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“Tomorrow’s judgments”
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Tomorrow’s Judgments

Good afternoon. It’s great to be back—I’m honored to once again address the students and faculty of the University of Illinois Department of Accountancy. This institution is truly cutting-edge and it is preparing students for a new reality. And here’s the proof.

This year 94 Illinois students will be joining Deloitte—94! More than any other business school in the U.S.

So why is Deloitte hiring so many students from the University of Illinois? Because we want to recruit probable Cubs and Bears fans? Not, exactly.

In fact, there’s a very compelling reason. You’ve got the *stuff*. Not just the GPA but the DNA—the wiring. The brains, certainly. The knowledge and education, obviously. The critical ethical and moral character, absolutely.

But, in the final analysis, even all this is not quite enough. At Deloitte we’re also looking for other critical skills—in fact, the very skills emphasized in your Project Discovery Program.

- Skills of inquiry and analysis—skills of discovery.
- Strong leadership and decision-making abilities.
- And collaborative skills—an ability to work effectively in teams.

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And one more thing: a thorough grounding in the complex decision-making process that guides the art and science of what we commonly call *judgment*.

As you know by now, when we speak of judgment in the context of our profession, we are not talking about inspired intuitions. We are talking about *a process used to reach a well-reasoned conclusion that is based on the relevant facts and circumstances available at the time of the conclusion*.

Now, judgment frameworks may differ. So, to better define what I mean, I’ll mention that ours involves a three-step approach:

STEP1: Transaction Analysis. First we identify and document the issue at hand. Understanding economic substance is paramount—often involving considerations beyond “accounting” per se. And documentation should be contemporaneous.

STEP 2: Accounting Research: Next comes development of research focusing not only on the relevant technical literature, but also any alternative views. There will be increased sensitivity to differing practices.

STEP 3: Decision-making: Here, the review process should include all key individuals involved in deliberating the issue, which may include non-accounting professionals. There will be increased emphasis on the appropriateness of the assumptions made in formulating the final decision, with particular attention to appropriate disclosure in the financial statements.

Those are the three basic steps. But the next steps in the journey we are preparing to embark upon may be giant ones, comparatively speaking.

I say this because I believe we're entering a global era that will lead us to exercise ever-increasing levels of judgment—judgment new in degree and scope; more transparent in how it is reached, and more forthcoming in venturing unbiased professional opinions.

Please understand: I'm not suggesting that today's professionals do not render judgments—of course they do, and always have. The difference will largely be one of degree. Under the framework provided by International Financial Reporting Standards, accountants will work more closely with others to make accounting judgments based on the underlying economics of transactions.

Now granted, judgments involve a degree of risk. But I see a big upside to this new story. In the not so distant future, I foresee that this same accountability will make us more scientifically-minded, better understood, and more respected as a profession. I also think it will make our work more meaningful—more exciting and interesting.

In fact, my friends, you may feel that, as an accountant, you didn't fall so far from your dreams and aspirations as a six year-old—you know, of being an astronaut or a famous scientist or technology whiz.

I see three trends driving this future:

- **Trend 1: New global standards of financial reporting.** I mean, of course, standards driven by the coming world of IFRS.
- **Trend 2: New expectations driven by the digital age.** From Wikis to blogs to i-Phones, the digital age is creating a new generation of knowledge consumers with big expectations of how we report financial reality and the judgments behind it. And, potentially, even the frequency of those judgments.
- **Trend 3: New expectations unleashed by the global downturn.** Today, among investors and the public, there is a feeling of 'never again.' We will all have a role to play in rebuilding public trust in the capital markets.

In the next few minutes, I would like to give you a real-world perspective on these three trends. Then I'll offer some ideas and advice on how to succeed in this tough new environment.

And with one caveat: By training I'm a lawyer and a tax accountant—a tax guy. I hope this doesn't disqualify me!

I'm also learning—learning every day running an organization of 45,000 professionals with a major audit practice as one of our world class businesses. In the words of the great Yogi Berra, “You can observe a lot by seeing.”

Let's dive into these major trends a little deeper.

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Let's begin with **Trend #1—the advent of global reporting standards known as IFRS.**

Wondering if and when IFRS will come to the U.S., some jokingly call IFRS “Iffers.” Personally, I don't think there's much ‘if’ about it. U.S. investors—and businesses, for that matter— won't long tolerate a global system where the U.S. remains the square peg in a world of round holes.

The change is driven by many factors. Of course, our economy is increasingly global—in 2001, only 32 percent of U.S. companies had a percentage of their sales outside of the U.S. By 2007, that number had grown to 46 percent, almost one in every two companies.

The other reasons are regulatory and political. As you may know, last November the SEC issued for public comment a ‘roadmap’ with milestones and a timeline for mandatory adoption of IFRS for public companies, beginning in 2014. It includes proposed amendments that would permit certain U.S. companies to be early adopters.

Obviously, between the downturn and the new administration, much is in flux—just last week the SEC extended the IFRS comment period by two months. The time-table and details may change but the discussion continues and, in the meantime, we're continuing to see that our professionals and our clients are prepared.

So, as the Obama Administration proceeds with its plans, we look forward to working with new SEC Chairman Mary Shapiro and other incoming officials on the IFRS issue. I think debate around these issues is healthy and will strengthen the quality of the ultimate solution.

In the meantime, as I've indicated, we are getting ready in many ways for IFRS.

Last December, we hosted an IFRS Summit, with our guest Sir David Tweedie, Chairman of the IASB. We have long had a U.S. IFRS Center of Excellence. And there is also our IFRS University consortium collaborating with professors at more than 200 universities as they re-shape what and how students are taught.

And we're assisting our clients with IFRS work. In total, that's thousands of people being trained—people across Deloitte and hundreds of thousands across the profession, academia and business.

But more than compliance concerns are driving this financial reporting revolution. As IFRS is demonstrating, it is more than a ‘reporting’ system. It doesn't just comply, it describes.

It's also shorter and simpler. As a system based on principles, IFRS is relatively compact: some 2,500 pages. By contrast, the more rules-based U.S. GAAP system comes to some 25,000 pages—ten times that size.

But the GAAP vs. IFRS debate is really not a battle between rules and principles. As practitioners have long recognized, there can sometimes be a 'disconnect' between the accounting treatment as recognized in financial statements under U.S. GAAP, and the economic reality that underlies the transactions being accounted for. In today's global world, we believe the judgment focus of IFRS is better able to reflect an extraordinarily complex and fast-changing reality.

Now, likely there are some who will not agree with my assessment about the future of IFRS. It's a matter of debate and I am happy to have that discussion.

Okay: **Next trend - new expectations driven by new digital media.**

Face book, YouTube, Wikipedia—unlikely as it sounds at first, all may have implications for the future of financial reporting and the character of tomorrow's judgments. Why? Because they are radically changing people's expectations, first, in how they locate and consume information. And, second, in *what* and in *whom* they trust.

Take Wikipedia. Here's a collaborative encyclopedia ten times the size of the Encyclopedia Britannica. Owned by no-one, with a handful of paid employees, Wikipedia is the creation of tens of thousands of enthusiasts who write—and zealously check—its thousands of entries.

The point: As with food labels, Wikipedia and similar models are creating a public that, by the day, is growing more critical, savvier, and often more involved in the information they consume or reject.

Blogging is also having its influence. In blogs, we find instant, more personal and more unvarnished reporting of reality (or, at least, perceived reality)—again, a trend that holds the potential to raise expectations in those who rely on us as a profession. Don't just report. Give me the complete picture. And give it to me faster.

Finally, there is the lesson of the i-Pod and the i-Phone, two of the most successful consumer products in history. These i-Products are simple, powerful, and intuitive. And so in time, we might wonder if the investing public will come to expect the same intuitive elegance and simplicity in how financial information is presented. Something to consider as we look toward the future.

TREND #3: The Downturn.

In last month's inauguration speech, President Obama called for a new era of responsibility—and few would disagree when trillions of dollars have been exhausted and employment has fallen to levels not seen in decades.

Well, my attitude is anything but gloom and doom. I've lived and led through several recessions, most recently the Dot-Com crash of 2000 and the aftermath of 9/11. In every case, I've seen two

things. First, hard as times may seem when they are happening, they always end. And second, when it comes to recovering from recessions, the U.S. system excels at figuring it out and addressing the underlying issues.

Still, to fix it, we need to better understand it. That means not only keenly examining judgments made, but the common beliefs that may unduly influence those judgments. Consider three once-common beliefs that influenced the global downturn:

- The belief that home prices might stall, but they would never go down nationally.
- The belief that events like the Great Depression were things of the past—now handled by new checks and balances. Risk shock absorbers. Economic safety brakes.
- The belief that through new models and products, risk could be better shared and distributed—meaning, that enterprises could assume even *greater* risk.

You're young. You've seen what can happen. You now know how easy it is for humans, even the smartest, to forget common sense and follow the herd. The point is: You're a professional, ultimately serving the public trust, operating in a regulated environment and dedicated to the health of the capital markets.

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So, to wrap up, let me try to put a little more perspective around the changes coming to our profession.

The notion of a single set of global accounting standards—so long debated—now seems to me a reality driven by the world economy's expansion, diversification and integration. I'd like to make an interesting parallel suggested by Deloitte's resident IFRS expert--my colleague D.J. Gannon, who is with us here today.

D.J. sees a parallel in the work of Thomas Kuhn and his book, *The Structure of Scientific Revolutions*. As a book on evolution and revolution, Kuhn's ideas can be applied to many fields—including ours.

And here's the tie-in. Much like scientific development, financial reporting has tended to develop along a steady line. But in the face of a rapidly changing future... *is* the steady path now necessarily the *best* path?

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You see, as Kuhn concludes, science is not the result of steady progress along a single line. He points out that periods of "normal" scientific research are punctuated by major breakthroughs. Why? Because anomalies crop up—exceptions that suddenly don't fit the existing and commonly accepted approach. And as a result, an entirely new approach is proposed that eventually replaces the old one.

Recent events suggest that the credit crisis—and its complex global ripple effects—might be this kind of precipitating event for financial reporting. In other words, we may be at a crossroads where having a global perspective on financial reporting is not longer a choice, but rather a necessity.

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Which leads me to the big question for *you*, the next generation: What can YOU do to prepare for this new world? To up your game and make the judgments required?

Let me offer four suggestions.

1. Commit to the highest values of your profession. The process of judgment requires patience and discipline. Recent events show what can happen when judgment goes missing. So be scientists—always committed to the truth, and to the process of *finding* the truth.

2. Think more like an historian, and begin focusing on a particular industry. Today, being a generalist—even a brilliant one—is no longer enough. If you're not going to repeat the mistakes of the past, you need a thorough grounding in business history. And that's not all. Today's clients expect you to understand their business and their industry. So begin thinking of industries and areas in which you might want to specialize.

3. Learn—and focus on—how you communicate. Work on your writing. Polish your speaking and presentation skills. Your future isn't just about numbers. It's about words, and about the trust you are able to build with clients and colleagues. Especially in successfully navigating the complex nuances of a global environment.

4. Finally, look for mentors. I would not be where I am if I had not found and listened to my own mentors. Find a workplace mentor. And don't forget to return the favor. We must never lose sight of the apprenticeship traditions of our profession. Especially in rendering tomorrow's judgments.

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No doubt about it: You are all standing at the frontier of a new era in our profession. In fact, it reminds me of one of our greatest explorers.

I'm thinking of Meriwether Lewis of the Lewis & Clark expedition, the first Americans—short of Native Americans—to cross the American interior to the Pacific. In the U.S. in 1803, this was like crossing the dark side of the moon.

It was President Thomas Jefferson who sent them. And when he did, he wanted to be very sure of the person who would lead that bold party—that he had a scientific mind, fine principles, and a close grip on reality. And so—if you can believe it—for a while Meriwether Lewis camped out at the White House, in the unfinished East Room in a wood and canvas shelter, him and his hunting dogs.

Imagine that, living at the White House while studying science side by side with the President. Studying so Lewis could return with the samples, specimens and maps that Jefferson wanted—in short, the most complete picture of a new reality.

Like Lewis, you are among the leading elements of a party charged with bringing back comprehensive and objective reports of the future. It will be an adventure and a grand journey. And in that noble pursuit, I wish you well.