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Competent and Versatile: How Professional Accountants in Business Drive Sustainable Organizational Success.

Good morning everyone. I am truly delighted to be in Cape Town. Before I begin, let me first express my appreciation to CIMA for inviting me to speak here today.

Perhaps before I start my presentation I should introduce IFAC.

- IFAC is the global body for the accounting profession—we have 164 members (CIMA is a founding member) in 125 countries
- The members of our members total approximately 2.5 million accountants, more than half in business, government, or academia
- Based in NYC, we have 75 staff (most in NY) and a budget of $27m, 55% from member bodies, 45% from the Forum of Firms
- In terms of resources, we also have very significant support from our member bodies through their nomination of people to sit on our boards and committees.

So what do we actually do at IFAC? Below is a table of our key services:

Overview of Service Delivery

<table>
<tr><th>Standards & Guidance (2012: US $17 million)</th><th>Adoption & Implementation (2012: US $2 million)</th></tr>
<tr><td>Developing international standards:
Auditing, assurance, and quality control
Ethics
Public sector accounting
Accounting education
Developing / facilitating sharing of guidance:
Professional accountants in business (PAIBs)
Small and medium practices (SMPs)</td><td>Promoting adoption of international standards and guidance
Providing high-level advice on technical and legal approaches to adoption
Facilitating availability and accessibility of international standards and guidance, including translations
Developing / facilitating sharing of implementation material and tools
Assessing the effective implementation of new international standards</td></tr>
<tr><th>Quality & Development (2012: US $4 million)</th><th>Representation of the Profession (2012: US $4 million)</th></tr>
<tr><td>Implementing Member Body Compliance Program
Encouraging membership of the Forum of Firms
Advocating / supporting capacity-building initiatives to strengthen professional accountancy organizations
Increasing awareness of PAIBs, and supporting Member Bodies in enhancing PAIB competence
Improving the quality of business reporting, including integrating social, economic and environmental reporting
Enhancing the global identity, visibility, and value-recognitions of SMPs, and supporting MBs to enhance their competence / opportunities</td><td>Commenting on issues relevant to the profession
Developing / maintaining relationships with stakeholders
Developing policy position addressing issues relevant to the profession</td></tr>
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I have to commend CIMA not only for organizing this conference, but for 90 years of developing and qualifying management accountants, whose strategic and management skills not only contribute to successful careers in business, they also contribute to the success of their organizations. And CIMA's engagement with both the business and academic communities—we just heard from Andrew Harding about some of these connections—has enabled it to ensure that its qualification remains relevant to the changing environment, and to the needs of employers.

CIMA's engagement within IFAC also warrants mention, as one of our very few member bodies that exclusively comprises accountants in business. Within IFAC, CIMA not only contributes to the work of a range of our boards and committees, bringing the perspective of accountants in business, it also, especially through Charles Tilley, is effective in seeking to keep us focused on the needs of this segment of the profession. If we are not paying sufficient attention to the needs of accountants in business, I can rely on hearing from Charles! In the specific context of the global financial crisis, CIMA also reminds us that at a fundamental level, it is the work of the accountant in business, not the auditor, who determines the quality of financial information produced for capital markets. This is an important message and one we should not lose sight of.

The Role of the Professional Accountant and the Professional Accountant in Business (PAIB)

I will be speaking to you this morning about the role of the professional accountant, specifically the professional accountant in business (PAIB) in the context of sustainable organizational success. Worldwide, more than one million professional accountants work in commerce, industry, financial services, education, and the public and private sectors, many in leadership and managerial roles. These professional accountants in business, or management accountants, are in a key position to affect the long-term sustainable value of their organizations.

We need to recognize that the roles of the PAIB are very diverse, from that of the CEO, CFO, and COO to business and performance analyst, controller and reporter, to name but a few of the job titles that accountants in business carry. There are many more. We can view the different roles through the following diagram, drawing on the work of IFAC's Professional Accountants in Business Committee.

The roles professional accountants perform can broadly be described as creators, enablers, preservers, and reporters of sustainable value for their organizations—recognizing that they operate in both performance and conformance dimensions:

- As creators of value, by taking leadership roles in the design and implementation of strategies, policies, plans, structures, and governance measures that set the course for delivering sustainable value creation.
- As enablers of value, by informing and guiding managerial and operational decision making and implementation of strategy for achieving sustainable value creation, and the planning, monitoring, and improvement of supporting processes.
- As preservers of value, by ensuring the protection of a sustainable value creation strategy against strategic, operational, and financial risks, and ensuring compliance with regulations, standards, and good practices.
- As reporters of value, by enabling the transparent communication of the delivery of sustainable value to stakeholders.

One of the key challenges for accountants in business is how to achieve sustainability. At a strategic level—Integration of sustainability or (ESG) factors into the way an organization thinks about itself—its business must be led from the top. I do not intend to cover ground that was covered yesterday on integrated reporting; if you heard Mervyn King speak, you do not need me—other than to emphasize both our support for and involvement in this initiative.

At IFAC we believe this is a critical activity and are fully engaged:

- Through the membership of the IIRC by our President;
- Through my role as chair of the Working Group of the IIRC;
- Through our seconded staff member based in London;
- Through the support of the PAIB committee staff in New York.

From our perspective, this will be one of the big challenges for PAIBs and for the accounting profession in the next decade. CIMA has been a catalyst for this initiative, and has certainly provided us with valuable support in shaping and executing our role in the IIRC activity, as well as encouraging us to take this role in the first place.

In organizations, ideally, the CEO—with support from the CFO and other directors—will champion the integration of these ESG factors into the way the organization develops and delivers its strategy. Governance structures must support these integration efforts and this raises a number of issues including, for example:

- Does sustainability (or specific sustainability initiatives) need an individual board member as an identifiable champion?
- Is a separate subcommittee of the governing body needed to provide coordination and direction to sustainability activities, If so, does it report to the governing body or to another committee, such as the audit committee;
- To what extent do the Board's Audit and Risk Committees engage with issues of sustainability? Does the audit committee have a role in identifying, managing, and reporting on significant ESG risks and related internal controls and disclosures?
- How are sustainability initiatives and performance coordinated across various functions (e.g., sales, marketing and brand, product development, supply chain, facilities, procurement, and human resources?)

Another area for debate in which PAIBs will have a major role is on whether placing monetary values on costs and benefits is desirable—whether it can help persuade stakeholders make decisions which reflect the real economic, social, and environmental impacts of decisions. I would not want to pretend this is a simple issue, and may ultimately be resolved by governments rather than within firms, through such interventions as pricing carbon. PAIBs will also have a role in promoting an understanding of non-financial performance links to financials.

PAIBs should be well placed to participate in investor and wider stakeholder engagement. At a managerial and operational level, PAIBs have many opportunities to impact on the implementation of more integrated strategies. One very important way is through influencing the supply chain. Retailers and producers increasingly expect suppliers to reduce the negative impacts of the components of products and services they provide. PAIBs are equipped to guide informed and ethical decision making in supply organizations and helping to improve their sustainability performance.

More broadly, to support decisions, traditional financial-based decision analysis needs to be complemented with sustainability considerations. Various tools help to do this, such as environmental management accounting. PAIBs can also assist with carbon foot printing at an organizational or product level, adding value to a greenhouse gas emissions inventory through deeper analysis of causes and improvement options.

Obviously, organizations can always cut costs and improve sustainability by minimizing waste, including waste of energy and of water. Accountants, particularly those advising smaller businesses, can advise on simple and inexpensive measures and controls based on improved understanding of patterns of consumption.

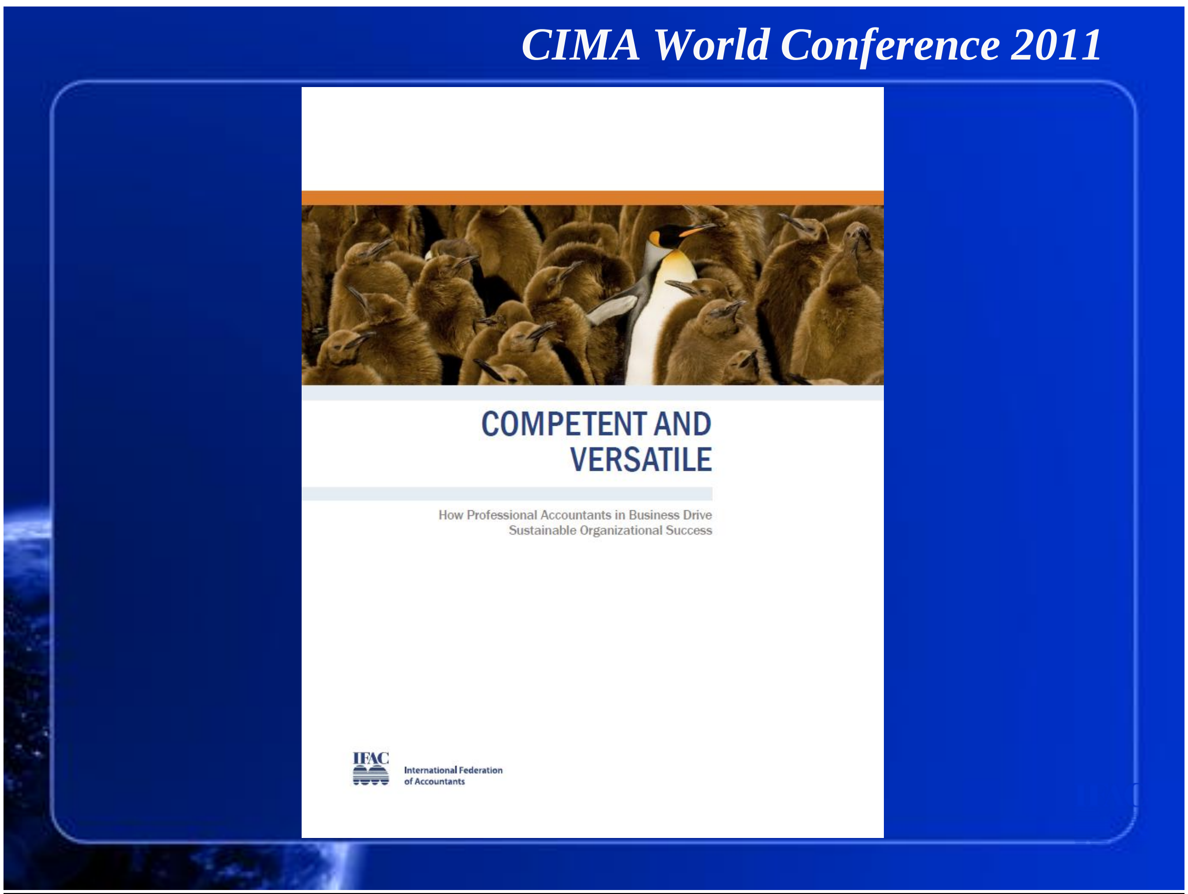
As preservers of value, accountants' focus will be on identifying, prioritizing, and controlling strategic and operational opportunities and risks, facilitating integration of the risks around sustainability into the mainstream risk management activity, and demonstrating how the risks bear on their organization's business operations and goals. And accountants should be well placed not only to identify but to interpret risks and propose actions to mitigate those risks.

The theme of integration extends to those PAIBs in reporting roles. While sustainability reporting has improved in most places over recent years, separate sustainability reports run the risk of being seen as an end in themselves. Many aspects of sustainability reporting are being accused of green washing—including long lists of activities apparently contributing to corporate responsibility—making it difficult to distinguish the truly important achievements, and ultimately undermine credibility in business reporting. PAIBs should know how to identify what's really important to the corporate story and how an integrated reporting approach can achieve greater transparency and understanding of how the organization creates sustainable value.

As an aside, I am one of the people who belief that expanded reporting will have little value unless it is accompanied by assurance statements.

<u>Profession Accountants in Business and IFAC</u>

How do professional accountants drive sustainable organizational success, both in the public and non-profit sectors? Some of the answers are in "Competent and Versatile":



Global recognition of professional accountants as organizational leaders and strategic partners in building long-term sustainable organizational success is the vision and central tenet of IFAC's Professional Accountants in Business (PAIB) strategy.

To achieve this vision, IFAC collaborates with its members and associates to promote and contribute to the value of PAIBs.

The PAIB strategy pursues two key complementary objectives:

- Increasing awareness of the important roles professional accountants play in creating, enabling, preserving, and reporting value for organizations and their stakeholders; and
- Supporting member bodies in enhancing the competence of their members to fulfill those roles by facilitating the communication and sharing of good practices and ideas.

To support the global accountancy profession respond to employer expectations, IFAC's PAIB Committee identified eight key drivers of sustainable organizational success. This analysis also provides a framework for understanding how the global accountancy profession needs to support the competency development of professional accountants. These drivers are being used as a framework to show how integrated governance, including relevant sustainability factors, can drive sustainable organizational success, and how professional accountants in business can support their organization in making governance and sustainability an integral part of their organization's DNA.

Let us look at this set of drivers:

- A customer and stakeholder focus: successful organizations first and foremost create value for customers, which consequentially leads to value creation for investors. Concurrently, organizations can only sustainably create value by taking account of the needs and expectations of other stakeholders. A customer and stakeholder focus involves ensuring that the whole organization, and not just front-line service staff, puts an understanding of customers and key stakeholder groups first. Stakeholder engagement is a fundamental precursor to effective integrated and sustainability reporting. We do not have time to go into this today, but I believe exactly the same focus is required for governmental and non-profit organizations.

- Effective leadership and strategy: achieving sustainable organizational success depends on effective and ethical leadership, which in turn enables coherent and focused strategy and execution. Above all, effective leadership and business strategy focuses on sustainable value creation over the long term. In decision-making processes, this means that long-term consequences of decisions should be taken into account, including how they impact operations, customers, employees, and the reputation of the organization. Successful organizations have leaders that have a deep understanding of (a) customer and stakeholder needs, (b) the organization's capabilities to generate the required products and services, as well as (c) the opportunities and threats that stem from its competitive environment.

- Integrated governance, risk, and control: sustainable value creation depends on how well organizations can integrate their governance, risk management, and control systems in all their activities and processes. Successful organizations integrate effective governance structures and processes with performance-focused risk management and control systems. They ensure that good governance is more than a compliance exercise by facilitating entrepreneurial and prudent management.

- Innovative and adaptive capability: successful organizations meet changing market demands, or, in some cases, shape them. They innovate their products and services, and adapt their structure, processes, and systems to changed circumstances. Building capacity to develop sustainable products and services, and supporting processes and systems, requires investment in an innovative capability and supporting organizational culture.

- Financial management: successful organizations have strong financial management underpinning their decisions and performance. They ensure that financial strategy and navigation support long-term economic viability rather than only focusing on short-term earnings performance. A deep understanding of historical, current, and potential performance forms the basis of developing strategy and setting credible stakeholder and market expectations. Confidence in articulating where an organization is going financially helps improve access to capital and the confidence of stakeholders. Effective financial management also involves delivering financial leadership in tax and treasury, cost and profitability improvement, working capital management, mergers and acquisitions, and raising finance and capital.

- People and talent management: organizations that attract and retain talent tend to outperform competitors. A bit of a truism, but successful organizations typically treat people and talent management as a strategic function and key driver of their sustainable success.

- Operational excellence: successful organizations are disciplined in ensuring that resource allocation decisions align with strategic direction, goals, and objectives. They ensure that performance measurement and reporting systems measure progress towards the achievement of strategic and operational objectives. Their business intelligence provides insight into the key drivers of shareholder and stakeholder value, and allows for better alignment of accountability for results, as well as rewards and recognitions.

- Effective and transparent communication: successful organizations typically have a systematic and carefully planned approach to engaging and dialoguing with various stakeholders. Investor relations and integrated business reporting are opportunities for management to provide investors and other stakeholders with the longer-term prospects for an organization, as well as a rationale and explanation for its vision, strategies, and results. Such organizations tend to excel in their reporting in terms of readability, usefulness, and relevance.

<u>Supporting the Development of Professional Accountants</u>

The ability of professional accountants in business to meet these expectations requires a range of professional skills, attitudes, and mindset. IFAC, through the PAIB Committee, has identified five key areas that will support the evolution of the PAIB:

- *Professionalism and ethical behavior*

  Professional accountants should uphold high ethical standards in accordance with the *Code of Ethics for Professional Accountants* which requires accountants to encourage an ethics-based culture that emphasizes the importance that senior management places on ethical behavior—professional accountants in business can support an organization's code of conduct and ethics through their own behavior and actions in the various roles that they perform.

- *Professional judgment*

  The vast range of circumstances and situations that can arise in organizations of any type, industry, and size makes the application of detailed rules ineffective for guiding management decisions. Therefore, the quality of professional judgment becomes a differentiating factor for high-performing professional accountants.

This includes balancing organizational nimbleness, and quick and intuitive decision making with a need for evidence-based decisions.

As professional accountants increasingly perform as “business partners,” their fundamental professional values of independence, integrity, and objectivity will be tested, and applying professional judgment and integrity will often involve reconciling conflicting commercial, financial, and sustainability interests.

- *Organizational and environmental awareness*

  Professional accountants need to be aware and possess knowledgeable of other disciplines, such as technology, people and project management, and of managing and measuring non-financial activities and performance.

  Organizational and environmental awareness and understanding are also critical in helping them to reconcile the detailed aspects of operational performance with strategic aims.

- *An investor and wider stakeholder focus*

  Professional accountants, particularly in CFO / FD roles, can be expected to lead in managing relationships with investors and other funders, and, in some industries, with regulators.

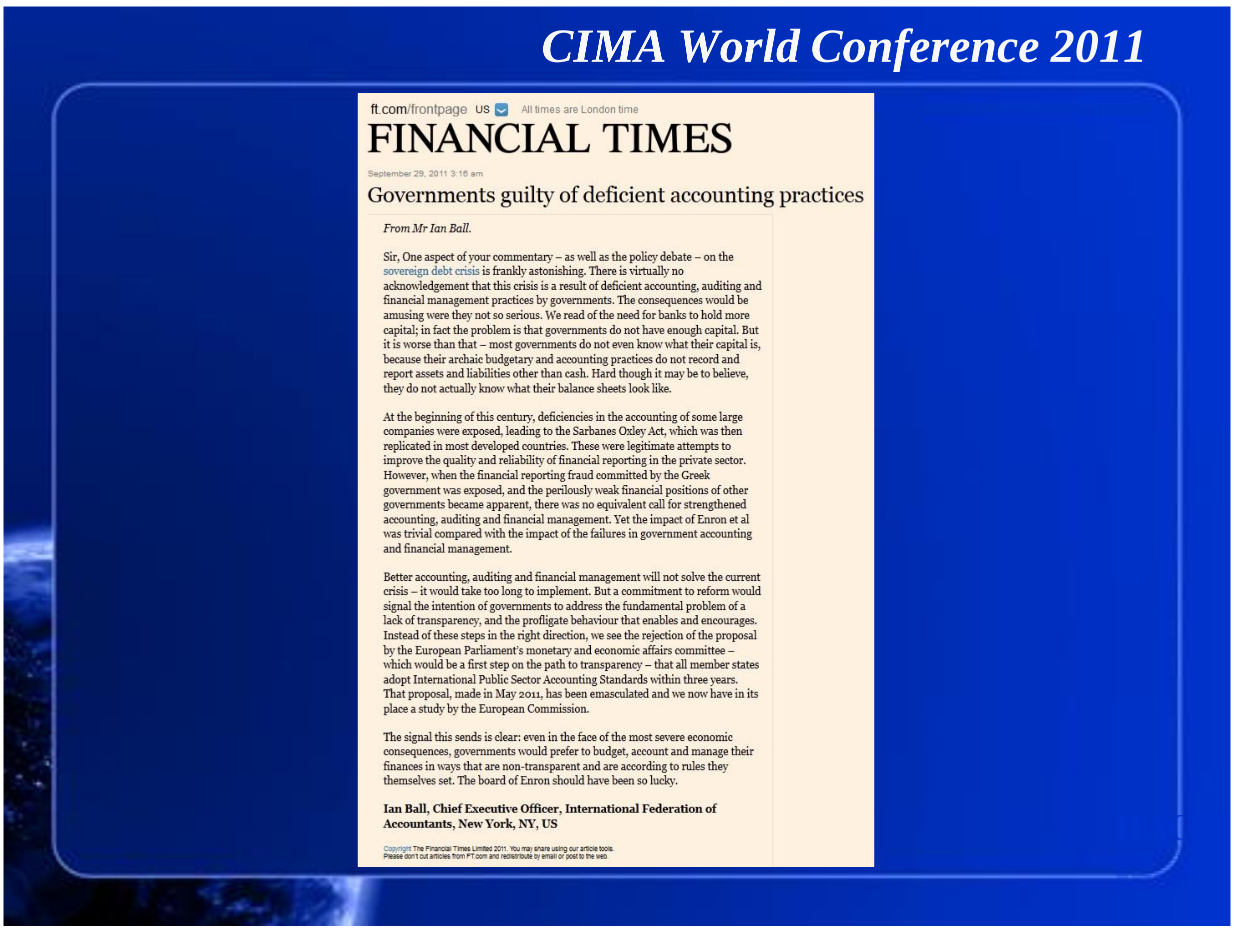
  They also need to consider a wider stakeholder perspective so as to ensure risk and performance are managed in the long-term interests of stakeholders. By effectively engaging with investors and other stakeholders, professional accountants can play a central role in identifying material sustainability issues and responsibilities of the organization and key opportunity and risk areas.

- *Being comfortable dealing with change, uncertainty, and complexity*

  As with their organizations, professional accountants will typically operate in a fast changing environment and will therefore have to be able to adapt to changing circumstances, applying professional skills and judgment to often ambiguous and imperfect information. In all kinds of roles, PAIBs need to be prepared to manage uncertainty, complexity, and strategic decision making within an overall context of heightened focus on effective governance, risk management, and control.

Sustainability for The Public Sector

We have been looking at issues of sustainability and the role of the PAIB in the corporate sector, but sustainability factors are also important in the public sector. The situation in the public sector is, nevertheless, quite different. The future course of the global financial and sovereign debt crises remains uncertain, putting fiscal sustainability into the spotlight. As countries, hopefully, begin to emerge from the crisis, albeit with a sharp deterioration in their public finances and significant loss to the global economy, the focus on public sector financial reporting cannot be overlooked.



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FINANCIAL TIMES

September 29, 2011 3:16 am

Governments guilty of deficient accounting practices

From Mr Ian Ball.

Sir, One aspect of your commentary – as well as the policy debate – on the sovereign debt crisis is frankly astonishing. There is virtually no acknowledgement that this crisis is a result of deficient accounting, auditing and financial management practices by governments. The consequences would be amusing were they not so serious. We read of the need for banks to hold more capital; in fact the problem is that governments do not have enough capital. But it is worse than that – most governments do not even know what their capital is, because their archaic budgetary and accounting practices do not record and report assets and liabilities other than cash. Hard though it may be to believe, they do not actually know what their balance sheets look like.

At the beginning of this century, deficiencies in the accounting of some large companies were exposed, leading to the Sarbanes Oxley Act, which was then replicated in most developed countries. These were legitimate attempts to improve the quality and reliability of financial reporting in the private sector. However, when the financial reporting fraud committed by the Greek government was exposed, and the perilously weak financial positions of other governments became apparent, there was no equivalent call for strengthened accounting, auditing and financial management. Yet the impact of Enron et al was trivial compared with the impact of the failures in government accounting and financial management.

Better accounting, auditing and financial management will not solve the current crisis – it would take too long to implement. But a commitment to reform would signal the intention of governments to address the fundamental problem of a lack of transparency, and the profligate behaviour that enables and encourages. Instead of these steps in the right direction, we see the rejection of the proposal by the European Parliament's monetary and economic affairs committee – which would be a first step on the path to transparency – that all member states adopt International Public Sector Accounting Standards within three years. That proposal, made in May 2011, has been emasculated and we now have in its place a study by the European Commission.

The signal this sends is clear: even in the face of the most severe economic consequences, governments would prefer to budget, account and manage their finances in ways that are non-transparent and are according to rules they themselves set. The board of Enron should have been so lucky.

Ian Ball, Chief Executive Officer, International Federation of Accountants, New York, NY, US

There has been limited mention in the public debate about the crisis being the result of poor accounting, auditing, and financial management, not to mention financial reporting fraud, by governments. Late last month the *Financial Times* published my Letter to the Editor—[Governments guilty of deficient accounting practices]—on the sovereign debt crisis and the need for transparency in government reporting. My letter was in response to their commentary and debate on the sovereign debt crisis.

What was most astonishing, which I note in the letter, is that there was virtually no acknowledgement that this crisis is a direct result of deficient accounting, auditing, and financial management practices by governments. Ten years ago, when deficiencies in the accounting of some large companies were exposed, it led to the Sarbanes Oxley Act in the United States, which was then replicated in various countries. There were, and continue to be, efforts to improve the quality and reliability of financial reporting in the private sector, but what about the public sector?

I will talk in a moment about sustainability reporting in the public sector, but before doing that we need to be clear, at the global level, about the current state of financial management, and management accounting, in most governments. Frankly, it is unforgivable. As a profession, we should be distressed, and vocally distressed, that our skills and expertise are so little used by governments. The cost of this to us, as taxpayers, and to our economies and to our social welfare, is huge.

Let me illustrate how bad it is with a few simple points:

- Most national (sovereign) governments still operate (budget, appropriate, manage and report) on a cash basis—his means they do not know what assets they hold and liabilities they owe
- The cash basis creates incentives to finance activity through creating liabilities (such as pensions) rather than through current cash expenditure, thus deferring recognition of the consumption of resources and creating obligations that will have to be met in the future
- Governments are often are not at all clear what their outputs (services) are, frequently confusing them with outcomes, inputs, activities, programs, objectives—the list goes on
- Without accrual accounting they do not know what their costs are, and if they also do not know what their outputs are, they certainly cannot cost them and be in a position to compare costs with alternative providers. Certainly they will not be in a position to use the advanced management accounting techniques such as Activity Based Costing that Andrew referred to earlier

Through the work of the International Public Sector Accounting Standards Board IPSASB—and I do not want to steal the thunder of the Chairman of the IPSASB, Andreas Bergmann, who will be speaking to you later in this conference—we have made some progress in shifting the benchmark for government accounting from cash to accrual, but in terms of budgeting, appropriations, and financial management, there is still a very long way to go. That is a real challenge for the profession.

A recent project of the IPSASB bears directly on long term fiscal sustainability, with the release of an Exposure Draft (ED), *Reporting on the Long-Term Sustainability of a Public Sector Entity's Finances.* This objective of this project is to provide guidance on how to present information on a public sector entity's long-term fiscal sustainability to supplement information in the general purpose financial statements and meet the objectives of financial reporting—accountability and decision-making. The ED is open for public comment until February 29, 2012.

While this project is important for government reporting in the longer term, the immediate problem thrown up by the sovereign debt crisis is the more pointed one of short-term financial survivability. So while it is encouraging to see some developments in sustainability reporting in the public sector, which I will refer to in a moment, there are perhaps some more fundamental matters that more urgently need attention; that is to get the basics of financial reporting in place.

However, the United Kingdom has taken a very important step in the move toward sustainable reporting in the public sector. In 2004, HRH The Prince of Wales established Accounting for Sustainability (A4S) to bring organizations together to develop practical tools to enable environmental and social performance to be better connected with strategy and financial performance, and thereby embedded into day-to-day operations and decision making. In keeping with a commitment to fully implement sustainable reporting, this year, for the first time, there was a mandatory requirement for all central government departments and the NHS to publish in their Annual Reports and Accounts a Sustainability Report that included details of departments' carbon emissions, waste management, and use of finite resources which reflected the integrated reporting requirements recommended by A4S.

To increase transparency and accountability across the public sector, departments will be required to report non-financial data on:

- Direct and indirect greenhouse gas emissions;
- The absolute cost of waste disposal; and
- Consumption of water and other material finite resources.

This first step is key in the United Kingdoms' commitment toward even more advanced sustainability reporting in government over time and will hopefully set the stage for governments worldwide to follow suit. While governments around the world have a lot to do to improve their financial reporting, they could also report better on ESG factors, where the UK example is certainly one to be closely examined.

IFAC and the International Governance Framework for the Public Sector Project

To help public sector leaders, and PAIBs in the public sector, IFAC is considering a project to develop a new international governance framework for the public sector that embraces a wider view of governance by (a) focusing on economic, social, and environmental as well as financial outcomes; (b) instilling good governance in all strategic, operational, and reporting processes; (c) focusing on both conformance (compliance) and performance responsibilities; and (d) emphasizing how critical public financial management is to any public sector governance system.

Conclusion

As a profession that operates with both business and government, we have some big challenges ahead.

Financial reporting is increasingly inadequate to its task, and seen to be so. The IIRC Discussion Paper cites data that suggests as little as 19% of market capitalization of large listed companies is reflected in their physical and financial assets. We need better guidance as to the value of companies.

Integrated reporting, as the leading contender in addressing this problem, will itself create a different set of challenges to the profession, requiring new skills and competencies on the part of the profession.

And in the public sector there is a huge job to be done to get the most basic financial information produced.

These are challenges for you, accountants in business, for your professional body, CIMA, and for IFAC. They are challenges we need to meet together.

Thank you for your attention.