Institution: London School of Economics and Political Science		
Unit of Assessment: 17 – Business and Management Studies		
Title of case study: Shaping global accounting standards		
Period when the underpinning research was undertaken: 2012-2020		
Details of staff conducting the underpinning research from the submitting unit:		
Name(s):	**Role(s) (e.g. job title):**	**Period(s) employed by submitting HEI:**
Stefano Cascino	Associate Professor of Accounting	2011-present
Period when the claimed impact occurred: 2013-2020		
Is this case study continued from a case study submitted in 2014? No		

1. Summary of the impact (indicative maximum 100 words)

The International Accounting Standards Board (IASB) *Conceptual Framework for Financial Reporting* (henceforth the *Conceptual Framework*) provides the foundation for International Financial Reporting Standards (IFRS). IFRS enhance global corporate transparency, strengthen accountability, and improve capital allocation. Over 50,000 companies listed in 166 countries are required or permitted to use IFRS to prepare their financial statements. Research carried out jointly at the London School of Economics (LSE) and University of Bristol was used by leading professional bodies in the UK and other European countries to successfully lobby for important changes to the objectives of financial reporting in the *Conceptual Framework*. In line with the research recommendations, a revised 2018 version of the *Conceptual Framework* emphasises the importance of financial reporting information in assessing "stewardship" - managers' responsibility to protect shareholders' interests. By *directly* specifying why companies prepare and disclose financial reporting information, the objectives *indirectly* affect the decisions of tens of thousands of investors, lenders, and other users globally.

2. Underpinning research (indicative maximum 500 words)

Research by Stefano Cascino (LSE), Mark Clatworthy (University of Bristol), and four other researchers from across the EU, investigated whether the stewardship objective of financial reporting can be subsumed under a single overall "decision usefulness" objective encompassing *both* a valuation objective *and* a stewardship objective. The initial research involved a systematic review and analysis of the extensive academic literature on the use of information by capital providers **[1] [2]**.

The primary research involved a large-scale interview survey of experienced investment professionals from 16 countries around the world **[3] [4]**. All researchers made an equal contribution to the project.

Understanding the role of stewardship in accounting

The first output underpinning impact described here is a literature review **[1]**, which evaluated the dual function of financial reporting:

i) to provide information for estimating future cash flows associated with debt and equity capital to inform investors' capital allocation decisions (the "valuation role"); and

ii) to provide information used to preserve investors' capital and control and incentivise managers (the "stewardship role").

The focus in **[1]** on the critical role of stewardship in accounting challenged an existing focus among standard-setters on the valuation role alone. The review further showed that capital providers use accounting information for different purposes, raising questions about the feasibility of a truly "general-purpose" financial accounting regime prepared under one single "decision usefulness" objective.

One of the principal conclusions of the academic literature review published in **[2]** is that financial accounting information is typically used in conjunction with other sources. This indicates that the design of a financial reporting system should seek to maximise the competitive advantages of financial accounting, namely: verifiability, objectivity, regularity, and standardisation. These characteristics make accounting information especially (and, arguably, uniquely) useful for stewardship and contracting purposes.

The research published in **[1]** and **[2]** concluded that there is significant variation in capital providers' use of information, and that they sometimes have competing objectives when using different sources of information. However, direct evidence on this issue is limited. To address this, original empirical evidence was generated through 81 face-to-face interviews with investment professionals in 16 countries. An innovative survey, which embedded an experimental design, examined investment professionals' assessments of the usefulness of the *same* financial reporting information for *different* purposes. The results (published in **[3]** and **[4]**) indicate that objectives make an important difference to the type of information investors gather and how they use and value that information. In particular, the research showed that the relevance of financial reporting information is contingent upon whether it is being used for stewardship or valuation purposes. When assigned a stewardship objective, investors prefer information that excludes factors beyond managers' control; for valuation, they prefer information that helps them in forecasting future cash flows and understanding the business.

Challenging the absence of stewardship in the 2010 *Conceptual Framework*

The IASB develops IFRS for public and private sector entities around the world. These standards are underpinned by the *Conceptual Framework*, which provides the foundation for global principles-based accounting standards. The *Conceptual Framework* establishes a comprehensive set of concepts to:

1. Assist the IASB in producing and revising accounting standards;
2. Help preparers develop consistent accounting policies in areas not directly covered by specific standards; and
3. Assist preparers, auditors, and users (equity investors, creditors, lenders, etc.) in preparing, understanding, and interpreting financial statements.

Previous revisions by the IASB of their 2010 *Conceptual Framework* included the removal of stewardship as a separate objective of financial reporting. Some national standard-setters and accounting regulators expressed concern that this would impair the usefulness of financial reporting information for holding the managers of public companies to account. Its removal particularly prompted concerns that financial reporting was moving away from its historical roots as a primary means of mitigating conflicts of interest between managers and outside stakeholders. The focus in **[1]** and **[2]** on the critical role of stewardship in accounting strongly challenged the focus in the 2010 *Conceptual Framework* on the valuation role alone. The comprehensive analysis of the available academic literature showed that different objectives sometimes imply different informational properties for accounting.

Taken together, the findings of the research published in **[1]**-**[4]** strongly indicate that accounting information cannot always simultaneously satisfy the valuation and stewardship objectives of financial reporting.

3. References to the research (indicative maximum of six references)

[1] Cascino, S., Clatworthy, M. A., Osma, B. G., Gassen, J., Imam, S., and Jeanjean, T. (2013). *The use of information by capital providers: Academic literature review*. Report published by EFRAG, ICAS, and Scottish Accountancy Trust for Education and Research (SATER). ISBN: 9781909883000. Available at: http://old.efrag.org/files/Academic Research/EFRAG_ICAS_27-12-17.pdf. Reviewed by ICAS Research Committee members (academic and non-academic) and EFRAG (non-academic).

[2] Cascino, S., Clatworthy, M. A., Osma, B. G., Gassen, J., Imam, S., and Jeanjean, T. (2014). Who uses financial reports and for what purpose? Evidence from capital providers. *Accounting in Europe*, 11(1), pp. 185-209. DOI: 10.1080/17449480.2014.940355.

[3] Cascino, S., Clatworthy, M. A., Osma, B. G., Gassen, J., Imam, S., and Jeanjean, T. (2016). Professional investors and the decision usefulness of financial reporting. Report published by EFRAG, ICAS and SATER. Available at: http://old.efrag.org/files/EFRAG%20public%20letters/Use%20of%20financial%20statements/Professional_investors_and_the_decision_usefulness_of_financial_reporting.pdf. Reviewed by

ICAS Research Committee members (both academic and non-academic) and EFRAG (non-academic).

[4] Cascino, S., Clatworthy, M. A., Osma, B. G., Gassen, J., and Imam, S. (2020). The usefulness of financial accounting information: Evidence from the field. Working Paper. Available at SSRN. DOI: 10.2139/ssrn.3008083.

4. Details of the impact (indicative maximum 750 words)

High-profile corporate failures underscore the importance of managerial accountability and effective stewardship as fundamental concerns for investors, accountants, and regulatory and standard-setting bodies. The research described here has helped restore standard-setters' focus on these important aspects of financial reporting. The principal mechanism for this is the influence of the work on a revised version of the *Conceptual Framework for Financial Reporting*, published by the IASB in 2018. This replaced the 2010 version, which had reduced emphasis on the stewardship objective. The 2018 version clarifies and re-emphasises the role of stewardship as part of the decision usefulness objective. Its increased emphasis on the stewardship objective has implications for the more than 50,000 companies in 166 countries around the world, which use the IFRS based on the *Conceptual Framework* to prepare their financial statements.

Informing industry discussion and debate about the revision of the *Conceptual Framework*

The research published in **[1]**-**[4]** catalysed and informed international financial sector discussion and debate in the run-up to the IASB's publication of the revised *Conceptual Framework*. It was widely cited and discussed in international financial sector coverage and analysis of processes relating to the IASB's development of the revised *Conceptual Framework*, as seen in **[A]**. Global auditing network PricewaterhouseCoopers (PwC), for example, which employs more than 250,000 people worldwide, commented in its February 2014 IFRS news bulletin: "*The IASB will probably feed the discussion [produced by the research] into its Conceptual Framework project*". News bulletins from multinational auditing firms Deloitte and Grant Thornton also discussed the research and its implications for the *Conceptual Framework*. International preparers of financial reports engaging with the research included the Group of 100 (G100), an Australian organisation of Chief Financial Officers. The G100 summarised and discussed the implications of key findings of **[3]** in its April 2016 members' update. The professional investment community also engaged with the research, including via its discussion in an op-ed in the *International Accounting Bulletin*, written by the (then) Director of Financial Reporting Policy at the CFA Institute. This noted that the research should "*enrich the ongoing accounting standard-setting considerations and debates within the conceptual framework around the objectives of financial statements*". Practitioner engagement with the research was further promoted by its discussion on Twitter by IASB Board Member Ann Tarca, who commented on 13 December 2018: "*Helpful research cited in Primary Financial Statements paper 21B - Li 2016 JAR 54:4 and Cascino et al 2016 ICAS EFRAG report*".

Providing evidence for international accounting professional bodies to lobby for change

As well as informing practitioner discussion about the revision of the *Conceptual Framework*, the underpinning research was instrumental in providing independent evidence available to and presented by professional bodies - and subsequently reviewed by the IASB - as part of the revision process. The evidence it provided was widely used by such bodies to advocate for the revisions ultimately reflected in the 2018 version. This influence resulted primarily from the use of the research (particularly **[1]** and **[3]**) by ICAS and EFRAG to lobby for the reintroduction of the stewardship objective as a central tenet of the *Conceptual Framework*. At a series of events run by EFRAG in 2015 in Amsterdam, Paris, and Helsinki, practitioners and users of financial information emphasised the critical importance of stewardship. Findings from the literature review **[1]** and empirical research **[3]** **[4]** were presented at five events with EFRAG (held between December 2012 and July 2015) and three with ICAS (between September 2014 and September 2015), as well as with the International Forum of Accounting Standards Setters (IFASS) (see, for example, discussion of the research by IFFAS in Toronto in 2016 **[B]**).

On publication of **[3]**, the (then) EFRAG Chairman Françoise Flores commented:

> "*The findings of the study helped EFRAG reaffirming that the income statement has a major role to play and that stewardship should be acknowledged as a distinct objective of financial*

reporting in its comment letter in response to the IASB's Exposure Draft Conceptual Framework for Financial Reporting. EFRAG thanks the academic team for their thorough work and ICAS for the fruitful cooperation." **[C]**

EFRAG subsequently encouraged the IASB to place more emphasis on stewardship. In so doing, they used evidence published in **[3]** showing that financial statements are relatively more important for assessing management's stewardship than for buying, holding, and selling decisions. This was cited in their feedback on the IASB's 2015 Exposure Draft on the *Conceptual Framework*, where they disputed comments that the assessment of stewardship should be considered secondary to buying, holding, and selling decisions **[C]**. ICAS' response to the IASB Exposure Draft also refers to evidence published in **[3]** suggesting that fewer alternative sources of information are available to users when assessing stewardship. It uses this to propose that, in this context, "*the role of the financial statements is [therefore] arguably more important than in a decision-usefulness objective*" **[D]**. The use of the research in responses submitted by other major professional bodies - including, for example, the Financial Reporting Council **[E]** - further increased its impacts on the IASB's development of the revised *Conceptual Framework*.

The research also directly informed the IASB. Findings from **[1]** were presented at its board meeting in early 2014, and its Exposure Draft **[F]** subsequently suggested increased emphasis on the provision of information for assessing managerial performance. The stewardship objective received much more emphasis by the time the final revised draft appeared in 2018, influenced, in part, by the advocacy efforts of organisations such as EFRAG and ICAS which used the research to reinforce their case.

Shaping global financial reporting guidance: reintroduction of the stewardship objective

These lobbying efforts were ultimately successful: the 2018 *Conceptual Framework* recognises that the objective of financial statements is to provide information that is useful to investors and creditors in assessing and influencing managers' performance and stewardship **[G]**. This reflects the research conclusion that stewardship cannot be subsumed within an overall objective of "decision usefulness" (the production and use of financial information to inform investment decisions) as the IASB had previously suggested.

The revised *Conceptual Framework* specifically clarifies why information used in assessing stewardship is required to achieve the overall objective of financial reporting. In particular, it states that users need information about the resources of an entity, not only to assess that entity's prospects for future net cash inflows, but also to understand how effectively and efficiently management have discharged their responsibilities by deploying the entity's existing resources. As the research showed, the properties of the information required for both types of decisions often differ significantly. In particular, designing a financial reporting regime around a pure valuation objective risks sacrificing the relevance of financial reports for evaluating managerial performance. The most significant outcome of the use of the research both by the IASB and by professional bodies lobbying for change has been its contribution to this increased emphasis on the stewardship principle as a cornerstone of financial reporting globally. Since the *Conceptual Framework* provides the fundamental principles guiding the IASB's standard-setting process, the impact of its revision extends to the individual financial reporting standards and their post-implementation assessments.

Informing financial reporting practices

By helping to shape the foundation of financial reporting standards, the research had a direct impact on standard-setters and professional accountancy bodies. This is evident, for example, in its use in discussion papers issued by the IASB since the 2018 revision **[H]**. The work has contributed to improvements in regulatory practice, including by improving regulators' understanding of the ways in which capital providers use financial reporting information **[I]**.

It also has very wide-reaching indirect implications for the financial reporting practices of companies, which number more than 50,000 listed companies and a greater number of private companies from 166 countries, as well as auditors, investors, lenders, and many other stakeholders.

5. Sources to corroborate the impact (indicative maximum of 10 references)

[A] See attached evidence for discussion of the research in the professional press and on social media.

[B] For discussion of the research by the International Forum of Accounting Standard Setters, see Section 3 (pp. 4-5) of the report on their Toronto meeting, 4-5 April 2016.

[C] For impacts of the research on EFRAG's input to development of the revised *Conceptual Framework,* see EFRAG: "New investor insights into financial reporting", 9 March 2016; and *Feedback to Constituents – EFRAG Comment Letter*, February 2016 (p. 7).

[D] ICAS, Response to IASB Exposure Draft ED/2015/3: *Conceptual Framework for Financial Reporting*, 25 November 2015. See p. 3, *n*.1 for reference to **[3]**.

[E] Financial Reporting Council, *Response to the IASB Exposure Draft on the Conceptual Framework for Financial Reporting*, November 2015. See p. 13, *n*.7 for reference to **[1]**.

[F] IFRS, Exposure Draft ED/2015/3: Conceptual Framework for Financial Reporting, May 2015.

[G] IFRS, Conceptual Framework for Financial Reporting, March 2018.

[H] For continued use of the research in discussion papers published by the IASB, see *International Accounting Standards Board (IASB)*, Primary Financial Statements Project - EBITDA, December 2018, p. 14 for reference to **[3]**.

[I] EFRAG Short Discussion Paper, January 2014: *The use of information by capital providers – Implications for standard setting* summarises key research findings and discusses its contributions to improving accounting regulators' understanding of the ways in which capital providers use financial reporting information.