Accounting and Business Research

ISSN: (Print) (Online) Journal homepage: https://www.tandfonline.com/loi/rabr20

‘Preparers and the financial reporting system’ – a practitioner view

Julia Wilson

To cite this article: Julia Wilson (2021) ‘Preparers and the financial reporting system’ – a practitioner view, Accounting and Business Research, 51:5, 508-510, DOI: 10.1080/00014788.2021.1932260

To link to this article: https://doi.org/10.1080/00014788.2021.1932260

Published online: 09 Aug 2021.

Accounting and Business Research, 2021
Vol. 51, No. 5, 508–510, https://doi.org/10.1080/00014788.2021.1932260

'Preparers and the financial reporting system' – a practitioner view

JULIA WILSON*

3i Group, London, UK

I am speaking both as Chair of the 100 Group, which is a collective of the FTSE 100 CFOs, and as a CFO myself. I have been a CFO at 3i Group plc for 12 years. I have also chaired the Audit Committee of Legal & General in the past as well. Through all of that I have worked out that I have worked with about 11 CEOs in my career.

3i is a long-term investor in mid-market companies, and we use permanent capital to do that, so we have a very long-term view, and we absolutely believe that good governance both protects the value but can also enhance the value. Because we are buying medium-sized companies, we are often taking over businesses out of families or founder situations, and often the very first set of investment that we do is absolutely into the finance team, the financial controls, because we recognise its absolute importance. So I bring that in my mindset as a CFO. I do think that good CEOs have to have an ego both to survive and to succeed, and the best CEOs will then build strong teams around them, including strong and very well-qualified CFOs.

There is a lot in McVay and Szerwo (2021) that I can recognise. I do think the overall conclusions are a bit pessimistic, and, certainly in my experience, and having met lots of CFOs, I don't think that there is as much emphasis and focus as appears to be implied about manipulating the financial results. I find that too pessimistic, but I do absolutely recognise what Sarah calls the slippery slope. Again, I would have that in a less pejorative sense but actually, probably compounded by some of the features of IFRS and the way that accounting works, I can absolutely recognise, having observed other companies, that sense of, when you are making a judgment, a bias towards a good outcome. You can call it optimism if you want but it is a bias to 'This assumption is not too aggressive – we're in the grey but it's not too aggressive and once this has happened and that's happened, it will be fine.' Then a company gets into that slippery slope of the thing that you hoped would happen does not happen, and, before you know it, it is built up. We can all think of some high-profile examples, typically around revenue recognition,

*Email: Julia.Wilson@3i.com

as McVay and Szerwo (2021) say, where that sort of optimism bias has certainly come out in the wrong sort of way.

I do not really recognise in a UK context as strongly as suggested in the paper this idea of the CEO capturing the board. I think the UK Corporate Governance Code has done a good job of putting checks and balances around the CEO to make sure that the board is more independent, and every company I have been involved in the board has taken a direct interest in me as a CFO and the CFOs in those companies to make sure that you've got that sort of independence. I think it is really important.

The other observation I would make is about the role of the audit committee – again, we have seen that in the UK Corporate Governance Code – which has been beefed up substantially in the time that I have been involved in these sorts of things, as has the role of internal audit. If you look at what has happened in UK financial services, the PRA (Prudential Regulation Authority) has played a big role in making sure that the competence of internal audit is enhanced – I don't want to say that we have got that completely sorted out in the UK, but I think there are some positive differences compared with the US system. As I say, I do not think the UK is perfect. Carillion is the posterchild of things not going right, and the response in terms of regulatory responses to that will play out for a very long time.

Which brings us on to the Sarbanes-Oxley Act (SOX). I was working at Cable & Wireless when it was introduced, and I was part of the implementation team. My main memory of that, frankly, was the cascades of sign-offs that would have to happen. We are talking about introducing something like that in the UK now. We talk about a light version of SOX. I think it is really important that any 'SOX' in the UK allows for equivalence with the US. Clearly, there is plenty that we can learn from the US in the UK about how to implement any new regime. I do think that a formal requirement to sign a piece of paper, the related conversation about the competence of the CFO and the qualification of the CFO, can enhance many businesses. I like to think in the FTSE 100 generally speaking that is not so much of an issue, and indeed, in the FTSE 100 you have got many companies that do report under SOX anyway, but clearly many more companies could learn from that.

A final comment I would just make as well about internal audit functions. As I have already mentioned, the PRA in financial services has done a lot to increase the competence of those, and it is very clear now that the head of internal audit needs to have a strong reporting line into the audit committee. Personally, I think the most value that an internal audit function can add is around operational controls, so whether that would identify the operational earnings management alluded to in McVay and Szerwo (2021) is a question.

We have gone through this whole discussion so far without really talking about culture. Culture is the buzzword of the moment but it is about that tone from the top, and, having said I do not recognise the CEO capture point, we should never underestimate the strength of the CEO's influence in an organisation. For me, culture comes down to the day to day. So you can put as much reporting line protection around the CFO, around an internal audit function; but all it really needs is for the CEO to raise their eyebrow and show to the executive committee that they do not really listen to the head of internal audit or the CFO to undermine a lot of processes and controls. So keeping an eye on that culture is critical. Boards can play a very strong role in that, not just sitting in your six board meetings a year but getting out and about in companies, testing the culture at every opportunity, even if that is just talking to the receptionist when you walk into the building, I think will tell you a lot. Then that will play through to how companies are responding to accounting challenges.

Disclosure statement

No potential conflict of interest was reported by the author(s).

Reference

McVay, S. and Szerwo, B., 2021. Preparers and the financial reporting system. *Accounting and Business Research*, 51(5), 508–510.