



CRISIS AND ACCOUNTANCY

In discussions about the choppy financial seas, many experts from different fields are in agreement on the origin of the present crisis and the factors behind it. But some have pointed the finger at changing accountancy practices.

The adoption by developed countries of the International Finance Reporting Standards (IFRS) involved incorporating a new conceptual framework based on an advanced model suitable for collecting information on the new economic/business reality.

Of course the new regulations allow for a certain degree of discretion by people who prepare financial information: they propose an approach of principles over one of particular rules; they reflect operations in terms of economic background and prioritize substance over style; in some cases, they use fair value, as it is nonsensical to value goods at the time of their acquisition; they record assets only when they generate future benefits - in short, they aim to boost transparency over conservatism and opacity.

“But what about the principle of prudence?” some academics ask. This principle distances accountancy from its final goal as a basic instrument in taking business decisions in order to boost the transparency of markets and assess the way businesses are run.

The application of fair value has nothing to do with whether unrealized profit is distributed as dividends, nor whether businesses are worth more or less according to the accounting standards used. Accountancy is one thing; business valuation another - yet it seems some people are still confused about the difference.



It is true that fair value emphasizes accounting results in good times and reduces them in periods of crisis, and we should work on this in order to introduce corrective measures – but that does not mean it should be abandoned as a criterion, which is how many international institutions have understood it.

Accountancy is not, nor does it pretend to be, an exact science, but rather a discipline of the social sciences and therefore subjective and partial. This is because the uncertainty that surrounds all business activity demands choices in accountancy policies and criteria and therefore subjective decisions.

But we needn't tear our hair out. The increased importance of accountants is not bad *per se*; in fact it enables more precise information-gathering on an economic and financial reality at any given time, and is also exploited fully and freely by society in commercial transactions.

The Anglo-Saxons have been leading the way for a number of years, awarding an important role to accountants, their experience and



their sound professional judgment in determining criteria to apply, estimates to take, previous valuations to draw from, etc.

Some people aren't agreeable to this increased freedom, preferring to keep things hidden rather than promote transparency and a more precise reality. But the time for such ideas has given way to more solid principles in keeping with the Chinese proverb that "the best kind of closed door is the one you can leave unlocked".

What is surprising is that accountants should be singled out as being responsible for the crisis! Of course it is always tempting to shoot the messenger, but in the here and now our role is quite the opposite, and indeed fundamental. Audit reports, essential to restoring confidence, are proving their credentials for navigating a course out of the crisis, and states are supporting the profession in an attempt to get to the bottom of the 'black hole' of toxic assets, helping plug the gaps and errors of control committed by a number of countries.

In short, pointing the finger at accountants for the present financial situation is a big mistake. As John K. Galbraith astutely remarked, "We have 2 classes of economists: those who don't know – and those who don't know they don't know".



FINANCIAL CRISIS AND BUSINESS RESTRUCTURING



Crisis. ¿Qué crisis?

An economy or business in crisis is an economy or business that is sick. A business in crisis is an anti-natural reality. The *raison d'être*, the very goal of the existence of a business is to generate wealth - wealth for the shareholder/proprietor through the attainment of profit and the distribution of dividends; wealth for the employee, who receives payment in return for his or her work; and, ultimately, wealth for society, through the creation of

value and the contribution of the goods that are produced and released onto the market, or the services the company provides that are aimed at society in general.

If we agree that a business in crisis is a sick business, we have to acknowledge the situation and diagnose the illness. The adoption of any therapeutic measure requires previous diagnosis and the success of the treatment depends on the diagnosis being made in time and its

origin and causes properly determined. We can't solve a problem if we don't accept and acknowledge its existence first. In the field of business management, failure to acknowledge the existence of a problem immediately blocks the proprietor and, worse still, the management team responsible for the company's day-to-day operation. A type of irremediable resignation spreads, by virtue of which the origin and causes of the sickness and the difficulties the business is experiencing escape the reach of proprietor and management team alike. This ensures the solutions will also hinge on the fate of factors external to their ability to take decisions.

Origin and causes of the crisis

Following a decade of economic growth and fierce expansionism, we are now facing a financial crisis that is shaking the most solid foundations of the capitalism of the past century. This is the first financial crisis of the 21st century, the first big one in the age of globalization. It is a crisis whose existence and scope we were slow to acknowledge because we didn't see it coming - let alone its disproportionate effects. Overnight we saw the principles we thought were the cornerstones of economic-development policies fall apart.

There are many possible reasons why the leading Western economies have reached this point. It is hard to single out any one in particular. However, there does seem to be a certain degree of consensus in the identification of some of them, which most academics agree on:



The global economy

The paradigm of all the ills afflicting the majority of Western economies, its origin lies in the excesses produced by the prolonged good times and unbridled growth that led to the relentless development of new financial instruments and products to keep the boom rolling. Excess liquidity, which in turn generated greater economic and social imbalances, which was sustained on volumes of limited resources, demanding artificial turnover that created no value other than the simple movement of capital, made it easy to use a single financial product in an indeterminate number of operations. These types of actions, taken in the farthest-flung corners of the world, wound up affecting financial institutions at the heart of our economic geography. Human greed, unregulated and uncontrolled globalization and easy finance sowed the seed for financial speculation.

The global financial crisis

This in an easy way to justify the catharsis in which our economy languishes, i.e., the problem was external and, together with the global economy, swept us up in its path. However, the Spanish economy and the world of finance in particular were not passive spectators to the fierce expansionism of Western economies over the past 10 to 12 years – quite the opposite. They played an active role, accepting the creed of ‘growth above all’ and that not joining in would see them fall behind in the race towards progress and economic development. The need to find artificial turnover for existing financial products and the subsequent forced drops in interest rates, together with a number of zany ideas at play in the major US banks, and Anglo-Saxon banks in general, resulted in the appearance of a number of financial products aimed at customers who did not pass even the simplest tests of prudence, control or arrears risk. So much has already been said about subprime mortgages that I don’t need to raise them again here. Instead I would like to draw attention to the serious lack

of control of national banks and financial market regulatory authorities.

Lack of control of the financial markets

We have to question the role the financial markets played in this panorama of excessive growth and lack of control. There is no doubt the global financial boom would not have lasted as long as it did without the financial products that made it possible. The markets’ active participation in the process is a point I touched on earlier, but I would now like to focus, from a critical perspective, on the laxity of the authorities responsible for establishing control over the operation of the financial markets. It is hard to justify the very significant holes in the big banks of nearly all the most advanced nations. Holes so extraordinarily large they brought down prestigious, centuries-old financial institutions in the US and crippled many more in Europe, forcing them to turn to their respective governments for aid. Can we really attribute all our woes to an unexpected and unjustified alignment of the unluckiest stars in the financial firmament? What degree of



responsibility should we ascribe to frivolous management on the part of the rating agencies?

More and more people are openly questioning the aid measures offered the banks. The gloves are coming off and while some say that not helping financial institutions now could accelerate the crisis and worsen the situation, other experts argue it would be better to let unviable banks fall by their own sword.

How long will the crisis last?

That is the million-dollar question in all the forums and debates about the economic situation - from the arbitrary, irresponsible and quixotic positions of certain governments that venture a guess at recovery coming in the second half of this year through to the dramatic positions of prudence and fear tendered by the likes of Paul Samuelson, who predicts we still have a decade to go before there is light at the end of the tunnel.

In any case, it looks likely that the road will not be easy and that a solid and stable recovery will not come until at least halfway through 2012.

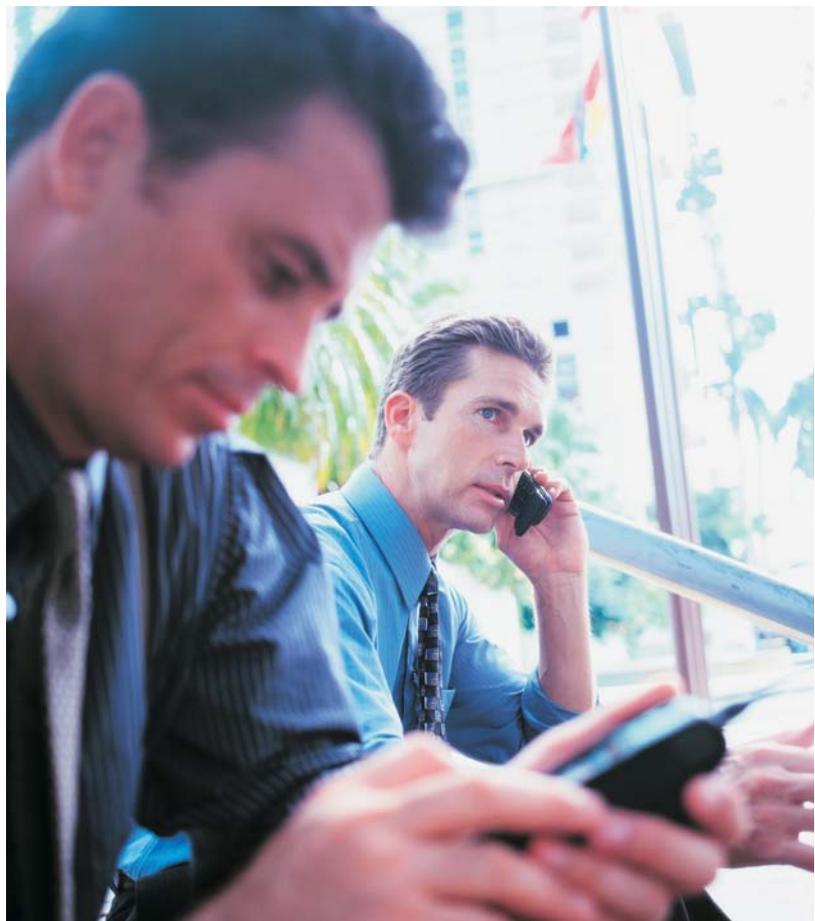
How can we emerge from the crisis?

Having reached this point, we are forced to accept that we are indeed in the midst of a crisis. So how do we emerge from it? I have already said that the first step towards solving a problem is to acknowledge its existence. That is why it is so important to have a suitable and accurate diagnosis of the situation. Knowing the origin and causes will be essential to addressing the problem and designing a strategy to solve it.

Statistics show it generally takes around 18 months to react to a crisis. The losses produced in this period, both in economic and market-credibility terms, can render the recovery of a business unviable as well as reduce the liquid assets it needs to tackle problems head-on. Two main reasons are put forward to justify the lack of reaction to a crisis. First there is the problem of accepting that a cycle of expansion and growth has ended, and a period of contracting activity and business has begun. Then there is the lack of experience in addressing restructuring processes. Under these circumstances, unusual complicity between proprietor and management becomes essential. The role management plays in handling the crisis will be a determining factor in whether or not the company emerges intact. A balance should be

struck between the tension normally required in these types of situations and the strength of courage of the people responsible for managing the company. Retaining the key members of the management team will be fundamental.

A series of urgent measures must be adopted in the first ninety days after becoming convinced that a firm is floundering. The first, extremely important step is to put together a three- to five-year business plan that anticipates the future position of the company and the measures to be implemented. It is important to understand clearly that measures and policies that were legitimate during the period of expansion will not apply in times of crisis. Managers need to take this onboard and get with it.



NUBA: ASSESSMENT AND DEVELOPMENT OF POTENTIAL



In today's Knowledge Age, an organisation's ability to build intellectual capital is a crucial element to creating value and gaining a competitive edge. One of the main challenges now facing organizations is getting each individual to perform successfully and for this conduct to be in line with corporate goals. NUBA is the most effective tool for identifying and developing successful individuals and equipping them with the abilities an organization needs.

Sergio García, Gervasio Deferr, Natalia Vía Dufresne and Arancha Sánchez Vicario are very different people (who they ARE), but they all learnt to play golf, tennis or sail and to work hard (what they DO) to

become number 1. Fernando Alonso, Mika Hakkinen and Michael Schumacher are very different people (who they ARE), but they all learnt to race Formula 1 cars and to work hard (what they DO) to become number 1.

This means that:

- We can all learn effective behaviour that we can apply in our professional fields.
- With practice, feedback and more practice improvements can be made, which will be reflected in better personal and professional achievements.

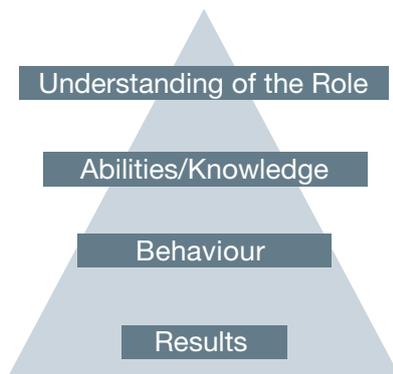
Professional sportspeople are not the exception. The same goes for

lawyers, doctors and pilots, as well as managers, executives and project managers. In other words, all successful professionals demonstrate more effective and efficient behaviour in critical situations, even though they have different personalities.

As Dr. F. B. Skinner says, "A vague feeling of order is born from the rigorous observation of human conduct". This becomes clear if we observe managers, executives and project managers in their daily work: beyond their individual differences, it is possible to identify a number of common patterns of successful behaviour.

NUBA measures what sets successful managers, executives and project managers apart from less successful people. It measures what they do; what they do differently; what they could do differently, and what they think about their own behaviour.

We know that to identify and develop successful people there are various factors we should look at, including:



- Understanding one's own role: in other words, what the person understands about the expectations

of the actions they take and the significance of their jobs.

- Attitudes: how the person believes he or she should behave and address particular critical situations.
- Conduct/Behaviour: which types of behaviour really make a difference to results.
- Results: the type of results the person should obtain.

It is also important to mention that potential is a psychological construct and cannot be measured as precisely as we might like, but only estimated. That is why potential is not assessed by results but by considering the processes that lead to them.

NUBA responds to requirements that exist in assessing the potential of people with critical responsibilities. The advantage of NUBA compared to other ability-assessment systems is that it compares results with models of excellence in performance.

We need to use the same ways we use to improve in order to compare

ourselves with people who work optimally. This ensures ongoing possibilities of professional progress.

This is how NUBA can support the development of people's abilities. It considers you should:

- Establish a model of excellence against which to compare your skills.
- Determine your strong points and work on them, as this is the only way to deliver above-average output.
- Consider your weak points, particularly ones you could work on to allow your strong points to be fully developed.
- Ask yourself which tasks you find easiest and which you find hardest.
- Ask yourself what you can do to improve your performance.
- Consider your goals and desires, and consider what you do not want to happen.
- Set reasonable goals you will be able to achieve.



INTERVIEW WITH MARIO ALONSO AND ANTONIO GÓMEZ on how to survive the present economic situation



“We have to stop complaining about it, except that the situation has changed and look at ways to address it”.

In the midst of the global financial crisis we should probably begin with this question when discussing the business situation: is the current economic context really so bad or can we interpret the latest unemployment figures as the start of a recovery?

Mario Alonso: I think the unemployment figures are good news, but we shouldn't break out the champagne just yet and declare that the crisis is coming to an end. I think unemployment will continue to rise and that the crisis is very profound, but of course we're going to embrace any good news with open arms.

The situation has been blamed on the banks, the property developers and even the public for taking on too much debt. What percentage of blame should business take for what is happening?

MA: Many factors have come together to form this crisis – it's the same as when an accident happens. Some are financial, because a number of business practices led to a financial bubble (as well as the property bubble) and amongst these we have to include a major crisis in values and lack of business ethics. Then there are reasons of a more economic nature which will require a substantial overhaul of the model; and psychological reasons, which can be just as important as others. The real situation is as important as the perceived one, and at the moment it is the perceived one which is making people lose faith, hold onto their

investments, rein back on consumption and business dealings, etc. – and this slows the economy down even further.

Antonio Gómez: The big problem with this crisis is that we are part of a globalized market and what is happening in Spain is largely a result of what is happening in the rest of the world. We can't distance ourselves from what is going on in the world markets and the steps being taken to address the crisis.

You talk about needing a change of model. What were we doing wrong and what has to change in order to recover?

MA: The problem in Spain is that for many years the economy was driven by three main sectors: property, domestic consumption and tourism -

partly the car industry, too, although to a lesser extent. And when the property sector collapsed it took consumption and, indirectly, tourism, down with it, which meant the system no longer worked and it had to change. However, this does not mean we have to do away with the model completely. It's not a question of innovating and creating sectors out of thin air. Finland had a small telecommunications sector and today it leads the world. Here we have incipient biotech, alternative-energy and fashion industries (the latter very important in Galicia) and if they are managed well they can generate wealth.

But the fashion sector here, like many other industries, is reporting a trend towards dismantling because of relocation. What effect is this having on the present world situation, where it appears to be impossible to compete with certain economies?



AG: It is extremely difficult to compete whilst maintaining artificial economic barriers that only make products more expensive but that do not prevent goods from reaching the rest of the world. It is forcing us to seek added value and to create – which are other values we can use to compete with. Fashion is a good example: the definitive factors are still in Spain even though production is distributed around the world. But there are certain production costs we cannot compete with; we also have to recognize that this is part of a process. As poorer countries gain purchasing power, their wages begin to climb. It's what happened in Spain when we joined the EU. Back then we were the favoured destination of a great deal of investment because production was cheaper here. And purchasing power will rise in countries like China and India, generating opportunities for us - because when the Chinese begin to travel, for example, the Spanish tourism market will be practically inexhaustible. It is an incredible opportunity. What we need in a globalized market and world is specialization.

MA: World models have changed and Europe has a number of values that neither the US nor the emerging countries have: culture, history, know-how....things we can take advantage of.

We have been seeing reports for months now about companies cutting back on staff and applying for employment regulation procedures. Are companies overly dependent on them or are they necessary in the present situation?

MA: When a business proprietor lodges an employment regulation application it is because he or she believes it is the only way forward,

but that is not always the case. They could probably look into other ways to restructure; be imaginative; open up new lines of business; and above all consider the personnel they want to get rid of very carefully. The situation should be studied on a case-by-case basis, seeking the best solution.

I imagine that is another function Auren has now. What does this consultancy firm offer that sets it apart from the rest?

AG: Auren is a multidisciplinary services firm that covers many business needs, from auditing (with complete data reliability), to advice and support in legal situations and consultations. The field has expanded and we have to help businesses become more efficient by learning how to negotiate financing with financial institutions, increase customer loyalty and retain talent. In Galicia, for example, one of the sectors with the greatest development potential (it will be particularly promising when we emerge from the current economic cycle) is supporting management succession in family businesses. We presently address the question of succession by helping businesses establish protocols they can use to settle conflicts and restructure with a view to taking changes onboard. We also support the management skills of the up-and-coming generation and prepare employees to accept that this person, who they may have seen growing up, will one day become their boss - not because they inherited the business but because they are ready and able to run it. Certainly many family companies are presently finding it hard to pay the wages at the end of the month and can't see beyond that, but the situation will change and it will become necessary to again



accept the position that a number of companies find themselves in. Don't forget that 70% of family businesses collapse when passed down from one generation to the next, and it is a pity to lose this business ability that will later be needed to maintain a country's development.

Small companies are often more reluctant to seek outside help. Is that the way you see it?

AG: I would say they accept it pretty well here in Galicia, maybe because we are also more receptive than our competitors. We have a much more extensive services environment which is better adapted and more innovative, but also we are close and can offer the personalized attention that makes a businessperson's daily work much easier. In all honesty, we haven't yet seen the demand we would like: unfortunately many companies ask what something will cost them rather than what they will

get in return, but when you know what you will get you can weigh up whether it is worth the cost. However, we have many loyal customers who presumably stay with us because they think they're getting a good return on their money.

Finally, any tips on how to survive the critical period ahead?

MA: Well I would say, first of all, we have to stop being scared. I know it's not easy, but we have to stop complaining and accept that the situation has changed; that we are facing new circumstances and that we have to learn how to handle them. We also have to change the defeatist attitude typical of this country. From there we can look out for new opportunities and ways to restructure a company; improve its processes; reduce costs, and find the right people for the job - or if you already have them, how to keep them motivated. In short, you must adjust as much as possible so that when the cycle changes, which sooner or later it will, you have a business that can face the future with confidence.

AG: You need to be very flexible in adapting to the environment – a company that fails to adapt to a changing environment will sink, while one that has been capable of adapting will emerge stronger. Unfortunately, when things are going well many companies think the situation won't change, when in fact it is precisely when things are going well that you need to prepare for a crisis. That's when you should be investing in new markets, developing new products, working on customer loyalty...because when the going gets tough there won't be as much room for manoeuvre. Any company that can keep its head above water now

will be in a good position in the near future.

MA: I think we have a number of businesses with extraordinary international capacity, particularly big business, the large multinationals. Sure, there are more problems in the SME sector, but I believe our business culture has made great strides in recent years and a number of sectors are extremely well placed for development.

AG: Also there are more and more medium-sized enterprises (we have many of them among our clientele) who know the world is their market and which are more than able to compete with any business from abroad. In fact, it was our customers wanting to expand overseas that forced us to internationalize and create a network of offices in various different European and Latin American countries to help them grow there, which would otherwise be very difficult to do. Another thing to bear in mind is that we currently have the best-educated generation in our history... our average Spanish graduate is just as well qualified as his or her counterparts in the US, France or the UK.

Just as well qualified in terms of studies, maybe, but not with regards the job situation...

AG: That is why it is absolutely essential for businesses to realize that the human resources department is not just a production factor but an essential part of the company. Otherwise it would be very hard for a proprietor to expect employees to give their all for the company. If the company doesn't respond, the staff won't either and some great opportunities will be lost.