



Peter Burgess LinkedIn Blogs

Conventional Accounting is Failing Society

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Conventional accounting is a very powerful tool for business management used both for reporting money profit performance to investors and used within the internal business MIS to optimize the performance of the organization by reducing costs and increasing profits.

Many generations of business school students have learned how to optimize business performance using conventional accounting numbers and have positioned themselves to become highly paid financial engineers.

But all of this is failing society.

Simple accounting metrics that help a business operate efficiently results in a good business, is good economics and is also good for society ... and this works in a world that has the characteristics of a free market as described by Adam Smith in 1776. It does not work well in a society and economy that is as complex as we have today and where a very large part of the economic activity in the world is controlled by very very large multinational entities. Many of what we call 'markets' are gamed in a variety of ways, and rarely serve the purpose described by Adam Smith.

Optimizing the performance of big business entities using metrics based on conventional accounting is most likely going to result in serious impact on people and planet. The profits will be reported, the impact on people and planet will be ignored. To the extent that reporting of these is required, at the moment this will be qualitative reporting not something that is rigorously quantified.

Quantification of impact is essential and it can be done.

The simple arithmetic for payroll is that payroll is a cost to the company and a negative for profit. At the same time payroll is an income for the employee, money for the employee's family and money circulating in the community where the family lives. A company should have metrics for all of this, and not just the payroll cost in the money profit accounts.

Other parts of conventional accounting need to be supplemented by impact analysis. The money spent on energy is also an impact on the planet in terms of resource depletion and environmental degradation.

All of the materials used in production come through a supply chain. The conventional money profit accounts only report the immediate money cost of the materials, but these materials have a whole supply chain story embedded in them. This needs to be extracted and brought into account. This covers all the environmental issues, the workplace safety issues, the profits, the taxes, the pluses and the minuses.

Products being sold have a price and the revenues go to profit in the conventional accounts. Products have a history that includes not only the elements from this part of the manufacturing chain, but all the prior supply chains. Products also have perceived value to the buyer and an embedded story about the supply chain, and then the impacts during use and eventually the post use waste chain. Products are the link from people and their quality of life and everything else down to the impact on the environment.

Investors applaud a company when it reduces the taxes it pays. When taxes are not paid, it is society that loses. The idea that almost every government entity on the planet is bankrupt suggests that more taxes are needed (though I will also observe that the efficiency and effectiveness of government leaves a lot to be desired ... something that better metrics can help to fix).

Conventional accounting is powerful because it has an interesting data architecture ... the idea of balance sheet accounts and profit and loss accounts. There are other important concepts that make accounting so very effective including clarity about the reporting boundary. All of this has been used for a very long time to account for the organization and the performance of the organization.

I argue that these ideas from conventional accountancy need to be used to help understand the performance of people and their society ... and the impact a good quality of life for people is having on the planet, on nature and everything that relates to the natural world. In this data architecture or analytical structure, the organization is an intermediary between these two primary forces. The efficiency or effectiveness of the organization should be seen in the context of the progress of people and the impact on planet.

Conventional accounting is failing society ... but the framework of accounting is strong, and it could be re-purposed to be of immense value in better decision making for society and the planet.

Exciting possibilities

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