JOINT COMMITTEE ON CORPORATIONS

AND FINANCIAL SERVICES

<u>INQUIRY INTO</u>

<u>AUSTRALIAN ACCOUNTING STANDARDS</u>

SUBMISSION

by

Barbara Mescher, B.Juris, LLB, LLM (UNSW)
Solicitor, NSW Supreme Court,
Lecturer, Discipline of Accounting and Business Law,
University of Sydney, Australia

19/12/04

SUMMARY

1. This submission examines the legal effect of the accounting standards as they are presently drafted and implemented, upon the directors' solvency declaration required under s 295(4)(c) of the Corporations Act.

2. There is no profession of company director. Consequently directors are forced to rely heavily upon the accountants: a reliance that is problematical due to the perceived flexibility of some of the accounting standards.

3. Accountants and directors have a different view of the meaning of solvency. Directors are compelled to take the legal meaning of the term in order to satisfy the legal requirement stated in s 295(4)(c) and their other duties in law. Accountants provide directors with information based upon the accounting standards. There is a gap between what the law requires of directors and what the accounting standards provide.

4. The accounting standards and/or their interpretation may create a misleading view of the financial health of the company. If the company is performing well the misleading view is only relevant to the level of company performance. However, if the company is under performing directors may not be alerted in time if the accounting information fails to reveal the true state of the company's finances. "Unexpected" corporate collapses may result.

5. The flexibility of application and interpretation of the accounting standards is not only an issue for accountants and those setting the accounting standards. It is also an issue for directors, their legal advisers, members of companies, the Australian Stock Exchange and ASIC. A solvency declaration by the directors is a statement to the market. If it is misleading it may be a market offence under s 1041E, Corporations Act.

6. *The accuracy of the accounts and related financial reports is a significant issue in law and commerce. The accounting standards as they are presently interpreted undermine the credibility of public companies financial statements.*

INTRODUCTION

It is the purpose of this submission to examine the obligations of company directors, accountants and the accounting process. Directors and accountants have a close but complex relationship in practice and in law. The basis of the relationship is that the company accounts reflect the true financial position of the company.

A common feature of the most publicized recent company collapses is the element of surprise. The failure of the HIH Insurance Group in Australia and Enron in the United States was not expected by members, creditors, brokers and the regulators. This submission studies public listed companies.

The issues discussed are those arising as a result of accountants and directors complying with the law. One of the purposes of this submission is to highlight the unsatisfactory state of the company's financial affairs that may result when parties act *within* the existing law.

THE RELATIONSHIP BETWEEN DIRECTORS AND ACCOUNTANTS

1. The obligation to keep accounts

The *quid pro quo* for the privilege of incorporation is that the company has disclosure obligations to its investors and the market: the most significant of which concerns the keeping of company accounts that are transparent. The *Corporations Act 2001* (Cth)[1], s 286 requires a company to keep written financial records that:

---

[1] *Corporations Act 2001* (Cth), s286. All subsequent sections refer to this *Act* unless otherwise indicated. See the *Act* at http://www.austlii.edu.au/au/legis/cth viewed 26 November 2004

"(a) correctly record and explain its transactions and financial position and performance; and
(b) would enable true and fair financial statements to be prepared and audited."

Section 286 has been interpreted by the Courts to mean that the accounts should be capable of disclosing or exhibiting the financial position of the company at *all times* and at *any time* with the underlying policy being to guard against directors and officers "flying the company blind": *Van Reesema v Flavel* (1992) 10 ACLC 291 at 295; 7 ACSR 225 (emphasis added). The company commits an offence if it fails to keep adequate accounts: s 286(3). Directors who do not take reasonable steps to ensure proper accounts are kept contravene s 344, a civil penalty provision and each director may be fined up to a maximum of $200,000: s1317(1B). If there is dishonest intent a further fine to $200,000 and/or a maximum term of imprisonment of 5 years applies: Schedule 3 of the Act.

The essence of the relationship between accountants and directors is complex both factually and legally. It is based upon trust and reliance and is arguably the most important relationship in the company as it concerns the directors' most significant obligation. If the accounting standards are not clearly drafter directors cannot adequately fulfill their duties due to the possibility of creative accounting.

The law requires the directors to ensure that an adequate accounting system is in place and working well. The important issue for directors is how they determine this. The law specifies 2 apparently conflicting means of

assessment, that: (a) directors be proactive and monitor the accounts; and (b) directors be passive and rely upon the accountants.

2. Monitoring the accounts

The standard of care for directors and been examined in *Daniels and others (formerly practicing as Deloitte Haskins and Sells) v Anderson and others* (1995) 37 NSWLR 438 at 503-504; 118 FLR 248; 16 ACSR 607 and *Statewide Tobacco Services Ltd v Morley* (1990) 2 ACSR 405 at 431; 8 ACLC 827 Ormiston J held that:

> * "What each director is expected to do is to take a diligent and intelligent interest in the information either available to him or which he might with fairness demand from the executives or other employees and agents of the company…
>
> * Even in a small company a director should ask for and receive figures, albeit of a basic kind, on a more or less regular basis…
>
> * Directors are required to seek more information if the company's accounts…[and] other information from the company's executives, put them on inquiry."

A director's responsibility in a large or small company is not limited to asking for and receiving figures on a regular basis but extends to checking facts and clarifying matters.[2]

Most large public listed companies have audit committees to perform the monitoring function but this is usually restricted to external reporting. Few

[2] Coburn N, *Coburn's Insolvent Trading: Global Investment Fraud and Corporate Investigations* (2nd ed, Lawbook Co., 2003) p 83.

companies employ these committees to examine the adequacy of information given to company boards.[3] Accounting Professor Robert Walker found in a review of company annual reports (June 2002) for the top 200 listed companies on the Australian Stock Exchange, that 98% of companies had established audit committees. Within this group, 85% had a prime responsibility to review the company's financial statements, and 53% monitored risk assessment. Significantly only 2% of companies gave the audit committee responsibility to assess the quality of internal financial reporting to the board.[4]

Whether or not the accounting information given to directors is good quality, it remains a matter of concern whether directors have the skills to understand it. It follows that adequate monitoring of the accounts is unlikely to occur. Nor will directors be put on inquiry to seek further information.

3. Reliance upon the accountants

It is, therefore no surprise that directors, many of whom have insufficient or no accounting knowledge, are forced to rely upon the expertise of the accountants concerning the company's financial affairs. It is implicit under s 290, which permits a director to apply to Court for a person to inspect financial records, that directors are unable to evaluate those records and that they need to rely on others.

Section 189 permits directors to raise reliance as a defence when there is an alleged breach of statutory duties under ss 180-184. For example, if directors fail to ensure the company keeps adequate accounts, it is a contravention of s

[3] Walker RG, "Gaps in Guidelines on Audit Committees" (2004) 40 Abacus 2 at 170
[4] Walker, n 3 at 173-175.

286. This would be interpreted as a breach of s 181: not acting in the best interests of the company. The reliance claimed by the director under s 189 refers to information or professional advice given by an employee, expert or other director.

Section 1309 has a more general application but it is also related to reliance. If accountants provide material information to a director that is misleading or false or omit material information, they are guilty of a criminal offence with a penalty to $200,000 and/or 5 years imprisonment, Schedule 3. Accountants will not always have the safeguard that directors will discover information given is misleading or false. Directors may not be sufficiently knowledgeable in the area of company accounts to make this deduction.

THE COMPANY ACCOUNTS AND THE ACCOUNTING STANDARDS

It is not an exaggeration to say that the keeping of accounts as required under s 286, constitutes the building blocks of the company: without accurate accounts the company does not exist. A company without accurate accounts is presumed at law to be insolvent: s 588E(4). One could say that the company's survival and that of its directors, depends upon the company's accountants.

Adequate accounts enable the company's financial report to be produced. This comprises financial statements for the year such as profit and loss, balance sheet and cash flow statements and the directors' declaration: s295. The declaration concerns 3 significant matters. The 1st is that in the directors' opinion, there are reasonable grounds to believe the company is solvent. The 2nd and 3rd omit "reasonable grounds" and merely ask for the directors' opinion

whether the financial statements comply with the accounting standards and if they give a true and fair view of the financial position of the company. The solvency declaration is further discussed below.

The question must be asked: Is the financial report an accurate representation of the company's financial health? The analysis below implies a negative answer or at best uncertainty, even though the accountants and directors studied in this submission have acted within the law. This has serious implications for the company and the community.

1. Accountants and the accounting standards

The accounting standards are a set of principles whose function is to apply practical procedures and rules concerning the recording, measuring, analyzing, summarizing and reporting upon the economic activities of business entities.[5]

In 2003 the Australian Federal Government established a Royal Commission to prepare a report on the reasons for and the circumstances surrounding the failure of the HIH Insurance Group. This followed the collapse of the Group with an estimated loss of up to $5.3 billion dollars. This has been Australia's largest corporate collapse.

One of the matters examined by the Royal Commissioner was the financial reporting system in Australia. The Commissioner found that the accounting standards originated as mere guidelines although they came to be set by the Australian Accounting Standards Board (AASB) and overseen by the

[5] Ford HAJ, Hinde GW and Hinde MS, *Australian Business Dictionary* (Butterworths, 1985) "accounting principles", p 3.

Financial Reporting Council (FRC). Some of the standards lack clarity due in part to the consultative process of standard setting. This is a process that often involves compromise and inconsistency. In addition, some standards are poorly worded and subject to wide or inconsistent interpretation while others are clearly worded but capable of incorrect application.[6]

There is a gap between what the law expects in relation to the company accounts and accounting practice.[7] It is said that the accounting standards are in effect delegated legislation[8] and that accountants need to refer to case law and the Courts' attitude to accounting requirements as a reference point when developing accounting rules and standards.[9] The standards have been given legislative status by being incorporated into the *Corporations Act.* Section 296 states that the accounts must comply with the accounting standards yet some standards are ambiguous and unlike legislation, they are not rigorously drafted. This ambiguity gives the impression that the accounting standards are flexible.

2. Flexible accounting standards

The adoption by Australia in January 2005 of the international accounting standards and the Australian Federal Government amendments that commenced in July 2004 to the *Corporations Act* and the *Australian Securities and Investments Act*[10], see below, do not resolve the central concern discussed here, which is the accounting standards.

---

[6] HIH Royal Commission, *The Failure of HIH Insurance*, Vol 1 (National Capital Printing, 2003) p 136. The Report is also available on: http://www.hihroyalcom.gov.au viewed 6 October 2004.

[7] Purcell J, "The Contrasting approach of Law and Accounting to the Defining of Solvency and Associated Directors' Declarations" (2002) 10 Insolv. LJ 192 at 199.

[8] HIH Royal Commission, Vol 1, n 6 at 137.

[9] Purcell J, n 7 at 203.

[10] The amendments are known as Corporate Law Economic Reform Program, 9 or CLERP 9.

The HIH Royal Commissioner's investigation of the HIH accounts found that there was a misinterpretation not only of the accounting standards but also the requirement to present financial statements that were "true and fair". HIH, therefore, published financial statements that did not satisfy the true and fair requirement.[11] The Commissioner found that the accounts submitted to the corporate regulator were often wrong and that the board failed to satisfy itself that the accounting system was appropriate to its business.[12] Further, that the accounts were distorted by questionable and aggressive accounting practices. These practices strained the letter of the accounting standards as far as possible. The process was fatally flawed.[13] It has been said that the accounting information system was at the centre of the failure of HIH.[14] This is not to deny that many of the directors of HIH contravened the law and their illegal actions clearly contributed to the group's demise. However, HIH is being studied here to inform us about the state of the accounting system and, importantly, to provide another example of the gap between accounting practice and the law.

The problem is exacerbated when one studies company groups. The accounting standards are more flexible in relation to company groups. Accountants are able to treat companies within the group as a single economic entity by consolidating their accounts. Data relating to all within-group transactions are eliminated from the calculation of "group" profits and losses.[15] It

---

[11] HIH Royal Commission Report, n 6, Vol 1 at p 138.
[12] HIH Royal Commission Report, n 6, Vol 1 at pp xliii-xliv.
[13] HIH Royal Commission Report, n 6, Vol 1 at pp xlvi-xlvii.
[14] George G, "Accounting, Auditing and Auditors – What is to be done?" (2002) 14 Aust Jnl of Corp Law 51 at 53.
[15] Clarke F, Dean G and Oliver K, *Corporate Collapse: Accounting, Regulatory and Ethical Failure* (Cambridge University Press, 2003) p 253.

is said that the methods of consolidation of group accounts have facilitated financial deception.[16] In law there is no concept of consolidating companies, although by specifying the need to comply with the accounting standards, s 296, the law recognizes the consolidation of group accounts. In law, *each company,* whether or not a member of a group, is regarded as a separate legal entity in its operations and the liabilities of directors and accountants. The contrasting accounting treatment of the company group is said to potentially mask through individual company obligations to external creditors and the extent of each company's asset ownership.[17]

There are legal consequences for accountants and directors if the accounting standards are so flexible they enable the production of misleading financial statements in the company's annual report. In law this report is a statement by the company to the market generally and the members in particular. The making of a misleading or false statement is a market offence if the statement is materially misleading and is likely to induce persons to buy or sell financial products, such as shares: s1041E. Statements giving favourable reports on a company's financial position are likely to have this effect. This is a criminal offence with a penalty of up to $200,000 and/ or 5 years imprisonment for directors, Schedule 3. The company could be fined 5 times this amount: s1312, which in this case is $1 million dollars. Fortunately for directors and companies this cause of action has rarely been litigated, partly due to the acceptance of the flexible nature of the accounting standards. Misleading

[16] Clarke et al, n 15, p 247.
[17] Purcell, n 7 p 193.

statements to the market by public listed companies constitute a breach of the Stock Exchange Listing Rules: LR 3.1.

In *Daniels and others (formerly practicing as Deloitte Haskins and Sells) v Anderson and others* (1995) 37 NSWLR 438; 118 FLR 248; 16 ACSR 607, the company, AWA Ltd, sued its auditors for breach of contract and negligence because of their failure to report upon the absence of internal controls and inadequate accounting records concerning the company's foreign exchange dealing. The Court held that the directors (rather than the accountants) were negligent because it is the directors who have the duty of care to the company to ensure it keeps proper accounts. The auditors were also found to be negligent. Damages were apportioned between AWA Ltd (1/3) because it failed to keep proper accounts, and the auditors (2/3).[18] AWA Ltd could have then taken legal action against its directors for their breach of duty.

3. <u>The international accounting standards</u>

In 3 July 2002 the Australian Financial Reporting Council (FRC) announced that Australia would adopt the international accounting standards (IAS) from the reporting period commencing on or after 1 January 2005. The advantages of the IAS for Australia include reducing the cost of capital and improving access to foreign capital for Australian companies.[19] Europe and New

---

[18] *Daniels and others (formerly practicing as Deloitte Haskins and Sells) v Anderson and others* (1995) 37 NSWLR 438 at 578.

[19] Knapp J and Kemp S, *Accounting Handbook,* Institute of Chartered Accountants (Pearson Prentice Hall, 2004) Vol 1, p xviii.

Zealand (to a limited extent[20]) are also adopting the IAS. Canada and the United States have chosen not to adopt the international standards.

From 1996 the Australian Accounting Standards Board (AASB) began to harmonize its standards with those issued by the International Accounting Standards Board (IASB). As a result the majority of Australia's generally accepted accounting principles (GAAP) are already consistent with the international (GAAP). It is argued by Professors Clarke and Dean that because of this consistency between the AAS and the IAS the present criticism of the system continues to apply;[21] that is, flexible accounting standards will remain a problem after 1 January 2005. Within both the international GAAP and IAS there remains significant discretion for accountants in the application and interpretation of accounting standards.[22] Professors Dean and Clarke maintain that compliance with the International Financial Reporting System (IFRS) will arguably not improve the serviceability of financial information produced by Australian companies and that "true and fair" should be the sole criterion dictating directors' and auditors' reporting.[23]

4. <u>The CLERP 9 reforms</u>

The Australian Federal Government reforms of audit practice and financial reporting, known as CLERP 9, were introduced in the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth) which

---

[20] There is voluntary adoption from 1 January 2005 and it is mandatory from 1 January 2007.
[21] Clarke et al, n 15 p 331.
[22] George, n 14 at 56.
[23] Dean G and Clarke F, editorial "Principles vs Rules: True and Fair View and IFRSS" (2004) 40 Abacus 2, at p iii,

amended both the *Corporations Act* and the *Australian Securities and Investments Commission Act.*[24]

One specialist accounting commentator lamented that the Federal Government has failed investors and the general community in rejecting much-needed reforms to the oversight of accounting and audit standard setting.[25]

The proposed reforms to financial reporting provisions were studied by the Parliamentary Joint Committee on Corporations and Financial Services.[26] One of the main issues concerning the Committee was the need to improve the application of the true and fair requirement. The Committee recommended a definition of "true and fair view" be included in the *Corporations Act.*[27] Unfortunately this recommendation was not adopted in CLERP 9 although the standard of the financial reporting requirements was improved. The reforms, commenced on 1 July 2004, but have not reinstated the supremacy of the true and fair override clause. However, its status has been enhanced by the insertion in the *Corporations Act* of 2 new sections: ss295A and 299A.

Section 295A requires the company's chief financial officer or chief executive (being a person directly responsible to the board) to make a declaration, s 295A(2), regarding the proper maintenance of the accounts, compliance with the accounting standards and the resulting true and fair view.

---

[24] See McConvill J, *An Introduction to CLERP 9* (Lexis Nexis Butterworths, 2004) for a discussion of the CLERP 9 reforms. The 3 Acts discussed are available on: http://www.austlii.edu.au/au/legis/cth viewed 25 November 2004.

[25] Ravlic T, "CLERP 9 Squibs on Real Accounting Reform" (2004) BCLB [361] at 11.

[26] Senator G Chapman, Chairman, Parliamentary Joint Committee on Corporations and Financial Services.

[27] Senator G Chapman, Chairman, Parliamentary Joint Committee on Corporations and Financial Services, Media Release, "Senator Chapman Tables Part 2 of Report on CLERP 9", 15 June 2004, Recommendation 4, at 10: http://www.senatorchapman.com/press_14_1_2000.html viewed 26 November 2004.

This is an additional declaration to that required of directors under s 295(4) as to solvency, the accounting standards and the true and fair view. This accountant's declaration, s 295A(2), precedes the directors' declaration under S 295(4). In fact it is likely the directors' declaration will concur with the accountant's declaration although the directors cannot claim reliance. The directors' declaration remains *their* primary obligation: s 295A(8). It is interesting that the law now requires the executive accountant to also have a primary obligation to make a declaration. This raises the level of responsibility of accountants.

The other new section, s 299A, refers to the annual directors' report of public listed companies. Section 299A(1) requires that this report must contain information that *members of the company would reasonably require to make an informed assessment* of the company's: operations, the financial position and the business strategies and the company's prospects for future financial years. This section is capable of a very broad interpretation because directors have to make an evaluation of their company's membership and what they know and what additional information they might require to make an "informed" assessment.

COMPANY SOLVENCY

It is vital that the company directors know the solvency status of their company. If the company is drifting towards insolvency directors need to know. They have legal obligations to the company, its creditors, members and employees as well as the market. Early knowledge of impending disaster may

prevent insolvency or restrict the harm to those affected by it. Between January and September 2004 there were 7,361 insolvencies and 4,423 external administrations in Australia[28] and this in a period of economic success where company profits are at record levels! In 2003-04 profits for listed companies on the Australian Stock Exchange jumped by over 20%.[29]

1. <u>The solvency declaration</u>

The company's annual financial report consists of the financial statements and related notes as well as the directors' declaration. The declaration under s 295(4) requires directors to give an opinion whether the financial statement and notes comply with the *Act*, the accounting standards and constitute a true and fair view. Solvency problems may be inferred from these statements and notes. However, the law requires more than an inference for such an important matter. The section specifically requires directors to focus upon the issue of solvency and make a declaration whether in their opinion there are reasonable grounds to believe the company is able to pay its debts as and when they become due and payable. This opinion as to solvency is the most important part of the directors' declaration yet it has been argued that the assessment of solvency and the prediction of insolvency are not possible under conventional accounting standards.[30] If the directors' declaration is at best, unreliable, then it is matter of concern as directors and accountants, will fail to take remedial steps to protect

---

[28] ASIC Insolvency Statistics see ASIC Insolvency and Liquidators homepage: http://www.asic.gov.au viewed 25 November 2004.
[29] Maiden M, "US Walks a Fine Line as Greenback Slides" ("The Sydney Morning Herald", 26 November 2004) Business News: http://www.smh.com.au viewed 26 November 2004.
[30] Clarke et al, n 15, p241.

the company and themselves from liability. If the company continues to trade while insolvent, directors are personally liable to unsecured creditors: s 588G.

2. <u>Accountants and the meaning of "solvency"</u>

Accountants and directors have different views of the meaning of solvency. There is no accounting standard of solvency. However, when preparing the financial statements accountants make an assessment of the company's ability to continue as a going concern.[31] This means that the company is expected to be able to pay its debts as and when they become due and payable and continue operating without any intention or necessity to liquidate.[32] In assessing whether the "going concern" basis is appropriate, the accountants need to consider all available information for the foreseeable future; that is, at least 12 months from the reporting date.[33]

However, accountants interpret "solvency" based upon accounting principles often referred to as the *balance sheet test.* The law requires accountants to do this by stating that the financial report must comply with accounting standards: s 296. Accounting statements such as the balance sheet are *retrospective* in nature as they reconcile opening and closing cash balances.[34]

[31] Knapp et al, n 19, p 104, para 7.1.
[32] Knapp et al, n 19, p 108, para 9.1.
[33] Knapp et al, n 19, p104, para 7.1.1.
[34] Purcell, n 7, at 197.

3. Directors and the meaning of "solvency"

In law, the Court applies the cash flow test of solvency which is *prospective* in that it examines available cash resources including ability to realize assets.[35] The Court interprets solvency on this basis. Directors feel bound to follow the legal interpretation of "solvency", s 95A, as company solvency is linked to directors' duties which are legal obligations. These obligations are fiduciary duties to the company, ss 180-184. In addition directors have a duty to prevent the company trading while insolvent, s 588G. Directors are, therefore, compelled by the law to take the legal meaning of "solvency" rather than the accountants' view. A task made more difficult when it is acknowledged that directors rely upon accountants and their financial statements to make their declarations and issue the directors' report. Here again is an example of the gap between what the law demands of directors and accounting practice.

Section 95A of the *Corporations Act* defines "solvency" as the ability to pay all of a person's debts as and when they become due and payable. A person, meaning a company, is insolvent when they are unable to do this. This statutory definition is regarded as unsatisfactory because it fails to provide clear guidance in relation to insolvency thus leaving it to the Courts to interpret the term.[36] Some of those interpretations are as follows.

In *Powell and Duncan v Fryer, Tonkin and Perry* (2000) 18 ACLC 480 at 482 the Court held that s 95A does not refer to a requirement that debts must be

---

[35] Keay A, *Insolvency: Personal and Corporate Law and Practice* (2nd ed, Longman Business and Professional, 1994) p 271.
[36] Coburn, n 2, 63.

payable from the company's own money. Access to money of others is a relevant consideration. Commercial solvency of a company is not proved by merely looking at its accounts and comparing assets and liabilities. Rather the statutory focus is on solvency, not liquidity. It is appropriate to consider the terms of credit and financial support available to the company with which to pay creditors.

Sandell v Porter (1966) 115 CLR 666 at 670-671 the High Court held that solvency is a question for the Court. It is not determined by experts although experts may give evidence as to the likelihood of the debtor's liquidity upon realization of assets.   In other words once the plaintiff has a legal cause of action that can be related to a company's financial problems such as insolvent trading or liquidation, it is the Court that decides the matter of solvency because it has become a legal matter not purely an accounting issue. Accountants may give expert evidence as to a company's solvency but the legal interpretation of s 95A "solvency" by the Court is paramount.

CONCLUSION

It is a perennial issue that "unexpected" company collapses continue unabated.

It is the director's primary responsibility to monitor company accounts and, if necessary, make further inquiries.   The reality is that many directors do not or cannot fulfill this obligation due to their lack of skills and training in this area. Necessity dictates directors must rely upon the accountants. Professor Walker recommends that the audit committee's monitoring tasks should include a

requirement that directors are provided with financial and non-financial information that is high quality.[37] This recommendation is supported.

This submission examined legal obligations concerning the company accounts and the directors' declaration as to the solvency of the company. The reliability of the accounts and consequent solvency declaration has been undermined because the accounts, by law, must comply with the accounting standards. Some of these standards were found to be ambiguous and capable of misapplication. The resulting accounts do not always give a true and fair view of the company's financial position.

The status of the true and fair view has been raised in recent reforms to the *Corporations Act* but the reforms have not gone far enough. They need to both clarify accounting standards and achieve a true and fair override. It is hoped that the current inquiry will enable this to happen.

The uncertainty of the company's financial position is not only an ethical issue for accountants. It is an ethical issue for directors. Financial inferences are drawn by users of the published financial data and it is a matter of concern that they may be unreliable. It is said the major purposes for which the accounts exist cannot be adequately met. These purposes include the need to establish the company's solvency and to provide security for creditors.[38] Unless these purposes are met "unexpected" insolvencies will continue.

*** *** ***

---

[37] Walker, n 3 at 187.
[38] Clarke et al n 15 pp 304-306.