloom cleared', *The Times*, 27 June 1970, p. 3. According to *Brewer's Rogues, Villains and Eccentrics*, in 2002 Bloom had been 'last heard of running a restaurant bar in Majorca' (W. Donaldson, *Brewer's Rogues, Villains and Eccentrics*, London: Cassell, 2002, p. 82).
45 Email to the author from Robin A. Crocombe, Department of Trade and Industry, 7 February 2003.
46 Benson, *Accounting for Life*, p. 143.
47 Investigation Into the Affairs of Rolls Razor Limited By Order of the Board of Trade Dated 24 July 1964: Inspectors Mr Morris Finer QC and Sir Henry Benson, CBE, FCA, redacted version released to the author under the Freedom of Information Act by the Department of Trade and Industry Companies Investigation Branch, 17 August 2005.
48 Ibid., chapter 8; see, particularly, paragraphs 547, 678, 721, 807 and 857.
49 Ibid., paragraph 741.
50 Ibid., paragraph 866.
51 Ibid., see, particularly, paragraphs 547, 681, 744–46 and 849.
52 Stanley Duncan (elected 1966) and Richard Wilkes (elected 1969) (Jones, *True and Fair*, pp. 305–6). Douglas Morpeth, who was directly involved in the events described in this chapter, was a partner in Touche, Ross, Bailey & Smart, the auditors of GEC.
53 For example in *The Times*, 'Text of the Takeover Panel's Statement', 29 August 1969, pp. 21 and 23.
54 'Making sure of due diligence and care', *The Times*, 30 July 1968, p. 21.
55 'Matters of fact and judgement', *The Economist*, 3 August 1968, p. 68.
56 Coverage by *The Times* and *The Economist* of the AEI-GEC gap in later months does not indicate that either publication changed its view of the causes of the problem (Rutherford, 'The AEI-GEC gap revisited', pp 149–50).
57 'Auditing the auditor', *The Economist*, 9 August 1969, p. 50. See below, note 75.
58 'Stock Exchange is asked to suspend Pergamon dealings', *The Times*, 22 August 1969, p. 15.
59 'Pergamon: Questions for the Panel', *The Times*, 25 August 1969, p. 18.
60 'Leasco gives fuller reasons why Pergamon talks failed', *The Times*, 26 August 1969, p. 15.
61 'A true and fair view', *The Economist*, 30 August 1969, pp. 43–44.
62 Ibid. p. 44.
63 See, for example, *The Times* 2 August 1967, p. 1, 20 March 1968, p. 2, 25 April 1968, p. 5, 26 April 1968, p. 3, 9 July 1969, p. 15, 31 July 1969, p. 4, 30 May 1970, p. 1, 27 June 1970, p. 3, and 30 October 1971, p. 17. There was no coverage in *The Economist* from January 1968 to December 1970.
64 See M. Mumford, 'Edward Stamp (1928–86): A crusader for standards', in J. R. Edwards (ed.) *Twentieth Century Accounting Thinkers*, London: Routledge, 1994.
65 Ibid. p. 274.
66 Ibid. p. 275.
67 E. Stamp, 'The public accountant and the public interest', *Journal of Business Finance*, 1969, 1, p. 32.
68 Ibid. p. 33.
69 R. J. Chambers, 'Financial information and the securities market', *Abacus*, 1965, 1:1.

70 Ibid. p. 16.
71 The Reid Murray affair is not covered in detail here because of its limited relevance to the British scene. Some accounting policies may have been unacceptable by the standards of the time but poor business practice was heavily implicated in the group's collapse and there were also deficiencies in audit practice. The affair probably offers a more clear-cut argument for standardization than any of the British cases because one device used to obscure a dramatic fall in profits was to *change* accounting policies between methods acceptable in themselves, mainly in the area of revenue recognition. See, E. Stamp, 'The Reid Murray affair', *Accountancy*, August 1964.
72 Stamp, 'The Public accountant and the public interest', p. 33, emphasis added.
73 Ibid. p. 42.
74 Zeff, *Forging Accounting Principles in Five Countries*, p. 36.
75 The piece referred to in note 57 above. Although unsigned, Stamp was identified as its author by *The Accountant* on the basis of parallels with his *Journal of Business Finance* article, 'A High Court of audit?' 23 August 1969, pp. 229–30. The sole case mentioned is Reid Murray and the piece also refers to Chambers' million combinations.
76 'Auditing the auditors', *The Times*, 11 September 1969, p. 25. The *Sunday Times* had carried an attack on both variety in accounting methods and the position of auditors in its Business News section the previous weekend, 'Time to clean up the accounts chaos', 7 September 1969, p. 23.
77 Leach, 'The birth of British accounting standards', p. 4.
78 Interview with Sir Douglas Morpeth, 3 July 2002. For biographical details of Morpeth, see p. 31.
79 'Attacks on the profession', *The Accountant*, 20 September 1969, p. 342, and Zeff, *Forging Accounting Principles in Five Countries*, p. 38.
80 Stamp and Marley, *Accounting Principles and the City Code*. The book is in fact two short and separate works, one by Stamp and the other by Marley.
81 'Auditing the auditors: Professor Stamp questioned at Manchester meeting', *The Accountant*, 15 November 1969, pp. 666–67; at p. 666.
82 Stamp and Marley, *Accounting Principles and the City Code*, p. 69.
83 For example in P. A. Bird, 'The development of standard accounting practice', in B. Carsberg and A. Hope (eds), *Current Issues in Accounting*, Oxford: Philip Allan, 1977, p. 51.
84 Michael Renshall, comments at a meeting of the Financial Reporting Group of the London District Society of Chartered Accountants, 12 March 1987.
85 Ibid.
86 Graham, 'Robert Maxwell's Chinese cracker', p. 755.
87 Quoted in 'An art or a science? Lord Shawcross on accountancy practices at Manchester dinner', *The Accountant*, 27 November 1969, p. 747.
88 'London Chartered Accountants' annual meeting', *The Accountant*, 13 May 1971, pp. 641–42; at p. 642.
89 Ibid. The accuracy of the remark was subsequently confirmed by Morpeth to Zeff in correspondence dated 13 July 1971 (Zeff, *Forging Accounting Principles in Five Countries*, p. 40).
90 P. A. Bird, *Accountability: Standards in Financial Reporting*, London: Haymarket, 1973, p. 64.
91 Interview with Michael Renshall, 17 June 2002.
92 H. Edey, 'How inventory valuation affects profits', *Financial Times*, 1 August 1968, p. 15.
93 See Zeff, *Forging Accounting Principles in Five Countries*, p. 37.
94 Sir Ronald Leach, 'Accountants and the public interest', *The Times*, 22 September 1969, p. 25.

95 Stamp's original *Times* article, Leach's response, and a letter from Stamp responding to Leach, dated 26 September, are all reproduced in Stamp and Marley, *Accounting Principles and the City Code*, appendix I.
96 H. Edey, 'Uniformity in profit measurement', *The Accountant*, 25 October 1969, p. 539.
97 Ibid. p. 540.
98 The article appeared in the *Financial Times* on 10 November 1969. It is described in some detail in 'A true and fair view of accountants', *The Accountant*, 15 November 1969, pp. 636–37, and 'The trouble with accountants', *Accountancy*, December 1969, p. 888.
99 Reported in 'Call for tax simplification at South Eastern Society's dinner', *The Accountant*, 15 November 1969, pp. 663–64.
100 Ibid. p. 663.
101 Reported in 'Accountants' role in the community', *The Accountant*, 15 November 1969, p. 665.
102 Tentative Proposals for Strengthening Accounting and Auditing Standards, Special Report to the Council from the President, Minutes of the Ordinary Meeting of the ICAEW Council, 5 November 1969, ICAEWA/MK. The quotation is a section heading. The report is considered at greater length in chapter 2. The terms 'accounting standards' and 'police' are actually used in the report.
103 Taken from the account of the press conference in *The Accountant*, 18 December 1969, pp. 841–42. Although the story does not claim that it is providing direct quotations, it seems likely that it follows the President's words closely.
104 See, for example, R. Baldwin and M. Cave, *Understanding Regulation: Theory, Strategy and Practice*, Oxford: Oxford University Press, 1999, chapter 1, and particularly the sources cited at p. 3.
105 Zeff, *Forging Accounting Principles in Five Countries*.
106 See, for example, the collection of national studies in S. McLeay (ed.), *Accounting Regulation in Europe*, London: Macmillan, 1999.
107 J. R. Edwards, *A History of Financial Accounting*, London: Routledge, 1989, chapter 11, and B. Underdown and P. J. Taylor, *Accounting Theory and Policy Making*, London: Heinemann, 1985, pp. 25–27.
108 See Zeff, *Forging Accounting Principles in Five Countries*, p. 121, and R. Van Riper, *Setting Standards for Financial Reporting: FASB and the Struggle for Control of a Critical Process*, Westport, Connecticut: Quorum Books, 1994, p. 94.
109 Zeff, *Forging Accounting Principles in Five Countries*, p. 121.
110 See R. K. Storey, *The Search for Accounting Principles*, New York: AICPA, 1964, and Zeff, *Forging Accounting Principles in Five Countries*.
111 Storey, *The Search for Accounting Principles*, pp. 14–15, footnotes in the original omitted.
112 Zeff, *Forging Accounting Principles in Five Countries*, p. 311.
113 See, for example, P. S. Florence, *Ownership, Control and Success of Large Companies*, London: Sweet & Maxwell, 1961.
114 See D. Mathews, M. Anderson and J. R. Edwards, *The Priesthood of Industry: The Rise of the Professional Accountant in British Management*, Oxford: Oxford University Press, 1998, pp. 78–86.
115 Bower, *Maxwell*.
116 Zeff, *Forging Accounting Principles in Five Countries*, p. 63.
117 B. Levin, *The Pendulum Years: Britain and the Sixties*, London: Jonathan Cape, 1970, p. 343.
118 M. Greener, 'Published company accounts – A critical review', *The Accountant*, 6 January 1968, 'The companies you keep', *The Accountant*, 9 August 1969, 'Accounting standards: I Inconsistencies in accounting principles', *The Accountant*, 20 September 1969, 'Accounting standards: II Consistency in application', *The Accountant*, 27 September 1969, and 'Accounting standards: III Inconsistencies in auditing and accounting methods', *The Accountant*, 4 October 1969.

119 Including R. J. Chambers, 'The role of accounting: Difficulties are no excuse for inadequacies', *The Accountant*, 22 February 1969, and K. S. Most, 'Accounting principles and public controversy', *The Accountant*, 20 November 1969.
120 The only coverage in 1969 was reproduction of Leach's reply to Stamp's *Times* article, though not of the original article ('The President answers back', *Accountancy*, October 1969, pp. 725–27), a piece on the Maxwell affair (Graham, 'Robert Maxwell's Chinese cracker'), two letters complaining that the journal had reproduced Leach's response without Stamp's original article, receiving a waspish reply from the editor to the effect that he was, 'sorry that *Accountancy* did not reprint Professor Stamp's article ... but only because if that had been done [he] might have been spared [these] letters' (Letters to the editor, *Accountancy*, December 1969, p. 925), and a report of Stamp's address to the Manchester Society of Chartered Accountants ('The client v. the auditor', *Accountancy*, December 1969, p. 987).
121 The body now called the Association of Chartered Certified Accountants was, at the beginning of the period covered by this volume, known as the Association of Certified and Corporate Accountants. It changed its name twice, in 1971, to the Association of Certified Accountants, and in 1984, to the Chartered Association of Certified Accountants. For convenience, it is referred to throughout this volume as the ACCA, the abbreviation it has continued to use since 1939, or the Association. Other accountancy bodies have also changed their names since 1969. The Institute of Municipal Treasurers and Accountants became the Chartered Institute of Public Finance and Accountancy in 1973 and the Institute of Cost and Works Accountants became the Institute of Cost and Management Accountants in 1972 and the Chartered Institute of Management Accountants in 1986 (see Mathews, Anderson and Edwards, *The Priesthood of Industry*, pp. 284–85). Unfortunately no convenient abbreviation or short-form name is available in these cases and references use their name at the time. The labyrinthine nature of the serial name changes was largely due to the objections of the original chartered institutes to the attempts, by bodies achieving their royal charters more recently, to work their holding of a charter into their titles and the designations of their members.
122 Editorial introduction to Greener, 'Accounting standards: I', p. 347.
123 Letters to the editor, 'Accounting standards', *The Accountant*, 11 October 1969, pp. 479–81.
124 Ibid. p. 481.
125 It was his willingness to use the generalist press to air his views that appears to have attracted most criticism when Stamp addressed the Manchester Society of Chartered Accountants – see pp. 11–12.
126 Interview with Michael Renshall, 17 June 2002.
127 Interview with David Hobson, 1 March 2002.
128 Mathews, Anderson and Edwards, *The Priesthood of Industry*, appendix by P. G. Boys.
129 Interview with Robert Willott, 10 June 2002.
130 Mathews, Anderson and Edwards, *The Priesthood of Industry*, appendix by P. G. Boys, p. 286.
131 S. E. Squires, C. J. Smith, L. McDougall and W. R. Yeack, *Inside Arthur Andersen*, Upper Saddle River, New Jersey: FT Prentice Hall, 2003.
132 Interview with Robert Willott, 10 June 2002.
133 Sir William Slimmings, 'The Scottish contribution', in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards*, p. 17.
134 Ibid.
135 Interview with Michael Renshall, 17 June 2002.
136 Interview with David Hobson, 1 March 2002. When the ICAEW Council came to discuss a public statement to be issued about action to be taken in the wake of the failure of the profession's integration scheme in 1970, some members argued that

it should refer to 'the poor quality of the work of . . . many of the smaller firms'. Others, 'while endorsing the views which had been expressed . . . had reservations' about actually making such a comment in public, and the idea was dropped (Minutes of the Special Meeting of the ICAEW Council on Development Policy, 4 November 1970, ICAEWA/MK).

137 Interview with Michael Renshall, 17 June 2002.

138 Zeff, *Forging Accounting Principles in Five Countries*, p. 40.

139 'Business sessions at the Annual Meeting of The Institute of Chartered Accountants in England and Wales: Stock Exchange recommendations', *The Accountant*, 22 May 1965, pp. 683–84.

140 Zeff, *Forging Accounting Principles in Five Countries*, pp. 27–32.

141 See R. H. Parker, 'Flickering at the margin of existence: The Association of University Teachers of Accounting, 1960–71', *British Accounting Review*, 1997, 29.

142 Reported in *The Accountant*, 24 May 1969, pp. 752–59.

143 Report of the District Societies Committee, 1 July 1969, Minutes of the ICAEW Council, 6 August 1969, ICAEWA/MK.

144 Reported in *The Accountant*, 5 July 1969, pp. 26–27.

145 Ibid. p. 26.

146 Ibid. p. 27, emphasis added.

147 See Slimmings, 'The Scottish contribution', pp. 13–15.

148 Interview with Sir John Grenside, 27 March 2002.

149 Stamp, 'The public accountant and the public interest', p. 33.

150 'Institute's Oxford Summer Course', *The Accountant*, 12 July 1969, pp. 57–58.

151 'Varied fare at Cambridge', *The Accountant*, 27 September 1969, pp. 399–400.

152 Ibid., p. 400. *The Accountant* had apparently bought the line of a long string of scandals.

153 'London Chartered Accountants' annual meeting', *The Accountant*, p. 642. This is the meeting referred to in note 88 above.

154 Leach, 'The Birth of British Accounting Standards', p. 4.

155 Grey, 'The last of the household names?' p. 30, ellipsis in the original.

156 'Auditors under a cloud', *The Guardian*, 22 October 1969, p. 15; quoted in Zeff, *Forging Accounting Principles in Five Countries*, p. 35.

157 Storey, *The Search for Accounting Principles*, p. 5.

2 The Invention of the Accounting Standard

1 Respectively Stanley Kitchen, John Grenside, Laurence Clark and Stanley Duncan (Minutes of the Ordinary Meeting of the ICAEW Council, 2 July 1969, ICAEWA/MK).

2 Special Report to the Council from the President: Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October 1969, Minutes of the Ordinary Meeting of the ICAEW Council, 5 November 1969, paragraph 1, ICAEWA/MK.

3 Ibid., paragraph 7.

4 Ibid.

5 Interview with Sir John Grenside, 27 March 2002.

6 Interviews with David Hobson, 1 March 2002 and Sir John Grenside, 27 March 2002.

7 He was also, in its final years, to become chairman of the standard-setting committee whose establishment is described in this chapter; see chapter 10.

8 Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October 1969, paragraph 2.

9 Ibid., paragraph 3.

10 Ibid., paragraph 4. For the APB, see S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and an Analysis of Trends*, Champaign, Illinois: Stipes, 1972, chapter 3.

11 Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October 1969, paragraph 4. For the APB's objectives, see R. T. Sprouse and D. F. Vagts, 'The Accounting Principles Board and differences and inconsistencies in accounting practice: An interim appraisal', *Law and Contemporary Problems*, 1965, and E. S. Hendriksen, *Accounting Theory*, Homewood, Illinois: Irwin, 1970, pp. 75–77.

12 Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October 1969, paragraph 8.

13 The recommendations were originally issued as a section of the members' handbook and had only recently become officially available to non-members by publication as a separate volume ('Institute's Recommendations on Accounting Principles', *The Accountant*, 4 October 1969, p. 444). See P. Taylor and S. Turley, *The Regulation of Accounting*, Oxford: Basil Blackwell, 1986, pp. 21–22, and Zeff, *Forging Accounting Principles in Five Countries*, 1972, pp. 14–23.

14 Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October 1969, paragraph 8.

15 Ibid.

16 Ibid., annex, pp. 4–7.

17 Ibid., paragraphs 1–6.

18 Ibid., paragraph 5.

19 Ibid. p. 7.

20 Ibid., paragraphs 7–9.

21 Ibid., paragraphs 10–12.

22 Minutes of the Ordinary Meeting of the ICAEW Council, 5 November 1969, ICAEWA/MK.

23 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N9 'Depreciation of Fixed Assets', January 1945, paragraph 12.

24 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N22 'Treatment of Stock-in-trade and Work in Progress in Financial Accounts', November 1960, paragraph 34.

25 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1968–1969*, London: ICAEW, 1970, pp. 93–95.

26 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N27 'Treatment of Taxation in Accounts of Companies', July 1968, paragraph 11.

27 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1968–1969*, p. 99.

28 See pp. 61–66 and 110–11.

29 In 1969 the position was that Auditing Statements issued by the ICAEW Council had the status of guidance. This remained the case until the adoption of the first mandatory Auditing Standards in 1980. See E. Woolf, 'Are the new auditing standards the answer to a major problem?' *Accountancy*, 1978, and Auditing Practices Committee, 'Auditing Standards and Guidelines', *Accountancy*, 1980.

30 Minutes of the Ordinary Meeting of the ICAEW Council, 3 December 1969, ICAEWA/MK.

31 Zeff, *Forging Accounting Principles in Five Countries*, 1972, p. 39.

32 Interview with Sir John Grenside, 27 March 2002.

33 See chapter 1, note 7.

34 Interview with Michael Renshall, 17 June 2002.

35 Zeff, *Forging Accounting Principles in Five Countries*, 1972, p. 39.

36 Sir Henry Benson, later Lord Benson of Drovers in the County of West Sussex, was born in 1909 and grew up in South Africa. He was the grandson of Francis Cooper, one of four brothers who built up the firm bearing their name, and joined Cooper Brothers & Co. on leaving school. According to his autobiography, the

offer of articles was made via his mother, who had known a number of the firm's partners in the period before she left for South Africa, some twenty years earlier. It was apparently made to fill an awkward pause in the conversation after she dropped in to see her former acquaintances, unannounced and with no other communication having occurred in the previous two decades. He became a partner in 1934 and President of the ICAEW in 1966. For further information, see Lord Benson, *Accounting for Life*, London: Kogan Page, 1989, a rare example of an autobiography by an accountant.

37 Interview with Sir John Grenside, 27 March 2002.

38 Interview with Michael Renshall, 17 June 2002.

39 Ibid.

40 Some, at least, argue that such professional leadership has rarely been achieved since (interview with Robert Willott, 10 June 2002).

41 The Statement was widely published (see chapter 1, note 8) and is reproduced in Appendix 2.

42 ICAEW, Recommendation on Accounting Principles N9. For example, paragraph 12(b) refers to 'the straight-line method', while 12(c) uses 'the straight-line basis'.

43 See pp. 177–92.

44 'Accountancy: A tougher line is needed', *The Times*, 15 December 1969, p. 21. This was the only adverse comment identified by Zeff, see *Forging Accounting Principles in Five Countries*, 1972, p. 48.

45 It should be noted that the quotations given here are drawn from excerpts from replies, chosen within the ICAEW secretariat for reporting to the Council, so there may have been an element of selectivity (see the Special Report to the General Purposes and Finance Committee from the President: Implementation of the 'Statement of Intent on Accounting Standards in the 1970s', 12 December 1969, Minutes of the Ordinary Meeting of the ICAEW Council, 7 January 1970, ICAEWA/MK, attachment).

46 See p. 12.

47 See p. 11 and chapter 5.

48 H. Edey, 'Uniformity in profit measurement', *The Accountant*, 1969. Edey actually uses development expenditure as his principal example.

49 P. A. Bird, 'The development of standard accounting practice', in B. Carsberg and A. Hope (eds), *Current Issues in Accounting*, Oxford: Philip Allan, 1977.

50 Ibid. p. 50.

51 Ibid.

52 Correspondence from Stephen Zeff, 5 January 2005, and Michael Renshall, 25 April 2005.

53 For further details of the Recommendations on Accounting Principles, see above, note 13. For an example of the criticisms made of the series, see the comments of the anonymous Council member quoted on p. 25. For an example of the indecisiveness of the series, see pp. 70–71.

54 Implementation of the 'Statement of Intent on Accounting Standards in the 1970s', 12 December 1969.

55 Ibid., paragraph 1.

56 Ibid., paragraph 2. The capitalization is in the original. This appears to be the first occasion on which this title (and its abbreviation) were used in an official document.

57 Ibid., paragraph 3. Sir Douglas Morpeth recalls that it was originally suggested that the committee would steer the work of the Institute's Technical Committee without taking over responsibility for the production of pronouncements. He argued that this would leave the new committee shouldering the blame if the Technical Committee was too slow or produced unsatisfactory pronouncements and that it would be better if the new committee itself took on the responsibility

(correspondence from Sir Douglas Morpeth, 10 February 2005, and interviewed in D. Mathews and J. Pirie, *The Auditors Talk: An Oral History of a Profession from the 1920s to the Present Day*, New York: Garland, 2000, pp. 314–20; at pp. 318–19). In the event, the Institute's technical arm, including its Technical Committee, did take responsibility for the initial preparation of material (see p. 33).

58 Sir Ronald Leach, 'The birth of British accounting standards', in Sir Ronald Leach and E. Stamp, (eds), *British Accounting Standards: The First Ten Years*, Cambridge: Woodhead-Faulkener, 1981, p. 5.

59 Implementation of the 'Statement of Intent on Accounting Standards in the 1970s', 12 December 1969, paragraph 4.

60 For further biographical detail, see 'New Vice President', *The Accountant*, 4 June 1970, p. 840, and 'Retirement marks long history of service', *Accountancy*, April 1984, p. 46.

61 Implementation of the 'Statement of Intent on Accounting Standards in the 1970s', 12 December 1969, paragraph 5.

62 Ibid., paragraph 6.

63 Interview with Michael Renshall, 17 June 2002.

64 Report of the General Purposes and Finance Committee, 17 December 1969, Minutes of the Ordinary Meeting of the ICAEW Council, 7 January 1970, ICAEWA/MK.

65 Minutes of the Ordinary Meeting of the ICAEW Council, 7 January 1970, ICAEWA/MK.

66 Report of the ASSC, 26 January 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 4 February 1970, ICAEWA/MK.

67 References in official papers generally link the invitations to the two Institutes, for example a later set of minutes reports that they 'had been invited *jointly* to fill two places on the committee'. (Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK, emphasis added). The references are sufficiently common to suggest that linking the invitations was deliberate but it is not clear from the references what it was intended to achieve. Michael Renshall's recollection is that it was intended that the two institutes would between them decide how to fill the seats, so that, in principle, there might be two Scots or two Irish representatives. He points out that the arrangement was 'perhaps mischievous' (correspondence with the author, 25 April 2005).

68 Only the version after amendment survives, ASSC: Constitution, Minutes of the Ordinary Meeting of the ICAEW Council, 4 February 1970, ICAEWA/MK.

69 Ibid., clause 1.

70 Ibid., clause 3.

71 Report of the ASSC, 26 January 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 4 February 1970, ICAEWA/MK.

72 ASSC: Constitution, clause 8.

73 Ibid., clause 17.

74 Ibid., clause 18.

75 Sir William Slimmings, 'The Scottish contribution', in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards*, 1981, p. 16.

76 Ibid. p. 17.

77 Ibid. p. 18.

78 Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK.

79 Slimmings, 'The Scottish contribution', p. 18.

80 Report of the ASSC, 6 May 1970.

81 Report of the Research Committee, 3 March, 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 8 April 1970, ICAEWA/MK.

82 Interview with Sir John Grenside, 27 March 2002.
83 Correspondence from Michael Renshall, 25 April, 2005.
84 Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK. Council approved the recommendation.
85 See p. 48.
86 Report of the ASSC, 6 May, 1970, Attachment No. 2, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK.
87 Ibid., clause 3A.
88 The new arrangements were explained to ICAS members in a note prepared by the President and published in *The Accountant's Magazine*, 'Accounting standards', June 1970, p. 235.
89 ASCA, 5/3/5.
90 Report of the President's Advisory Committee, 24 May 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 2 June 1971, ICAEWA/MK.
91 Slimmings, 'The Scottish contribution', pp. 18–19 and ASCA, 5/3/5. No affiliation is given for Morrow in the relevant members' list; by the early 1970s he was working as a consultant specializing in company rescue and he was responsible for restructuring Rolls-Royce after its problems with the RB211 (see p. 137; Obituary, *The Guardian*, 18 May 2006, p. 38).
92 Slimmings, 'The Scottish contribution', pp. 18–19.
93 ASCA, 5/3/5.
94 Report of the ASSC, 1 June 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 1 July 1970, ICAEWA/MK.
95 K. Shackleton, and S. Walker, *A Future for the Accountancy Profession: The Quest for Closure and Integration 1957–1970*, Edinburgh: ICAS, 2001.
96 Minutes of the Ordinary Meeting of the ICAEW Council, 1 July 1970, ICAEWA/MK.
97 Progress Report of the ASSC for the year ended 30 April, 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 5 May 1971, ICAEWA/MK, paragraph 6. The Progress Report for the year ended 30 April 1971 adopted the rather unhappy approach of describing the wider consultative machinery variously as 'Plenary Meetings' and as the meetings of a 'Plenary Committee'. If they were plenary meetings of the ASSC, the term is being used to mean not, as the dictionary would have it, a meeting to be attended by all the Committee's members, but rather a meeting of the Committee together with other parties. If the wider group really does constitute a Plenary Committee it seems hardly necessary to describe its meetings as plenary meetings, since it never meets other than in plenary. The only logical solution to this conundrum would be to view the ASSC meetings proper as an 'inner session' of the Plenary Committee, which does not seem to be how either the ASSC, the professional accountancy bodies, or the other associations represented on the Plenary Committee saw the position. It seems likely that the terminology was used to avoid describing the arrangements as designed (merely) for liaison, implying a weak role for the non-accounting bodies.
98 Shackleton and Walker, *A Future for the Accountancy Profession*.
99 Minutes of the Ordinary Meeting of the ICAEW Council, 7 October 1970, ICAEWA/MK.
100 J. R. Edwards, *A History of Financial Accounting*, London: Routledge, 1989, p. 287.
101 Letter from Desmond Goch, 'Accounting standards', *The Accountant*, 18 March 1971, p. 352. At the time Goch was a member of the ACCA's Moderator's Committee and he later served as President of the Association.
102 Editorial, 'Two points of view', *The Accountant*, 25 March 1971, pp. 362–63; at p. 363.
103 Minutes of the Ordinary Meeting of the ICAEW Council, 13 October 1971, ICAEWA/MK. The rejection of the integration scheme by the ICAEW membership

in the previous year would have made it difficult for the ICAEW to move beyond the 'associate' arrangement with any of the other accountancy bodies.

104 Report of the President's Advisory Committee, 29 September 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 13 October 1971, ICAEWA/MK.
105 Ibid., paragraph 4.
106 Ibid., paragraph 5.
107 Ibid.
108 Ibid., paragraph 7.
109 'New definitive standard', *The Accountant,* 4 November 1971, p. 611.
110 Leach, 'The birth of British accounting standards', p. 4.
111 ASSC: Constitution, clause 1.
112 See p. 42.
113 The new arrangements were recommended by the Wheat Study Group in a report, issued in March 1972, which used the term 'financial accounting standards'. The change in terminology in the USA was heavily influenced by Professor David Solomons who was, however, unaware at the time of the introduction of the term in the UK (see S. A. Zeff, 'David Solomons (1912–95) – An appreciation', *Accounting and Business Research*, 1995, 25:100, p. 317).
114 'Proposed new accounting standards', *The Accountant*, 8 April 1971, pp. 450–51.
115 Leach, 'The birth of British accounting standards', p.5. The Statement of Intent did not get quite to the point of using the term standard for the pronouncements to be produced; see p. 37.
116 Zeff, *Forging Accounting Principles in Five Countries*, pp. 321–23.
117 W. A. Paton and A. C. Littleton, *An Introduction to Corporate Accounting Standards*, np: American Accounting Association, 1940.
118 See pp. 110–13.
119 Paton and Littleton, *An Introduction to Corporate Accounting Standards*, pp. 4–5.
120 Hendriksen, *Accounting Theory*, pp. 79–80.
121 Ibid.
122 Interview with Michael Renshall, 17 June 2002.
123 See p. 16.
124 M. Greener, 'The companies you keep', *The Accountant*, 9 August 1969, p. 170.
125 M. Greener, 'Accounting standards: I Inconsistencies in accounting principles', *The Accountant*, 20 September 1969, p. 347.
126 Ibid.
127 M. Greener, 'Accounting standards: II Consistency in application', *The Accountant,* 27 September 1969, p. 388.
128 See p. 13.
129 Edey, 'Uniformity in profit measurement', p. 539.
130 Interview with Michael Renshall, 17 June 2002. Renshall particularly recalls Victor MacDougall as a prominent critic of the term, especially in the phrase 'definitive standards', as used, for example, in the Statement of Intent (see p. 26). MacDougall was secretary of the ICAS and, given its previous position on technical guidance, it is unsurprising that the Scottish institute would have been particularly sensitive to connotations of rigid uniformity (correspondence from Michael Renshall, 25 April 2005).
131 Attachment No. 6, Agenda for the Meeting of the ASSC, 25 March 1970, ASCA, 4/2/1.
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133 Ibid., paragraph 4.
134 Ibid., paragraph 5.
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136 Ibid., paragraph 8.
137 Ibid., paragraph 9.

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139 Memorandum from Keith Robinson to P. G. A. Thomas, 10 October 1983, ASCA, 2/53/3.
140 Letter from J. G. Hurst to Ian H. Davison, 23 January 1984, ASCA, 2/53/3.
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142 Special Report to the Council from the President: Tentative Proposals for Strengthening Accounting and Auditing Standards, 27 October, 1969, paragraph 8.
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149 Leach, 'The birth of British accounting standards', p. 5.
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151 Explanatory Foreword to Statements of Standard Accounting Practice, paragraph 3.
152 Minutes of the Special Meeting of the ICAEW Council on Development Policy, 4 November 1970, ICAEWA/MK.
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163 Explanatory Foreword to Statements of Standard Accounting Practice.
164 'Inverness dinner', *The Accountant's Magazine*, February 1971, p. 48.
165 Report of the ASSC, 23 July 1971, and Minutes of the Ordinary Meeting of the ICAEW Council, 4 August 1971, ICAEWA/MK.
166 Report of the Technical Committee, 17 December 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 6 January 1971, ICAEWA/MK.
167 Zeff, *Forging Accounting Principles in Five Countries*, p. 47, note 93.
168 Institute of Chartered Accountants in England and Wales, Statement on Auditing U17 'The Effect of Statements of Standard Accounting Practice on Auditors' Reports', February 1971, paragraph 2. The Statement was reproduced in *Accountancy*, March 1971, p. 154.
169 Ibid., paragraph 3.
170 Ibid., paragraph 4.
171 K. Sharp, 'Accounting standards after twelve months – Addendum: A note on the further development of accounting standards 1971/72', in Zeff, *Forging Accounting Principles in Five Countries*, 1972, p. 88.

172 See p. 41.
173 Taylor and Turley, *The Regulation of Accounting*, pp. 135–36.
174 ASCA, 1/80/1.
175 Explanatory Foreword to Statements of Standard Accounting Practice, paragraph 4.
176 For the standard concerned, see pp. 75–81.
177 'Whose job to enforce accounting standards?' *Accountancy Age*, 19 September 1975, p. 7.
178 Interview with Sir Douglas Morpeth, 3 July 2002.
179 The most recent edition was dated April 1969.
180 The relevant provisions are set out in Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1970–71*, London: ICAEW, 1972, appendix 3.
181 The relevant provisions are set out in Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1971–72*, London: ICAEW, 1972, appendix 3.
182 Ibid., paragraph 9.
183 Ibid., note 28.
184 Correspondence from Sir Douglas Morpeth, 11 February 2005.
185 News item, *Accountancy Age*, 2 June 1972, p. 3.
186 'Whose job to enforce accounting standards?' *Accountancy Age*, p. 7.
187 Zeff, *Forging Accounting Principles in Five Countries*, p. 311.
188 Ibid.
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3 Honeymoon Period: 1970–1974

1 Sir Ronald Leach, 'The birth of British accounting standards', in Sir Ronald Leach and E. Stamp, (eds), British Accounting Standards: The First Ten Years, Cambridge: Woodhead-Faulkener, 1981, p. 5.
2 S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and an Analysis of Trends*, Champaign, Illinois: Stipes, 1972, p. 42.
3 Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK, paragraph (a).
4 Ibid., Attachment 1.
5 Ibid., paragraph (c) and Attachment 1. The report referred to the project as concerning 'the fundamental objects and *purpose* of periodic financial statements', rather than 'principles', the word appearing in the programme itself. See chapter 5.
6 Ibid., paragraph (a).
7 Twenty-nine statements in 28 years, 1942–69.
8 'Institute's approach to accounting standards', *The Accountant*, 7 May 1970, pp. 685–86, and Zeff, *Forging Accounting Principles in Five Countries*, p. 211.
9 The survey was established by the Institute's Research Committee to focus on 'problem areas dealt with in the Institute's "Recommendations on Accounting Principles" or arising from the disclosure provisions of the Companies Act 1967' (Report of the Research Committee, 3 March, 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 8 April 1970, ICAEWA/MK). In other words, it was seen as a 'deliberate device' to 'shame people into complying' (interview with Sir John Grenside, 27 March 2002).
10 'Facts and fallacies', *Accountancy*, May 1970, p. 407, and 'Institute's approach to accounting standards', *The Accountant*.
11 'Facts and fallacies', *Accountancy*, p. 407. The list provided to journalists, and published, for example in *The Accountant* (see above, note 10), actually included 19 items, omitting insurance company accounts.

12 'Institute's approach to accounting standards', *The Accountant*, p. 686. The slip in referring to 'recommendations' may well have crept in at the reporting stage.
13 'Institute's immense task on accounting standards: President's comments at Bristol dinner', *The Accountant*, 5 March 1970, p. 354, emphasis added.
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15 Interview with Michael Renshall, 17 June 2002.
16 See p. 33.
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29 Sharp, 'Accounting standards after twelve months', p. 241.
30 Leach, 'The birth of British accounting standards', p. 6, and interview with Sir Douglas Morpeth, 3 July 2002.
31 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1968–1969*, London: ICAEW, 1979, p. 36.
32 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N20 'Treatment of Investments in the Balance Sheets of Trading Companies', November 1958.
33 Ibid., paragraph 41.
34 Ibid., paragraph 23.
35 Leach, 'The birth of British accounting standards', p. 6.
36 For an extensive analysis of the emergence of equity accounting, including the origin of its terminology and the development of criteria for its application, see C. Nobes, 'An analysis of the international development of the equity method', *Abacus*, 2002, 38:1.
37 American Institute of Certified Public Accountants, ARB51 'Consolidated Financial Statements', August 1959, paragraph 19.
38 Accounting Principles Board, Opinion No. 10 'Omnibus Opinion 1966', December 1966, paragraph 3.
39 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1968–1969*, pp. 36–39.
40 Leach, 'The birth of British accounting standards', p. 6.
41 See pp. 88–89.
42 Interview with Sir Douglas Morpeth, 3 July 2002.
43 Sharp, 'Accounting standards after twelve months', p. 241.
44 Zeff, *Forging Accounting Principles in Five Countries*, p. 44.
45 Interview with David Hobson, 1 March 2002.
46 Sharp, 'Accounting standards after twelve months'.
47 Leach, 'The birth of British accounting standards', p. 6.

48 Report of the ASSC, 1 June 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 1 July 1970, ICAEWA/MK.
49 Minutes of the Ordinary Meeting of the ICAEW Council, 1 July 1970, ICAEWA/MK.
50 ED1, Preface. It was subsequently referred to as ED1, however, and that convention is followed here.
51 Ibid.
52 p. 40.
53 ED1, paragraph 3.
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55 ED1, paragraphs 6–7.
56 Zeff, *Forging Accounting Principles in Five Countries,* p. 44.
57 25 June 1970, pp. 957–60.
58 July 1970, pp. 496–98.
59 July 1970, pp. 299–303.
60 Contents page, *Accountancy*, July 1970, p. 485.
61 'Notes and comments', *The Accountant's Magazine*, July 1970, pp. 290–91.
62 'A revolutionary proposal', *The Accountant*, 25 June 1970, pp. 945–46.
63 For details, see Zeff, *Forging Accounting Principles in Five Countries*, note 84, p. 44.
64 Ibid. p. 45.
65 'Accounting for the results of associated companies', *The Accountant*, 17 September 1970, pp. 366–70.
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67 For ED6 'Stocks and Work in Progress'; see pp. 75–81.
68 Sharp, 'Accounting standards after twelve months'.
69 Ibid. pp. 240–41.
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72 Report of the ASSC, 2 December 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 6 January 1971, ICAEWA/MK.
73 Editorial, *Accountancy Age*, 23 April 1971, p. 7.
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76 See chapter 2.
77 SSAP1, paragraph 19.
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92 Ibid., paragraph 17.
93 All at SSAP1, paragraph 6 and APB, Opinion No 18, paragraph 17.

94 APB, Opinion No 18, paragraph 17.
95 Editorial, *Accountancy Age*, 23 April 1971, p. 7.
96 'International co-operation on standards', *The Accountant*, 15 October 1970, p. 504.
97 See pp. 55–56.
98 Editorial, *Accountancy Age*, 17 September 1971, p. 4.
99 International Accounting Standards Committee, IAS3 'Consolidated Financial Statements', June 1976.
100 Leach, 'The birth of British accounting standards', p. 6. The text actually reads 'overseas companies'.
101 See p. 42.
102 ED2, paragraph 1.
103 See p. 26 and Appendix 2. The Statement of Intent referred to disclosure of the accounting bases adopted by individual preparers without giving the particular bases adopted by a preparer in practice a specific title and this usage appears to have continued until fairly close to the finalization of ED2 (ASSC Agenda, 5 November 1970, ASCA, 4/2/1).
104 See pp. 50–51.
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106 Letter dated 26 October 1970, ASCA, 4/2/1.
107 Letter dated 30 October 1970, ASCA, 4/2/1.
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115 ED2, paragraph 8.
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118 Ibid., paragraph 4.
119 Ibid., paragraph 10.
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123 Minutes of the Ordinary Meeting of the ICAEW Council, 13 October 1971, ICAEWA/MK. The terms of the minute do not appear to comply with the relevant clause of the ASSC's constitution; see p. 34.
124 Report of the ASSC, 14 July 1971.
125 SSAP2, paragraph 14.
126 Ibid., paragraph 16.
127 Explanatory Foreword to Statements of Standard Accounting Practice, paragraph 1.
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129 Accounting Principles Board Opinion No. 22 'Disclosure of Accounting Policies', April 1972.
130 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1973–1974*, p. 22.
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132 Ibid.

133 Institute of Chartered Accountants in England and Wales, *Survey of Published Accounts 1973–1974*, Table 11, p. 68.
134 Ibid. p. 67.
135 Ibid., Table 23, p. 103.
136 Ibid., Table 22, p. 101.
137 R. W. Perks and L. Butler, 'Accountancy standards in practice: The experience of SSAP2', *Accounting and Business Research*, 1977, 8:29, p. 32.
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139 Ibid. pp. 32–33.
140 Zeff, *Forging Accounting Principles in Five Countries*, p. 84. For extraordinary items, see pp. 70–75.
141 ED5, footnote to paragraph 5.
142 Extract from the minutes of ICAEW Technical Committee, 30 September 1971, ASCA, 1/10/1.
143 Correspondence, ASCA, 1/10/1.
144 ED7.
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146 Ibid.; in paragraph 7.
147 Ibid., paragraph 12.
148 Ibid., paragraph 16.
149 Ibid., paragraph 8.
150 Accounting Principles Board Opinion No. 20 'Accounting Changes', July 1971, paragraph 16.
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153 International Accounting Standards Committee, IAS1 'Disclosure of Accounting Policies, January 1975.
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166 'Accounting for acquisitions and mergers', *Accountancy.*
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169 'Accounting for acquisitions and mergers', *Accountancy.*
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171 'Accounting for acquisitions and mergers', *Accountancy.*
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174 'Accounting for acquisitions and mergers', *Accountancy*, p. 105.
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180 Ibid. p. 449.
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188 Ibid. and correspondence from Michael Renshall, 25 April 2005. This was one of the earliest public examples of a firm aligning itself with a potential client's interest in order to win business.
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205 'What is profit?' *The Accountant*, 24 September 1970, p. 399.
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207 Accounting Principles Board, Opinion No. 9 'Reporting the Results of Operations', December 1966.
208 Zeff, *Forging Accounting Principles in Five Countries*, p. 45.
209 Editorial, *Accountancy Age*, 27 August 1971, p. 5.
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229 ED7, Foreword.
230 'Prior year not extraordinary', *The Accountant*, 6 July 1972, p. 3.
231 See Appendix 9.
232 SSAP6, paragraph 11.
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235 Editorial, *Accountancy Age*, 27 August 1971, p. 5.
236 See pp. 122 and 275.
237 Interview with Michael Renshall, 17 June 2002.
238 See p. 43.
239 Interview with David Hobson, 1 March 2002.
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242 Ibid. p. 93.
243 ICAEW, Recommendation on Accounting Principles N22, paragraph 10.
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245 Ibid., paragraph 32.
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274 Edge-Partington, 'Accounting for stock and work in progress', p. 106.
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280 See pp. 136 and 177–92.
281 See Appendix 9.
282 Submissions are available in the files of the ICAEW Library.
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293 Ibid., p. 422.
294 Minutes of the Ordinary Meeting of the ICAEW Council, 2 February 1972, ICAEWA/MK. The minutes wrongly record the series number as 2.
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310 See chapter 9.
311 'Guidance on VAT accounting', *The Accountant*, 3 May 1973, pp. 595–96.
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314 'Imputation system shocks', *The Accountant*, 24 May 1973, pp. 701–2; at p. 701.
315 See p. 48.
316 Sharp, 'Accounting Standards after Twelve Months', p. 241.
317 Technical Committee: Progress Report for the Year ended 30 November 1971.
318 ASSC: Progress Report for the Year ended 30 April, 1971.
319 Leach, 'The birth of British accounting standards', p. 8.
320 See pp. 122–28.
321 See p. 12.
322 'Accountants meet Panel', *The Accountant*, 15 October 1970, p. 503.
323 Interviewed by *The Banker*, comment reproduced in 'Dissatisfied customer', *The Accountant*, 15 July 1971, p. 77.
324 Report of the ASSC, 21 October 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 4 November 1970, ICAEWA/MK. This does not necessarily add weight to the evidence that the government had been pressing informally for action earlier, see chapter 1. It is possible, for example, that the government's concern about the pace of standardization was in part a response to the profession's own decision that this was the appropriate way forward.
325 News item, *Accountancy Age*, 21 May 1971, p. 28.
326 P. Weetman, 'Accounting standards: A pause for reflection', *Accounting and Business Research*, 1977, 7:27, p. 176.
327 Reported comment at a press conference, 'More on accounting standards', *The Accountant*, 21 January 1971, p. 71.

4 Accounting for Changing Prices: The Struggle Begins

1 The terms 'price-level accounting' and 'inflation accounting', often used to describe accounting for changing prices, could be argued to imply systems that reflect movements in prices *generally* as distinguished from specific price changes. The title of this chapter is intended to be neutral on that issue. The present work

focuses on the place of accounting for changing prices in the ASSC's own history; for a more wide-ranging survey, see D. P. Tweedie and G. Whittington's excellent study, *The Debate on Inflation Accounting*, Cambridge: Cambridge University Press, 1984. Whittington has also written a lucid guide to the theoretical considerations underpinning accounting for price changes, *Inflation Accounting: An Introduction to the Debate*, Cambridge: Cambridge University Press, 1983, and the reader interested in this aspect of the problem is referred to this and to the other material cited in it. This chapter draws particularly on Tweedie and Whittington's volume and on C. A. Westwick, 'The lessons to be learned from the development of inflation accounting in the UK', *Accounting and Business Research*, 1980, 10:40.

2 See Whittington, *Inflation Accounting*, chapter 6.

3 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N12 'Rising Price Levels in Relation to Accounts', January, 1949.

4 Research and Technical Committee of the Institute of Cost and Works Accountants, *The Accountancy of Changing Price Levels,* London: ICWA, 1952, and Taxation and Research Committee of the Association of Certified and Corporate Accountants, *Accounting for Inflation: A Study of Techniques under Conditions of Changing Price Levels*, London: Gee & Co., 1952.

5 Institute of Chartered Accountants in England and Wales, Recommendation on Accounting Principles N15 'Accounting in Relation to Changes in the Purchasing Power of Money', May, 1952.

6 See M. Mumford, 'The end of a familiar accounting cycle', *Accounting and Business Research*, 1979, 9:34.

7 Source: All Items Retail Prices Index, Table RP04, National Statistics.

8 Research Committee of the Institute of Chartered Accountants in England and Wales, *Accounting for Stewardship in a Period of Inflation*, London: ICAEW, 1968.

9 Ibid. p. 2.

10 Interview with Sir Douglas Morpeth, 4 July 2002.

11 He is named as author in Morpeth's survey of the development of current cost accounting, D. S. Morpeth, 'Developing a current cost accounting standard', in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards: The First Ten Years*, Cambridge: Woodhead-Faulkener, 1981, p. 43.

12 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 47.

13 See p. 1.

14 Westwick, 'Lessons', p. 356.

15 Minutes of the Ordinary Meeting of the ICAEW Council, 7 April 1971, ICAEWA/MK.

16 See chapter 2, note 97.

17 For example in the report of the meeting to Council, Report of the ASSC, 9 June 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 7 July 1971, ICAEW/MK.

18 Ibid.; see p. 96.

19 Dated 7 May 1971 and quoted in Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 48.

20 Report of the ASSC, 9 June 1971.

21 Correspondence from Chris Westwick, 17 May 2005.

22 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 48.

23 'Inflation and accounts', *Accountancy*, September 1971, pp. 496–506.

24 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 48.

25 See p. 48.

26 Progress Report of the ASSC for the year ended 30 April 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 5 May 1971, ICAEWA/MK.

27 Report of the Technical Committee, 22 April 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 5 May 1971, ICAEWA/MK.
28 Financial Management and Accounting Under Inflationary Conditions: A Record of a Meeting of the ASSC, 10 May 1971, Report of the ASSC, 9 June 1971, Minutes of the Ordinary Meeting of the ICAEW Council, 7 July 1971, ICAEWA/MK, p. 1.
29 Ibid. p. 3.
30 Ibid. pp. 4 and 6.
31 Ibid. p. 3.
32 Research and Technical Committee of the Institute of Cost and Works Accountants, *The Accountancy of Changing Price Levels*; see pp. 91–92.
33 Financial Management and Accounting Under Inflationary Conditions, 10 May 1971, p. 2.
34 Ibid. p. 3.
35 Ibid. p. 4.
36 Ibid. p. 3.
37 Ibid. p. 5.
38 Ibid. p. 1.
39 Leach, 'The birth of British accounting standards', p. 9.
40 Minutes of the Ordinary Meeting of the ICAEW Council, 7 July 1971, ICAEWA/MK.
41 Ibid. The representative of the Bank at the 10 May meeting had indicated that, it was possible the Governor of the Bank of England might be able to help.
42 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 49. On the other hand, the practical difficulties of implementing replacement cost should not be understated – for example, available price indices were limited in scope (correspondence from Chris Westwick, 17 May 2005).
43 Westwick, 'Lessons', p. 356.
44 Ibid.
45 'Accounting for inflation: Cambridge Conference', *Accountancy*, October 1971, pp. 564–68.
46 Ibid. p. 567.
47 'Inflation and accounts – Institute Conference', *Accountancy*, October 1971, p. 549 (the 'lead in' to the main story provided on the contents page).
48 'Accounting for inflation: Cambridge Conference', *Accountancy*, October 1971, p. 564.
49 The membership is recorded in Westwick, 'Lessons', appendix 2. The academic, Professor D. L. Hally, had not previously contributed to any notable extent to the development of any model.
50 Interview with Chris Westwick, 10 July 2002.
51 Ibid.
52 Ibid.
53 See Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 63.
54 Ibid. pp. 63–64.
55 Westwick, 'Lessons', p. 357.
56 See, for example, C. A. Westwick and N. J. Ballanger, 'The Institute's field test results', *Accountancy*, 1975 and 'An easier path for inflation accounting', *Accountancy Age*, 14 April 1972, p. 32.
57 Interview with Chris Westwick, 10 July 2002.
58 R. S. Cutler and C. A. Westwick, 'The impact of inflation accounting on the Stock Market', *Accountancy*, March 1973.
59 Ibid. p. 15.
60 Westwick, 'Lessons', pp. 357–58.
61 Interview with Chris Westwick, 10 July 2002, and correspondence from Chris Westwick, 17 May 2005.

62 Interview with Chris Westwick, 10 July 2002.
63 Westwick, 'Lessons', p. 358.
64 See Appendix 9.
65 See Westwick, 'Lessons', p. 359.
66 Tweedie and Whittington, *The Debate on Inflation Accounting*, pp. 64–73.
67 Ibid. p. 66.
68 Published in *The Accountant*, 28 June 1973, pp. 887–89.
69 Ibid. p. 887.
70 Ibid.
71 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 64.
72 Westwick, 'Lessons', p. 358.
73 Interview with Michael Renshall, 17 June 2002.
74 'Accounting for inflation now', *The Accountant*, 2 August 1973, pp. 137–38; at pp. 137–38.
75 'Slow start to inflation inquiry', *The Accountant*, 18 October 1973, p. 492.
76 Communications between the ASSC and government concerning accounting for price changes are discussed, without specific sourcing, in Tweedie and Whittington, *The Debate on Inflation Accounting*, pp. 74–75.
77 Tweedie and Whittington, *The Debate on Inflation Accounting*, pp. 75–78. The rest of the discussion of this point draws on the evidence presented there.
78 T. W. McRae and R. Dobbins, 'Behavioural aspects of the inflation accounting controversy', *Accounting and Business Research*, 1974, suggest that civil servants generally favoured current cost methods.
79 *Accounting for Changes in the Purchasing Power of Money*, Report of the ASSC, 9 June 1971, p. 4.
80 Sharp, 'Accounting Standards after Twelve Months – Addendum', p. 89.
81 Reproduced in *The Accountant*, 20 April 1972, p. 510.
82 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 75.
83 Westwick, 'Lessons', p. 358.
84 Interview with David Hobson, 1 March 2002.
85 'Accounting for inflation now', *The Accountant*, p. 137.
86 Ibid.
87 Westwick, 'Lessons', p. 359.
88 Ibid., p. 360.
89 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 82.
90 PSSAP7, paragraph 34.
91 Ibid. p. 3.
92 Ibid. p. 4.
93 Westwick, 'Lessons', p. 360, and Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 355, note 12.
94 PSSAP7, appendix 1, paragraph 5.
95 Interview with David Hobson, 1 March 2002.
96 Interview with Michael Renshall, 17 June, 2002.
97 Tweedie and Whittington, *The Debate on Inflation Accounting*, pp. 79–80 and 'Inflation inquiry committee members named', *Accountancy*, March 1974, p. 10.
98 Tweedie and Whittington, *The Debate on Inflation Accounting*, p. 80.
99 Ibid. p. 353, note 19; see also Westwick, 'Lessons'.
100 Westwick, 'Lessons', p. 357.
101 There are the usual problems about proving a negative. Much of the relevant documentation (for example the minutes of the ICAEW Technical Committee and its sub-committees) does not appear to have survived in the official archives.
102 Interview with Michael Renshall, 17 June 2002.
103 Lord Benson, *Accounting for Life*, London: Kogan Page, 1989. The remedy for bedwetting, eating a raw mouse sandwich, is at p. 90.

104 Interview with Sir John Grenside, 27 March 2002.
105 See pp. 91–92.
106 'The British historian A. J. P. Taylor used to delight in provoking more sober historians by positing tiny causes for vast events. The First World War, for instance, in his view was caused by railway timetables, because this locked the belligerent powers into a sequence of troop mobilisations and war declarations from which they could not escape.' (R. J. Evans, *In Defence of History*, London: Granta, 1997, p. 132).
107 Interview with Chris Westwick, 10 July, 2002.
108 Interview with Sir Douglas Morpeth, 3 July 2002.

5 The Holy Grail

1 Quoted in 'The search for the Holy Grail', Accountancy Age, 25 January 1980, p. 11.
2 Quoted in 'Framework that fails to bear fruit', Accountancy Age, 21 March 1980, p. 15, describing work on the Financial Accounting Standards Board's conceptual framework project.
3 '*Accountancy* talks to the President', *Accountancy*, December 1969, p. 937, cited in S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and an Analysis of Trends*, Champaign, Illinois: Stipes, 1972, note 97.
4 Sir Ronald Leach, 'The birth of British accounting standards', in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards: The First Ten Years*, Cambridge: Woodhead-Faulkener, 1981, p. 5.
5 See p. 48.
6 Report of the ASSC, 6 May 1970, Minutes of the Ordinary Meeting of the ICAEW Council, 12 May 1970, ICAEWA/MK, Attachment 1, paragraph (c).
7 'New accounting reforms to be felt soon', *Financial Times*, 30 April 1970, p. 10, cited in Zeff, *Forging Accounting Principles in Five Countries*, p. 49.
8 Institute of Chartered Accountants in England and Wales, *Annual Report 1970*, London: ICAEW, 1971, p. 5, cited in Zeff, *Forging Accounting Principles in Five Countries*, p. 49.
9 'Research – A matter of principle', *Accountancy Age*, 7 May 1971, p. 7.
10 Zeff, *Forging Accounting Principles in Five Countries*, p. 49.
11 Editorial, *Accountancy Age*, 14 May 1971, p. 7.
12 'International Centre for Research in Accounting', *The Accountant's Magazine*, October 1971, p. 513.
13 See p. 12.
14 Zeff, *Forging Accounting Principles in Five Countries*, p. 50.
15 For a historical survey of the role of academics in the accounting policy process, contrasting the English and German context, see Power, M., 'Academics in the accounting policy process: England and Germany compared', in C. Leuz, D. Pfaff and A. G. Hopwood (eds), *The Economics and Politics of Accounting: International Perspectives on Research Trends, Policy and Practice*, Oxford: Oxford University Press, 2004, pp. 376–92.
16 See, for example, 'Auditing the auditors', *The Times*, 11 September 1969, p. 25.
17 Zeff, *Forging Accounting Principles in Five Countries*, pp. 224–30, and Study Group on the Objectives of Financial Statements, *Objectives of Financial Statements*, New York: AICPA, 1973.
18 See Zeff, *Forging Accounting Principles in Five Countries*, pp. 14–23.
19 ASSC, *The Corporate Report*, 1975, p. 1.
20 Interview with Michael Renshall, 17 June 2002.
21 Working Group of the Labour Party Industrial Policy Sub-Committee, *The Community and the Company: Reform of Company Law*, London: The Labour Party, 1974.
22 Interview with Michael Renshall, 17 June 2002.

23 D. P. Tweedie, 'Standards, objectives and "The Corporate Report"', in Leach and Stamp, *British Accounting Standards*, 1981, p. 174.
24 Interview with Derek Boothman, 24 February 2003.
25 Tweedie, 'Standards, objectives and "The Corporate Report"', p. 174.
26 ASSC, *The Corporate Report*, appendix 7.
27 Ibid., paragraph 1.1.
28 Ibid., paragraph 1.9.
29 Ibid., paragraph 3.2.
30 R. R. Sterling, '"A Statement of Basic Accounting Theory": A review article', *Journal of Accounting Research*, 1967, p. 100.
31 ASSC, *The Corporate Report*, paragraphs 4.29–30.
32 Ibid., chapter 6.
33 Ibid., paragraph 8.17.
34 ASC, Comment Letters on 'The Corporate Report', Edey Archive, Box 9.
35 'Company remains unconvinced', *Accountants Weekly*, 30 April 1976, p. 8.
36 Ibid.
37 See p. 120.
38 'Company remains unconvinced', *Accountants Weekly*.
39 'ASC gives its backing to The Corporate Report', *Accountants Weekly*, 7 May 1976, p. 5.
40 Ibid.
41 Tweedie, 'Standards, objectives and "The Corporate Report"', p. 176.
42 'ASC – Cautious welcome for Corporate Report', *Accountancy Age*, 23 July 1976, p. 2.
43 'ASC plays it cool', *Accountants Weekly*, 23 July 1976, p. 8.
44 ASSC, *The Corporate Report*, paragraph 6.7.
45 B. A. Rutherford, 'Value added as a focus of attention for financial reporting: Some conceptual problems', *Accounting and Business Research*, 1977, 7:29, and B. A. Rutherford, 'Published statements of value added: A survey of three years' experience', *Accounting and Business Research*, 1980, 11:41.
46 M. F. Morley, *The Value Added Statement*, Edinburgh: ICAS, 1978, and M. Renshall, R. Allan and K. Nicholson, *Added Value in External Financial Reporting*, London: ICAEW, 1979.
47 Tweedie, 'Standards, objectives and "The Corporate Report"', p. 176.
48 Department of Trade, *The Future of Company Reports* (Cmnd. 6888.), London: HMSO, 1977.
49 'Scots President slams Corporate Report', *Accountants Weekly*, 24 June 1977, p. 5.
50 Tweedie, 'Standards, objectives and "The Corporate Report"', p. 176.
51 Interview with Michael Renshall, 17 June 2002. Some of *The Corporate Report*'s ideas, including narrative reporting and disclosure of objectives and future prospects, have found a place in the modern canon (correspondence from Michael Renshall, 25 April 2005).
52 See pp. 61–66.
53 ED2, paragraph 2, and SSAP2, paragraph 2.
54 ED2, paragraph 14, and SSAP2, paragraph 14.
55 SSAP2, paragraph 2.
56 Interview with Michael Renshall, 17 June 2002.
57 Accounting Principles Board, Statement No. 4 'Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises', October 1970.
58 M. Moonitz, *The Basic Postulates of Accounting* (Accounting Research Study No. 1), New York: AICPA, 1961.
59 P. Grady, *Inventory Of Generally Accepted Accounting Principles For Business Enterprises* (Accounting Research Study No. 7). New York: AICPA, 1965.
60 SSAP2, paragraph 14(d). The statement was actually made, somewhat curiously, within the *definition* of the accruals concept.

61 For critical comments, see, for example, B. Underdown and P. J. Taylor, *Accounting Theory and Policy Making*, London: Heinemann, 1985, pp. 46–49, and B. Carsberg and C. W. Noke, *The Reporting of Profits and the Realisation Concept*, London: ICAEW, 1989. For the adoption of the concepts more widely, see p. 115.
62 For a full account of the work up to 1985, see P. Gore, *The FASB Conceptual Framework Project 1973–1985: An Analysis*, Manchester: Manchester University Press, 1992.
63 See p. 158.
64 ASC, *Setting Accounting Standards: A Consultative Document*, 1978, paragraph 7.7.
65 Tweedie, 'Standards, objectives and "The Corporate Report"', p. 179.
66 Interview with Graham Ward, 18 September 2003.
67 Macve told the British press that he would be visiting the FASB to study their progress first-hand. This was described in *Accountancy Age* in the following terms: 'Standard-setters in Britain and America are to cooperate closely on a project to draw up a conceptual framework for accounting' ('US and UK link for framework', *Accountancy Age*, 1 June 1979, p. 1). For some, at least, fog in the channel still closed the continent.
68 R. Macve, *A Conceptual Framework for Financial Accounting and Reporting: The Possibilities for an Agreed Structure*, London: ICAEW, 1981.
69 Ibid. pp. 82–84.
70 See, for example, 'A conceptual framework? It still all depends what you mean . . . ', *Accountancy*, November 1981, p. 11, and 'US conceptual ideas snubbed', *Accountancy Age*, 19 June 1981, p. 3.
71 I. F. H. Davison, *The Accounting Standards Committee 1982–1984* (Julian Hodge Lecture to The University of Wales, 12 February 1985), London: Arthur Andersen & Co., 1985, p. 18.
72 Interview with Michael Renshall, 17 June 2002, and see the quotations at the head of this chapter.
73 See, for example, P. B. W. Miller and R. J. Redding, *The FASB: The People, the Process, and the Politics*, Homewood, Illinois: Irwin, 1986, pp. 115–16.
74 Quoted in ibid., p. 115.
75 See, for example, Miller and Redding, *The FASB*, and P. Gore, 'A response to the revised Exposure Draft of the Statement of Principles', in M. Mumford and M. J. Page (eds), *Trying Again: Proceedings of the ACCA Conference on the ASB's 1999 Revised Draft Statement of Principles*, London: ACCA, 1999.
76 International Accounting Standards Committee, 'Framework for the Preparation and Presentation of Financial Statements', July 1989.
77 D. Solomons, *Guidelines For Financial Reporting Standards*, London: ICAEW, 1989. The addressee is given on the title page.
78 G. Whittington, 'Accounting standard setting in the UK after twenty years: A critique of the Dearing and Solomons reports', *Accounting and Business Research*, 1989, 19:75.
79 Renshall, quoted in 'Time to stitch up an old wound', *Accountancy Age*, 13 October 1988, p. 17.
80 ASC, Foreword to the IASC 'Framework for the Preparation and Presentation of Financial Statements', December 1989, paragraph 3. See p. 263.
81 'The Accounting Standards Committee and the Academic Community: Establishing Closer Links', Address by Anthony Carey, undated, ASCA, 1/26/3, p. 1. Internal evidence suggests that the speech was given some time after 1 January, 1988.
82 See, for example, pp. 240–41.
83 'The Accounting Standards Committee and the Academic Community', undated, p. 4.

84 For a review of the role of academics in UK accounting standardization, see Power, 'Academics in the Accounting Policy Process'. Very few studies of the type described here have been undertaken in the UK, largely because of the small size of the academic community and the limited opportunities, compared to the USA. For an account of one US attempt to involve academics in standard-setting along the lines suggested here, see R. Van Riper, *Setting Standards for Financial Reporting: FASB and the Struggle for Control of a Critical Process,* Westport, Connecticut: Quorum Books, 1994, p. 33.

85 J. G. Chastney, *True and Fair View – History, Meaning and the Impact of the Fourth Directive*, London: ICAEW, 1975, and B. A. Rutherford, 'The true and fair view doctrine: A search for explication', *Journal of Business Finance and Accounting*, 1985, 15:1. One senior finance director described the true and fair view doctrine as an 'outrageous nonsense imposed by an unrealistic law' ('Bowater's Tegner slams "true and fair view" as nonsense', *Accountancy Age*, 8 December 1978, p. 3).

86 Strictly speaking, the law *required* preparers to depart from detailed requirements if necessary to show a true and fair view but, since the meaning of the phrase was so vague, the provision was, in effect, generally discretionary.

87 See S. J. Gray and A. G. Coenenberg (eds), *EEC Accounting Harmonisation: Implementation and Impact of the Fourth Directive*, Amsterdam: North-Holland, 1984.

88 C. Nobes, 'The true and fair view requirement: Impact on and of the Fourth Directive', *Accounting and Business Research*, 1993, 24:93.

89 'Study Group steps forward on harmonisation', *Accountancy*, May 1973, p. 4.

90 Interview with Keith Robinson, 4 September 2003.

91 Ibid.

92 The opinion, by Leonard Hoffman QC and Mary H. Arden, is reproduced in *Accountancy*, November 1983, pp. 154–56. The paragraphs quoted are at p. 155.

93 Davison, *The Accounting Standards Committee 1982–1984*, p. 11.

94 See Whittington, 'Accounting standard setting in the UK after twenty years', p. 196.

95 See Rutherford, 'The true and fair view doctrine'.

96 Taylor and Turley, *The Regulation of Accounting*, p. 68.

97 Zeff was among the first to use the term ('The rise of economic consequences', *Journal of Accountancy*, December 1978). J. Blake ('A classification system for economic consequences issues in accounting regulation', *Accounting and Business Research*, 1992, 22:88) identifies discussion of the phenomenon dating back to the 1930s but there was little systematic treatment of it in the academic or professional literature until the 1970s.

98 See Blake, 'A classification system', pp. 312–13.

99 Ibid.

100 See p. 82.

101 See pp. 77–78.

102 See, for example, the summary in B. Rees, *Financial Analysis*, London: Prentice Hall, 1995, chapter 6, and S. P. Kothari, 'Capital markets research in accounting', *Journal of Accounting and Economics*, 2001, 31.

103 See pp. 66–70 and 202–209.

104 Blake, 'A classification system', p. 307.

105 D. Solomons, 'The politicisation of accounting', *Journal of Accountancy*, November 1978, p. 71.

106 Taylor and Turley, *The Regulation of Accounting*, pp. 68–69.

107 D. Tonkin, 'Politics and accounting standards', *Accountancy*, April 1981.

108 R. Hines, 'Financial accounting: In communicating reality, we construct reality', *Accounting, Organisations and Society*, 1988, 13:3, and T. Tinker, 'The accountant as partisan', *Accounting, Organisations and Society*, 1991, 16:3.

109 See p. 83–84.

110 R. D. Hines, 'The FASB's conceptual framework, financial accounting and the maintenance of the social world', *Accounting, Organisations and Society*, 1991, 16:4.

6 The Going Gets Tougher: 1975–1979

1 ASC, *Setting Accounting Standards: A Consultative Document*, 1978, section 1.3.
2 The amended constitution came into effect from 1 February 1976. It is included in ASC, *Setting Accounting Standards: A Consultative Document*, 1978, appendix 2. See also P. Taylor and S. Turley, *The Regulation of Accounting*, Oxford: Basil Blackwell, 1986, chapter 4 and 'Committee restructured', *Accountants Weekly*, 6 February 1976, p. 8. According to internal documentation, the ASSC was renamed the Accounting Standards (Joint) Steering Committee in October 1971, following the admission of the Association of Certified Accountants and Institute of Cost and Works Accountants as associate members (ASCA, 5/3/5). This title does not appear to have been used publicly.
3 Correspondence from Michael Renshall, 25 April 2005.
4 Ibid.
5 Interview with Chris Westwick, 10 July 2002.
6 Paragraph 19.
7 'Meeting new challenges', *Accountancy Age*, 2 April 1976, p. 7.
8 ASC, *Setting Accounting Standards: A Consultative Document*, section 1.2.
9 For further biographical details, see C. N. MacKay, '£5 train fare decided his career', *Accountancy*, April 1978.
10 Quoted in 'The tortoise of the profession ends his race', *Accountancy Age*, 1 July 1982, p. 14, which contains further biographical details. See also G. Holmes, 'Tom Watts – A dedicated European takes his bow', *Accountancy*, June 1982.
11 'New ASC chairman takes a hard look at its future role', *Accountants Weekly*, 13 January 1978, p. 3.
12 'Inquiry reviews how ASC works', *Accountancy Age*, 13 January 1978, p. 1.
13 Ibid.
14 See chapter 7.
15 'ASC change of balance', *Accountants Weekly*, 9 June 1978, p. 10.
16 'Sir Ronald bids farewell to the ASC', *Accountancy Age*, 2 July 1976, p. 3.
17 Membership at 1 June 1978 is listed in ASC, *Setting Accounting Standards: A Consultative Document*, appendix 7.
18 'ASC Study Group will dig deep', *Accountancy Age*, 20 January 1978, p. 3.
19 'Inquiry reviews how ASC works', *Accountancy Age*.
20 'Sir William stays on', *Accountants Weekly*, 31 March 1978, p. 8.
21 See Taylor and Turley, *The Regulation of Accounting*, chapter 9, and Lord Benson, *Accounting for Life*, London: Kogan Page, 1989, chapter 6.
22 International Accounting Standards Committee, Preface to Statements of International Accounting Standards, 1975, paragraph 2.
23 This was reported to the ASSC at its meeting of 12 December 1973, ASCA, 4/2, microfilm 0003/1–3.
24 IASC, Preface to Statements of International Accounting Standards, paragraph 10.
25 See p. 149.
26 'An extraordinary state of affairs', *Accountancy Age*, 23 May 1975, pp. 14–15; at p. 14.
27 'That sixth standard will be changed', *Accountants Weekly*, 14 March 1975, p. 9.
28 Ibid. and 'Seven-months delay over standard angers trusts', *Accountancy Age*, 8 August 1975, p. 2.
29 See pp. 276–77.
30 See pp. 177–92.
31 'Heavy stand against SSAP9', *Accountants Weekly*, 11 June, 1976 p. 8.
32 See p. 237.
33 'Anger over new standard', *Accountants Weekly*, 6 June, 1975 p. 8, and 'Arguing the stock change', *Accountancy Age*, 9 December 1977, p. 13.

34 'Arguing the stock change', *Accountancy Age*.
35 'Sugar accounts ignore standards once again', *Accountancy Age*, 16 February 1979, p. 3.
36 S. Davidson, 'LIFO or market and compulsory tax reporting requirements', *Journal of Accounting Research*, 1965, 3:1; and see 'Reagan's budget set to ease LIFO conformity', *Accountancy Age*, 23 January 1981, p. 4.
37 'Tootal's "Catch 22" leads to SSAP9 qualification', *Accountancy Age*, 3 June 1977, p. 5.
38 'Wedgwood has doubts on SSAP9', *Accountancy Age*, 17 June 1977, p. 6; 'The perils of SSAP9: Being kind to be cruel', *Accountants Weekly*, 8 December 1978, pp. 8–9; and 'Steetley disagrees', *Accountancy Age*, 1 April 1977, p. 4.
39 See pp. 75–81.
40 SSAP9, appendix 3, paragraph 9. The following paragraphs draw on B. A. Rutherford, 'Creative compliance and behaviour in response to mandatory changes in accounting policy: Three cases from Pre-Dearing Britain', *Accounting History*, 1999, 4:1.
41 '"Bad accountancy" attack on new stocks standard', *Accountancy Age*, 29 August 1975, p. 3.
42 Quoted in 'Industrial challenge to stocks standard fails', *Accountancy Age*, 3 September 1976, p. 1. The minutes of the ASC meeting of 23 August 1976, record that 'it was agreed that the matters referred to in [the letters from Edge-Partington and Norris] had been discussed in detail by the Committee when SSAP9 was prepared and that there were no grounds at the moment for recommending deferment of the starting date for this Standard.' (Edey Archive, Black Binder). Seasoned bureaucrats would accept Norris' characterization of this as a dusty reaction.
43 'Industrial challenge to stocks standard fails', *Accountancy Age*, 3 September 1976, p. 1.
44 Quoted in 'Fairclough takes swipe at "unrealistic standard"', *Accountancy Age*, 15 April 1977, p. 5.
45 S. Mansell, 'Breaking down the work-in-progress disparity', *Accountants Weekly*, 3/10 June, 1977, p. 11.
46 'Builders dig heels in over SSAP9', *Accountants Weekly*, 2 June 1978, p. 3, and 'SSAP9: Tysons is now in step', *Accountants Weekly*, 13 June 1980, p. 4.
47 See p. 3.
48 GEC, Annual Report and Accounts for the year ended 31 March 1976, p. 9.
49 GEC, Annual Report and Accounts for the year ended 31 March 1977, p. 9.
50 Principally in Rutherford, 'Creative compliance'.
51 This definition is drawn from Rutherford, 'Creative compliance', p. 33, where it is adapted from D. McBarnet, and C. Whelan, 'The elusive spirit of the law: Formalism and the struggle for control', *The Modern Law Review*, 1991, 54:4, p. 848. McBarnet and Whelan are writing about *legal* rather than regulatory frameworks. For an account of creative compliance in a later phase in the ASC's history, see A. K. Shah, 'Creative compliance in financial reporting', *Accounting Organizations and Society*, 1996, 21:1.
52 SSAP9, paragraph 23.
53 'Bowater Group rejects SSAP8', *Accountants Weekly*, 30 April 1976, p. 8.
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7 Reforming the System

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> Having read *Forging Accounting Principles in Five Countries* by Professor Zeff . . . and observed the painstaking way he pieces together the genesis of accounting self-regulation from the distant recollections of those who took part, I have resolved to make the path of the future historian of self-regulation that much easier by setting my recollections down in the form of a personal memoir. (p. 1).

This historian is very grateful.

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181 'Revamp for ASC aims to strengthen standards', *Accountancy Age*, 3 June 1982, p. 1.
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216 Ibid., paragraph, 2.1.6.
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218 Ibid., paragraph, 3.7.
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221 Ibid., paragraph, 3.10.
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225 See p. 166.
226 Davison, *The Accounting Standards Committee 1982–1984*, p. 1.
227 Ibid. p. 2. The agreement that Davison would serve only two years rather than the normal three-year term was not widely known at the time and what appeared to be an early departure caused some surprise (correspondence from Michael Renshall, 30 May 2005).
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261 The latter point is made by Peter Holgate, interview, 2 September 2003.
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263 Letter from Peter Holgate to Peter Godfrey, 17 April 1986, ASCA, 2/104/2.
264 Letter from Susan Baker to Mr Waggott, 2 June 1986.
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268 Ibid. The quality of the staff is also attested to by, for example, Michael Renshall (interviewed 17 June 2002) and Christopher Morgan (interviewed 31 October 2002).
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33 Analysis of submissions on ED21 by the author. Submissions are held in the ICAEW Library. The difference between the number of submissions in the official archive and the figure quoted in Appendix 9 is probably attributable to a respondent asking for confidentiality.
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35 Submission on ED21 from Dowty Group Limited.
36 Submission on ED21 from Steel Brothers and Company Ltd.
37 See p. 179.
38 See pp. 137–44.
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9 Accounting for Changing Prices: The Struggle Continues — and Ends Badly

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288 Accounting Standards Board, FRED1 'The Structure of Financial Statements – Reporting of Financial Performance', 1991, Accounting Standards Board, UITF Abstract 2 'Restructuring Costs', 31 October 1991, and, Accounting Standards Board, FRS3 'Reporting Financial Performance', October 1991. The term 'home grown' is used here to exclude standards following directly on from exposure drafts in issue at the point at which the new standard-setting machinery was established.
289 See pp. 147–48.
290 C. Nobes, *Depreciation Problems in the Context of Historic Cost Accounting*, London: Deloitte Haskins & Sells, 1984, sections 2.3 and 3.3.
291 See Nobes, *Depreciation Problems*, and B. A. Rutherford and R. T. Wearing, *Cases in Company Financial Reporting*, London: Harper & Row, 1987, case 4.
292 'A review of progress', *Accountancy*.
293 ASC, Discussion Paper 'A Review of SSAP12 – Accounting for Depreciation', December 1982.
294 See, for example, Nobes, *Depreciation Problems*.
295 SSAP12, paragraph 20 of the version issued in December 1977 and paragraph 21 of the version amended in November 1981 to exclude investment properties.
296 Nobes, *Depreciation Problems*, section 3.4.

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300 See Appendix 9.
301 See p. 242.
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303 ED37, paragraph 10.
304 SSAP12 (1977), paragraph 12.
305 ED37, paragraph 24. The surrounding text was slightly revised. The wording in ED37 survived into the revised standard.
306 Ibid., paragraph 25.
307 SSAP12 (1987), paragraph 10.
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309 Ibid., paragraph 10.
310 'Depreciation controversy', *Accountancy*, February 1987, p. 7.
311 Letter to members of the SSAP12 Working Party from Paul Ebling, Under-Secretary, ASC, 26 January 1987, ASCA, 1/37/1.
312 Paul Ebling, Acting Secretary of ASC, Commentary on ICAS Letter of 13 November 1986, ASCA, 1/37/1.
313 Letter to members of the SSAP12 Working Party, 26 January 1987.
314 Draft letter to Michael Renshall from Paul Ebling, Acting Secretary, ASC, 20 October 1986, ASCA, 1/37/1. Appended to the draft is a note from the author indicating that the letter was not sent because the matter was dealt with by telephone on 20 October.
315 Ibid.
316 Ibid., appended note.
317 Letter to Michael Renshall from Isobel Sharp, Director, Accounting and Auditing, ICAS, 13 November 1986, ASCA, 1/37/1.
318 Ibid.
319 Commentary on ICAS Letter of 13 November 1986.
320 Rutherford, 'Creative Compliance', pp. 46–47. The subject was dropped from the survey in 1993.
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322 SSAP12 (1987), paragraph 15.
323 A. Carey, *Depreciation: The Time for Change*, London: ICAEW, 1993.
324 Ibid. p. 68. The standard contained no advice on how appropriateness was to be determined. Had there been an academic member of the working party, he or she could have explained the overwhelming logic behind Arthur Thomas' famous (within universities) demonstration that no such advice can be inferred from the economic substance of asset use, see A. L. Thomas, *The Allocation Problem in Financial Accounting Theory*, (Studies in Accounting Research No. 3), Evanston, Illinois: American Accounting Association, 1969, and *The Allocation Problem: Part Two* (Studies in Accounting Research No. 9), Sarasota, Florida: American Accounting Association, 1974.
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328 'Ignorance is not always bliss', *Accountants Weekly*, 15 August 1980, pp. 10–11.

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330 'Ignorance', *Accountants Weekly*, p. 11.
331 '"Take stock of SSAP9" call', *Accountancy Age*, and interview with Professor Christopher Nobes, 23 July 2003. The use of LIFO was advocated by James Carty in responding to a later review of SSAP9, 'Revised SSAP9 in progress', *Accountancy Age*, 8 October, 1987, p. 2.
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333 'Brokers put dent in stocks standard', *Accountants Weekly*.
334 See p. 169.
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336 Ibid., paragraph 90.
337 Consultative Committee of Accountancy Bodies, TR481 'The Determination of Realised Profits and Disclosure of Distributable Profits in the Context of The Companies Acts 1948 to 1981', 1982, reproduced in *Accountancy*, October 1982, pp. 122–23.
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340 Ibid., paragraph 89.
341 A. Hardcastle and M. Renshall, *The Companies Act 1981 Handbook*, London: ICAEW, 1981, section 3.27.
342 'SSAP9 and the Companies Acts – Impasse?' *Accountancy*, April 1983, pp. 19–20.
343 Companies Act 1948, section 149, as amended by the Companies Act 1981.
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347 'Impasse?' *Accountancy*, p. 20.
348 'ASC backs down', *Accountancy*.
349 Institute of Chartered Accountants in England and Wales, *Financial Reporting 1984–85: A Survey of UK Published Accounts*, London: ICAEW, 1984, pp. 254–56.
350 'Impasse?' *Accountancy*.
351 Quoted in 'Work-in-progress – Technical Release due', *Accountancy*, May 1983, p. 5.
352 'ASC backs down', *Accountancy*.
353 Ibid.
354 'ASC looks at long-term work-in-progress', *Accountancy*, May 1985, p. 21.
355 Ibid.
356 ED40 'Stocks and Long-term Contracts', paragraph 29(c).
357 S. Crook, J. Pakulski and M. Waters, *Postmodernisation: Change in Advanced Society*, London: Sage, 1992, p. 32. Incredulity towards meta-narratives is the defining characteristic of postmodernism according to one of its principal theorists, Jean-François Lyotard (*The Postmodern Condition: A Report on Knowledge*, translated by G. Bennington and B. Massumi, Manchester: Manchester University Press, 1984).
358 International Accounting Standards Committee, IAS11 'Accounting for Construction Contracts', March 1979.
359 For example in 'Proposals for changes to SSAP9 "Stock and work in progress" as regards accounting for long-term contract work in progress', attachment 5 to the agenda of the Working Party on SSAP9 meeting of 3 April 1986, ASCA, 1/12/2.
360 Ibid.
361 Letter from Ann Wilks, DTI, to Philip Pawson, Under-Secretary, ASC, 4 July 1986, ASCA, 1/12/2.

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363 Ibid., paragraph 11.
364 Letter from Michael Renshall to Philip Pawson, Under-Secretary, ASC, 20 May 1986, ASCA, 1/12/2.
365 Interview with Christopher Morgan, 31 October 2002.
366 Davies, Paterson and Wilson, *UK GAAP*, 1989, section 7.2.
367 G. Dick and R. Rikert, *Accounting Trends and Techniques 1973*, New York: American Institute of Certified Public Accountants, 1973, pp.107–8.
368 Letter from I. J. Till, Group Chief Accountant, Shepherd Building Group Ltd., to Peter Holgate, ASC, 28 April 1986, ASCA, 1/12/2, capitalization in the original.
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372 ASC, *ASC Report*, No 3.
373 'Scots defer decision on SSAP11 amendment', *Accountancy Age*, 30 June 1988, p. 1.
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380 Ibid., paragraph 1.3.
381 W. Nixon, 'Finding a solution'.
382 Ibid.
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387 Ibid.
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392 ASC, *ASC Report*, No. 6.
393 Ibid. p. 161.
394 E. Hodgson, 'When is a cost really new?' *Accountancy*, March 1990, pp. 28–29.
395 Ebling, 'Fixed assets'.
396 B. A. Rutherford, 'How many ways can a value go down?' *Accountancy*, September 1990.
397 ED51, paragraph 1.3.
398 Ibid., paragraph 18.
399 'Cash flows or funds flows?', *Accountancy*, July 1989, p. 30.
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404 Ibid., paragraph 91.
405 As found, for example, in SSAP2.

406 B. Carsberg and C. W. Noke, *The Reporting of Profits and the Realisation Concept*, London: ICAEW, 1989.
407 Marking to Market under the Companies Act 1985, Note of a Meeting with DTI staff, ASC, 6 April 1990, author's files.
408 Ibid.
409 ED55, paragraph 1.6.
410 Ibid
411 Note to Members of the ASC's Investments Working Party from Martin Evans, Under-secretary, ASC, 4 June 1990, author's files.
412 Accounting for Investments: Note of a Discussion at ASC on 25 July 1990, ASC, author's files.
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414 R. Macve, 'Investments: Conceptual clarity v legal muddle', *Accountancy*, March 1991, p. 85.
415 A. Wilson, M. Davies, M. Curtis and G. Wilkinson-Riddle, *UK and International GAAP: Generally Accepted Accounting Practice in the United Kingdom and under International Accounting Standards*, Seventh edition; London: Tolley, 2001, p. 1081.
416 C. Harrison, P. Barden and K. Rigelsford, *GAAP 2004: UK Financial Reporting and Accounting*, Kingston, Surrey: Croner CCH, 2004, p. 553.
417 ASC, TR808 'Final Report and Recommendation of ASC to CCAB', August 1990.
418 Quoted in 'ASC hands over its hot potato', *Accountancy*, September 1990, p. 14.
419 Ibid.
420 1970 – 74: 13; 1975 – 79: 12; 1980 – 84: 10; 1985 – 89: 11.
421 Quoted in 'ASC hands over', *Accountancy*, p. 14.
422 See p. 170.
423 'A SORP will be issued when a need is seen for a pronouncement on a specific topic, but when that topic does not meet all of the criteria for an accounting standard. Although companies will be encouraged to comply with SORPs, compliance will, unlike standards, not be mandatory' (ASC, *Review of the Standard-Setting Process,* 1983, paragraph 2.1.6). See also Davison, *The Accounting Standards Committee 1982–1984*, p. 12.
424 'Hitch hits plans for specialist statement', *Accountancy Age*, 9 June 1983, p. 2.
425 See pp. 8–12.
426 Quoted in 'Hitch', *Accountancy Age*, p. 2.
427 Davison, *The Accounting Standards Committee 1982–1984*, p. 12.
428 ASC, TR808 'Final Report', and 'Accounting for insurance business', *Accountancy*, July 1990, p. 41.
429 ASC, *ASC Report*, No. 2, January 1988, reproduced in *Accountancy*, February 1988, pp. 161–62.
430 Interview with Brian Singleton-Green, 12 December 2002.
431 Explanatory Foreword to Accounting Standards (Revised August 1886), reproduced in *Accountancy*, September 1986, pp. 145–46.
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433 Explanatory Foreword to Accounting Standards (Revised August 1886).
434 'Is there a GAAP in small company standards?' *Accountancy*, August 1989, pp. 27–28.
435 ASC, *ASC Report*, No. 3, p. 173.
436 ASC, TR 690 'Statement on the Application of Accounting Standards to Small Companies', February 1988, reported in ASC, *ASC Report*, No. 3.
437 ASC, TR706 'Statement on the Definition of Small Company for the Purpose of Applying Accounting Standards', July 1988, and see 'Is there a GAAP?' *Accountancy.*
438 'CIMA is to review tax in SSAPs', *Accountancy Age*, 5 October 1989, p. 3.
439 Martin Evans, quoted in ibid.

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442 Ibid.

11 Setting Accounting Standards 1969–1990: Technical and Political Realms

1 I. F. H. Davison, *The Accounting Standards Committee 1982–1984* (Julian Hodge Lecture, delivered at the University of Wales, 12 February 1985), London: Arthur Andersen & Co., 1985, p. 20.
2 See p. 243.
3 Davison, *The Accounting Standards Committee 1982–1984*, p. 20.
4 See p. 249.
5 Davison, *The Accounting Standards Committee 1982–1984*, p. 20.
6 'Why the ASC should go it alone', *Accountancy*, September 1986, p. 16. The article was in fact suggested and largely drafted by Peter Holgate, at the time secretary of the ASC, but the sentiments it expressed were fully shared by Peter Godfrey (interview with Peter Godfrey, 17 December 2002).
7 'Odyssey', *Accountancy*, March 1987, p. 12, and 'Preparations for the Odyssey', *Accountancy*, May 1987, p. 11.
8 Interview with Michael Renshall, 17 June 2002, and 'ASC may become mirror image of FASB', *Accountancy*, August 1987, p. 5.
9 Quoted in 'ASC may become', *Accountancy*, p. 5.
10 Interview with Michael Renshall, 17 June 2002.
11 Correspondence from John Warne, 1 February 2005. The ICAEW Council had lost a resolution increasing subscriptions in 1985 and this undermined its confidence (and, possibly, the confidence of other CCAB Councils) that funding for expanded activity could be secured.
12 Interviews with Derek Boothman, 24 February 2003, Michael Renshall, 17 June 2002, and John Warne, 3 March 2003; 'A fundamental review', *Accountancy*, August 1987, p. 1, and 'ASC may become', *Accountancy*.
13 Interview with Desmond Wright, 14 August 2003.
14 Ibid.
15 'ASC may become', *Accountancy*, p. 5.
16 Interview with John Warne, 3 March 2003.
17 'Dearing to head ASC review body', *Accountancy*, November 1987, p. 6.
18 Interviews with Professor Christopher Nobes, 23 July 2003, and Desmond Wright, 14 August 2003. Wright, as ASC secretary, had been told that he could confirm to all staff they would be offered employment with the ICAEW when the ASC secretariat was wound up.
19 See chapter 10.
20 See, for example, S. A. Zeff, *Forging Accounting Principles in Five Countries: A History and an Analysis of Trends*, Champaign, Illinois: Stipes, 1972, and A. R. Rahman, *The Australian Accounting Standards Review Board: The Establishment of its Participative Review Process*, New York and London: Garland, 1992. Strictly speaking, these developments occur in Braudel's middle level, social time, and not in the slowest-moving geographical time of the *longue durée*; see R. J. Evans, *In Defence of History*, London: Granta, 1997, pp. 154–55.
21 'The tortoise of the profession ends his race', *Accountancy Age*, 1 July 1982, p. 14.
22 B. Singleton-Green, 'The rise and fall of the ASC', *Accountancy*, August 1990.
23 Ibid. p. 85.
24 Ibid.
25 See p. 248.

26 G. Whittington, 'Accounting standard setting in the UK after twenty years: A critique of the Dearing and Solomons reports', *Accounting and Business Research*, 1989, 19:75, p. 195.
27 G. Holmes, 'Birthday reflections on things to come', *Accountancy*, July 1989, p. 69.
28 Michael Renshall wrote a reply vigorously rebutting the charge, Letter from Michael Renshall to The Editor of the Financial Times, 7 November 1988, ASCA, 1/34/1.
29 Apart from anything else, failure to deliver a solution to the price change accounting problem undermined civil servants' confidence in the profession.
30 Interview with Brian Singleton-Green, 12 December 2002.
31 C. Pong and G. Whittington, 'The withdrawal of current cost accounting in the United Kingdom: A study of the Accounting Standards Committee', *Abacus*, 1996, 32:1, p. 51.
32 Interview with Desmond Wright, 14 August 2003.
33 Interview with Professor Christopher Nobes, 23 July 2003.
34 Interview with Brian Singleton-Green, 12 December 2002.
35 P. Taylor and S. Turley, *The Regulation of Accounting*, Oxford: Basil Blackwell, 1986, pp. 135–36.
36 See p. 198.
37 Interview with Professor Christopher Nobes, 23 July 2003.
38 C. Nobes, 'A political-history of goodwill in the UK – An illustration of cyclical standard setting', *Abacus*, 1992, 28:2, p. 146. Nobes points out that other ASC standards offering options, where no similar alternatives were permitted in the USA, included SSAPs 4, 13, 20, 23 and 24.
39 Interview with Peter Godfrey, 17 December 2002, and Nobes, 'A political-history'.
40 Whittington, 'Accounting standard setting', p. 196.
41 Interview with Professor Christopher Nobes, 23 July 2003.
42 Nobes, 'A political-history'. See also D. Solomons, 'The political implications of accounting and accounting standard setting', *Accounting and Business Research*, 1983, 13:50, pp. 116–17.
43 Interview with Professor Christopher Nobes, 23 July 2003, and Nobes, 'A political-history'.
44 See chapter 7.
45 Interview with Ian Hay Davison, 13 June 2002.
46 Interview with Professor Christopher Nobes, 23 July 2003.
47 Some, for example Brian Singleton-Green, argue that the increase in resourcing post-Dearing was not a significant factor in the performance of the new regime (interview with Brian Singleton-Green, 12 December 2002).
48 Interview with John Warne, 3 March 2003.
49 The correspondence is in ASCA, 5/3/6.
50 Interview with Peter Godfrey, 17 December 2002.
51 See p. 166.
52 Interview with Peter Godfrey, 17 December 2002.
53 Interviews with Ian Hay Davison, 13 June 2002, and Keith Robinson, 4 September 2003.
54 Interview with Ian Hay Davison, 13 June 2002.
55 Interview with Keith Robinson, 4 September 2003.
56 Ibid.
57 The correspondence is in ASCA, 2/53/1
58 Interview with Ian Hay Davison, 13 June 2002.
59 Davison, *The Accounting Standards Committee 1982–1984*; this view is shared by Peter Godfrey, interview with Peter Godfrey, 17 December 2002.
60 K. Shackleton and S. Walker, *A Future for the Accountancy Profession: The Quest for Closure and Integration 1957–1970*, Edinburgh: Institute of Chartered Accountants of Scotland, 2001.

61 See pp. 161–65.
62 Whittington, 'Accounting standard setting', p. 195; see pp. 295–96.
63 See chapter 5.
64 See p. 263.
65 See pp. 258–64.
66 See p. 267.
67 See p. 248.
68 Whittington, 'Accounting standard setting', p. 197.
69 D. P. Tweedie, 'The ASC in chains: Whither self-regulation now?' *Accountancy*, March 1983.
70 Interview with Professor Christopher Nobes, 23 July 2003.
71 Whittington, 'Accounting standard setting', p. 197.
72 Correspondence from John Warne, 1 February 2005.
73 Whittington, 'Accounting standard setting', p. 197.
74 For an example of such advocacy, see G. J. Benston, 'Are accounting standards necessary?' in Sir Ronald Leach and E. Stamp (eds), *British Accounting Standards: The First Ten Years*, Cambridge: Woodhead-Faulkener, 1981.
75 See p. 48. Strict comparisons of output rates between standard-setters are difficult, not least because the scope of individual documents differ and revisions may result in a new pronouncement in one jurisdiction (adding to the work rate) but an amendment in another.
76 See p. 48.
77 See p. 26.
78 See p. 31.
79 D. Hanson, 'Developments in financial reporting over the last twenty years', in Institute of Chartered Accountants in England and Wales, *Financial Reporting 1988–89: A Survey of UK Reporting Practice* (London: ICAEW, 1989).
80 See pp. 64–65.
81 See pp. 80 and 123–24.
82 See p. 76.
83 See p. 54.
84 Hanson, 'Developments in financial reporting'.
85 Ibid. p. 24.
86 See p. 140.
87 S. A. Zeff, 'How the US accountancy profession got where it is today: Part I', *Accounting Horizons*, 17:3, 2003, pp. 197–98.
88 See p. 265.
89 See pp. 265–66.
90 See pp. 139 and 141.
91 See pp. 137–44.
92 S. A. Zeff, '"Political" lobbying on proposed standards: A challenge to the IASB', *Accounting Horizons*, 2002, 16:1. See pp. 128–36.
93 Zeff, *Forging Accounting Principles in Five Countries*, pp. 178–80 and 219–21.
94 Zeff, '"Political' lobbying', pp. 49–50.
95 Ibid. p. 50. In fairness, it should be pointed out that the political climate for US standard-setting is very different from that in the UK: see the sources cited in the previous two notes.
96 T. Hope and J. Briggs, 'Accounting policy making – Some lessons from the deferred taxation debate', *Accounting and Business Research*, 1982, 12:46, p. 87.
97 See p. 201.
98 See pp. 195–98.
99 See pp. 144–48, 209–14 and 277–81.
100 See pp. 190–92.
101 See p. 24.

102 For example, the need, imposed by an articulated system of financial statements, for all debits to be classified as assets, expenses, or reductions in equity, and the inability of the system to reflect probabilistic observations.
103 For a discussion of Taylor's views on this issue, see A. Sisman, *A. J. P. Taylor: A Biography*, London: Mandarin, 1995, pp. 127–28.
104 R. J. Evans, *In Defence of History*, London: Granta, 1997, p. 61.
105 G. J. Previts, L. D. Parker and E. N. Coffman, 'Accounting history: Definition and relevance', *Abacus*, 1990, 26:1, p. 5.
106 For a description of the post-Dearing regime and the migration to International Financial Reporting Standards, see A. Wilson, M. Davies, M. Curtis and G. Wilkinson-Riddle, *UK and International GAAP: Generally Accepted Accounting Practice in the United Kingdom and under International Accounting Standards*, Seventh edition; London: Tolley, 2001, chapter 1.
107 It is, perhaps, optimistic to think that it might also have avoided SSAP20 being constructed in a way that permitted Polly Peck's manoeuvre, which came to light at the very end of the ASC's life, of charging exchange losses on monetary items held in a rapidly depreciating currency against reserves while crediting the high interest earned to reflect the same circumstance in the profit and loss account. See D. Gwilliam and T. Russell, 'Polly Peck: Where were the analysts?' *Accountancy*, January 1991.
108 Whittington, 'Accounting standard setting', pp. 196 and 197.
109 For an analysis suggesting a conceptual framework would not have helped in the case of the deferred taxation debacle, see Hope and Briggs, 'Accounting policy making'.
110 The ASC's successor body and the FASB disagreed about whether goodwill in fact constitutes an asset of the entity to which it is attributable according to their respective conceptual frameworks, which do not differ in ways that easily explain this disagreement; see B. A. Rutherford, *An Introduction to Modern Financial Reporting Theory*, London: Paul Chapman Publishing, 2000, pp. 99–102.
111 This argument for a systematic approach is advocated by D. P. Tweedie and G. Whittington, 'Financial reporting: Current problems and their implications for systematic reform', *Accounting and Business Research*, 1990, 21:81, who cite the treatment of depreciation of property in SSAPs12 and 19 as an example of apparent inconsistency.
112 Not as straightforward as it may appear: all other things being equal, a larger committee will reduce the chances of a decision being made by a small majority, and thus being vulnerable to swing voting on the next occasion; but larger committees may be prone to intermittent attendance (for motivational reasons) and make individual members less conscious of the potential impact of a change in their vote.
113 R. K. Storey, *The Search for Accounting Principles*, New York: AICPA, 1964, p. 60.
114 C. A. Westwick, 'The lessons to be learned from the development of inflation accounting in the UK', *Accounting and Business Research*, 1980, 10:40.
115 See, for example, p. 222.
116 The role of *Accountancy Age* in publicizing, and perhaps stirring up, disagreement within the profession has already been alluded to (for example, on pp. 125–26); the magazine was read in the Treasury and the DTI and did little to improve confidence in the profession there (correspondence from John Warne, 1 February 2005).
117 Renshall rightly makes the point that the tone of openness was set by Leach in the early days of the committee's life as a response to previous criticism of the profession. Once adopted, it would have been difficult to reverse and a 'doctrine of secrecy' would have been equally likely to engender suspicion (correspondence, 30 May 2005). My suggestion is not intended to argue for secrecy but rather for more

carefully managed disclosure – for example giving fully considered target dates rather than 'off the cuff' aspirations.

118 See pp. 295–96.

119 See p. 248.

120 Where the analysis can be performed.

121 C. Pong and G. Whittington, 'The withdrawal of current cost accounting in the United Kingdom: A Study of the Accounting Standards Committee', *Abacus*, 1996, 32:1, p. 52.

122 See, for example, Westwick, 'Lessons', p. 368, and Pong and Whittington, 'Withdrawal', p. 52.

123 Though why the problem could not have been dealt with in other ways remains an open question; see p. 143.

124 Interviews with Professor Christopher Nobes, 23 July 2003, and Desmond Wright, 14 August 2003.

125 Zeff, *Forging Accounting Principles in Five Countries*, p. 331.

126 See Westwick, 'Lessons'.

127 The need to co-ordinate with the USA clearly complicates this question.

128 A point argued forcibly and specifically in the context of the early history of the ASC at a 1979 conference by, among others, Watts. See 'Errors inevitable claim', *Accountancy Age*, 29 June 1979, p. 3, and 'Accountants "unduly diffident" claims Watts', *Accountancy Age*, 6 July 1979, p. 9.

129 A point made several years before the establishment of the ASC by Storey, *The Search for Accounting Principles*, p. 63.

Appendix 1

Sources

1 Books, reports, scholarly articles and substantial articles in the professional press are included in the bibliography.
2 Statements of standard accounting practice and exposure drafts issued by the ASC are frequently referred to by their number alone; full details are to be found in Appendices 7 and 8 respectively. Where other ASC documents and the publications of other standard-setters are referred to, publication details are given in the notes.
3 Details of short articles in the professional press, unpublished items, interviews and legislation are given in the notes.
4 Material in archives is referred to in notes as follows:

ASCA	Accounting Standards Committee Archive, John Rylands University Library, University of Manchester (1/48/4 indicates File or Microfilm No. 4 in Box 1/48).
Edey Archive	Papers of Professor Harold Edey, London School of Economics and Political Science.
IASGA	Inflation Accounting Steering Group Archive, London School of Economics and Political Science.
ICAEWA/MK	Institute of Chartered Accountants in England and Wales Archive, held at the ICAEW Offices in Milton Keynes.
NA	National Archives.

Appendix 2

Statement of Intent on Accounting Standards in the 1970s

Embargoed until 12 December 1969

At the outset of the 1970s, the Council of the Institute of Chartered Accountants in England and Wales reaffirms its continuing determination to advance accounting standards. The Council issues the following statement for the information of directors, accountants, auditors and users of company accounts to make clear the steps the Council intends to take in pursuit of its aims in the field of accounting standards and as a reminder of some of the basic problems in the preparation of financial statements.

Accounting Standards

It is the Council's intention to advance accounting standards along the following lines:

1 *Narrowing the areas of difference and variety in accounting practice*
The complexity and diversity of business activities give rise to a variety of accounting practices justifiably designed for and acceptable in particular circumstances. While recognising the impracticability of rigid uniformity, the Council will intensify its efforts to narrow the areas of difference and variety in accounting practice by publishing authoritative statements on best accounting practice which will wherever possible be definitive.

2 *Disclosure of accounting bases*
The Council intends to recommend that when accounts include significant items which depend substantially on judgements of value, or on the estimated outcome of future events or uncompleted transactions, rather than on ascertained amounts, the accounting bases adopted in arriving at their amount should be disclosed.

3 *Disclosure of departures from established definitive accounting standards*
The Council intends to recommend that departures from definitive standards should be disclosed in company accounts or in the notes thereto.

4 *Wider exposure for major new proposals on accounting standards*
In establishing major new accounting standards the Council will provide an opportunity for appropriate representative bodies to express their views by giving wide exposure to its draft proposals.

5 *Continuing programme for encouraging improved accounting standards in legal and regulatory measures*
The Council will continue its programme of suggesting appropriate improvements in accounting standards established by legislation, of which the proposals in 'Companies Legislation in the 1970's' submitted to the President of the Board of Trade in March this year are an example. The Council will also continue to support and encourage the improvement of accounting standards in relevant regulatory measures such as the City Code on Take-overs and Mergers and Stock Exchange requirements.

Auditing

In support of the proposals on accounting standards outlined above, the Council will, after appropriate notice, recommend that if disclosure of accounting bases or of departures from definitive accounting standards is not made in the accounts or in notes then appropriate reference should be made in auditors' reports.

Support and Maintenance of Standards

The council will do all in its power to assist and support members in the observance of established standards. To this end, it intends to strengthen its machinery for investigating and pointing the lessons of lapses from standards.

Restatement of the Underlying Nature of Company Accounts

Those who prepare, audit and use company accounts should keep in mind the following essential points, against the background of which this statement of intent is issued.

Company accounts are presented by directors, not by auditors. The auditors' function is to express an independent opinion on the truth and fairness of the view presented by the accounts.

The activities of a company are continuous, whereas the period covered by the accounts is no more than an arbitrary segment of time out of a company's continuing existence. The determination of amounts of income and expenditure properly attributable to an accounting period, particularly in respect of uncompleted transactions, and of the amounts at which related items are shown in the balance sheet, can be arrived at only by informed judgement exercised in accordance with accounting conventions.

Implementation

The Council will forthwith establish machinery for furthering these proposals and to this end will seek the advice and assistance of representatives of industry, finance and commerce.

Appendix 3

Extracts from the Watts Report

Summary of Conclusions and Recommendations

Conclusions

Chapter 2

(a) Accounting standards are necessary and will continue to be necessary in order to complement statutory regulation. (Paragraphs 2.1–2.4)

(b) One of the main aims of the standards is to narrow the choice of accounting treatment so that financial statements are expressed in a common language to make them reasonably comparable one with another. (Paragraph 2.4)

(c) The tasks of the standards setting body will continue as far ahead as can be foreseen. No more standards should be produced than are necessary; nor should they be produced faster than recipients can fully absorb them, but the standards body must be equipped to meet the need for effective standards in an efficient and timely manner. (Paragraphs 2.5–2.10)

(d) Standards should continue to be used as definitive principles in financial statements and not merely as a benchmark against which deviations can be measured. (Paragraphs 2.12–2.13)

(e) A material departure from a standard should be permitted only in those exceptional circumstances where to adhere would fail to give a 'true and fair view'. This would involve a change to the Explanatory Foreword to SSAPs (by deleting the criterion of 'inappropriate') and should be accompanied by a review of existing standards. (Paragraphs 2.18–2.23)

(f) Although comparability might be aided if, in the event of a material departure from a standard, the financial effect of the departure were to be disclosed in the notes together with the reasons for the departure (irrespective of whether the departure is necessary for the giving of a true and fair view), any possible benefits would be outweighed by the practical disadvantages involved. (Paragraph 2.24)

Chapter 3

(a) Accounting standards should continue to be set in the private sector and not by the legislature, government department or government agency. (Paragraph 3.5)
(b) The standards setting body should consist primarily of accountants because of their skills in that field, but the wider public interest and the needs of users should be more clearly recognised in the membership of the ASC. Non-accountants should be appointed in appropriate cases. (Paragraphs 3.6–3.7)
(c) The ASC believes that the constitutional power to issue standards should remain with the CCAB Councils. However, the Councils should review with ASC their operating procedures so as to ensure there is adequate consultation at the formative stages with the intention of avoiding conflict with the findings of the standards body arrived at after due processes of consultation and debate. (Paragraphs 3.8–3.14)

Chapter 4

(a) Supervision of accounting standards should remain in the private sector. (Paragraph 4.5)
(b) A supervisory body, beyond the deterrent of a qualified audit report, is a necessary adjunct to accounting standards. (Paragraph 4.6)
(c) The CCAB and CSI should adopt the proposals (already accepted by the Stock Exchange) to establish a joint panel to review non-compliance with accounting standards by listed companies. (Paragraph 4.8)

Chapter 5

(a) For practical reasons some standards will need to be confined to large enterprises. (Paragraphs 5.2–5.4)
(b) If a standard applies only to large enterprises, then those enterprises excluded from the scope should disclose that fact and also whether they have complied voluntarily. (Paragraph 5.5)
(c) The ASC believes that specific industry standards should only be issued to deal with problems unique to major industries. (Paragraph 5.6)

Chapter 6

(a) Standards should be set only after the widest and most open consultation and debate and the ASC has already moved quickly towards that objective. (Paragraph 6.1)
(b) In future, discussion papers will be published for comment at an earlier stage in development of an accounting standard. (Paragraph 6.2)
(c) The ASC will continue to hold its own meetings in private but this policy will be reviewed periodically. (Paragraph 6.3)

(d) The Consultative Group should be involved more closely in the debates on accounting standards. (Paragraph 6.4)
(e) Increased 'openness' of the ASC's affairs has resulted in greater and regular press coverage. The ASC hopes to be able to issue in due course at modest cost regular progress reports for the press and other interested parties. (Paragraph 6.5)
(f) Substantial technical staff support for the ASC is needed. A 'director of accounting standards' should be appointed. (Paragraphs 6.6–6.7)
(g) The position of chairman of the ASC is almost full-time. At present it is an honorary position but it may not be possible to continue in this way indefinitely. (Paragraph 6.8)
(h) In so far as is practical the ASC staff will continue to give oral guidance in response to general enquiries. (Paragraph 6.9)
(i) Non-mandatory guidance notes are preferable to recommendations and are likely to prove a particularly useful adjunct to standards on complex subjects. (Paragraph 6.10)
(j) It is more appropriate to amend or supplement an existing standard using established procedures rather than issue authoritative interpretations. (Paragraph 6.11)

Chapter 7

(a) The ASC, having commissioned research into the possibility of developing an agreed conceptual framework for setting accounting standards, should devote further resources to this work. (Paragraph 7.1)

Chapter 8

(a) The ASC must devote time and effort to avoid, as far as possible, conflicting standards being set by the major standards setting countries. (Paragraph 8.4)
(b) The ASC believes that the reasons for any necessary significant differences between standards in the major territories should be made clear to the public and other standards setting bodies. (Paragraph 8.1)
(c) The ASC believes that it is essential to complement its co-operation with international bodies with direct relationships with other major standards setting bodies and by maintaining close links with the profession in Europe and throughout the world. (Paragraph 8.9)

Chapter 9

(a) The minimum cost (at present prices) of operating the standards setting body on the lines set out in this report would be £263,000 in its first full year (the governing bodies have already budgeted for a cost of almost £200,000 for 1981). In due course the cost could rise to £400,000 per annum. (Paragraph 9.2)

Recommendations to Governing Bodies

Chapter 2

(i) The explanatory foreword to SSAPs should be amended so as to permit a material departure from a SSAP only in those exceptional circumstances when to adhere would fail to give a true and fair view.

Chapter 3

(i) The constitution of the ASC should be changed to permit say four or five additional members, who need not be accountants, to be appointed to the ASC – these additional members should be nominated by the chairman of the CSI and/or the chairman of the Stock Exchange for appointment by the chairman of CCAB after consultation with the chairman of the standards body.
(ii) Although the constitutional power to set standards should remain with the Councils of the CCAB bodies, they should review with the ASC their operating procedures so as to ensure that there is adequate consultation at the formative stages in the standards setting process and to avoid the risk of being in conflict with the findings of the ASC arrived at after due processes of open consultation and debate.

Chapter 4

(i) The governing bodies should, as a matter of considerable importance, adopt the proposals to establish a joint panel to review non-compliance with accounting standards by listed companies, and should urge the CSI to do likewise.

Chapter 6

(i) A director of accounting standards should be appointed, being a person of a calibre somewhat equivalent to that of a technical partner in a major practising firm in the profession or the equivalent in industry or commerce.
(ii) Other adequate resources should be provided.

Source: ASC, *Setting Accounting Standards: Report and Recommendations*, 1981, pp. 39–43.

Appendix 1: Joint Panel to Review Non-Compliance with Accounting Standards

Objective

1 The objective of the Panel shall be to review cases of disclosed or apparent departure from accounting standards by companies whose securities are

listed on, or have been admitted to trading on, an organised market, being departures which in the opinion of the Panel are significant and merit examination.

Procedures

2 Cases for review would be derived from a number of sources, including:
   (a) referral by Quotations Department of the Stock Exchange;
   (b) referral by the Professional Standards Committee or equivalent committee of one of the accountancy bodies;
   (c) the general public.

3 Prior to review by the Panel, a factual brief on each case would be prepared, including an explanation of why the case is thought to merit examination.

4 Where the Panel decides that a case merits examination, the appropriate officers of the company and the auditors would be invited to submit comments in writing on the information assembled in the brief (a copy of which would have been sent to them) and to explain the basis for arriving at the particular accounting practice(s) in question. Thereafter the officers of the company, the auditors and any other interested parties might be invited to appear in person before the Panel.

5 A report on the evidence obtained, including such recommendations on the facts as might be appropriate, would be prepared and sent to the company, its auditors, the Stock Exchange, the accountancy body(ies) of which any party to the case is a member, the Accounting Standards Committee and the Council for the Securities Industry. The Panel could then publish the report at its own discretion.

6 If the Panel concluded the non-compliance was unjustified, the matter would normally be referred to the Stock Exchange to consider such action as may be appropriate.

7 If the Panel concluded that, in the light of all the circumstances, the text of the relevant accounting standard deserved re-examination, this would be referred to the ASC.

Annual report

8 The Panel shall prepare and deliver an annual report on the work of the Panel to the Stock Exchange, the Consultative Committee of Accountancy Bodies and the Council for the Securities Industry.

Composition of Panel

9 The Panel shall comprise seven members, one of whom shall be the Chairman.

10 The Chairman and members of the Panel shall be appointed jointly by the Chairmen for the time being of the Council for the Securities Industry, the Stock Exchange and the Consultative Committee of Accountancy Bodies.

11 The Chairman shall be appointed for an initial term of three years, but shall not be disqualified from re-appointment for a further term thereafter.

12 Members of the Panel, other than the Chairman, shall comprise:

(a) two qualified accountants, of whom only one shall be in public practice, to be nominated by the Chairman for the time being of the Consultative Committee of Accountancy Bodies;
(b) two Members of the Council of the Stock Exchange;
(c) a person appointed after consultation with the President of the Confederation of British Industry;
(d) a person appointed after consultation with the Chairman of the Institutional Shareholders' Committee.

13 Members of the Panel shall be appointed for a term of three years, except that the initial appointments shall be such that two members serve for two years, two members serve for three years and two members serve for four years. Casual vacancies shall be filled so that the composition of the Panel is maintained as described in paragraph 12.

14 Members of the Panel shall not regard themselves as representing sectional interests, but shall be guided by the need to act in the general interest.

15 The Panel may, for the purposes of an individual case under review, appoint one or more persons to act as technical adviser to the Panel and attend meetings of the Panel in that capacity, but persons so appointed shall not be members of the Panel, nor be permitted to exercise any of the powers or duties vested in a member of the Panel.

Source: ASC, *Setting Accounting Standards: Report and Recommendations*, 1981, appendix 1.

Appendix 4

Chairmen of the Accounting Standards Committee

Formation – 30 June 1976, Sir Ronald Leach
1 July 1976 – 31 May 1978, Sir William Slimmings
1 June 1978 – 30 June 1982, Thomas (Tom) R. Watts
1 July 1982 – 24 July 198, Ian H. Davison
25 July 1984 – 31 August 1986, Peter Godfrey
1 September 1986 – 31 July 1990, J. Michael Renshall

Note: Terms of office are as given in Institute of Chartered Accountants in England and Wales, *Accounting Standards 1990/91*, London: ICAEW, 1990. The establishment of the Accounting Standards Steering Committee was formally approved by the Council of the Institute of Chartered Accountants in England and Wales on 7 January 1970 but the committee had already met by then, on 2 January 1970. The formal notice of the first meeting, naming its members, was issued on 30 December 1969, by which date it might be considered that the committee had been formed.

Appendix 5

Secretaries to the Accounting Standards Committee

1969 – 1977 J. Michael Renshall
1977 – 1981 James P. Carty
1981 – 1983 Keith O. Robinson
1984 Brian Singleton-Green
1984 – 1986 Peter A. Holgate
1987 – 1990 Desmond Wright

Appendix 6

Members of the Accounting Standards Committee

Professional body membership and organisational affiliation

Name	*Body*[a]	*Affiliation*[b]
Adams, David H.	P	British Rail Pension Trustee Company Ltd.
Anderson, Gordon	S	Arthur Young
Anderson, J. N. (Ian)	S	Peat Marwick McLintock & Co.
Appleyard, George R.	E	Thorne, Lancaster & Co.
Artus, Ronald E.	-	Prudential Corporation Plc
Barrett, Francis J.	I	Arthur Andersen & Co.
Berman, Norman	E	National Westminster Bank Ltd.
Bishop, Kenneth G.	E	Debenhams Ltd.
Blacker, Norman	P	British Gas Corporation
Bonham, Derek C.	E	Hanson Plc
Boothman, Derek A.	E	Binder Hamlyn
Boreham, Brian P.	A	Wilson Wright & Co.
Bowman, Jeffery H.	E	Price Waterhouse
Bromwich, Professor Michael	M	University of Reading
Bruce, John P. H.	I	Atkinson & Boyd
Burns, Alexander K.	I	Stokes Kennedy Crowley & Co.
Child, Denis M.	-	National Westminster Bank Plc (to 1987)/None given (1988 to 1989)/ International Commodities Clearing House Ltd.
Clark, Laurence H.	E	Harmood Banner & Co.
Clemes, John W. W.	E	Allied-Lyons Plc
Collier, J. Anthony	E	Guest, Keen & Nettlefolds Ltd.
Cook, Alan V. C.	E	Shell
Cormie, J. David	E	Reed International Ltd.
Damant, David C.	-	Paribas Asset Management
Davison, Ian F. Hay	E	Arthur Andersen & Co. (to 1982)/Lloyd's
Dewar, George D. H.	S	Peat, Marwick, Mitchell & Co.

Name	*Body*[a]	*Affiliation*[b]
Dixon, Stanley	E	The Midland Yorkshire Tar Distillers Ltd.
Duncan, Stanley M.	E	Price Waterhouse & Co.
Edey, Professor Harold C.	E	London School of Economics and Political Science
Edwards, R. A. Shaw	P	North East Thames Regional Health Authority (to 1988)/Arthur Young
Foulds, Michael H.	A	Foulds & Grant
Fowler, Derek	P*, A	British Railways Board
Frith, John W. G.	E	C. & J. Clark Ltd.
Fryer, Arthur	M	ICI Ltd.
Gardner, Hugh J.	M*, S	Reckitt and Coleman Ltd.
Gibbs, P. Martin D.	E	Phillips & Drew
Giffin, Ronald	M	CCAB Ltd.
Godfrey, Peter	E	Ernst & Whinney
Gray, Professor Sidney J.	A	University of Glasgow
Grenside, John P.	E	Peat, Marwick, Mitchell & Co.
Harding, Stanley R.	E	The Thomas Tilling Group Ltd.
Harris, Martin R.	E	Price Waterhouse & Co.
Harrison, F. Brian	E	National Coal Board
Heady, Donald E.	E	Donald Heady & Co
Hegarty, Diarmuid A.	I	Business and Accounting Tutors
Hobson, David C.	E	Coopers & Lybrand
Hyde, William	M*, A	Chief Accountant, University of Oxford
John, Arthur W.	E	Unigate Ltd.
Johnson, Burton H. F.	P*, A	The Electricity Council
Joyce, Collin W.	A*, M	Baker Perkins Holdings Plc
Kett, R. B.	-	CCAB Ltd.
Kitchen, Stanley	E	Foster & Stephens
Knight, Jeffrey R.	E	The International Stock Exchange
Langford, Robert E.	E	Lloyds Bank Plc
Leach, Sir Ronald G.	E	Peat, Marwick, Mitchell & Co.
Llowarch, Martin E.	-	British Steel Coproration
Lyster, William B.	I	Craig, Gardner & Co.
Main, Donald E.	S	Trusthouse Forte Plc
Mallett, Michael J.	E	James Neill Holdings Plc (to 1985)/ Record Holdings Plc
McKinnon, James	S	Imperial Group Plc
McMahon, Noel M.	I	Craig, Gardner & Co.
Miller, Leslie T.	S	Ernst & Whinney
Molony, Alan M.	I	Craig Gardner & Co. (to 1987)/ None given
Morpeth, Sir Douglas S.	E	Touche Ross & Co.
Morris, Kenneth S.	P	Shropshire Health Authority
Morrison, Alexander	M	Anglian Water Board

Name	*Body*[a]	*Affiliation*[b]
Morrow, Ian T.	S	None given
Munson, Roger J.	E	Coopers & Lybrand Deloitte
Nelson, Alan W.	A	Opass Billings Wilson & Honey
Neville, Thomas	S	Vickers Plc (to 1987)/None given
Nobes, Professor Christopher W.	A	University of Reading
Norris, Harold[c]	E	George Wimpey & Co. Ltd.
Ogle, Bertram D. G.	A	ICI Ltd. (to 1979)/ Formerly ICI Ltd.
Ould, John E.	M	Reed International Plc (to 1987)/None given
Palmar, Derek J.	E	Bass Plc
Paterson, Ronald M.	S	Ernst & Young
Patrick, E. John	P	Oxford City Council/ Oxford District Council
Pearcy, Jeffrey	S	ICI Ltd. (to 1981)/ formerly ICI Ltd.
Phillips, Brian H.	A	Nationwide Building Society
Potter, Ernest F.	M	Cable & Wireless Plc (to 1987)/None given
Quinton, John	-	Barclays Bank Plc
Renshall, J. Michael	E	KPMG Peat Marwick McLintock
Risk, William S.	S	None given
Shanagher, Anthony D.	I	Wilkinson Match Ltd.
Sharp, Kenneth J.	E	Armstrong, Watson, Milburn, Wyllie & Co. (to 1972)/ Head of the Government Accountancy Service
Sherriff, Denis G.	I	Ernst & Whinney
Slimmings, Sir William	S	Thomson McLintoch & Co.
Southall, Henry P.	M	The Plessey Co. Ltd.
Spain, Alex J.	I	Stokes Kennedy Crowley & Co.
Stacy, Graham H.	E	Price Waterhouse
Stilling, Peter J.	E	Touche Ross & Co.
Stronge, Christopher J.	E	Deloitte Haskins & Sells
Tanner, Brian M.	P	Somerset County Council
Tegner, Ian N.	S	Bowater Industries Plc
Thomson, Stanley	A	Ford Motor Co. Ltd.
Thring, Peter S.	E	Ernst & Young
Waddington, John P.	E	Spicer and Oppenheim
Walton, Arthur H.	E	Hallidays
Watts, Thomas R.	E	Price Waterhouse & Co.
Whiteoak, John E. H.	P	Cheshire County Council
Wilkins, Stanley P.	E	Deloitte Haskins & Sells
Wilkinson, Henry R.	P	Audit Commission
Wilson, Hon. Geoffrey H.	M	Delta Metal Co. Ltd.

Terms of office[d]

	7.1.70	1.7.70	1.7.71	1.7.72	1.7.73	1.7.74	1.7.75	1.7.76	1.7.77	1.7.78	1.5.79	1.6.80	1.5.81	1.6.82	1.7.83	1.9.84	31.8.85[e]	1.9.86	1.7.87	31.7.88	31.7.89	31.7.90
Adams, D. H.																				X	X	X
Anderson, G.																		X	X			
Anderson, J. N.															X	X	X	X	X			
Appleyard, G. R.	X																					
Artus, R. E.															X	X	X					
Barrett, F. J.				X	X	X	X	X	X													
Berman, N.									X	X	X	X	X	X								
Bishop, K. G.										X	X	X	X									
Blacker, N.													X	X								
Bonham, D. C.																				X	X	X
Boothman, D. A.						X	X	X	X	X	X	X	X									
Boreham, B. P.															X	X	X					
Bowman, J. H.														X	X	X	X	X	X			
Bromwich, M.													X	X	X							
Bruce, J. P. H.							X	X														
Burns, A. K.												X	X	X								
Child, D. M.																		X	X	X	X	X
Clark, L. H.	X	X	X	X	X	X	X	X														
Clemes, J. W. W.															X	X	X	X	X			
Collier, J. A.														X								
Cook, A. V. C.																				X	X	X
Cormie, J. D.				X	X	X	X	X	X	X	X											
Damant, D. C.																				X	X	X

	7.1.70	1.7.70	1.7.71	1.7.72	1.7.73	1.7.74	1.7.75	1.7.76	1.7.77	1.7.78	1.5.79	1.6.80	1.5.81	1.6.82	1.7.83	1.9.84	31.8.85[e]	1.9.86	1.7.87	31.7.88	31.7.89	31.7.90
Davison, I. F. H.														X	X							
Dewar, G. D. H.		X	X	X	X	X	X	X														
Dixon, S.	X																					
Duncan, S. M.	X	X	X	X	X																	
Edey, H. C.	X	X	X	X	X	X	X	X	X	X	X	X	X	X								
Edwards, R. A. S.																		X	X	X	X	
Foulds, M. H.																		X	X	X	X	
Fowler, D.															X							
Frith, J. W. G.		X	X	X																		
Fryer, A.				X																		
Gardner, H. J.												X	X	X								
Gibbs, P. M. D.										X	X	X	X	X								
Giffin, R.																					X	X
Godfrey, P.																X	X					
Gray, S. J.																X	X	X	X			
Grenside, J. P.										X	X	X	X	X								
Harding, S. R.	X	X	X	X	X	X	X	X														
Harris, M. R.						X																
Harrison, F. B.																X	X					
Heady, D. E.															X	X	X					
Hegarty, D. A.																						
Hobson, D. C.		X	X	X	X	X	X	X	X	X	X	X	X	X								
Hyde, W.					X	X	X	X	X	X	X											
John, A. W.					X	X	X															

	7.1.70	1.7.70	1.7.71	1.7.72	1.7.73	1.7.74	1.7.75	1.7.76	1.7.77	1.7.78	1.5.79	1.6.80	1.5.81	1.6.82	1.7.83	1.9.84	31.8.85[e]	1.9.86	1.7.87	31.7.88	31.7.89	31.7.90
Johnson, B. H. F.										X	X	X										
Joyce, C. W.															X	X	X	X	X			
Kett, R. B.																				X		
Kitchen, S.	X	X	X	X	X																	
Knight, J. R.															X	X	X	X	X	X	X	
Langford, R. E.																						X
Leach, Sir R. G.	X	X	X	X	X	X	X															
Llowarch, M. E.																		X	X			
Lyster, W. B.		X	X	X	X	X																
Main, D. E.																						X
Mallett, M. J.															X	X	X	X	X	X	X	
McKinnon, J.										X	X	X	X	X	X							
McMahon, N. M.									X	X	X											
Miller, L. T.									X	X	X	X	X	X								
Molony, A. M.																		X	X	X	X	X
Morpeth, Sir D. S.	X	X	X	X	X	X	X	X	X	X	X	X	X	X								
Morris, K. S.																X	X					
Morrison, A.												X										
Morrow, I. T.		X	X																			
Munson, R. J.																		X	X	X	X	X
Nelson, A. W.				X	X	X	X	X	X	X	X	X	X	X								
Neville, T.																		X	X	X	X	
Nobes, C. W.																				X	X	X
Norris, H.[c]																						

	Ogle, B. D. G.	Ould, J. E.	Palmar, D. J.	Paterson, R. M.	Patrick, E. J.	Pearcy, J.	Phillips, B. H.	Potter, E. F.	Quinton, J.	Renshall, J. M.	Risk, W. S.	Shanagher, A. D.	Sharp, K. J.	Sherriff, D. G.	Slimmings, Sir W.	Southall, H. P.	Spain, A. J.	Stacy, G. H.	Stilling, P. J.	Stronge, C. J.	Tanner, B. M.	Tegner, I. N.	Thomson, S.	Thring, P. S.
31.7.90		X		X			X	X		X								X	X					X
31.7.89		X		X				X		X								X	X					
31.7.88		X		X				X		X								X	X					
1.7.87		X						X		X									X					
1.9.86		X						X		X									X					
31.8.85[e]		X							X	X							X					X	X	
1.9.84		X							X	X							X					X	X	
1.7.83			X						X				X				X			X	X		X	
1.6.82						X						X	X							X	X		X	
1.5.81	X				X	X							X	X						X				
1.6.80	X				X	X							X	X										
1.5.79	X				X	X							X	X										
1.7.78	X				X	X							X	X	X									
1.7.77	X				X	X							X		X									
1.7.76	X				X	X							X		X									
1.7.75	X					X							X		X	X								
1.7.74	X					X									X	X								
1.7.73	X										X				X	X								
1.7.72	X										X				X	X								
1.7.71													X		X									
1.7.70													X		X									
7.1.70													X											

	7.1.70	1.7.70	1.7.71	1.7.72	1.7.73	1.7.74	1.7.75	1.7.76	1.7.77	1.7.78	1.5.79	1.6.80	1.5.81	1.6.82	1.7.83	1.9.84	31.8.85[e]	1.9.86	1.7.87	31.7.88	31.7.89	31.7.90
Waddington, J. P.																		X	X	X	X	X
Walton, A. H.				X	X	X																
Watts, T. R.							X	X	X	X	X	X	X	X								
Whiteoak, J. E. H.																X	X	X	X			
Wilkins, S. P.		X	X	X	X	X	X	X	X	X	X	X										
Wilkinson, H. R.																						X
Wilson, Hon. G. H.								X	X	X	X											

Sources: Internal documentation of the ASC secretariat (ASCA, 5/3/5); Annual bound volumes of standards published by the ICAEW; 'New members for standards group', *Accountancy Age*, 24 June 1977, p. 2; 'Know the ASC members', *Accountancy*, January 1978, p. 6; 'Powerful and private: The standard setters', *Accountants Weekly*, 11 May 1979, pp. 20-25; 'Accounting Standards Committee - New members', *Accountancy*, November 1987, p. 47. Some forenames and affiliations are extracted from professional body membership lists.

Notes:

[a]Professional body membership is indicated as follows: A = ACCA, E = ICAEW; I = ICAI; P = IMTA/CIPFA; S = ICAS; M = ICWA/ICMA/CIMA. For names of bodies, see the List of Abbreviations (pp. xiv–xv). Where multiple qualifications are shown, the appointing body is indicated by an asterisk.

[b]Where the organisation to which a member was affiliated changed name during the period of affiliation, the most recent name is given.

[c]Place not taken up.

[d]Information for those years in which an annual bound volume of standards was published is compiled from that source. The date at which membership is given in the bound volumes varies from year to year and two successive lists do not always correspond to successive 'committee years'.

[e]No date is specified in the bound volume for 1985/86 but it is stated that the list includes members whose term of office will expire on 31.8.85.

Appendix 7

Statements of Standard Accounting Practice Issued

No.	Title (s)	Issued	Revisions
	Explanatory foreword to accounting standards	January 1971	Revised May 1973. New version issued May 1975; revised August 1986
1	Accounting for associated companies	January 1971	Amended August 1974; revised April 1982 [Withdrawn November 1997 — superseded by FRS9]
2	Disclosure of accounting policies	November 1971	[Withdrawn December 2000 — superseded by FRS18]
3	Earnings per share	February 1972	Revised August 1974 [Withdrawn October 1998 — superseded by FRS14]
4	Accounting treatment of government grants/Accounting for government grants	April 1974	Revised July 1990
5	Accounting for value added tax	April 1974	
6	Extraordinary items and prior year adjustments	April 1974	Revised August 1986 [Withdrawn October 1992 — superseded by FRS3]
7	Accounting for changes in the purchasing power of money (Provisional)	May 1974	Withdrawn January 1978
8	The treatment of taxation under the imputation system in the accounts of companies	August 1974	Appendix 3 added December 1977 and revised 1988 [Withdrawn December 1999 — superseded by FRS16]
9	Stocks and work in progress/ Stocks and long-term contracts	May 1975	Part 6 added August 1980; revised September 1988
10	Statements of source and application of funds	July 1975	Part 4 added June 1978 [Withdrawn September 1991 — superseded by FRS1]

No.	Title (s)	Issued	Revisions
11	Accounting for deferred tax	August 1975	Withdrawn October 1978
12	Accounting for depreciation	December 1977	Amended November 1981; revised January 1987 [Withdrawn February 1999 — superseded by FRS15]
13	Accounting for research and development	December 1977	Revised January 1989
14	Group accounts	September 1978	[Withdrawn July 1992 — superseded by FRS2]
15	Accounting for deferred tax	October 1978	Revised May 1985 [Withdrawn December 2000 — superseded by FRS19]
16	Current cost accounting	March 1980	Withdrawn April 1988
17	Accounting for post balance sheet events	August 1980	[Withdrawn May 2004 with effect from 1 January 2005 — superseded by FRS21]
18	Accounting for contingencies	August 1980	[Withdrawn September 1998 — superseded by FRS12]
19	Accounting for investment properties	November 1981	
20	Foreign currency translation	April 1983	[Withdrawn December 2004 with effect from 1 January 2005 — superseded by FRS23]
21	Accounting for leases and hire purchase contracts	August 1984	
22	Accounting for goodwill	December 1984	Revised July 1989 [Withdrawn December 1997 — superseded by FRS10]
23	Accounting for acquisitions and mergers	April 1985	[Withdrawn September 1994 — superseded by FRS6]
24	Accounting for pension costs	May 1988	[Withdrawn November 2000 (subject to transitional arrangements) - superseded by FRS17]
25	Segmental reporting	June 1990	

Note: Where the title of a standard was altered on revision, both titles are given. SSAPs extant at 1 August 1990 were adopted by the Accounting Standards Board. Subsequent withdrawals by the ASB to April 2006 are shown in square brackets.

Appendix 8

Exposure Drafts Issued

No.	Title	Issued
1	Accounting for the results of associated companies	June 1970
2	Disclosure of accounting policies	January 1971
3	Accounting for acquisitions and mergers	January 1971
4	Earnings per share	March 1971
5	Extraordinary items and prior year adjustments	August 1971
6	Stocks and work in progress	May 1972
7	Accounting for extraordinary items	July 1972
8	Accounting for changes in the purchasing power of money	January 1973
9	The accounting treatment of grants under the Industry Act 1972	March 1973
10	Accounting for value added tax	May 1973
11	Accounting for deferred taxation	May 1973
12	The treatment of taxation under the imputation system in the accounts of companies	May 1973
13	Statements of source and application of funds	April 1974
14	Accounting for research and development	January 1975
15	Accounting for depreciation	January 1975
16	Supplement to 'Extraordinary items and prior year adjustments'	September 1975
17	Accounting for research and development (Revised)	April 1976
18	Current cost accounting	November 1976
19	Accounting for deferred taxation	May 1977
20	Group accounts	July 1977
21	Accounting for foreign currency transactions	September 1977
22	Accounting for post balance sheet events	February 1978
23	Accounting for contingencies	November 1978
24	Current cost accounting	April 1979
25	Accounting for the results of associated companies	October 1979
26	Accounting for investment properties (An addition to SSAP12 'Accounting for depreciation')	September 1980
27	Accounting for foreign currency translations	October 1980
28	Accounting for petroleum revenue tax	March 1981

No.	Title	Issued
29	Accounting for leases and hire purchase contracts	October 1981
30	Accounting for goodwill	October 1982
31	Accounting for acquisitions and mergers	October 1982
32	Disclosure of pension information in company accounts	May 1983
33	Accounting for deferred tax	June 1983
34	Pension scheme accounts	April 1984
35	Accounting for the effects of changing prices	July 1984
36	Extraordinary items and prior year adjustments	January 1985
37	Accounting for depreciation	March 1985
38	Accounting by charities	November 1985
39	Accounting for pension costs	May 1986
40	Stocks and long-term contracts	November 1986
41	Accounting for research and development	June 1987
42	Accounting for special purpose transactions	March 1988
43	The accounting treatment of government grants	June 1988
44	Accounting for goodwill - additional disclosures	September 1988
45	Segmental reporting	November 1988
46	Disclosure of related party transactions	April 1989
47	Accounting for goodwill	February 1990
48	Accounting for acquisitions and mergers	February 1990
49	Reflecting the substance of transactions in assets and liabilities	May 1990
50	Consolidated accounts	June 1990
51	Accounting for fixed assets and revaluations	May 1990
52	Accounting for intangible fixed assets	May 1990
53	Fair value in the context of acquisition accounting	July 1990
54	Cash flow statements	July 1990
55	Accounting for investments	July 1990

Appendix 9

Submissions on Exposure Drafts

ED		Total	Firms of accountants	Companies	Representative bodies		Academics	Other individuals	Other identified groups	Others
					Accountants	Others				
1	Associated companies	152	22	51	26		7	46		
2	Accounting policies	69	13	16	22		4	14		
3	Acquisitions and mergers	88	28	17	32		4	7		
4	Earnings per share	66	18	9	24		0	15		
5	Extraordinary items	83	17	25	30		0	11		
6	Stocks and work in progress	153	21	72	32		2	26		
7	Extraordinary items	77	13	19	29		0	16		
8	Changes in the purchasing power of money	113	13	27	36		11	26		
9	Grants under the Industry Act	76	14	24	26		4	8		
10	VAT	52	9	11	27		0	5		
11	Deferred taxation	118	25	44	33		4	12		
12	Taxation	67	18	14	27		0	8		
13	Source and application of funds	98	22	29	32		6	9		

ED		Total	Firms of accountants	Companies	Representative bodies		Academics	Other individuals	Other identified groups	Others
14	Research and development	66	15	15	31		2	3		
15	Depreciation	101	21	36	31		4	9		
16	Extraordinary items (Supplement)	79	19	27	26		0	7		
17	Research and development (Revised)	49	9	8	28		2	2		
18	Current cost accounting	746	83	336	123		30	174		
19	Deferred taxation	115	26	29	43		0	17		
20	Group accounts	85	18	28	33		0	6		
21	Foreign currency transactions	116	23	45	32		0	16		
22	Post balance sheet events	91	23	29	31		2	6		
23	Contingencies	81	21	19	35		0	6		
24	Current cost accounting	248	34	75	74		65			
25	Associated companies	109	24	31	29	17	8			
26	Investment properties	107	21	44	9	16			3	14
27	Foreign currency translations	107	20	46	12	13				16
28	Petroleum revenue tax	30	8	18	1	3				
29	Leases and hire purchase contracts	137	23	59	8	22				25
30	Goodwill	97	24	25	28	9				11
31	Acquisitions and mergers	86	22	17	28	11				8
32	Disclosure of pension information	71	14	7	27	12	6		5	
33	Deferred tax	77	24	25	5	10				13
34	Pension scheme accounts	70	17		25	6	8		8	6
35	Changing prices	125	17	41	14	12	39			2
36	Extraordinary items	83	16	14	33	6	12			2
37	Depreciation	89	20	27	29	6	5		2	
38	Accounting by charities	54	15		2	4	13		17	3
39	Pension costs	75	19	22	5	18	9			2
40	Stocks and long-term contracts	41	15	9	9		4		2	2
41	Research and development	49	14	8	15		9			3

ED		Total	Firms of accountants	Companies	Representative bodies	Academics	Other individuals	Other identified groups	Others
42	Special purpose transactions	56	13	13	18	6			6
43	Government grants	48	15	6	14		6		7
44	Goodwill-additional disclosures	43	15	8	10		4		6
45	Segmental reporting	60	16	18	6		4		16
46	Related party transactions	38	16	6	6	5	2		3
47	Goodwill	148	19	73	7	8	24		17
48	Acquisitions and mergers	47	17	8	5	6	5		6
49	Substance of transactions	36	13	8	4	9	0		2
50	Consolidated accounts	42	14	15	5	4	0		4
51	Fixed assets and revaluations	78	18	28	6	13	5		8
52	Intangible fixed assets	37	15	10	4	4	3		1
53	Fair value	32	13	9	4	3	2		1
54	Cash flow statements	81	28	20	6	8	11		8
55	Investments	43	13	10	8	4	1		7

Sources: EDs 1 to 24: T. Hope and J. Briggs, 'Accounting policy making - some lessons from the deferred taxation debate', *Accounting and Business Research*, 1982, 12:46; EDs 25 to 45 except 28, 35 and 42: the Technical Release issued on publication of the subsequent SSAP or, where a further ED was issued, the ED (see ASC, TR808 'Final Report and Recommendation of ASC to CCAB', August 1990 and Appendix 8); EDs 28, 35, 42 and 46 onwards: the covering report in the files of submissions held in the Library of the ICAEW (for this range, classification of 'others' between representative bodies and others is by the author).

Note: The precise titles of some of the categories used by the ASC to analyse submissions changed through time. A blank cell indicates that a category was not used in the analysis for the relevant document. 'Other identified groups' indicates a group identified for the analysis of a particular document but not used generally. For ED34, other identified groups include companies responding as sponsoring employers.

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