



## Confidence Accounting Putting Uncertainty Back Into Accountancy

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### Confidence Accounting Putting Uncertainty Back Into Accounting

transcript of a talk by  
**Professor Michael Mainelli, Executive Chairman, Z/Yen Group**  
at  
**The Museum of London EC2Y 5HN**  
on  
**Monday, 6 February, 2006 at 18:00**

recording available at  
<http://www.gresham.ac.uk/event.asp?PageId=4&EventId=450>

Good evening. I'm pleased that Professor Joshua Ronen has taken the time to come to London to promote his reforms. I'm pleased to have the opportunity tonight to put forward some of my thoughts on the future of audit. But I'm most pleased to see so many other people interested in improving one of the most important elements of commerce, and one of the most frequently denigrated, the audit. Thank you for coming.



## A Recent View Or Ancient History?

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“The quality of information we now receive from companies in the U.S. is about the best we have ever seen and exceeds that of almost any other nation...”

[Abby Joseph Cohen, Chair, Investment Policy Committee, Goldman, Sachs & Co., as quoted in the Financial Accounting Foundation (Financial Accounting Standards Board and Governmental Accounting Standards Board), Annual Report, 2000]

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The trust that audits give to investors and other stakeholders such as employees, creditors, banks, governments and the general public is crucial to the functioning of modern commerce. If we believe that we have a true and fair view of our economic entities, then we can better understand them, better contract with them and better manage them. Yet we know that that trust is ebbing away. Audits are now more seen as a process 'one goes through' rather than a process that adds value. Public confidence in audits is low.

It is easy to open a lecture on audits with a reminder of the high-profile failures of the profession, Enron, WorldCom, etc., but the problems with audits preceded these headline collapses, as bad diet precedes symptoms of illness. The problems in the audit industry were noticeable much, much earlier. As companies themselves moved towards automated accounting systems in a rapidly-moving, real-time world, fairly evident by the mid-1980's, the Dickensian practices of auditors inspired less and less confidence about their relevancy and their value. By the late 1980's we were clearly heading, for a variety of reasons, towards an oligopoly in the provision of audits. The coalescing of this oligopoly was due to a number of factors, such as regulation, economies of scale and low differential added value (and would make an interesting lecture in its own right). By 1970 we had the Big Ten fusing to the Big 8 (1970s-1989), the Big 6 (1989-1998), the Big 5 (1998-2002) and the Big 4 (2002-present).



## Concentration

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"Measures of concentration such as the Big Four concentration ... and the Hirschman-Herfindahl Index ... reflect a tight oligopoly over the market for public-company auditing."

"In 1997 and 2002, the four-firm concentration ratios measured by the number of clients for the public company audit market were 65% and 78%, respectively. Measured by total sales of audited public companies, the four-firm concentration ratios for those years were even higher: 71% and 99%."

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"Consolidation and Competition in Public Accounting", CPA Journal, June 2005

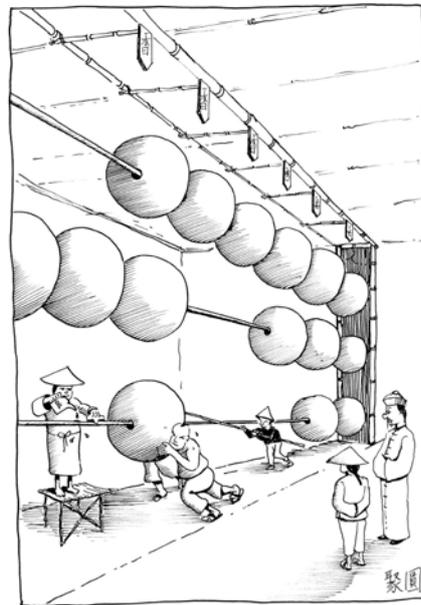
As we moved to a more restricted list of audit firms, we created an increasing number of conflicts of interest as audit firms branched out into numerous business lines, most noticeably consulting and IT outsourcing, again very evident by the late 1980's. As Anglo-

Saxon societies, we moved towards litigation to solve the problems of poor quality and conflicts of interests, again very evident by the late 1980's. Litigation generated predictable changes in the risk profile of auditors and their firms, not least of which were attempts to circumscribe liability, pretending to be one-stop international shops while collapsing nationally or threatening to collapse and create less so-called competition. The decline in confidence in audit has been going apace for some while. If anything, the recent Public Company Accounting Oversight Board assessments shows that the loss of confidence may have some justification.



## Outline

- Con? or con-fidence?
- Call of a lifeline
- Goodwill hunting
- Confidence accounting
- Better sensitivity
- Fine, in theory
- Getting out from under depreciation



“Get a detailed grip on the big picture.”  
*Chao Kli Ning*

### Con Or Con-fidence

This paper is about “Reforming Auditing - Incremental Change or Radical Action?”. I think that radical surgery is required at the heart of auditing and accounting. I’ll make a few bold statements to get the blood up:

- ◆ the typical financial audit process is one of throwing information away as early as possible rather than using it;
- ◆ the typical financial audit presents information that is precisely wrong;
- ◆ the typical financial audit environment hides information that others need to spend time wastefully recovering.

I happen to support a number of other measures for reforming auditing. People are trying to remove conflicts of interest and bring clearer accountability and liability, such as Professor Ronen, people are trying to bring more transparency to the processes of appointment and oversight, and people are trying to bring more competition to an oligopolist audit industry. But I contend that the way we present accounts is flawed and therefore our audits are



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flawed. In the past few years we have not so much put confidence back into accounting as much as we have put the 'con' into 'con'-fidence game. I would like to show how uncertainty can put the confidence back into accountancy – Confidence Accounting.

Radical enough for you?

### Call Of A Lifeline

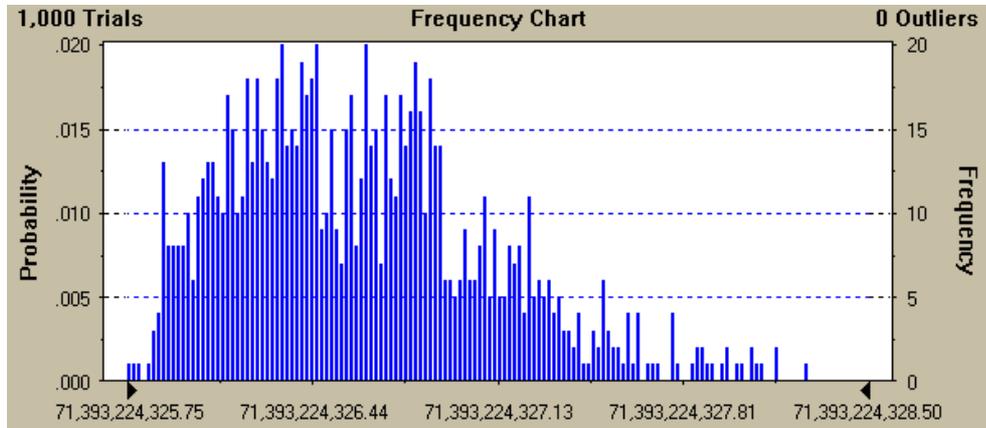
I came to accountancy late in life after a period in science and technology. I found myself in the 1980's as the only non-accounting partner in a 2,200 person firm with over 200 as partners who were qualified accountants. I decided that in order to beat them, I had to join them – possibly a too accurate view of the old-style partnerships. I took my first examinations well into my 30's. Having had a fairly intensive education, I thought these examinations would be straightforward, so, in accord with ancient academic tradition, I left everything to the last minute. The first, basic examinations were on financial accounting, management accounting and general business and law. Having cracked the course books a bit early, on the night before the exam, by around 10pm I found myself in a sweat over two items. The first panic item was, of course, double-entry book-keeping. Just think about having your first encounter with double-entry while an examination ticks 10 hours away. So I called a friend, Ian Harris by name, who had qualified years ago. In a few minutes we concluded that double-entry was definitely what you needed before you had computers and the problem largely evaporated.

The second panic item was the theory of audit. Audit is about measurement. As a former scientist I couldn't understand why the course books seemed to be missing all the usual terminology one finds around measurement – confidence intervals, range estimates, sampling techniques, probability distributions – all the measures of uncertainty one would expect to see. The course books had a lot of verbiage, but not a lot of science. Sure, they touched on estimation under stock control, but the entire process cried out for statistical process measurement. So I called Ian again. No one likes getting calls around midnight from a student in panic, but he took the perfect position. Ian calmly concluded that I had a point and went back to sleep. I took the exam, and didn't even do that badly, but I called Ian again and again over the months towards qualification and we both agreed, not just for the sake of a quiet night, that financial audits needed to be more scientific.

If auditors practise risk-based auditing, then why can't we see the odds they face? This simple question raises a number of concerns about the approach to financial statements and auditing by today's accountants. "Balancing the odds" might well give a truer and fairer picture of accounting than traditional ways of "balancing the books". To be fair, it is interesting to note that accountancy arose as a profession during the 1800's, somewhat before the 1900's movement towards statistical measurement as the foundation of metrics in numerous UK and USA standards bodies.



## Balancing The Odds



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### Global MegaCorp turnover - exactly £71,393,224,326.73

There is a surfeit of old jokes in which an accountant delivers the punchline, “What do you want the number to be?”. The uncomfortable truth is that accountants have quite a bit of influence over the final number. When Global MegaCorp states its turnover as £71,393,224,326.73 we know this number is a fiction. This is an estimate of the mean of turnover but we don’t actually have the distribution of values to know more. Accountants grapple with significant uncertainties when computing turnover. Auditors have materiality issues with the consequences of that uncertainty. Realising the obvious absurdity and statistical improbability of purporting to know a huge corporation’s turnover to the penny, accountants laugh and happily round things off, but still neglect to give us any idea of the range of the distribution. One number alone is sought to describe complex distributions, typically the mean. The three frequency charts before you all provide the same mean turnover, £71,393,224,326.73 under today’s deterministic, “one number” paradigm. However, that mean turnover has a very different meaning in each case.

The first chart exhibits an unbelievably large range: £50 billion to £90 billion, normally distributed around the mean of £71 billion. There is a 90% likelihood that the turnover falls within the range £61 billion to £84 billion. The second chart is vastly different. The distribution is heavily skewed, with the most likely outcomes being significantly lower turnover than the mean outcome (median turnover is £50 billion). There are possible outcomes at significantly higher turnover than the mean. All that you can say with 90% likelihood is that turnover falls within the range £0 billion to £172 billion. The third chart has an insignificant range of possible outcomes. The accountant is grappling with rounding differences of pennies and the auditor couldn’t care less. All of this is a nightmare for the accountant who is being asked “just give me the figure”. It is also a nightmare for the auditor trying to work out whether “the figure” is justifiable.



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In the above cases, accountants and auditors will seek guidance from accounting standards, sometimes conflicting guidance, all in pursuit of a single number to describe the distribution. I recognise and understand the distinction between the roles of accountants and auditors, but also recognise that both draw on virtually the same intellectual frameworks and regulations, as well as sometimes being employed by the same organisations.

So let's return to my three assertions:

- ◆ the typical financial audit process is one of throwing information away as early as possible rather than using it – the annual report would state £71 billion and add 62 footnotes;
- ◆ the typical financial audit presents information that is precisely wrong – it's fairly obvious that, as things unwind, the probability that last year's turnover is £71 billion and a bit is darn close to zero, but we laugh that off, as professionals;
- ◆ the typical financial audit environment hides information that others need to spend time wastefully recovering – look at the process that then kicks in with the analysts. First, they question the management about the figures, desperately trying to get some idea of the ranges. Then, the analysts start comparing lots of figures with other companies and suppliers to try and establish some ranges, resulting in some distributions that then become the ranges they use to recommend buy, sell or hold.

The accountants and the auditors are throwing away tremendous amounts of information as they principally use fixed numbers in almost all their calculations. The financial community knows that the annual report is subject to tremendous uncertainty, but will find little evidence therein. The key community for the annual report, investors, spend more of their time on reconstruction of the underlying ranges or guessing other investors' sentiments than worrying about the annual reports singular guess at what might reality be. A lot of effort is wasted. Surely no theory of measurement has wasted so much effort ignoring the real world.



## Goodwill Hunting

- Capitalisation of research & development
- Intangible assets
- Pensions and health-care obligations
- Executive stock options
- Off-balance sheet items
- Reserves and provisions
- Insurances
- ...

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*“The pure and simple truth is rarely pure and never simple.”  
Oscar Wilde*

So what theoretical issues do cause real-world problems?

- ◆ capitalisation of research and development, where assessments need to be made on the likelihood of a future revenue stream;
- ◆ intangible assets whose future value may fluctuate markedly, such as long-term contracts, patents, trademarks, and licensing agreements;
- ◆ handling pensions and health-care obligations where actuarial assumptions become crucial;
- ◆ executive stock options which may, or may not, be exercised under certain conditions;
- ◆ off-balance sheet items which may have some effect, but are mostly off-balance sheet;
- ◆ reserves and provisions, e.g. bad debts, requires estimates of future outcomes;
- ◆ insurances, even Sir David Tweedie admits that the IASB and others really haven't gotten to grips with insurance.

The common thread is that the asset value and revenue implications require an assessment of future probabilities, not certainties. Even aspects of accounting which we believe to be less contentious, where we are mainly using hindsight, raise similar concerns about future probabilities, for example:

- ◆ inventory valuation relies on estimates of future sales and prices;
- ◆ work-in-progress needs careful handling of divergent assessments of earned value;
- ◆ numerous measures are marked-to-market, but through devices such as an annual average, e.g. interest calculations or foreign-exchange movements, which could have different results under different assumptions;



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- ◆ asset valuation every few years on big ticket items such as property assumes inherent stability in prices, yet even supertanker sales prices can fluctuate wildly and rapidly.

The search for a single number is intertwined with debates of historic, current or fair value. Accountancy's theoretical framework assumes a deterministic system which outputs a single number. In book-keeping, the focus on an exact single number is important. After all, what's the point in trying to "balance the books" if "close enough" is adequate? Without the discipline of "balancing the books" lower-level mistakes would be missed and misunderstandings wouldn't be cleared up. However, higher-level interpretations are probabilistic, i.e. inputs into a higher-level figure such as turnover include many sorts of estimate. Not everything can, or will, balance. Accountants need to move to a new theoretical framework where *inputs are probabilities* and *outputs are distributions*. At a very low level, book-keeping skills remain, but the interpretation and presentation of financial information needs to shift to distributions.

### Confidence Accounting



## Confidence Accounting

	Bottom £'000	Expected £'000	Top £'000
Income	2100	2187	2400
Staff Costs	1600	1655	1780
Other Expenditure	220	248	350
Depreciation	25	36	50

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For want of a phrase for this theoretical framework, let's call it "Confidence Accounting". If every output is a probability distribution, we need to have statements of the confidence the accountant and auditor have of the range. I contend that a single number for accounting terms such as turnover is "clear and simple and wrong". As long as accountants continue to indulge this false simplicity, they will leave themselves exposed to misunderstandings of what they said and consequent misunderstandings of their role.

If outputs from Confidence Accounting are distributions, then they should materially affect the way financial statements look and feel. The structure of financial statements would



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remain similar to the three current, primary statements, viz. income statement (profit & loss), balance sheet and cashflow. However, the accountant would present three distributions as histograms for profit, net assets and cash.

The auditor would ensure that the distribution functions presented are not materially misleading and would perform sensitivity analysis on the distributions to determine where greater investigation would narrow the range at the same confidence level.

Let me give an example of how this might work in practice. Let's take a professional services firm, not unlike an accountancy practice. Here is a slide showing typical ranges of estimates for income, staff costs, other costs and depreciation. All of these are estimates. These estimates result in the following slide showing a range of estimates for the various figures. Some are inputs, some are outputs. The key outputs on this slide are income and profit.



### P&L

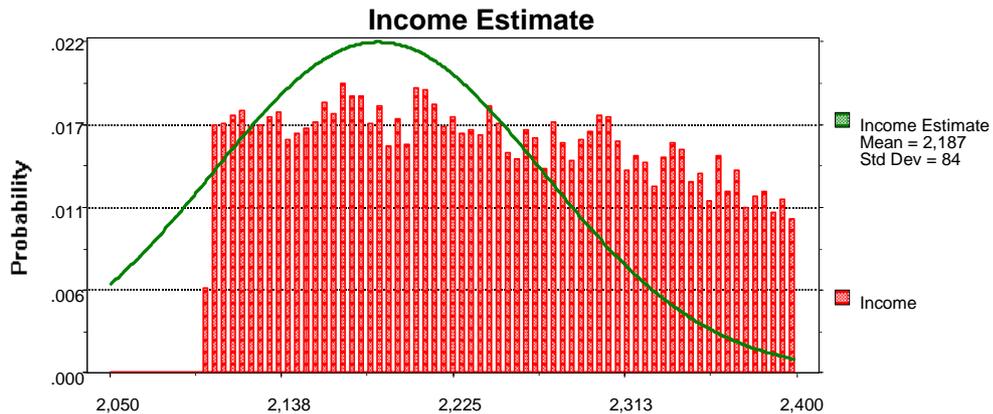
Profit & Loss Account (£ '000)	
<b>Income</b>	2,187
<b>Staff Costs</b>	1,655
<b>Other Expenditure</b>	248
<b>Depreciation</b>	36
<b>Expenditure</b>	1,939
<b>Profit</b>	248

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Looking at a traditional Profit & Loss, we see that everything is very straightforward, and ignorant. Hold on to the idea of income being £2,187,000. We have no notion here that five key contracts are both in trouble yet possibly hold out very good returns, among other things.



## Income - First Pass

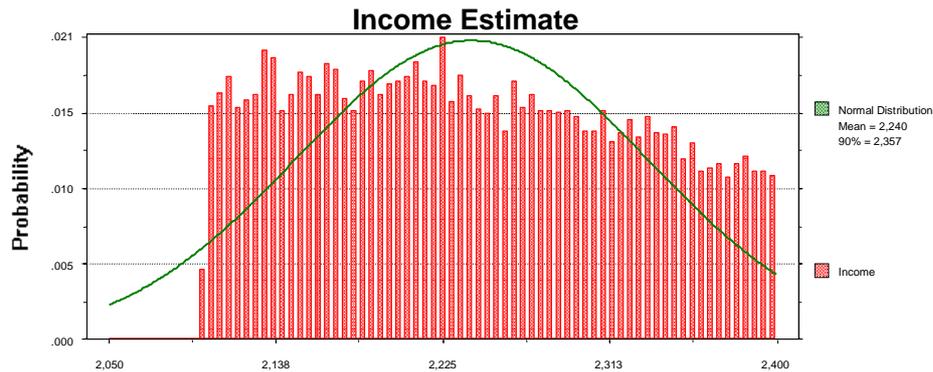


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This calculated distribution shows how various assumptions about the range of income turn out. The income ranges from £2,100,000 to £2,400,000, but interestingly seem conservative in total, as we can see that a higher figure of perhaps £2,240,000 better fits the likely outcome, rather than £2,187,000.



## Income - Second Pass



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Naturally, this analysis leads to a better picture focused around £2,240,000. What we see is the “flaw of averages” – averages conceal more than they reveal.



## Uncertainties

- Income uncertainties
  - extent to which projects are complete
  - extent to which profit might be taken at given stage
  - would look line-by-line “in real world”, e.g. opportunity tracking
- Staff cost uncertainties
  - staff rewarded on income – depends on income above
  - line-by-line “in real world”
- Other expenditure uncertainties – accruals methods and contingencies
- Fixed asset valuation uncertainties – longevity, valuation at any instant...

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Quite rightly, it is important to see what may be contributing to this uncertainty. In this case, there are income uncertainties about extent to which projects are complete, the extent to which profit might be taken at given stages or the likely out-turns on opportunities. There are also cost uncertainties as some staff are rewarded on income that depends on income, other expenditure uncertainties such as accruals methods and contingencies, as well as fixed asset valuation uncertainties due to estimates of longevity or changing market values.



## Confidence Accounting Putting Uncertainty Back Into Accountancy



### Balance Sheet

		<b>Balance Sheet (£ '000)</b>	
<b>Fixed Assets:</b>	<b>Cost</b>	145	
	<b>Accumulated Depreciation</b>	103	
			<u>42</u>
<b>Current Assets:</b>	<b>Cash</b>	144	
	<b>Accounts Receivable</b>	419	
	<b>Work in Progress</b>	121	
			<u>684</u>
<b>Liabilities:</b>	<b>Accruals</b>	70	
	<b>Advanced Sales</b>	241	
	<b>Other Creditors</b>	62	
			<u>373</u>
			<u>353</u>
<b>Equity:</b>	<b>Brought Forward</b>	105	
	<b>Profit in Year</b>	248	
	<b>Carried Forward</b>		<u>353</u>

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Turning to the balance sheet, we can see that it hardly reflects the P&L uncertainty in its traditional state. Stochastic effects on the balance sheet flow from the P&L stochastic model, such as project completeness affecting credits for advanced sales or profit taken as work-in-progress or expenditure uncertainties affecting accruals. A handful of large assets represents most of the asset valuation uncertainty, e.g. property, major IT systems. Cash flow statements are unchanged as they already incorporate the idea of probabilistic flows.

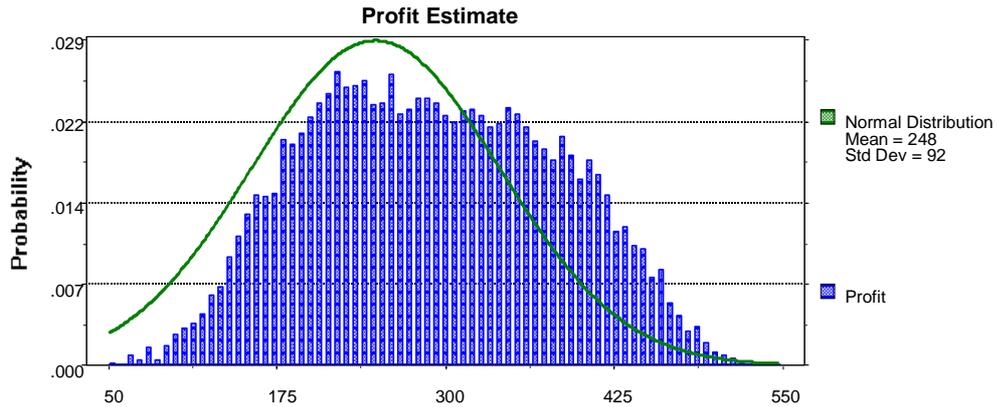


## Confidence Accounting Putting Uncertainty Back Into Accountancy

We can turn to Profit and see a reasonable range of estimates.



### Profit - First Pass

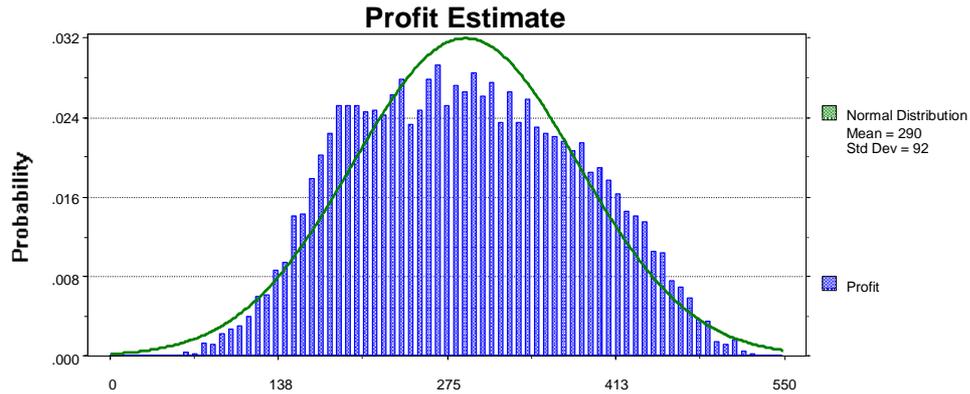


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Here we can see that the 'deterministic' accounts showing a profit of £248,000 were too conservative. A better estimate might be around £290,000, as shown here.



## Profit - Second Pass



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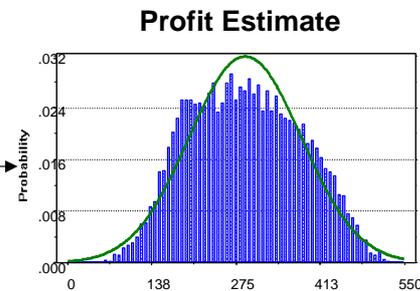
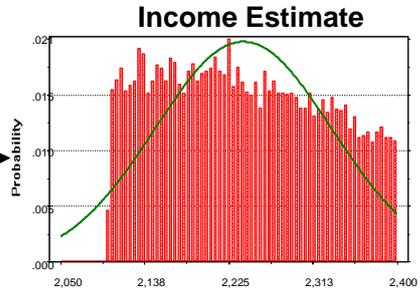
So we've found that real ranges indicate a better fit of income some £53,000 higher and a profit some £42,000 higher than a standard P&L. These ranges could be presented alongside traditional statements to give a genuine true and fair view.



## P&L – Clearly Conservative

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Profit & Loss Account (£'000)	
Income	2,187
Staff Costs	1,655
Other Expenditure	248
Depreciation	36
Expenditure	<u>1,939</u>
Profit	<u><u>248</u></u>



In fact, published accounts could well be made much more understandable using simple illustrations of reasonable distributions to permit such variations and estimates to be made clear.

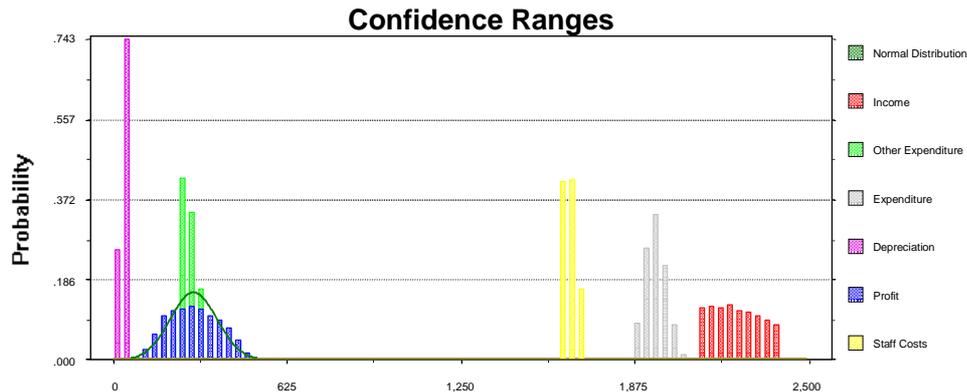


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## Better Sensitivity



## Better Sensitivity



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Auditors and accountants have to address whether they wish to be “an art or science”. During the dot.com era, accountants subjected themselves to needless criticism by endorsing business plans based on deterministic numbers which were incapable of showing the all-too-frequent reality - a small chance to make money and lots of chances to lose money. Had accountants submitted plans which showed the distributions, they may well have served investors better, reduced unreasonable expectations and minimised criticism of the accountants’ role. Instead they presented single numbers or played with high, medium or low forecasts to calculate “average” forecasts, none of which contained the possibility of winding-up the business or wild success.

Some accountants would claim that things have moved on. Auditors will point out that they already use probabilistic techniques in establishing sample sizes. Without getting into a detailed debate on evidence in their working practices, the crucial evidence of successful Confidence Accounting would be the presentation of audited accounts in a probabilistic manner. Beneath that evidence we would expect to see methods which established input distributions, determined their interactions (e.g. sensitivity analysis, Monte Carlo simulations and some statistical calculations) and presented their impact in meaningful statements.



## Confidence Accounting Putting Uncertainty Back Into Accountancy

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### Fine - In Theory

There are some obvious complications that many of you will already have identified. Standard representations of distribution histograms will have to be specified. Distribution function measures will have to be specified as well, to ensure accurate presentation. Alongside existing numerical descriptions of shape such as kurtosis or skewness, people will seek single number measures for comparison, e.g. riskiness. Some of these measures may well help, particularly if they are calculated and presented in standardised forms.

Many people will claim that the mythical “Aunt Agatha” cannot understand all this. It’s too complicated. Life is complicated. While I would support more research on how presentation of distributions could be improved, I would contend that Aunt Agatha cannot understand today all the footnotes that only help a sophisticated financial analyst partially reconstruct the probabilities

Many firms have too little data to give any statistical validity to a distribution. However, much can be done to provide data through intra-firm comparisons, benchmarking or auditor input, e.g. what is a standard actuarial curve for bad debts in a given business sector. As directors must “prepare annual financial statements that give a true and fair view of the state of affairs”, in many cases they will have to provide a qualitative distribution curve (in fact, quite a bit of software supports homemade distribution curves). If this seems artificial, in fact it’s quite the opposite. Which is worse, forcing directors to a single number, such as a guess-timated mean when none exists, or asking them to specify their views of the likely range of outcomes?

Some organisations will want to provide extremely wide ranges in their distributions. Where this reflects reality, so be it. In other cases managers will hope that a wide range removes some responsibility of meeting target. However, markets will punish managers who have not invested enough in gathering information to reduce uncertainty. Expect phrases such as “Global MegaCorp was punished today on release of its results, with a range for ROA of over 15% in an industry where 5% is the norm, much of this attributed to overseas licence problems...” Further, managers will be forced to, in Baruch Lev’s terms, “true up”. If they are consistently providing silly future estimates, and these are now recorded in the financial accounts, they are there for investors to judge.

There will also be a competitive force on auditors, both from an increased ability to compare their previous years’ approvals with outcomes, and also from being known to be prone to wild ranges. Markets will transparently price the value of tighter distribution ranges.

If accountants are to move from a deterministic towards a stochastic paradigm, much work needs to be done, largely in three areas – commitment by the accounting establishment to reform, restructuring of accounting training, and better communication to users of financial information. The starting point is an open debate about extending the conceptual framework of accounting to include stochastic concepts. This debate ought to lead to commitment from the accounting establishment for Confidence Accounting and recognition that deterministic accounting is the root of many current problems. Confidence Accounting is a change of perspective that resolves inconsistencies. Evidence of that commitment would be more presentations incorporating distributions rather than single points, a review of accounting standards (GAAP and IASC) to see where replacing a single number with a



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distribution would simplify statements and a review of audit methodology to change risk-based auditing to a more rigorous method based on quantitative evidence of estimation.

### Getting Out From Under Depreciation



## A Range of Change

Characteristic	Deterministic Problem	Confidence Accounting
<b>Relevance</b>		
predictive value	requires a single number guaranteed to be wrong	range is fully described
feedback value	discussion centres on whether being only a little bit wrong was close enough	clear discussion on results within predicted ranges; if not, why was certainty factor wrong
timeliness	much discussion and revision to choose a single number	prompt presentation of the "way things are" and ability to see convergence over time
<b>Reliability</b>		
verifiability (objectivity)	difficulty in obtaining consensus among different experts	ability to use different experts when necessary
neutrality	difficulty in changing standards without affecting certain sectors	reduction in the number of special standards
representational faithfulness	poor agreement between real world and measures	accurate reflection of real world phenomena

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Financial information is evaluated by its usefulness in making financial decisions. Moving to Confidence Accounting improves several characteristics of accounting information. Imagine the following snippets of dialogue among an accountant, the finance director and their auditor:

*[Accountant presents draft accounts to auditor and finance director]*

*Accountant:* "Well, here they are. I'm 95% confident that Global MegaCorp's profit is somewhere between losing £5 billion and making £20 billion."

*Finance director (spluttering):* "What, is that the best we can do?"

*Accountant:* "Hey, that's not so bad, you should have seen the numbers before I rechecked our fleet inventory."

*Auditor:* "How tight do you need the numbers to be?"

*Finance director:* "Well, the analysts will expect us to have no greater than a £3 billion range, assuming we're confidently into profit, say over £7 billion".



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*Auditor:* “That’ll cost, but we’ll get cracking.”

*[three weeks later]*

*Auditor:* “The sensitivity on work-in-progress directed me to spend almost 80% of our effort examining the state of some of Global MegaCorp’s largest construction projects, but I’ve managed to tighten the range to your required £3 billion, giving an estimated profit of £6.5 billion. Unfortunately, that has meant quite a bit of overspend on the audit, about £2 million. If you could in future live with say a £5 billion range, we can keep the audit costs down.”

*Finance director:* “A wide range this year will be a hard sell to the analysts, but we can probably do it. Next year’s profit looks to be much better, so this might be the time to start selling the analysts on a wider acceptable range.”

### Audit’s Razor



## Audit’s Razor?

“The central role assigned to decision making leads straight to the overriding criterion by which all accounting choices must be judged. The better choice is the one that, subject to considerations of cost, produces from among the available alternatives information that is most useful for decision making.”

“Summary of Principal Conclusions”, Statements of Financial Accounting Concepts No. 2 (FASB, May, 1980)

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As in so many other areas of measurement, I believe that we should ask for four basic numbers – bottom, expected, top and the % of things being in that range, or BET% as I coin it. As I said last year on in a lecture measurement:

“... we don’t follow through on the obvious implication, a specific number is the wrong measure. Too many things in profit, as in all accounting statements, are ranges, from the estimate of gains in freehold land value to the likely profit on individual contracts to the value of insurances, etc. To ensure total clarity, we litter the financial accounts with explanatory footnotes to the point that only highly sophisticated financial analysts can



## Confidence Accounting Putting Uncertainty Back Into Accountancy

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understand them. When the accounts are presented, these financial analysts tear them apart in order to try and re-build estimates based on ranges. Intriguingly, the auditors get off very, very lightly, practically skipping away. How do you hold an auditor to account? Is being off by £1 enough to claim the accounts are invalid? Certainly not. £2? Well, when? In fact auditors have cleverly avoided giving us anything substantive to go on, such as “we are 95% certain that profits were between £X and £Y”. Let’s think about forcing auditors to lay these ranges out clearly. In fact, let’s pin down all commercial measurers to their estimates using BET%.”

The public are sceptical of the state of financial information produced by auditors and accountants, and by implication the accounting techniques upon which their work is based. Before accountants indulge in trendy ideas such as Triple Bottom Line reporting (corporate disclosure which integrates financial, environmental and social reporting), it might be better to straighten out the way in which they currently report good-ole financial information, or risk further loss of public confidence. I believe that users of financial statements are ready to handle Confidence Accounting. I believe that by presenting a true and fair view of distributions, accountants will gain respect by showing the complexity of the situation, rather than losing respect when a single point number turns out to be either ridiculous or wildly inaccurate.

There are a number of old jokes that, “an actuary is someone who couldn’t handle the excitement of accountancy”. Until accountants adopt Confidence Accounting, perhaps a more accurate paraphrase is that “an accountant is someone who couldn’t handle the honesty of being an actuary”.

So, let’s take the con out accounting, put the uncertainty back in and help the confidence increase.

Thank you.



## Discussion

1. Are accounting or book-keeping truly deterministic or stochastic?
2. Where do distributions not apply in financial statements?
3. How does Confidence Accounting simplify standards?



“Get a big picture grip on the details.”  
*Chao Kli Ning*

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### Further Discussion

1. Are accounting or book-keeping truly deterministic or stochastic?
2. Where do distributions not apply in financial statements?
3. How does Confidence Accounting simplify standards?

### Further Reading

1. Michael Mainelli and Ian Harris, “Balancing the Odds: Stochastic Accounting”, Balance Sheet, Volume 10, Issue 2, pages 22-27, MCB University Press (2002) - [http://www.zyen.com/Knowledge/Articles/Balancing\\_the\\_Odds.htm](http://www.zyen.com/Knowledge/Articles/Balancing_the_Odds.htm)
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6. J.D. Spiceland and J.F. Sepe, Intermediate Accounting, Irwin/McGraw-Hill, 1998.
7. Mark Lee Inman, “Towards a Conceptual Basis for Accounting”, ACCA Students’ Newsletter, June 1992.

### Further Surfing

1. <http://physics.nist.gov/cuu/Uncertainty/> - “The NIST Reference on Constants, Units and Uncertainty”, the National Institute of Standards and Technology, 2006.
2. <http://www.unitedkingdomaccreditationsservice.net/Library/downloads/publications/Lab34.pdf> - “The Expression of Uncertainty in EMC Testing”, LAB, Number 34, United Kingdom Accreditation Service, August 2002.

### Thanks

My special thanks to Ian Harris for his assistance not just with this talk, but over the years on this subject. In almost every way this is a joint paper, unless the flak hits, in which case it’s mine.