

VI. TÜRKİYE MUHASEBE DENETİMİ SEMPOZYUMU

Sempozyum Sunuş Bildirisi:

GLOBALISATION - THE ACCOUNTING PROFESSION AT THE CROSSROADS

Michael Birch

Technical Leader – PricewaterhouseCoopers Central Eastern Europe

There can be no doubt that the accounting and auditing profession has reached a crossroads where decisions that are taken will profoundly affect the image of the profession in the public eye, and consequently the livelihoods of its members. How did we get here?

Business was booming

Throughout the 1990's economic growth continued to accelerate. Globalisation became a driving force, notably in Asia, Turkey, and Eastern Europe. The technological revolution continued at a breathless pace. The USA continued to grow as the largest single economy, and, based on the belief that markets can regulate themselves, continued to promote a philosophy of minimum regulation of business. The US became the largest source of capital, also for many foreign companies whose home markets were too small to meet their increasing capital requirements. There seemed to be a one – way train of rising prosperity – for Companies, investors, bankers, lawyers, accountants

Wake up calls

However, there were wake up calls. The Asian financial crisis was a traumatic experience. It put national accounting standards into focus – large global institutions such as the World Bank and the IMF were astonished to find how diverse and misleading these could be. In the European Union the steady progress towards a single market continued, with consequences for harmonisation in all walks of life, including the accounting profession. IOSCO was formed to bring standards to the world's fragmented stock markets, and looked to International Accounting Standards as one of the issues to bring consistency. Share prices clearly no longer could be related to historical audited financial statements. And increasingly, to everybody's embarrassment restatements of audited financial statements became common- \$31.2 billion market value wiped out for 156 corporations whose financial statements had to be restated in 2000 alone.

The Crisis of Capitalism

In retrospect it was, therefore, perhaps not so surprising when the crisis did come. What did shock the world were the scale and its effects. The astonishing tale of Enron was quickly followed by major scandals of Global Crossing, WorldCom and others. Even more astonishing was the sudden disintegration of Arthur Andersen, one of the world's most respected accounting firms with a reputation for quality and integrity - also very much a driving force in the development of auditing in Turkey. Faced with a crisis of confidence, the collapse of the stock markets and the collapse of the US\$ followed. Inevitably there arose a loud clamour for immediate regulatory action. Questions were raised about the responsibility of Chief Executive Officers – and their pay. Investigations started into the Audit Profession,

Investment bankers, and role of tax advisers, lawyers.

US Reaction

US reaction was severe, emotional and the result of almost uncontrolled fury from a variety of sources. It culminated in the Sarbanes Oxley Act, with severe consequences for the companies and the accounting profession. Under the resulting SEC independence rule the auditor broadly cannot:

Carry out a function in the role of management
Audit his or her own work
Serve in an advocacy role for the client

The interpretation of the details is still the subject of much debate and negotiation, but there can be no question that the focus has swung very much back on the responsibility of the auditor to maintain his independence visibly.

The US Did Not Require Rotation Of Audit Firms

One of the hotly contested issues, auditor rotation, finally came down in favour of rotation of partners, but not firms. It is worth dwelling on how this came about, because it is a subject discussed in many countries, including Turkey. The implications for the future of the profession. Countries everywhere have been forced to take note because of the number of foreign SEC registrants. Mandatory rotation of audit firms already exists in some countries (e.g. Italy for listed companies, Canada for banks), with some negative results. The US concluded that, although there are arguments in favour, the cost to the corporations and the audit profession outweigh the benefits and that the rotation of key partners could achieve the same result at much lower cost to the companies. It also took note that the highest risk of audit failure is in the first year after a change of auditors.

Transparency

The key issue for public corporations is now transparency. Investors need transparent, reliable information across the globe. The IASB has addressed this with the update and convergence with USGAAP projects. Although it is clear these will result in much tighter accounting principles, similar in complexity to USGAAP today, we should note that the convergence project is not to merge with USGAAP, rather to identify the best principles which can be adopted. The EU has issued directive for IAS by 2005 for listed companies in the EU, and is also examining implications of IFRS for small economic enterprises („SME's"). FEE has set itself the target of harmonising auditing standards by 2005.

Consequences for the profession

In order to recover its image in a global market, the profession must also think and act globally, aiming for the highest quality across borders. IFRS will become much more complicated and will need to be applied consistently internationally – no local deviations (including in the US!!) Technical excellence is a priority. The profession needs to attract the highest calibre of people in an increasingly regulated environment.

What Should The Shareholder Expect From His Auditor?

In the context of shareholders expectations from their auditors, Warren Buffet's comments to his shareholders this year are extremely perceptive and worth noting. Here are some extracts:

If the auditor were solely responsible for preparation of the company's financial statements, would they have in any way been prepared differently from the manner selected by management?

If the auditor were an investor, would he have received the information essential to his understanding the company's financial performance Is the company following the same internal audit procedure that would be followed if the auditor himself were CEO?

Is the auditor aware of any actions – either accounting or operational – that have had the purpose and effect of moving revenues or expenses from one reporting period to another.

Warren Buffet's Advice For investors

The following advice of Warren Buffet to investors about companies is also very relevant to auditors concerned about their reputation and image:

Beware of companies displaying weak accounting. If a company still does not expense stock options, or if its pension assumptions are fanciful, watch out.

Unintelligible footnotes usually indicate untrustworthy management. If you can't understand a footnote or other managerial explanation, it's usually because the CEO doesn't want you to. Enron's descriptions of certain transactions still baffle me.

Finally, be suspicious of companies that trumpet earnings projections and growth expectations. Businesses seldom operate in a tranquil, no-surprise environment, and earnings simply don't advance smoothly.

Implications for Turkey and the Turkish accounting profession

It has long been apparent that all countries need foreign capital for economic development. Despite the rapid progress made in Turkey over the last twenty years, this is still extremely important – not least with the aspirations to join the EU. It is noteworthy that the USA finances the largest trade deficit in the world to large extent through capital markets. Within this context, the *quality* of the accounting profession, working together with the capital markets, gives foreign capital a great deal of confidence in making individual investments, and thereby can make a significant contribution to the development of the economy as a whole

GLOBALISATION - THE ACCOUNTING PROFESSION AT THE CROSSROADS(Presentation Outline)

Michael Birch
Technical Leader – Central Eastern Europe

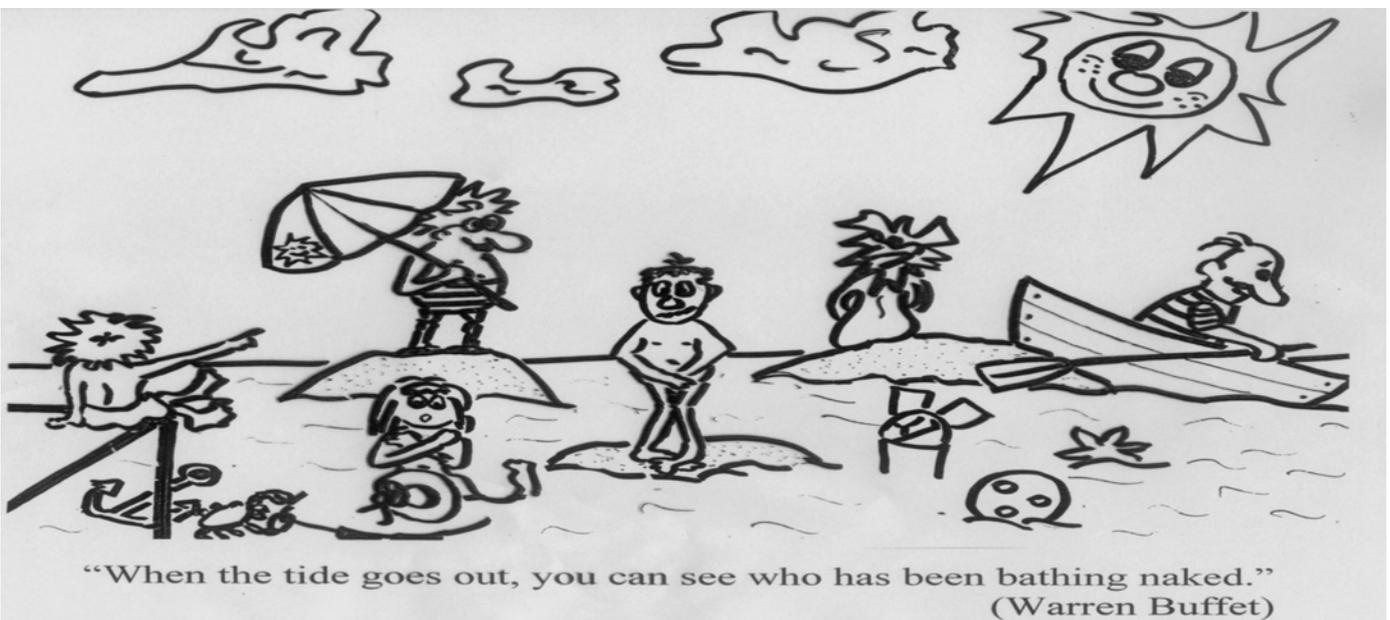
Business was booming!

- Accelerating economic growth in the 1990's
- Globalisation – Asia, Turkey, Eastern Europe
- Technological revolution
- USA, largest single economy, belief that markets can regulate themselves
- USA largest source of capital, also for foreign companies
- Rising prosperity – Companies, investors, bankers, lawyers, accountants

Wake up calls

- The Asian financial crisis
 - National accounting standards
- European Union
 - Progress towards a single market
- IOSCO
 - Fragmented Stock markets
- Share prices
 - Clearly no longer related to audited financial statements
- Restatements of audited financial statements
 - \$31.2 billion market value wiped out for 156 corporations in 2000

The crisis of capitalism



- Clamour for regulatory action
- CEO responsibility
- Investigations into Audit Profession, Investment bankers, role of tax advisers, lawyers

US Reaction

- Sarbanes Oxley Act
- SEC independence rule .The auditor cannot
 - Function in the role of management
 - Audit his or her own work
 - Serve in an advocacy role for the client
- Rotation of partners, but not firms

The US did not require rotation of firms

- Huge implications for the future of the profession
- All countries forced to take note – foreign SEC registrants
- Mandatory rotation already exists in some countries, with some negative results
- US concluded that, although there are arguments in favour, the cost to the corporations and the audit profession outweigh the benefits and that the rotation of key partners can achieve the same result at much lower cost
- The highest risk of audit failure is in the first year

Transparency

- Investors need transparent, reliable information across the globe
- IASB reorganisation and convergence project
- EU directive for IAS by 2005 for listed companies
- EU examining implications of IFRS for small economic enterprises („SME’s”)
- FEE: Harmonise auditing standards by 2005

Consequences for the profession

- In a global market, the profession must also think and act globally , aiming for the highest quality
- IFRS will become much more complicated
- IFRS needs to be applied consistently internationally – no local deviations (including USA!!)
- Technical excellence is a priority
- Profession needs to attract high calibre people

What should the shareholder expect from his auditor

- Warren Buffet’s comments
 - If the auditor were solely responsible for preparation of the company’s financial statements, would they have in any way been prepared differently from the manner selected by management?

- If the auditor were an investor, would he have received the information essential to his understanding the company's financial performance

What should the shareholder expect from his auditor?

- Warren Buffet's comments (2)
 - Is the company following the same internal audit procedure that would be followed if the auditor himself were CEO?
 - Is the auditor aware of any actions – either accounting or operational – that have had the purpose and effect of moving revenues or expenses from one reporting period to another

Warren Buffet's advice for investors:

1. Beware of companies displaying weak accounting. If a company still does not expense options, or if its pension assumptions are fanciful, watch out.
2. Unintelligible footnotes usually indicate untrustworthy management. If you can't understand a footnote or other managerial explanation, it's usually because the CEO doesn't want you to. Enron's descriptions of certain transactions still baffle me.
3. Finally, be suspicious of companies that trumpet earnings projections and growth expectations. Businesses seldom operate in a tranquil, no-surprise environment, and earnings simply don't advance smoothly.

Implications for Turkey and the Turkish Accounting Profession

- All countries need foreign capital for economic development
- The USA finances the largest trade deficit in the world through capital markets
- The quality of the accounting profession, working together with the capital markets, gives foreign capital a great deal of confidence in making individual investments, thereby contributing to the economy as a whole