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Focus on

Research

The research newsletter of The Institute of Chartered Accountants of Scotland

THE
INSTITUTE OF
CHARTERED
ACCOUNTANTS
OF SCOTLAND



IN THIS ISSUE

- RESEARCH FUNDING OPPORTUNITIES
- NEW PPP RESEARCH
- NEW AUDIT CHOICE STUDY



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EDITORIAL

Dear colleague

Welcome to the latest edition of *Focus on Research* - we hope you like the new format!

This will be my last edition of *Focus* as my term as Director of Research comes to an end in July 2009 after 6 years in the post. I have thoroughly enjoyed my time with ICAS and wish my successor all the best in the role. The name of my successor will be announced in May or June.

We have recently published our new Research Funding Brochure, details of this are on page 3. You can access this on our website at www.icas.org.uk/research or contact the Research Centre and we can post a copy to you. Copies are also included in the BAA and EAA participant packs. The new Funding Brochure outlines our key research themes and a separate document gives details of our current research priorities. We are always pleased to offer advice and feedback informally on any research ideas you have - either see us at the EAA or BAA conferences or drop us an email.

We have published two new reports in 2009, one on accountability and PPP and the other on audit choice, both are available to download free of charge on the website and are profiled on pages 6 to 11. 2009 is expected to be another busy year for ICAS research publications – to be notified of new reports as they are published and other research opportunities join our email news service by emailing research@icas.org.uk.

The ICAS Research team will be exhibiting at the BAA and EAA conferences – please drop by our stand and say hello and you could also enter our prize draw!

Christine Helliar
Director of Research

THE RESEARCH TEAM



Professor Christine Helliar
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Research funding opportunities

ICAS has recently published its new research funding brochure which can be downloaded at www.icas.org.uk/researchfunding

ICAS is committed to supporting high quality research which is timely and relevant to the accountancy profession or business. Applications are encouraged from researchers and institutions anywhere in the world and are welcome at any point in time. Successful applicants benefit from a close working relationship with a world class professional body that has close links with national and international policy makers and regulators. Research results are widely distributed and discussion events may be held to launch reports and encourage debate.

ICAS seeks research proposals that are in the public interest and which will help to inform the development of future policy. Research proposals should normally demonstrate that they contribute to one or more of the following policy objectives:

- Ensuring accountants act in the public interest
- Ensuring accountants act with ethics and integrity
- Supporting principles rather than rules and the exercise of professional judgement
- Improving the effectiveness of regulation
- Improving the entrepreneurial environment

The research themes which are of particular interest are:

- The Future of Financial Reporting and Assurance
- Ethics and Integrity
- Key Business Issues
- Insolvency

- Not for Profit Sector
- Development of the Profession

Specific examples of topics within these themes which are currently of interest to ICAS are set out in the Research Priorities list which is updated regularly on the ICAS website. Some of these research priorities are highlighted on page 4 of this newsletter.

Three levels of grants are normally available:

- Seedcorn (up to £750)
- Small project (under £2,000)
- Large project (£2,000-£25,000)

For further details of the application process and to download an application form please go to www.icas.org.uk/researchfunding

If you have any questions or would like some feedback on a proposed application, please contact Christine or Michelle at research@icas.org.uk or phone 0131 347 0237.

Specific calls for research will be advertised on the ICAS website and emailed to subscribers of our email news service. To subscribe for this service please email research@icas.org.uk.

Research is funded by The Scottish Accountancy Trust for Education and Research (SATER), an independent charitable trust, where the research is consistent with its objectives of promoting research into accountancy, finance and management, and related subjects.

We look forward to receiving your applications.

Research funding opportunities

Specific examples of research areas that are currently of interest to ICAS are set out below:

The Future of Financial Reporting and Assurance

- Boundaries of financial reporting and auditing
- Highlighting subjectivity and uncertainty in financial statements
- Accounting and assurance for smaller companies

Ethics and Integrity

- What is an ethical company?
- Accountants' roles in developing an ethical culture in business
- Management pressures and incentives

Key Business Issues

- Balancing corporate governance and business enterprise
- The effectiveness of Audit Committees
- Defining effective regulation and investigating enforcement

Insolvency

- The need for regulation in the debt consolidation market
- Impact of recent Insolvency Reforms - personal and corporate
- Accountability and effectiveness of public sector bodies involved in insolvency

Not for Profit Sector

- Improving accountability of public sector bodies
- The challenges of IFRS implementation in the public sector
- Differences in the definition of charities internationally

Development of the Profession

- The challenges and threats facing the profession now and in the future
- Effective regulation of the profession
- Cultural factors in the development of the global profession

For a full list of research priorities please visit www.icas.org.uk/site/cms/download/res_Research_Priorities.pdf

Research events

ICAS research development event 2009

On 16th and 17th March 2009, ICAS hosted its fourth Research Development event in CA House Edinburgh. Thirty two early career academics from 19 Universities across the UK and Ireland attended the two day event, a record number of attendees thus far.

Attendees included PhD students and new lecturers and the programme gave participants the opportunity to discuss their own research with professors from the ICAS Research Committee and share experiences with the other participants. The programme also provided an opportunity to find out more about ICAS research funding and included sessions on 'planning your research' and 'getting published'.

This event is free-of-charge to attend and after another successful event, we are planning to host a similar event next spring. To hear when next year's dates have been agreed - as well as other ICAS Research news - register for our free email notification service by contacting - research@icas.org.uk.

Financial black holes: Accounting for privately financed roads in the UK

Discussion event to launch new PFI report

On 12th February, ICAS, in conjunction with the Economic and Social Research Council, held a discussion event in Edinburgh to debate the findings of the new ICAS research report *Financial Black Holes: Accounting for Privately Financed Roads in the UK* by Professor Jean Shaoul, Professor Pam Stapleton, Dr Anne Stafford and Peter MacDonald from the University of Manchester.

The event was chaired by Alan Thomson, ICAS Vice President and included a presentation by the authors of the report. This was followed by a presentation from two panel members and then a lively question and answer session. The panel members were Dick Gill, a Portfolio Manager in the Public

Reporting Group of Audit Scotland and Peter Reekie from the Scottish Futures Trust. The Scottish Futures Trust is the new body established by the Scottish Nationalist Party to deliver future infrastructure projects in Scotland.

The use of private finance is obviously a very topical issue but the focus of the research and the discussion event was not on the merits of different types of private finance, but instead on the type and quality of information that is required for accountability purposes; whether this information is currently available; and what steps need to be taken to improve public accountability for existing and new projects.

This event was well attended and an interesting debate ensued as to what level of information should be available in the public domain to ensure accountability over public monies. The debate will no doubt continue and it will be interesting to see how this will be affected by the credit crunch with the resultant lack of financing deals; the adoption of IFRS for public sector bodies which is likely to bring most, if not all, PPP schemes onto the public sector balance sheet; and the development of new funding mechanisms in Scotland.

For further details on the findings of the report see the article on page 6 or view Jean Shaoul's video interview at - www.camagonline.co.uk.



New books published

Financial black holes: Accounting for privately financed roads in the UK

Jean Shaoul, Anne Stafford, Pam Stapleton and Peter MacDonald - University of Manchester

Private funding for public projects has always been controversial. Now research for ICAS finds that it is, at best, extremely difficult to get any sort of handle on how much the public is paying for those roads and hospitals.

The aim of this research was to establish the degree to which the reporting of public-private partnerships (PPPs) meets the Treasury's standard that it should provide accurate, transparent and credible accounts that allow the public to judge the scope, direction and sustainability of public spending and investments.

The financial reporting and disclosure of expenditure on PPPs by the public and private sector partners was examined, focusing on the roads sector because it is the largest and most international PPP sector.

International experience of such projects, which have not been uniformly successful, shows that it is necessary to consider the potential cost of a buy-back of the asset and/or debt guarantees. That is, any contingent liabilities need to be explained and, where possible, quantified.

Six PPP road projects with a combined capital value of £1.3 billion, that is, 40 per cent of the total capital value of signed deals for roads and bridges were examined. The cases include large-scale projects, commissioned by different types of public entities, and embrace a variety of different financing regimes. Some were toll concessions and some were paid for by the state.

Documents that are in the public domain or were requested under the Freedom of Information Act or the Audit Commission Act 1998 were examined.

The research posed several inter-related questions.

What additional problems does the PPP policy create?

The problems surrounding PPPs take several forms.

Firstly, the context in which they operate and the operation of the policy differ from those set out formally in the law, regulations, concessions, licences and government budgets. The result is that the real distribution of risk and costs may fall more on taxpayers and users and less on the financiers than is apparent.

Secondly, PPPs remove public expenditure from the direct control of the public sector and establish contractual relations that commit future governments and taxpayers over very long periods of time.

Thirdly, the adoption by the public sector of the private sector accounting framework means that public sector accounting has become embroiled in issues, particularly in relation to off-balance-sheet liabilities and contingent liabilities, that have been problematic in the private sector.

What reporting and disclosure is needed for public accountability?

There are three inter-related information flows. First is the traditional upward flow from public authority to Parliament. The second is the downward flow of information to citizens, which includes non-financial information about access to services, service performance, and transparency and equity in resource allocation.

PPPs also give rise to a horizontal flow, from the private sector partner acting in effect as a public authority. Information held by private sector companies is crucial for accountability for public expenditure. Without the horizontal flow, upward and downward accountability has little meaning.

For PPPs, the public needs to be able to understand: the basis for and nature of the procurement decision; the costs of contracts; the values of any reported assets and liabilities, including contingent liabilities; the form and amount of any

New books published



public support; the financial viability of the projects and their operators; and the termination arrangements for completed projects.

Thus accountability to the public implies forms of reporting and disclosure, over and above the private sector-oriented financial statements, that enable judgements about value for money and the impact of large projects on budgets. Accountability also implies information that is easy to get and understand.

To what extent does current reporting of PPP projects provide public accountability?

1 Information routinely placed in the public domain

Perhaps the most striking finding is how little financial information on PPPs is routinely provided by the procuring agencies. The public depends almost entirely on a project summary that provides a description of some key features. Such information has improved in recent years as a result of the internet, but is very limited with respect to financial information, which may differ across government websites.

The public authorities do not routinely release:

- the original strategic case setting out the reasons and detailed justification for the project;
- information on how competitive tension was achieved;
- the financial case for using private, not public, finance;

- the contracts; and
- information about the costs and performance of the projects, including risk sharing, monitoring costs and any internal reviews, and evaluation after contract termination.

Some information is discovered incidentally via the financial press or questions in Parliament, but this is neither systematic nor easily accessible.

Various public bodies scrutinise the accounts from the procuring agencies, but the level of aggregation makes this difficult. There is no evidence from the scrutineers' reports that these contracts have attracted their attention.

The corporate structure of the private sector partner is typically a consortium constituted as a special purpose vehicle (SPV). It is largely debt financed with no recourse to its parent companies and operates through a complex web of subcontracting to sister companies. Its accounts contain limited useful financial information, and it is impossible to track public sector monies through the extended supply chain.

2 Additional means of securing information

While the 2000 Freedom of Information (FoI) Act was expected to make government more open, it has proved to be of limited value in the context of private finance contracts. It requires considerable persistence and insistence to obtain information. The way that public agencies respond and their helpfulness and speed of response vary enormously. In part, this is because the officials do not always understand what information is required.

More importantly, FoI proved to be of limited value because the act allows public authorities to refuse to disclose information.

They may refuse on the grounds that such information is commercially sensitive. Since only some provide the information, this begs the question why such information is commercially sensitive in some authorities and not in others. In some cases, the public authorities released the information

New books published

requested, but with significant parts, such as termination clauses, cut.

They may also refuse on grounds of cost. One agency refused all requests for information on these grounds.

The variations between authorities make it difficult to avoid the conclusion that some use the exemptions to refuse to disclose information that could quite reasonably have been provided.

The act does not apply to the private sector. It gives the Lord Chancellor power to designate private sector companies as public authorities if they deliver public services under long-term contracts such as PPP, bringing them or the relevant parts of them under the act. He has not done so.

The Audit Commission Act 1998 provides that, while annual local government audits are being prepared, the public may request financial information, including information relating to private sector contracts, and question the authority's auditor. This provision does not appear to be widely known about or used.

This facility was used in the case of a local authority contract, but the authority refused to proceed via this mechanism, offering to provide information required informally. It provided some contextual information, but the financial information it provided was limited, incomplete and did not match information that has become publicly available elsewhere. It took the authority more than a year to provide the key documents requested.

More information is forthcoming when the level of popular opposition to a project, for example the Skye Bridge, provides the impetus for press articles and/or investigation by the National Audit Office (NAO) or its regional counterparts.

3 The reporting framework

The public sector has adopted a framework of reporting intended to meet the needs of shareholders. Information

of value to citizens, especially in relation to actual against expected expenditures, estimates of future expenditures, risk transfer, and contingent liabilities, is not reported in the annual report and accounts.

The private sector has long recognised that the presentation of consolidated accounts for large diversified organisations is problematic for shareholders because it disguises the risk profiles of individual segments. This is now being replicated in public sector consolidations where departmental accounts made up of numerous public authorities may disguise the risks involved in the turn to private finance.

The lack of information from public authorities means that the main source of financial information on the cost of a project is the SPV's financial statements, but these too have their limitations.

First, while the SPVs and their sub-contractors should be the source of horizontal accountability, their reporting is limited and opaque.

Second, their complex group structures means that there is little disclosure of related party transactions. The web of sub-contracting and the accounting regulations that permit close companies to hide behind the "corporate veil" makes it impossible to see where public money is going, and difficult to assess total returns to the private sector.

Furthermore, although the public authorities and the NAO have the right to examine the books of accounts relevant to the contract throughout the extended supply chain, there is no publicly available evidence that they have done so.

4 The cost of private finance

The cost of using the private sector as financial intermediaries is significant.

The cost of finance constitutes the main expenditure in roads projects. But the additional annual cost of private over public finance on these projects, assuming the same level of debt, is

New books published

conservatively estimated at between 8 per cent and 40 per cent of revenues.

The additional total cost of the completed projects, the Dartford Crossings and Skye Bridge, was similarly estimated very conservatively at 7 per cent and 25 per cent of revenues respectively. This must affect the public authorities' budgets and create affordability problems.

The additional cost is attributed to the cost of risk transfer, but a lack of information means that the public cannot assess whether such costs are commensurate with the benefits to the public sector or the risks to the private sector.

Information is lacking about original bids, expected and actual traffic flows, expected and actual payments, any penalty deductions, the cost of operating and maintaining roads, contractual performance and any contractual changes. Despite this, there has been no examination of the additional cost of private finance after the fact by public authorities or watchdogs. At the very least, the high cost attributable to risk transfer raises questions as to whether appraisals of the use of private finance for public infrastructure are appropriate.

Conclusion

These findings are important because other forms of private finance are proliferating. Thus, the problems identified go far beyond the cases cited.

Furthermore, the scale and nature of the problems identified in a sector such as roads, whose projects are large and visible, are likely to be found elsewhere. For projects in local authorities and non-departmental public bodies where reporting is more diffuse, accountability issues may be even more problematic.

The lack of consistent, comparable and understandable financial information in the context of PPP makes it difficult for public sector stakeholders to understand where public money is going, how it is being used, and the extent of future commitments and liabilities.

This makes it all but impossible to gauge the implications for future government expenditure and, perhaps more importantly, the government's implicit debt, which is clearly mounting.

This is not to say that there were ever any "good old days". Rather, the increasing expenditure outside the direct control of the public bodies creates additional reporting problems that make scrutiny, control and thus accountability difficult.

Finally, and most importantly from the perspective of this study, the absence of clear financial information makes it impossible for the public to participate in an informed debate about public and fiscal policy.

The key recommendations arising from the research are targeted in four areas: guidance to public authorities; quality of annual public sector information; information about the private sector partners; and information release.

This report can be downloaded free of charge at www.icas.org.uk/shaoul



New books published

However, if a four-to-three scenario arose because a firm elected to leave the market or merged with another, interviewees believed that the effects would be less severe.

A four-to-zero scenario, where if one of the Big Four failed, the rest chose to leave the audit market of their own accord, was mooted. Several partners used this line of thought to argue strongly for the introduction of proportionate liability (in addition to the limitation of liability by contract enabled by the Companies Act 2006).

However, other interviewees were not convinced of the merits of proportionate liability for auditors and argued that the MPG had bypassed the issues of broadening the audit market in favour of recommendations aimed at preventing another withdrawal. Further work on the advantages and disadvantages of limits to liability, proportionate liability and the likelihood of a catastrophic claim is therefore essential.

Six policy recommendations arise from this study:

- The larger non-Big Four firms should implement marketing strategies to inform audit committees of their abilities and work harder to win the tenders for FTSE 350 companies' audit and consultancy contracts.
- The FRC, as it has indicated, and other stakeholders should assess the level of take-up and the impact of the new auditor liability limitation agreements enabled by the Companies Act 2006.

- The government should seek to remove any barriers to non-Big Four growth, such as contractual obligations to appoint only a Big Four firm as auditor.
- Directors and audit committees should be encouraged to shortlist firms beyond the Big Four.
- The FRC should evaluate the issue of choice in the UK audit market annually. If the supply and demand side measures suggested by the MPG do not improve choice, the FRC should consider non-market-based measures if improved choice is seen as desirable to the majority of stakeholders.
- The FRC, with the support of audit firms and audit committees, should commission a thorough review of the likelihood and economic consequences of a further withdrawal of a Big Four accounting firm from the market.

This report can be downloaded free of charge at www.icas.org.uk/mcmeeking

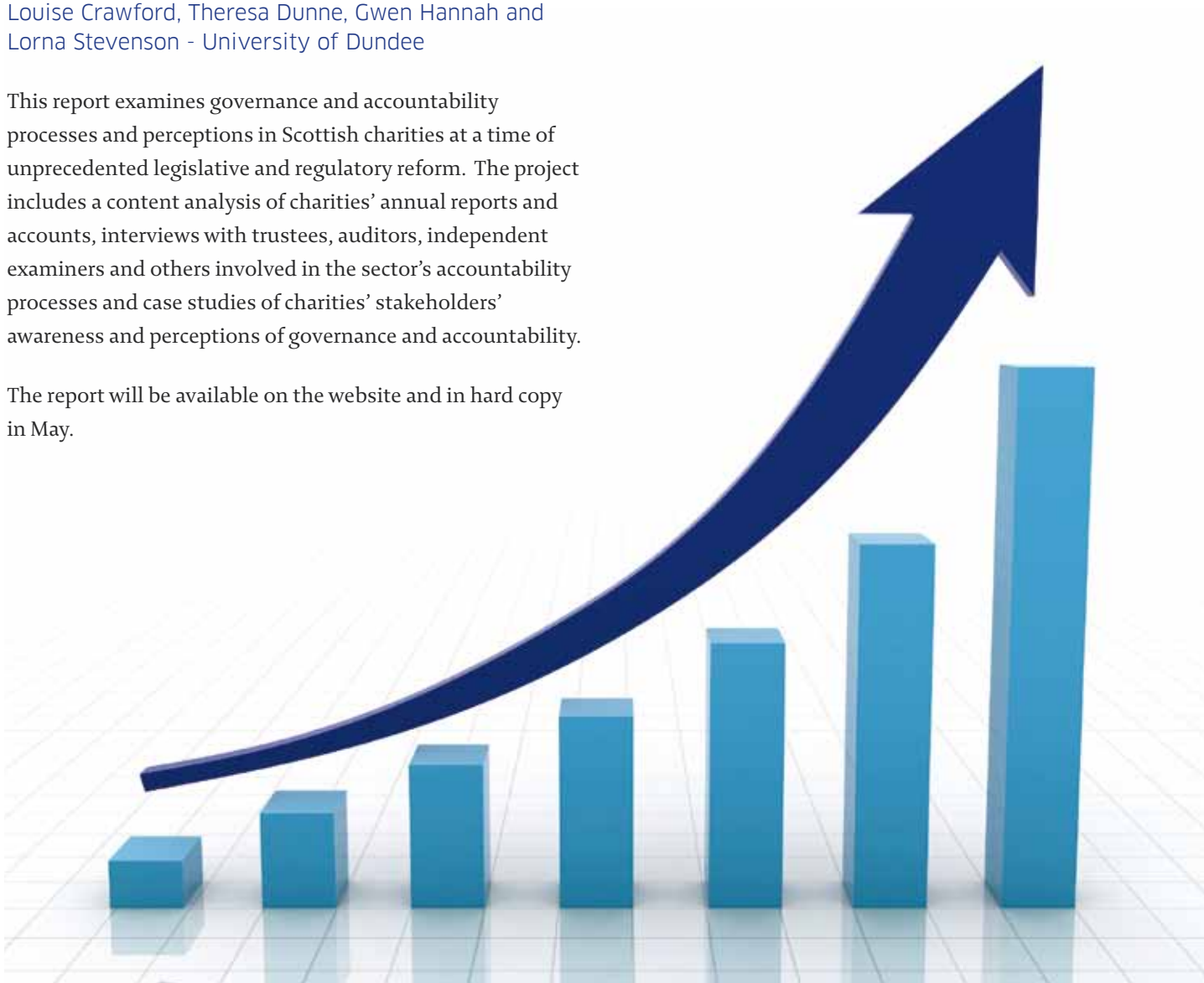
Coming soon...

An exploration of Scottish charities' governance and accountability

Louise Crawford, Theresa Dunne, Gwen Hannah and Lorna Stevenson - University of Dundee

This report examines governance and accountability processes and perceptions in Scottish charities at a time of unprecedented legislative and regulatory reform. The project includes a content analysis of charities' annual reports and accounts, interviews with trustees, auditors, independent examiners and others involved in the sector's accountability processes and case studies of charities' stakeholders' awareness and perceptions of governance and accountability.

The report will be available on the website and in hard copy in May.



All our new publications can be downloaded free of charge from the ICAS website: www.icas.org.uk/research. If you would prefer to order a hardcopy - priced £15 - please contact Angie at the Research Centre on 0131 347 0237 or email: research@icas.org.uk

New grants awarded

Large project grants awarded

The teaching research nexus in accounting

Angus Duff - University of West of Scotland and Neil Marriott - University of Winchester

This project aims to assess how academic research in accounting and finance influences the curriculum, teaching practice, and student learning in universities and professional training. A significant literature has evolved which examines the relationship between academic research and teaching. However, no prior study has considered how research affects teaching, or vice-versa, in the disciplines of accounting and finance, with strong links to professional bodies.

The study investigates academics' perceptions of the relationship between research in the accounting and finance curriculum, student learning, teaching practice, curriculum development and intrinsic/extrinsic rewards for creating integrating research into teaching, and vice-versa. This is termed as the teaching-research nexus. A survey, case study and interview approach will be adopted in the study.

Small project grants awarded

The role of auditors in Swiss banking supervision

Ian Dewing and Peter Russell - University of East Anglia

Work-life balance of female Scottish Chartered Accountants

Catriona Paisey - Glasgow Caledonian University and Sonja Gallhofer - University of Dundee

The effects of gender and family structure on partnership prospects in accountancy public practice

Elizabeth Gammie - Robert Gordon University, Kathleen Herbohn - University of Queensland and Rosalind Whiting - University of Otago

Seedcorn grants awarded

The history of the Cadbury Committee

Laura Spira - Oxford Brookes Business School

A holistic approach to the control systems in the Italian banking sector

Pier Luigi Marchini - University of Parma, Italy

Compliance with IFRS in developing countries

Mazni Abdullah, Lisa Evans and Ian Fraser - Stirling University



These research grants have been funded by the Scottish Accountancy Trust for Education and Research

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Seedcorn projects - research results

Perceptions and attitudes toward corporate website presence and its use as an investor relations tool: the case of Jordan

Clare Roberts and Amer Qasim - University of Aberdeen

For this seedcorn project fourteen interviews were undertaken in Amman, Jordan in the summer of 2008 to understand the attitudes and perceptions of the use of corporate websites in investor relations activities in the Jordanian context.

The interviews investigated the following issues:

- Motivations of Jordanian companies listed in the Amman stock exchange having a website presence and using it in investor relations activities;
- Perceived benefits of a website presence;
- Factors affecting the decision to postpone having a website presence; and
- The perceptions of the Jordanian Securities Commission regarding the use of corporate websites in investor relations activities.

Motivations for developing corporate websites

Company's image

Most interviewees agreed that having a corporate website presence is considered to be a tool to reflect a company's image and reputation locally and internationally. The degree to which a company maintains its website is also related to the way in which a company perceives itself amongst its competitors.

Overseas affiliations and activities

The level of website usage is also affected by having overseas activities with clients, suppliers and shareholders. Companies' with international activities tend to copy website structures

of their rivals in the same sector. In addition, merging with overseas organizations that have highly structured and maintained websites forces a company to restructure its old website.

Rebranding

All companies which renewed their obsolete websites took this decision as part of a re-branding exercise as a result of: offering the company's shares in the stock exchange for public trading; reviewing its marketing campaign due to the increasing level of competition; and merging with other companies.

Management's role

Interviewees also pointed to other factors that have an important role in facilitating the development of corporate websites: management flexibility toward accepting new ideas; employees' participation in recommending the website's structure; and a friendly working environment.

Generally speaking, decisions taken regarding developing a new corporate website or restructuring and updating an old website were in the hands of the company's CEO.



Seedcorn projects - research results

Perceived benefits

The two main benefits identified by the interviewees for having a website presence were:

- savings in terms of time, money, and efforts linked to printing and mailing documents; and
- improvements in internal and external communication with stakeholders.

Benefits to stock market participants

All interviewed individuals agreed that having investor relations information on the company's website does not affect the company's share price or its marketability. However, it does increase the awareness about the company both inside and outside Jordan.

Factors affecting postponing corporate website presence

Management's influence

Interviews were conducted with two companies with no website presence to explore the factors for this decision. Both companies agreed on two factors. Firstly, that the company's operations would not be affected by having a website presence and that Jordanian individuals are not used to using the internet for acquiring and/receiving information. Secondly, there is a lack of legal requirements forcing listed companies to go online. One of the interviewees added that the Jordanian Securities Commission already publishes companies' news and annual reports on its website and there is therefore no need to do that again elsewhere. In addition, being in a monopolistic position in the Jordanian market gave these two companies reasons to feel safe about their operations and hence affected the way they communicated with their stakeholders.

Start-up barriers

Other interviews were conducted in companies that had recently reconstructed and developed their websites and provided reasons for the postponement of a company's website presence. In one company the delay was due to continuous management change. The other company had existed in the Jordanian market for a long time and had a strong relationship with suppliers, customers and shareholders that allowed management to overlook the company's online activities.

Perspectives of the Jordanian Securities Commission

The Jordanian Securities Commission has called for transparency and information availability for stock market participants, as this has a strong impact on reaching a fair valuation of the shares traded in the Amman stock exchange and protects the shareholders from negative surprises. The Commission has therefore taken a number of steps to improve and enhance listed companies' disclosure practices; including the use of websites for the dissemination of companies' news, financial reports, communications, and any other information that might affect investors' decisions. The Head of the Disclosure Department believes that the Commission's website has an essential role in the communication process with stakeholders.

A new regulation is to be issued by the Commission encouraging Jordanian companies listed in the Amman stock exchange to use their corporate websites to publish and disseminate their financial and non financial information that might affect company's shares performance in the market. The new regulation is planned to be voluntary in the first year and then become compulsory in later years.

Seedcorn projects - research results

A comparison of the risks disclosed by UK companies with observed events

Santhosh Abraham - Heriot Watt University
Phil Darby - Napier University

Problem addressed and its importance

Investor pressure and regulatory requirements have driven an increase in narrative reporting in annual reports. Risks and uncertainties are a key component of these reports. Corporate risk reporting is important in helping investors assess the risk profile of a company and in enabling investors to efficiently allocate limited resources in the most efficient manner to suit their risk tolerance. Given the increasing trend towards disclosing risk factor information in annual reports, this pilot project evaluates the relevance of this information by specifically evaluating three questions for four listed companies.

1. Do the types of risk factors disclosed change between annual reports?
2. Are the significant observed events discussed in the subsequent annual report?
3. Are the identified risk events experienced?

Results

The study compiled the risks looking forward and observed events looking back over a trading year. External news sources were searched to determine if the identified risks had been reported. Interesting events were identified by finding days on which there were significant price changes. These sources were then analysed for congruence over time.

Key product failures or success account for the majority of significant negative and positive price changes. There was little or no discussion in the risk factor statements or in other sections of the narrative discussion of factors that

could adversely affect key products. However, information on sales and profits from key products are provided to infer the importance of these products or markets.

Despite an increase in risk factor disclosure over time, the majority of information does not relate to company or product specific information which would be useful for investors' decision making. The companies in the sample also did not emphasise the changing nature of risk disclosure over time in their reporting and there was no connection to risk disclosures made in the previous year.

Pilot interviews were also conducted with representatives from two key investment institutions based in Edinburgh. A number of issues addressed by both parties echoed the earlier findings. The general finding was that annual report narrative disclosure has been improving, as measured by the amount of information provided. Risk reporting is seen as new and evolving as companies are not clear what different user groups require from such a report. Both interviewees stressed the importance of focusing on the quality of information rather than increasing the quantity of general information; in particular risk disclosure information needs to be specific to the company.

While this pilot research provides some interesting insights into risk reporting practices among a select group of companies, further research is needed with a larger sample of



Seedcorn projects - research results

companies to be able to generalise the findings. In order to widen the knowledge of the issues involved in risk reporting it is also important to be able to discuss these findings with preparers and users of annual reports. Interviews with preparers would allow an understanding of some of the constraints (such as proprietary as well as legal costs and a lack of information) that prevent full reporting. Interviews with user groups would gather perceptions on the current state of reporting as well as information sources used to gather risk-related information on a company. In particular the pilot interviews revealed the importance of interviewing sell side analysts as information provided by them is used heavily by fund managers and investment analysts in their decision making.

Conclusions

Despite the small sample, the findings from this pilot study shows that changes need to be made to reporting to allow stakeholders to make crucial economic decisions in the full knowledge of these risks, since the purpose of risk reporting is to avoid surprises. Companies need to focus on the quality rather than the quantity of information provided. Measures could include prioritisation of the significant risk factors with clear explanations of the impact on shareholder value along with mitigating actions rather than the production of a long list of general risks.

Compliance with IFRS in developing countries: The case of Malaysia

Mazni Abdullah, Lisa Evans, Professor Ian Fraser -
University of Stirling

This seedcorn project was funded to develop and test the validity of a disclosure checklist to examine compliance with IFRS in Malaysia.

The disclosure checklist was constructed based on a checklist prepared by the PricewaterhouseCoopers (PWC) Malaysia and with reference to the Financial Reporting Standards (FRSs) issued by the Malaysian Accounting Standards Board (MASB). The FRSs issued and enacted by the MASB are identical to IAS/IFRS.

Annual reports of 12 public listed companies with year ends of 31st December 2007 were selected as a sample. To avoid bias related to audit quality, half of the sample companies selected were audited by one of the 'Big 4' audit firms and the other half by 'Non Big 4' audit firms. To avoid an industry effect, the sample covered all major industries.

Given the small sample size in this study, it may not be appropriate to generalise the findings, but the preliminary findings of the pilot suggest that:

- The level of disclosure compliance by Malaysian public listed companies ranges between 63% and 94%; and
- The low compliance scores are found in three FRSs: FRS 117 Leases; FRS 136 Impairment of Assets; and FRS 138 Intangible Assets.

Based on the findings of this pilot study, the researchers will undertake a full study with a large sample size to investigate compliance issues in Malaysia. They will also conduct interviews with preparers and auditors.

Small projects - research results

The impact of the adoption of IFRS on executive compensation design

Lisa Shifei Liu and Ann Ling-Ching Chan - University of Liverpool

This project investigated the influence of the mandatory adoption of International Financial Reporting Standard (IFRS) on the design of executive compensation schemes using a sample of non-financial firms in the FTSE 100 index in the period 2003 to 2007.

Research questions

The project investigated the following research questions:

- Is there any change in the design of executive remuneration schemes of UK listed firms associated with the advent of IFRS due to the recognition of employee share options as an expense under IFRS 2 'Accounting for Share-based Payment'?
- Do remuneration committees continue to use accounting earnings as the performance criteria after the advent of IFRS adoption? This research question is motivated by the argument that although IFRS provides timelier, more value-relevant information, it inevitably makes reported earnings more volatile and in turn increases executives' compensation risk.

Results

The results show that firms gradually reduced the use of employee share options and increased the grants of long term incentive plans (LTIPs) in the advent of IFRS adoption in the UK. In the sample, 44% of CEOs received LTIPs two years before the IFRS enactment and this number increased to 76% in the IFRS adoption year (2005). The number of CEOs receiving employee share options reduced from 62% to 24%. However, only rarely do the sample firms disclose the reasons for such changes. The mean value of employee share options

as a percent of total compensation declined from 20% to 6% for CEOs and from 23% to 7% for other executive directors from 2003 to 2006. Other pay components expressed as a percentage of total compensation experienced slight increases during the period. Overall, the findings support, to some extent, the conjecture that there are employee share option cutbacks around the mandatory IFRS adoption and the level of these cutbacks appears to be replaced by the increasing use of LTIPs and other forms of equity incentives.

It was found that the majority of companies continue to use earnings per share (EPS) and/or total shareholder returns under IFRS as measures of performance targets. When compound annual real growth in EPS was used as the performance condition, sample firms adjusted EPS to exclude exceptional items and goodwill amortisation. This is referred to as 'normalised' EPS and is recommended by the Association of British Insurers. Some companies explicitly stated that they recognised the impact of IFRS on reported earnings as the performance condition and adjustments were made to ensure that fair performance measures were used. Very few companies explicitly discussed and assessed the potential impact of IFRS on remuneration policy.

Conclusion

Following the introduction of IFRS in 2005 for listed parent companies in the UK the new accounting treatment for share-based payment may influence the design of directors' remuneration packages and the use of EPS as a performance target. The empirical evidence confirms there is a decreasing trend of awarding executive directors with share options in the test period. There is also little evidence of companies avoiding the use of EPS as one of the performance targets in options, bonus and share awards schemes following the introduction of IFRS in the UK. While the compliance of IFRS has a short-term effect on capital markets in the UK, its medium-term impact on managerial incentives and corporate governance remains unclear and deserves future research.

Small projects - research results

Understanding plagiarism by accounting students

Xin Guo and Angus Duff - University of the West of Scotland

The purpose of this project is to create a model of what motivates accounting students to engage in plagiarism. A literature review identifies eight factors that are likely to influence accounting students' plagiaristic behaviour. These eight factors are labelled: (i) moral capability; (ii) demographics; (iii) attitudes; (iv) pressures; (v) the pedagogy and curricula of accounting education; (vi) new technology; (vii) institutional issues; and (viii) cultural influences.

To allow a better understanding of the intersection of plagiarism, accounting education, and the cultural context three focus groups were conducted. The focus groups used undergraduate and postgraduate participants from different cultural backgrounds. An 81-item questionnaire was created to measure students' attitudes towards the precursors of plagiaristic behaviour and the extent of plagiarism involved. The inventory was administered to 381 students enrolled in accounting programs at two universities in Scotland. Structural equation modelling (SEM) via AMOS 7.0 was used to assist data analysis.

Results indicate that gender, moral capability, cultural influences, and attitudes towards study are the four antecedents of plagiarism. Specifically:

- male students are more inclined to engage in plagiarism than their female peers;
- low levels of moral capability may encourage plagiarism;
- the lack of course work experience and ambiguous knowledge of authorship are the principal causes of plagiarism; and

- students' lack of academic integration and laziness are associated with plagiaristic behaviour.

The research has six implications for accounting educators seeking to prevent and reduce the incidence of plagiarism:

- educate students what constitutes plagiarism with a special focus on paraphrasing;
- equip students with a clear understanding of the problems and copyright implications of plagiarism;
- provide additional language support for overseas students;
- provide institutional support to integrate students into academic life;
- provide clear guidance and feedback on students' written assignments; and
- adopt a consistent and ethical approach to encourage students not to fall into plagiarism.



Research news...

ICAS Research Committee welcomes new member



ICAS is pleased to announce that Riona Bell has accepted an invitation to join the ICAS Research Committee.

Riona is Director of Funding at the Scottish Further and Higher Education Funding Council where she is responsible for managing the allocation and payment of the main grants for teaching and research to Scotland's 43 colleges and 20 higher education institutions.

Riona trained and qualified as a CA with Scott Moncrieff and then spent 15 years with KPMG and its predecessors. She then worked for the Scottish Office/Scottish Executive in various finance-related roles until moving to her present post in 2004.

Until recently, Riona served as a member of the ICAS Public Sector Committee.

A guide for PhD students 2009

Accountancy and finance research study in Scottish Universities



A Guide for PhD students

The Research Committee has recently published the 2009 edition of the guide for postgraduate research supervision in accounting and finance departments in Scotland. It is intended that the guide will assist potential PhD students to identify the supervisor whose research interests are closest to the students' intended field of study. Copies of *Accountancy and Finance Research Study in Scottish Universities: A Guide for PhD Students* are available free of charge from the Research Centre and can also be downloaded from the website - www.icas.org.uk/phdGuide. Copies have been sent to all university Accountancy Departments and libraries in the UK and Ireland.

ICAS technical news

ICAS guidance: 'Pension trustees: getting the balance right in evaluating the employer covenant'

This guidance addresses an outline of the issues which may be relevant when evaluating and monitoring the ability and willingness of the employer to support its defined benefit pension scheme. It also contains practical examples to illustrate these issues.

The guidance notes that trustees may appoint external advisers to conduct this review or they may collate the necessary information and undertake the analysis of the employer covenant themselves. In either case, this ICAS tool is designed to be of practical help to trustees in the context of a review of the employer covenant and to help them to recognise and discharge their responsibilities.

A copy of the guide is available on the ICAS website at www.icas.org.uk/EmployerCovenant

ICAS guidance: 'Pension trustees: Evaluating your scheme auditor'

ICAS has issued guidance 'Pension Trustees: Evaluating your Scheme Auditor', a further publication in its useful series for pension trustees.

The guide is designed to assist trustees in their evaluation of the auditor of their pension scheme, and to maximise the benefits from the audit.

A copy of the guide is available on the ICAS website at www.icas.org.uk/PensionAudit

ICAS representations to the G20 governments

There is currently considerable debate as to whether financial stability should become a primary objective of financial reporting. Political pressure is currently being exerted on the International Accounting Standards Board (IASB) to amend its approach to give this objective primacy.

ICAS in its submission to the G20 secretariat is urging the G20 governments to show support for the IASB's view that the primary objective of financial reporting is to provide economic transparency - a necessary prerequisite for financial stability.

A copy of the ICAS submission is available on the ICAS website at www.icas.org.uk/G20

ICAS key policies in relation to the economic and financial crisis

The accountancy profession, with its involvement and expertise in financial reporting, auditing and the business and financial communities more widely, clearly has a vital part to play in re-building confidence in the current economic climate. ICAS recognises that accountants have a role to play at all levels of the economy and has developed policies to guide members and its work as a leading representative of the accountancy profession through the challenging times ahead. ICAS seeks to be involved in the debate in those areas where it has a recognised standing and clear expertise.

A copy of the key policies is available on the ICAS website at www.icas.org.uk/EconomicCrisis

ICAS technical news

Fair value accounting and its role in the current financial crisis

At the annual Aileen Beattie Memorial Lecture, hosted by The Institute of Chartered Accountants of Scotland (ICAS) on 23rd March 2009, Professor Avinash Persaud, one of the world's leading financial experts, Chairman of the Warwick Commission and Member of the UN Commission of Experts on Financial Reform, argued that accountants are right to be concerned that fair value accounting should not stray from its primary objective of serving shareholders, but for some types of institutions, there are alternatives to "mark-to-market" that may serve both shareholders and the financial system better.

He stated that while fair value accounting has its detractors, employing it in a boom and suspending it in a crisis cannot be right from a systemic point of view.

Professor Persaud outlines his position, "In the financial sector, value accounting should not be influenced by the fantasy of intentions. Financial companies without the wherewithal to survive one day are valuing assets on the basis that they intend to hold them for the next 20 years. But it should be influenced by the risk capacity of institutions and this risk capacity is most obviously and transparently reflected in the maturity of liabilities.

From a financial stability point of view, those with short-term liabilities are risk traders and those with long-term liabilities are risk-absorbers. The system needs both. Through a host of measures we have weeded out the risk absorbers, planted more risk traders and are now reaping what we have sowed.

Institutions with short-term funding or liabilities, whatever their intentions, cannot deviate from mark-to-market accounting. Institutions with long-term funding should at a minimum, consider two types of valuation, one reflective of tomorrow's market price and one reflective of the real risks they face. If this second valuation was the one used for risk-

control and risk management, it would serve Lord Turner's concern for systemic stability, whilst being a closer reflection of the real risks being faced by the long-term firm. Liabilities are key and remember that long-term liabilities can be found in parts of banks in the same way that short-term liabilities are present in pension funds and insurance companies."

A full transcript of the event will be available on the ICAS website at www.icas.org.uk/AileenBeattie

Can financial reporting be made simpler and more useful?

ICAS is a member of The Global Accounting Alliance (GAA), an alliance of ten of the world's leading accounting bodies, brought together to promote quality services, share information and collaborate on important international issues.

The GAA has published its report *Getting to the heart of the issue – Can financial reporting be made simpler and more useful?* - which is based on a series of interviews conducted in 2008 with financial regulators from the UK, Canada, China, the United States of America, South Africa, France, the European Commission as well as international regulators. Interviewees also included a leading US litigation lawyer and representatives of the world's leading accounting and auditing practices.

The research was undertaken to consider the barriers to the implementation of a more principles based accounting regime, and the increasing complexity and detail in company financial statements. The GAA is arranging a number of roundtable events where regulators and other stakeholders in financial reporting around the world can begin discussions on a number of ideas emerging from the research.

A copy of the report is available to download at www.globalaccountingalliance.com

Dates for your diary

21-23 April 2009

BAA Annual Conference 2009
University of Dundee

12-15th May 2009

EAA Annual Congress 2009
University of Tampere, Finland

20-22nd May 2009

BAA Accounting Education SIG Conference
Wivenhoe House Conference Centre, Colchester

15th June 2009

BAA Scottish Doctoral Colloquium
University of Stirling

31st August 2009

BAA Scottish Conference
University of Stirling

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