

Contribution to Prosperity

A Proposal to Establish a New Accounting Standard

28/03/18

This paper sets out a process to develop a new accounting standard for reporting an organisation's contribution to prosperity.

Background

There is a growing awareness that monetary reporting of an entity's profits and a nation's GDP is insufficient to serve the needs of modern society. This is underscored by economists' failure to forecast the financial crash of 2007, coupled with growing populist discontent with the achievements of society.

Alternative emerging measures of the success of an economy focus on evaluating prosperity, measured in terms of human experience, and sustainability, measured in terms of individual resources. Examples of prosperity indices include the World Happiness Report¹, and the Legatum Prosperity Index².

The accounting profession needs to develop new accounting methodologies for entities reporting under the new paradigm. Any such methodology needs to accommodate two established economic principles:

1. GDP

There is a reasonably direct link between an organisation's impact measured in monetary terms in its financial statement and monetary GDP. There is unlikely to be an equivalent link between an organisation's impact measured in social terms and national prosperity. Prosperity is a combination of many factors, such as health, education and safety/security. The contribution an individual organisation makes to each individual member of society varies depending on the individual's personal circumstances.

2. The Invisible Hand

A positive feature of economic capitalism is the existence of the “invisible hand”. It helps achieve an optimal allocation of resources between competing demands through profits. It rewards organisations through a pricing mechanism that reflects relative supply and demand for output, to favour the optimal supply by the best organisations, through profitability and return on investment. The authority of this model has become substantially undermined. As inequality has continued to grow, many of the needs and aspirations of the general public are neglected. In support of the new measures of prosperity, we need a new “invisible hand” that aligns with the prosperity of members of society as a whole.

Accounting Approaches

The new accounting methods should reflect an entity's contribution to prosperity. Two evolving approaches include:

1. Societal Impact

An entity identifies one or more social objectives, articulates its objective(s), and measures its performance by reference to the objective(s). The merit of this approach is to give effect to an entity's social responsibility, whilst fulfilling its primary objective of generating profits. A challenge is that success is measured by reference to objectives set by the entity itself, with little regard to other ways in which it has positive or negative social impacts.

1 <http://worldhappiness.report/ed/2018/>

2 <http://www.prosperity.com/rankings>

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2. Contribution to Social Cohesion

Entities may not be able to measure their overall contribution to prosperity, but they can measure their contribution to social cohesion. Social cohesion describes the level of trust, inclusion and common purpose between members in society. It has a positive correlation with national prosperity, and it is profoundly influenced by the behavioural cultures of organisations and institutions. The approach requires organisations to identify and assess the values they exercise in their interactions with all stakeholders, and the wider community. The merits of this approach include simplicity, standardised measures that allow comparison between entities, and an “invisible hand” pointing towards social wellbeing. A challenge is that values need to be defined consistently to allow them to be measured consistently.

There are a number of variations or “flavours” of the above approaches, and other approaches exist or will come into existence.

Proposal

A body of interested parties will be established to solicit and evaluate methods of accounting suited to the reporting of national prosperity. We expect to include representatives from: accountancy; economics; industry; long-term investors such as pension funds, insurance and charity; and academia.

It is expected the body will define its own framework and programme.

It is expected the programme will include:

- raising awareness of the initiative and of the issues.
- soliciting proposals.
- evaluating them.
- summarising the key proposals in a single paper.
- soliciting opinion from interested parties about the proposals.
- creation of a white paper with formal proposals.