



## **Changing times...food for thought**

### **Andrew Ratcliffe**

On March 28, 1210, Rubeus de Campo of Genoa agreed to pay a debt of 100 marks sterling in London on behalf of Vivianus Jordanus from Lucca.

What is so unusual about this transaction from more than 800 years ago that I use it to start my speech today?

Well, there is nothing unusual about it all. It is but one of the many thousands of agreements that we know about in Europe at that time. De Campo and Jordanus lived in a period of remarkable economic growth in Europe with increasing population, urbanisation, capital investment and trade.

What I think is interesting is that this entirely ordinary agreement reflects a very well-functioning market. These two Italian merchants were prepared to transact a payment of a significant amount of money at a remote location. Genoa to London does not seem far for us today; but at that time it would have taken four weeks or so for any message to be transmitted from one city to the other. They did this before the infrastructure that we take for granted had been established: before the law of contract was properly established in either country and certainly before any of today's international payments infrastructure.

If that legal and institutional infrastructure wasn't there, there must have been a high degree of trust between the two merchants and their agents in London and elsewhere for them to do this.

You would hope and assume that the infrastructure in the European, and indeed the world's, economy is better established today than it was in 1210 and that the degree of trust and confidence in business has increased. But we are still living with the aftermath of an event only five years ago that will be more familiar to you: the bankruptcy of Lehman Brothers on 15 September 2008, when the world's credit markets froze and even banks would not lend to each other.

So times have indeed changed since de Campo and Jordanus.

In this context, I was struck by the Ipsos Mori State of the Nation survey published at the beginning of this year. 61% of people across the UK agreed with the statement that they would rather be British than any other nationality. Only 14% disagreed. But when they were asked to say what made them proud, only 6% said that they were proud of British business. I find this very worrying.

It is business and commercial activity that creates the jobs, growth and wealth on which we all depend. It pays wages and generates the profits from which taxes are paid. It innovates to improve people's lives. It builds infrastructure and communities. A climate in which business is not seen as something of which we are proud is not just an inconvenience. It could lead to a downward spiral of cynicism and disengagement that would be dangerous to how our democracies work.

So, this does matter, and this morning I would like to talk about:

- why those qualities of trust and confidence have been eroded;
- how that affecting us as accountants; and
- what we can do about it.

Now, I wrote the first draft of this speech over the summer break; and in that I argued that this loss of public trust in companies and business and, by extension, what we accountants do, was part of a more comprehensive loss of trust in all institutions as a result of increased individualism. There are many sociologists who will describe how, previously, we lived in relatively stable societies in which people formed strong bonds with those with whom they lived and worked. Now people have to navigate a more fluid social environment, they choose their own lifestyles rather than inherit those of their parents or naturally adopt existing models. This change, it is claimed, has made people more self-reliant and sceptical.

But last week, I read the recent British Social Attitudes Survey, published by the National Centre for Social Research. This compares attitudes today with those of up to 30 years ago and this has changed my views.

The moral of this story is: stop reading new material in between writing a speech and delivering it!

The first thing that struck me in the Survey was that the proportion of people who agreed with the statement that “most people can be trusted” has hardly changed. It has stayed at around 40% throughout the 30 year period.

Some institutions have certainly seen their reputations suffer:

- In 1987, 38% felt that a UK government would put the needs of the country above the needs of their own party, now it's only 18%;
- 53% felt the media was well run, now it's only 27%;

And unsurprisingly the fall in trust in banks is the greatest:

- 90% thought they were well run in 1987; that has fallen to 19%.

I mentioned this last one to a banker friend of mine last weekend and he thought 19% was a surprisingly good score!

It is no coincidence that those institutions that have done badly are the ones that have had their own particular challenges for reasons that no-one would try to excuse. So, it is a mistake to assume that what has happened to them is evidence of a generalised loss of confidence in institutions.

Indeed the Survey shows that there are other institutions that are still well regarded. The NHS and the trade unions maintained their positions in terms of people who thought they were well run at about 55% and 30% respectively.

And if I go back to the Ipsos Mori Poll about what makes people proud to be British (only 6% mentioned British business remember), the NHS, the Armed Forces, Team GB at the Olympics and the Royal Family top the list, all with more than 30%.

This is an audience of accountants and I am sure you will all have quickly realised that four lots of 30% is more than 100%, I should say that respondents were asked to name two or three institutions!

The Royal Family is interesting. The British Social Attitudes Survey shows that its reputation was on a long downward slide but that it has made a substantial recovery. In 1983, 63% said it was important for Britain to continue to have a monarchy. Little more than 10 years later that had slumped to 32% and by 2006 it was only 27%. Numerous items of bad news over that period no doubt took their toll; but, the figure has now recovered to 45%. Maybe it is dangerous to draw too wide a conclusion from this example. After all, the Royal Family has its own special way of renewing itself. We might expect to see their reputation to further improve following the birth of Prince George in July!

So my thoughts on what is happening here have changed and they are still changing. The full answer is more complex than I gave it credit. I still think there is an element of the effects of increased individualism which I described earlier. If around 40% of us think that people can generally be trusted, 60% of us are more sceptical.

That bias towards scepticism means that reputations and trust are fragile. Are you familiar with the saying "trust arrives on foot and departs on horseback"? "Horseback" is the give-away. It dates from a Dutch politician in the mid 19<sup>th</sup> century.

But what is new is that the effect that technology is having on the velocity and ease of flow of information and what that means for the volatility of the public perceptions that drive trust and confidence. In the course of my working life and (looking around the room) I think this goes for most of you:

- Business correspondence has changed from a process of receiving post, drafting a reply, thinking about it for a bit and then posting the letter back, to a timescale of a matter of minutes by email.
- Getting information is no longer a matter of waiting to read tomorrow's paper or visiting the business library. News channels are rolling 24 hour operations and are themselves in danger of being overtaken by social media.

In a less connected, slower moving, less transparent, world there was time to fix problems and correct imbalances before they become contagious and often before they become evident. For example, compare the collapse of Northern Rock in 2007 with the near collapse of Cedar Holdings in 1973. Very similar circumstances:

- Cedar Holdings had grown rapidly specialising in second mortgages arranged by outside brokers which were funded by borrowing in the money market.
- The cost of the wholesale funds on which Cedar depended rose sharply and became available only for shorter periods. Then suddenly, not at all.
- Depositors began queuing to withdraw their money. The bank faced a liquidity crisis and bankruptcy was imminent.

In stark contrast to what happened with Northern Rock, the Bank of England forced a quick and effective solution upon reluctant City institutions. On the evening of 19 December 1973, the institutional investors and bankers of Cedar Holdings were told by the Bank that they had a "moral obligation" (and what an interesting phrase that is) to prevent its failure and, after a few hours of tough negotiation, agreed to provide loans to cover Cedar's deposits and the controlling shareholders ceded their entire interest over to them.

Globalisation and the size and interconnectedness of financial markets meant that the events of five years ago made themselves felt throughout the world in a matter of hours.

And this is not going to change. Unless someone works out how to uninvent the internet, information flow is just going to get faster and easier.

So I think the reasons for the loss of trust and confidence are not simply a loss of trust that the commercial system is inherently good and can never go wrong; but also because it has lost some of the capacity to act sufficiently quickly and decisively to fix problems as they arose.

Trust still arrives on foot, but it now leaves in a Formula One.

## **And this applies to us as well.**

Let me give you a personal perspective.

When I began my training contract in 1976, I think it is fair to say that accountancy was regarded as a fine and upstanding profession. There had been some scandals, but essentially there was a sound bedrock of public trust: a view that accountants would act and advise impartially in their clients' best interest while having regard to the public interest and that they would adhere to the highest standards of ethics and competence.

In my view, and in my personal experience, the profession as a whole remains committed to behaving ethically and responsibly. We put our clients' interests and the public interest before our own. The sense of being a professional is, I would guess for all of us in this room, a matter of not just a job but part of how we define ourselves.

But public attitudes to what we do have changed and what may be obvious to us is not obvious to others. Forgive me if I take audit and tax in the UK as examples:

- Long incumbency of any audit is now seen as evidence that the relationship between auditor and client must have been suspect, that it is “too cozy” and lacking in challenge, even when the individuals on either side of the relationship change regularly.
- On tax, we have been caught up in the debate over tax structuring as a number of high profile multinationals and individuals have been attacked for not “paying their fair share”, whereas the UK tax system just would not work if it were not for our members..

The practice of accountancy, together with banking and other financial services, indeed all public services, is subject to societal expectations that are constantly changing and evolving.

## **So what can we do about this?**

I think it is time to remind ourselves what a profession is for.

It is not just the means to acquire the skills and qualification that enable us to find employment through our lives. We are part of the infrastructure of society and the economies in which we live and our professional institutes give us the means to act collaboratively in the public good. The very word “profession” derives from concepts of belief, commitment and making a promise, a compact with society about what we'll do and how we'll do it. I think we need to rediscover some of those qualities and ensure that they are picked up by new generations as they set out on their professional journey.

However sophisticated our institutions, if we lose the intangible qualities of trust and confidence at their root, they will fail.

If, as I mentioned earlier, there is a gap between public perception and reality, we cannot ignore those perceptions. It is essential that we do not just retreat into defending what we do. We must innovate and collaborate to create something new. We need to be prepared to stand up for what we believe in, play an active part in the issues that our societies face and help our members in practice and in business determine what the right thing to do is.

Our reputation and the degree of trust that society puts in us will be formed through what we do far more than what we say.

In that spirit, let me give you six areas of what we are doing at ICAEW.

### **First, developing our audit and tax services**

- Last year we started Audit Futures, a project to look at how audit should develop to meet society's needs.
- We are facilitating better engagement between auditors and regulators and auditors and investors

- We are vocal on the need for responsibility in what tax advice our members give to their clients – there is no place for highly artificial tax avoidance schemes in our profession. Michael Izza’s blog on this, from more than a year ago, continues to be cited.

### **Second, helping with financial services reform – for many the most relevant aspect**

- We initially focussed on banks and audit, but this has spread to many other areas.
- Earlier this year we developed a framework for assurance of LIBOR and other market indices. Similar concerns have been raised in the energy and commodity markets.
- The need to change behaviour in financial services and particularly in banking is commonly recognised, but driving that change is difficult. Earlier this year, we established our new Valuing Integrity Programme to provide practical training on driving value based cultural change.

### **Third, helping to get the economy growing again**

Our members advise about 1.5m businesses, about a third of all UK businesses, and we’re doing more to focus on growth.

- helping our members to help businesses export more through our papers on International Trade and Export Finance.
- through the work we do in getting finance to businesses such as our Corporate Finance Faculty’s latest paper on SME Finance.
- And over 3,000 of our member offices volunteer free advice to start-ups and growing businesses through our Business Advice Service.

### **Fourth, public sector reforms**

The financial crisis has produced additional challenges for strong public finances. In Brussels, we are talking to policy makers about promoting better financial management, accountability and transparency in the public sector. Earlier this week, we held a meeting with the Commission, the ECB, the ESB and the World Bank.

In our paper CFO at the Cabinet Table, we have suggested three key reforms to help Whitehall plan for the long-term:

- transforming HM Treasury into a government group finance function for government that manages overall public finances rather than just allocating funds.
- Allied to that, creating an HMG Chief Financial Officer with responsibility for financial disciplines across government: quite incredibly none of the top three UK civil servants currently hold such a strategic responsibility for finance.
- Third, elevating the status of finance directors in government departments to create a strong finance function across government.

### **Fifth, employment and access to the profession**

Two major problems continue to bug the UK: high youth unemployment of around 20% and reduced social mobility. Put simply, if you are young it’s harder to get a job than before and if you come from a disadvantaged background it’s even harder. This means wasted talent: it’s bad for economic growth and it’s storing up problems for the future. If we have a generation that is disconnected from the world of work, the problems of trust that I spoke about earlier are only going to get worse.

- We are working with the firms to create more non-graduate routes into the profession, so that – at a time of high student fees - the profession becomes more accessible and more diverse.
- We actively encourage young people to go into business and accountancy. Over 1,500 school students took part in BASE, our business game, this year and we are doubling its size in 2013-14 to reach more students.
- And, not least, we operate one of the biggest recruitment sites for finance personnel.

**And the last of my six,**

Since I started with my two Italian merchants, I should finish on an international note.

We have always worked with IFAC, FEE and other international bodies to advance our profession, More recently we have been active in building capacity to support emerging professional bodies in developing countries.

And just over 18 months ago, we started the Accounting Profession Strategic Forum bringing together professional bodies in Central, Eastern and Southern Europe – sharing experiences and looking at the role of the profession in their national markets.

Now it's over to you. I would be happy to take your questions and comments.