Setting Standards, Rules and Regulations: the public versus the private sector

Prof Dieter Gloeck
Executive President:
Southern African Institute of Government Auditors

Thought control in modern societies

Members of our communities, as the users of various products, are influenced and "accustomed" to focussing almost exclusively on *content*. This also applies to the products of accounting and auditing labour. The "manufacturers" of various products achieve this "thought control" through continuous and relentless advertising and by influencing and often even controlling the debate with regard to their product.

It is only a recent development that minority groups have started to focus on *process* rather than *outcome* (product). The plight of those highlighting faulty processes has mostly been a distressing one as they experience the wrath of the producers, mostly "big business". Fortunately, their efforts are gaining momentum and organisations are finding it more difficult to suppress reform.

Whereas in the past certain manufacturers merely promoted their products' performance and other qualities, they now assure buyers that their products are built from recyclable material in environmentally friendly processes, and that they care for their workers and the environment. Housewives no longer look for the largest and most colourful vegetables, but will buy a smaller and lesser brightly coloured item if it has been grown organically. The debate about generically modified food is another example.

Steadily, more and more people are concerned about the *process* rather than the outcome, since after all, the process is the most important part as it can add or remove qualities which cannot be seen or assessed by looking at the product.

Steadily, more and more people are concerned about the *process* rather than the outcome, since after all, the process is the most important part as it can add or remove qualities which cannot be seen or assessed by looking at the product.

Accounting and auditing products

Unlike other producers, who have started to recognise the importance of *process*, the producers of accounting and auditing products have not yet undergone the above-mentioned change in viewpoint.

Accounting standards and the resulting accounting practices directly affect the public and society. Depending on accounting practices applied, companies report either profits or losses and thus pay more or less tax. These figures are also used to determine payouts to shareholders and bonuses to the workforce and are used as the basis for negotiating wage increases.

There are two major differences between corporate governance in the private and public sectors:

- ***due process***
- ***legal backing.***

The product of the Accounting Standard Setting *Process* has a major legitimising influence on social communications and the discharge of corporate and social responsibilities. This makes us aware of the prominent influence the *process* has on accountability relations affecting income distribution and resource allocation.

Whilst the Government's annual budget is publicly debated and extensively criticised due to its influence on wealth creation and distribution, and whilst corporations conduct environmental impact studies before power stations or dams are constructed, the calculation of headline earnings and other influential financial indicators are changed by new accounting conventions without open debate or similar studies being conducted by the accounting standard setters. Available information on standard-setting is scarce and the process takes place behind closed doors.

Since influential bodies are responsible for standard-setting, they direct their influence at controlling the debate and exercising censorship of the available information. The many so-called "captured" journals published by accounting institutes world-wide support this point. No critical discourse is published and information is selectively passed to members.

Whilst the Government's annual budget is publicly debated and extensively criticised due to its influence on wealth creation and distribution, and whilst corporations conduct environmental impact studies before power stations or dams are constructed, the calculation of headline earnings and other influential financial indicators are changed by new accounting conventions without open debate or similar studies being conducted by the accounting standard setters.

Corporate Governance

By the same token, as the current awareness focuses on the term "corporate governance", much is written about *content*, but few examine *processes*.

It is interesting to note that the private sector now reminds the public sector of the need for good "corporate governance". Recently a chartered accountant involved in accounting and auditing education jumped onto the bandwagon and urged government departments to have a good look at the King Report on Corporate Governance and consider implementing its recommendations. His plea was published in an article in the lay-press. This is a classic example of the thought control, referred to above. As can be seen it is often accompanied by deception and misleading statements.

So the question arises: "What is the difference between corporate governance in the private and the public sector?"

There are two major differences between corporate governance in the private and public sectors:

- *due process*
- *legal backing.*

Everyone should take note of this.

The time may have come for our legislatures to review the immense powers arrogated by the accounting and governance standard-setters in the private sector.

Due process

In the public sector, corporate governance is introduced through the Public Finance Management Act, Treasury Regulations and related legislation such as the Public Service Regulations. The *processes*, which result in the formulation of these rules of governance, are well known to us. They are based on transparency, openness and inclusivity. The public is part thereof and the debate is not censored. Members of the public can approach those in "high" positions (e.g. chairpersons of portfolio committees), the records of proceedings are not only open, but also readily available at little or no cost.

Now consider who sets the corporate governance standards for *private* businesses. To what extent is the public involved? Are meetings open to the public? Can the public obtain minutes of the proceedings? Are all stakeholders represented? The negative answers to these and many other questions speaks for themselves.

Legal backing

Government departments, public entities and those under their ownership control have no choice when it comes to their corporate governance. The South African public sector governance rules are backed by Acts of Parliament, most prominently, the *Public Finance Management Act*.

The *guidelines* of what constitutes good corporate governance in the *private* sector in South Africa were published in 1994 by the King Committee on Corporate Governance, an initiative by the Institute of Directors of Southern Africa. The King report relies heavily on the Cadbury Report published in the UK in 1992. Although there have been numerous developments in the UK since then in the form of reports by Cadbury, Greenbury and more recently Hampel, the King report has not been changed. Furthermore, the King recommendations are not in any way backed by legislation, leaving South African companies the choice of applying them only partially or even ignoring them completely.

The way into the future

When the King Committee on Corporate Governance or its successor eventually reviews the existing guidelines, it is time for government, the public and all affected by these rules to have a close look at the *process* which is being followed.

Having said that, the time may have come for our legislatures to review the immense powers arrogated by the accounting and governance standard-setters in the private sector and at least ensure that the standard-setters adhere to the basic principles of openness, transparency, accountability and inclusiveness which govern our democratic society. *Auditing SA*

Visit: **www.polity.org.za/govdocs/parliament**
to find out more about the legislative process in South Africa