

**THE IMPORTANCE OF PROFESSIONALISM
IN GLOBALLY INTERDEPENDENT MARKETS**

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Introduction

Thank you very much for the invitation to speak at this annual convention.

As you know, I speak as Deputy President of the International Federation of Accountants (IFAC). It so happens that I am also a Chartered Accountant, a member of the ICAEW, though as has just been explained actuarial issues do have a special place in my heart!

The issues which face all financial services professionals – not only accountants or actuaries – are global issues.

In the light of recent corporate collapses, the key role of finance professionals in the capital markets has been more widely acknowledged, as well as drawing attention to the legal profession, bankers, analysts and so on.

So this really is an appropriate time in which to be talking about professionalism. The role of the professions, what it means to be a profession, how it conducts itself and its systems of regulation, our very license to operate, is being publicly questioned and re-examined.

In the UK, at the same time that the accountancy profession has had its system of oversight overhauled by the government and is still ironing out the details, Sir David Clementi is leading a review of the legal profession, with which I am helping. As we know, Sir Derek Morris's review of the actuarial profession began just last month.

Such reviews have been happening all over the world in developed and developing economies alike.

The professions are recognising the need to change and regulators are taking a more proactive role in driving those changes than ever before. It is one of the reasons why IFAC has invested so much time and energy on relationship building with regulators internationally. We want to ensure that they understand that our goals are aligned with their public interest objectives (in our case, ensuring high quality audit and accounting worldwide) and so build transparency and trust between us.

Before I continue, let me say, when I use the example of the UK accounting profession to illustrate some of my points it is:

- a) because the UK profession has a unique place in the history of standard-setting, particularly in the development of professional and technical standards; and
- b) because the lessons learned in the development of the UK's system of financial regulation were a precursor to much of what is now occurring globally.

Perhaps I should start by asking what is a profession and what do we mean by professionalism?

The generic term profession (pro-frater: to confess, own or acknowledge) goes back in history and originally was understood only in a religious sense when it was used to describe someone who made a public declaration of service to God. Today, this sense has been secularised and transformed to being about a duty of service to the public interest.

The claimed professionalisation of all types of work, however, is one of the characteristics of our modern society. Sociologists speak of the professionalisation of everyone and everything from housecleaning to car repairs!

There is a distinction to be made, therefore, between what constitutes a profession and what constitutes professionalism.

What constitutes a profession?

Let me begin with a 20th century definition. A profession is not a business. A profession is a body of people defined by its concern with commanding respect and building trust by acting first and foremost in the public interest, a duty to subordinate personal financial reward to responsibility to others.

In this sense, the traditional professional role was to put the interests of the client before one's own. It was therefore perhaps the institutionalising of professions that first led to the public interest being primary for a profession as a whole. It is certainly at the heart of a Royal Charter in the UK where its granting is reliant upon a body being able to prove that it is in the public interest for it to be subject to Privy Council (ie. Government) regulation under that Charter.

Over the last few decades, the enormous shift from client interest to greater emphasis on public interest has been driven by developments in the capital markets: especially so for auditors and accountants. As the Law Society President so rightly pointed out recently, an auditor's duty of independence is a duty owed to the public whereas a lawyer's duty of independence is owed only to the client.

To some extent, the public interest agenda of governments is forcing the professions to become unpaid agents of government through, for example, the money laundering regulations. We all accept that money laundering should be stopped. But it would be interesting to study how the disproportionate weight of criminal sanctions against professionals for failing in even the smallest matter here might be working against the public interest if fear of it is affecting the focus and therefore the quality and effectiveness of their services to clients.

Be that as it may, today the accepted distinguishing marks of a profession are the requirements of:

- extensive formal training and life-long learning
- admission to practice by qualifying licensure
- a code of ethics
- a system for discipline of its members for violation of the code of ethics and, notably,
- an obligation on its members, even in non-professional matters, to conduct themselves as members of a learned, disciplined and honourable occupation.

This definition encapsulates the principles for a profession outlined by Lord Benson, one of the UK's foremost chartered accountants of the last century. The underlying values he outlined – those of transparency, integrity and competency – underpin our licence from society to operate and are the core values subscribed to by IFAC. Indeed, volunteers who work with IFAC, myself included, have taken an oath to abide by them in the public interest.

The fundamental importance of all of this has clearly been recognised in the terms of reference of the Morris Review, which encapsulate the same elements.

Professionalism - trust and demonstration

Professionalism, on the other hand, is about individual modes of behaviour that command respect and build trust. It is about excellence in service as measured by recognised standards. It is about delivering services or working to standards that meet the needs of and are expected by our clients.

Such behaviours are indeed a necessary part of belonging to a profession but almost any trade could be described as professional in these terms!

As any of us here knows, what separates the professionalism of members of a professional body from the behaviours of other types of so-named professionals, is the requirement to continually reinforce and demonstrate our professionalism, not merely assert it through a one-off qualification. And it is our membership of a professional body – one which embodies the distinguishing features I have defined – that confers on us the obligation to abide by professional standards and regulation.

It is therefore no longer enough for professions to say to the public ‘you must trust me’, today we must earn that trust and demonstrate: clearly, openly and often, why that trust should be given.

This is why IFAC works together with its 158 member bodies from 118 countries to enshrine its values into the quality standards that we are developing for the global profession and need to ensure we enforce throughout the world. Those standards include membership obligations for the professional bodies themselves covering, for instance, quality assurance and investigation and discipline.

All of this informs our education and training and puts ethics right at the heart of all our work. It is the foundation on which rests the integrity of our professional reputation. IFAC’s Code of Ethics for Professional Accountants is, today, applicable to some two and a half million accountants worldwide in the private and public sectors alike, across all areas of business and commerce.

History shows why demonstration is important

Historically, the professional accountancy bodies in the UK enforced standards in reaction to complaints received from the public. That became unacceptable as the accountants’ roles in sizeable financial scandals emerged. It was only in the late 80’s that the bodies became proactive by setting up an independent practice inspection unit called the Joint Monitoring Unit (JMU), that was paid for solely by the profession, to monitor whether the processes enshrined in Auditing Standards had been followed.

Today, however, as you are aware, in relation to auditing we are moving on to independent practice inspection by a wholly independent body under the new FRC arrangements, one which (significantly) is concerned not only with process but will also be taking a view on how professional judgement has been exercised.

This type of ‘demonstration of trust’ – wholly independent oversight - is the logical culmination of the history of accounting standard-setting and professional self-regulation in the UK. Our license from society to exist as professional bodies has been questioned with every set of financial scandals and we have entered a new phase of professional regulation.

Three themes

This new phase has been informed by three significant themes that have emerged through the evolution of the UK’s history in standard-setting that are relevant to all professions:

- First, recognition that standard-setting is a public interest activity. This recognition has been driven by the effects of financial scandals. Globalisation and increased interdependence of economies have only served to reinforce that point on an international level. So standard-setting has been taken out of the profession’s sole hands and moved either to independent bodies which include a variety of stakeholders, including independent professionals or to oversight by independent bodies, in order to credentialise the standards.
- Second, the status of standards has been strengthened by enshrinement in law. Compliance therefore has become mandatory. This has meant setting up monitoring systems and enforcement mechanisms to provide public assurance of quality. But these have moved from being run and funded solely by the profession to being a partnership with government, in terms of monitored self regulation.

- Third, the move from client interest to public interest, again driven by financial scandals. The role of professions, particularly of accountancy, in the capital markets has ensured increased public expectation of assurance on accountability. Self-regulation, therefore, is being overtaken by the political and public emphasis on the perceived benefits of independent public oversight.

IFAC's experience is that these themes will continue to be reinforced as regulators around the world work more closely together and regulatory thinking on professional regulation begins to converge, despite the differences in culture and business structures around the world.

Let me explain how these themes have emerged.

Evolution of UK standard-setting supports these themes

If one were writing a history of the capital markets, it is a fair bet that the single most important innovation shaping those markets was the idea of generally accepted accounting principles. Given the politicisation and globalisation of the accounting and professional standard-setting process in today's capital markets, it is perhaps hard to believe that until 1990 accounting standards in the UK, one of the most international financial markets, were set solely by the accountancy profession.

Prior to World War II, there was a plethora of differing accounting practices and undisclosed lack of consistency. Then, just after the war, the ICAEW Council announced that it would publish accounting recommendations which would not be mandatory but would, it was hoped, become best practice. A quiet revolution therefore took place with far less fuss than would be needed for a minor change in the Institute's constitution! In all, the Institute issued 29 Recommendations on accounting up to 1969.

It was the major financial scandals of 1969 that forced recognition that 'recommendations' did not have sufficient status to ensure compliance. The accountancy profession therefore needed to address the resulting criticisms. So the Accounting Standards Steering Committee, as well as an Auditing Practices Committee, were formed and began to issue standards on accounting and auditing.

As a matter of interest, it was shortly after this that the UK profession led the foundation of the International Accounting Standards Committee (now the IASB), followed by the creation of IFAC in 1977, because we felt that globalisation of trade would also drive these issues internationally.

The UK standard-setting process, however, had what turned out to be significant flaws in public and regulatory eyes, principally a perception that it was a self-serving exercise. This is because it was standard setting undertaken and funded solely by the profession. The Councils of the accountancy bodies were responsible for ratifying the standards, there was no independent influence. Also, the lack of direct legal responsibility to comply with standards was compounded by the perception that enforcement by professional bodies was weak.

Once again, it was major financial scandals, now in the mid to late 80's, which drove change through the system.

But this time, public perception that standard-setting and enforcement by the profession had signally failed to contribute to the prevention of financial chicanery forced a major sea-change in the standard-setting process and the status of standards themselves.

The resulting structure under the Financial Reporting Council, set up in 1990, was designed precisely to gain wider acceptance of the standards established – to build public confidence. It was recognised that to reinforce objectivity and credentialise the standard-setting process, it must achieve buy-in from the corporate sector and the city.

It became, therefore, a partnership between the profession, government, the City and industry. This time, funding was divided between those constituents, not solely provided by the profession. Senior business leaders became involved as part of the credentialisation process, the Government and Bank of England appointed the independent chairman.

It was viewed as a huge step forward that the new Accounting Standards Board took responsibility for standard-setting, not the accountancy Institutes' Councils. Standards were to be set by a broader constituency than merely accountants to get the buy-in of the very people who would need to use them in business.

Significantly, financial reporting standards were built into law to ensure greater compliance. And as I have said, this is a trend that continues. So, for instance, we are seeing the European Commission building auditing standards into EU law in the 8th Directive, as well having made mandatory the adoption of International Accounting Standards next year. In the UK, the new Companies Bill will also bring auditing standards into the force of the law. The regulatory perception, therefore, is that legal instruments ensure compliance far more than professional enforcement.

Monitored self-regulation moving to independent oversight

Another significant development in the late 80's was the change of approach to self-regulation by the accountancy profession. As I mentioned earlier, it was at the same time that the Joint Monitoring Unit was set up in partnership with the government. The Institutes began to and still do, report annually to government on how they have undertaken that work.

This partnership was seen to work well. But in 1997, the accountancy profession foresaw that there would come a time when it would need to provide additional public assurance on self-regulatory activities. So it began, with the consent of government, to formulate and implement plans to create a system of independent public oversight in the form of the Accountancy Foundation.

Obviously, we could not have foreseen quite how important such oversight mechanisms would become in the major developed markets.

As you are aware, the government's review in 2002 of regulation of the profession in the light of US corporate scandals, resulted in a number of changes to strengthen the system of monitoring of financial reporting by UK companies and oversight of auditors. The FRC has taken over the independent regulatory activities first proposed for the Accountancy Foundation. Numerous changes have been made that again follow the patterns I have described in terms of funding, pro-activity in monitoring, of independence and status of the parties involved.

In the international arena, with similar credentialisation of objectives in mind, IFAC, supported by the international regulators, is setting up a Public Interest Oversight Board to oversee its audit and ethics related standard-setting activities. We must demonstrate to the public that the international accountancy profession is responsive to the public interest.

Conclusion

In the same way that the public invests trust in the auditing profession in respect of its investments, it places equal trust in the actuarial profession in providing for old age, long term savings and protection, both life and non-life.

The developments which I have described in the accountancy world are likely to translate to the regulation of other professions, including actuaries.

We have seen the move from our profession acting alone, with the consent of government, to a partnership amongst government, regulators, the profession and users.

But that partnership of monitored self-regulation is moving more and more towards independent regulation. In a way, we are in the phase of the 'last chance saloon'. If the partnership doesn't work, professional bodies could be taken out of the equation and we will lose our status and standing.

The best people will no longer join us. Professional bodies acting in the public interest will become trade associations acting in the private interest and the resultant lower quality of service delivery will irreparably damage investment in markets; jobs; and indeed, society as a whole.

Regulators do recognise that independent public oversight on its own is not sufficient to ensure quality or compliance with standards. They therefore seek assurance that the professions are themselves taking seriously and demonstrating their commitment to high standards of professional and ethical behaviour through monitoring, enforcement and discipline. That aspect of self-regulation remains as important today as it always has been.

But if we are not to die in the 'last chance saloon', independent regulation and monitored self-regulation must constitute a mutually reinforcing circle, in the public interest.

What is needed, therefore, is a 'contract of trust' between government, regulators, users and the professions and this contract must not be broken. The future of professionalism and of our professions, yours and mine, very much depends on it.