

**The London School of Economics and Political Science**

**MISTRUST IN NUMBERS**

**The rise of non-financial and future-oriented reporting in  
UK accounting regulation in the 1990s**

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**A thesis submitted to the Department of Accounting of the  
London School of Economics for the degree of Doctor of Philosophy**

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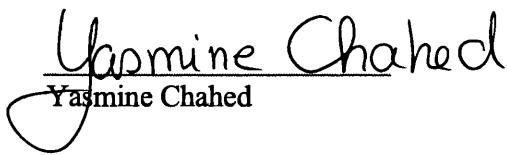
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## **Abstract**

This thesis studies the rise of non-financial and future-oriented narratives in the regulatory framework for financial reporting standard-setting and legislation in the UK in the 1990s. The questioning of financial reporting numbers that surfaced in these debates is called here a “mistrust in numbers”.

To study the moments when a ‘trust in numbers’ is destabilised through these debates, the thesis focuses on three interrelated processes of financial reporting change. First, the thesis addresses the ways in which accounting sought to expand into new territory – territory in which the emergence of a category of non-financial and future-oriented accounting became closely linked to a rethinking of the concepts of how to govern British companies in the last two decades of the 20<sup>th</sup> century. Second, the thesis analyses how the expansion of accounting standard-setting beyond a focus on the financial statements in the early 1990s was made possible by the interplay of a number of ideas – some complementary, others competing – about the technical, professional, and international role of the British Accounting Standards Board. Third, the thesis analyses the agenda-setting process for the British Company Law Review between 1998 and 2002. It outlines how, through this reform process, a realignment between law, accounting, and “the State” was sought, one that mediated and structured at the same time modes of economic governance pertaining to both “the State” and “the market”.

This thesis concludes that the calls in the UK for supplementing financial statements with non-financial and future-oriented reporting elements constitute a significant rethinking of the roles of accounting and regulation in organising economic life. This rethinking entails, it is suggested, a move away from an emphasis on the neutrality and objectivity which has typically been associated with accounting numbers, and towards one aspiring to provide “transparency” based on an underlying economic reality.

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## Chapter 1

### FINANCIAL REPORTING BEYOND THE NUMBERS

*“I think the OFR is going to be THE document that should be really looked at, because the [financial] accounts will only be the appendices to it.”*

*(Standard-setter F)*

#### **1 Expansions of financial reporting frameworks**

Narrative non-financial and future-oriented reports have increasingly been elaborated as an integral part of the financial reporting framework, both in the UK and internationally. They are expected to give visibility to a broad range of economic activities and relations – much broader than those contained in the financial statements. In these reports, company directors are supposed to present an evaluation of the performance and the prospects the business. This is supposed to include reporting on the objectives of the business and the strategies for successfully achieving them – given the resources available, and the principal risks and uncertainties facing the company. From the perspective of report-users, additional non-financial and future-oriented statements in the annual report of companies are seen as a means of interpreting the current and future operating performance and financial position of companies in increasingly complex and dynamic economic environments.

This research analyses the events that made financial reporting “beyond the numbers” possible. It focuses on the rise of regulatory frameworks for non-financial and future-oriented reporting in accounting standard-setting and regulation in the UK in the 1990s. Britain has been leading the regulatory developments in this area for almost two decades. The British Accounting Standards Board (ASB) was the first national standard-setter which launched a project for standardising the voluntary presentation of non-financial and future-oriented management commentary in the annual report of companies. The *Statement: Operating and*

*Financial Review* was published in 1993.<sup>1</sup> The UK was also the first jurisdiction to pick up ideas of non-financial and future-oriented accounting as subject for statutory regulation. A mandatory Operating and Financial Review (OFR) was proposed during the British Company Law Review (CLR) launched in March 1998 by the Department of Trade and Industry (DTI). In 2005, a legal requirement for directors of British listed companies to prepare a mandatory OFR as part of the annual report was introduced.<sup>2</sup> Although the *OFR Regulations 2005* were repealed after a short political turmoil in the same year (Brown 2005; DTI 2005), section 417 of the *New Companies Act 2006* still requires all medium to large British companies to prepare a conceptually similar “enhanced Business Review”.<sup>3</sup>

Since the start of the 21<sup>st</sup> century, similar expansions of the financial reporting framework into the areas of non-financial and future-oriented reporting have taken place in other countries, too. The Australian *Corporations Act 2001*, for example, introduced a requirement for listed companies to report on strategies and future prospects.<sup>4</sup> In Canada, the Ontario Securities Commission (OSC) reformed the existing requirement to produce a *Management's Discussion and Analysis of Financial Condition and Results of Operations* (MD&A) in 2004 to discuss and analyse past corporate performance and future prospects.<sup>5</sup> Since 2005, formal requirements for additional non-financial and future-oriented narrative disclosures in financial reporting have also been introduced in the European Member States. They were implemented into national law following the introduction of the *Modernisation Directive* (EC 2003a). It introduced a basic Business Review requirement, including the reporting of financial and non-financial key performance indicators (KPIs). The Directive also demanded that environmental and employee matters be covered “to the extent necessary” for an understanding of the current and

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<sup>1</sup> The term “Operating and Financial Review” (OFR) was coined by the ASB in one of the meetings of the Board in 1991/92 to describe narrative statements in which company directors explained their perception of the current position and future prospects of the business (Standard-setter D).

<sup>2</sup> *The Companies Act 1985 (Operating and Financial Review and Directors' Report etc.) Regulations 2005*.

<sup>3</sup> The requirement came into force for financial years beginning on or after 1 October 2007 (BERR 2007a). For the definition of medium sized companies and a concluding definition of large companies, see sections 465 to 467 CA 2006.

<sup>4</sup> Section 299A Corporations Act 2001.

<sup>5</sup> The original Canadian MD&A requirement was introduced in 1989 with the Policy Statement No. 5.10 *Annual Information Form and Management's Discussion and Analysis of Financial Condition and Results of Operations*. The 2004 revisions are laid out in Canadian Securities Regulators National Instrument 51-102 *Continuous Disclosure Obligations*.

future performance of the business.<sup>6</sup> Most recently, on 23 June 2009, the International Accounting Standards Board (IASB) published an *Exposure Draft: Management Commentary* (IASB 2009) with proposals for a non-mandatory framework to guide the preparation of additional narrative disclosures on the underlying financial and non-financial drivers of long-term business performance. It will provide the first set of international financial reporting guidelines for voluntary disclosure on non-financial and future-oriented information.<sup>7</sup>

The regulation of OFR-type reporting, including the enhanced Business review, in the UK and internationally emphasises the role narrative statements from the point of view of company directors play in providing the context within which the information that is provided in the financial statements should be interpreted. The preparation of OFR-type reports, therefore, significantly extends the range of reporting issues within the financial reporting framework: The stress on reporting on the main trends and issues which are likely to affect the future of the business open up financial reporting to environmental, social, and community considerations. They also require that wider stakeholder relationships, including employees, customers, and suppliers, be taken into account and discussed in financial and quantitative, but also in non-financial and qualitative statements. Although accounting professionals were already developing alternative measurement and reporting techniques by the end of the 1970s (Abbott & Monsen 1979), the focus of OFR-type management commentary is different from that of voluntary frameworks for environmental and social disclosure.<sup>8</sup> Ideas of “social accounting”, which originated in the early 1970s, focus on accountability mechanisms that go beyond representations of corporate activity in economic terms and, instead, emphasise their ethical and ecological aspects (cf. Gray 2002). In contrast, calls for additional non-financial and future-oriented statements in financial reporting stem from a development in the 1980s and the 1990s during

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<sup>6</sup> The Directive 2003/51/EC of the European Parliament and of the Council (*Modernisation Directive*) amended the 4<sup>th</sup> (EEC 1978) Council Directive on annual accounts of companies and 7<sup>th</sup> (EEC 1983) Council Directive on consolidated accounts.

<sup>7</sup> The MC project was added to the active agenda of the IASB in December 2007 (IASB 2008). The comment period on the ED will end on 1 March 2010 (IASB 2009).

<sup>8</sup> For example, Ernst & Ernst, which was then a “big 8” accounting firm, was the first to develop a list of measurement categories for “social responsibility disclosures” in the UK (Abbott & Monsen 1979). For a review of professional initiatives in the emerging field of social reporting in the US during the 1970s, see Ramanathan (1976).

which notions of social and environmental performance became more closely linked to ideas of financial reporting and economic performance (Shaw 1990, p. xxi; Eccles 1991).

However, the recent calls for additional disclosures to supplement the financial reports in the UK and internationally are in themselves not new. The provision and regulation of additional narratives in the annual report has a relatively long history in the UK and other jurisdictions, such as Germany and the US. Germany already introduced a mandatory management report (*Lagebericht*) to explain and comment on the financial statements of public limited companies in the *Aktienrechts(not)verordnung 1931* (Eierle 2005). And directors of UK companies have published voluntary narrative statements on “the state of the company's affairs” for more than a century (Lynex 1945; Camfferman & Zeff 2003). The British legislator introduced regulatory provisions for the preparation of a “Directors’ Report” in the UK as far back as the *Companies Act 1948*.<sup>9</sup> In the US, the Securities and Exchange Commission (SEC) introduced the requirement for the presentation of an MD&A in the annual report of US public companies in 1968 (Dieter & Sandefur 1989; Collins et al. 1993; Hübner 2007).<sup>10</sup> Transnational regulation at European Union (EU) level also introduced a basic management commentary requirement for limited liability companies through the 1978 Fourth European Accounting Directive. This required companies in all Member States to “[...] include at least a fair review of the development of the company's business and of its position” in their annual report (EEC 1978, art. 46).

Despite the relatively long history of regulating additional disclosures in the annual report, the recent debate differs in three ways. First, it no longer focuses only on the past. Recent proposals for narrative disclosure emphasise the provision of information on the current potential of the firm to meet its long-term objectives. Second, it regards the presentation of additional narratives as an integral part of the financial reporting package rather than a separate form of disclosure. The third and most striking aspect of the proposals for additional management commentaries in

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<sup>9</sup> Section 157 CA 1948.

<sup>10</sup> The US Securities and Exchange Commission (SEC) reformed the framework for “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in 1980 (SEC 1980). The current framework emphasises a focus on the financial statements as a whole. The original MD&A (SEC 1968) had been primarily concerned with a summary analysis of earnings and their components (Dieter & Sandefur 1989).

financial reporting has been the fundamental questioning of financial reporting numbers as an issue for governing that has surfaced in many different environments in the UK as well as internationally. Ideas of non-financial and future-oriented reporting can be traced back to the emergence of significant doubts about the neutrality and objectivity of financial reporting numbers as an instrument for intervening in business enterprises and the economy. The development of new ways of questioning the role of accounting in governance is described as a “mistrust in numbers” in this research. The term is used in this thesis to describe the view that financial statements alone were not sufficient to convey a picture of the economic reality of companies to internal and external decision-makers in times of increasingly complex and dynamic business environments. These observations seem to be contrary to the argument that the role of accounting in governance is founded on a “trust in numbers” (cf. Porter 1995). This idea of a “trust in numbers” refers to a financial mentality that accords numbers a particular neutrality and objectivity in the operationalisation of political programmes aimed at governing social and economic activities in many different domains (cf. Miller 1990; Rose 1991; Robson 1992; Miller 1994a, 2001; Mennicken & Vollmer 2007; Mennicken et al. 2008). In particular, the idea of translating complex processes of production and exchange into a “single financial figure” (Miller 1994a, 2001) has been referred to in explanations of the close ties between accounting and economic decision-making (Hopwood 1992).<sup>11</sup>

This thesis explains the problematisations of financial reporting numbers as an issue for governing and their translation into regulatory reform projects in the last two decades of the 20<sup>th</sup> century. This is also a study of the conditions which made the rise of a category of non-financial and future-oriented accounting possible as an issue for accounting standard-setters and regulators in the UK during the 1990s. Moreover, what distinguishes this study of the role of accounting in regimes of governing economic life is the attention paid to the interplay between accounting and other forms of ordering, such as law. Studies of the role of accounting in government have so far concentrated on the role of accounting as an element of decentralised regimes of governing which were somewhat distanced from the

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<sup>11</sup> The discussion of accounting numbers in the “pursuit of objectivity” (cf. Porter 1995) in economic governance is further elaborated in the final chapter of this thesis.

administrative apparatus of “the State” (Miller 1990). The mandatory OFR event, however, suggests to explain the role of accounting in governance in relation to the moments in which accounting was caught up in the making of centralised forms of regulation in state-law.

The remainder of this chapter outlines the theoretical, conceptual, and methodological considerations which underlie the study of the moments in which financial reporting numbers were problematised as an issue for governing. This is done in three parts. The next section presents the conceptual implications of studies of accounting and government that have focused on similar destabilising moments of accounting change. It introduces the body of literature which provides the analytical framework for the study of the specific moments of problematising financial reporting numbers and proposing non-financial and future-oriented practices as alternative “accounting solutions” The concepts that are referred to include a perspective on accounting as an element of *governmentality*; ideas of change as processes of *problematizing*; a notion of *arenas* and *constellations* of accounting change; and the concepts of *regulatory space* and *logics of appropriateness*. The third section that follows addresses the “questions of method” regarding the collection and analysis of data that result from the conceptual framework in this research. The section outlines the central role of the study of discourses in analyses of governance reform. In addition, it gives an overview of the sources that have provided the primary empirical data for addressing the questions in this research and outlines the process of the data collection. This chapter ends with an overview of the issues that are addressed in the remaining four chapters of this thesis.

## **2 Destabilising moments**

Studies of accounting and governance have proposed that accounting reform is never complete. This is because new accounting practices, once introduced, seldom achieve full operationalisation of the programmatic aspirations in the name of which they were put forward. This results in further problematisations of existing modes of governing and the perpetual translation of “failures” of accounting into proposals for the “improvement” of accounting practice (Hopwood 1983b; Miller & Rose 1990, p. 10; Hoskin & Macve 1994; Young 1995). Correspondingly, this thesis sees the OFR events as destabilising moments - moments of change in which

the ideas and practices of governing economic life were contested, adjusted, and reinvented.

The study of the rise of non-financial and future-oriented reporting in accounting standard-setting and regulation in the UK in this thesis draws considerably on a small number of writings that describe similar destabilising moments in which the roles and purposes of the financial reporting statements as an issue for governing were called into question. These studies of financial reporting standard-setting and regulation have drawn on multiple concepts and theories from other areas and disciplines, such as sociology and political science, and developed new perspectives on the study of accounting change. For example, they proposed to examine accounting change at the intersection of the wider accounting and non-accounting debates that make their distinct and otherwise disparate concerns self-evident in accounting terms (Burchell et al. 1985; Robson 1991). Furthermore, they suggested that incremental changes in regulation take place when accounting issues come to be seen as problematic and lead to calls for improvements to the financial reporting framework (Young 1994). These studies have also emphasised that what counts as “right” accounting may differ according to the different programmes of governing in whose name financial reporting reform is mobilised (Young 1995). Finally, existing studies of financial reporting standard-setting have proposed that regulatory reform is driven by concerns with the ability of financial statements to provide input into the economic decisions of account users (Young 2006).

Interestingly, these studies of accounting regulation have not suggested a general questioning of financial reporting numbers as a central element in regimes of governing social and economic life. Their analyses of processes of financial reporting change do not indicate doubts about an underlying ability of accounting numbers to provide “facts” (Young 1995). Although the studies by Burchell et al. (1985) and Robson (1991) are also concerned with the introduction of additional accounting reports, the “value added event” in the UK in the 1970s, which they analysed, still attempted to improve financial measures of corporate performance and wealth creation. This study of the OFR events in the UK, however, suggests that the proposals for non-financial and future-oriented reporting co-emerged with problematisations of the roles and purposes of financial reporting numbers as an issue for governing business enterprises and economic life at large. Accordingly,

the accounting change in the OFR events in the UK was not a case of calls for “better” financial representations, but of calls for different accountings.

The observation of a “mistrust in numbers”, therefore, opens up a new set of questions in the study of accounting change. First, how do “new” categories of non-financial and future-oriented accounting emerge? Second, how do they become an issue for regulatory reform in accounting standard-setting and legislation? And, finally, how does this change existing views on the interrelations between accounting and wider ideas of governing businesses and economic life? To address these questions, this research focuses on the particular moments in which accounting numbers have been problematised and non-financial and future-oriented “solutions” were proposed. In doing so, the analysis draws upon a set of interlinked literatures which focus on the interrelations of political programmes and the calculative practices of accounting in the governance of social and economic life.

The remaining paragraphs of this section develop the conceptual approach in this thesis. They outline the benefits and limits of drawing on studies of accounting as an element of *governmentality* and on the analytical constructs of the *accounting constellation*, *regulatory space*, and *logics of appropriateness*.

## 2.1 Accounting and government

The calculative practices of accounting have come to be seen as an intrinsic and constitutive element in the governance of social and economic relations throughout the 20<sup>th</sup> century (Miller 2001; Vollmer 2003).<sup>12</sup> Studies of accounting and government generally relate to an intellectual movement of the 1970s which expressed growing reservations about Marxist accounts of power and conflict between interest groups and “the State” as the central element in public policy making (Krasner 1978, p. 6; Skocpol 1985, pp. 4 & 7; Hall 1993).<sup>13</sup> As part of this movement, the social sciences and policy makers increasingly described “the State” as a heterogeneous actor, that was made up of dispersed social networks, which

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<sup>12</sup> The works of Weber (1978) already proposed a central role for the monetary practices of “capital accounting” in the rise of capitalism. Recent writings in the area of economic sociology have emphasised a *performativity* of calculating practices in constituting “the economy” (cf. Callon 1998; Mackenzie et al. 2007).

<sup>13</sup> The term “policy” is used in this research in its broadest definition as “the objectives and practices of any agent in the economic sphere” that “are articulated and made operable through particular calculative practices” (Miller 1994b, p. 13). “Public policy” in this research will be referred to in a narrower sense as Governmental policy.



replaced “realist” perceptions of a relative power-monopoly of regulatory authorities (Foucault 1976, p. 123).<sup>14</sup> From that point of view, “the State” only indirectly shapes political and social processes while it is at the same time constituted and influenced by them (cf. Skocpol 1985; Foucault 1991b; Rose & Miller 1992; Hall 1993; Hunt 1997; Wickham 2006). As Burchell et. al. (1991, p. x) suggest:

*“[G]overnment is not just a power needing to be tamed or an authority needing to be legitimized. It is an activity and an art which concerns all and which touches each.”*

The departure from Marxist perceptions of “the State” as a “unitary agent” (Hunt 1992) was among other things reflected in an emerging scholarly body of studies of *governmentality* (cf. Foucault 1991a). They propose a view of “the State” as a “mythicized abstraction” (ibid., p. 103) whose powers to govern “the wealth, health and happiness of populations” (Rose & Miller 1992) are widely dispersed in “governance networks”. These networks consist of complex and fluid associations between multiple political entities and practices which rise above a dichotomy between “State” and “civil-society” (cf. Miller 1990; Miller & Rose 1990; Foucault 1991a; Rose & Miller 1992; Miller & Rose 2008a). Nevertheless, the notion of “governance” maintains the assumption that the “real” is programmable and “can be acted upon and improved by authorities” in the name of higher ends (Rose & Miller 1992, p. 183; Miller 2001).<sup>15</sup> Accordingly, it has been proposed that:

*“As with government, we find a conviction that there exists a calculable answer to the problems of the enterprise and even of social life.” (Miller 1994a)*

To describe the networks that attempt to act upon social and economic activities, analyses of *governmentality* suggest a focus on the historically and spatially specific *rationalities, programmes, and technologies* of government. Highly abstracted

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<sup>14</sup> Foucault interpreted the powers that govern behaviour in modern society as widely dispersed “micro-powers” that align and realign in specific moments (Foucault 1980b, 1981; Hunt 1994, p. 18).

<sup>15</sup> In this research, the terms “governance” and “government” are used interchangeably to refer to any mechanism for steering the conduct of others or oneself (Hunt 1997, p. 116; Pierre & Peters 2000, pp. 1-2). This is consistent with a notion of “regulation” in its widest sense, involving all forms of social control over the actions of individuals, organisations, or society as a whole (Baldwin et al. 1998a). The term “law” is used exclusively in relation to public laws. The capitalised term “Government” is used to refer to the group of persons who hold the principal executive positions in a nation state. In the United Kingdom, they are the Prime Minister and the Cabinet, including the heads of government departments.

*political rationalities* outline the ways of thinking about who governs what and how (Miller 1990; Miller & Rose 1990; Gordon 1991; Miller 1991; Rose & Miller 1992). These “principles of government” (Miller 1990) do not necessarily describe clearly distinguishable historic eras, yet particular vocabularies for describing authority may be shared over longer periods of time. This has allowed the social sciences to identify general families of govern-mentalities. For example, the governing rationales of “liberalism” have been associated with a notion of “the private”. Ideas of “the welfare state” are based on common aspirations to “the social”. Contemporary “neo-liberal” and “advanced liberal” regimes of governing have been linked to an emphasis on “the market” and “ideas of freedom” as the structuring themes of government (Miller & Rose 2008b).

On the issue of how these abstract ideas link to the local activities that they seek to govern, writings in *governmentality* suggest an analytical focus on the more specific *programmes* and *technologies* that make the practices of government possible (Miller 1990; Miller & Rose 1990; Rose & Miller 1992; Miller & Rose 2008b). *Programmes* of government outline particular strategies, claims, and prescriptions, such as getting accounting “right” (Young 1995) or “securing” economic competitiveness within the wider frameworks of political *rationalities*. They are closely linked to notions of *technologies* of government. These refer to the explicit practices and techniques that are expected to help operationalising abstract ideals at the level of local processes and activities (Miller 1990; Miller & Rose 1990; Miller 1991).

*“[T]echnologies of government seek to translate thought into the domain of reality, and to establish ‘in the world of persons and things’ spaces and devices for acting upon those entities of which they dream and scheme.” (Miller & Rose 1990)*

The argument that government is at the same time technical and ideological is consistent with studies of accounting as a social and institutional practice (cf. Hopwood 1983b; Hopwood & Miller 1994; Napier 2006). These studies are built on the idea that accounting is “much more than an isolated technical endeavour” but “imbued with an ever expanding set of purposes” (Hopwood 1992) that define the

roles of accounting “in the context in which it operates” (Hopwood 1983b).<sup>16</sup> This links the study of government to the study of accounting. Programmes of governing “at a distance” (cf. Latour 1987) in widely dispersed governance networks have placed particular weight on mechanisms of information gathering and devices of inscription:

*“Recording, counting, tabulating, calculating, comparing have become both the means by which governmental intervention expands and one of its chief by-products.” (Hunt 1994, p. 27)*

The calculative practices of accounting in particular have been ascribed a key role in rendering the objects of economic government visible and comparable to norms and standards of social and economic behaviour. By elaborating the calculative techniques of accounting in terms of a political language of, for instance, “economic efficiency” (Hopwood 1992), “modernising society” (Miller & Rose 1990), or “order and commerce” (Miller 1990), accounting practices become a translation mechanism between highly abstract policy programmes and the activities of individuals and organisations.<sup>17</sup> This means that, on the one hand, accounting allows the recorded activities to be seen in terms of these abstract notions. On the other hand, accounting representations create possibilities for direct modes of monitoring and intervening by others or through indirect modes of self-control and self-governance (Miller 1990; Miller & Rose 1990; Miller 1991; Miller & Power 1992; Rose & Miller 1992; Miller 1994a; Rose 1999, p. 153; Miller 2001).

Above all, the language of “neoliberalism” has been associated with regimes of governing that are only loosely connected to modes of formal intervention by the executives and bureaucracies of national Governments (Miller & Rose 1990, p. 1).<sup>18</sup> Related studies of the relationship between neoliberal modes of economic management and accounting suggest a conceptual interconnection of accounting and “the economy” (Miller 1990; Hopwood 1992). The “transformative capacities” of accounting in regulation, therefore, rest on the idea that processes of information

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<sup>16</sup> Similarly, Hacking points at the idea that new ways of categorising accounting do not emerge in a social and historic vacuum (Hacking 1986, p. 233).

<sup>17</sup> The emergence of accounting and “the State” as “mutually supportive sets of practices” is not a new phenomenon in modern capitalist societies but has already been shown for the period of Louis XIV (Miller 1990, p. 332).

<sup>18</sup> Power (1994; 1997) presents a related discussion on the rise of audit in regimes of governing that emphasise self-regulation, performance standards and accountability (cf. BRTF 1999, 2000).

gathering, recording, and reporting have the potential to shape decision-making in the name of more abstract ideas of “efficiency” and “effectiveness” even without the direct interventions of a governing authority (Miller 1990; Miller & Rose 1990; Rose 1991; Rose & Miller 1992; Miller & O’Leary 1993; Miller 1998a; Rose 1999, p. 153). That is, accounting practices are expected to contribute to the transformation of individuals into economic “decision makers” by translating policy programmes into presumably neutral indicators of economic performance that facilitate “rational” decision-making for actors inside and outside the organisation (Hopwood 1983a; Miller 1990, 2001). In addition, studies of the role of accounting in neoliberal governance have proposed a de-politicising role for accounting knowledge (and in a wider sense the formal human sciences) in connecting the local sites of economic activity to the programmatic ideals of government. Accounting has been understood as offering a particular form of objectivity that translates the inherently political interests of authorities into seemingly apolitical “scientific-technical” terms (Miller & Rose 1990; Rose 1991).<sup>19</sup> Accordingly, accounting numbers have been described as a means to “tame” the political power of authorities. That is, claims to decision making on the basis of accounting information assign interventions in the activities of individuals and organisations an aura of acting according to neutral and objective decision models (Rose 1999p. 153).

## 2.2 Processes of problematising

Studies of *governmentality* have proposed a particular focus on the situations “in which governing is called into question” (Dean 1999, p. 27) in order to explain how new regimes of governing emerge. This shifts the analytical focus from the study of programmes, technologies, and rationalities that constitute a particular regime of governing to a study of the processes in which abstract macro-level programmes and specific micro-level practices become linked and mobilise each other in processes of governance reform (cf. Miller 1990; Miller & Rose 2008a). Furthermore, studies of accounting and governance have drawn on the concepts of *translation* (cf. Miller 1991; Robson 1991) and *problematisation* (cf. Miller 1991; Rose & Miller 1992; Miller 1998a) to analyse accounting change in terms of the

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<sup>19</sup> For further discussion of the political powers of numbers, see Rose (1991; 1999, p.197) or Hopwood (1992).

processes in which multiple and diverse “problems” of government begin to be linked to accounting.

*“Frequently, these alleged problems have nothing immediately or self-evidently to do with accounting. But, with some guidance, people can often be helped or persuaded to recognize hitherto unintended connections [...]” (Miller 1998b, p. 607)*

Although the related writings on actor-network theory (ANT) in science and technology studies (STS) have not been explicitly referred to in this research (cf. Callon 1980; Callon & Law 1982; Latour 1987; Law 1992; Callon 1999; Law 1999), a focus on the moments of *translation* and *problematization* (cf. Callon 1980; Callon 1999) gives a sense about emphasising processes rather than structure in the interrelations between human and non-human actors (Law 1992).

Accordingly this thesis interprets the emergence of fundamental doubts about ideas of governing through financial reporting numbers as destabilising moments – points in time in which “problems” with governing emerged and were translated into calls for new accounting practices and techniques. This leads this thesis to examine the multiple events and processes that gave rise to significant doubts about the neutrality and objectivity of financial reporting representations of the economic reality of business enterprises. The analysis includes the *processes* of *translation* and *problematization* that make the emergence of links between high-level ideas of governing and non-financial and future-oriented accounting possible. However, a focus on the destabilising moments of government does not explain how programmes and technologies of governing emerge in the first place. To address the question how a category of non-financial and future-oriented reporting and the problems of government it was supposed to solve emerged during the OFR events, this study referred to the concept of the *accounting constellation* as introduced by Burchell et al. (1985).

### **2.3 Accounting constellations**

Starting from the view that accounting issues are “not simply there” (Young 1994) but have themselves a history of increasingly being seen as “accounting”, the concept of the *accounting constellation* helped to study the rise of new ways of reasoning and categorising accounting within a programmatic language of government. The concept is based on the idea that accounting changes within a

historically and spatially specific interplay of accounting and non-accounting *arenas* of discourse which come to express their distinct and otherwise disparate concerns in accounting terms.<sup>20</sup> Thinking about accounting change in terms of *arenas* and *constellations* directs this study to the multiple events, bodies of knowledge, institutions, and practices that create possibilities for new ways of reasoning and categorising the rationales and practices that come to be seen as “accounting” (Miller & Napier 1993).

*“For what we call ‘accounting’ is an entity that has been made up out of techniques and practices drawn from diverse disciplines and domains. Accounting changes in both content and form over time, only ever achieving a temporary stability.” (Miller 1994b)*

However, similar to a notion of problematisation in the study of accounting in regimes of governing, the problem discourses which give rise to new ways of reasoning and categorising accounting are understood to be “something relatively rare” (Dean 1999, p. 27).

*“[Problematisations] have particular dates and places, and occur at particular locales or within specific institutions or organizations.” (Dean 1999, p. 27)*

Accordingly, *accounting constellations* are understood to emerge largely haphazardly out of the actions of a number of different actors, who seek different things when relating their distinct concerns to accounting (Miller 1991). Robson (1991, p. 552) also calls the arenas “demarcated field[s] of problems”, which may share an accounting issue as a common point of reference. Accordingly, an *accounting constellation* is created when they start linking – intendedly or unintendedly – the particular “problems” of their own arena to perceived failures of accounting.<sup>21</sup>

The use of the concept of the *accounting constellation* has three implications for this research. First, the analytical perspective on the historically specific constellations of accounting change helps to unravel the multiple events that gave

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<sup>20</sup> The idea that accounting becomes a shared element in expressing the expectations and ideals of diverse actors, agencies, or bodies of knowledge is conceptually similar to the idea of “boundary objects” as presented in science and technology studies (Star & Griesemer 1989).

<sup>21</sup> The concept of the *accounting constellation* is similar to the notion of an *accounting complex*, in which accounting becomes part of broader discourses in other bodies of knowledge (Miller 1986).

rise to a category of non-financial and future-oriented accounting at a specific moment in the late 1980s. Second, it is consistent with the proposed focus on the destabilising moments in which accounting and government are problematised. Ideas of translation and problematisation between the *arenas* of accounting change shift the empirical focus from a study of the wider arenas that get linked to the processes in which a programmatic language of “problematics of government” reframes certain practices and ideas as “accounting solutions” (Miller 1991; Robson 1991). Third, this focus on the emergence of links between programmes and technologies in constellations of accounting and non-accounting debates points at the reflexivity and constitutive capacities of accounting change (cf. Burchell et al. 1980). It allows to study how the emergence of a category of non-financial and future-oriented accounting created possibilities for reshaping and expanding “the terms of political debate” (Rose 1999, p. 277).

#### **2.4 Regulatory spaces and logics of appropriateness**

The study of change at “the margins of accounting” also means to recognise that problematisations of accounting may be advanced from within the discipline of accounting, but also by non-accounting actors from other disciplines, such as economics or law (Miller 1998a). The concept of *regulatory space* (cf. Hancher & Moran 1989b) emphasises more explicitly the multiple actors and ideas that mobilise a technical language of accounting in attempts to intervene in economic activities by means of accounting regulation and standard-setting. Similar to the *accounting constellation*, the concept of *regulatory space* stresses the social and political elements of change. It suggests that the “experience of regulation” is framed by the political, legal, and cultural factors that define the scope of issues that become subject to regulatory debate in a community (Hancher & Moran 1989b; Scott 2001). The original concept as introduced by Hancher and Moran (1989b) places particular weight on processes of bargaining between large and powerful organisations and the interplay of state and non-state actors in regulatory change. In particular, a strand of socio-legal literature in law and studies in political science have drawn on *regulatory space* when analysing power-struggles over the regulation of social and economic activities (Black 1997; Hall et al. 2000; Scott 2001; Lange 2003; Lodge 2003; Thatcher 2008). Their analyses of the factors that shape the actors, issues, and power relations in regulatory reform processes have

been closely aligned with ideas of the embeddedness of change in national cultural, political, and institutional environments.<sup>22</sup>

*“Expectations about the purpose of regulation, about who are the legitimate participants and about their relations with each other, are subject to great variations – across historical time, across nations, and between different economic sectors in industries.” (Hancher & Moran 1989a, p. 3-4)*

Accounting research has also examined power relations and institutional environments and the ways in which they play out in *regulatory space*. For example, Sikka (2002) referred to the analytical construct of *regulatory space* to evaluate the formation of the UK Auditing Practices Board (APB) in the interplay of power relations among “the State”, the audit industry, and accounting professionals. Similarly, a study of the formation of the Public Accountant's Council of Ontario stressed the role of multiple actors and ideas in the construction of identity for the new regulatory agency in Canada (MacDonald & Richardson 2004). Recent studies of the dynamics of agenda-setting at the IASB have featured processes of accounting change in *transnational regulatory spaces* (cf. Djelic & Sahlin-Andersson 2006) which an even greater variety of actors may enter and exit over the term of a regulatory debate (Botzem & Quack 2006).<sup>23</sup> In these studies, disputes over the production of “material traces” for organisational activities in accounting terms have been attributed to expected social and “economic consequences” of accounting (cf. Zeff 1978). Control over processes of accounting regulation allows particular actors to define the standards according to which organisations are made “calculable”, visible, and held accountable in the name of abstract programmes of government (Miller & O'Leary 1987; Miller & O'Leary 1994).

This research also draws upon the concept of *regulatory space* to emphasise the situational and relational nature of the processes of contest and agreement among a multiplicity of actors and agencies over the “the proper ends and means of

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<sup>22</sup> A concept closely related to notions of institutionalised environments and power relations in *regulatory space* is that of the *organisational field* in which “conceptions of control” outline the scope of organisational activity (cf. Fligstein 1990; Fligstein 2001).

<sup>23</sup> A notion of “soft actors” further captures the idea that the identity of the participants in *regulatory space* is “always somewhat blurred” (Djelic & Sahlin-Andersson 2006)



government” (Miller & Rose 1990, p. 5).<sup>24</sup> This means that the powers to intervene in the production of accounts of economic activities are not limited to the regulatory agencies that are formally responsible for the administration of the processes of accounting standard-setting and regulation, such as the ASB or the DTI in the UK (ibid.). This thesis, however, does not explicitly analyse the power relations between the individual actors in *regulatory space*. Instead, it aligns the study of accounting change with a focus on the emergence of links between programmes and technologies of government in processes of regulatory reform. References to the concept of *regulatory space* help to outline the “specific problem space” (Rose & Miller 1992, p. 182) in which accounting and the sphere of governing connect. This puts greater weight on the study of ideas rather than particular organisations in creating possibilities for regulatory reform and the emergence of particular regulatory “solutions” at specific moments in history.

Not a lot of accounting research has addressed the question of how high-level ideas of governing make change in financial accounting standard-setting and regulation possible. Studies of the agenda-setting at the FASB in the US have emphasised the “uneasy position” of decision making at the FASB within a wider social and institutional context (Young 1994, 1996). Young (1994) also introduced a notion of *logics of appropriateness* (cf. March & Olsen 1989) to explain the actions (and inactions) of actors within the regulatory space.<sup>25</sup> The concept generally replaces anticipatory and consequential explanations of decision making with a focus on the roles actors play in a particular social context (ibid., pp. 160-161). For the situation of agenda-setting, a notion of *logics of appropriateness* implies that a regulator will take an issue on its agenda if it meets the expectations about the role and purpose of the regulator in dealing with a particular “accounting problem” (Young 1994). Accordingly, self-interested behaviour in regulatory agenda setting is not entirely obviated, but it will be limited to situations where it is consistent with expectations of other actors in *regulatory space* (ibid.).

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<sup>24</sup> Although not explicitly discussed in this research, ideas from ANT on the linkages between human and non-human actors and the role they play within an elaborate network (Latour 1986; Callon 1998) might further help answering the question for the assemblage of actors and issues in events of accounting regulation for specific situations.

<sup>25</sup> For a discussion of *logics of appropriateness* in organisational action, see, e.g. Czarniawska & Sevón (1996), or Lounsbury (2007) on the interplay of multiple rationalities in processes of change in organisational fields.

A small number of accounting studies has employed the concept to study the efforts of standard-setters in constructing authority for their activities. These studies observe consistency between the activities of the standard-setter with wider social and institutional factors in seeking to secure the survival of the organisation (Sikka 2002; Young 2003; MacDonald & Richardson 2004).<sup>26</sup> This research interprets *logics of appropriateness* as inherently programmatic elements in the construction of temporary stability and legitimacy of regulatory issues on the agenda of accounting regulators and standard-setters. In line with the observation that much accounting change has been driven by ideas of “getting the accounting right” in the construction of a regulatory mandate for the FASB in the US (Young 1994, 1995, 2003), this research highlights the situational and relational emergence of *logics of appropriateness* in the interplay of wider ideas of governing that outline the different demands that are placed on the role and mandate of the regulatory body.

Overall, the analytical approaches that are referred to in this research step beyond notions of “the micro” and “the macro” in the study of the relations between accounting, regulation, and wider ideas about the means and ends of seeking to govern economic life. Furthermore, they emphasise the multiple processes and encounters between the many actors, issues, and ideas of governing that constitute the destabilising moments in which accounting, regulation, and the ideas of governing economic life are put into question. This has further implications for the collection and analysis of empirical data in this research which will be discussed in the next section.

### 3 “Questions of Method”

Studies of accounting and governance do not provide a closed theory or systematic mode of analysis for the study of changes in accounting regulation. Instead, they draw on concepts and approaches from many different areas and disciplines, such as the writings by Michel Foucault, social studies of science, ideas from economic history, economic sociology, or the sociology of the professions (cf. Miller & Rose 2008a). These approaches share, at most, an interest in discursive processes of

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<sup>26</sup> Their perspective on the ways in which individual and collective frames of reference affect what is perceived as “rational” in the construction of regulatory problems and solutions is consistent with ideas of *bounded rationality* (cf. Simon 1957) and *institutional thinking* (cf. Douglas 1987). The latter emphasises that individuals refer to shared expectations and knowledge in individual thinking, which makes it ultimately a social activity (ibid.).

*problematizing*, in which the use of a specific language and vocabulary establishes the issues that “need” governing (Miller & Rose 2008b). The data collection and analysis in this research draws upon *Foucauldian* notions of the discursive nature of governance and calculation (Foucault 1991c). The “questions of method” (cf. Foucault 1991d) which are associated with the work of Foucault are generally interested in the production of power and meaning in the historically specific language of regulation of conduct (Hall 1997). Foucault (1976, p. 133) describes discourses (and silence) as the instrument and the outcome of power – in this case the power to govern – but also as the representation of resistance and opposition in power relationships. However, as mentioned earlier, this research is less concerned with analyses of power relations than with the ways a programmatic and technological vocabulary of governing emerges in the local language of specific instances of regulatory reform. The work of Foucault provides a general methodological reference point which focuses this research on the idea that regulatory change is largely about the operation of thought within social and political practices (Dean 1999, pp. 17-18). Accordingly, the data collection and analysis has been guided by references to Foucauldian ideas of *eventalisation* (cf. Veyne 1979b; Foucault 1991d), *genealogy* (cf. Foucault 1980a; Miller & Napier 1993), and the discursive nature of governance and calculation (Hacking 1986; Foucault 1991c). These concepts stress the role of a historically specific language in constituting the singularity of events. The term *genealogy* signals the departure from the search for causalities that has been associated with historical analyses.

*“Genealogy, consequently, requires patience and a knowledge of details and it depends on a vast accumulation of source material.”  
(Foucault 1980a, p. 140)*

References to a notion of *eventalisation* meant to trace the multiple branches of historical developments and unintended encounters that give rise to new practices. This focus on the singularity of events and their genealogy is, therefore, different from a historic perspective on the “origins” of practices and ideas as the outcome of evolutionary processes in response to contextual conditions (Foucault 1980a, p. 140; Miller & Napier 1993). It constantly re-focuses the analysis in this study on the local processes and interactions that make single events possible (cf. Veyne 1979b). At the same time, these single events have the potential to change “what

subsequently counts as being self-evident, universal and necessary.” (Foucault 1991d, p. 76).

### 3.1 Governance reform as discourse

The view that the destabilising moments of accounting change are largely constituted by processes of translation and problematisation in which different accounting and non-accounting arenas begin to express their distinct and otherwise disparate concerns in accounting terms has further implications for the methodological approach in this research. It leads this study of the OFR events in the UK to focus on the discursive processes of constructing financial reporting practices as “problems” of economic governance and the presentation of non-financial and future-oriented measurement and reporting as possible accounting “solutions”. According to the view that “to govern is to act under a certain description” (Rose 1999, p. 28), language in this research is understood to make government and regulatory change possible.<sup>27</sup> That is, when new categories for describing the means, objects and objectives of government emerge, they also create new possibilities for acting and intervening in the conduct of others or oneself (Hacking 1986; Rose 1999, p. 19). In other words:

*“[I]t is through language that governmental fields are composed, rendered thinkable and manageable.” (Miller & Rose 1990, pp. 6 & 7)*

This implies that the study of regulatory discourse is more than an analysis of mere rhetoric or of neutral reflections on what has been stated elsewhere (Carabine 2001, p. 275). The vocabulary that is used when developing or reforming regulatory regimes frames possibilities for action (cf. Hacking 1986) by making the programmes, technologies, problems and solutions of government intelligible.<sup>28</sup> This suggests that studies of regimes of governing should be undertaken through an analysis of the ways in which a language of highly abstract political rationalities frames the “discursive fields” (Rose & Miller 1992, p. 175) for “intelligible contestation” (Rose 1999, p. 28) about the objects and objectives of government.

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<sup>27</sup> For further discussion of narratives in social science research, see Czarniawska (1997; 2004).

<sup>28</sup> For a discussion of framing possibilities for action through language in governance reform, see, Rose (1999, pp. 28-30), Miller and Rose (1990), or Rose and Miller (1992).

*“Language here serves as a ‘translation mechanism’ between the general and the particular, establishing a kind of identity or mutuality between political rationalities and regulatory aspirations. [...] as well as establishing the place of certain objects and problems within the legitimate obligations and power of rulers [regulators], and enabling them to be formulated programmatically [...]” (Miller & Rose 1990, pp. 6 & 7)*

Although broad families of “governmentalities” may be identified in the language of “liberalism”, “welfare”, or “neoliberalism”, the study of language in this research is mainly concerned with the vocabularies of government that emerge in relation to very specific events of regulatory change. This helps to address the question of how specific networks of reform actors began to see financial reporting numbers as a “problem” of governance. It also tackles why reform actors simultaneously come to agree that ideas of non-financial and future-oriented accounting provided a “solution” at a certain point in time without presupposing any larger or underlying rationality of change.

Although this research is not a study of actor-networks in the sense of ANT (cf. Callon 1980; Callon & Law 1982; Latour 1987; Callon 1999), the proposed focus on the processes of *translation* helps to think about, firstly, the different forums in which accounting change may take place and, secondly, raises awareness of the different actors that may become involved in regulatory change. To unravel the moments in which a status quo of governing gets problematised, these studies have focused the analysis of change on the processes in which particular problems move from one person, place, or arena to another and, thereby, draw in different actors and ideas around a shared issue. They lead this research to understand that new ideas and vocabularies of governing may be carried from one place to another by human and non-human actors, such as academic texts, government publications or professional magazines (Miller 1991). However, the methodological implications of ANT would only suggest to “follow” these human and non-human actors and actants (Law 1992; Latour 2004), but they do not address the role of programmatic issues in these networks. This research, therefore, takes a wider focus on discursive representations of political rationalities, programmes, and technologies in the interactions between discursive fields (cf. Robson 1991). This kind of analysis becomes possible through the study of the rationalising language of the persons and documents that come to interact in governance reform spaces at certain moments in

history. Accordingly, the data collection and analysis in this study focuses on the articulations of the roles and purposes of financial reporting in relation to wider programmatic ideas about the governance of economic life.

In addition, each of the conceptual approaches has specific methodological implications for the study of discourses in this research. Although the vocabularies of government may be very specific for the relational networks in which they emerge (Carabine 2001, p. 275), this research suggests that they may point to a more global re-conceptualisations of accounting and the governance of business enterprises and economic life. The study assumes that the rise of a category of non-financial and future-oriented accounting rests upon a vocabulary that attributes it with a range of wider meanings and political ideals (Hopwood 1983b; Miller 1990; Miller et al. 1991; Hopwood 1992; Miller & Napier 1993; Miller 1994b). The analysis of the different elements of policy discourse which intersect in an intended or unintended manner in a particular *accounting constellation* helps to unpack the wider demands in whose name new accounting practices are constructed and mobilised in governance reform programmes. However, it is important to understand that the arenas of accounting change are themselves constituted to a large extent by forms of reasoning and categorising that cannot clearly be compartmentalised. Arenas may generally be conceptualised as “bodies of expertise that depend upon systematised conceptual and discursive schemas” (Miller & Power 1992). This implies looking for the particular discourses that share common “concepts, categories, and rhetoric of the discourse” when trying to define the arenas of accounting change (Robson 1991, p. 552). Similarly, the categorisation of *logics of appropriateness* rests on the assumption that ideas about what is “appropriate” and what is not emerges from the communications among the actors in a regulatory space. From that point of view, not only the language of the regulatory agency itself (cf. Young 2003) but also that of other actors in the field outlines the “appropriateness” of regulatory issues and the role and responsibility of a regulatory body in dealing with it.

In line with the approach proposed by Robson (1991), the data analysis in this study starts from tracing the programmatic elaborations of non-financial and future-oriented accounting as an issue for governing in the empirical materials. Accordingly, the data collection and analysis is concerned with the ways in which

language constructed the historically specific “problem spaces” (Rose & Miller 1992) that establish non-financial and future-oriented accounting as an issue for regulatory reform by “the State”. The review of the materials follows an iterative approach. The data is revisited several times to check if certain patterns emerge from the debates.

However, the interpretation of the accounts of the reform actors within the conceptual framework of this study poses a particular challenge in this research. *Ex post* explanations of regulatory reform tend to represent change as an apolitical, technical response to otherwise changing conditions of production and exchange in the search for progress and improvement (Miller 1991; Garsten & Jacobsson 2007); even though the underlying processes of their construction may “be anything but technical” (Brunsson & Jacobsson 2000a). References to accounting and disclosure often seemed instrumental and strongly influenced by normative conceptions about principal-agent relationships and transactions-costs (cf. Villiers 2006).<sup>29</sup> The analysis in this thesis, therefore, remains critical about taking the discursive rationalisations of events and decisions as representations of an underlying “reality” (Colebatch 1989; MacDonald & Richardson 2004). It interprets the verbal and written accounts of the events in this study as part of the distinct vocabulary of a specific *regulatory space* which created possibilities for the construction of “accounting problems” and “solutions”. In order to support and illustrate the findings and conclusions in this research, the discussions of the empirical materials in chapters two, three, and four make large use of selected quotes.

### **3.2 Data sources and collection**

Concerning the collection of empirical data, this study understands that the historic-specific language of problematising accounting in governance becomes visible in academic, professional, governmental, or inter-governmental texts and publications (Miller 1991). A “mistrust in numbers” in the problematisations of financial reporting in existing modes of governing is, therefore, studied on the basis of a wide range of empirical materials. They include the published and unpublished documents and other accounts of events that relate to, first, the rise of a category of

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<sup>29</sup> For further discussion of economic accounts of disclosure regulation see also Leftwich (1980), Beaver (1998), and Healy & Palepu (2001).

non-financial and future-oriented accounting in British accounting reform-debates in the UK from the late-1980s onwards.

A large albeit never complete amount of data has been collected over the term of this study. The primary data in this research consists of the published and unpublished documents and reports that were prepared as part of calls for financial reforms “beyond the numbers”. Furthermore, this research draws on written and personal ex-post accounts of key persons who participated in the reform processes. The documents which were publicly available were either ordered from the regulatory organisations or accessed through libraries or on the internet. Internal written documentations of the agenda-setting debates during the CLR were obtained directly from the DTI (and later the BERR) during several on-site visits in the summer of 2006 and 2007.<sup>30</sup> For a chronological overview of the key reports and discussion papers that have been reviewed for this study, see appendix 2 in this thesis.

In addition, 15 semi-structured research interviews were conducted between January 2005 and January 2008. The interview partners were selected according to the degree of their involvement in the relevant accounting reform debates. The difficulty in drawing from a very small pool of specific people whose schedules were oftentimes tight meant that the collection of interview data was constrained. For each interview, a list of open-ended interview questions was prepared in advance. They covered the personal experience of the interviewee with the events under scrutiny and asked for their point of view on key events, points of conflict, and the role of particular ideas, individuals, or organisation in shaping the regulatory debates. The interviews lasted between 15 and 90 minutes. Eleven interviews were digitally recorded. Eight were fully and three partly transcribed by the author. Where recording was not possible, minutes were prepared from memory and on the basis of detailed notes on the same day of the interview. Copies of six transcripts have been sent to the respective interviewees. Four returned a revised version of the transcript by e-mail. For a list of interviewees and further details, see appendix 3 in this thesis.

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<sup>30</sup> The DTI was replaced by the Department for Business Enterprise and Regulatory Reform (BERR) in July 2007. Its predecessor until 1970 was the Board of Trade (BERR 2007b). The BERR has been merged into the new Department for Business, Innovation and Skills (BIS) in June 2009 (BERR 2009).



The remaining paragraphs of this section summarise the key data sources that have been used to study the emergence of a category of non-financial and future-oriented accounting, the voluntary OFR project at the ASB, and the introduction of the mandatory OFR during the CLR. The structured collection of empirical data was further broadened by tracing further references from the core materials or as indicated by interview partners. The author ceased to collect further material and to conduct further interviews once they failed to provide any more insights into the British accounting reform debates.<sup>31</sup> In order to remain within the scope of this thesis, other narrative reporting initiatives which were not directly linked to the OFR projects in the UK were excluded from the analysis.

The study of the arenas of accounting change in this thesis rests on an in-depth analysis of policy proposals for accounting reform in the mid 1970s, in the late 1980s, and in the mid 1990s. The data consists *inter alia* of a series of research reports and discussion papers that provided some of the key arguments for the launch of the voluntary OFR project at the ASB and the mandatory OFR project during the CLR. They were identified by tracing back references from documents that have been prepared as part of the regulatory reform processes or following the recommendations of interview partners. The documents that directly preceded the explicit initiatives for regulating supplementary reporting in a voluntary and later a mandatory OFR in accounting standard-setting and company law date back to 1988. The study *Making Corporate Reports Valuable* (McMonnies 1988) marked a starting point for the financial reporting reform debates which followed throughout the 1990s. The review of debates relating to the publication of the discussion paper *The Corporate Report* (ASSC 1975) helped to better understand the points of difference between post 1988 calls for accounting reform and those which preceded them. To remain within the scope of this thesis, the reviews of secondary sources are limited to a review of those debates in the general management literature and in accounting research that directly connect to problematisations of financial reporting numbers and ideas of non-financial and future-oriented accounting.

The analysis of the agenda-setting process for a voluntary OFR draws on documents that outlined a role for the ASB in the regulation of non-financial and

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<sup>31</sup> For a further reflection on the data collection and analysis in this research, see chapter five.

future-oriented reporting. The policy of the ASB to hold its meetings behind closed doors (Turley 1992) and the confidential treatment of meeting minutes, however, limited the data collection to publicly available documents, including the reports and discussion papers from the Financial Reporting Council (FRC) and the ASB between 1991 and 1993 (ASB 1991; FRC 1991; ASB 1992, 1993). A hard copy of 102 out of in total 104 responses to the ASB's invitation for public comment in the 1992 discussion paper was obtained directly from the ASB.<sup>32</sup> However, the somewhat limited insight into the internal work of the ASB constrains a discussion of the points of conflict and agreement about the macro-ideas of governing within the internal debates. Therefore, this research interprets the *OFR Discussion Paper* (ASB 1992) and the *OFR Statement* (ASB 1993) as representing the consensus that had been found between the diverse members of the ASB and other external contributors. The degree to which individual responses were taken into account in the agenda-setting debates, therefore, remains unclear. The document analysis in chapter three is complemented by interviews and written communications with the three key members of the original OFR working group at the ASB. To substantiate the findings from the primary sources and the ex-post descriptions, the study draws on additional secondary sources that elaborate the history and context of accounting regulation in the UK in more detail.

The study of the emergence of the OFR on the agenda of the CLR is based on a wide range of archival materials that have been produced in the run-up to the CLR and following its launch. The former set of documents includes the economic policy proposals from the Labour Party in the run-up to the 1997 General Election (Labour Party 1997b, 1997a) and ministerial speeches and official documents and press releases from the DTI. The latter set of documents includes among others the consultation documents published by the DTI (1998b) and the formally independent Company Law Review Steering Group (CLRSG 1999a, 2000b, 2000a) and the *Final Report* to the Government (CLRSG 2001). Other data sources include the unpublished internal working papers of the DTI and the CLRSG, their meeting minutes, and supporting documents that have been prepared by the sub-working groups of the CLRSG or by external parties in commissioned research. They also include the public responses to the consultation or summary statements thereof.

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<sup>32</sup> Two letters were missing in the set of documents that could be obtained from the ASB.

Further insight into the developments under study was gained from short conversations with key members of the CLRSG and representatives of other organisations which were closely involved at conferences and workshops.<sup>33</sup> In addition to these, a review was conducted of related publications by members of the CLRSG prepared during and after their participation in the steering group (Radcliffe et al. 1998; Kelly & Parkinson 2000; Parkinson 2002; Rickford 2002; Davies 2003, 2005).

#### 4 Outline of this research

Each of the following chapters focuses on a different aspect of the rise of non-financial and future-oriented narratives as an issue for accounting standard-setting and regulation in the UK in moments of a severe questioning of financial reporting numbers as a problem for governing.

Chapter two on the process of moving accounting into new territory outlines the co-emergence of non-financial and future-oriented accounting and programmes of governing business and the economy in the UK in different policy forums since the late 1980s. The study of the different *arenas* and *constellations* of accounting change illustrates two aspects of the process of reforming accounting and governance: First, it shows how a “mistrust in numbers” is founded on the expectation that accounting should and could provide information on “economic reality” in a managerial context. Second, the discussion in chapter two illustrates how new ideas about the roles and purposes of accounting in business management create possibilities for co-designing the problems of government that they seek to solve at the same time.

Chapters three and four are concerned with the reconfiguring of UK accounting regulation in *regulatory space*. Chapter three analyses the process of shifting the boundaries of accounting standard-setting in which non-financial and future-oriented reporting emerged as an agenda issue for the ASB in the early-1990s. Attention to the emergence of *logics of appropriateness* helps to explain how

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<sup>33</sup> Major conferences and workshops attended in the conduct of this research were the CriticalEYE “OFR Summit” on 02.11.2005; the ICSA seminar series on non-financial reporting on 26.10.2005 and 06.12.2005; the IoD seminar “Narrative Reporting – The Future?” on 12.12.2005; the ACCA, Tomorrow’s Company, and h<sup>2</sup>glentferm event “The Future of Narrative Reporting” on 28.06.2006; “The Future of Financial Reporting, BAA/ACCA Seminar” on 12.01.2007; and the ICAEW-FRDG Meeting “Narrative Reporting” on 28.02.2007.

multiple ideas of governing gave rise to the voluntary OFR as an agenda-issue for accounting standard-setting. Furthermore, chapter three outlines the indicators for a general re-positioning of the ASB and accounting standard-setting in relation to ideas of governing in the name of “the profession”, “the State”, and “the markets”. Questions of legitimacy and *logics of appropriateness* are also implicit in the study of agenda-setting for a mandatory OFR during the British CLR between 1998 and 2001. Chapter four on the process of realigning law, accounting, and “the State” illustrates the rise of non-financial and future-oriented reporting within a programme for reforming the international competitiveness of the British economy. The analysis of the mandatory OFR event helps to address the wider question how accounting practices connect to “the State”. This provides new insights into the particular role of law in overcoming a state–market dichotomy in the conceptualisation of accounting as an element of governance.

Chapter five pulls together the previous themes and summarises the multiple factors and dimensions of a “mistrust in numbers” in financial reporting change in the UK. It also includes a short reflection upon the variety of literatures and materials that provide the conceptual and empirical basis for this research and outlines the benefits and limits of using an interrelated body of writings on accounting and government in this thesis. Finally, chapter five develops the conceptual implications of a “mistrust in numbers” for thinking about accounting, regulation, and the governance of economic life at large. It proposes that the OFR represents a significant shift in elaborations of the roles and purposes of accounting in governing from a focus on neutrality and objectivity in economic governance to a focus on seeking to reveal the underlying complexity and subjectivity of economic reality.

## MOVING ACCOUNTING INTO NEW TERRITORY

*"The income statements, cash flow, balance sheet, they all show you the raw economic detail and the OFR will have to now tell you what it all means - because accounts are getting too complicated, because the economy is getting complicated."*

*(Standard-setter F)*

### 1 "Mistrust in numbers" as an issue for governing in the UK

This chapter traces the factors and events that made it possible for a category of non-financial and future-oriented accounting to rise and maintain momentum in British policy reform debates since the late 1980s. The rise and fall of similar proposals for extending the scope of financial reporting in the 1970s suggests that non-financial and future-oriented measurement and reporting practices were not always considered part of accounting. The findings from this chapter support the view that accounting categories should not be taken for granted in the study of regulatory reform. They show that widely shared conceptions of the roles and purposes of accounting in the OFR events emerged as part of a wider "strategisation", "marketisation", and "socialisation" of the language of business management and governance throughout the 1980s and 1990s. This chapter also illustrates the multiplicity of voices which were involved in creating momentum for ideas of non-financial and future-oriented reporting in the period preceding the launch of the OFR projects at the ASB and the DTI.

#### 1.1 Rise and fall in the 1970s

A questioning of the "neutral" and "objective" nature of financial reporting numbers has been part of calls for financial reporting reform at least since the formation of the first British accounting standard setting body in 1970.<sup>1</sup> The purpose of the standardisation programmes of the Accounting Standards Steering

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<sup>1</sup> For further discussion of the history of the regulation of accounting practice in the UK, see chapter three.

Committee (ASSC) was to overcome the use of many alternative approaches to the measurement and presentation of economic activities and resources in accounting practice (cf. Stamp & Marley 1970). The possibility to produce accounting numbers in different ways was formally acknowledged with the publication of the *Statement of Standard Accounting Practice 2: Disclosure of Accounting Policies* in 1971.<sup>2</sup> After the publication of *SSAP 2*, the work of the ASSC continued to focus on:

*“[T]he task of narrowing the areas of difference and variety in accounting practices and establishing objective standards of financial reporting [...]” (ASSC 1975, p.7)*

The publication of the discussion paper *The Corporate Report* (ASSC 1975) marked the starting point for an intended “major review of the users, purposes and methods of modern financial reporting” by the British accounting institutes (ibid., p. 7).<sup>3</sup> It was prepared by a working party comprising eleven members, including the chairman and the technical director of the ICAEW, audit firm partners, financial managers, and one academic – working on behalf of the ASSC over a term of eight months starting in October 1974. The working party set out to re-examine the fundamental purposes of financial reports “in the context of existing and probable future legal and social requirements” (ibid., para. 0.9). The project team recognised that the published annual reports of UK companies mainly complied with the minimum legal requirements for the provision of the financial statements (ibid., paras. 4.3-4.6). Nevertheless, it concluded that presenting “a rounded picture of economic activities” (ibid., para. 0.5) required “putting profit into proper perspective” (ibid., para. 6.7).

*“The reporting of profit and loss and balance sheet figures only will be insufficient to impart a comprehensive picture of economic activities. Additional information and statements are needed which will assist the understanding of financial statements and reveal more fully how resources have been utilised.” (ASSC 1975, para. 6.3)*

These conclusions marked “quite a radical development” for their time (Rutherford 2007, p. 109). The call for reform was part of a fundamentally new way of looking

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<sup>2</sup> SSAP2 was superseded by Financial Reporting Standard (FRS) 18 *Accounting Policies* in 2000.

<sup>3</sup> The discussion paper was produced on behalf the ASSC/ ICAEW in association with the Institute of Chartered Accountants of Scotland (ICAS), the Institute of Chartered Accountants in Ireland (ICAI), the Association of Certified Accountants (ACA), the Institute of Cost and Management Accountants (ICMA), and the Chartered Institute of Public Finance and Accountancy (CIPFA).

at the roles and purposes of financial reports in terms of their “usefulness”. For example, the previously dominant concept of “distributable profit” as a measure of business performance was rejected as the only legitimate indicator of *true and fair* view of “economic value” (ASSC 1975, paras. 4.29-4.30; Gilmore & Willmott 1992).<sup>4</sup> To meet the objective of “usefulness”, the corporate report *inter alia* proposed the inclusion of additional statements in the annual report on issues such as value added, future prospects, corporate objectives, or strategic targets (ASSC 1975, para. 6.5). The discussion paper also encouraged descriptive and interpretive chairman statements on corporate activities to explain and supplement the information in the financial statements (*ibid.*, para. 6.54).

Ideas of complementing financial reporting with additional statements also surfaced in public policy proposals for reforming company law (DTI 1973). The publication *The Future of Company Reports* by the Department of Trade (1977a) explicitly referred to the suggestions from the ASSC when it proposed to introduce a mandatory value added-statement. However, the law reform proposals never made it into statute. According to other studies of these debates, this was due to a lack of parliamentary time before the change of Government in the 1979 general election (Burchell et al. 1985, p. 110; Woodward 2004; Rutherford 2007).<sup>5</sup> In addition, the inflation crisis of the mid 1970s had shifted momentum in the spheres of professional and public accounting regulation from a focus on supplementary financial reports back to increased concerns with financial reporting numbers (Standard-setter F).<sup>6</sup> An article in *The Accountant's Magazine* considered the issue as follows:

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<sup>4</sup> The phrase *true and fair* was introduced with the Companies Act 1948 in order to focus compliance on the spirit of the law and not merely the letter. The ways in which *true and fair* were interpreted seem to have shifted over time from the unbiased presentation of historic cost to an emphasis on concepts of economic value (Gilmore & Willmott 1992).

<sup>5</sup> For a detailed discussion of the rise and fall of the value added-statement on the additional wealth created by the company and its employees in the UK, see Burchell et al. (1985).

<sup>6</sup> Other authors interpreted that change of focus as a response to political threats to deprive the accounting profession of its self-regulatory privileges, if they did not react appropriately to a series of misrepresentations in public audited accounts (Sikka & Willmott 1995).

*“[A] good case can be made for broadening the scope of the corporate reporting. There are, however, many problems to be overcome in the presentation of the current corporate report, and consequently, there may be an equally strong case for priority being given to the improvement of the reporting accountant’s present methods of communication.” (Tweedie 1975)*

For another decade or so, reform in British financial reporting standard-setting remained preoccupied with ideas of “improving” economic representations in financial reporting numbers. The solutions proposed in these reform debates largely focused on changing the techniques for recognition and measurement of the reporting items in the financial statements. Especially the development of metrics for inflation accounting and profit measurement remained high on the agenda of the ASC before professional debates in accounting standard-setting turned their attention again to the context in which financial reporting numbers were produced.<sup>7</sup>

## **1.2 Rise and rise since the late 1980s**

The first publication that picked up ideas of “improving” financial reporting in the UK through additional reports explaining and complementing financial statements was *Making Corporate Reports Valuable* (McMonnies 1988) by the Research Committee of the Institute of Chartered Accountants of Scotland (ICAS). The report, which later became to be regarded as a “milestone” in thinking about reforming financial reporting (Standard-setter F), was prepared at a time when the British accounting bodies engaged in a new cycle of discussions on the future of financial reporting and the role of the accounting profession. It was followed by a series of profession-led research reports and debates in which ideas of expanding the scope of financial reporting gained further momentum (ICAEW 1988; ICAS 1988; McMonnies 1988; Arnold et al. 1990; Arnold et al. 1991b, 1991a). Eventually, ideas of supplementing the financial statements with additional reporting elements translated into regulatory reform projects at the British

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<sup>7</sup> Similar debates took place internationally, too. For example, the Canadian Institute of Chartered Accountants (CICA) engaged in a debate on the “future evolution” of corporate reporting at the beginning of the 1980s. The *Stamp Report* called for supplementary information in corporate reports to amplify the financial information provided in the financial statements (Stamp 1980). In the US, proposals for the disclosure of non-financial key performance indicators were published in the 1994 report *Improving Business Reporting – A Customer Focus: Meeting the Information Needs of Investors and Creditor* by the “Special Committee on Financial Reporting” of the American Institute of Certified Public Accountants (AICPA 1994).



Accounting Standards Board (ASB) and during the British Company Law Review (CLR).<sup>8</sup>

Failure to attract wide-ranging support for the proposals in *The Corporate Report* was retrospectively interpreted to be the result of a “too academic” approach that departed “too radically” from perceived commercial reality (Standard-setter E). The suggestions to rethink the scope of financial reporting were also explicitly criticised for being driven by only a small group of individuals with little empirical foundation or research into existing reporting practice (ICAS 1976b; Stamp 1985). Although some companies in the UK had started to publish additional voluntary reports, such as value added statements (Burchell et al. 1985) or operational reviews including indicators of future prospects (Gifford-Gifford 1976), the wider accounting community remained sceptical about an expansion of corporate financial reporting beyond the financial statements (Tweedie 1975; ICAS 1976a; Tierney 1976). Even the ICAS, which would become one of the strongest supporters of additional management commentaries a decade later, was not convinced by the proposals from *The Corporate Report*:

*“The Committee would caution the accountancy profession against attempting to be the arbiter of what corporate reports should contain other than in matters directly relating to financial reporting.” (ICAS 1976a)*

It seems *The Corporate Report* was ahead of its time. It anticipated a perspective on the role of business in society and ideas about managerial “best practice” that needed further evolution through history before it was more widely agreed in the later governance reform debates. The proposals for measuring and reporting “economic performance” in non-financial and future-oriented terms in the 1988 study *Making Corporate Reports Valuable* gained acceptance much more quickly among accounting practitioners. They were welcomed for their “more technical” accounting language and “better” alignment with “economic reality” (Standard-setter F).

The history of the rise and fall of narrative reporting in the 1970s and the rise and rise of calls for additional explanatory reports in financial accounting since the late

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<sup>8</sup> Both cases are further explained in chapters three and four respectively.

1980s supports the view that neither accounting issues nor the programmes in whose name they are mobilised are “simply there” by the time they begin to be linked in governance reform debates (cf. Young 1994). Starting from the view that the emergence of *programmes* and *technologies* of governing (and the links between them) are situational and relational (cf. Miller 1990; Rose & Miller 1992; Miller 2001), this chapter traces a genealogy (cf. Miller & Napier 1993) of events and developments that gave rise to widespread agreement on non-financial and future-oriented accounting as an issue for British policy-makers.

The discussion is organised in four sections. The first section briefly outlines some additional conceptual considerations that were necessary to frame the study of the complex processes of co-designing *programmes* and *technologies* of government. The second section outlines the rise of a category of non-financial and future-oriented accounting as part of a re-conceptualisation of managerial “best practice” during the 1980s. The findings provide the implicit background knowledge for the third section which discusses the links between similar theoretical-abstract ideas of “economic reality” and three arenas of British policy reform debates. The final part summarises the findings from this chapter and discusses their implications for the further study of accounting change in the remainder of this thesis.

## **2 Local and de-localised arenas of change**

On the one hand, the perspective in this chapter on the time that preceded the OFR events at the ASB and the DTI helps to understand changes in the programmes and objectives of governing that guided the regulatory reform debates at the ASB in the early 1990s and later during the CLR. On the other hand, it helps to explain the rise of a widely shared view of accounting as a means for thinking about and acting upon business activities that were not directly captured in the financial accounts.

The idea that accounting change is reflective and constitutive at the same time (Hopwood 1983b; Miller 1994b) suggests that the study of accounting and governance should take the ways in which “new” accounting categories mobilise “new” programmes of policy reform and *vice-versa* into account. This implies stepping beyond a dichotomy between policy-making and organisational accounting measurement and reporting techniques and to view them as intrinsically linked. However, only a small number of studies examined the processes through which a

specific vocabulary of organisational accounting practice mediated and shaped the programmatic language of high-level policy reform. These studies have looked at the encounters between accounting and various policy arenas, such as financial reporting standard-setting, industrial relations, or macroeconomic policy-making (Burchell et al. 1985; Miller 1991; Robson 1991; Young 1994). Although they provide helpful concepts for framing the study of accounting change in extra-organisational spaces, there has been little exploration of a process of co-designing *programmes* and *technologies* of government (cf. Miller & Rose 2008a). That is, the question of how programmes and technologies emerge in governance spaces in the first place has not been addressed, like the study by Burchell et al. (1985) on “the sudden upsurge of interest in value added” focuses on tracing apparently given notions of “value added” in three arenas of policy discourse. Although the conceptual refinement by Robson (1991) helps to explain how different arenas begin to express their distinct programmatic concerns in terms of value added, the studies do not explain how notions of accounting practices contribute to shaping government reform programmes.

To study the processes in which wider programmes of governing and a category of non-financial and future-oriented accounting co-emerged and reinforced each other, the analysis in this chapter takes the idea that the practices and rationales that happen to be labelled “accounting” emerge and transform in relation to more abstract ideas about the governance of economic and social life (Miller & Napier 1993) as its starting point. This leads to a focus on the “decisive” moments in which accounting, other bodies of knowledge, and the sphere of governance connect (Miller 1991). This research, therefore, rephrases the concept of the *accounting constellation* (cf. Burchell et al. 1985) and distinguishes between “local” and “de-localised” dimensions of problematising accounting as an issue for governing business enterprises. As in the study by Burchell et al. (1985), the local dimension of problematising accounting in this research relates to a set of specific British policy debates which called upon non-financial and future-oriented accounting to “solve” their distinct problems with governing. The introduction of the voluntary OFR at the ASB was preceded by a series of calls for reform in the arena of financial reporting standard-setting since the late 1980s. Similarly, the proposals for a mandatory OFR during the CLR seem to have grown out of various initiatives that

shared concerns with macroeconomic policy-making. Both arenas shared many of their concerns with a third series of policy debates on corporate governance. Therefore, the debates in the latter arena, though not directly linked to the OFR events, will be briefly sketched out in this chapter, too. Each arena is characterised by a distinct vocabulary of governing rationales. The policy debates that have been summarised under the label financial reporting standard-setting focused primarily on the “decision usefulness” of accounting reports when problematising financial reporting numbers as an issue for governing. Concerns with “corporate accountability” aligned the debates in the corporate governance arena. Finally, debates on public economic policy making were understood to concentrate primarily on the integration of corporate activities with a “public interest”.

In contrast, the term “de-localised” in this research refers to changing descriptions of the role of accounting in managerial processes that appear somehow detached from the distinctively British policy debates. They may be grouped according to a generic language of managerial “best practice” in terms of strategic management, financial management, and corporate social responsibility (CSR). The distinction between local and de-localised levels allows for a more diversified view of the different “conditions and demands placed upon accounting and accounting reports” (Young 1994). The notion of a de-localised dimension of problematising accounting in the British reform debates takes into account the idea that much accounting change seems to be mobilised “in the name of quite abstract notions of its roles, potential and functioning” and of “highly abstract notions of managerial process” (Hopwood 1983a, p. 3).<sup>9</sup> In particular, extra-organisational communities, such as academics, consultants, or policy-makers, often seem to assume a rather normative relation between organisational accounting practices and internal and external decision-making processes when elaborating calls for governance reform. However, the study of de-localised views on the role of accounting in business management is conceptually different from ideas of translation between local reform processes and a *transnational* level. Research on the “travel of ideas” (cf. Czarniawska & Joerges 1996) has proposed that highly abstracted and rationalised models of managerial

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<sup>9</sup> A similar relation between abstracted notions of practice in concrete regulatory policy making processes has been described for accounting standard-setting in the US as “making up users” (Young 2006). Problematisations of the “remote and abstract” representations of the enterprise in accounting reports have also been discussed by Miller and O’Leary (1993) in a study of the “politics of the product” event in the US in the 1980s.

practice take the form of a *transnational knowledge* (Meyer et al. 1997; Sahlin-Andersson & Engwall 2002) which gets diffused in different national or organisational contexts through the interventions of *epistemic communities* (cf. Haas 1992). This means that transnational organisations or professional networks with claims to policy-relevant knowledge in a particular domain (ibid., p. 3) come to act as “carriers” of management knowledge between a world-society level and the local (Portes 1997; Brunsson & Jacobsson 2000b; Sahlin-Andersson & Engwall 2002; Mennicken 2008). In contrast to a *transnational* perspective on change, a notion of “de-localised arenas” in this research emphasises that “a ‘consciousness’ of accounting techniques and calculations” (Robson 1991, pp. 551-552) may be inherent in local policy discourses even without the direct involvement of transnational actors or ideas.

The analysis of a range of British policy documents from the arenas of financial reporting standard-setting, corporate governance, and public economic policy making suggests that the links between local and de-localised dimensions are largely established through joint references to a historic specific “context” or “economic reality” of accounting change (Hopwood 1983b; Miller & Napier 1993). Previous research by Young (1995) on market value accounting in the US savings and loan crisis already identified a particular role of references to “economic reality” in accounting reform. This chapter uses the term *new global competition* to summarise the perceived impacts of wider economic, social, and political developments on economic activities from the 1980s onwards. They include notions of the complex, dynamic, and often unpredictable nature of global change (Holzner & Holzner 2006, pp. 50 & 53) which have historically grown out of the gradual removal of trade barriers to capital and labour mobility since the 1950s (Kahler & Lake 2003, pp. 4-7). *New global competition* further refers to the profound changes in processes of production and exchange that resulted from improved technologies, reduced transport and communication costs, and the increasing relevance of intangible assets in the asset-mix of modern business operations (Hall & Soskice 2001). These developments have also been recognised in accounting research, where references to increasingly global, dynamic and complex business environments have been acknowledged as a key element in accounting change throughout the 1980s (Hopwood 1989a; Bromwich 1990).

The categorisation of discourses as local and de-localised arenas of problem discourses in this study was, however, not an easy task. Arenas have to be understood as complex categories that may embrace a number of sub-arenas and sub-constellations. In addition, their boundaries are in constant flux, so that any definition will be historically and culturally specific (Foucault 1991d; Miller & Power 1992) and can never be clearly compartmentalised (Miller & O'Leary 1993). Nevertheless, the parallels in conceptualising “economic reality” and managerial “best practice” in a *transnational* body of literature and in the British reform debates were striking. The categorisation of the de-localised arenas was further supported by a review of Anglo-American writings on the development of “best practices” in business management since the 1980s. This literature review also helped to trace a general history of the interrelations between accounting and managerial practice which provides the background knowledge for the more in-depth analysis in this and the remaining chapters of this thesis.

### **3 Accounting and management in the 1980s**

Since the mid 1980s, an Anglo-American body of general management literature has treated accounting as almost synonymous with management (Miller 1998a).<sup>10</sup> The developments relate in particular to the rise of an economic discourse of management accounting since the Second World War which emphasised ideas of conscious planning and decision-making. As part of these encounters between management, economics, and accounting, the techniques for measuring and representing entrepreneurial activities in financial terms were increasingly seen as a key means for the “efficient” and “effective” management and monitoring of organisations (Hopwood 1992; Miller 1998a). This rationale of accounting as a technology of governing business enterprises according to economic principles has, however, been interpreted differently at different moments in time.

The remainder of this section outlines the rise of three arenas that were seen to constitute managerial “best practice” at times of *new global competition*. The discussion focuses on the ways they redefined conceptions of “economic reality” and how this became part of an increasing questioning of the role of financial

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<sup>10</sup> The term “management” has been increasingly used since the 1950s to describe the administrative process of planning, organising, resource allocation, directing, and controlling (Newman 1951; Newman 1953). In addition, studies of management were increasingly concerned with the development of a general management theory since World War II (Wren 1994, p. 349).

accounting numbers as an issue for governing business enterprises since the mid 1980s.

### 3.1 Strategic management

The concept of *management by objectives* (cf. Drucker 1955) and related notions of goal-setting and performance evaluation took centre stage in general management thought during the post-war period. Since the 1960s, they were complemented by notions of *strategy* – originally a military concept. Managerial goal setting and enterprise management in the name of strategy was conceptualised as an issue of matching long-term objectives and action plans with the allocation of resources as a means for their achievement (Chandler 1962). Throughout the 1970s, the catchphrase “strategic management” became widely recognised in business education, practice, and consultancy (Wren 1994, pp. 349 & 423). It grew into an even more prominent element of the management literature throughout the 1980s, when normative notions of strategy contributed to the development of a series of decision-tools for thinking about the deployment of internal organisational resources and the interactions with the organisation’s external environment (Dent 1990).<sup>11</sup> Models, such as the concept of “competitive strategy” or the “five forces model of strategic positioning” (Porter 1980, 1985) suggested that planning and decision-making should be based on a systematic analysis of the competitive environment.<sup>12</sup> The rise of concerns with strategic management throughout the 1980s was closely related to changing perceptions of the terms of competition in a global economy. As part of these changing theoretical perspectives, the role of managers was redefined in terms of identifying and managing strategic “opportunities” and “challenges” (cf. Collis & Montgomery 1995; Teece et al. 1997). A long-term perspective in business management looking to secure competitive advantage came to be regarded as a crucial success factor in times of increasingly dynamic and highly innovative environments (Hayes & Abernathy 1980). Since then, normative notions of strategic management have become part and parcel of the conceptualisation of the

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<sup>11</sup> The strategic management literature is divided into prescriptive (e.g. Ansoff 1965; Porter 1980, 1985) and descriptive notions of strategy (e.g. Mintzberg & McHugh 1985; Mintzberg 1987).

<sup>12</sup> The “five forces” concept describes an industry as being influenced by five factors that impact the potential of a business to achieve competitive advantage over other organisations in the same industry. The concept of “competitive strategy” provides an analytical approach for thinking about the relative competitive advantage of a business within its markets in terms of three generic strategies of cost leadership, differentiation, or the focus on a market segment (Porter 1980).

tasks of top managers. They are closely tied in with another debate on managing the financial bottom-line.

### **3.2 Financial management**

The globalisation of capital flows and changes to the financing structure of businesses throughout the 1980s were further linked to calls for increased *financial management* of the firm. These proposals responded to an observed concentration of ownership in the hands of large institutional investors.<sup>13</sup> Their potential to take action against the decisions of the board of directors led to the reinterpretation of the role of the so-called “markets of corporate control” in managerial decision making (Jensen & Ruback 1983). An undervaluation of businesses in the stock market was supposed to increase the risk for managers to be replaced and/or for the company as a whole to become subject to a so-called “hostile” takeover. In response, managers were urged to focus their efforts on the creation of long-term “shareholder-value” (cf. Rappaport 1986). The rise of a shareholder value rhetoric was part of a general *financialisation* (cf. Fligstein 1990) of Anglo-American business management and competition throughout that decade. From the perspective of financial management, the organisation came to be seen as a portfolio of investment projects which should be managed according to the principle of maximising the returns on equity. Academic endorsers of “shareholder value” emphasised the perceived economic benefits and efficiency gains from a managerial focus on market valuations. Aspirations to operationalising “shareholder value” in day-to-day management provided the basis for an avalanche of value-based management concepts from the consulting industry (Froud et al. 2000). In general, it was suggested that “shareholder value” became a holistic management approach permeating any aspect of corporate activities in order to meet the objective of maximising return on equity.

### **3.3 Corporate social responsibility**

In addition to the re-definition of performance targets in terms of “shareholder value” and a general “strategisation” of the language of goal setting throughout the 1980s, the economic based models of business management increasingly embraced

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<sup>13</sup> In 1998, 80% of the shares of UK companies were held by national and international institutional investors. For further details about institutional investors in the UK see the “Myners Review” (Myners 2001).



ideas of *corporate social responsibility* (CSR).<sup>14</sup> Debates on the “social responsibilities of the businessman” (Bowen 1953) had already emerged in the field of industrial relations soon after WWII. During the 1960s, the question “Can business afford to ignore social responsibilities?” (Davis 1960) established first theoretical linkages between notions of CSR and a firm’s economic success. Ansoff (1965), for instance, already argued that the achievement of long-term corporate objectives required the recognition of further “social” objectives beyond the “economic” objectives of the business. From the 1970s onwards, ideas of a mutual permeability of business organisations and society began to challenge the specific definitions of high-level objectives in business management (Carroll 1979, 1991, 2000; Sharp Paine 2003). Around that time, the issue gained increasing public attention. Western governments and top-managers began to openly recognise the possibility of a “social contract” that established ethical and moral norms of business’ conduct beyond basic economic and legal requirements (see, e.g. CBI Company Affairs Committee 1973, para. 22; Tweedie 1975).<sup>15</sup> However, CSR related issues still remained largely separated from concerns with managing economic performance until the development of a *stakeholder theory* (cf. Freeman 1984) in the mid-1980s. The concept proposed close links between “social performance” and “economic performance” which fed into a growing interest in operationalising CSR in business management. Moreover, the notion of “stakeholders” allowed for the breaking down of the abstract concept of the “social” into specific key relationships as an issue for managerial intervention. CSR became intelligible in a language that was more consistent with the emerging programmes of goal setting and performance management in the names of “strategy” and “shareholder value” (Drucker 1984; Wren 1994, p. 410). The vocabulary of a so-called “CSR business case” translated the management of non-shareholder relations into a language of risks and opportunities and long-term value-maximisation

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<sup>14</sup> A generic definition of corporate social responsibility (CSR) identifies four general levels of corporate responsibilities to society. They may be categorised as economic, legal, ethical, and philanthropic obligations (Carroll 1979, 1991). Depending on local adoptions of the concept the boundaries of a general CSR category, however, always remain somewhat blurred (Carroll 1999). For example, British debates on CSR have been mainly associated with economic implications of wider accountability of businesses to society (Gray et al. 1996; Shearer 2002), whereas a US perspective on CSR seems to emphasise its philanthropic aspects (Anon. 2002).

<sup>15</sup> In addition, a survey among the chairmen of the 300 largest UK-listed companies indicated their appreciation of the interests of employees, shareholders, and customers in decision making (ASSC 1975, paras. 4.28-4.28). Other commentators of the time argued that company managers considered their “social and economic obligations” largely in order not to “risk public disapproval of their activities” in practice (Tweedie 1975).

(Carroll 1999). As a result, the management of stakeholder relations became increasingly seen to be part of the strategic and financial management of the firm.

### **3.4 Relevance lost and found**

The three areas of rising normative notions of “best practice” in business management were soon linked to calls for accounting to support the operationalisation of interlinked notions of “strategy”, “shareholder value”, and “CSR” in day-to-day management practice. In times of reduced product life circles and advanced production and information technologies, a “strategisation” of accounting was perceived to be crucial for the company’s long-term success (cf. Simmonds 1981; Bromwich 1990).<sup>16</sup> However, the new demands placed on accounting began to challenge the exclusive use of financially focussed accounting figures in managerial accounting (Hopwood 1985). The debates were characterised by a “relevance lost” rhetoric (cf. Johnson & Kaplan 1991), which gained momentum in the field of management accounting research and consultancy by the end of the 1980s.<sup>17</sup> Johnson and Kaplan (1991, p. xii) introduced the thesis “that the management accounting systems in Western companies were no longer providing relevant information for decision making and control”. Their problematisations of financial accounting numbers were closely linked to perceptions of a new “economic reality” that affected the nature of processes of production and exchange. From a “relevance lost” point of view, the days of financial accounting-based management systems were numbered at the dawn of the “information age” and increasing global competition (Ezzamel et al. 1990; Johnson & Kaplan 1991, p. 209). For example, the treatment of investments in intangible assets as cost of the same period according to financial reporting rules was criticised for possibly deterring managers from making long-term investment decisions at the expense of future profitability. Traditional accounting systems were further criticised for giving visibility to processes of production and exchange that were no longer representative of the “modern” business enterprise (Johnson & Kaplan 1991, pp.2-3) and for concentrating only on the company itself but not on its outside markets and future developments (Shank & Govindarajan 1992, p. 196).

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<sup>16</sup> For a review of the strategisation of management accounting since the beginning of the 1980s, see Langfield-Smith (2008).

<sup>17</sup> The book “Relevance Lost: the rise and fall of management accounting” by Johnson and Kaplan was first published in 1987. All of the following references refer to the reprinted edition of 1991.

Accounting always seems to be called upon to deliver more than its practices were originally designed for (cf. Hopwood 1983b; Hopwood & Miller 1994). As much as financial accounting numbers were problematised as a means for operationalising emerging notions of managerial “best practice”, accounting in itself was still seen to be able to provide the “solution” to its own “problems”.<sup>18</sup> The general critique that historical cost numbers in financial accounting were unable to give visibility to “economic reality” stimulated discussions on new “measures of economic value” for the strategic management of the firm (Johnson & Kaplan 1991; Ittner & Larcker 1998). Research into the re-conceptualisation of management accounting in the name of strategy explored the possibilities for making the financial and non-financial drivers of long-term “competitive advantage” and “shareholder value” calculable (cf. Simmonds 1981; Govindarajan & Gupta 1985; Simons 1987; Bromwich 1990).<sup>19</sup> Different models for alternative systems of accounting-based performance measurement were proposed. They supported, for example, the idea of a “value tree” in which top-financial measures of economic value could ideally be broken down into a series of further financial key performance indicators (KPIs) that systematically linked strategic goals from the corporate to the operational level (Copeland et al. 2000; Gary 2002; Weber et al. 2002). Among the numerous measures of “economic value” as the top-financial indicator of shareholder value maximisation that were proposed by the consulting industry were, for example, McKinsey’s economic profit (Copeland et al. 1989), Stern Steward’s economic value added (Stewart 1991; Stern et al. 1995), or Arthur Andersen’s shareholder value added (Froud et al. 2000).

Other models proposed to integrate financial and non-financial measures in order to present a more holistic picture of the underlying drivers of competitive advantage. Maybe one of the most prominent examples for an “integrated” performance measurement system is the *Balanced Scorecard* (BSC) by Kaplan and Norton (1992; 1993; 1996; 2000; 2004; 2006). The BSC is supposed to support the

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<sup>18</sup> The inherent optimism in the will to govern through accounting technologies goes hand in hand with the observation that government is a “congenitally failing operation” (Miller & Rose 1990, p. 10; 2008b), which implies that connections between programmes and technologies of regulation are in an “always unstable and incomplete” form (Hunt 1997, pp. 113-114).

<sup>19</sup> Concerns with making the future calculable in accounting change have emerged at earlier points in history. One example is the rise of discounted cash flow techniques for evaluating investment opportunities in the 1960s (Miller 1991, 1998a).

balanced measurement of financial, non-financial, backward-looking, and future-oriented indicators of long-term shareholder value creation (Kaplan & Norton. 1996, p. viii). The model suggests that it is possible to capture and provide calculations for “soft” or intangible issues, such as relationships with customers, employees, and suppliers in management information systems.

Of course, the above summary of the mainly Anglo-American concepts of “best practice” in general management is far from being exhaustive. Nevertheless, it helps to redraw the multiple aspects of business activities that non-financial and future-oriented accounting systems were supposed to render visible when mobilised in policy reform debates. The next sections outline how very similar notions of “best practices” in terms of “strategic management”, “financial management”, and a “CSR business case” created possibilities for the problematisation of financial reporting numbers as an issue for governing business enterprises and the British economy in different policy debates since the late 1980s. At the same time, they became part of new ways of reasoning and categorising the role of accounting in economic governance which this research interprets as the rise of a new “de-localised” category of non-financial and future-oriented accounting.

#### **4 Accounting and British policy making**

Ideas of a “strategisation”, “marketisation”, and “socialisation” of business management also became prominent in economic governance discourses in the UK. It seems that changing ideas about the range of managerial activities that accounting could and should render visible created possibilities for rephrasing the programmes of governing in each of the policy arenas. However, the ways in which ideas of non-financial and future-oriented accounting were mobilised in three local governance arenas in the UK suggest that the de-localised notions of the role of accounting in business management did not represent a single closed category or unanimously agreed set of techniques. Instead, each of the policy debates in financial reporting standard-setting, corporate governance, and public economic policy-making put different emphasis on the various practices and rationales that made up a category of non-financial and future-oriented accounting.

#### 4.1 Financial reporting standard-setting

Assumptions about the multiple dimensions that constituted the “economic reality” of reporting entities increasingly became part of calls for a “better” representation of managerial activities within the financial reporting framework. They were accompanied by a re-definition of the concept of “usefulness” in corporate financial reporting that increasingly embraced the changing conceptions of “best practices” in the economic management of business enterprises.

The general focus on “users”, which had taken centre stage in financial reporting alongside a growing emphasis on “the market” as a governing rationale of standard-setters, has remained relatively stable in accounting standard-setting since the 1970s.<sup>20</sup> However, aligning the notion of “users” in accounting standard-setting with a focus on investors under the stewardship reporting convention and company law requirements has been challenged in various reform debates (ASSC 1975, para. 4.11). Both *The Corporate Report* (ibid., para. 3.2) and *Making Corporate Reports Valuable* (McMonnies 1988) proposed to revisit the definitions of “users” and “usefulness” in financial reporting standard-setting. *The Corporate Report* suggested to widen the scope of corporate reporting in order to meet the information needs of investors as well as other stakeholders (ASSC 1975, paras. 6.2-6.3). These proposals were largely linked to a more general re-conceptualisation of the role of business in society and the question of how it could be accountable to a wider public (Rutherford 2007, p. 108). However, when the proposals from *The Corporate Report* did not translate into regulatory reform, ideas of widening the scope of “users” were not further pursued either. In line with the refocusing of financial reporting standard-setting on “improving” the financial statements, a notion of “users” as shareholders also occupied a central role throughout the 1980s. Yet, the concept of “usefulness” was more closely aligned with the emerging “shareholder ideology” in the increasingly capital market-oriented Anglo-Saxon models of corporate governance during that period (Engelen 2002; Martinez Lucio & MacKenzie 2004; Cooper & Robson 2006). In addition, non-shareholder stakeholders were increasingly portrayed as economic decision-makers whose interests in the company largely overlapped with those of shareholders. These

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<sup>20</sup> For a detailed discussion of the changing rationales in UK accounting standard-setting, see chapter three. On the growing preoccupation with supporting and protecting the interests of investors as “users” in financial reporting standard-setting, see also Young (2003; 2006).

perceptions gave the high-level discussion on “users” and “usefulness” in *Making Corporate Reports Valuable* a different quality.<sup>21</sup> In a similar way as the “relevance lost” debate, the discussion started from the view that the existing framework of financial reporting was mostly disregarded in internal decision-making.

*“Management is much more concerned about the future than the past. From this point of view, they almost never use their own published accounts when taking policy decisions (though they will think about the impact on the accounts of the decisions they take).”*  
(McMonnies 1988, para. 5.38)

The ICAS-study then identified possible reasons for a “relevance lost” of financial reporting:

*“We identified the basic shortcomings of present-day financial reporting, – the adherence of legal form rather than economic substance, the use of cost rather than value, the concentration on the past rather than the future and the interest in “profit” rather than wealth”* (McMonnies 1988, para. 1.18)

To remain “useful”, it was demanded that external corporate reporting catch up with that “reality”. Abstract conceptions of “best practices” in managerial processes were thereby translated into new ideas about the roles and purposes of the financial reporting framework. Additional narrative reporting was supposed to result in “enhanced” opportunities for monitoring and decision making (McMonnies 1988, paras. 8.6-8.16) – enabling present and future shareholders in particular to form better informed views “about the future of their investment” (ibid., para. 5.37).

*“The corporate report should cover the past, present and future, providing some continuum and so reflecting the nature of the entity itself. [...] the corporate report ought to provide sufficient quantitative and qualitative information to help those users involved with the entity to make assumptions/predictions about its future performance.”* (McMonnies 1988, para. 3.17)

The provision of additional management commentary in the annual report was supposed to make different aspects of managerial concerns, such as long-term objectives or judgements of the competitive environment, visible to external report

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<sup>21</sup> The range of users, to which *Making Corporate Reports Valuable* referred, was not as wide as that promoted by *The Corporate Report* (ASSC 1975), which suggested additional accountability to creditors, employees, analyst-advisers, business contact groups (suppliers, customers, competitors), the government, and the public (ASSC 1975, paras. 2.1 - 2.40). *Making Corporate Reports Valuable* only referred to equity investors, creditors, employees, and business contacts (McMonnies 1988, para. 3.6).

users (McMonnies 1988, e.g. paras. 5.4-5.5, 7.53 and 5.41-5.44). In turn, more efficient and effective accounting disclosures to external market participants were supposed to support the achievement of “best practice” in the managerial process itself. The preparation of non-financial and future-oriented reports was expected to lead managers to develop an improved understanding of their own business and to build a reputation for being strategic and forward looking.

The idea that not only internal, but also external accounting reports should reflect “economic reality” to a wider range of users was widely welcomed by those involved with financial reporting in practice and regulation. The 1989 joint research conference *Financial Reporting: the way forward* by the ICAS and the ICAEW gathered preparers, accounting professionals, and accounting academics to discuss the implications of international research on the future of financial reporting in the UK. The discussion reiterated the role of economic decision-makers that had been assigned to non-shareholder stakeholders. One of the contributions to *Financial Reporting: the way forward* described the connection between non-financial and future-oriented reporting and the “information needs” of wider stakeholder groups as follows:

*“[F]inancial reporting serves decision makers – in the first instance investors and potential investors, but also a much wider constituency of interested parties who are regarded, or regard themselves, as being concerned to evaluate the economic performance of the company. Nowadays it is not just economic but wider social performance which is in question.” (Shaw 1990, p. xxi)*

Other contributions focused more explicitly on the type of information that was considered “useful” by internal and external decision-makers. In line with the 1988 ICAS-study (para. 5.38), a review of differences between the internal use of financial information by managers and their external communication concluded that (hitherto undisclosed) future-oriented data was highly relevant for decision makers, both internally and externally (Cook 1990).

*“[A] well written management commentary can significantly enhance the usefulness of the financial statements by providing a bridge between the formalised presentation in the financial statements and management’s insight into and strategy for its business.” (Cook 1990)*

The idea that persons outside the company “should know what management knows” (Cook 1990) was further elaborated on in subsequent debates.<sup>22</sup> Following the research conference, an Action Group was established to sustain the momentum that was created by the earlier reports. The group’s report *The Future Shape of Financial Reports* outlined recommendations for practicable financial reporting reforms (Arnold et al. 1991a, 1991b). The debates in the financial reporting standard-setting arena, eventually led to calls for regulatory interventions by the ASB. The regulatory reform proposals also drew on the emerging ideas about managerial “best practice” and “economic reality” when elaborating regulatory interventions in non-financial and future-oriented reporting as a way to “solve” perceived “problems” of financial reporting.<sup>23</sup> Although the first guidelines for the voluntary preparation of Operating and Financial Reviews (OFR) in the annual report did not mention the term “strategy” explicitly, the recommendation to cover future-oriented aspects in terms of reporting on the business’ competitive environment, its internal resources, and the risks and uncertainties of the business (ASB 1993, para. 12) showed strong parallels with a general language of “strategic management” and ideas of long-term shareholder-value creation.<sup>24</sup> The *OFR Statement* was supposed to “improve” reporting practice on the financial position and results of increasingly complex businesses (ibid., p. 1) through additional narrative reporting elements “rather than merely numerical analysis” (ibid., para. 3). The standard-setting activities at the ASB eventually limited the definition of “users” to equity investors following the recommendations from the *Dearing Report* (ICAEW 1988) and the launch of the *Statement of Principles* project.<sup>25</sup> From the point of view of the standard-setters, however, this did not exclude the concept that the narrative statements that were produced under the ASB’s OFR regime were still “useful” for wider stakeholder groups (Standard-setter B). These considerations in the financial reporting reform debates were also connected to a growing attention to the integrity of business leaders (DTI 2001) which made

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<sup>22</sup> Allan Cook later became Technical Director of the ASB.

<sup>23</sup> For further discussion, see chapter three.

<sup>24</sup> The statement did not explicitly mention the term “strategy”, as this was considered by the standard setters’ working group to be too sensitive on information commercially and that any requirement to report on strategy would lead to bland statements (Standard-setter D). However, the term was later used in the revised Reporting Statement (ASB 2003b) and in the *OFR Regulations 2005*.

<sup>25</sup> The role of formal framework criteria in the standard-setting process is further discussed in chapter three.



notions of “corporate governance” a focal point in regulatory reforms in Western economies since the mid and late 1980s (Tricker 2000).<sup>26</sup> These overlaps between notions of “usefulness”, “corporate accountability”, and “economic prosperity” for the benefit of society are further discussed in the next section.

## 4.2 Corporate governance

Corporate governance is difficult to single out as a separate policy arena. Its concerns with corporate accountability closely tie in with public economic policy debates and the sphere of financial reporting.<sup>27</sup> The definitions of the term “corporate governance” are ambiguous due to wide national variations (Morck & Steiner 2005). For instance, notions of wider corporate responsibilities beyond shareholders and distributive justice exist traditionally in Continental Europe and Japan (Villiers & Boyle 2000; Chahed & Müller 2006; Luo 2007). In general terms, the Anglo-American corporate governance discourse has been characterised by economic notions of “agency” and a focus on shareholder “interests” in the system of corporate accountability.<sup>28</sup> This based on rising concerns about processes of monitoring and control in the relation between managers and shareholders since the creation of the limited liability company in the mid-nineteenth century (Berle & Means 1968; Villiers & Boyle 2000; Davies 2003; Luo 2007). Corporate governance also marks the point of intersection between legal and economic theory on the issue of agency costs. This leads to a focus on market inefficiencies and imperfections and their reduction through regulatory interventions (Easterbrook & Fischel 1991; Grantham 1998; Kraakman et al. 2004).

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<sup>26</sup> The rise of a corporate governance talk has also been associated with some of the most prominent business scandals in the UK and the US, such as the UK “Guinness scandal” (1986) and “Maxwell collapse” (1991) and the US insider trading scandals around Ivan Boesky and others (1986).

<sup>27</sup> The work of the Cadbury Committee on the financial reporting aspects of corporate governance and the ASB’s OFR project took place at the same time but did not directly intersect (Accounting professional B). The Committee, however, explicitly acknowledged the contribution of the ASB’s voluntary OFR guidelines in its final report (Cadbury Committee 1992, para. 4.53).

<sup>28</sup> From the perspective of economic theory, agency problems arise from the separation of ownership and controls in cases where markets are not fully efficient. As a result, shareholders are considered unable to fully observe the efforts by managers to act in the interest of the owners (moral hazard problem). In line with the economics-based perspective on agency-relationships, traditional legal theory emphasises a special role for equity investors as bearers of a residual risk that reserves them particular control rights (Willems, 1997; Grantham, 1998). That is, they are considered to hold a share in an always uncertain capital surplus that remains after any contractual obligations to pay other stakeholders, such as debt providers, suppliers, or employees, have been served (Grantham, 1998). Accordingly, company law has been described as a mechanism for reducing the costs arising from inefficiencies in the markets of corporate control by a system of directors’ duties and legal enforcement mechanisms (Berle & Means 1968; Easterbrook & Fischel 1991; Grantham 1998; Kraakman et al. 2004). For a critique of a shareholder orientation in company law, see e.g. Engelen (2002).

The more recent rise in worldwide political interest in corporate governance in particular relates to expectations about the economic implications of corporate governance systems and corporate accountability mechanisms for business and society (cf. OECD 2004). According to the OECD (2004) “[c]orporate governance is one key element in improving economic efficiency and growth as well as enhancing investor confidence” through a set of relationships, rules, and measures that help companies achieve their objectives. The idea that a focus on long-term shareholder-value maximisation in managerial processes correlates with the maximisation of overall social wealth was also part of an increasing interest in “promoting high standards of corporate governance” outside the legal framework in the UK in the early 1990s (FRC 2008). In May 1991, the Financial Reporting Council (FRC) created a committee on “The Financial Aspects of Corporate Governance” in cooperation with the London Stock Exchange (LSE) and the accounting profession.<sup>29</sup> The work of the so-called “Cadbury Committee” started from a perceived lack of public trust in the corporate system in general after a series of accounting and auditing scandals in the 1980s and the early 1990s (Davies 2003).<sup>30</sup> Accordingly, the aim of the project was to develop approaches for increasing the accountability of directors and to “contribute positively to the promotion of good corporate governance as a whole” (Cadbury Committee 1992, para. 1.2).

The results of the Cadbury review were published in a final report and a Code of Best Practice in December 1992. The documents included calls for accounting change to “solve” the perceived problems with financial reporting numbers as an issue for corporate governance. The Cadbury Report (1992) portrayed the focus on financial reporting numbers in external corporate reporting as particularly problematic in the operationalisation of a shareholder-value ethos. On that point, the Cadbury Committee shared many of the concerns of the financial reporting standard-setting arena. The framework for financial reporting which existed then, was doubted to provide the information that was necessary to monitor and control

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<sup>29</sup> The FRC, which also oversees the work of the ASB, has been formally responsible for the voluntary corporate governance framework in the UK (FRC 2008).

<sup>30</sup> The most prominent scandals include the UK “Guinness scandal” (1986) and the “Maxwell collapse” (1991); US insider trading scandals involving Ivan Boesky and others (1986). For further discussion of their impact on trust in professional experts, see chapter three.

how directors ran a business and how they could be held accountable for their actions. The use of “creative accounting” techniques by managers was seen as obfuscating shareholder-value calculations and to create obstacles to the monitoring and control of corporate activities by external parties. Nevertheless, the reports emphasised “improvements” in the financial reporting regime as a way for enhancing corporate accountability in the relationship between boards of directors and shareholders in the UK.<sup>31</sup> The Cadbury Committee suggested that accounting reports should provide additional non-financial and future-oriented information beyond the financial accounts. This was aimed at ensuring balance of “good” and “bad” news in external disclosures and was also supposed to contribute to an “understandable assessment” of the past, present and future position of the company (Cadbury Committee 1992, para. 4.50).

*“What is required of financial reporting is that it should be honest and that it should present a balanced picture of the state of the company’s affairs.” (Cadbury Committee 1992, para. 3.6)*

*“Balance requires that setbacks should be dealt with as well as successes, while the need for the report to be readily understood emphasises that words are as important as figures.” (Cadbury Committee 1992, para. 4.50)*

Notions of non-financial and future-oriented accounting also created possibilities for re-defining the nature of the tripartite relationship between the members of the board, shareholders, and auditors in discharging, monitoring, and controlling corporate accountability (ibid., para. 1.6). The emphasis on increasing the accountability of directors in their long-term “shareholder value” orientation to shareholders by means of non-financial and future-oriented reporting also included ideas about how to meet the information needs of wider stakeholder groups.<sup>32</sup>

*“What shareholders (and others) need from the report and accounts is a coherent narrative, supported by the figures, of the company’s performance and prospects.” (Cadbury Committee 1992, para. 4.50)*

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<sup>31</sup> The term “corporate accountability” generally describes the degree of transparency in corporate activities and the responsiveness to external concerns through financial reporting and other transparency mechanisms (Luo 2007, p. 129).

<sup>32</sup> Similar shifts in the definitions of the responsibilities, rights and duties of the members of an economic community have been observed in other jurisdictions. For example, Miller & O’Leary (1993) observed a re-orientation of accountability relations from a focus on capital markets to the relation between customers and products within changing perceptions of economic citizenship in the US in the 1980s.

Overall, the review of the Cadbury Committee suggested that improving the financial aspects of the system of corporate governance had implications beyond direct agency relationships. This linked the debates on additional narrative disclosures more explicitly to concerns with economic governance in the sphere of public policy making:

*“The country’s economy depends on the drive and efficiency of its companies. Thus the effectiveness with which their boards discharge their responsibilities determines Britain’s competitive position. They must be free to drive their companies forward, but exercise that freedom within a framework of effective accountability. This is the essence of any system of good corporate governance.” (Cadbury Committee 1992, para. 1.1)*

*“An open approach to the disclosure of information contributes to the efficient working of the market economy [...].” (Cadbury Committee 1992, para. 3.6)*

Later reviews of corporate governance in the UK (Greenbury 1995; Hampel 1998; Turnbull 1999) continued to emphasise the role of additional narrative disclosures in overcoming “problems” in the agency relationship between shareholders and managers. As mentioned before, the calls for wide ranging corporate governance reforms in the Cadbury and later the Hampel review were also linked to public economic policy concerns with securing a wider public interest (Shaw 1989). The Ministerial speech on the launch of the CLR (Beckett 1998) explicitly referred to the corporate governance reviews by the Hampel (1998), Greenbury (1995), and Cadbury (1992) Committees. The next section focuses more explicitly on the mobilisation of a category of non-financial and future-oriented accounting in public economic policy reform debates.

### **4.3 Public economic policy making**

*“Questions of accounting measurement and reporting touch the public interest very deeply”. (Shaw 1989)*

As laid out before, UK public policy makers in the 1970s had already engaged in debates about the public interest role of large corporations. The *Bullock Report* (Department of Trade 1977b) stressed that socially responsible companies which took account of their employees were a core element of a democratic society. However, these earlier public policy debates on the role of business in society had remained largely disconnected from concerns with macroeconomic performance.

This changed significantly throughout the 1990s. Ideas of “stakeholding” and a role for economic and political institutions in supporting a system of social citizenship in “the modern welfare state” gained increasing attention around the mid 1990s (Hutton 1995; Anon. 1996).<sup>3334</sup> Public policy research shifted attention to exploring possible ways for operationalising “careful economic management and institutions that fostered co-operation and commitment” in order to achieve “successful capitalism” that did not constrain competition and flexibility (Hutton 1995, p. 17). For example, the Royal Society for the encouragement of Arts, Manufactures & Commerce (RSA) launched the *Tomorrow’s Company Inquiry* in January 1993 to explore the role of business in society. The outcome of the research into the views of UK business leaders was a series of public policy recommendations, which were published in an interim report (RSA 1994) and in the final report *Tomorrow’s Company: the role of business in a changing world* (RSA 1995). They largely mirrored theoretical abstract notions about managerial “best practices” in times of *new global competition*. The work of the RSA among others referred to “evidence [...] for a strong correlation between issues concerning people, including relationships, and sustainable business success” (ibid., p. 6). In line with ideas of a CSR business case, both reports emphasised ideas of an “inclusive approach” to internal management.

*“In tomorrow’s company, priority needs to be given to optimising the company’s performance in all its relationships [...] Directors and investors alike need to improve their understanding of what the most important measures are for a particular business, and how each is linked to sustainable financial performance.” (RSA 1994, p. 19)*

In addition, the public policy debates called for managerial attention to the definition of its purposes and values in a “success model” that took account of wider stakeholder relationships (RSA 1995). In line with the “relevance lost” and “found” debates, internal and external accounting systems were assigned a particular role in operationalising the “inclusive approach”. The RSA suggested that

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<sup>33</sup> Ideas of a “stakeholder society” in the early days of the New Labour project (cf. Anon. 1996) were later toned down (Burkitt 2006, Regulator B). By the time the CLR was launched, the language of public economic policy making was more closely aligned with ideas of a “business case” for CSR.

<sup>34</sup> This research finds explicit references to individuals, such as the economist John Kay or the philosopher Charles Handy. (Beckett 1998). Further secondary sources suggest that the New Labour Movement followed Hutton’s (1995) proposals in *The State We’re In*, when considering “stakeholding” in its public policies (Anon. 1996; Burkitt 2006; Howard 2006).

managers should translate the key drivers of long-term success into appropriate financial and non-financial performance measures (RSA 1995, pp. 8-9 & 29). These calls for change were supported by a critique of the then existing system of financial reporting.

*“By itself, financial performance does not gauge the overall health of the business. It neither defines competitive performance, nor measures the broader value created through product quality, speed of response and service. Companies which rely solely on financial measures of success are exposing their shareholders to unnecessary risk and denying themselves the opportunity to improve returns.” (RSA 1994, p. 20)*

*“To act inclusively UK companies need to go beyond the limitations of traditional accountancy. They need new criteria, new measures and a new language of success.” (RSA 1995, p. 12)*

The idea that accounting systems were already able to provide “inclusive” measures of business performance was reflected in the explicit critique on the “ignorance of world standards” in the UK (RSA 1995, p. 1). Existing accounting measurement and reporting practice in the UK was perceived to lag behind new “best practice” in business management. Consequently, the RSA called for the introduction of “established” BSC-type performance measurement systems (ibid., p. 13) or other models, such as “McKinsey’s Value Based Management system” (ibid., p. 7). The view was also expressed that accounting played a particular role in the “socialisation” of corporate activities.

*“Tomorrow’s Company will produce annual reports containing clear statements about its purpose and values, its definitions of success, and its key relationships – with customers, suppliers, providers of capital, employees and the community – as well as relevant disclosure of its progress.” (RSA 1995, p. 13)*

The recommendations of the RSA were later picked up by other public policy think tanks and by Government. In 1995, the Institute of Public Policy Research (ippr) set up the “Commission on Public Policy & British Business”. Its 1997 report *Promoting Prosperity: a business agenda for Britain* integrated ideas of long-term “stakeholder-” and “shareholder value” with the objective of fostering economic prosperity.

*“The UK’s economy would be sounder if more companies followed best practice in dealing with customers, investors, employees, suppliers – all those groups that have a common interest in the company’s performance – and if more companies operated with a far-sighted business ethos.”(Commission on Public Policy and British Business 1997, pp. 3-4)*

In order to overcome a general “lack of trust” in the corporate system, the Commission on Public Policy and British Business (1997, pp. 96-100) recommended a sustainable reform of the existing regulatory frameworks. The “solution” was supposed to be provided by a “light” and co-operative approach to regulatory reform that largely focused on a clarification of directors’ legal duties and otherwise relied on external accounting reports as mechanisms for monitoring and enforcement. The issue of an “inclusive” company reporting was more explicitly followed up by the report *Sooner, Sharper, Simpler* by the Centre for Tomorrow’s Company (1998).<sup>35</sup> The report outlined a “vision of the future of reporting” which also left its mark on the later work of the Company Law Review Steering Group (Regulator A). Similar thoughts about public policy reform and a central role of accounting and reporting for achieving abstract concepts of managerial “best practice”, eventually emerged in the company law reform debates at the DTI (Beckett 1998; DTI 1998b, para 3.7).

*“Our companies find themselves in an increasingly competitive, globalised marketplace. [...] Successful firms, whether large or small, are those in which the Board, the shareholders and the employees have a common purpose because they each know that their long term wealth, health and happiness depend on the long term stability, growth and prosperity of their company. [...] Their leaders have a clear vision that inspires the whole company to exceed their customers’ expectations. [...] Such companies also work with all their employees to unlock the full potential of each. [...] Modern companies work too in vibrant supply chains, actively helping their suppliers to improve performance, anticipating and contributing to innovation at all stages of the chain, not just their own. [...] And the modern company is open with its investors, building on their expertise, particularly in relation to investment decisions.” (Beckett 1998)*

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<sup>35</sup> The Centre for Tomorrow’s Company was set up as an independent think tank following the RSA inquiry – in the same year. The organisation gained further influence on the CLR through the membership of its then Chairman in the CLRSG and the participation of its Director in the Consultative Committee (CLRSG 1999a, annex A) and in Working Group G on “Accounting, Reporting and Disclosure”.

The Government drew explicitly on the idea of an “inclusive approach” to business management and annual disclosure as outlined by the ippr and further elaborated in the work of Tomorrow’s Company (Beckett 1998; DTI 1998b, para 3.7). The encouragement to report on strategic objectives, relationships and non-financial performance measures came to be seen as a “solution” to perceived problems with governing the economy at large that would allow operationalising the various objectives of public economic policy making without compromising one for the other (Beckett 1997b).

## **5 Co-emergence of programmes and technologies**

*“Accounting practitioners may invoke ideas of what is common sense, but that ‘common sense’ has a history of formation and what is accepted today as obvious was not always so.” (Power 1997, p. xii)*

The findings from this chapter support the view that programmes and technologies of governance co-emerged in processes of problematising financial reporting numbers as an issue of governing. Ideas about a new category of non-financial and future-oriented accounting arose from a variety of policy debates that took place in different forums prior to the OFR projects at the ASB and during the CLR. Their analysis illustrate how new models of organisational reality established new objects for accounting measurement and reporting. The actors in these governance spaces came to agree that decision-making on the basis of financial reporting numbers constituted a “problem” of economic governance in the UK. At the same time, they increasingly shared the view that accounting should and could provide measures of non-financial and future-oriented aspects of business management. These new ways of reasoning and categorising accounting created possibilities for new courses of action (cf. Hacking 1986). The view that non-financial and future-oriented measurement and reporting was part of the accounting category provided policy makers with new ways of thinking about the scope of activities that should and could be made governable “at a distance” through the calculative practices of accounting. At the same time, the emergence of a category of non-financial and future-oriented accounting bolsters the view that accounting change reflects and at the same time constitutes the organisational and political environments in which it emerges (cf. Burchell et al. 1980; Hopwood 1983b; Covalski & Dirsmith 1986, 1987; Hopwood & Miller 1994). Each of the policy arenas mobilised the emerging



accounting category in the name of a distinct language of governing. From the perspective of accounting standard-setting, non-financial and future-oriented measurement and reporting was expected to increase the “usefulness” of annual reporting in a market setting. In turn, “usefulness” in financial reporting was increasingly seen in terms of a future-oriented, strategic perspective. That is, the provision of additional narrative statements in the annual report was understood to “better” reflect the “economic reality” of business enterprises than the financial statements alone. Similarly, corporate governance discourses drew on narrative reports as a means to realise “enhanced” corporate accountability. In line with ideas of managing for long-term shareholder-value, the concept “corporate accountability” was rephrased to embrace the consideration of a long-term perspective in managerial decision making. Finally, the language of public economic policy making explicitly embraced ideas of CSR in its programmes for enhancing economic competitiveness in the name of a “public interest”. Here, the policy debates mainly drew on accounting as a means for shaping the economic and social relations of the firm in socially responsible terms. Simultaneously, the preparation of non-financial and future-oriented reports was expected to help operationalising the objective of securing the international competitiveness of the British economy at large.

The analysis of the multiple bodies of knowledge and programmatic aspirations that have come to intersect in a category of non-financial and future-oriented accounting since the mid 1980s also helped to explain different facets of a “common knowledge” about the roles and purposes of accounting in governing economic activities. The findings from this chapter illustrate that accounting categories may be made up of a variety of practices and rationales that allow for their translatability into “solutions” for different governance “problems”. The mobilisation of accounting in local governance reform programmes reinforced different aspects of a de-localised category of non-financial and future-oriented accounting in business management.<sup>36</sup> For example, the policy reform proposals in the arena of financial reporting standard-setting placed greater weight on the role of new ways of measuring and reporting the non-financial and future-oriented aspects performance

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<sup>36</sup> On the idea that the meanings that get attached to accounting practices through language outline an expected “performative” element of accounting representations, see Miller and Rose (1990) and Rose and Miller (1992).

in terms of “shareholder value”. The corporate governance debates were mostly concerned with discharging accountability on the consideration of long-term objectives and strategic plans through narrative reporting. Finally, the reform debates in the arena of public economic policy making emphasised more explicitly the idea of a CSR business case when calling for the widespread implementation of non-financial and future-oriented measurement and reporting practices in business management and corporate reporting.

The findings on the different meanings that have been assigned to a category of non-financial and future-oriented accounting in the governance of economic life provide the background knowledge for the study of the agenda-setting processes for a voluntary and a mandatory OFR in the remainder of this thesis. Although the notion of *eventalisation* in this thesis suggests that a category of non-financial and future-oriented reporting always remains fluid and relational, the findings from this chapter seem to indicate a widely shared and largely unquestioned view of the interrelations between accounting, “strategic management”, “shareholder value” and “CSR” across the different arenas of policy making. These findings may be interpreted as part of a process of institutionalisation that establish new unquestioned “truths” about “the proper government of economic and social life” (Miller 1994b).<sup>37</sup> This view seems to be supported by the widespread rise of non-financial and future-oriented accounting as an issue for governing in the UK and internationally in the last two decades (e.g. EC 2003b; IASB 2008).<sup>38</sup> The next chapters, therefore, start from a situation where non-financial and future-oriented measurement and reporting are widely recognised as part of the accounting category and rarely questioned in regulatory reform debates. This allows for a shift from the analytical focus from the category of non-financial and future-oriented accounting to the links that form between programmes and technologies of governing.

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<sup>37</sup> Changing perceptions of the legitimate ways of reasoning and categorising accounting have also emerged outside the national British context at a *world-society* or *world-polity* level (cf. Boli & Thomas 1997; Meyer et al. 1997; Drori et al. 2003). This seems supported by the growing engagement of transnational organisations in the standardisation and regulation of additional management commentary as part of the financial reporting framework (EC 2003b; IASB 2005, 2008).

<sup>38</sup> Even strong contestation and problematisation of the mandatory OFR to be a “regulatory burden” and its ultimate abolition by the Government in 2005 (DTI 2005) could not undermine an apparently widely shared view that financial accounting could and should expand beyond the reporting in the financial statements (see, e.g. Eaglesham & Burgess 2005; Friends of the Earth 2005; Grant 2005; Phillips 2005; Tilley 2005). Following large public protest, most of the original OFR provisions were eventually re-introduced into law with the requirement for medium to large companies to prepare an “enhanced” Business Review in the *New Companies Act 2006*.



## Chapter 3

### SHIFTING THE BOUNDARIES OF ACCOUNTING STANDARD-SETTING

*“[Standard-setters] can be radical as long as we don't say we are.”*

*(Standard-setter F)*

#### **1 Narrative reporting as an agenda-issue for the ASB**

This chapter explores the process through which the “unusual” was made possible in the agenda-setting process at the British Accounting Standards Board (ASB). The publication of the *Statement: Operating and Financial Review* in 1993, significantly extended the scope of activities of the accounting standard-setter in the UK. The *OFR Statement* provided the first non-mandatory guidance for voluntary reporting by business management on the underlying financial and non-financial drivers of the operating performance and financial position of their company. The multiple ideas of governing that came to intersect in the *regulatory space* (cf. Hancher & Moran 1989b) for a voluntary OFR suggest that the process of agenda setting at the ASB in the early 1990s was part of a wider reconfiguration of the accounting regulatory world, in which the reference points for “getting accounting right” in the name of “the profession”, “the market”, and “the public interest” were realigned.

The first explicit proposals to expand the activities of the ASB to non-financial and future-oriented reporting surfaced in the early 1990s, when the British Financial Reporting Council (FRC) opened a high-level debate about *The State of Financial Reporting* (FRC 1991).<sup>1</sup> The report included the explicit recommendation by the Chairman of the FRC, Sir Ron Dearing, to consider the regulation of narrative reporting as a way to “interpret” the financial reporting figures:

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<sup>1</sup> The FRC is the independent UK regulator which is responsible for “promoting confidence in corporate governance and reporting”. As part of its work, the FRC among others oversees the work of the ASB and appoints its members (FRC 2008).

*“I should like to see greater recognition that the figures, which form the essence of accounts, need to be supported by commentaries which interpret them [...] there would be benefit from debate leading to a consensus on the characteristics of excellence in such statements, and more widely in the [annual] report as a whole.”*  
(FRC 1991, para. 22)

These concerns with “the responsibilities of directors in preparing reports and accounts” (FRC 1991, para. 4) raised questions about possibilities for a more structured provision of management commentary on the underlying drivers of the operational performance and financial position of the business. Following the high-level debate at the FRC, *The ASB’s Future Work Programme* (ASB 1991) proposed to introduce a document similar to the US and Canadian MD&A, but by means of non-mandatory guidance in a statement of best practice.<sup>2</sup> The Board’s agreement to take the project on the agenda of the ASB marked a first step towards shifting the boundaries of UK accounting standard-setting. It moved the scope of standard-setting activities beyond their traditional focus on questions of recognition, measurement, and presentation in the financial statements. It also brought concerns with additional disclosures in the annual report other than in the annual accounts closer to the “core” of financial reporting regulation; thereby blurring the boundaries between financial reporting and other forms of narrative statements, such as the statutory Directors’ Report, or the voluntary Chairman’s Statement.<sup>3</sup>

This chapter analyses the circumstances under which a wide range of reform actors agreed on the voluntary OFR as an “appropriate” agenda-issue for the ASB in the early 1990s. Building on the findings from the previous chapter, the analysis of the agenda-setting process for a voluntary OFR takes a situation as its starting point where the idea that additional narrative statements should and could provide insights into an “economic reality” of businesses remained relatively unquestioned. The statements by the ASB and the public responses to the *Discussion Paper: Operating and Financial Review* (ASB 1992) suggest that the inclusion of the OFR in the regulatory agenda of the ASB was not a question of *whether* company directors should report additional information on the underlying drivers of current

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<sup>2</sup> For further discussion of the regulatory frameworks for MD&A disclosures in the USA and in Canada, see chapter one.

<sup>3</sup> By the time of the OFR project, the annual accounts in the UK formally consisted of the Balance Sheet and the Profit and Loss Account. The requirement to prepare a Cash Flows Statement was introduced in 1996 via amendment to FRS 1.

and future performance. Instead, the question was *how* the provision of non-financial and future-oriented narratives in financial reporting should and could be regulated.

To address the question how the regulatory mandate of the ASB was extended beyond the traditional boundaries of accounting standard-setting, the analysis takes the historic specific complexes of actors and ideas that made up the regulatory authority of the ASB in the voluntary OFR event into account (cf. Miller 1990; Miller & Rose 1990; Foucault 1991b; Rose & Miller 1992; Miller & Rose 2008b). This shifts the analytical focus beyond the administrative boundaries of the ASB and focuses attention on the ways in which a variety of actors debated the roles and responsibilities of the standard-setter in dealing with a particular accounting issue. Like MacDonald and Richardson (2004), this chapter draws on the concept of *regulatory space* to emphasise the processes of constructing the identity of a private regulatory body in the interactions with other actors and demands in order to overcome uncertainty about the legitimacy of its standards and guidelines. However, the study in this chapter does not attempt to define the relative “powers” and “interests” of individual reform actors (cf. Hancher & Moran 1989b), but takes a wider, macro-level perspective on the emergence and interplay of different programmatic ideas of governing in the process of agenda-setting (cf. Miller & Rose 1990; Foucault 1991a). On the one hand, this lays out that regulatory change takes place in politically contradicting environments. On the other hand, it shifts the focus of the study to the emergence of links between *programmes* and *technologies* of government in the construction of a regulatory mandate.

Furthermore, the analysis of the process in which various actors came to agree on the OFR as an “appropriate” agenda issue for the ASB takes as its basis the idea that an overarching rationality of “getting the accounting ‘right’” (Young 1994, p. 86) provides a general mandate for regulatory intervention by accounting standard-setters. What counts as “right” accounting is, however, mediated in the situational and relational networks of a specific *regulatory space*. That is, versions of “right” accounting may change in relation to the accounting issues, actors, and ideas that

come to intersect at a certain moment in time (cf. Young 1994; Young 1995).<sup>4</sup> The notion of *logics of appropriateness* (cf. March & Olsen 1989) in this research helps to describe the expectations about the role and responsibility of a standard-setter in dealing with a particular accounting issue. These expectations surface in the historically and spatially programmatic language of accounting reform (cf. Foucault 1991d). For example, existing studies of the activities (and inactivities) of the US Financial Accounting Standards Board (FASB) have found that the Concepts Statements (often referred to as the FASB Conceptual Framework) provided the more specific reference points for considering a particular accounting issue. Accordingly, the emergence of reform programmes in financial reporting regulation in the US has been closely tied to claims to financial reporting quality criteria, such as relevance, reliability, and representational faithfulness (Young 1994, 1995, 1996, 2003). In principle, these findings are transferable to the agenda setting process at the ASB. A similar “programme for encouraging improved accounting standards” (ICAEW 1969) has also characterised the accounting standard-setting agendas in the UK since the introduction of the first British standard setting-body in 1970 (Rutherford 2007). However, the findings from the study of the OFR event suggest that *logics of appropriateness* may relate to more ideas of governing than only technical financial reporting quality criteria. The analysis of the British reform debates demonstrates the co-emergence of multiple complementary but also competing “technical”, “professional”, and “international” *logics of appropriateness*. They have been classified according to the wider ideas of governing to which the reform debates at the ASB referred when constructing the development of the voluntary OFR guidelines as an “appropriate” agenda issue. A focus on “international” *logics of appropriateness* involves the consideration of cross-border influences on ideas about the “legitimacy” of national accounting standard-setting programmes. This has been missing in previous evaluations of accounting standard setting-processes in a national *regulatory space* (Young 1994, 1995, 1996). In these studies, the construction of regulatory issues and legitimacy at the FASB appeared as a more self-referential process within national boundaries of thought. A notion of “professional” *logics of appropriateness* stresses the

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<sup>4</sup> The idea that accounting may be mobilised in the name of different programmatic aspirations at different stages of the regulatory process has been illustrated in a study of the “savings and loan crisis” in the 1980s in the US (Young 1995).

historically grown path dependencies in conceptualisations of the role and responsibility of accounting standard-setters. These may vary considerably in different institutional environments. For example, the accounting bodies in the US were historically state-founded and state-accredited. As a result, they did not achieve the same “elite” image and impact on professional conduct as the self-formed and self-regulated UK accounting bodies throughout their history (Lee 1995). However, it seems that no research has been conducted on the ways a professional self-image emerges in accounting standard-setting processes and manages the expectations of a wide range of accounting and “non-accounting” actors in financial reporting standard-setting.<sup>5</sup>

The remainder of this chapter outlines the construction of a regulatory mandate for the ASB to intervene in non-financial and future-oriented reporting. The discussion is organised in four parts. The next part introduces the key developments during the voluntary OFR project at the ASB between 1991 and 1993. Starting with a short review of the history of self-regulation of accounting practice in the UK, the second section traces the various ideas of governing in the name of “the profession”, “the State”, and “the market” that defined the position of the ASB by the time it took the OFR project on its agenda. The third section discusses the emergence and interplay of more specific *logics of appropriateness* that allowed a wide range of reform actors to agree on the voluntary OFR as an agenda-issue for the ASB. The final part summarises the findings from this study and sets forth their implications for conceptualising the inherent programmatic elements of policy reform in national accounting standard-setting.

## 2 The voluntary OFR project

*“A constructive solution requires the co-operation of three parties; standard setters, users and preparers.” (Cook 1990).*

The standard-setting process at the ASB facilitates a close internal and public dialogue with key stakeholders whilst being open to comments from other interested parties. The development of an Accounting Standard or an ASB

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<sup>5</sup> The terms “accounting” and “non-accounting” professionals are carefully used in the British context, where professionally trained accountants may retain membership with the professional bodies even if they move into “non-accounting” careers, such as business management. The absence of a business education system in the UK up to the 1970s, for instance, reinforced a mutual influence of accounting and business practice, because professional accounting qualifications were common among those who pursued a career in general management (Matthews et al. 1998).



Statement generally begins with the Board’s decision to include an issue in its work programme (ASB 2007b). The management of the project is then delegated to one of the internal project directors who work under the supervision of the Chairman and the Technical Director of the ASB. An additional panel of ad hoc consultants with representatives from accounting firms, preparers, users, and academia supports the identification of “issues” and “solutions” that will be taken before the Board for further discussion. In the next step, a Discussion Paper is prepared and issued, inviting the views of the interested public on the proposed new or revised regulation. The views expressed in the public comments, further direct enquiries and field-tests normally inform the preparation of an Exposure Draft (ED). The ED is published for further public comment before the Board reaches a final conclusion and publishes an Accounting Standard or an Accounting Statement (ASB 2007b).<sup>6</sup>

The procedures during the OFR project followed a similar approach. The only difference was that it did not call for the additional publication of an ED in the development of the voluntary guidance (ASB 1993). The internal work on the *OFR Statement* formally began in 1991 with the appointment of a Project Director who worked closely with the Chairman and the Technical Director of the ASB (Standard-setter D). In addition to a series of Board meetings, input from the “main players” in regulatory decision making at the ASB – finance directors, big accounting firms, and analysts – was generally sought through regular personal meetings “every two or three months” (Standard-setter F). The ASB also conducted a series of non-public consultations with representatives of the business community, who the ASB considered as one of the most important allies for ensuring success of the OFR project (Standard-setter E). These meetings were regarded as very helpful to secure support from analysts and the 100 Group of Finance Directors before the publication of the first discussion paper:

*“And in a way we knew we were going to win before we published, because we got people on site first.” (Standard-setter F)*

Further personal consultations with business representatives took place after the publication of the discussion paper. A small working group of finance directors

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<sup>6</sup> In contrast to Accounting Standards, ASB Statements do not cover mandatory accounting requirements, but either explain the ASB’s principles and procedures or aim at developing “best practice” in reporting outside the statutory annual accounts (ASB 2007a).

from the 100 Group was set up and met about four to five times to discuss the details of the OFR Statement. The group identified possible practical problems and developed a set of “suitable solutions” (Standard-setter D). The OFR project manager was also involved in a research project by the Institute of Chartered Accountants of Scotland (ICAS) on the views of preparers and users of the proposed OFR in 1993 (Weetman et al. 1994). The study included an analysis of the written submissions to the Discussion Paper and 20 additional interviews with professional investors, including brokers and institutional investors. The aim was to redress the “imbalance” of user and preparer submissions to the Discussion Paper and to represent a more “user-focused” perspective on OFR reporting (ibid.).

The additional behind the scene work at the ASB prior to and after the publication of the discussion paper may explain the largely positive responses to the OFR proposals in the public consultation. Overall, the 102 analysed response letters welcomed the proposals for a voluntary *OFR Statement* and rarely questioned the role and responsibility of the ASB in engaging with accounting issues beyond the financial statements (Table 1).

Category of respondent	Welcome OFR proposal	Concerned about OFR proposal	Reject OFR proposal	Other or no explicit comment	Total
Accounting profession (accounting firms)	8	1	0	0	9
Accounting profession (professional associations)	5	1	0	0	6
Preparers (company Finance Directors and professional associations)	38	5	8	6	57
Trade organisations	9	0	0	0	9
Mixed user / preparer organisations	5	0	1	1	7
Users (incl. professional and representative associations)	4	1	0	0	5
Law profession	2	0	0	1	3
Individuals	2	0	0	1	3
Other	3	0	0	0	3
Total	76	8	9	9	102
	74%	8%	9%	9%	100%

Table 1: Responses to the *Discussion Paper: Operating and Financial Review* (ASB 1992)

A majority of 76 out of 102 (74%) respondents generally welcomed the proposals for a voluntary OFR. They included explicit support from eight out of nine (88%) accounting firms, from 38 out of 57 (66%) potential preparers of OFRs (including

finance directors and their professional associations), and from five out of the six professional organisations that had submitted a response letter. Even though they did not entirely reject the OFR proposals, eight (8%) of the total response letters expressed severe concerns about the proposed Statement. They supported additional reporting in an OFR in principle but questioned the proposed responsibility of the ASB for regulating disclosure outside the financial statements. For example, the Chartered Association of Certified Accountants (ACCA) generally welcomed additional commentary on underlying corporate performance, but strongly criticised the ASB for prioritising work on the OFR over the other accounting issues from its original 1991 Work Programme, such as off-balance finance, goodwill, or consolidation. In addition, the ACCA expressed doubts about the effectiveness of the proposed voluntary OFR and called for formal legal backing:

*“This is a disappointing draft. As the proposals are not mandatory it is difficult to see how they will be implemented given the broad and discretionary framework that the discussion draft proposes.” (ACCA letter to the ASB, 16 July 1992)*

The accounting firm Touche Ross & Co argued that the additional disclosures did “not fall within the scope of accounting standards” and should be dealt with by the FRC as part of its work on corporate governance.<sup>7</sup> The response from the Group of Scottish Finance Directors questioned the need for additional reporting and commentary from the point of view of directors, pointing out that this was already sufficiently covered by other channels of communication.<sup>8</sup> Finally, one preparer and one professional investor argued that reliance on market forces was sufficient and that no further regulatory intervention by the ASB was needed.<sup>9</sup> Only nine (9%) of the respondents explicitly rejected the proposals in the Discussion Paper. They were mostly received from potential preparers of OFRs. One of the preparer-companies, for example, explicitly questioned the general ability of accounting and additional narrative statements to reflect the dynamics of business as, according to them, more reporting would open the potential for “hiding” rather than “revealing” information about the business.

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<sup>7</sup> Touche Ross & Co letter to the ASB, 8 July 1992.

<sup>8</sup> The Group of Scottish Finance Directors letter to the ASB, 15 July 1992.

<sup>9</sup> Boustead plc letter to the ASB, 22 July 1992; S.G. Warburg Group Management Ltd. letter to the ASB, 13 August 1992.

In the light of the numerous positive responses and the comparatively few points of criticism, the ASB issued the *Statement: Operating and Financial Review* in 1993. This marked a durable shift in the scope of accounting standard-setting in the UK. The issue of non-financial and future-oriented reporting has stayed on the agenda of the ASB to date and may be one of its proudest contributions to financial reporting regulation and practice (Standard-setters C, D, E, and F). A “routine update” (Metcalf 2002) of the 1993 *OFR Statement* took place in 2002. The revised *OFR statement* included the explicit recommendation to identify financial as well as non-financial “key performance indicators” including reporting on environmental and social issues (ASB 2003a). Its publication in January 2003 coincided with emerging proposals for a mandatory OFR from the Company Law Review Steering Group, which will be further discussed in the next chapter (Metcalf 2002). Despite the repeal of the *OFR Regulations* shortly after their enactment in 2005, the ASB still provides non-binding voluntary guidance for reporting in the mandatory Business Review according to the new *Companies Act 2006* in the *Reporting Statement: Operating and Financial Review* (ASB 2006).

The discussion in the next section highlights the various programmatic aspirations that have come into play in defining the roles and purposes of the accounting standard-setter in the OFR event. Placing the work of the ASB in the early 1990s in a wider historic and political context helps to shed light on the conditions of possibility for the expansion of the scope of the regulatory mandate of the ASB.

### **3 Ideas of governing in UK accounting standard-setting**

The general “need [of accounting standard-setters] for a public legitimacy and rationale for action” (Burchell et al. 1980, p. 10) has been attributed to their “uneasy [position] between the accounting profession and the state” (Young 1994).<sup>10</sup> This is believed to pose a dilemma for the production of accounting standards as they can neither rely on claims to “professional expertise” and “independence”, nor on a democratic mandate as sources of authority (Hopwood 1983a, p. 84). Similarly, the members of the OFR Working Group at the ASB interpreted the early 1990s as a particularly challenging time (Standard-setters D, E, and F). Although the ASB was

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<sup>10</sup> Other studies have suggested that pressures for accounting change may also arise through further interventions by general media, academia, or strong individual personalities (Burchell et al. 1980; Sikka & Willmott 1995; Rutherford 2007, pp. 8-12 ).

recognised by the *Companies Act 1989* as the responsible standard-setting body, the accounting standards themselves were not authorised by parliamentary approval (Baldwin & McCrudden 1987). To be effective, they needed to be in line with the programmes of those who sought to govern through accounting standards and also needed to be accepted by those who were supposed to be governed:

*ASB knew that its objective of improving financial reporting needed more than the statutory backing for accounting standards: it needed a commitment from all sides of the financial community to work for such an improvement and to support the standard setting process.”*  
(Standard-setter E)

The remainder of this section reviews the rise and realignment of interconnected rationales of governing that shaped the history and identity of accounting standard-setting in the UK in relation to a series of national and international developments. The broad distinction between ideas of governing in the name of “the profession”, “the State”, and “the market”, helps to structure the multiple demands that were placed on the regulation of accounting practice before and after the creation of the ASB in 1990.

### **3.1 The rise of “professional” self-regulation**

Ideas of self-regulation by the accounting bodies traditionally played a central role in the regulation of the technical procedures of accounting and auditing in the UK. They have been characterised by general notions of “independence” and “expertise” that were supposed to legitimise the practice recommendations of the accounting bodies (Robson et al. 1994). However, claims to self-regulation have been caught up in political, economic, and social changes throughout the 20<sup>th</sup> century. These encounters between “the profession”, “the State”, and “the market” brought about various shifts in the rationales that guided standardisation projects in accounting.

The first accounting institutes in Great Britain were established as self-formed professional organisations in the second half of the 19<sup>th</sup> century. They were granted royal permission for self-regulation of membership and conduct (Lee 1995).<sup>11</sup> Until

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<sup>11</sup> The first Scottish institutes were formed in 1853 and 1867. They merged into the Institute of Chartered Accountants in Scotland (ICAS) in 1951. The Institute of Chartered Accountants in England and Wales (ICAEW) was formed in 1880 following the merger of four provincial societies with the Society of Accountants in England. The Institute of Chartered Accountants in Ireland (ICAI) was established in 1888 (Edwards 1989, p. 277).

about the middle of the 20<sup>th</sup> century, the system of professional self-regulation provided the main mode of control in the market for accountancy services in Britain. This system was characterised by a generally informal, cooperative and discrete regulatory culture. The members of the chartered institutes were able to build a professional reputation and social standing on the basis of claims to knowledge in the areas of accounting, auditing, tax, as well as legal and business issues. Notions of “professionalism” were also carried into practice through a system of training and education for the members of the accounting bodies (ibid.). Accordingly, the regulatory authority of the accounting bodies largely arose from public trust in expert elites and their close and informal networks of control and communication (Baggott 1989; Lee 1995).<sup>12</sup>

Throughout the history of the chartered accounting bodies however, the roles and self-regulatory powers of the accountancy profession in the UK were always at least loosely tied to a public interest rationale (Hopwood 1983a).<sup>13</sup> From early on, accountants based their professional identity on claims to a “social contract” between their occupation and the wider public. This meant that the services of the members of the accounting bodies were traditionally linked to ideas of supporting processes of corporate accountability for the benefit of society at large (Robson et al. 1994). A more explicit alignment between the system of professional self-regulation and public policies and regulations developed around the beginning of the 20<sup>th</sup> century. By that time, the formal ties between accounting practice and company law began to grow closer (Hopwood 1983a).<sup>14</sup> Statutory accounting and reporting requirements in the *Companies Consolidation Act 1908* and the *Companies Act 1929* introduced a minimum level of recording and reporting (Noguchi & Edwards 2004), including the presentation of an audited balance sheet and the publication of a profit and loss account (Edwards 1989, pp. 128-130).<sup>15</sup> The relative stability of these arrangements between “the profession” and “the State” has been identified as one of the key reasons for there being little explicit engagement

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<sup>12</sup> For further discussion of the role of self-regulation in British regimes of governing throughout the 20<sup>th</sup> Century see, e.g. Baggott (1989), Baldwin et al. (1998b), or Ogus (1998).

<sup>13</sup> For a critical perspective on the public interest implications in the formation of the profession see, e.g. Willmott (1986).

<sup>14</sup> For further discussion of the interrelations between accounting and law, see chapter four.

<sup>15</sup> Basic publicity requirements to file annual accounts with the Registrar of Companies had already been introduced by the Joint Stock Companies Act 1844 (DTI 1998b).

by “the accounting profession” in standard-setting activities until the 1940s (Lee 1995) and for little regulatory control of accounting practice in company law (Edwards 1989, pp. 126-127).

A major shift in the relation between accounting and “the State” occurred in the 1940s, when a notion of “professionalism” was questioned in the light of the presumed public interest-role of accounting (Napier & Noke 1992). Early accounting scandals in the 1930s and 1940s had called into question a general reliance on professional elites, who were trusted to serve the “public interest” by guaranteeing competent services (Lee 1995).<sup>16</sup> The ICAEW responded to the criticism with the publication of a series of *Recommendations on Accounting Principles* from 1942 onwards (ICAEW 2009). In addition, the introduction of the *Companies Act 1947* and the *Companies Act 1948* formally ended the prior liberal rationale in accounting regulation (Noguchi & Edwards 2004). The new legislation significantly expanded statutory disclosure provisions and audit requirements (Edwards 1989, p. 209).<sup>17</sup> At the time, the shift towards regulatory formalisation in company law was, however, still largely supported by the accounting bodies. They interpreted statutory regulation of accounting practice as a way to complement their efforts to secure and expand the scope of their responsibilities (Robson et al. 1994; Noguchi & Edwards 2004).

### **3.2 Self-regulation in the name of “the public” and “the market”**

Throughout the 1970s, the status quo between “the profession” and “the State” in the accounting regulatory regime in the UK fundamentally changed. Another series of accounting scandals in the 1960s had called into question the extent to which the various accounting institutes could reliably provide accounting information that met the demands and expectations of various constituents (Rutherford 2007pp. 2-8).<sup>18</sup> The accounting bodies followed the public critique with proposals for greater

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<sup>16</sup> The *Royal Mail Steam Packet* case of 1931, in which the issuance of false accounts was supported by the company’s auditor, was one of the most prominent cases that caused corporate accountability concerns and eventually led to increased reporting requirements in the *Companies Act 1948* (Patent 1992).

<sup>17</sup> For instance, specific headings for disclosure in the balance sheet and the profit and loss account were specified. The audit requirement was expanded to cover the profit and loss account. Formal responsibility for conducting an audit was located with the members of the professional institutes (Edwards 1989, p. 209).

<sup>18</sup> Three of the most prominent accounting scandals of the time were the collapse of Rolls Razor Limited in 1964, the takeover of Associated Electrical Industries Limited (AEI) by General Electric Company (GEC) in 1967, and the failed Pergamon-Leasco takeover in 1969 (Rutherford 2007, pp. 2-8).

standardisation of accounting practice in the system of professional self-regulation in an attempt to regain public trust and to silence public calls for stricter legislation (Rutherford 2007, pp. 12-13).<sup>19</sup>

The ICAEW (1969) *Statement of Intent on Accounting Standards in the 1970s* set out a programme for developing a set of standards for more consistent financial reporting in the UK. This included proposals for replacing the system of non-binding and non-standardised guidelines which existed then and which had, until then, been issued by the individual British professional accounting institutes with a regime of jointly devised standards (Blake & Lunt 2001, pp. 1-2).<sup>20</sup> Eventually, the Accounting Standards Steering Committee (ASSC) was created in 1970 as the first professional standard-setting organisation in the UK (Rutherford 2007). Following amendments to the constitution of the ASSC in 1976, the name of the standard-setting body was changed to Accounting Standards Committee (ASC).<sup>21</sup> Under the new system, standard-setting remained under exclusive control of the UK accounting bodies and without official recognition by Government (Turley 1992; Zeff 2007b). Nevertheless, programmatic ideals of acting in the name of “the State” and “the markets” increasingly influenced the activities of the standard-setter.

Around the time of the creation of the ASC, definitions of the roles and purposes of financial reporting began to shift away from a traditional stewardship-perspective towards an emphasis on the “users” and “usefulness” of financial accounts for economic decision-making in a capital market setting (Hopwood et al. 1990, p. 76). Although ideas of financial reporting as a means of disclosing “relevant and efficient information for investor decision-making” had already accompanied the accounting reforms in the 1940s (Noguchi & Edwards 2004), the rise of a neo-liberal paradigm in British policy thought further strengthened aspirations to define the subjects and objects of governance in economic terms (Robson et al. 1994). The emphasis on autonomy and decision-making in economic governance also brought

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<sup>19</sup> Rutherford (2007, p. 13) highlights that the Government itself did not explicitly suggest intervening in professional conduct by means of legislation. Yet the profession felt that even the possibility that Government could change its views already created sufficient pressure for a greater degree of standardisation in the system of professional self-regulation.

<sup>20</sup> Enforcement of the standards was supposed to be based on a comply or explain approach in the statements themselves or if they failed to do so in the audit report (Rutherford 2007, p. 41).

<sup>21</sup> The 1976 amendments allocated greater responsibility for the initial drafting of standards to the ASC itself, lessening the role of the individual professional bodies (Rutherford 2007, p. 120).



the focus on the “functioning” of capital markets in line with the public interest-role of accounting standard-setting (Willmott et al. 1993; Robson et al. 1994; Cooper & Robson 2006). That is, the system of professional self-regulation was expected to support “the efficient working of the commercial sector” (Rutherford 2007, p. 13).

The internationalisation of national accounting practice was another important influence on UK accounting standard-setting after the 1970s. This was brought about by the increasing economic interaction between the UK and the US (ibid., p. 17) as well as the accession of the UK to the European Union. The former denotes some form of awareness of international developments in accounting regulation prior to explicit transnational harmonisation projects or active cross-country cooperation on financial reporting reform (Hopwood 1989a).<sup>22</sup>

*“Accounting has never been a purely national phenomenon. [...] both its techniques and the significances that are in part created by them have a history of penetrating national boundaries, moving along the pathways established by commerce and patterns of political influence.” (Hopwood 1989b, p. 1)*

The British accession to the European Community in 1972 was a turning point for the British accounting institutes and the relatively high degree of national autarchy they had enjoyed (Napier & Noke 1992).<sup>23</sup> The supra-national standardisation projects of the European Commission (EC) emphasised a more legalistic approach to accounting regulation, which was typical of Continental Europe. This approach also included formal restrictions on the scope of activity undertaken by UK standard-setters (Bromwich & Hopwood 1992). The transposition of requirements for the form and content of company accounts from the Fourth (EEC 1978) and Seventh (EEC 1983) European Company Law Directives into UK legislation, for example, increased the influence of statutory provisions in the regulation of accounting practice.<sup>24</sup>

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<sup>22</sup> Examples of international intellectual influences that were independent from the explicit standardisation and harmonisation projects by transnational regulators and standard-setters include the attention paid to the Conceptual Framework project at the FASB since the 1970s by British accounting standard-setters (Tweedie & Whittington 1990) or direct references to Canadian and British developments in the US Jenkins Committee report on “Improving Business Reporting” (AICPA 1994, appendix IV).

<sup>23</sup> For a discussion of the “Europeanisation” of national governance following the deliberate decisions of nation states to participate in the creation of an integrated European market, see Fligstein and Merand (2002).

<sup>24</sup> For further discussion on the changing interrelations between law and accounting in the UK see chapter four.

### 3.3 A new system for accounting standard setting at the ASB

The re-positioning of accounting standard-setting at the intersection of three ideas of governing –professional standards, a public interest, and growing concerns with user-needs in a capital market-setting – was accompanied by a decline in public trust in the self-regulatory system of the accounting profession. A series of widely publicised scandals in the mid 1980s, such as the “Guinness scandal” (1986) and the US insider trading scandals involving Ivan Boesky and others (1986), had exposed the members of the accounting profession to even greater public scrutiny. Around the same time, businesses, the Stock Exchange, and even accounting firms in the UK began to strongly question the role, authority, and ability of the ASC to develop “acceptable” standards for financial reporting. Standard-setting was a particular target of their criticism (Hopwood et al. 1990; Turley 1992). Standards at the ASC had to be passed and endorsed by each of the six UK accounting institutes (Zeff 2007b). This was criticised as a complex and time consuming process (Standard-setter F). The exclusive control the profession had over accounting practice was further targeted by the competition policies of the Thatcher Government. Those policies were aimed at opening up the professional networks of the accounting profession and business leaders (Lee 1995; Worcester 2002).

The *Dearing Committee* was established in 1987 by the Consultative Committee of Accountancy Bodies (CCAB) to address perceived structural problems of standard setting and to find ways to restore trust in accounting standards (Turley 1992).<sup>25</sup> The *Dearing Report* (ICAEW 1988) proposed a new system for accounting standard-setting which demanded broader formal commitment from preparers, users, and auditors of financial statements. These proposals were further developed in the *Guidelines for Financial Reporting Standards* (Solomons 1989). Following the recommendations in these reports, the *Companies Act 1989* introduced substantial changes to UK accounting standard setting. Within the new system, the development of accounting-standards became a joint responsibility for the accounting bodies, large accounting firms, industry, the financial community, and the Government (Turley 1992). In 1990, the *Companies Act* recognised the ASB as the only formally independent accounting standard setting-body in the UK in

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<sup>25</sup> The CCAB was formed in 1974 as a forum for regular exchange between the accounting bodies that were involved in the work of the ASSC (Rutherford 2007, p. 35).

1990.<sup>26</sup> The ASB itself was created as a private company limited by guarantee and funded by the accounting institutes, the Department of Trade and Industry (DTI), the London Stock Exchange and the banking community (Turley 1992). The first members of the Board included a Chairman and a Technical Director, both working full-time and with a strong accounting background. The ASB was further made up of seven part-time members; three from large accounting firms, two from industry, one from the financial community, and one from a regulatory agency (ibid.). The FRC was established as a state-accredited umbrella body to supervise and oversee the preparation and enforcement of financial reporting standards. Its members came from the business and the accounting community (Lee 1995).

The new framework for accounting standard-setting in the UK was supposed to ensure the standards held authority with the business and the public (Bromwich & Hopwood 1992) even though the standards themselves were not legally binding (FRC 1991).<sup>27</sup> At the same time, the membership and sponsorship structure of the ASB was meant to make the standard-setting process more transparent by formally positioning the work of the ASB between public interest controls and direct accountability to its sponsors (Davies 2003, p. 51). The structure was devised to overcome problems with low credibility and legitimacy of exclusively profession led standards (Hopwood et al. 1990; Turley 1992) and to rebuild trust in the adequacy of accounting standards to serve “public interests” (Rutherford 2007). Nevertheless, the ASB’s lack of formal hierarchical authority to enforce reporting standards has been taken as creating a “need” for securing wide-ranging support from those stakeholders who have the potential to question the legitimacy of the standards (Brunsson & Jacobsson 2000a, p. 2). In addition, a series of acute business failures, such as the spectacular “Maxwell collapse” in 1991 (DTI 2001), continued to put in question the legitimacy of the British system for accounting standard-setting at just the time that the OFR project was being launched.

*“To govern, one could say, is to be condemned to seek authority for one’s authority.” (Rose 1999, p. 27)*

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<sup>26</sup> Section 256 CA 1985.

<sup>27</sup> The position of the ASB was further strengthened in the new governance arrangement as the courts tended to interpret compliance with the legal “true and fair” requirement in line with the adherence to “professional” standards (Davies 2003, p. 543). However, there is no so called “statutory rebuttable presumption” that accounting standards should be followed in any case (FRC 1991).

This short review of the various ideas of governing which have come into play in accounting standard-setting suggests viewing the ASB's "uneasy position" in the context of wider historical, social and international developments. The reference points for accounting standard setting since the formation of the ASSC in 1970 have been provided by various ideas of governing. They include programmes of governing in the name of "the profession" and a "public interest" as well as ideals of "efficiency and effectiveness" in a market setting. These programmes have been realigned over time – driven by a series of national and transnational developments, and a general decline of public "trust" in the system of self-regulation by the accounting profession. The next section outlines how these wider ideas of governing became connected to ideas of non-financial and future-oriented accounting in the agenda-setting process for a voluntary OFR at the ASB. Furthermore, the next section illustrates how these links were strengthened and legitimised in the processes in which a set of interrelated *logics of appropriateness* co-emerged and at times challenged each other in the regulatory reform debates.

#### **4 Mediating "appropriateness" in the agenda-setting process**

The study of the OFR event at the ASB suggests that agreement on voluntary non-financial and future-oriented reporting as an agenda-issue for the ASB was made possible by the interplay of three perspectives on the role and responsibility of the ASB in dealing with non-financial and future-oriented reporting: "Technical" *logics of appropriateness* were characterised by a perceived responsibility to ensure "quality" in financial reporting practice. Secondly, theories of the relative position of the OFR project in relation to regulatory developments in the USA and Canada emerged as "international" *logics of appropriateness*. Finally, a "professional" dimension of *logics of appropriateness* was defined by a professional self-consciousness that was shared by the various actors in the accounting standard-setting process. The emergence of each of these *logics of appropriateness* and their points of congruence and disagreement in the agenda-setting debates are outlined in the following paragraph.

##### **4.1 Technical logics of appropriateness**

Studies of accounting standard-setting in the US have concluded that references to the diversity in accounting practice are a key element in the processes of constructing "accounting problems" and "solutions" in the agenda-setting process at

the FASB. In these cases, “problems” with accounting practice related to a general expectation that published accounts should meet a set of technical quality criteria, such as comparability, consistency, relevance, or reliability, which had been formally outlined in the FASB Conceptual Framework (Young 1994).<sup>28</sup> References to institutionalised quality criteria in the rhetoric of accounting standard-setting have supported a technical “myth of accounting objectivity” in the standard-setting process and provided the basis for authority and acceptance for new accounting regulations (Young 2003). The different formal institutional arrangements in the US and the UK may arguably limit the transferability of these findings regarding the role of conceptual framework criteria in facilitating “appropriateness” in agenda-setting to the specific situation at the ASB. The *Conceptual Framework* project in the US has a much longer history than the UK *Statement of Principles*. It was launched in 1973, the same year the FASB started work. The first of seven *Statements of Financial Accounting Concepts* (SFAC) was issued in 1978 (Gore 1992). In contrast, the ASB did not issue the first official *Statement of Principles for Financial Reporting* (ASB 1999) in the UK until 1999. Until that date, the “true and fair” requirement for financial reporting provided the only formal boundaries for British standard-setters. This left more room for judgement in the preparation of financial accounts and supported a principles-based approach to UK accounting standard-setting (Parker 1989; Kirk 2001).<sup>29</sup> Nevertheless, similar ideas of financial reporting “quality” have played a central role in the process of accounting standard-setting in the UK since the 1970s. There was an increasing interest in the development of “systematic principles” to address “problems” with financial reporting practice around the same time as the conceptual framework debates emerged in the US (Tweedie & Whittington 1990). The development of a framework of principles against which accounting standards could be judged was part of the programmes for “strengthening” accounting standards in the newly created system of financial reporting standard setting at the ASB (FRC 1991). The

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<sup>28</sup> The first FASB Concept Statement as of 1978 dealt with the *Objectives of Financial Reporting by Business Enterprises*. FASB Concept Statements No. 2-6 (including the Concept Statements *Qualitative Characteristics of Accounting Information* and *Recognition and Measurement in Financial Statements of Business Enterprises*) were issued by 1985. The most recent Concept Statement No. 7 *Using Cash Flow Information and Present Value in Accounting Measurements* was issued in the year 2000 ([www.fasb.org](http://www.fasb.org)).

<sup>29</sup> The principles-based approach in the UK contrast a more rules-based US-approach that – in the absence of a authoritative definition of “true and fair” – required conformity with generally accepted accounting principles (GAAP) (Parker 1989; Kirk 2001).

ASB developed a set of informal criteria at an early stage. They were based on the recommendations for more formalisation of framework principles in the *Dearing Report* (ICAEW 1988). This guided the internal work of the ASB until the official publication of the *Statement of Principles* (ASB 2009) and also influenced conceptualisations of “quality” in the OFR project.

The debates about voluntary OFR guidelines were based on the perception that the financial statements failed to sufficiently represent “relevant” economic matters. This failure was believed to make it difficult to operationalise a “decision-usefulness” criterion in financial reporting (ASB 1992, para. 7). In line with the earlier arguments put forward by the professional accounting bodies with respect to expanding the scope financial reporting (cf. chapter two), the project team at the ASB identified a divergence between the reporting practice of listed UK companies and emerging notions of “best practice” in financial reporting. This was viewed as a general “weakness of UK reporting at the time” (Standard-setter D). This view was shared by the members of the Board, who recognised an increasing complexity of corporate activities as a limitation to representing underlying “economic reality” in the financial statements alone (Standard-setter F). Accordingly, the inclusion of the OFR on the regulatory agenda of the ASB was constructed as a regulatory “solution” that was supposed to contribute to “improving” financial reporting in two ways: The introduction of the voluntary *OFR Statement* was supposed to “enhance” the “quality” of information in the financial reporting package at large by complementing and explaining the information provided in the financial accounts. Secondly, by linking the *OFR Statement* to financial reporting quality criteria, perceived inconsistencies within current narrative reporting practice were to be eliminated and a framework for being candid about “good news” as well as “bad news” was to be provided (Standard-setters D and F).

*“The Accounting Standards Board (ASB) is of the firm opinion that the quality of financial reporting of major companies in the United Kingdom would be enhanced by the inclusion in annual reports of an Operating and Financial Review (OFR) in which management might take the opportunity to discuss in a structured way some of the main factors underlying the performance and financial position portrayed in the financial statements.” (ASB 1992, para 1)*

The ASB saw its responsibility in the OFR project in relation to its role in ensuring the provision of “improved” information to capital markets (Standard-setter E). Reliance on market forces was considered insufficient to guarantee a balanced presentation of the underlying “economic reality” of the business in voluntary statements (Standard-setters D and F). In relation to that idea, the debates at the ASB criticised the practice of voluntary narrative reporting used at the time for its presumed tendency to favour “fair weather” reporting. In addition, existing voluntary reports such as the Chairman’s report, were criticised for a lack of balance and quality in the disclosure of information on the underlying non-financial factors that may affect the future of the business (Standard-setter D and F).

*“You don’t often understand the true story behind them, the numbers, and in those days, the sort of narratives that you got in Chairmen’s reports were very biased and one-sided. [...] certainly at that time, we felt that there was scope for considerable improvement in the quality of information.” (Standard-setter D)*

The introduction of voluntary guidelines for non-financial and future-oriented reporting was expected to help promote “best practice” in business management and reporting (Standard-setters D and F).

*“What we’re after is management going behind the numbers and helping people understand their business.” (ASB Chairman in Financial Times 30.04.1992, p. 22)*

The alignment of voluntary reporting practice with the guidelines in the proposed *OFR Statement* was supposed to provide “a way of clearing a path through a rather difficult, complex set of accounts, and telling you what’s going to happen” (Standard-setter F). The objective of giving greater visibility to the underlying drivers of financial reporting numbers was further associated with the more general idea of meeting “the objective of financial statements as stated in the ASB’s draft Statement of Principles” (ASB 1992, para. 2). This included a distinction between an overarching objective of financial statements to provide “useful” information to investors for economic decision-making and traditional stewardship purposes and more specific quality standards, including the principles of relevance, reliability, comparability, and understandability (ASB 1999). The deliberate decision of the OFR project team to link its further work on the *OFR Statement* with the emerging *Statement of Principles* (Standard-setter D) was aimed at creating greater

consistency between the project and the overall objective of the ASB to ensure high standards of quality in financial reporting for the benefit of current and future shareholders (ASB 1993, para. 3; Weetman et al. 1994).<sup>30</sup>

Despite the emphasis on financial reporting quality criteria in the publications of the ASB and the personal statements of the members of the working group, there were only few explicit references to financial reporting quality criteria in the public responses. For example, only six (8%) of the 77 respondents who welcomed the introduction of the OFR Statement also mentioned specific financial reporting quality criteria.<sup>31</sup> This suggests that the proposed links between the OFR and technical quality criteria had remained relatively unquestioned. Nevertheless, the proposals for voluntary OFR guidelines were not readily accepted. They were challenged by the participants in regulatory space based on concerns with developments in the US and expectations about historically grown conventions in UK accounting standard-setting. The emergence and interplay of these “international” and “professional” *logics of appropriateness* in the process of agenda-setting for a voluntary OFR is further discussed in the remainder of this section.

#### **4.2 International logics of appropriateness**

The ASB’s internal work on the OFR Statement formally began in 1991 with an analysis of existing MD&A requirements in the US and Canada by the Project Director (Standard-setter D). This was supposed to provide a starting point for the development of a regulatory framework by the ASB that would help meet the objective of “enhanced” market communication through accounting standard-setting. Accordingly, the existing North American regulatory regimes not only inspired the drafting of the British OFR (*ibid.*), but elements from the MD&A were also included in the initial OFR discussion paper (ASB 1992, para. 22).

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<sup>30</sup> The internal use of the informal framework prior to the official publication of the *Statement of Principles* in 1999 was supposed to overcome a perceived lack of consistency and comparability of emerging financial reporting practices which was seen to “contradict the principle of standardisation” (Tweedie & Whittington 1990, p. 87).

<sup>31</sup> The comment letters were submitted by Coopers & Lybrand, BAT Industries plc, Royal Dutch / Shell Group of Companies, Unilever plc, Ranks Hovis McDougall plc, Institute of Investment Management and Research (today CFA Institute).



*“It sounded a sensible thing to put in. A lot of the detailed points [in the OFR Discussion Paper] were very similar to what the US and the Canadians were asking for.” (Standard-setter D)*

The similar programmatic aspirations to “the market” and to “improving” market communication inherent in the North American requirements for additional narrative management commentary may explain the initial appeal of the MD&A as a role model for the British standard-setting debates (Sahlin-Andersson 1996; Sevón 1996).<sup>32</sup> This interpretation is supported by a set of positive responses to the 1992 Discussion Paper welcoming a cross-border perspective in the development of a regulatory framework for narrative reporting in the UK. Six submissions explicitly welcomed a move towards the US approach as a step towards greater international harmonisation of accounting standards which they thought would increasingly benefit international businesses.<sup>33</sup> Other respondents to the public consultation, such as the ACCA, viewed a move towards the US regime as a way to integrate an already “more workable” and “specifically drafted” approach (ACCA letter to the ASB, 16 July 1992). Interestingly, the exemplary role of the North American frameworks was limited to the observation that requirements for narrative reporting had been introduced at all. Apart from that, the debates in the OFR regulatory space strongly criticised the institutional design of the MD&A regimes and particularly questioned the “effectiveness” of the US approach. “Legalistic”, “coercive”, “boilerplate”, and “burdensome” were some of the adjectives used in comment letters and by the ASB to criticise the US regime in action. Potential preparers of OFRs, including finance directors and their representative organisations, were particularly vocal in criticising the MD&A regime for its inflexible format and compliance-based approach to supplementary reporting.<sup>34</sup> Seven of the response letters, which otherwise welcomed a general move to greater consistency in international reporting, expressed concern that a similar approach in the UK would

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<sup>32</sup> Sahlin-Andersson (1996) proposes a role for joint *reference systems* in the intra-organisational travel of ideas. Similarly, Sevón (1996) talks about “thought worlds” of organisations within the same “activity field”. Joint references to a shareholder paradigm in the UK and North America may also explain why the Discussion Paper did not refer to other narrative reporting regimes, such as the German *Lagebericht*, which had grown out of a stakeholder paradigm in corporate accountability (Engelen 2002).

<sup>33</sup> They include letters from the Investor Relations Society, the Chartered Institute of Management Accountants (CIMA), the Chartered Association of Certified Accountants (ACCA), British Gas plc, English China Clays plc, and Willis Corroon Group plc.

<sup>34</sup> They include, for example, the replies from BAT Industries plc; Standard Platforms Holdings plc; Titon Holdings plc.

result in mechanistic and “bland” reports which would fail to give more insight into the “economic reality” of companies.<sup>35</sup>

The ASB project manager also reviewed the general status quo of compliance in the US. After additional internal consultation with members of the 100 Group of Finance Directors on their experience with MD&As under the regime of the Securities and Exchange Commission (SEC), the ASB eventually decided to adopt only “sensible” parts of the North American rules (Standard-setters D and F). The OFR regime in the UK was supposed to deliberately depart from the “prescriptive” tone of the American regulations (ibid.).

*“We were trying to get away from the US approach, which was very much [...] a long list of things you had to put in and it didn't really say why you were doing it. [...] Looking at a lot of MD&As at the time, they were just disjointed paragraphs [...] But there wasn't any sort of coherent story behind the numbers.” (Standard-setter D)*

*“We were very scared [the OFR] would become a boilerplate document. You know, like the MD&A - with the lawyers all over it.” (Standard-setter F)*

*“We wanted not to get the list of things they need to talk about but to say what is the sort of main message behind what's happened last year and explain that in sufficient detail. [...] what we wanted was management to tell their story. [...] to give the whole picture.” (Standard-setter D)*

The debate centred on the conflict between technical and international points of reference in the construction of “appropriateness” for the voluntary OFR project. The actors in the OFR regulatory space agreed that meeting the objective of ensuring “quality” in OFR reporting in order to “improve” financial reporting overall would require a departure from the idea of international harmonisation. The decision in favour of a voluntary Statement was seen as an opportunity to gradually raise awareness and acceptance for the new type of statement (Standard-setter F). There was a general view at the ASB that standard setters should give companies

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<sup>35</sup> Comments explicitly criticising the US MD&A regime as a model for the UK were for instance received from Cadbury Schweppes plc, Medeva plc, Ranks Hovis McDougall plc, SmithKline Beecham plc, the Confederation of British Industry (CBI), the Institute of Directors (IoD) and the Scottish and the Midlands groups of finance directors.

“room to breathe”, and that they should encourage experimentation in voluntary reporting instead of “rushing in with new standards” (Cook 1990).<sup>36</sup>

*“[W]e thought: Well rather than lose it, let’s try and get best practice to force it through. So that’s why we did it as a [...] Statement [...]. So we just put that out as best practice and it caught on.” (Standard-setter F)*

The explicit departure from the North American MD&A model seems to contradict the view that regulatory design often mirrors other regulatory arrangements by imitating rules and institutions from countries with great economic and political power (Hancher & Moran 1989b, p. 160f).<sup>37</sup> The next section further analyses the turning point at which positive references to the MD&A regimes in North America gave way to severe criticism. It outlines the debates in which the international points of reference were compared and contrasted with a professional self-image of accounting standard-setting in the UK.

### **4.3 Professional logics of appropriateness**

A perceived discrepancy between the role of the accounting profession in accounting reform in the US and the UK made it possible for the actors in the OFR regulatory space to agree on a deliberate departure from the institutional structure of the North American model. The “professional” self-image of accountancy in the UK has traditionally been characterised by a language of neutrality and independence in the self-regulation of accounting practice (Cooper et al. 1994). “Professionalism” was also linked to an “entrepreneurial” mentality in the development of accounting practice (Robson et al. 1994, p. 530). Although the standard-setting process at the ASB was no longer exclusively controlled by the accounting bodies, similar perceptions of “professional independence” and “thought leadership” were maintained in the language outlining the role of the ASB in taking regulatory action in the area of non-financial and future-oriented reporting. The connection of the proposed OFR regime with points of reference relating to

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<sup>36</sup> The final *OFR Statement* also included an “escape clause” for commercially sensitive information in the final OFR Statement (ASB 1993). Its insertion into the guidelines took account of a particular concern about questions of confidentiality that finance directors and the Law Society had voiced in both the public and the internal consultations (Weetman et al. 1994; Standard-setter D).

<sup>37</sup> This also seems to contrast a theory of *institutional isomorphism* according to which organisations in dynamic and uncertain environments (DiMaggio & Powell 1983) will copy the structure of other seemingly “successful” organisations with similar organisational forms and within similar external conditions (Hannan & Freeman 1977).

conventional aspects of standard-setting by the British accounting profession was seen to be more in line with the emerging technical focus on the “quality” of UK financial reporting. The historic trajectories of accounting standard-setting in a system of self-regulation by the accounting bodies was also seen to conflict with the North American approach to regulating disclosure in the MD&A. In addition to the criticism of the MD&A regime for not meeting technical quality criteria if implemented in the UK context, the reform debates at the ASB further questioned the general compatibility of the US regime in regulating financial reporting and additional disclosures with UK traditions.

Under US legislation, the SEC, a US Government agency, has authority over the regulation of disclosures by listed companies. The SEC in turn delegates most responsibilities to the FASB. (Bromwich & Hopwood 1992; Lee 1995). Within that system, the responsibilities of the FASB were limited to the standardisation of financial reports, whereas responsibility for other mandatory disclosures, such as the MD&A, remains with the SEC. Individual states also regulate accounting practices by means of legislation (Lee 1995). Under this “top-down” approach to accounting regulation, Congress retains its right to intervene. This constitutes a political influence on the regulation of accounting practice (ibid.). The allocation of responsibility for the regulation of the MD&A regime with the SEC and the limited scope for flexibility in the preparation of the filings was seen to conflict with the assumption that the historic mission of UK accounting standard-setters was the provision of “thought leadership” in a regulatory system emphasising a cooperative relationship between the standard-setter and business (Baggott 1989; Mitchell 1989). Maintaining an aura of “innovation” and meeting ideas of governing in the name of “the profession” was considered to be a more important factor in establishing widespread acceptance for the proposed OFR regime in the UK than following the path of international harmonisation.

## **5 The re-positioning of accounting standard-setting**

The findings from this chapter help trace the more elusive ideas of “the art of the possible” (Standard-setter F) in accounting change. The study of the conditions under which non-financial and future-oriented accounting issues could emerge and become established on the agenda of national accounting standard-setters in the voluntary OFR event helps to explain “unusual” accounting change. The OFR event

illustrates that shifting the boundaries of accounting standard-setting beyond a mere “tinkering with existing practices and financial statements” (Young 1994, p. 85) can become possible when there is an interplay of multiple and complementary but also competing *logics of appropriateness*. Technical, international, and professional ideas of governing provided the reference points which allowed regulatory intervention by the ASB in non-financial and future-oriented reporting to be seen as a way to get accounting “right”. The findings from this chapter have wider implications for the study of *logics of appropriateness* in regulatory space. The OFR event shows that multiple ideas of governing may relate to each other in different ways. The shift in references to ideas of international harmonisation in the OFR event from the initially positive to the negative shows that what counts as “appropriate” in relation to a specific accounting issue may shift during the agenda-setting process as different logics come to complement and contradict each other.

The expansion of the regulatory mandate of the ASB into the field of non-financial and future-oriented reporting further supports the view that accounting standard-setters fulfil a wider role in the governance of economic life than being mere arbiters of technical knowledge of financial reporting. The “mistrust in numbers” in the voluntary OFR event at the ASB seems to be part of a more general re-positioning of the British system of accounting standard-setting. This move happened at the intersection of ideas of governing through accounting standards in the name of “the profession”, “the State” and “the market”. This has created possibilities for the role and identity of the ASB to go beyond questions of recognition, measurement, and presentation in the financial statements. This study, therefore, suggests the need to understand the position of British accounting standard-setting at the ASB as part of a complex web of ideas of governing. In the case of the agenda-setting process for a voluntary OFR this consisted of four elements which may also apply to other instances of accounting standard-setting at the ASB or other national standard-setters. First, there has been a growing formalisation of public interest-rationales in the work of the national standard-setter through direct sponsorship from of the Government and indirect effects from national and European regulations. Second, although the accounting profession no longer has exclusive control over the standard-setting process at the ASB, the role and identity of the British standard-setter remains closely tied to ideas of

“independence”, “expertise”, and “thought leadership” that roots in the history of professional self-regulation in the UK. Third, the emergence of regulatory issues on the agenda of the ASB is closely related to demands to enhance the “efficiency and effectiveness” of financial reporting in a capital market setting. Finally, the standard-setting process at the ASB has been characterised by a growing responsiveness to international developments in accounting standard-setting and regulation. The final point in particular seems to have taken centre stage in more recent debates regarding the role and position of national accounting standard-setters. The ASB faces ongoing pressures to establish its role and legitimacy under the increasing influence of the International Accounting Standards Committee (IASC), the impact of transnational regulation from the EU (Camfferman & Zeff 2007, p. 408), and the growing relevance of other national GAAP in the global business of UK companies and accounting firms (Rutherford 2007, p. 17).

The next chapter focuses in more detail on the rising emphasis on a public interest-rationale of non-financial and future-oriented reporting during the British Company Law Review (CLR). It also examines links between programmes and technologies in *regulatory space* and links them to the study of regulatory reform which happens in the direct realm of “the State”.

## Chapter 4

### REALIGNING LAW, ACCOUNTING, AND “THE STATE”

*“A fundamental consideration in examining the extent to which statutory requirements should extend into new areas is: to whom, in a modern economy, should the directors be accountable and in what respects?”*

*(CLRSG 1999a, para. 6.31)*

#### **1 Narrative reporting as an issue for economic governance**

This chapter discusses the rise of non-financial and future-oriented reporting as an agenda-issue for statutory regulation at a time when British political culture increasingly emphasised ideas of co-governing the economy in public-private partnership. The originality of this study lies in the emphasis placed on the role of law in mediating and structuring the “the interrelations between accounting and the state” (Miller 1990). This chapter shows that the British Company Law Review (CLR) was characterised by a close alignment between company law and “the economy”. This assigned law a role in the framing of extra-legal “arenas for controversy” in which a wide range of non-state actors was expected to continuously contest and agree the alignment of corporate activities with the high-level public policy objectives of “the State”.

What is interesting about the introduction of the mandatory OFR as part of the British law review are the profound regulatory interventions in economic life that were taken in the name of “the State”. The proposals for a mandatory OFR co-emerged with calls for the expansion of the overall scope of company law beyond the exclusive focus on shareholders. Mandatory non-financial and future-oriented reporting was expected to enable markets and society to monitor and enforce compliance with a proposed set of “inclusive” directors’ duties that required managerial attention to the impact of stakeholder relations, environmental, and

social matters on long-term shareholder value.<sup>1</sup> The combination of law and accounting in the new governance regime sought to turn a public policy programme of international macroeconomic competitiveness into practice, but without compromising the ideas of entrepreneurial freedom and decision-making. The introduction of the mandatory OFR together with the codification of “inclusive” directors’ duties in company law seems to challenge the idea that accounting plays a particular role in the operationalisation of decentralised regimes of economic governance that are only loosely associated with “the State” (Miller 1990; Miller & Rose 1990; Miller 1991; Miller & Power 1992; Rose & Miller 1992). This is consistent with writings on the rise of a *new regulatory state* in Britain and Europe (cf. Majone 1994; Moran 2001). They argue that a withdrawal of central Government from direct interventions in the economy since the 1970s has shifted responsibility for the regulation of economic life to private regulatory agencies and modes of self-regulation (Moran 2003, p. 5). Nevertheless, these studies also observed increases in state-initiated regimes of governing despite a strong emphasis on “the market” in neo-liberal policies. This has been interpreted as one of the great “paradoxes” of the *new regulatory state* in Britain (Ayres & Braithwaite 1992; Majone 1994; Moran 2000, 2001; Jordana & Levi-Faur 2004).

This chapter draws on the idea that the rise in public regimes of governing appears less “paradoxical” if we understand that laws and markets do not represent opposing ends of a regulatory spectrum but are interconnected and sometimes overlapping representations of different modes of governing in dispersed and complex networks (cf. Ayres & Braithwaite 1992). This is linked to the view that the problems and tactics of government may, at the same time, be centralised around references to “the State” and widely dispersed in governance networks that are external to the bureaucracies of central Government (Foucault 1991b). Although the related body of literature does not view “the State” as a unitary agent with a centralised power monopoly (cf. Skocpol 1985; Rose & Miller 1992; Hall 1993; Hunt 1997; Moran 2003), these writings do not entirely obviate a role for a centralised notion of “the State” in the making and shaping of otherwise decentralised regimes of governing (cf. Curtis 1995; Miller & Rose 1995).

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<sup>1</sup> The “inclusive” directors’ duties have been implemented in section 172 (1) of the *New Companies Act 2006*. For details, see appendix 4 in this thesis.



References to an overarching public authority of “the State” have been interpreted to maintain a focus on achieving a higher good for society (Foucault 1991b; Rose & Miller 1992; Hunt 1994, p. 54; Rose 1999, p. 141; Murray Li 2007, pp. 4-5).

*“In many cases the state has become regulator of last resort, operating indirectly through new forms of control [...] which have the appearance of being apolitical.” (Power 1994, p. 13)*

This includes expectations about the role of “the neoliberal State”: Economic management has remained one of the taken for granted tasks of national Governments even within a language of “deregulation” and “privatisation” (Dean 1999, p. 16). “The State” is at least expected to preserve a basic degree of public order and to provide the infrastructures that enable “the markets” to contribute to national economic prosperity and societal welfare (Rose & Miller 1992, p. 139; Dean 1999, pp. 11-12; Rose 1999; Grossman et al. 2008). In the UK, notions of neoliberal governance particularly refer to an era after the general election victory of the Conservative Party in 1979 that became known as “Thatcherism”. Throughout the 1980s, British political culture largely shifted its vocabulary away from ideas of public ownership and direct economic management by the “interventionist state” to ideological aspirations to “the markets” and “civil society”. They were supposed to provide indirect modes of intervening in the conduct of private organisations. At the same time, this was expected to ensure that the activities of business organisations contributed to macroeconomic growth and competitiveness (Rose 1999, p. 17; Pierre & Peters 2000, p. 55).

The rise of accounting in largely decentralised regimes of governing in the last quarter of the 20<sup>th</sup> century has been closely linked to the neoliberal vocabulary of “choice” and “entrepreneurship” (Miller 1991; Miller & Power 1992; Miller & O’Leary 1993; Hopwood et al. 1994; Miller & Power 1995; cf. Miller & Rose 2008a).<sup>2</sup> Studies of neoliberal regimes of governing assign accounting a particular role in creating possibilities for regulatory interventions that retain space for managerial discretion and autonomy (Miller 1991). However, studies of the

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<sup>2</sup> Despite the central role of calculative practices in neoliberal regimes of governing, the connections between accounting and rationales of macroeconomic management share a relatively long history in the UK (Gilmore & Willmott 1992, p. 162). Accounting has been mobilised in the name of a range of “higher ends” of economic government, such as increased efficiency, improved decision making, economic growth and competitiveness, or enhanced responsibility and accountability (Miller & O’Leary 1987; Miller 1991; Miller 1994b; Miller 2001).

interrelations between accounting and dispersed modes of governing by “the State” have still paid insufficient attention to the role of law in linking public policy programmes and the calculative practices of accounting. Studies of the interrelations between law and accounting in economic governance have mainly focused on ways in which the calculative practices of accounting create possibilities for intervention at the local level in the name of high-level policy objectives. These debates have largely focused on the ways in which “extra-legal forms of knowledge and expertise”, such as accounting, constitute the operation of laws in practice (Miller & Power 1992, p. 242). Law itself was assigned a relatively “static” role in formally outlining, ordering, and inscribing the objects and means of government. Besides that recognition of a role for law in securing “public rights to corporate knowledge” (ibid., p. 233), in specifying and clarifying the use of certain accounting techniques (Miller 1990), or in promoting specific calculative practices in the name of Government (Miller 1991), there has been little explicit attention to law in mediating and structuring the interrelations between accounting and a notion of “the State” in contemporary regimes of governing. Previous studies on “accounting innovation beyond the enterprise”, for instance, only discussed the role of legislation as a means for coercing the use of specific calculative techniques, such as discounted cash-flow (DCF) in the investment decisions of nationalised industries (Miller 1991). Other studies on the interrelations between law and accounting have largely focused on professional struggles (cf. Abbott 1988) over territorial claims between law and accounting as two distinct bodies of expertise that search for professional closure (Hopwood 1983a; Richardson 1988; Sugarman 1995; Walker 2004; Cooper & Robson 2006). From their point of view, the relation between law and accounting in advanced liberal societies has been characterised by competition and interdependence between the two bodies of knowledge (Miller & Power 1992).

The lack of studies of the role of law in linking accounting to “the State” is, however, surprising. In particular, given the many points of intersection between accounting and company law since the creation of the joint stock company in the 19<sup>th</sup> century (Gilmore & Willmott 1992; Napier & Noke 1992).<sup>3</sup> To address the

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<sup>3</sup> The *Joint Stock Companies Act 1844* introduced the incorporated company as a separate legal entity. It was followed by the *Limited Liability Act 1855*. For further discussion of the intersections between law and accounting in the UK Companies Acts since the beginning of the 20<sup>th</sup> century, see chapter three.

question of the role of law in the making and shaping of regulatory regimes in which a centralised notion of “the State” links to the decentralised practices of accounting, this study draws on a theoretical perspective on “law in action” (Hunt 1993, 1994, 1997), and reframes it in terms of a study of “law in the making”. This requires viewing law as a “lived experience” (Hunt 1993) that is constituted by, and at the same time itself constitutes a range of social relations among state and/or non-state actors, issues, and ideas (Hunt 1997, p. 104) instead of being a representation of “monolithic state power” (Hunt 1992).<sup>4</sup>

The remainder of this chapter outlines the interplay of law and accounting in the agenda-setting stage of the British CLR between 1998 and 2001. The first part illustrates the rise of ideas of co-governing the economy in public-private partnership around the mid 1990s and its implications for a close alignment of the spheres of lawmaking and macro-economic management. The second part presents the debates on the expansion of the scope of company law in the name of the high-level objective of “improving” the competitiveness of the British economy. The third part outlines the rise of the OFR as an agenda issue for legal reform in the close interplay of aspirations to “the State” and “the market” that were inherent in the debates on “inclusive” directors’ duties. This chapter concludes with an interpretation of the shifting role of law in mediating and structuring the links between accounting and “the State” within a political culture that emphasises ideas of public-private partnership.

## **2 Company law reform in public-private partnership**

By the mid-1990s, and according to a range of metrics, the British economy was largely underperforming in comparison to other Western countries (RSA 1994, pp. 8-9). The UK had the lowest real-term Gross Domestic Product (GDP) of the Western economies. It was the only EU country with a trade deficit in merchandised goods and came last of all Western countries in product development (RSA 1994, pp. 8-9). During that time, general ideas of “growth” and “competitiveness” continued to provide the underlying theme in the language of macroeconomic policy making and governance reforms (Miller & Rose 1990; Miller 1991; Miller & O’Leary 1993; Dean 1999). In order to achieve these

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<sup>4</sup> Hunt defines law as the “the historically specific production of regulatory devices that mediate between state and civil society and between state and individual” (Hunt 1994, pp. 54-55).

objectives, a series of public policy reports in the mid 1990s called for reforms to modernise and renew British institutions in a way that would “improve” the economic position of the UK (DTI 1994, 1995; RSA 1995; Commission on Public Policy and British Business 1997).<sup>5</sup>

## 2.1 Ideas of co-governing the economy

Almost two decades of Conservative Government had left their mark on perceptions of the “appropriate” degree of public intervention in economic matters (Hall 1993), the 1990s were also a time of transformation: However, the strong market ethos of the old “Thatcherism” in public policy debates was increasingly challenged by ideas of co-governing the economy in public-private partnership (Moran 2003).

*“We believe that the agenda of market liberalisation has largely run its course. More than that, it has cleared an arena in which government must now consult and work with the business community to improve corporate and national economic performance.” (Commission on Public Policy and British Business 1997, p.3)*

Signs of political change also emerged in the “New Labour” election manifesto which supported a programme of modernising the relation between business and Government as a key element in promoting global competitiveness of the UK economy (Labour Party 1997b; Rickford 2002):

*“The vision is one of national renewal, a country with drive, purpose and energy. A Britain equipped to prosper in a global economy of technological change [...]. We see healthy profits as an essential motor of a dynamic market economy, and believe they depend on quality products, innovative entrepreneurs and skilled employees. We will build a new partnership with business to improve the competitiveness of British industry for the 21st century, leading to faster growth.” (Labour Party 1997b)*

Under the newly elected Labour Government, the Department of Trade and Industry (DTI) announced a consultation on the state of UK competitiveness in June 1997 to follow up on the issue of “improving” the competitive position of the British economy (Beckett 1997c). A month later, the *Competitiveness Summit*

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<sup>5</sup> The Department of Trade and Industry’s (DTI) White Paper *Competitiveness: Helping Business to Win* (DTI 1994), followed by *Competitiveness: forging ahead* (DTI 1995), was the first survey of the UK’s competitive position under the John Major government.

brought together Government and the business community to sketch out the intended cooperative relationship in dealing with the economic problems:

*“Our task is to identify [...] a way in which both the Government and the business community have clearly identified and agreed roles and responsibility. A way in which the dynamics of market forces are used - not surrendered to, not opposed, but used - to deliver the results we all want.” (Beckett 1997a)*

Besides the explicit recognition of a role for “the market” in governing economic life, the Government concluded that the provision of regulatory incentives and the removal of obstacles for a long-term orientation in business management were a possible area for public action:<sup>6</sup> As part of these developments, law was increasingly seen as a mechanism for intervention in economic activity that was in line with an overarching policy objective of “enhancing” the international competitiveness of British business and the economy at large.

*“The general framework of commercial law and regulation at local and national Government level also impact hugely on business. [...] the right framework is essential for business competitiveness.” (Beckett 1997a)*

*“There is no doubt that company law is an area where the Government's role is paramount. We set the rules by which every company must operate - how companies are to structure themselves; the proper duties of directors; the rights and the obligations of shareholders; what rules are necessary to protect creditors; and what companies must do to communicate with their shareholders. [...] The issues on which I have touched are part of the good governance practices which the modern company needs to develop. Boards, shareholders, employees and others each have their role to play in this. The roles differ, but it is essential to get them right.” (Beckett 1998)*

A ministerial speech at the Annual Conference of the Confederation of British Industry (CBI) in November 1997 reiterated the case for reforming company law in the name of international economic competitiveness, making the alignment of law and “the economy” the starting point for the development of further reform programmes (Beckett 1997b).

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<sup>6</sup> To explain the rise of regulatory initiatives and reform, Hunt (1993) proposes a “desire to regulate”, whereas Rose and Miller (1992, p. 191) refer to a “will to govern” that drives authorities to constantly engage in policy reforms that seek to “improve” social and economic conditions.

## 2.2 The law reform programme

The British Government eventually launched a root and branch reform of the framework of core company law in March 1998 and placed it under the supervision of the DTI. This was a major step in the history of the UK Companies Acts. Since the beginning of the 20<sup>th</sup> century, company law had only been subject to partial review about every twenty years – often as a piecemeal response to business scandals (DTI 1998b; Rickford 2002).<sup>7</sup> In contrast, the CLR aimed for a complete realignment between company law and economic activity in the UK which implied a role for company law in achieving macroeconomic success and competitiveness:

*“Company law lies at the heart of our economy. Although technical and often left to be handled by specialists, it provides the legal basis for all companies and is fundamental to our national competitiveness.” (DTI 1998b, p. i)*

Hence, from the point of view of Government, UK company law was “part of the nation’s basic [economic] infrastructure” (Beckett 1998). The fundamental review of the company law framework was, therefore, seen as a way to act upon the fundamental structure of corporate relationships in a way that would have a “positive” impact on the international competitiveness British economy (ibid.).<sup>8</sup>

*“I want the review to [...] deliver a framework which promotes consistency, predictability and transparency; which underpins high standards of company behaviour and corporate governance; and which above all enhances the competitiveness of British business in a new millennium.” (Beckett 1998)*

The development of explicit proposals for the law reform started from the identification of “problems” within the system of company law, which existed then. The company law framework was seen as an “outdated” relict of Victorian times which subsequent piecemeal amendments had made hard to implement in “the modern age” (Beckett 1998; DTI 1998b, paras. 1.1-1.2; Rickford 2002). By the start of the CLR in 1998, the sources of British company law were widely dispersed in a

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<sup>7</sup> Major amendments to the Companies Act took place in 1908, 1929 and 1948 (DTI 1998b, para. 2.5). The last major review was conducted in 1960-62 by the Company Law Committee (Jenkins Committee 1962). The recommendations were, however, never fully implemented as the regulatory policy focus shifted to incorporating Directive requirements of the European Commission (EC) into primary UK law (Rickford 2002).

<sup>8</sup> The law reform was also seen as a way to encourage incorporation in the UK rather than elsewhere in an international context (Beckett 1998; DTI 1998b, paras. 4.1-4.7).

complex patchwork of contractual relationships, legislation, common law principles, and rules issued by regulatory bodies with a legal mandate, such as the ASB (Davies 2003, p. 45). The main piece of legislation was the Companies Act 1985. Quasi-legal “soft laws”, such as the Combined Code on Corporate Governance (Hampel 1998), and entirely voluntary self-regulatory frameworks at the level of professions, industries, or individual firms complemented the overall set of formally inscribed regulatory frameworks (Davies 2003, chapter 14).<sup>9</sup> Moreover, market forces in the so called “markets for corporate control” were seen as another authority that governed the behaviour of UK companies (Khemani & Shapiro 1993). However, this system was seen to be “seriously out of date” by the start of the CLR (DTI 1998b, p. i). On a more general level, the calls for legal reform assumed that there was a “mismatch” between the underlying philosophy of the framework of company law and “the real modern needs of incorporated businesses” (Rickford 2002). Law was seen to have “failed, in both its substantive and its transparency rules, to reflect sound perceptions of the real sources of value and performance in the modern economy” (ibid.).<sup>10</sup>

*“For all these reasons, the government has decided that the time is now right for a thorough review of core company law. The stripping out of obsolescent and over-complex provisions and the repair of defective ones will not be easy or straightforward. But we need clear and simplified arrangements which, starting from first principles, better capture the balance of obligations, protections and responsibilities which are required to underpin the modern marketplace [...].” (DTI 1998b, para. 3.8)*

The Government’s proposals were widely welcomed in the public responses to the first consultation document *Modern Company Law: For a Competitive Economy*. By 30 June 1998, the DTI received response letters from 156 individuals and organisations. 65 (42%) explicitly welcomed the law review. The agreement was founded on the general principle of the law review that “company law should reflect

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<sup>9</sup> Davies (2003, p. 323) uses the term “soft law” with reference to the “comply or explain” approach in the corporate governance obligations under the Listing Rules. It limits compliance with the Combined Code to a disclosure obligation on the extent to which a company has complied with the individual requirements and on reasons for non-compliance. The “comply or explain” principle, therefore, allows for full compliance with the Listing Rules even if none of the recommendations from the Combined Code are followed, as long as the company explains this to its shareholders in the annual report.

<sup>10</sup> The problematisations of Company Law in relation to economic reality resemble the debates on the “relevance lost” (cf. Johnson & Kaplan 1991) of financial reporting numbers as means of business management that have been outlined in chapter two of this thesis.

the reality of the modern corporate economy” that was carried forward throughout the remainder of the CLR (CLRSG 2001, para. 9). Only two responses explicitly rejected the CLR (DTI 1998a, para. 2.1).<sup>11</sup>

### 2.3 Co-legislation

The idea that law and “economic reality” should and could be closely aligned in regimes of governing in public-private partnership was also reflected in the formal organisational arrangements of the CLR that introduced an approach to lawmaking that has been described as “co-legislation” (Rickford 2002). After the launch of the law review in March 1998, the DTI delegated the task of developing the specific reform proposals to “distinguished” experts with “in-depth practical knowledge of the implications of policy proposals” and “the necessary authority and credibility to control the review” (Rickford 2002). An “independent” Company Law Review Steering Group (CLRSG), consisting of senior lawyers, academics, business representatives, and accountants, was created by the DTI over the summer of 1998.<sup>12</sup> The CLRSG was led by an externally appointed project director and chaired by a DTI official (DTI 1998b, para. 7.2).<sup>13</sup> Its task was to oversee the review and to develop a set of “factual” and practicable, but non-binding law reform proposals for the Government to take before Parliament (Rickford 2002). The DTI also established a so called Consultative Committee with the mission to balance the views of the Steering Group with those of external “key groups”, including the Law Society, the CBI, the Trades Union Congress (TUC), the professional accountancy bodies, and other Government departments (DTI 1998b, para. 7.3). Additional working groups were formed around issues such as “corporate governance” and “disclosure and financial reporting” (ibid., para. 7.6). Each working group was chaired by a member of the CLRSG, who provided initial input to the working group and reported back to the Steering Group. The Project Director was a member of all working groups. The CLR also followed a general preference for public “notice and comment” procedures over closed consultations (cf. OECD 2002). The CLRSG invited public comments to a series of consultative documents with the

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<sup>11</sup> The DTI classified 24 of the comment letters as “non substantial” (DTI 1998a).

<sup>12</sup> The role and authority of experts in governance (Miller & Rose 1990; Hunt 1994; Baldwin & Cave 1999) and their roles as “carriers of knowledge” in processes of institutional change (Jepperson & Meyer 1991, p. 226) are not further discussed within the scope of this research.

<sup>13</sup> For a full list of members of the CLR-groups and other participants in the review, see Annex A of *The Strategic Framework* (CLRSG 1999a).



stated objective to ensure “wide support not simply from business and industry but also in the community at large” (DTI 1998b, para. 1.3). In addition, the group engaged in direct dialogue with the “key groups” and commissioned independent research projects on some areas of debate. However, the members of the CLRSG and the DTI retained some authority over the views that were advanced in the internal and public debates. The direct impact of public consultations on the work of the CLRSG was, for example, limited by the group’s decision to weigh the responses according to perceived merit, soundness of reasoning, and status of the submitting body (CLRSG 2000a; Rickford 2002).

The remainder of this chapter outlines the more specific processes of problematising company law and accounting that took place during the agenda-setting debates at the CLRSG. The perceived discrepancy between the company law framework and “economic reality” opened the CLR to wider debates on a possible expansion of the scope of activities and relationships that should be subjected to regulation by “the State”. The discussion is based on archive materials, published texts, and personal interviews with key members of the CLRSG.

### **3 The codification of “inclusive” directors’ duties**

On the question of how a “better” alignment between company law and “economic reality” could be achieved, the law review turned its attention to the more specific field of directors’ legal duties. The CLRSG established a case for legal reform on the grounds that the existing definitions of directors’ duties in common law and statute had “failed” to foster economic prosperity. Fiduciary duties of loyalty and good faith to act in the interest of the company and the duty of skill and care had developed outside the Companies Acts as common law principles. They were interpreted as being owed to “the company”, but company law had remained imprecise in specifying the interests of “the company” (Davies 2003, p. 371). The Companies Act included an ambiguous duty of directors to pay attention to “the interest of the company’s employees in general, as well as the interests of its members” that left enforcement of employees’ interests to legal action by shareholders.<sup>14</sup>

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<sup>14</sup> Section 309 CA1985.

### 3.1 The case for legal reform

The formulation of directors' legal duties was considered to be too dispersed and unclear and to result in inefficiency and substantial compliance-costs to businesses (DTI 1998b, paras. 3.1-3.3). Furthermore, current legislation was deemed insufficient to provide a focus on the long-term in managerial decision making and to counterbalance market pressures for short-term shareholder wealth maximisation (CLRSG 1999a, para. 5.1.17).<sup>15</sup> The views of the CLRSG were supported by a study commissioned by the Law Commission and the Scottish Law Commission (1999) which concluded that directors found it difficult to understand their legal obligations. The CLRSG, consequently, proposed to unify and clarify directors' duties in primary legislation. Additional surveys of company directors by the Institute of Directors (IoD) and by the Law Commissions suggested widespread support for the proposals (CLRSG 1999b, para. 7.5): 61% of the surveyed 836 directors welcomed the clarification of the existing common law duties in a codified statement (Deakin & Hughes 1999).

However, the definition and interpretation of legal constraints on directors' powers had always posed a particular challenge for company law reformers throughout the 20<sup>th</sup> century (DTI 1998b). It was understood that the definition of the "objectives in accordance with which companies should be run, and correspondingly the range and priority of interests that company law should seek to further" had major implications for the fundamental scope of influence of the legal framework on corporate activities (Parkinson 2002). The DTI, therefore, invited a high-level "philosophical" debate on "first principles" and the scope of company law as a whole. The question was, to whom explicitly directors' duties should be owed in order to promote "high standards of company behaviour and corporate governance" (ibid., para. 5.1)?

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<sup>15</sup> The market for corporate control was deemed ineffective for disciplining directors towards a focus on long-term economic competitiveness (cf. Davies 2003, p. 326), because the possibility to become subject to a hostile takeover created pressures on directors for short-term profit oriented decision making (CLRSG 1999a, para. 5.1.17).

*“A wider issue for the review is whether directors’ duty to act in the interests of their company should be interpreted as meaning simply that they should act in the interests of the shareholders, or whether they should also take account of other interests, such as those of employees, creditors, the environment, and the wider community.” (DTI 1998b, para. 3.7)<sup>16</sup>*

The arguments presented by the DTI further elaborated on the views from a series of earlier public policy publications that had promoted a broader approach to managing stakeholder relationships and social and environmental responsibilities as a way to “improve” Britain’s economic position (Hutton 1995; RSA 1995; Commission on Public Policy and British Business 1997; Tomorrow’s Company 1998).<sup>17</sup> The Government added an emphasis on the possible role of company law in facilitating the management of wider business relationships and in promoting a focus on the long-term:

*“[C]ompanies need to have an inclusive approach to their customers, products, people. Government has a role to play in setting decent standards [...]” (Beckett 1998)*

Similarly, the members of the CLRSG came to agree that competitiveness and efficient wealth creation in a modern economy were best achieved through the harmonious cooperation of all internal and external stakeholders and the recognition of wider community interests (CLRSG 1999a, para. 5.1.17). Since a broader stakeholder perspective was not reflected in the present framework of company law, the DTI and the CLRSG suggested evaluating to which degree the overall scope of company law could be shifted from the traditional “monist” focus on shareholder-interest to a more “pluralist” approach (DTI 1998b, para. 3.7; CLRSG 1999a, paras. 5.1.12-13).

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<sup>16</sup> The question how to define the scope of directors’ duties and accountability mechanisms was and maybe still is one of the greatest controversies in the making of centralised regulatory frameworks. Up until now, different conceptions of the duties of directors continue to exist in the national corporate governance systems. The question whether non-financial strategic objectives are equivalent (cf. Blair 1995; Kelly & Parkinson 2000; Gamble & Kelly 2001; Williamson 2003) or subordinate (cf. Easterbrook & Fischel 1991; Willetts 1997; Grantham 1998; Scott 2003; Kraakman et al. 2004) to financial goals fuels ongoing conceptual debates about a *pluralist* vs. shareholder-focused conception of the business.

<sup>17</sup> For a detailed discussion of the proposals in these reports, see chapter two.

*“The principal arguments which are advanced for change are that the present scheme of the law fails to adequately recognise that businesses normally best generate wealth where participants operate harmoniously as teams and that managers should recognise the wider interests of the community in their activities.” (CLRSG 1999a, para. 5.1.9)*

The CLRSG, therefore, proposed to combine the codification of directors’ legal duties with changes to the fundamental shareholder principle in company law. This was supposed to “point the way to a more performance-based, progressive and 'holistic' managerial approach, to the benefit of the whole British economy” (CLRSG 1999b, para. 7.33).

### **3.2 Contesting the scope of company law**

The public responses to the first consultation document of the CLRSG *Modern Company Law for a Competitive Economy: The Strategic Framework* (CLRSG 1999a) rarely questioned that considering wider stakeholder relations was already “reality” in business management.<sup>18</sup> However, controversial debates arose in the public consultations and among the members of the CLRSG out of the question of directors’ duties and to whom they ultimately owed their legal duties. Diverging views on the role of “the State” vs. “the market” in regulating economic activities materialised in a deep disagreement about the degree of specification of directors’ duties in statute. On one side were the supporters of fundamental reform who argued that a “pluralist” basis for company law would better reflect the growing impact of wider stakeholder groups, the environment, and society at large on corporate performance (cf. Blair 1995; Carroll 1999; Kelly & Parkinson 2000; Gamble & Kelly 2001; Williamson 2003). They argued that statutory recognition of the “business case” (DTI 1998a, para 14.3) and of a general “license to operate” that was granted by society at large (CLRSG 1999b, paras. 7.5 & 7.15) would raise awareness for the commercial relevance of actively managing wider stakeholder relationships in a capital market setting. On the other side, the opponents of a pluralist approach argued that the traditional focus on the legal relationships between the company and its shareholders in company law already provided sufficient legal underpinnings as the play of forces in otherwise “free markets” already ensured that a “business case” for socially and ecologically responsible

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<sup>18</sup> 26 (17%) of the 156 submissions explicitly commented on the idea to expand the scope of directors’ legal duties.

behaviour would be taken into account (DTI 1998a, para. 14.2; CLRSG 1999b, para. 7.4).<sup>19</sup>

*“[A]ccountability to shareholders was currently clear and this was fundamental to the operation of the free market in a competitive economy. A dilution or dispersion of this accountability would risk making Britain less attractive to foreign capital and British companies less competitive. “ (CLRSG 1999b, para. 7.4)*

The CLRSG concluded that the majority of opinion was against the stakeholder model (CLRSG 1999b, para. 7.14; Davies 2003, p. 292) and eventually decided to discontinue the debates on a pluralist approach in late summer 1999 (CLRSG 2000b; Parkinson 2002). Although the group recognised a “theoretical superiority” of the pluralist approach, the members were aware of possible practical limitations. The members of the CLRSG were able to agree on the point that a stakeholder approach to company law might result in counterproductive conflicts of interest, over-litigation, or no enforcement at all (CLRSG 2000a, para. 3.5; Parkinson 2002, Regulator B). This was seen to risk diluting the focus of directors in business management and to complicate enforcement (Parkinson 2002; Rickford 2002). The group further pointed at practical difficulties to draft a “one fits all” pluralist duty in statute (CLRSG 2000b, paras. 3.24-3.31).

However, the decision against a pluralist approach in company law was far from unanimous. It resulted in strong opposition from environmental and development groups such as Friends of the Earth, Oxfam, and Traidcraft Exchange, and even led to the resignation of the former head of social and environmental policy at The Body Shop from the CLRSG (Cowe 1999).

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<sup>19</sup> Any additional requirements for the protection of employees or the environment were suggested to be regulated in separate legislation and not in the Companies Act (DTI 1998a, para 13.3). The proposals to maintain the scope of company law as it was, were mainly advanced by representatives from the legal profession. They explicitly rejected a mandatory OFR on the grounds that it was not an issue for company law to regulate corporate behaviour in areas that may be better left to separate employment, health and safety, and environmental laws. In its response to *Completing the Framework*, the Law Society of England and Wales explicitly requested to “keep lawyers out of accounting”, rejecting the creation of responsibility of the legal profession for practices that they perceived a part of the professional territory of accountants (letter from the Law Society, 28.07.2000).

*“Enlightened business will find it hard to forgive the government for its cold feet about stakeholder rights. If their company law review backs off fundamental reform it will miss the opportunity to put business on a 21st-century footing. Worse, they will confirm the damaging impression that business responsibility goes no further than making a profit - a lie which is doing enormous damage to people, the environment and communities around the world.” (Roddick 2000)*

Despite the continued controversy over the “scope”, the remaining members of the CLRSG refused to consider the stakeholder issue. They stated that “none of the responses suggested a practicable means of dealing with the crucial question of how such a duty could be enforced” (CLRSG 2000a, para. 3.5). At the same time, the group was aware that a widely shared consensus on the question of “scope” was important for the “success” of the law review:

*“I wanted to reform British company law, and if we couldn't solve this problem, this stakeholder problem, we weren't going to get legislation at all. It would just be lost. And all the work that we put in would be lost.” (Regulator B)*

In order “to overcome the tensions” (Regulator B), the review group opted for a so called “enlightened shareholder value” approach (CLRSG 1999a, para. 5.1.11). The concept was already included in earlier consultations as a possible middle way for approaching the high-level question of “scope” (DTI 1998b, para. 3.7). The proposed approach was supposed to continue the existing arrangement under which only shareholders could take legal action against directors in case of a breach of their legal duties. However, these statutory duties were supposed to be expanded by the explicit requirement for directors to take into account a company’s long-term relationships with internal and external parties, as well as the community and the environment when managing for shareholder-value (CLRSG 1999a, para. 5.1.17).

*“It may be asked whether this proposal overall is an “enlightened shareholder value” or a “pluralist” one. The overall objective should be pluralist in the sense that companies should be run in a way which maximises overall competitiveness and wealth and welfare for all.” (CLRSG 2000b, para. 2.21)*

At a later time, the CLRSG only referred to the term “inclusive” directors’ duties, although technically not different from the “enlightened shareholder value” proposal. The change in language was supposed to signal the consensus that had

been found between the supporters of a shareholder vs. a stakeholder approach within the CLRSG (Regulator A).

*“[W]hat was extraordinary was the extent to which the different camps were actually carried in the same direction by this basic sort of enlightened shareholder value/inclusive logic [...]” (Regulator A)*

Indeed, even strong proponents and opponents of the pluralist model, such as the TUC and the CBI eventually welcomed the inclusive approach to “act as a restraint on the seemingly relentless maximisation of shareholder value” (Brown & Peel 2001, Regulator A).

The next section of this chapter illustrates how the widespread agreement to introduce an “inclusive” set of directors’ legal duties into the Companies Act was made possible by debates on law reform in the area of company reporting. Among other things, these debates were dealt with the role of published accounting reports in creating accountability for directors and shareholders *vis-à-vis* the wider public (CLRSG 1999a, para. 5.1.44).

#### **4 The mandatory OFR**

Since the proposals for “inclusive” directors’ duties implied that formal litigation rights in case of breach of duties would be reserved to shareholders only, the CLRSG had to design a balanced monitoring and enforcement regime with few constraints on managerial decision making, while at the same time honouring the directors’ responsibility *vis-à-vis* a wider group of stakeholders.

*“The way to square that circle was to have public accountability through published reporting for the wider range of constituents, whilst maintaining the focus within the field of corporate governance [...] with shareholder-value for the board.” (Regulator B)*

The general idea that a combined regime of law and accounting might help “solve” the “problem” of international competitiveness of the British economy led to a series of further debates. First, there was a general discussion about public accountability as a means of linking questions of lawmaking to questions of market-based enforcement in extra-legal spaces. Second, the discussions fed into the more specific debates in which the reform actors agreed on the mandatory OFR as an agenda issue for the CLR.

#### 4.1 Ideas of extra-legal accounting-based enforcement

The view that the behaviour of investors and managers could be aligned with the high-level objectives of the CLR by means of “extra-legal [...] disciplines”, including corporate financial reporting, had surfaced early in the law reform debates (Regulator B). Although none of the initial seven Working Groups of the CLRSG explicitly dealt with accounting and reporting, a general focus on the principle of transparency and accountability had accompanied the law reform debates since the launch of the CLR.<sup>20</sup>

*“So I would like companies to think more deeply about how they can be transparent and accountable to all those with an interest in their business. One way may be for companies to look at improving how they communicate with all those groups in all kinds of ways - including in the annual report. (Beckett 1998)*

The CLRSG took the issue further in its internal debates on possible ways to enforce an “enlightened” or “inclusive” shareholder value approach in practice. The group made a first step towards linking law and accounting in the proposed “inclusive” approach to company law when it developed the idea that “public sanction” was “implicit in the notion of public accountability” (Regulator B). The argument was that not only directors, but also capital markets were constrained by public views about “appropriate” corporate behaviour. Shareholders were expected to pass that pressure on to directors (ibid.).

*“Enhanced reporting obligations operating within a structure of enlightened shareholder value have the capacity in principle to achieve the objectives of a more pluralist approach, by ensuring that it is in the self-interest of members that such pressures should be satisfied. Effective reporting might also [...] reduce short-term pressures by shareholders on directors” (CLRSG 1999a, paras. 5.1.44-5.1.47).*

*“[T]here's a great deal of de-facto accountability of shareholders in that sense through the political system and the financial press, and so forth. And there's also now much higher level of recognition than there used to be by institutional investors of the need to ensure that companies do satisfy these constituencies, because otherwise their business will go wrong.” (Regulator B)*

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<sup>20</sup> For further discussion on the rise of transparency in governance, see Hood and Heald (2006).



*“[I]t will work through, because the directors are accountable to the shareholders and the shareholders will be influenced as to what’s in their best interest by the pressures from outside. If the shareholders are accountable to the public [...] they’ve got in that sense a pluralist obligation” (Regulator B)*

These debates drew on the idea that accounting reports provided a possible vehicle for giving visibility to and acting upon the various areas of business management. In addition, the group emphasised that the published information for shareholders might also be of interest to non-shareholder stakeholders and society at large.<sup>21</sup>

*“We have already noted that in practice the fact that a company’s accounts and reports must be published enables the public at large to evaluate its performance and bring pressure to bear on the company as a whole, both members and directors, so as to satisfy relational and wider social interests.” (CLRSG 1999a, para. 5.1.44)*

In a next step, the CLRSG considered possible implications of “accounting and reporting issues” for the law review project. A focus on non-financial and future-oriented reporting in company law was proposed as a possible way to make new areas of business management governable in the name of the high-level public-policy ideas of macroeconomic management by “the State”. Company law was assigned a role in formally outlining the types of information that would demonstrate how far directors had considered their “inclusive” duties in the running of the company. Furthermore, the publication of that information in the annual report was expected to subject directors’ decision-making to interventions by “the markets” and society. The CLRSG recognised that businesses already voluntarily responded to growing demands for new forms of qualitative and future-oriented reporting (CLRSG 1999a, para. 5.1.47) but identified a “problem” of missing checks and a lack of enforcement of voluntary reports (ibid., para. 6.30).

*“The extent of non statutory reporting suggests that there is a market need or a wider demand for financial and non-financial information on companies which the existing statutory requirements fail to reflect.” (CLRSG 1999a, para. 6.30)*

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<sup>21</sup> A similar rhetoric on the welfare-effects of accounting for wider groups in society had surfaced previously in British debates on the role of accounting in public policy in the 1970s. They were accompanied by discussions about the widening groups of legitimate users of financial accounts (ASSC 1975; Department of Trade 1977a, 1977b; Burchell et al. 1985; Hopwood et al. 1994). During the Thatcher/Regan era in the UK and the US in the 1980s, these stakeholder debates in corporate governance and corporate reporting were largely marginalised in public policy discourses and the role of directors to serve the interests of shareholders was reinforced (Tricker 2000).

Initially, the review group was undecided about whether or not to take further steps towards the introduction of requirements for non-financial and future-oriented reporting in company law:

*“This does not necessarily point to a need for increased statutory requirements. The growths of non-statutory reporting could be said simply to demonstrate that companies are responding flexibly to the demands from interested groups, a response which should be left to develop. [...] On the other hand voluntary reporting implies an inequality of information as between companies and, perhaps, the disclosure only of information which shows a company in a positive light. Is it fair that companies which provide such information should be placed at a possible competitive advantage?” (CLRSG 1999a, para. 6.30)*

According to the internal meeting minutes, the CLRSG doubted the quality, comparability, and usefulness of existing voluntary reports for which they blamed a tendency for “fair weather” reporting under voluntary regimes (CLRSG 1999a, para. 6.31). Additional transparency provisions were expected to help “reveal” the “real sources of value and performance in the modern economy” (Rickford 2002, p. 11).

*“[T]here's nothing new or rocket science about this. Anybody with any sense, who is trying to assess the merits of an investment in a company needs to look at the things that matter for its future. And, so far as they were concerned, it was just obvious that the existing structure of corporate reporting was defective. It wasn't in itself leading to properly informed markets.” (Regulator B)*

The translation of non-financial and future-oriented accounting into a possible issue for legal intervention was linked to a perceived “mismatch” between “the real modern needs of incorporated businesses” and the underlying philosophy of the British framework for corporate accountability (Rickford 2002).<sup>22</sup> The CLRSG assumed that the “right” balance of good and bad news and a long-term focus could only be achieved through the disciplinary effects of additional mandatory reporting requirements. The proposed mandatory version of the OFR was expected to bridge the gap between the current status quo of financial reporting practice and the presumed additional information needs of markets and other stakeholders (CLRSG

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<sup>22</sup> The reform proposals also suggest a strong believe in the “usefulness” of disclosures and information provision for capital markets which seems to be in line with the predominance of an abstract and unquestioned notion of “the user” in financial reporting regulation (Young 2006).

2000b, para. 2.22) by providing “a discussion and analysis of the performance of the business and the main trends and factors underlying the results and financial position and likely to affect performance in the future” (ibid., para. 5.79). As in the earlier agenda-setting debates at the ASB, the CLRSG also used the argument that additional narrative reporting had the potential to overcome perceived “limitations” of the then existing financial reporting framework. The discussions emphasised the possible benefits of statutory inscription to ensure companies informed “effectively” on “a wide range of relationships and resources, which are of vital significance to the success of modern business” (CLRSG 2000a, para. 3.4). “Improvements” in corporate reporting were also directly linked to the high-level objective of the CLR. Additional mandatory reporting on non-financial and future-oriented issues was seen as a way of reconciling the multiple aspects of the CLR that defined “the overall objective of wealth generation and competitiveness for the benefit of all” (CLRSG 2000b, para. 7) in terms of shareholder value, sustainable stakeholder engagement, and social and environmental responsibility (CLRSG 1999b, para. 7.33). In addition, a codified OFR requirement was also expected to have an educational effect on directors and to stimulate the connection between internal management information and control-systems and a focus on long-term business performance (CLRSG 2001, para. 3.34). Statutory reporting provisions were expected to trigger voluntary changes to internal management practice which would “secure that companies are operated to achieve their proper purposes” (CLRSG 1999a, para. 5.1.50)

#### **4.2 Contesting the scope of mandatory reporting**

*“We believe that the time has come to require larger companies [...] to provide an OFR, which will cover the qualitative, or “soft”, or intangible, and forward looking information which the modern market and modern business decision making requires, converting the practice of the best run companies into a requirement for all.”*  
(CLRSG 2000b, para. 5.77)

Although the members of the CLRSG supported the view that a legal base for additional reporting was an integral part of a regulatory framework promoting the objectives of the CLR (CLRSG 2000a, para. 3.9), the members of the group were also aware that:

*“[T]his was one major piece of interventionist regulation: a new report.” (Regulator B)*

The CLRSG, therefore, introduced a new internal working group on “Accounting, Reporting and Disclosure” (CLRSG 1999a, paras. 6.1 and 9.4, and annex I) to explore the possible scope, purpose, and stakeholder aspects of financial reporting in company law. The Accounting Working Group later formed a sub-group on qualitative reporting and the OFR to deal with the more specific issues of mandatory OFR reporting.<sup>23</sup> The Working Group wanted to model the intended “enhanced” mandatory reporting regime on the structure and terminology of the existing voluntary *Statement: Operating and Financial Review* (ASB 1993) as it believed this would reduce initial uncertainties about a new statutory report among preparers and users (CLRSG 2000b, paras. 5.74-5.77 & 5.79). The Working Group assumed that the voluntary *OFR Statement* would provide a framework on which businesses and the accounting profession had at least agreed in the early 1990s (Regulators A and B).

*“That was very important politically. [...] To be able to say: ‘Well this is an adoption with modifications of a concept that is tried and tested, and accepted as best practice by the ASB’ [...] which was at that stage probably the most prestigious accounting regulator in the world.” (Regulator B)*

Among others, the accounting and reporting Working Group held a seminar on the proposed new regime for company reporting on 5<sup>th</sup> of June, 2000.<sup>24</sup> The aim was to secure widespread support for a reform of statutory financial reporting requirements and to identify the biggest areas of agreement and disagreement. The main issues arising from the CLRSG’s proposals in *Developing the Framework* were related to questions about the “information needs” of accounts users or the “right” balance between rules, standards, and best practice.

*“[O]bviously a lot of work was going on under the surface. Consulting and aligning. Trying to find out what would satisfy the maximum number of constituencies.” (Regulator B)*

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<sup>23</sup> For a list of members of the sub-group, see CLRSG (2000b), annex A.

<sup>24</sup> Participants included *inter alia* representatives from the ASB, the UK accounting bodies and audit firms, the CBI and individual companies, Amnesty International and other NGOs, and academia. The seminar was chaired by the Director of Tomorrow’s Company, a non-profit think-tank which promoted the “inclusive” approach through its work.

The CLRSG also commissioned a study on the practical impacts of the proposed mandatory OFR regime by the Industrial Society (2001). Between November 2000 and February 2001, five public companies – British Airways Plc, British Telecommunications Plc, Clydesdale Bank Plc, Great Universal Stores Plc, and ITNET Plc – prepared trial OFRs. Their experiences were reviewed with support from the four audit firms Ernst & Young, Grand Thornton, KPMG, and PricewaterhouseCoopers (ibid.). According to the internal meeting minutes, the OFR Working Group concluded from the “test run” that the implementation of the new OFR framework had been unproblematic and would only result in marginal additional costs to business. The pilot study suggested that users and preparers of OFRs could equally benefit from “a superior assessment of company performance”, an “enhanced reporting and reviewing process”, the provision of “additional value for stakeholders”, an enhancement of corporate reputation, and “better comparability between firms” (ibid.).

The efforts of the CLRSG and its Working Groups to establish widespread awareness of and empirical evidence for the benefits of a statutory requirement for OFR-type reporting in various additional forums may have contributed to the mainly positive reactions in the later consultations. Of the 450 responses to the consultation document *Developing the Framework* (CLRSG 2000b), 86 (19%) referred to the proposed introduction of a mandatory OFR. About 60 (70%) out of the 86 responses to the OFR proposals generally supported the proposals. The public responses did however diverge on the question of whether a mandatory OFR should prescribe specific reporting items and how much flexibility directors should have to define the scope of reporting.<sup>25</sup> Respondents from non-profit organisations including Amnesty International, Friends of the Earth, the Royal Society for the Protection of Birds, Traidcraft Exchange, and the WWF, called for more mandatory items, such as environmental and social performance.<sup>26</sup> By contrast, representative bodies with closer links to company directors, such as the IoD, the 100 Group of

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<sup>25</sup> Particularly detailed comments on the mandatory OFR were made by three out of 15 responses from the accounting organisations (ASB, ACCA, ICAEW), one out of five from the investing community, four out of ten non-profit organisations (Centre for Tomorrow’s Company, Traidcraft Exchange, UK Shareholders’ Association, WWF), and two out of twelve preparers (BBC, Camelot Group plc). The CBI, the Environmental Industries Commission (EIC), and the TUC also contributed extended comment letters to the OFR discussion.

<sup>26</sup> With references to their main field of activity, these organisations asked to further prescribe reporting on issues such as human rights (Amnesty International), environmental performance and policies (Royal Society for the Protection of Birds, Traidcraft Exchange), and other non-financial issues.

Finance Directors, Business in the Community, and the CBI, rejected a mandatory approach. On the one hand, the business community largely “felt that the voluntary code was working very well” and therefore preferred to maintain and encourage a voluntary approach to OFR type reporting.<sup>27</sup> On the other hand, the critical responses expressed particular concern with the encouragement of “increasingly sterile” content or the possible disclosure of confidential and commercially sensitive information (CLRSG 1999b, para. 7.32). The legal profession expressed similar concerns. The Law Society of England and Wales along with another law firm suggested that a mandatory OFR would create an additional regulatory burden on business instead of providing UK firms with an international competitive advantage. Overall, those who rejected further statutory regulation of OFR reporting suggested encouraging greater flexibility for reporting practice to develop outside law and relying on market pressures to promote “good practice” in non-financial reporting (ibid., para. 7.32).

#### **4.3 A new framework for UK company law**

Following the consultations on the possible relationship between prescription and flexibility in legal reform, the members of the OFR Working Group reached the conclusion that:

*“[M]arkets and society are best served by frameworks of law which are very clear and simplistic about the obligation in principles but un-prescriptive about the detail of how you do it” (Regulator A)*

The proposed mandatory OFR reporting regime would mediate the relationship between the “inclusive” directors’ duties in statute and market-based enforcement mechanisms for the benefit of the British economy at large.

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<sup>27</sup> CBI representative at *The Operating and Financial Review Summit*, London 2005.

*“We argue that the overall objective of wealth generation and competitiveness for the benefit of all can best be achieved through the twin components of:*

*- an “inclusive” approach to directors’ duties which requires directors to have regard to all the relationships on which the company depends and to the long, as well as the short-term implications of their actions, with a view to achieving company success for the benefit of shareholders as a whole; and*

*- wider public accountability: this is to be achieved principally through improved company reporting, which for public and very large private companies will require the publication of a broad operating and financial review which explains the company’s performance, strategy and relationships (eg with employees, customer and suppliers as well as the wider community).” (CLRSG 2000b, para. 7)*

*The Final Report* (CLRSG 2001) to the Government suggested a mixed approach to reporting which would include a list of mandatory items that had to be covered in any case. There would also be a list of items required to be disclosed “to the extent that they apply to matters which the directors judge material” (ibid., 8.49).<sup>28</sup> The underlying idea was that “some form of mandatory requirement [was] needed”. The argument was based on the observation that compliance with the voluntary OFR guidelines was “patchy” – in particular among companies outside the FTSE 100 (ibid., para. 3.36, Standard-setters B and C). The “materiality threshold” was proposed as a means of reducing the regulatory burden and maintaining flexibility vis-à-vis business. It was also meant to overcome the risk of so called “boilerplate reporting” that was associated with a system considered too legalistic (CLRSG 2000b, para. 2.20). For both types of reporting items, the CLRSG suggested inscribing broad headlines only in statute while delegating the development of a more detailed standard outlining the content of an OFR to a standard-setting body with recognised responsibility for OFR reporting (CLRSG 2000a, para. 12.43) – namely the ASB (CLRSG 2001, para. 8.49). In addition, *The Final Report* proposed strengthening the role of auditors in the proposed framework by introducing a mandatory process review (ibid., paras. 8.58 - 8.63).<sup>29</sup> *The Final Report* (CLRSG

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<sup>28</sup> A distinction between mandatory and discretionary items had already been proposed by the Investor Relations Society in the first ASB consultation on the OFR Statement (Investor Relations Society letter to ASB, 12 August 1992).

<sup>29</sup> The DTI initially followed the recommendations from the CLRSG for a process review of the OFR. A proposed new paragraph 235 (3A) would require auditors to give an opinion on whether directors have prepared the OFR after “due and careful enquiry”, and whether the information given in the OFR was consistent with the annual accounts and other matters that have come to the auditor’s attention. The audit review requirement was, however, replaced with a limited requirement for auditors to check on consistency

2001) also recommended the codification of inclusive directors' duties in statute (CLRSG 2001, para. 3.8), based on the consensus that had been reached on the "inclusive" approach.

The Government responded to the recommendations in July 2002 in the White Paper *Modernising Company Law* (DTI 2002). The White Paper welcomed the proposed "inclusive" approach to a codification of directors' common law duties (ibid., part II, para. 3.3). The Government agreed that:

*"[T]he basic goal for directors should be the success of the company in the collective best interests of shareholders, but that directors should also recognise, as the circumstances require, the company's need to foster relationships with its employees, customers and suppliers, its need to maintain its business reputation, and its need to consider the company's impact on the community and the working environment" (DTI 2002, part II, para. 3.3).*

The Government also agreed "that companies should provide more qualitative and forward looking reporting" and welcomed the OFR as a new accountability mechanism that would give shareholders and other stakeholders "the information they require" (DTI 2002, para. 4.31-4.31). In addition, the White Paper explicitly emphasised the role of OFR reporting in promoting sustainability and corporate social responsibility:

*"A reporting requirement in these terms would also be a major benefit for a wider cross-section of a company's stakeholders. The new requirement to report, for example, on material environmental issues would be a major contribution to both corporate social responsibility and sustainable development initiatives. The Government has long recognised, and promoted, the business case for these and sees the OFR as the opportunity for directors to demonstrate their response to this business case." (DTI 2002, part II, para. 4.32)*

In the end, the DTI even decided to prioritise the introduction of the OFR for listed companies over the other company law reform proposals (DTI 2004a).<sup>30</sup> The *OFR regulations* were brought before Parliament in January 2005 (HMSO 2005) and

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with the company's accounts when conducting the statutory audit as part of a series of last-minute changes to the OFR Regulations in October 2004 (DTI 2004b).

<sup>30</sup> The development of a Companies Bill was halted after the publication of the White Paper to incorporate forthcoming regulations from the European Commission (EC) and to consider the implications of the Enron and WorldCom failures (Hewitt 2003).



passed by the House of Commons in the following months (HOC 2005).<sup>31</sup> The *OFR Regulations* followed the proposals by the CLRSG to cross the boundaries between law and standards and to involve self-regulatory bodies in the development of reporting standards (Rickford 2002). A new section 256A to the 1985 Companies Act expanded the statutory recognition of accounting standards<sup>1</sup> to OFR standards so that compliance with the reporting standard automatically constituted compliance with the law (DTI 2004a).<sup>1</sup> In November 2004, the ASB presented a draft standard *Reporting Exposure Draft (RED) 1: Operating and Financial Review*, which provided more detailed guidance for the preparation of an OFR in compliance with company law (ASB 2004). The final *Reporting Standard 1: Operating and Financial Review* (ASB 2005) was issued in May 2005.

Although the *OFR Regulations* were suddenly abolished in November 2005 (DTI 2005), section 417 of the new *Companies Act 2006* contains the requirement for an “enhanced Business Review” which covers most of the statutory requirements of the previous OFR regime.<sup>32</sup> In contrast to the initial mandatory OFR regime, the provisions do not demand reporting on business goals and strategies. And unlike in the statutory OFR, the current regime for non-financial and future-oriented reporting is not supported by a formally recognised accounting standard. The ASB’s current *Reporting Statement: Operating and Financial Review 2006* (ASB 2006) provides only non-binding voluntary guidelines.

## **5 The role of law in connecting accounting to “the State”**

The study of the rise of the mandatory OFR during the British law review suggests a particular role for law in mediating and structuring the link between accounting and “the State” in otherwise widely dispersed governance networks. Previous studies of the interrelations between accounting and macroeconomic programmes of governing by “the State” have already identified a role for law in framing the collection of “regulatory knowledge” in regimes of governing “at a distance” (cf. Miller 1990, 1991; Miller & Power 1992). Similarly, the role of law in the mandatory OFR event was to give formal visibility to regulatory arrangements which had previously been widely dispersed in society. These included the

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<sup>31</sup> *The Companies Act 1985 (OFR) Repeal Regulations 2005*.

<sup>32</sup> The *New Companies Act 2006* also implements the proposed system of “inclusive” directors’ duties in section 172 (1).

framework of directors' duties in common law and the "best practice" guidelines for voluntary OFR reporting.<sup>33</sup>

What is remarkable about the role of law in this case is that the CLR overcame the dichotomy between "state" and "non-state" in the relations between law and accounting in economic government. To begin with, the desire to unite and globalise existing but less formalised regulatory regimes in statute were different from ideas of a "static" inscription of widely dispersed regimes of governing already in existence. In addition, they did not refer to "the State" as regulator of last resort providing closure to societal processes contesting the general role of business in society. Finally, the wish to create a centralising and ordering role for statutory provisions during the CLR were far from a notion of "law and order" implying strict judicial penalties and a gravitation of regulatory powers towards "the State" (Hunt 1993).<sup>34</sup>

This study, therefore, supports and further analyses a view of law as a "lived experience" which is constituted by and at the same time constitutes a range of social relations (Hunt 1997, p. 104). The agenda setting processes during the CLR illustrate a situation in which both the lawmaking processes and the proposed legislation were assigned a role in framing "controlled arenas for controversy", where a wide range of actors could interact. During the lawmaking process, the introduction of the formally "independent" CLRSO and its working groups operationalised inherent aspirations to "co-legislation" (cf. Rickford 2002) in public-private partnership. This outlined a *regulatory space* (cf. Hancher & Moran 1989b) in which public and private actors could contest and agree on the scope and content of legal inscriptions. The idea of acting in the name of "the State" kept a focus on the high-level objectives of Government among the reform actors who came to agree on the law reform programme. The proposed legislation was also assigned a "spacing capacity". In that capacity, law was supposed to frame market-based enforcement mechanisms for the operationalisation of ideas of "co-

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<sup>33</sup> Similarly, Hunt (1993, p. 308) points at processes of "unification, concentration, condensation, and globalisation" in the making of state-law.

<sup>34</sup> Cf. Miller's (1990) description of the role of accounting in late-17<sup>th</sup> century France in the creation of a system of inquiry that would allow the King to govern his territory. Here, the codification of accounting rules in law followed a programme of making corporate activities knowledgeable to the central organs of "the State" and to allow for direct interventions.

governing” the economy in public-private partnership. The introduction of the “inclusive” directors’ duties and a mandatory OFR in statute was expected to outline the range of legitimate participants as well as their terms of debate for continuous contest over the economic, social, and environmental activities of British companies in extra-legal spaces. From the point of view of the CLRSO, company law was supposed to provide “the infrastructure which enables people to collaborate in productive business relationships, generating the wealth on which the whole community depends” (CLRSO 2001, para. 3). This links to a more general view of regulation as “processes of material and discursive construction” which make possible and facilitate “certain forms of social relations while discouraging and disadvantaging others” (Hunt 1993, p. 325). The construction of “stakeholders” as actors with a legitimate role in monitoring and challenging the activities of business enterprises on the basis of published non-financial and future-oriented information in the proposed combined regime of law and accounting, therefore, illustrates earlier theories about the role of law in framing regulatory authority of local and dispersed centres of calculation and empower them to act in the name of “the State” (Rose & Miller 1992):

*“[L]aw constitutes or participates in the construction of a terrain or field within which social relations are generated, reproduced, disputed and struggled over, the most important implication being that within such a field [...] the legal discourses in play both place limits of possibility on social action and impose specific forms of discursive possibility.” (Hunt 1992, pp. 31-32)*

Overall, this chapter finds that the CLR was a unique event in which the conceptualisations of law changed significantly. The observation that rules-based, principles-based, and market-based modes of governing permeated each other in the agenda-setting process supports Hunt’s (1993) criticism of viewing company law as an autonomous and clearly demarcated system. In this case, the close links between law and accounting during the agenda-setting process for a mandatory OFR seem to be part of a wider alignment between law and “the economy”. The rise of programmes of “co-legislating” and “co-governing” suggests that laws and markets were no longer seen as opposing ends of a regulatory spectrum as suggested in the “liberalisation” and “de-regulation” rhetoric of the Thatcher era (Moran 2003, p. 5). Instead, the market-ethos of the 1980s seems to have been replaced during the CLR by a mix of interventionist and market-focused rationales which give rise to “new”

programmes of co-governing the economy in public-private partnership. This leads to the conclusion that aspirations to “the State” and “the market” not only co-existed but re-enforced each other in the agenda-setting process for a combined regime of legal and accounting provisions.

The next chapter outlines the implications of the findings from this and the previous chapters for the changing role of accounting in government which emerged alongside a “mistrust in numbers” in accounting reform in the UK starting in the late 1980s.

## Chapter 5

### RETHINKING ACCOUNTING, REGULATION, AND ECONOMIC GOVERNANCE

*“When there is a radical transformation of ideas [...] whatever made the transformation possible leaves its mark on subsequent reasoning.”*

*(Hacking 1991, p. 184)*

#### 1 Accounting and the economy

The growth of accounting numbers as “a form of economic intelligence” (Hopwood et al. 1990, p. 76) has been linked to a more general “pursuit of objectivity” (cf. Porter 1995) in the ways social and economic life is governed. This, in turn, is linked to the increasing influence of a financial mentality in many spheres of social and economic activity in the last decades of the 20<sup>th</sup> century (cf. Fligstein 1987; 1990). Researchers in this field have argued that the central role of accounting in governing social and economic life derived largely from the expectation that accounting *numbers* represented an objectified reality which reduced the complexity of economic reality (Miller 1990; Rose 1999, pp. 204-205; Miller 2001). These numbers have been described as the outcome of a process of classification and quantification in which the diverse objects and activities that constituted the business organisation were rendered countable, comparable, and could be aggregated in monetary terms (Power 2004). The process of quantification and monetarisation has been held to create consistency between highly aggregated accounting numbers and economic decision models. This argument is based on the view that the figures provided by accounting practices were independent of the subjective judgements and political interests of those who produced them, or were at least perceived to be (Lee 1995; Porter 1995; Miller 2001). Consequently, economic decision-making on the basis of accounting numbers has been depicted as a technical act which was distanced from both the experience, status, or knowledge

of the persons who made the economic decisions, and from the actions that they empowered or constrained (Robson 1992; Rose 1999, pp. 198 & 208).

This translatability between accounting practices and actions carried out in the name of concepts derived in large part from economics has been examined in previous studies, and used to explain the appeal of accounting numbers as a generic reference-point for addressing various questions of governance (Miller 1998b). The link between the calculative practices of accounting and economic decision-models allowed accounting to be viewed as a form of mobile knowledge that created possibilities for distant centres of power to act upon remote locales (cf. Miller 1990; Miller & Rose 1990; Hopwood 1992; Robson 1992). It also helped explain how, within neoliberal regimes of governing accounting could contribute to the aligning of individual and organisational activities with economic ideals of efficiency and effectiveness, without direct intervention being required (Miller 2001).<sup>1</sup>

This thesis has suggested that these arguments about the roles of accounting in economic governance need to be supplemented by an analysis of those moments when the 'objectivity' of accounting is destabilised. It has been argued above that the Operating and Financial Review (OFR) was indicative of a series of destabilising moments in which the neutrality and objectivity which has typically been associated with accounting numbers was called into question. These destabilising moments have been called a "mistrust in numbers", even if accounting numbers have been supplemented rather than abandoned in the process. It has been suggested that the rise of this "mistrust in numbers" during the last two decades of the 20<sup>th</sup> century was made possible by increasing concerns with "transparency" in elaborations of the means and ends of seeking to govern economic life. The "mistrust in numbers", which has been analysed in this research, was also characterised by a growing distrust in those who were responsible for the production of accounting numbers. These doubts about financial reporting were translated into calls for accounting to operationalise an abstract ideal of "transparency" in economic governance. As a transparency mechanism, accounting was expected to reveal the underlying complexity and subjectivity of economic

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<sup>1</sup> The transformation of governance in the name of a financial mentality and neoliberal ideals has, for instance, also been observed in the spheres of healthcare and in programmes of public management reform in the UK (Rose & Miller 1992; Kurunmäki 2008; Miller et al. 2008).

reality by representing a wide range of social activities and practices in more than aggregate financial values.

Although the “mistrust in numbers” that has been observed in the OFR events unsettled the ways in which the fundamental role of accounting numbers in economic governance has been typically defined, it did not suggest their abandonment. Nor did it propose a retreat from viewing accounting as a means for making complex objects and processes comparable and calculable. As this study shows, claims regarding the representation of economic reality in accounting were not questioned during the OFR events, despite the question of how far financial reporting numbers represented a “factual knowledge” of economic relations and activities (Porter 1995, pp. 50-51; Young 1995; Miller 2001). This is consistent with the notion of “trust in numbers” (cf. Porter 1995) which recognised that accounting representations of the objects, processes, and relationships that constitute economic life never unambiguously matched economic reality (Robson 1992).

The remainder of this chapter looks at the implications that the study of the OFR events in the UK has for thinking about accounting, regulation, and economic governance. The discussion is organised in three major parts. Section two that follows summarises the key questions that guided the empirical analysis in this thesis. That section also reiterates the key empirical findings from the analysis of the rise of a category of non-financial and future-oriented reporting in UK policy debates during the 1980s and the 1990s, the extension of the boundaries of accounting-standard setting at the British Accounting Standards Board (ASB), and the interplay of law and accounting during the British Company Law Review (CLR). In section three, the focus is on the concepts and methods that have been used in addressing the destabilising moments of a “mistrust in numbers”. They are reviewed in three stages which reflect upon the conceptual approaches that have been used to study multiple aspects of change in accounting, regulation, and government. The third section also briefly discusses the combination of a case study design with ideas of *genealogy* and *eventalisation*, and outlines the benefits of collecting the empirical data for this study from archives as well as through interviews. In section four of this chapter, a number of suggestions are put forward concerning the interlinking of accounting, regulation, and rationales for the

governing of economic life. The section further elaborates the proposal that the OFR event illustrated a significant rethinking of accounting as a technology of transparency which is expected to provide a means of revealing an underlying complexity and subjectivity of economic reality. The observation of close links between non-financial and future-oriented accounting and ideas of governing economic life according to a high-level ideal of “transparency” also has wider implications for thinking about the role of accounting as an element of regulation by revelation. The section ends with a discussion of the possible implications of the OFR for rethinking economic governance as a mode of co-governing that intrinsically links the regulatory powers of “the State” and “the market”.

## **2 The OFR events in the UK**

This research has been concerned with three interrelated questions directed at analysing the destabilising moments of a “mistrust in numbers” that challenged conventional conceptualisations of accounting in government. They aimed to explain the problematisations of financial reporting numbers as an issue for governing and their translation into regulatory reform projects in the last two decades of the 20<sup>th</sup> century. First, there was the question of how a “mistrust in numbers” gave rise to a new category of non-financial and future-oriented accounting. The second question was how it changed perceptions concerning the roles of accounting in economic governance. Third, this thesis addressed the question of the linkages that could be discerned between these destabilising moments in the sphere of financial reporting, and wider concepts of how economic life should be governed. These questions were addressed empirically through the study of the emergence of the OFR as a regulatory issue for financial reporting standard-setting and company law in the UK in the 1990s. The voluntary and the mandatory OFR in the UK were selected as case studies for this research because the ASB was the first national standard-setter which published guidelines for voluntary statements by directors on the operating and financial position of the business, its future objectives, and plans for successfully achieving them. The UK was also the first jurisdiction to propose a statutory requirement for the presentation of an OFR in the annual report of companies. Similar regulatory frameworks have since emerged in other countries, too, and have become an issue for transnational



regulators and standard-setters, such as the European Union (EU) or the International Accounting Standards Board (IASB).

Chapters two, three, and four of this thesis each offered insights into the destabilising moments, during which conventional ideas about accounting and economic governance were called into question. The analysis in chapter two showed how the process of moving accounting into new territory became closely enmeshed in re-conceptualisations of the broader means and ends associated with the governing of British companies in discussions concerning financial reporting standard-setting, corporate governance, and public economic policy making. It identified the multiple and changing perceptions of economic reality in business management which had contributed to viewing accounting practice also as non-financial and future-oriented. The discussion in chapter two showed that the global economic, technical, and political developments of the 1980s and 1990s strongly influenced a new way of thinking about the governance of British companies in increasingly global and dynamic competitive environments. These developments drew on ideas of “strategic management”, “financial management”, and “social and environmental responsibility” in discourses of managerial “best practice” and of the more general role of business in society. Chapter two also showed that the shifting expectations about managerial “best practice” led to a marked questioning of the relevance of financial reporting numbers in economic decision making. The perceived discrepancy between the processes and objects captured in the financial statements and those that were seen to make up the “reality” of managerial decision-making constituted an important empirical factor in the rising demand for new measurement and reporting practices that were expected to capture financial as well as non-financial factors. Chapter two concluded that the emergence of new ideas about the programmes and technologies economic life in the UK was an indicator for a wider “strategisation”, “marketisation”, and “socialisation” of the language of management and governance throughout the last two decades of the 20<sup>th</sup> century.

Chapters three and four focused more explicitly on the rise of regulatory reform proposals in the arenas of accounting standard-setting and company law. They explained how a “mistrust in numbers” gave rise to demands for regulating non-financial and future-oriented reporting as part of the financial reporting framework.

Chapter three studied the introduction of guidelines for voluntary OFR reporting by the ASB in 1993. The chapter traced the programmatic objectives which led to the OFR becoming an agenda issue for the ASB. The analysis explained the expansion of the mandate of the UK standard-setter beyond a traditional focus on the financial statements. It showed that in order for the ASB to be able to intervene in the preparation of supplementary narratives, it would have to meet more expectations than just those related to the alignment of the proposed guidelines with technical quality criteria. In the process of shifting the boundaries of accounting standard-setting in the UK, the ASB was also required to demonstrate it was able to continue conventions of thought leadership, hitherto attributed to professional standard-setting in the UK, and to show awareness of international regulatory developments in the US and Canada. This led to a situation in which multiple ideas of governing placed different – partly complementary, partly competing – demands on the role and mandate of the ASB in dealing with the standardisation of OFR reporting. Chapter three concluded that the expansion of the regulatory agenda of the ASB into the field of non-financial and future-oriented reporting was part of a wider reconfiguration of ideas on governing which played out in standardisation projects in accounting. By the time the OFR project was launched in the early 1990s, UK accounting standard-setting had been placed at the intersection of “the profession”, “the market”, and “the public interest” – a position which had a noticeable effect on the ways in which the boundaries of accounting reform were set.

As chapter four illustrated, a process of seeking to align public and private spheres of ordering economic activities was also a key factor in the growing calls for a mandatory OFR during the British Company Law Review (CLR). The chapter outlined how a process of realigning law, accounting, and “the State” led to the inclusion of non-financial and future-oriented reporting on the agenda of the CLR. The discussion illustrated how a combined regime of law and accounting emerged as a “solution” to “problems” with the international competitiveness of the British economy. The introduction of a general framework of “inclusive” directors’ duties in company law was supposed to focus the attention of directors on factors that were perceived to promote the success of the company in times of *new global competition*. This included, amongst other issues, a long term perspective on decision-making and goal-setting, the proactive management of stakeholder

relations, and consideration of the impact of the activities of the business on the environment and the wider community. At the same time, OFR reporting was expected to make this regulatory regime work. Narrative statements on strategies, resources, and objectives were assigned a role in rendering the application of “best practice” visible and amenable to interventions by “the market”. Chapter four concluded that the CLR was a unique event in which law and the economy were closely aligned. Chapter four, therefore, suggested greater attention should be paid to the intersection between “the State” and “the market”. This meant to understand the interplay of law and accounting in regimes of governing that were, on the one hand, inscribed in centralised state-laws, but, on the other hand, supposed to be widely dispersed in private governance networks.

### **3 Explaining destabilising moments**

To make sense of the destabilising moments of “mistrust in numbers” and the rise of regulatory frameworks for non-financial and future-oriented reporting since the late-1980s, this thesis drew upon a set of interlinked literatures from many different areas and disciplines.<sup>2</sup> A small number of papers that addressed similar processes of accounting change, in which the roles and purposes of the financial statements as an issue for governing were called into question, inspired the conceptual and methodological approach to the study of the OFR events in this research. They proposed studying changes in financial reporting in terms of the constellations of events, processes, and ideas (Burchell et al. 1985) in which financial reporting numbers were problematised and calls for non-financial and future-oriented accounting emerged (Robson 1991). Further, these studies suggested that regulatory changes could be explained in large part in terms of the programmatic ideas in whose name financial reporting reform was mobilised (Young 1995) and the spaces in which regulatory interventions in accounting were agreed upon (Young 1994). In addition, this research used ideas from socio-legal scholars to explain the moments in which accounting was caught up in the making of centralised forms of regulation

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<sup>2</sup> The accounting literature that has been referred to in this research relates to multiple strands of writings on the role of accounting in organisations and society, which have attracted considerable interest in accounting research over the past 30 years (cf. Burchell et al. 1980; Hopwood & Miller 1994; Napier 2006). These studies have established an interdisciplinary discourse of accounting from the perspective of multiple concepts and theories, such as new institutional perspectives in sociology (cf. Powell & DiMaggio 1991) or Foucauldian writings on *governmentality* (cf. Burchell et al. 1991; Miller & Rose 2008a). In addition, political economy approaches, which have not been further drawn on in this research, have emphasised the study of power relations in research on the roles of accounting in organisations and society (cf. Tinker 1980; Cooper & Sherer 1984; Puxty et al. 1987).

in state-law. This interdisciplinary strand of research has focused on the intersection between law and society from a variety of perspectives such as sociology, history, political science, or anthropology (Friedman 1986). These studies share a view of law and regulation as social practices which equally shaped and were themselves shaped by broader social, political and economic ideas, institutions and relations (cf. Friedman 1986; Banakar 2009).

This thesis suggested that it was crucial to bring these conceptual considerations together to redraw and explain the complex processes in which the abstract programmatic ideas of economic government and the particular practices for intervening in economic activities were problematised, reinvented, and realigned in the last two decades of the 20<sup>th</sup> century. The next sub-section reflects in more detail upon the benefits and limitations of drawing upon studies of *governmentality*, the concepts of the *accounting constellation*, *regulatory space*, and *logics of appropriateness* in generating additional insights into the different processes of problematising financial reporting numbers as an issue for governing. The discussion outlines how the concepts complemented each other and helped to study changes in accounting and regulation as elements of the complex and always fluid networks that govern economic life. The remaining two sub-sections outline the implications the use of a multi-concepts framework had for the methodological approach in this thesis. They review, first, the combination of case studies and notions of *genealogy* (Foucault 1980a, p. 140; Miller & Napier 1993) and *eventalisation* (cf. Veyne 1979a; Foucault 1991d) in the research design; second, they outline the benefits of using archives and interviews in the data collection and analysis.

### **3.1 Explaining change in accounting, regulation, and government**

This thesis has suggested that the rise of non-financial and future-oriented accounting in accounting standard-setting and regulation in the UK in the 1990s can be analysed by considering the multiple events and processes through which accounting, regulation, and government have been called into question. These processes of change were seen to be constituted in discursive processes of *translation* and *problematization* (cf. Callon 1980; 1999) between multiple accounting and non-accounting events, high-level ideas of governing business enterprises and the economy at large, and specific practices of government, such as

law and accounting (cf. Miller 1991; Robson 1991; Rose & Miller 1992; Miller 1998a).

Ideas of accounting as an element of *governmentality* helped in framing more broadly the programmatic shifts which gave rise to the doubts about financial reporting numbers as an issue for governing in the OFR events. They led this study to pay greater attention to the rationalising language which outlined governance in terms of *rationalities*, *programmes*, and *technologies*, allowing for reflections about wider changes in the language of framing the organisation and governance of economic activities in the UK (cf. Miller 1990; Miller & Rose 1990; Rose & Miller 1992; Miller & Rose 2008b). As part of that process, changes in accounting regulation were also viewed as processes of continuous failure and reform in which the solutions of the past became the problems of the present (Miller 1990; Miller & Rose 1990, p. 10; Miller & O'Leary 1993; Hunt 1994, pp. 79-80 & 82; Miller 1998b, p. 606). In addition, references to a sub-strand of writings on the law-society interpenetration, which approached the study of law from the perspective of *governmentality* (cf. Hunt 1994), helped to address the close alignment between public and private spheres of ordering conceptually. They suggested the importance of seeking to bring closer together the study of accounting and law as elements of regimes of governing that are widely dispersed in private governance networks, but centralised around a notion of "the State" at the same time. However, to have limited the conceptual framing of this research to the concept of *governmentality* would have restricted the study of the rise of non-financial and future-oriented accounting as an issue for financial reporting regulation. Studies of accounting and high-level ideas of governing have so far largely failed to address the factors that made the linkages between the two possible and allowed for their incorporation in regulatory reform projects. This research, therefore, addressed the question of how regulatory issues and mandates were constructed through references to additional analytical concepts. They included the concept of the *accounting constellation*, a notion of *regulatory space*, and ideas of *logics of appropriateness*.

This thesis has used the concept of the *accounting constellation* (cf. Burchell et al. 1985) to analyse the processes through which accounting practices and ideas of governing economic activities have emerged alongside each other. It has further developed this concept by examining the *local* and *delocalised* discourses that seek

to operationalise accounting practices. The distinction between *local* and *delocalised* arenas of accounting change provided a way of examining the distinct, yet intrinsically linked levels on which accounting in governance reform debates is problematised. The idea of *delocalised* constellations gave meaning to the somewhat abstract ideas of accounting as an issue of managerial decision making. The idea of *local* constellations helped illuminate those policy discourses in the UK that linked their distinct governance concerns to the abstract ideas of accounting, management, and economic reality

Studying the *local* and *delocalised* discourses at play in this situation illustrated the reflexivity of accounting change in a particular social and institutional context (cf. Hopwood 1983b): On the one hand, the study of accounting change at the intersection of *local* and *delocalised* debates helped analyse the construction of abstract ideas of managerial “best practice” and organisational accounting techniques in extra-organisational forums (cf. Miller 1991).<sup>3</sup> The study of the linkages which developed between various arenas of political discourse and the economic reality of managerial activities made visible the many meanings and rationales that have been associated with non-financial and future-oriented accounting. On the other hand, the study of the linkages between *local* and *delocalised* discourses also revealed the ways in which a rethinking of accounting practice mediated the emergence of new programmes of economic governance and regulation. It showed that a category of non-financial and future-oriented accounting provided the basis for constructing issues such as short-termism or backward-orientation in management as problems in governance reform debates - just the problems it was meant to solve: The view that accounting had the potential to integrate and represent the firm in financial, non-financial, and future-oriented terms made “new” problems of governing economic activities in times of new global competition as well as their “solutions” more intelligible. Although the study of local and de-localised arenas and constellations of accounting change was helpful in illustrating the ways in which a category of non-financial and future-oriented accounting emerged alongside new ways of discussing the “problems” and “solutions” of economic governance in the UK, the analytical approach could not

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<sup>3</sup> For a discussion on how organisational accounting change reflects upon social, political, or institutional demands beyond the boundaries of the organisation and how this enables or constrains certain courses of actions within the organisation, see, e.g. Covaeski and Dirsmith (1986; 1987) or Richardson (1987).

explain the moments in which the accounting issues which were of general concern in governance debates turned into issues for concrete regulatory interventions by private standard-setting organisations or “the State”. To address this issue, this research utilised the concept of *regulatory space* (cf. Hancher & Moran 1989b) to explain the more specific moments in which high-level programmes of governing and specific practices became an issue for regulatory reform.

In this research, *regulatory space* was used as an analytical tool for framing the areas of controversy which formed around the issue of non-financial and future-oriented reporting as an agenda item for accounting standard-setting or law-making. This took the study of accounting regulation beyond a supply and demand perspective proposed in economics-based writings on regulation and policy reform (Watts & Zimmerman 1978, 1979, 1986, 1990; Ogus 1994; Peltzman 1998).<sup>4</sup> Instead, the concept of *regulatory space* focused on the multiplicity of voices involved in the re-imagining of the roles and purposes of accounting in economic governance and their position in the wider cultural and economic context which shaped and was itself shaped by the relations and discourses around regulatory reform events (Hancher & Moran 1989b, p. 297; Black 1997). Although the analytical construct of *regulatory space* was consistent with the proposed socio-legal perspective on regulation as a social phenomenon, the analytical construct could not explain how the mandates of accounting standard-setters or regulators to deal with a particular issue were ultimately agreed upon among competing, complementary, and conflicting sets of practices and discourses (Hunt 1997, p. 116). Therefore, this research also used the concept of *logics of appropriateness* (cf. March & Olsen 1989) to explain the areas of agreement and disagreement on the mandates of accounting regulatory bodies in politically contradictory environments. This allowed for the analysis of the factors that contributed to the temporary stability and legitimacy of the OFR on the agenda of accounting standard-setting and legal reform. The notion of multiple *logics of appropriateness* described the consensus on what was and was not “appropriate” in accounting reform and

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<sup>4</sup> From the normative perspective of a market-failure approach to regulation, regulators seek to overcome market imperfections in the interest of the public (Peltzman 1989; Baldwin et al. 1998a) in order to increase overall “social utility” or “net social benefit” (Diver 1998). Economic welfare justifications also imply a pluralist perception of the regulatory process (Noll 1989). This involves a positive perception of regulatory reform (Cheffins 1999), whereas a positive theory of regulation suggests that capture of the regulator by economically or politically powerful groups drives regulatory reform rather than public interest (Stigler 1971).

explained how even “unusual” developments in financial reporting-regulation, such as the introduction of the OFR, became possible. Although not explicitly discussed in this research, an understanding of these temporary equilibriums may also help to explain regulatory failure. This is because new calls for regulatory reform become more likely when the *logics of appropriateness* outlining temporary stability and legitimacy for regulatory reform in politically contradicting environments begin to shift.

### 3.2 Case studies, genealogies, and eventalisation

In line with the view that “empirical studies of government – of the regulation of madness, health, welfare, production [...] and so forth – do not simplify: they generate complexity” (Rose 1999, p. 277), the methodological framework in this thesis also drew on a whole spectrum of approaches when it came to the collection and analysis of empirical data. Corresponding to the multi-concepts framework, they allowed for the simultaneous analysis of “the micro” and “the macro” in the study of the moments in which the *programmes* and *technologies* of government linked and co-emerged in the OFR events. The notion of *eventalisation* focused the data collection and analysis in this thesis on the “multiple processes” (Foucault 1991d, p. 76) or “small events” (Hunt 1994, pp. 32-33) in which changes in the regulation of financial reporting became possible. Accordingly, the selection of two specific cases, namely the introduction of the OFR to the regulatory agendas of the ASB and the CLR illustrated the emergence of new governance regimes as part of the interactions between the multiple relations, ideas, and processes that constitute single events.<sup>5</sup> These were placed in a wider historical and geographical context by brief comparisons of the OFR proposals of the 1990s with, first, similar calls for reform in British policy debates during the 1970s. This comparison highlighted the different ways of thinking about the roles and practices of accounting, the practices and objectives of business management, and the role of business in society at large. Second, a review of the introduction of similar regulatory frameworks for narrative disclosures in other jurisdictions showed the distinctiveness of the British approach

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<sup>5</sup> However, the focus on the programmatic discourses of reform agents in this study did not explain the assemblage of specific actors in the *regulatory space* or their exclusion from that space (Hancher & Moran 1989a). This research has also not explained the factors that constituted the relative power of the reform actors to shape the regulatory outcomes (Hunt 1994).



in regulating the disclosure of non-financial and future-oriented information as part of the financial reporting framework.

At the same time, the view that regulatory culture was not a “historical constant” imposing itself on all situations (Miller & Rose 2008b) kept the focus on more specific processes, in which different macro-ideas of governing emerged in individual regulatory reform events (cf. Veyne 1979a; Foucault 1991d). By using the notion of *genealogy* this research highlighted the multiple branches of developments and accidental encounters of different practices and ideas that gave rise to the British OFR. It led to the tracing of ideas of non-financial and future-oriented accounting in the various programmatic discourses which contributed to the problematisation of financial reporting numbers as an issue for governing economic activities in the UK. The analysis included short histories of the system of professional self-regulation of accounting practice in the UK, a review of the rise of a notion of “the market” in accounting regulation since the 1970s, and a discussion of the re-conceptualisation of management practice throughout the 1980s. These additional analyses allowed for a more detailed study of the wider factors and events at play in the two cases of regulatory reform under study. They showed how many ideas and practices made up a category of non-financial and future-oriented accounting by the time the British OFR events took place in the 1990s.

### 3.3 Archives and interviews

The data used in this research is based primarily on interviews and archive materials.<sup>6</sup> The study of a wide array of documents, including discussion papers, draft standards, letters of comment, internal memos and correspondence, helped define the field in which accounting change took place. The published and unpublished documents provided the material traces of the events under study: They were the basis on which the key themes, activities, and actors that made up the mandatory and the voluntary OFR events were identified. The analysis of documents and interviews also had an influence on how the collection of empirical materials was structured. For example, a short series of exploratory interviews in early 2005 influenced the case selection for this thesis. The conversations with

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<sup>6</sup> The use of many different types of data to support the quality and robustness of findings in qualitative research has been referred to in the literature as methodological “triangulation” (Bauer & Gaskell 2000). The approach that has been taken in this research was, however, less structured. Different data sources were not selected *ex ante* but were chosen because they had been quoted in other documents or by interview partners.

persons closely involved in national and international accounting standard-setting projects helped identify a research topic that was unique, but – at the same time – had wider implications for future developments in accounting regulation. The documents or interviews were also used to trace further key documents or key persons who have played a role in the drafting of the agenda proposals for a voluntary and a mandatory OFR.

The analysis of published documents was limited by the fact that the material available to the public often took the form of *institutionalised artefacts* (cf. Wolff 2002). That is, its content was already the outcome of a careful rephrasing and structuring of events and decision making-processes (ibid.). Providing a detailed analysis of the points of conflict and their solution during regulatory reform debates was difficult when access to internal documentations of the process of drafting these reports was not possible. This study, therefore, had to make inferences about the key events and debates from the further analysis of additional documents that had been produced at the periphery of the OFR events. These included, for example, the contributions of persons also involved in the ASB project to other forums, a review of newspaper articles covering the OFR debates, and the study of other published comments and research dealing with the events under scrutiny. The collection of empirical data through personal interviews and other forms of direct communication with the persons directly involved in the reform projects at the ASB and the CLR contributed significantly to the advancement of this research. Their personal experience at different stages of the reform processes often provided new insights into the reading of published and unpublished texts. Of course, the *ex post* accounts were not taken to represent an underlying “reality” of events, but they were immensely helpful in understanding the dynamics, wider relevance, and historic developments of the accounting events under study.

Given the benefits of interview data in tracing and explaining the history of regulatory change, it is surprising that only very few studies of standard-setting in accounting draw on interviews with accounting regulators (cf. Young 1994; Ezzamel et al. 2007).<sup>7</sup> The collection and analysis of a wide range of data produced as part of the OFR projects and at their periphery adds methodologically to existing

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<sup>7</sup> Similarly rare seems to be the use of interviews in studies of the implementation of accounting and auditing standards in practice (cf. Mennicken 2008).

studies of the drivers of regulatory change. These studies seem to have been preoccupied with the counting, coding, and classifying of comment letters and the tracing of possible causalities in regulatory reform (Zeff 2007a). In addition, the combination of different types of qualitative data in the study of regulatory reform in this research allowed to step beyond a search for objectified causalities or “origins” (Foucault 1980a, p. 140) and allowed to trace the historically and spatially specific factors and encounters that made regulatory change possible.

#### **4 Conclusions on accounting, regulation, and economic governance**

This thesis has argued that ‘trust in numbers’ has been destabilised through various events. But it also acknowledges that this questioning of the neutrality and objectivity of financial reporting numbers may only be temporary. It is possible that the calls for supplementary non-financial and future-oriented statements in financial reporting, will be replaced by future calls for improvement in the figures contained in the financial statements. Nevertheless, the findings from this study suggest that the OFR events indicate a significant rethinking of the roles and techniques of accounting and regulation in economic governance during the last quarter of the 20<sup>th</sup> century.

This section lays out the three key contributions of this thesis to the accounting, governance, and regulation literature; and outlines possible avenues for further research. It discusses how the OFR events constituted a significant challenge to conventional views of the role of accounting as, first, a means for representing economic reality in financial terms and, second, a mechanism for monitoring and acting upon economic activities in a neutral and apolitical manner. The third subsection extends the discussion of accounting as a “technology of transparency” and a means of “regulation by revelation” to a discussion of the mandatory OFR event in the UK as a possible indicator for the rise of regimes of co-governing the economy governing that intrinsically link “the State” and “the market”.

##### **4.1 Technology of transparency**

This thesis suggests that the calls for non-financial and future-oriented reporting during the OFR events in the UK indicate a wider shift in accounting from a focus on aggregation and the reduction of complexity to viewing accounting as a technology of transparency. As a technology of transparency, accounting is

supposed to capture and represent the multiple financial and non-financial, quantitative and qualitative aspects of business decisions in equally diverse measurement and reporting systems. This proposed rethinking of accounting is based on the observation that the calls for additional non-financial and future-oriented reporting significantly challenge the view that accounting as an element of economic calculation is mainly concerned with the aggregation and ordering of complex economic processes and their representation in neutral and apolitical terms (Hopwood 1992; Miller 1994b; Miller 2001; Power 2004). Instead, this study has shown that economic decision-making has been recognised as a process that involved personal judgement and that required managers to deal with a mix of qualitative and quantitative, financial and non-financial factors. This research, therefore, proposes that accounting was increasingly expected to extend the scope of the issues it represented and the techniques for representing them in order to make this complexity of the economic reality of entrepreneurial activities intelligible and calculable.

The conclusion that the OFR indicates a wider shift in thinking about accounting as a means of revealing the underlying complexity and subjectivity of economic activities is further supported by other accounting studies that have observed an increase in calls for greater representation of complexity within performance measurement and reporting systems since the mid 1980s. The debates that have been observed in these cases include, for example, proposals to capture performance in economic, social, and environmental terms in so-called “triple bottom line” accounting; the production of risk maps; or activity based costing (Power 2004). Calls for accounting to provide transparency on an underlying complexity of economic reality have also occurred in debates on accounting for brands and other intangibles (see, e.g. Barwise et al. 1989) as well as in the ValueReporting™ initiative by the accounting firm PricewaterhouseCoopers (Eccles et al. 2001). Furthermore, Cooper and Robson (2006) pointed to the rise of a language of transparency in elaborations of accounting concepts and practices in corporate and public sector governance and regulation.<sup>8</sup>

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<sup>8</sup> In the area of public sector governance, transparency relates to ideas of public scrutiny in administrative and regulatory processes and ideas of “open government” at all levels of society (Grossman et al. 2008). They

The rethinking of accounting as a technology of transparency also has wider implications for the analyses of accounting standard-setting and regulation. So far, standardisation projects in accounting have been described as further enhancing the presumed neutrality and technicality of the process of producing accounting measures and reports (Robson 1992; Power 2004).<sup>9</sup> Although the regulatory frameworks for a voluntary and mandatory OFRs were also concerned with the standardisation and stabilisation of their structure, they did not aim to ensure a “mechanical objectivity” (Porter 1995, p. 4) of accounting reports. Instead, the OFR was supposed to provide a vehicle for managers to explain in their own words how they made sense of increasingly global and dynamic competitive environments. Thereby, the OFR standardisation projects explicitly allowed for variations and subjective statements in external reporting, which supports the view that the OFR was a case of viewing accounting as a means of giving visibility to an underlying subjectivity and complexity of the economic relations and activities that it was supposed to represent.<sup>10</sup> The findings from this study, therefore, suggests thinking more widely about the governing rationales in whose name accounting is mobilised, and which it helps to make intelligible in governance reform debates. Other authors have proposed that accounting has become “an indispensable ‘transparency infrastructure’ without which a modern economy cannot function” (Holzner & Holzner 2006, p. 224). This relates to the idea that ideas of accounting as a means of revealing rather than concealing the different aspects of economic life allow a broad range of policy debates to link their distinct concerns to accounting.

This thesis supports the view that accounting has increasingly been linked to a more general transparency-discourse in governance reform debates. While the issue of transparency has not been addressed explicitly in the core chapters of this thesis, it provided a common theme in the calls for accounting and governance change. For example, transparency mechanisms appealed equally to the supporters of a shareholder rationale in private sector governance, who aimed at facilitating the functioning of capital markets, and to the supporters of a stakeholder rationale, who

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have become visible, for instance, in the emphasis on “notice and comment” procedures in regulatory decision making (BRTF 1998; OECD 2002).

<sup>9</sup> On the increase in standardisation projects as a form of regulation, see, e.g. Brunsson and Jacobsson (2000) or Tamm Hallström (2004).

<sup>10</sup> Olesen (2008) calls the accounts that are produced in the name of transparency “situated revelations”.

favoured transparency as a means of democratic deliberation. In addition, ideas of transparency aligned different political views about how economic life should be governed. They provided a common reference point for those who emphasised individualism and entrepreneurship, those who preferred voluntary regulatory frameworks, and those who emphasised formalised behavioural standards and accountability mechanisms. It was, however, beyond the scope of this thesis to engage in more detail with the emerging literature on transparency in governance (cf. Holzner & Holzner 2006; Hood & Heald 2006; Florini 2007; Garsten & Lindh de Montoya 2008c; Grossman et al. 2008). These studies propose a more general rise of notions of transparency into a widely shared rationale of governing individuals, organisations, and societies since the mid-1980s. They have described the term as a “travelling keyword” (Garsten & Lindh de Montoya 2008a, p. 283) which easily connects with other terms and practices, facilitates communication, and aligns actors towards a common point of direction (Pateman 1970; Florini 1996; Sage 1999; Birkinshaw 2006; Holzner & Holzner 2006; Garsten & Lindh de Montoya 2008b).<sup>11</sup> This has been explained with the appeal of the abstract vision of transparency to “unveil the hidden” in the increasingly dynamic environments that were brought about by political and economic globalisation trends (Garsten & Lindh de Montoya 2008b, p. 19).

Further research may draw more explicitly on the rethinking of the practices and rationales that make up accounting as an element of economic calculation in relation to the rise of transparency programmes in national and transnational regimes of governing. These studies would contribute to the understanding of how accounting becomes “what it was not” (Hopwood 1983b, p. 289), because ideas of transparency may lead to a much wider variety of techniques than those for producing aggregated financial figures being subsumed under the label of accounting. Furthermore, studies of the ways in which accounting as a technology of transparency is called upon to “solve” a range of new “problems” of government may help to explain the continued and apparently unquestioned appeal of accounting as a technology of government even in moments of crises of trust in

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<sup>11</sup> This becomes possible because the ideas and practices of transparency are not clearly demarcated (cf. Grossman et al. 2008), but part of a “cluster of ideas” (Garsten & Lindh de Montoya 2008b, p. 3) that allows the use of the concept across organisational, social, cultural, and national boundaries and to mobilise a wide range of actors in the name of transparency (ibid.). Accordingly, a governing rationale of transparency differs according to the “areas of meaning” that refer to it in distinctive ways (Grossman et al. 2008).

accounting numbers. In addition, future research may help to explain how widely shared aspirations to an abstract notion of “transparency” in economic governance contribute to the blurring of the boundaries between financial accounting and other practices that seek to make the economic reality of companies visible and governable. This thesis has only briefly touched upon the shared calls for transparency on economic reality in financial reporting standard-setting, corporate governance, and public economic policy-making in the UK that brought ideas of reporting in the financial accounts, corporate governance statements, the Directors’ Report, and in voluntary social and environmental disclosures closer together. Further research might engage more closely with the relationship between accounting and other forms of corporate disclosure. Future research might also study the potential for aligning managerial and financial accounting; internal and external accounting in transparency-oriented accounting regimes. Although not elaborated in more detail, the findings from this research suggest significant parallels between ideas of decision-usefulness in debates on providing information on non-financial and future-oriented strategic success in external financial reporting and internal performance measurement and management reporting systems.

#### **4.2 Regulation by revelation**

This thesis also proposes that the introduction of the voluntary and the mandatory OFR indicates a growing emphasis on ideas of “regulation by revelation” (cf. Florini 2003). This links to the idea that transparency has been closely associated with the creation of regimes of trust, accountability, and control in the context of economic governance of business enterprises and the economy at large (Holzner & Holzner 2006; Garsten & Lindh de Montoya 2008b; Grossman et al. 2008). Viewing accounting as a technology of transparency implies a rethinking of the modes of intervening in economic activities. The OFR events illustrate how the process of discharging corporate accountability was increasingly seen in terms of making the complexity and subjectivity of economic decisions traceable and, thereby, comprehensible to a wide range of stakeholders. In addition, this study also points at a growing distrust in those who were seen as responsible for the

production and quality of accounting numbers, including business managers and accounting professionals..<sup>12</sup>

These findings on accounting as an element of “regulation by revelation” challenge the view that the regulation of financial reporting was concerned with replacing personal judgement and expertise in the process of producing accounting reports, turning it into a technical and apolitical act (Robson 1992). Instead, the acknowledgement that the narratives and numbers that were produced in the name of transparency would tell only one of many possible stories places the OFR within a wider gradual shift to a “show me” relationship between organisations and society. It defines a form of accountability in which business managers are expected to demonstrate their activities were in the interest of shareholders, wider stakeholder groups, and society at large (Roth 1999). In line with that view, the introduction of OFR-type reporting frameworks sought to encourage managers to present their individual evaluation of the business, and to explain the objectives and strategies of the business, from their point of view.

As an element of regulation by revelation, accounting reports were supposed to create opportunities for new forms of disciplining corporate activities and for re-establishing accounting as a “technology of trust” (Vollmer 2003, p. 366). The introduction of the OFR aimed to make a broad range of processes and relations visible in order to open them up to continued scrutiny and contestation by internal and external stakeholders.<sup>13</sup> Publicly available information about the financial as well as non-financial spheres of corporate activities in voluntary and mandatory OFRs was supposed to enable shareholders as well as other parties with or without a direct stake in the company to scrutinise and contest, first, the elements of subjectivity and ambiguity in the managerial decision-making process and, second, the scope of corporate activities and responsibilities. In turn, the accountability mechanisms that were established through self-reporting in narrative management commentaries were supposed to encourage managers to engage with their own

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<sup>12</sup> Other studies have observed similar links between calls for greater transparency and accountability and growing public uncertainty and decreasing trust in centres of power, such as Governments, corporations, and professions in times of increasingly dynamic and international economic activities (Holzner & Holzner 2006, p. 9).

<sup>13</sup> Other studies of financial reporting regulation already recognised the role of formally inscribed accounting regulations in empowering actors who did not directly participate in the regulatory reform debates to monitor and intervene in corporate activities (Young 2006).



conduct and practices by creating responsibility for judgements and their consequences. This means that the OFR as an instance of regulation by revelation implied a process of self-discipline and self-learning that took a more reflexive perspective on the management principle of “what gets measured gets managed”.<sup>14</sup>

Consequently, this research suggests that the OFR was a case of re-allocating the responsibility for economic decisions with individuals in accountability regimes that sought to build trust through subjective narratives and financial as well as non-financial measures. This challenges the view that accounting contributes to the regulation of managerial activities by making corporate performance visible in highly aggregated and impersonal financial figures. So far, the regulatory effects of accounting on managerial decision-making have been linked to a self-disciplining effect of translating the outcomes of individual activities and decisions into accounting *numbers* that could be compared to norms and standards of performance that were defined elsewhere (Miller & O'Leary 1987). The willingness of individuals to comply with these standards was established through the apparent technicality and neutrality of the process of translating personal attributes and activities into impersonal accounting terms and the assumption that the standards of economic performance against which they were judged were equally neutral and apolitical (cf. Miller & O'Leary 1987; Miller 1990; Power 2004).

It is, however, too early to tell if the OFR events and other calls for more complexity in financial reporting imply a growing “trust in narratives” as a mechanism for discharging corporate accountability. Further research may, therefore, begin to disentangle the relationship between numbers and narratives in regimes of governing that seek to create accountability for and trust in the activities of corporate decision-makers. These studies may, for example, examine the political controversies that arise in the process of implementing OFR type reports in practice and study the ways in which the scope of OFR reporting is negotiated. In particular, the ambiguous role of large audit firms in the calls for non-financial and future-oriented narratives in corporate reporting would merit further research. Although not further discussed in this thesis, the OFR events in the UK point at significant tensions between a desire to drive financial reporting change and to open up new

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<sup>14</sup> For a further discussion of the self-disciplining effect of transparency-based accountability regimes on corporate conduct, see e.g. Florini (1998; 2003; 2007).

business opportunities for consulting work and a reluctance to expand the scope of their audit responsibilities into these new areas of corporate reporting. Furthermore, future studies of the relationship between numbers and narratives in regimes of regulation by revelation may look at attempts to establish “best practice” in the area of narrative reporting on the non-financial and future-oriented aspects of the business. The analysis of the opinion papers, research, and prizes that are produced and awarded by various organisation may shed further light on the question how far the accounting reports of the future will be expected to report on current and future performance in terms of financial and non-financial, quantitative and qualitative information (see, e.g. CIMA 2002; ACCA 2005; PwC 2005; ASB 2006; IASB 2008; PwC 2008).

#### **4.3 Co- governance by “the State” and “the market”**

Finally, this thesis proposes that the voluntary and the mandatory OFR indicate a significant re-thinking of the relationship between public and private spheres of ordering economic activities. The OFR is a case of seeking to co-govern the economy through regulatory regimes in which the regulatory powers of “the State” and “the market” do not oppose, but reinforce each other. As this study shows, both the process of OFR regulation in the making and the proposed regimes for the voluntary and the mandatory OFR in action sought to closely align public and private spheres of organising economic activity. The use of the concept of *regulatory space* for the study of the agenda-setting processes at the ASB and during the CLR already highlighted the interactions among a wide range of ideas of governing in the name of “the State” and “the market”. Furthermore, the findings from this study suggest that the consensus that has been found in these *regulatory spaces* did not seek to provide closure on the process of contesting the economic, social, and environmental responsibilities of business organisations once the proposed laws or guidelines were put into action. Instead, the OFR sought to govern corporate activities through regulatory regimes that defined behavioural standards in laws, standards, or guidelines, but at the same time opened the governance process to further contest and agreement about the roles and responsibilities of individual business organisations.

The regulation literature has put forward several concepts to explain the phenomenon of state-enforced and yet market-based modes of regulation which rest

to a great extent on self-control and public scrutiny rather than direct intervention by national governments. For example, ideas of *enforced self-regulation* and *responsive regulation* (cf. Ayres & Braithwaite 1992) have focused on the delegation of regulatory powers from “the State” to the markets and on the different degrees of formal regulatory backing of otherwise self-regulated standards.<sup>15</sup> Related studies of the rise of state-regulation in the deregulatory environment of the *new regulatory state* (cf. Majone 1994) have proposed to view the process of formalising market based self-regulation in statute as a colonisation of “the State” in formerly “private” domains of governing (Moran 2003, p. 93). Analyses of the *open corporation* and the concept of *meta regulation* (cf. Parker 2002) have also recognised the interplay between laws and markets in the regulation of corporate behaviour. They have proposed to view these regimes of governing as a “triple loop” of regulation and self-regulation (ibid.) in which the process of intervening in managerial activities is opened up the governance processes to democratic deliberation through dialogue with a wide range of stakeholder groups (Parker 2002; Baldwin 2004).

However, regulation studies of the links between “the State” and “the market” in economic governance do not question a fundamental partition between the spheres of regulation and that of economic activity, but continue to view them as distinct and otherwise self-referential systems (cf. Teubner 1993; Luhmann 1995).<sup>16</sup> In contrast, this thesis proposes that the alignment between law and the economy, which has been observed in the OFR events, indicates a rise in regimes of governing that overcome a dichotomy between public and private spheres of ordering economic activities. Both the voluntary and the mandatory OFR suggest an unusual mix of different ideas of governing that make regulation in the name of “the State” and “the market” not a question of either/or or a question of one dominating the other to different degrees. The cases in this study were characterised by a close interplay and continuous realignment of “private” market-based and “public” rights-based approaches to regulation that blur any boundaries between the two. Writings

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<sup>15</sup> For a discussion on state-regulation in the *new regulatory state*, see also Moran (2000; 2001) or Jordana and Levi-Faur (2004). For studies on the role of independent regulatory agencies and private standard-setting bodies in the governance of economic life in the UK and elsewhere, see, e.g. Majone (1994; 1997), Moran (2001), or Coen & Thatcher (2005).

<sup>16</sup> For further critique of the rule-based conceptualisation of law, see Banakar (2009).

on *governmentality* have already proposed a rethinking of the conceptual distinction between public and private spheres of power. Their perspective on “law as a lived experience” (Hunt 1993) suggests to step beyond a notion of law as a representation of monolithic state power, emphasising the social and ideological dynamics in the creation and implementation of regulatory frameworks (cf. Hunt 1993, 1994, 1997; Banakar 2009). Moreover, this thesis suggests to further develop ideas of law as a social practice in studies of accounting regulation. The OFR events indicate a significant role for both, law and accounting, in the making and shaping of regimes of co-governing the economy in the name of markets and society at large.

Further research might engage in more detail with the processes of making and implementing regulation that crosses the boundaries between “public” and “private” spheres of ordering. Thereby, a focus on the roles of law and accounting might help to explain how possibilities for the co-production of governance by markets, private regulatory bodies, and national or international regulatory agencies emerge. The study of the roles of law and accounting in intrinsically linking “the State” and “the market” in economic governance could, for example, be taken further to study the regulatory responses to the global financial crisis that began in 2007 and had disastrous effects on national economies worldwide. The regulatory responses to the economic crisis are another case of simultaneous calls for “the State” and “the market” to ensure the economic activities of business organisations are in line with wider social and economic objectives. A centralised notion of “the State” has gained a new presence in the British and other international economic rescue and stimulus programmes. In the UK, the measures that were taken by Government included, for example, the reduction of value added tax (VAT), the radical reduction of interest rates, and the introduction of new money into the financial system. In addition to these fiscal and monetary stimuli, Governments have entered the financial services domain, which was until recently the hallmark of the market economy, through direct investments in large financial institutions that otherwise faced insolvency. In 2007 and 2008, the UK Government nationalised the British banks Northern Rock and Bradford & Bingley and, amongst others, acquired a 70% stake in the Royal Bank of Scotland Group. However, although neo-liberal rationalities of government have experienced a significant shake-up following the full or partial nationalisation of some financial institutions, the recent developments

seem far from being a mere return to Keynesian ideas of state ownership and management of nationalised industries. With the objective to return to full private ownership as soon as possible, the recent national economic rescue programmes in the UK and other countries aim at restoring confidence in capital markets. For example, the creation of the private company UK Financial Investments (UKFI) to manage the public investments in a way that maintained commercial freedom for the banks in their day to day business highlights the strong presence of ideas of governing in the name of “the market”. These links between the objective to promote competition “in a way that is consistent with a UK financial services industry that operates to the benefit of consumers and respects the commercial decisions of the financial institutions” (UKFI 2009) and the aim to protect and maintain social and economic justice (ibid.) are, therefore, consistent with the findings on a growing emphasis on processes of co-governing which intrinsically link “the State” and “the market”.<sup>17</sup> In addition, the current national and international regulatory debates imply that future economic governance regimes will place significant emphasis on making the complex networks, transactions, subjective judgements, and power struggles that constitute economic reality more visible and, hence, governable (FSA 2009). The emphasis on disclosure in the proposed regulatory responses to the financial crisis, therefore, supports the view that notions of transparency will continue to play a central role in thinking about the governance of economic life. Correspondingly, this would open up a field for further studies of accounting as a technology of transparency, modes of regulation by revelation, and the co-production of governance in the name of “the State” and “the market” in a mix of accounting and other forms of ordering, such as law.

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<sup>17</sup> In the UK, the wholly government owned company *UK Financial Investments Limited* was created on 3 November to manage public ownership of financial institutions in the UK (UKFI 2009).

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## Appendices

### 1 List of abbreviations

ACCA	Chartered Association of Certified Accountants
ANT	Actor-Network Theory
APB	Auditing Practices Board
ASB	Accounting Standards Board
ASC	Accounting Standards Committee
ASSC	Accounting Standards Steering Committee
ASSC	Accounting Standards Steering Committee
BERR	Department for Business Enterprise and Regulatory Reform
BIS	Department for Business, Innovation and Skills
BR	Business Review
BSC	Balanced Scorecard
CBI	Confederation of British Industry
CCAB	Consultative Committee of Accountancy Bodies
CLR	Company Law Review
CLRSG	Company Law Review Steering Group
CSR	Corporate Social Responsibility
DTI	Department of Trade and Industry
EC	European Commission
ED	Exposure Draft
EU	European Union
FASB	Financial Accounting Standards Board
FRC	Financial Reporting Council
GDP	Gross Domestic Product
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
ICAEW	Institute of Chartered Accountants in England and Wales
ICAS	Institute of Chartered Accountants of Scotland
IFRS	International Financial Reporting Standards
IoD	Institute of Directors
ippr	Institute of Public Policy Research
KPI	Key Performance Indicator
LSE	London Stock Exchange
MD&A	Management's Discussion and Analysis of Financial Condition and Results of Operations
OECD	Organisation for Economic Co-operation and Development
OFR	Operating and Financial Review
OSC	Ontario Securities Commission
RED	Reporting Exposure Draft
RSA	Royal Society for the encouragement of Arts, Manufactures & Commerce (RSA)
SEC	Securities and Exchange Commission
SFAC	Statements of Financial Accounting Concepts
STS	Science and Technology Studies
TUC	Trades Union Congress
VAT	Value Added Tax

## 2 Overview of key reports and discussion papers

Year	Organisation	Title
1969	IASB	Statement of Intent on Accounting Standards in the 1970s
1973	CBI	The Responsibilities of the British Public Company: final report
1975	ASSC	The Corporate Report: a discussion paper
1977	Department of Trade	Report of the Committee of Enquiry on Industrial Democracy (Bullock Report)
1977	Department of Trade	The Future of Company Reports
1988	ICAEW	The Making of Accounting Standards (Dearing Report)
1988	ICAS	Making Corporate Reports Valuable
1988	ICAS	Making Corporate Reports Valuable: the literature surveys
1990	ICAS	Financial Reporting: the way forward,
1991	ASB	The ASB's Future Work Programme
1991	FRC	The State of Financial Reporting
1991	ICAEW	The Future Shape of Financial Reports: research studies,
1991	ICAEW/ ICAS	The Future shape of financial reports,
1992	ASB	Discussion Paper: Operating and Financial Review
1992	Cadbury Committee	The Financial Aspects of Corporate Governance (Cadbury Report)
1993	ASB	Statement: Operating and Financial Review
1994	AICPA	Improving Business Reporting - A Customer Focus
1994	DTI	Competitiveness: Helping Business to Win
1994	RSA	Tomorrow's Company: the role of business in a changing world: interim report: the case for the inclusive approach
1995	DTI	Competitiveness: Forging Ahead
1995	Greenbury Group	Directors' Remuneration: report of a study chaired by Sir Richard Greenbury
1995	RSA	Tomorrow's Company: the role of business in a changing world
1997	Commission on Public Policy and British business	Promoting Prosperity: a business agenda for Britain
1997	Labour Party	New Labour: Because Britain Deserves Better
1998	DTI	Modern Company Law for a Competitive Economy
1998	Hampel Committee	Committee on Corporate Governance: final report
1998	Tomorrow's Company	Sooner, Sharper, Simpler: a lean vision of an inclusive annual report
1999	CLRSG	Modern Company Law for a Competitive Economy: The Strategic Framework
1999	Law Commission and Scottish Law Commission	Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties
2000	CLRSG	Modern Company Law for a Competitive Economy: Completing the Structure
2000	CLRSG	Modern Company Law for a Competitive Economy: Developing the Framework
2001	CLRSG	Modern Company Law for a Competitive Economy: Final Report
2002	DTI	Modernising Company Law (White Paper)

### 3 List of interviewees

<b>Interviewee</b>	<b>Organisation</b>	<b>Date</b>	<b>Duration</b>	<b>Record</b>
Standard-setter A	Standard-setting organisation A	06/01 and 11/04/2005	90 min. 60 min	Notes
Standard-setter B	Standard-setting organisation B	08/02, 15/04, and 19/12/2005	40 min. 50 min. 20 min.	Notes / Taped & transcribed
Consultant A	Consulting firm A	28/02/2006	45 min.	Taped & partly transcribed
Standard-setter C	Accounting firm A	03/03/2006	60 mn.	Taped & partly transcribed
Accounting professional A	Professional accounting body A	27/03/2006	73 min.	Taped & partly transcribed
Accounting professional B	Professional accounting body B	25/04/2006	60 min.	Taped & transcribed, reviewed by interviewee
Standard-setter D	Standard-setting organisation B	21/02/2007	70 min.	Taped & transcribed, reviewed by interviewee
Standard-setter E	Standard-setting organisation B	19/03/2007	15 min.	Notes
Regulator A	Think Tank A	30/08/2007	65 min.	Taped & transcribed,
Standard-Setter F	Standard-setting organisation C	03/10/2007	60 min.	Taped & transcribed, reviewed by interviewee
Regulator B	University A	10/10/2007	60 min.	Taped & transcribed, reviewed by interviewee
Standard-Setter G	Standard-setting organisation C	24/01/2008	60 min.	Taped & transcribed

## **4 Excerpts from relevant legislation**

### **4.1 The Companies Act 1985 (Operating and Financial Review and Directors' Report etc.) Regulations 2005**

#### **234AA. Duty to prepare operating and financial review**

- (1) The directors of a quoted company shall for each financial year prepare an operating and financial review.
- (2) The review must comply with Schedule 7ZA (objective and contents of operating and financial review), save that nothing in that Schedule requires the disclosure of information about impending developments or about matters in the course of negotiation if the disclosure would, in the opinion of the directors, be seriously prejudicial to the interests of the company.
- (3) For a financial year in which -
  - (a) the company is a parent company, and
  - (b) the directors of the company prepare group accounts,the operating and financial review must be a consolidated review (a "group operating and financial review") relating, to the extent specified in Schedule 7ZA, to the company and its subsidiary undertakings included in the consolidation.
- (4) A group operating and financial review may, where appropriate, give greater emphasis to the matters that are significant to the company and its subsidiary undertakings included in the consolidation, taken as a whole.
- (5) If an operating and financial review does not comply with the provisions of this Part relating to the preparation and contents of the review, every director of the company who-
  - (a) knew that it did not comply or was reckless as to whether it complied, and
  - (b) failed to take all reasonable steps to secure compliance with the provision in question, is guilty of an offence and liable to a fine.

#### **234AB. Approval and signing of operating and financial review**

- (1) The operating and financial review must be approved by the board of directors and signed on behalf of the board by a director or the secretary of the company.
- (2) Every copy of the operating and financial review laid before the company in general meeting, or that is otherwise circulated, published or issued, must state the name of the person who signed it on behalf of the board.
- (3) The copy of the operating and financial review delivered to the registrar must be signed on behalf of the board by a director or the secretary of the company.
- (4) If a copy of the operating and financial review-
  - (a) is laid before the company, or otherwise circulated, published or issued without the review having been signed as required by this section or without the required statement of the signatory's name being included, or
  - (b) is delivered to the registrar without being signed as required by this section, the company and every officer of it who is in default is guilty of an offence and liable to a fine."

## **SCHEDULE 7ZA**

### **Operating and financial review**

#### *Review objective*

1. An operating and financial review must be a balanced and comprehensive analysis, consistent with the size and complexity of the business, of-
  - (a) the development and performance of the business of the company during the financial year,



- (b) the position of the company at the end of the year,
- (c) the main trends and factors underlying the development, performance and position of the business of the company during the financial year, and
- (d) the main trends and factors which are likely to affect the company's future development, performance and position, prepared so as to assist the members of the company to assess the strategies adopted by the company and the potential for those strategies to succeed.

*Other general requirements*

- 2. The review must include-
  - (a) a statement of the business, objectives and strategies of the company;
  - (b) a description of the resources available to the company;
  - (c) a description of the principal risks and uncertainties facing the company; and
  - (d) a description of the capital structure, the treasury policies and objectives and the liquidity of the company.

*Details of particular matters*

- 3.-
  - (1) To the extent necessary to comply with the general requirements of paragraphs 1 and 2, the review must comply with paragraphs 4 to 6.
  - (2) If the review does not contain information and analysis of each kind mentioned in paragraphs 4 and 5, it must state which of those kinds of information and analysis it does not contain.
- 4. - (1) The review must include -
  - (a) information about environmental matters (including the impact of the business of the company on the environment),
  - (b) Information about the company's employees, and
  - (c) information about social and community issues.
 (2) The review must, in particular, include -
  - (a) information about the policies of the company in each area mentioned in sub-paragraph (1), and
  - (b) information about the extent to which those policies have been successfully implemented.
- 5. The review must also include -
  - (a) information about persons with whom the company has contractual or other arrangements which are essential to the business of the company; and
  - (b) information about receipts from, and returns to, members of the company in respect of shares held by them.
- 6. - (1) The review must include analysis using financial and, where appropriate, other key performance indicators, including information relating to environmental matters and employee matters.
 (2) In sub-paragraph (1), "key performance indicators" means factors by reference to which the development, performance or position of the business of the company can be measured effectively.

*Reference to and explanation of company's accounts*

7. To the extent necessary to comply with the general requirements of paragraphs 1 and 2, the review must, where appropriate, include references to, and additional explanations of, amounts included in the company's annual accounts.

*Compliance with standards*

8. The review must-
- (a) state whether it has been prepared in accordance with relevant reporting standards, and
  - (b) contain particulars of, and reasons for, any departure from such standards.

*Application of Schedule to group operating and financial review*

9. In relation to a group operating and financial review this Schedule has effect as if the references to the company (other than the last such reference in paragraph 1) were references to the company and its subsidiary undertakings included in the consolidation."

*Auditors' reports on operating and financial reviews*

10. In section 235 of the 1985 Act (auditors' report), after subsection (3) insert -
- "(3A) If the company is a quoted company, the auditors must state in their report -
- (a) whether in their opinion the information given in the operating and financial review for the financial year for which the annual accounts are prepared is consistent with those accounts; and
  - (b) whether any matters have come to their attention, in the performance of their functions as auditors of the company, which in their opinion are inconsistent with the information given in the operating and financial review."

*Reporting standards for operating and financial reviews*

11. After section 256 of the 1985 Act (accounting standards)[11] insert-
- " 256A. Reporting standards
- (1) In this Part, "reporting standards" means statements of standard reporting practice which-
    - (a) relate to operating and financial reviews, and
    - (b) are issued by a body or bodies specified in an order made by the Secretary of State in accordance with section 257(4B).
  - (2) References in this Part to relevant reporting standards, in relation to a company's operating and financial review, are to such standards as are, in accordance with their terms, applicable to the company's circumstances and to the review.
  - (3) Where or to the extent that the directors of a company have complied with a reporting standard, they are presumed (unless the contrary is proved) to have complied with the corresponding requirements of this Part relating to the contents of an operating and financial review."

## **4.2 Companies Act 2006**

### **172 Duty to promote the success of the company**

- (1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—
  - (a) the likely consequences of any decision in the long term,
  - (b) the interests of the company's employees,
  - (c) the need to foster the company's business relationships with suppliers, customers and others,
  - (d) the impact of the company's operations on the community and the environment,
  - (e) the desirability of the company maintaining a reputation for high standards of business conduct, and
  - (f) the need to act fairly as between members of the company.

### **417 Contents of directors' report: business review**

- (1) Unless the company is subject to the small companies' regime, the directors' report must contain a business review.
- (2) The purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company).
- (3) The business review must contain—
  - (a) a fair review of the company's business, and
  - (b) a description of the principal risks and uncertainties facing the company.
- (4) The review required is a balanced and comprehensive analysis of—
  - (a) the development and performance of the company's business during the financial year, and
  - (b) the position of the company's business at the end of that year, consistent with the size and complexity of the business.
- (5) In the case of a quoted company the business review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—
  - (a) the main trends and factors likely to affect the future development, performance and position of the company's business; and
  - (b) information about—
    - (i) environmental matters (including the impact of the company's business on the environment),
    - (ii) the company's employees, and
    - (iii) social and community issues, including information about any policies of the company in relation to those matters and the effectiveness of those policies; and
  - (c) subject to subsection (11), information about persons with whom the company has contractual or other arrangements which are essential to the business of the company.

If the review does not contain information of each kind mentioned in paragraphs (b)(i), (ii) and (iii) and (c), it must state which of those kinds of information it does not contain.

- (6) The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—
- (a) analysis using financial key performance indicators, and
  - (b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.
- “Key performance indicators” means factors by reference to which the development, performance or position of the company's business can be measured effectively.
- (7) Where a company qualifies as medium-sized in relation to a financial year (see sections 465 to 467), the directors' report for the year need not comply with the requirements of subsection (6) so far as they relate to non-financial information.

### **4.3 EC Modernisation Directive 2003**

#### **Directive 2003/51/EC of the European Parliament and of the Council of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings**

(9) The annual report and the consolidated annual report are important elements of financial reporting. Enhancement, in line with current best practice, of the existing requirement for these to present a fair review of the development of the business and of its position, in a manner consistent with the size and complexity of the business, is necessary to promote greater consistency and give additional guidance concerning the information a 'fair review' is expected to contain. The information should not be restricted to the financial aspects of the company's business. It is expected that, where appropriate, this should lead to an analysis of environmental and social aspects necessary for an understanding of the company's development, performance or position. This is consistent also with Commission Recommendation 2001/453/EC of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies (1). However, taking into account the evolving nature of this area of financial reporting and having regard to the potential burden placed on undertakings below certain sizes, Member States may choose to waive the obligation to provide non-financial information in the case of the annual report of such undertakings.

14. Article 46 shall be amended as follows:

(a) paragraph 1 shall be replaced by the following:

'1. (a) The annual report shall include at least a fair review of the development and performance of the company's business and of its position, together with a description of the principal risks and uncertainties that it faces. The review shall be a balanced and comprehensive analysis of the development and performance of the company's business and of its position, consistent with the size and complexity of the business;

(b) To the extent necessary for an understanding of the company's development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters;

(c) In providing its analysis, the annual report shall, where appropriate, include references to and additional explanations of amounts reported in the annual accounts.';

(d) the following paragraph shall be added: '4. Member States may choose to exempt companies covered by Article 27 from the obligation in paragraph 1(b) above in so far as it relates to non-financial information.';

10. Article 36 shall be amended as follows:

(a) paragraph 1 shall be replaced by the following:

'1. The consolidated annual report shall include at least a fair review of the development and performance of the business and of the position of the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face. The review shall be a balanced and comprehensive analysis of the development and performance of the business and of the position of the undertakings included in the consolidation taken as a whole, consistent with the size and complexity of the business. To the extent necessary for an understanding of such development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters. In providing its analysis, the consolidated annual report shall, where appropriate, provide references to and additional explanations of amounts reported in the consolidated accounts.';

(b) The following paragraph shall be added:

'3. Where a consolidated annual report is required in addition to an annual report, the two reports may be presented as a single report. In preparing such a single report, it may be appropriate to give greater emphasis to those matters which are significant to the undertakings included in the consolidation taken as a whole.';