Looking forward to the past

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Abstract

The paper considers whether financial reports of the past can be based exclusively on measurements of past events or whether imagining future events is a necessary condition for such measurements. Using an idealised notion of a factual account of each event completed at the moment at which the event occurs, the analysis brackets out arguments about the incomplete or constructivist character of accounting representations. Notwithstanding the assumption of immaculate perception, the paper demonstrates that accounts of the past require unexpungible assumptions about hypothetical future events. Retrospection requires anticipation. Difficulties which commitment to anticipation-free financial reporting generates is illustrated in a discussion of three discourses about accounting. A description of financial reporting time which goes beyond a mere chronological characterisation is outlined.

This paper considers the temporal properties of financial reports which seek to ‘tell it as it was’ (hereafter, ex post accounting). Specifically it establishes and explores an apparent paradox: whilst such reports seek to make true statements about the past, they cannot do so without anticipating the future. The anticipations which it will be argued are necessary to describe the past should not be confused with the increasing inclusion of ex ante statements (e.g. profit forecasts) in documents such as ‘annual report and accounts’. These are attempts to predict (strongly or weakly) future conditions, for example, that next year’s profits will/might be a particular amount. The class of anticipations considered in this paper are those which are necessary in order to make ex post statements about the past — such as that last year’s profit was a particular amount.

The necessity of imagining the future in order to describe the past only appears paradoxical within a particular notion of time. This paper describes that idea of time, illustrates its influence on various depictions of financial reporting; demonstrates its insufficiency for understanding the practice of financial reporting; explores the regulatory tensions it generates; and provides an outline of a description of time which better characterises the task of financial reporting.

The idea that reports about past periods can be constructed without anticipating future events

1 We are sometimes more certain about the future than the past. I am, for example, far more certain what my second-hand car’s top speed will be when I drive it tomorrow than I am about how it was serviced by its previous owner

2 Criticism of the adequacy of ex post corporate performance data has been voiced for many decades, and may have grown. But in parallel demands for measurements of past performances have also expanded (Power, 1994) and there is no evidence that national governments and other regulatory bodies plan to abandon requirements for the periodic production of such data for multiple purposes including calculation of tax liability.
surfaces in many contexts, for example, in some of the ideals of regulatory bodies; in particular versions of ‘income theory’; and in certain judicial assertions. The Statement of Principles of Financial Reporting of the [UK] Accounting Standards Board (ASB), for example, insists that: “[f]inancial statements attempt to capture in financial terms the effects on the entity of events occurring up to a certain date; they do not anticipate future events (Accounting Standards Board, ASB, 1995, para. 4.12).”

There is significant accounting and economic literature which discretely distinguishes between accounting income and economic income on such a basis (cf. Alexander, 1977 [1948]; Bartin, 1974; Besanko, Dranove & Shanley, 1996; Hansen, 1962; Mitchell, 1995 [1967]). In that literature ‘accounting income’ is defined as solely measuring “events that have actually occurred in the past” (Bartin) whilst ‘economic income’ is understood as assessments of “potentialities” (Boulding, 1977 in Baxter & Davidson, 1997), as “expectations of future income and [which] refers to transactions that have not occurred” (Bartin). The metaphorical comparison of income with a river, or a stream, appears to be significant. According to Canning, for example, accounting income is measured “as it comes ‘down-stream’ past a defined point (the reporting date), whereas [economic income is an attempt] to trace [sic] the possible flow of income from that point” (in Lee 1985, p.49). The UK’s Court of Appeal has declared that: “[a] statement that a fact exist now, or that it existed in the past, is either true or false at the time when the statement was made” (White, 1985:114).

The idea that past conditions can be described without recourse to anticipations assumes the descriptive adequacy of the ‘chronological’ or ‘ordinary’ notion of time. In that conceptualization time is conceived of as a succession of discrete time periods. The future becomes the present, which becomes the closed, the unalterable, past. An event recedes into the past at the rate at which time flows getting buried deeper and deeper in the past. This constantly increasing recession away from the present is the only change to the event: apart from which it is impervious to modification (Ricoeur, 1984 p.145). We seem to witness this chronological conception of time as a unidirectional flow every moment of our lives and describe it in our everyday language with words like last year, yesterday, earlier today, and so on. The dating of financial reports either ‘for’ a specified past period between two past dates, or ‘as at’ a specified past date, suggests that such reports of that past are pure retrospection — that they only include descriptions of past events. However, the discussion below demonstrates and considers why accounting descriptions of the past must transcend such simple seriality.

Let us consider the premise that reports of the past are based only on events in the past and thus do not, cannot, require anticipation of future events. A formal statement of such a report R (assuming for clarity just two events one $E_1$ which occurs at or before the date of the description $D_1$ and a second, $E_2$, which occurs after the date of the description) is:

A temporally ordered set of descriptions $<D_1 \ldots D_n>$ such that whenever event $E_1$, itself a member of the set $<E_1 \ldots E_n>$ occurs, which satisfies the truth conditions of $D_1$, does so never later than the inscription of $D_1$ in $R$. So if $D_1$ describes $E_1$, and $E_2$ occurs later than $E_1$, $D_1$ cannot rely on $E_2$ to describe $E_1$.

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3 Unless otherwise stated emphasis in quotations are those of this author and not in the original.

4 A position it does not consistently hold to either in the Statement or in the ASB’s financial reporting standards.
In this conception, reports, such as financial reports, are constructed only from actual events and not also from possible future events. Reported events may be chronologically future to other events also reported, but they are all past at the time of the end of the period reported on. Let us call that notion of financial reporting: closed ex post accounting. Such reports may be minimally characterized as seeking to make true statements about the past. What I now want to demonstrate is that the construction of financial reports of the past necessarily includes imagining: some form of anticipation or projection, of a future, that is, events or conditions which have not occurred by the time of the report. Let us call such accounting open ex post accounting. A formal statement of this position is that event $E_2$ (which has not occurred at the time of $E_1$) is a necessary condition for a description of $E_1$, (made at or after the time of $E_1$, but before the time of $E_2$). A distinction is drawn between an ontological sense of the past and how we can picture it, how we can produce accounts of it, and how these might alter. In summary, the argument is that the accounting task of describing the past cannot be accomplished only by considering that past. Financial reports make essential reference to events later than the events they are about.

1. Picturing the past

What is wrong with a description of time in ‘financial reporting’ which represents it simply as a linear succession of discrete time periods that are now past? The possibility that a financial report can and merely does this, might seem to be facilitated by a particular feature of accounting in entities. The production of financial reports does not, unlike most historiography, rely on traces: memories, archives, monuments, ruins (Lowenthal, 1985), but rather, has available, the data from contemporaneous record-keeping designed to measure events and conditions using predetermined methods (Ijiri, 1975). For historians, their data are usually what remains after periodic culling of material produced for other purposes to which later access may continue to be debarred or restricted. Financial reports, in contrast, are produced, and audited, by those with largely unrestricted access to data which have been gathered and processed through accounting systems designed to provide such accounts.

But the existence of contemporaneous record keeping does not mean that financial reports are pure descriptions of past events. There is a significant literature which has demonstrated that financial reports are constructed under a particular type of description. Arguments in the literature supporting this view have ranged along a continuum. At one end there are theories which stop just short of endorsing a correspondence notion of historical truth by acknowledging that an account can never be a total or ‘comprehensive’ account of the past (cf. FASB, 1980; Morgan, 1988) — because of unavoidable errors, limitations in measurement techniques, fraud, the over-complexity of reality, or whatever. An account of $x$ is not $x$, and it only can be an account of $x$ by leaving out things about $x$. At the other end, as it were, are those depictions of financial reporting which have been reliant on various ‘linguistic-turn’ notions of no access to the world apart from our ways of thinking and talking about it (cf. Boland, 1989; Hines, 1988; Hopwood 1987; McSweeney, 1997). Accounts, these commentators commonly argue with varying degrees of intensity, are relative to particular theories. There is no presuppositionless seeing. Because only partial or theory-laden

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7 A distinction is not made here between different kinds of imaging future events or conditions such as: projecting, anticipating, forecasting, expecting, intending. These are not necessarily predictions, but in common they are ‘descriptions’ of what has not yet and might not occur. Some accounting calculations require quite specific estimates of future conditions whilst others merely need a broad assumption that certain conditions or events will happen in the future.

8 This caricature of historiography is used here to reinforce the notion of financial reporting as a pure reflection of a closed past — a characterisation that is later critiqued. In some respects the most valuable traces are those which were not intended for our later information. They are what Marc Bloch called ‘witnesses in spite of themselves’ (Bloch, 1953).
descriptions can be made, potentially there are indefinitely many contemporary accounts and later revisions. However, in order to focus on the temporal characteristics of financial reporting, these representational criticisms are bracketed out. The argument is that there is a difference between events-as-reportable/recordable/wittnesable and events-as-actuality not merely because of the incompleteness or constructivist character of descriptions of the past, but because some events — essential for such descriptions — are imaginary in the sense that they are anticipated. Anticipations of the future make possible a report of the past. For financial reports of the past not everything necessary is, or has been, present.

To restrict the analysis to the temporal structures of financial reporting we use the heuristic device of the Idealised Financial Report, and, relatively an Idealised Financial Reporter who is theorized as having, as it were, immaculate perception. Thus we are deliberately assuming away the representational limitations which the partial knowledge and the constructivist literatures have described. It does not matter whether the Idealised Financial Reporter is conceived of as a person, a system, or a machine. What matters is the assumed capability to know and record everything as it happens, to “have the gift of instantaneous transcription” (Danto, 1985). But the ability to anticipate is cognitively forbidden. If the idea of chronological time were sufficient for financial reporting then this limitation would be irrelevant. In contrast, that constraint alone, I want to argue, is sufficient to prevent the construction of financial reports because there is a class of descriptions of financial reporting events which cannot be witnessed, even with the power of immaculate perception. If a description of $E_1$ requires reference to $E_2$ before $E_2$ is anticipated to occur, the Idealised Financial Reporter cannot give the description $E_1$, and thus financial reports cannot be closed ex post accounts.

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9 The idea of an incomplete account may presuppose: that it is impossible to know the totality; or that an account involves selection and exclusion.

2. Critique of the idea of closed ex post accounts

The ineliminable temporally open property of accounting descriptions of the past is illustrated by considering its role at three different levels, as it were, in financial reports: general principles, definitions, and specific calculations.

2.1. Level 1 — principles

A presupposition that an entity is a “going concern” (Accounting Standards Committee, ASC, 1971; Sterling, 1968; Storey, 1959; Van Seventer, 1969) is one of a number of “broad basic assumptions” (or “principles” or “postulates” or “concepts”) that underlie the periodic [historic] financial accounts” (ASC, 1971). It is defined in [UK] Statements of Standard Accounting Practice (SSAP) Number 2 as the “basic assumption” that:

...the enterprise will continue in operational existence for the foreseeable future. This means in particular that the profit and loss account and balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operations (ASC, 1971 para. 14.a).

The dependency of financial reports on this “concept” is, SSAP 2 states, “not necessarily self-evident from an examination of accounts, but [it has] such general acceptance that [it calls] for no explanation in published accounts and [its] observation is presumed unless stated otherwise” (ASC, 1971, para. 2).

Auditors when forming their opinion on historic accounts must consider “the entity’s ability to continue as a going concern” (American Institute of Certified Public Accountants, AICPA, 1992). Guidance given to auditors suggests that in order to access the appropriateness of this assumption in the historic accounts they should consider, amongst other matters: “the systems for identifying future risks [and the]...existence/quality of budgets or forecasts.” (Chidgey & Mitchell, 1995, p. 151). The Idealised Financial Reporter, debarred by definition from anticipating the future, cannot
assume that the entity reported on is, or is not, a going concern.

Similarly, a concept of “prudence” the principle that: “profits are not anticipated, but are recognised by inclusion in the profit and loss account only when realised” (ASC, 1971, para. 14d) requires anticipations. “Realised” [past tense] means, ASC states, that the recognised profit [or revenue] is: “in the form of cash or of other assets the ultimate cash realisation of which can be assessed with reasonable certainty; provision is made for all known liabilities (expenses and losses) whether the amount is known with certainty or is a best estimate in the light of the information available” (ASC, 1971, para. 14d). The non-anticipation of profit requires anticipation.10

2.2. Level 2 — definitions

The definitions of ‘assets’ and ‘liabilities’ which are central to the construction of financial reports are now examined. These vary at the margin over time and geography, but it seems that they all treat expectations of what the future will/might be as an essential characteristic (cf. ASB, 1995; Financial Accounting Standards Board, FASB, 1985; Schroeder & Clark, 1995). The [US] Financial Accounting Standards Board (FASB), for example, in its *Statement of Financial Accounting Concepts Number 6*, states that an essential characteristic of an asset is that it:

...embodies a probable future benefit that involves a capacity, singly or in combination with another assets, to contribute directly or indirectly to future net cash inflows (FASB, 1985, para. 26).

The International Accounting Standards Committee describes an asset as:

a resource controlled by the enterprise as a result of a past event and from which future economic benefits are expected to flow to the enterprise (in Johnson, 1994, p. 18).

The legitimate treatment of something as an asset is thus said to depend on assumptions about future events. Conversely, anticipation is also required in defining something as not an asset: “Expenditure which does not result in access to future economic benefits does not constitute an asset” (ASB, 1995, para. 3.15). A sense of time in which the present (or past) alone can be recorded by an *Idealised Financial Reporter* is clearly inadequate here. Nothing can be treated as an asset unless future (post-time-of-description) benefits are anticipated from it. What might superficially appear to be a mere label, a referring expression, a noun, such as ‘Long-lived Assets’, is a concealed future orientated sentence (Prior, 1993).11 Implicit around the ‘label’ long-lived assets is that at a particular date, the entity had long-lived assets [explicit] which [consistent with the definition of assets] had future benefit-generating capability which were anticipated to be long-term.

The use of particular methods of valuation such as ‘replacement cost’, ‘realisable value’, or ‘net present value’ adds another level of anticipation to the valuation of an asset as they require additional, more specific, estimations of future events (Casson & Napier, 1997). For example, inventories are almost universally required by regulators to be valued at future market prices (“net realisable value”) if that anticipated value is less than the estimated cost of the inventories (ASC 1988; International Accounting Standards Committee, IASC, 1993a). Even if ‘historic’ or ‘original’ cost only is used as the valuation base, an expectation about the generation of future benefits remains a necessary ‘recognition’ condition, a test of their “authenticity” (ASB, 1997a). In some circumstances that anticipation may be quantified for financial reporting purposes. As ASB states:

...sometimes assets are measured not by reference to an observable [or estimated] price in a transaction or market but by reference to [anticipated] future cash flows arising from the items. For example, in the calculation of

10 For a discussion of the notion of ‘realised profit’ see Carsberg and Noke (1989).

11 “Many expressions which look like nouns i.e. names of objects, are”, Arthur Prior argues, “not really nouns at all but concealed verbs” (Prior, 1993, p. 39).
revised values of impaired assets, value in use is measured on the basis of [anticipated] future cash flows (ASB, 1997b).

Definitions of liabilities also suppose expectations of future outflows of benefits. An example of a typical liability definition is: “a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying future benefits” (Davies et al., 1994 p. 645). According to a study of “future events” by a working party of board members and senior staff from five accounting regulatory bodies:12

Future events are implicitly embodied not only in the assets definitions (future economic benefits) but also in the liabilities definitions (transferring or sacrificing economic benefits in the future). And, because all other elements of financial statements (such as revenues, expenses, gains, losses etc.) are defined in terms of changes in assets and liabilities, it follows that future events are inherent in those definitions as well. Thus, there is a clear link between future events and the definitions of elements of financial statements (Johnson, 1994, p. 2) (emphasis in original).

A necessary condition for an expenditure to be treated as an asset is — as the asset definition above indicates — that it is anticipated that it will generate benefits beyond the time period reported on. That anticipation is, however, not sufficient — additional anticipations are required. Expenditures which may be potentially judged to create future benefit may nonetheless be treated in financial reports as an ex post expense. An example is non-capital expenditure on pure research (FASB, 1974; ASC, 1989; IASC, 1993b). To treat an expenditure as an expense (and not an asset) requires either an assumption that it will in the future generate no benefits, that all the benefits (if any) it contributed have been achieved, or, that the possibility of future benefits is too improbable to justify its recognition as an asset. The Idealised Financial Reporter could not distinguish between assets and expenses as both categories require anticipation as to how the future might be.

An examination of accounting calculation regulations reveals further evidence that financial reporting must anticipate future events. The example considered here is ‘depreciation’ expense.

2.3. Level 3 — calculations

Unless it is assumed that an asset has a permanent life (itself an assumption about the future), its valuation in the balance sheet must be periodically reduced. The estimated amount of ‘depreciation’ (or ‘amortization’) is treated as an expense which is charged against the relevant period’s revenue in the profit and loss (income) statement. “Depreciation” is defined by the ASB13 as:

[T]he measure of the wearing out, consumption or other reduction in the [future] useful economic life of a fixed asset, whether rising from use, effluxion of time or obsolescence through technological or market changes (ASC, 1987, para. 3).

A variety of depreciation methods acceptable to regulatory bodies are available. To calculate the depreciation charge for past periods, each method requires (amongst other matters) an anticipation of the asset’s “expected useful economic life” (ASC, 1987) (Davies et al., 1994, p. 539). An example: a long-lived asset is purchased in 1997 for £100m; any residual value is not estimated or is ignored, and the method chosen is ‘straight-line’. The calculation of the 1997 (and each subsequent period’s) depreciation expense cannot be made without anticipating when, in the future, the asset will cease to generate benefits for the current entity. Thus, in this example, if in 1997 the end of

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12 The Australian Accounting Standards Board, the Canadian Accounting Standards Board, the International Accounting Standards Committee, the United Kingdom Accounting Standards Board, and the United States Financial Accounting Standards Board.

13 The Accounting Standards Committee (ASC) was replaced by the Accounting Standards Board (ASB) on 1 August 1990. The ASB adopted the 22 ASC SSAPs extant at that date.
the asset’s estimated future economic life is 10 years hence, in the year 2006 the historic depreciation charge for 1997 will be calculated as £10m (£100m divided by 10 years). If, however, the estimated future economic life is assumed to terminate earlier, say, in 2001, the 1997 depreciation charge would be measured as £20m.

The “useful economic life” is the assumed future period over which the present owner will benefit; not the total potential physical life of the asset so that the duration of ownership must be estimated.14 What ultimately becomes the actual useful economic life of the asset is contingent on a range of unpredictable technological, market, legal, financial, physical and ownership events.

Three levels of financial reporting were considered above. Examples from each: the fundamental assumption of a ‘going [or not] concern’ and prudence; definitions of assets and liabilities; and the principal calculations required to determine a depreciation charge revealed, contrary to the temporally closed characterisation of an Idealised Financial Report, their unavoidable reliance on anticipation of the future. The paper considers further the sufficiency/insufficiency of the ordinary notion of time for the construction of financial reports by considering some temporal properties of adjustments to financial reports.

Revisions to accounts of past periods because of events obtained in a subsequent time are a chronic characteristic of financial reporting (cf. ASC, 1986; FASB, 1977; IASC, 1978, 1993c). Every significant accounting regulatory body has issued rules and guidance concerning them. The FASB, for instance, refers to “the normal, recurring corrections and adjustments which are the natural result of the use of estimates inherent in the accounting process” (1977). These regulations reveal a temporal characteristic of actual historic accounts: for some accounting events at least a final record of these events cannot be contemporaneously made. But if such adjustments are exclusively the results of recording imperfections (fraud, inaccuracy, incompleteness) the requirement to make them does not contradict the idea that financial reports rely wholly on the idea of ordinary time. Such errors would not appear in accounts produced by the Idealised Financial Reporter as perfect records of past events would have been made at the time of the event(s) described. The appropriate test of the sufficiency of the ordinary notion of time is whether any subsequent adjustments could be made to an Idealised Financial Report.

For a number of reasons, not addressed here, financial reporting regulatory bodies seek to ‘close the past’ by constraining retroactive adjustments.15 Nonetheless, it is possible through an examination of regulations covering permitted adjustments, to identify acknowledgements of the impact of future events (anticipated or unanticipated) on descriptions of the past. To do so the paper considers the retroactive financial accounting revision: post-balance sheet adjustments.

In the time period after that reported on and the completion and approval of the financial reports, the entity’s activities continue, significant events occur, new information becomes available. These may alter beliefs about what happened during the period reported on and thus the adequacy of the financial report on that period. Financial reporting regulations distinguish between two types of subsequent ‘events’: those which provide additional evidence relating to conditions existing during the reported period and which, if significant, must result in adjustments to financial reports and those which provide evidence of conditions which did not exist during the period reported on and “consequently do not result in changes in amounts” (ASC, 1980) in the financial reports of that period (cf. AICPA, 1972; IASC, 1978).

If an accurate description of the past does not require anticipation of future events, the Idealised Financial Reporter cannot be mistaken and thus post-balance sheet adjustments in actual financial reports would only result from imperfect knowl-

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14 The actual physical life of an asset could be shorter than its anticipated economic life as it could cease to exist for unpredictable physical reasons, no less than for economic reasons.

15 Regulatory closure is not unique to financial reporting. In most legal regimes, for example, there is a time limit after which a death following an injury cannot be treated as a murder (Clarkson & Keating, 1994).
edge about the past/present and not because of information about (post-balance sheet date) conditions. The conditions which required the change in accounts would have existed during the period accounted for although the new knowledge of them would only have become available after the accounting period. The ideals of regulation of retro-active adjustments to financial reports (‘post-balance sheet adjustments’) presume the chronological notion of time and, in principle, restrict permitted post-balance sheet adjustments to subsequent discoveries about pre-balance sheet events but this purity is not maintained in the enacted or detailed regulations. The discrete division between conditions which existed pre and post balance sheet date is not sustained. This failure, a consequence of the insufficiency of the chronological notion of time is illustrated below through an examination below of the examples in SSAP 17 (ASC, 1980) of adjusting and non-adjusting events. The ‘acid test’ of the ordinary notion of time is whether any of the adjustments required by SSAP 17 would be made to Idealised Financial Reports If any could they be the consequence of events which occurred after the period accounted for and are not mere illuminations of past events.

Only one of the ten illustrative examples in SSAP 17 of required adjustments passes the test, namely:

**Discoveries**: the discovery of errors or frauds which show that the financial statements were incorrect.

The remaining nine are either clear failures or are contestable. The original financial report of them “refers to at least two time-separated events though they only describe (are only about) the earliest event to which they refer” (Danto, 1985). The adjustment becomes necessary because the second event is different from that at first anticipated. Examples of such events, counter-factuals to the descriptive adequacy of the ordinary notion of time, which occur in a time later than that accounted for are:

**Fixed Assets**: The subsequent determination of the purchase price or of the proceeds of the sale of assets purchased or sold before the year end (ASC, 1980).

**Claim**: Amounts received or receivable in respect of insurance claims which were in the course of negotiation at the balance sheet date (ASC, 1980).

**Stocks & Work in Progress**: The receipt of proceeds of sales after the balance sheet date or other evidence concerning the net realisable value of stocks (ASC, 1980).

The event which triggers this adjustment is the sale of inventory after the balance sheet date at a price which showed that the earlier estimate of realisable value was incorrect. And,

**Debtors**: The renegotiation of amounts owing by debtors, or the insolvency of debtors (ASC, 1980).

The relevant event again occurs after the balance sheet date. A trade debtor goes into liquidation or receivership after the balance sheet date showing that the estimated value of good debts at that date was incorrect. And,

**Taxation**: The receipt of information regarding rates of taxation (ASC, 1980).

The relevant event is post-balance sheet: a change in taxation rates made in the period after the period accounted for but which is retrospectively applicable to periods before the balance sheet date.

Some of the other post-balance sheet adjustment examples in SSAP 17 treat the events as the termination of a process which commences at (or before) the balance sheet date but which does not terminate until after that time period, thus requiring a fallible imaginary conclusion in order to produce the financial reports. An example is:

**Claims**: Amounts received or receivable in respect of insurance claims which were in the course of negotiation at the balance sheet date (ASC, 1980).

Such negotiations commence on, or before, the balance sheet date but do not finish until after that date.

**Fixed Assets**: The subsequent determination of the purchase price or of the proceeds of the sale of assets purchased or sold before the year end (ASC, 1980).

It is difficult to conceive of instances in which such events wholly occurred at, or before, the balance...
sheet date but an estimate only is available of the price or proceeds for preparation of the original financial reports. Much more commonly, such adjustments occur because a post-balance sheet event was a necessary condition of the sale and either did not take place or the final price or proceeds was different from that originally estimated. For example, the conditional sale or purchase of some fixed assets might require shareholder approval at an extraordinary meeting held after the balance sheet date.

We have seen that some, indeed most, of SSAP 17’s examples of circumstances which require changes to financial reports do not merely “provide additional evidence relating to conditions existing at the balance sheet date” (ASC, 1980, para. 7), but are, or could be, events which occurred after the balance sheet date. Each of these events would have happened in whole or in part after the first description of the events. Up to and including the balance sheet date the Idealised Financial Reporter could not have known or recorded these events and yet when they occur, they alter the description of the past period.

2.4. Non-adjusting items

We now look at some of SSAP 17’s examples of “non-adjusting items” defined as: “events which arise after the balance sheet date and concern conditions which did not exist at the time” (ASC, 1980). Because they are regarded as wholly post-balance sheet date events, no adjustment is usually made to the original accounts, but disclosure of detail may be required in notes.

The assertion in SSAP 17 that these “non-adjusting” events occurred after the balance sheet date is not disputed here. What is relevant is whether anticipation of any of these events would have been necessary in order to produce a financial report. If so, and the event fails to occur either at all or on the scale anticipated, the accounts are in principle retrospectively false, regardless of what regulatory prohibitions there may be on retrospectively adjusting the original financial reports.

Anticipation of some of the examples of “non-adjusting events” in SSAP 17 would not have been required when making the financial reports. They are thus not counter-factuals of the adequacy of the ordinary notion of time. However, there are examples of such events in SSAP 17. Two are considered below. In principle, the first could alter the size of prior period’s depreciation calculations, the second could undermine a basic assumption of the original financial reports that the entity was a ‘going concern’.

The first example of a “non-adjusting event” taken from SSAP 17 is “sales of fixed assets [in the post-balance sheet period].” If a large loss or profit results from the sale of a fixed asset, this suggests that the depreciation charged in past periods was either inadequate or excessive as the estimated “residual value” used to calculate each prior period’s depreciation amount would have either been greater or less than the actual residual value (the sale price) (Davies et al., 1994). Although adjustments to the financial reports of prior periods are unlikely to be made, because of regulatory restrictions, earlier depreciation charges for preceding periods would have been calculated on the basis of an inaccurate anticipation of the future. This process is illustrated by a numerical example:

A machine was bought at the beginning of 1993 for 12 million Danish Kroner. Its estimated useful life was 4 years and its resale value as 4 million Danish Kroner. The depreciation method used was straight-line. Assume that the estimated useful life was correct, but that the resale value at the beginning of 1997 was only 1 million. In each of the years: 1993, 1994, 1995, and 1996 a depreciation expense of 2 million Danish Kroner would have charged against revenue. At the beginning of 1997 the Net Book Value of the asset would have been recorded as 4 million Danish Kroner but the asset was sold for only 1 million Danish Kroner. To conform with regulatory requirements a loss of 3 million Danish

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16 Save very unusual delays in relaying the information.

17 An adjustment to the accounts is also required by the standard if some events occurred after the balance sheet date indicate that the prior assumption that the whole or part of the entity is a “going concern” (discussed above) is no longer appropriate (ASC, 1980).

18 Discussed above.
Kroner would be recorded in 1997 accounts. However, had the original (1993) forecast of resale value been correct the 1993 to 1996 inclusive annual depreciation charge on that machine would have been 2.75 million Danish Kroner and not 2 million Danish Kroner and no loss would be reported in 1997.

Regardless of whether, or not, the disposing entity chooses to, or is debarred from, retroactively adjusting the depreciation charge for each of those four years, the estimated annual depreciation required a forecast of an event (in this instance in 1997). The forecast was inaccurate and thus too was the past depreciation charge.\textsuperscript{19} When the asset is sold, it is possible to retrospectively calculate and arrive at what is arguably a 'correct' total depreciation figure.

The second non-adjusting post-balance sheet event example from SSAP 17 which nonetheless has, in principle, retrospective effects on the accuracy of prior calculations is: “Closing a significant part of the trading activities if this was not anticipated at the year end”. This conflicts with the “basic assumption” in the entity’s prior period financial reports that it would “continue [to be a] going concern” (ASC, 1971). That assumption is defined in SSAP 2 (ASC, 1971, para. 14.a) as: the expectation that “the enterprise will continue in operational existence for the foreseeable future. This means in particular that the profit and loss account and balance sheet assume no intention or necessity to liquidate or curtail significantly the scale of operations.” Financial reports have to be built on the assumption that an entity is, or alternatively is not, a going concern. If later what was assumed to be true proves incorrect, the account of the past period will be incorrect.

The formal description of temporal openness of ex post accounting given above was that: event $E_2$ (which has not occurred at the time of $E_1$) is a necessary condition for a description of $E_1$, (made at or after the time of $E_1$, but before the time of $E_2$) and for us, in the time of $E_2$, to be able to check that description of $E_1$. The analysis in this section of ‘adjusting’ and ‘non-adjusting examples’ from SSAP 17 further illustrated the significance for financial reporting of events future to the time reported on — these are examples of the $E_2$s in the formal description. Idealised Financial Reports are not plausible.

3. Cash flow accounting

The financial reporting examples discussed above each illustrated a necessary reliance on anticipations of events future to the time period being described. But it might be argued that anticipation-dependence is not a general-property of financial reports as they often include cash flow [reports] statements.

In a note of dissent to SFAC Number 95 Statement of Cash Flows (FASB, 1987) FASB member Raymond C. Lauver asserted that a: “statement of cash flows involves no issues of recognition, measurement, or estimation; by definition it includes only the effects of identifiable, unquestioned transactions”. That argument is contestable on the basis that financial reports are necessarily incomplete or constructed representations (cf. McSweeny, 1997; Roberts, 1995). But focusing exclusively on the temporal characteristics of financial reports it is argued here, contra Lauver, that statements of cash flows also require anticipations of events later than the period to which they refer. The same test which the profit and loss account and balance sheet failed is now applied to cash flow statements.

It is, of course, possible to claim that all descriptions, including cash flow statements, are temporally open in the sense that subsequent events may ‘enrich’ later understandings of them. Thus, for example, we might now say that the building of the pyramids of Egypt inspired the design of the sand-castles we saw on the beach last summer. But that future event (sand castle building) is not of the type of future event which it has been argued is necessary in constructing financial reports. A post-description event is not necessarily an event whose anticipation is required in order to describe the past — even if we assume some causal influence. If we accept the causal link between the ancient pyramids and contemporary sand-castle

\textsuperscript{19} Even if the forecast estimated useful life had been correct, its anticipation would have been necessary to calculate the annual depreciation charge in the years prior to the sale of the machine.
building our knowledge of the past has been enriched but anticipation of sand-castle building is not, and was not, necessary to describe the pyramids. Similarly, it might later be said that a particular cash outflow, say for capital expenditure, proved to be very successful. But whilst that later knowledge enhances our knowledge of the past cash flow, it is not essential for the construction of a cash flow statement for the period in which the cash outflow occurred. As elsewhere in the paper, the pertinent type of anticipated future events are those necessary in order to make [financial] statements about the past. Are such anticipations essential in the construction of cash flow statements?20

Sometimes cash flow statements are produced according to the so-called ‘indirect method’ which focuses on, or at least includes, a reconciliation between operating profit and operating cash flow. Revenue and expense items not affecting cash, for example: increase in stocks; increase in debtors; depreciation, are added or deducted to arrive at “net cash provided by operating activities” (ASB, 1996). The inherent role of anticipation in some of those items, for example depreciation, was described above. However, let us consider only cash flow statements based on the ‘direct method’ which includes cash received and paid as opposed to converting accrual-basis income to cash flow information.

The definitional boundaries of what constitutes ‘cash’ varies. In addition to “cash in hand” (ASB, 1996) or “currency on hand” (FASB, 1987), its definition usually includes “deposits repayable on demand” (ASB, 1996) and sometimes short-term, highly liquid investments such as Treasury bills, commercial paper, and money market funds (FASB, 1987; IASC, 1992; ASB, 1996). Even “cash in hand” will have some temporal uncertainty as it likely to include various non-currency-note items — cheques and so forth — whose conversion may not be guaranteed. At the end of the period reported on, some of these items as well as some of the currency-notes may be in a denomination other than in the reporting currency. Because of exchange rate changes, the amount at which they are translated for the cash flow statement are unlikely to be the same as the converted or settled amount: the amount actually received in the post-statement period.

In order to make the strongest possible case against the idea of anticipatory necessity let us assume that the entity against which we want to test the Idealised Financial Reporter’s ability to produce a cash flow statement has the following characteristics. It has no transactions that do not result in cash flows;21 payments and receipts for those transactions are exclusively in currency-notes of the reporting currency;22 there are no restrictions preventing the transfer of cash from one part of the entity to another; and it has no deposits or cash equivalents (ASB, 1996).23

Within these restricted assumptions an Idealised Financial Reporter could record the amount and date of cash paid (and its payee/destination) and cash received (and its payor/source). This would be a chronological list, a sequential record, of cash payments and receipts, in other words: a cash chronicle. But a cash flow statement is not a mere chronicle it classifies the cash payments and receipts of a particular period into categories of source and use. I want to argue that the classification of cash flows is not confinable/definable within the reported on chronological time period. Central to cash flow classification is anticipation. The construction of cash flow statements requires “configurational acts” (Ricoeur, 1988) inconceivable without anticipation. Let us explore this argument.

The ASB specifies eight main cash flow configurations or classificatory headings: “cash receipts and payments from operating activities”; “returns on investment and servicing of finance”; “taxation; capital expenditure and financial investment”; “acquisitions and disposals”; “equity dividends paid”; “management of liquid resources”; “financing” (ASB, 1996). IASC and FASB require only three: “operating”; “investing”; and

20 As in the discussion of accrual based financial reports above, the objective here is not to provide a complete description of every type of anticipation necessary to produce cash flow statements. All that is necessary is to demonstrate that anticipations are required.

21 Examples of non-cash transactions are: conversion of debt to equity and acquisition of assets by assuming liabilities.

22 Of course, even bank notes represent ‘promises to pay’, but as the aim is to argue against the strong claim that cash flow statements do not require anticipations, this argument, trivial, in this context is ignored.

23 Further restrictions are introduced later below.
“financing” (IASC, 1992; FASB, 1987). Cash-flow classifications are mutually exclusive in the sense that a cash flow can only be included in one category. In what way are cash flow classifications anticipation-dependant?

Cash flow statements conforming with regulatory requirements sub-categorize the main classifications. Some of these sub-divisions overtly refer to post-reporting period events, for example: “debt due within a year” (ASB, 1996, p. 337). Clearly an Idealised Financial Reporter cannot allocate cash flows to such sub-categories. But what if sub-classification was defined as a non-essential characteristic of cash flow statements; and the main classifications were limited to the minimal triple classification: ‘operating’ ‘investing’ and ‘financing’ cash flows? I want to argue that even with these further concessions, an Idealised Financial Reporter could not complete a cash flow statement. To illustrate that claim I will consider two features of cash flow statements: composite payments (or receipts) and the distinctions between the three standard classifications.

Composites: Let us take the example of composite cash outflows associated with “finance” (ASB, 1984) or “capital” (FASB, 1976a) leases. These are composites of (re)payments of: (i) the principal — classifiable as financing cash flow, and of (ii) the interest or financing charges — classifiable as “operating” cash flow. The undifferentiated cash flow could be recorded by an Idealised Financial Reporter as a particular amount paid on a specific day or during a particular period, to a named payee, but s/he could not disaggregate the two components, or “aspects” (FASB, 1987), and hence could not allocate each to a separate classifications. Decomposing such payments in order to classify requires a series of projections including: the duration of the lease; the timing and volume of future cash flows; future residual value; and the extent of future cancellability of the agreement. Take a very simple example:

An asset is leased on a non-cancellable contract with a primary term of five years from the beginning of a financial reporting year. The rental is fixed in advance as a uniform £26,000 per annum payable in advance. The fair value of the asset at the inception of the lease is deemed to be £100,000 and it is expected to have a residual value at the end of the lease of £2372 (being its anticipated tax written down value at that time) which will be passed to the lessee as a refund of rentals. In addition, the lessee is responsible for all maintenance and insurance costs.

A range of calculations impossible for an Idealised Financial Reporter — as they require anticipations — are necessary to determine the carrying value of the leased asset in the balance sheet and the periodic charges in the profit and loss account. But our concern here is only with the cash flow statement. Could an Idealised Financial Reporter decompose the annual cash payment of £26,000 into: (i) ‘financing’ (or alternatively: ‘investment’) and; (ii) ‘operational’ components? Total lease payments would amount to £130,000 [five annual £26,000]. The total finance charges would over the life of the lease be £30,000 (i.e. £130,000 - £100,000). At the end of the five year period £100,000 should have been allocated in total to financing cash flow and £30,000 in total to operational cash flow. To make the above calculations required a number of anticipations. Unable

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24 It is possible to argue for different and/or additional classifications. “There is”, as Pratt (1976, p. 383) argues, “no such number as the number of attributes that an (object) has” (in Roberts, 1995, p. 648).

25 Unlike FASB, ASB requires that the financing costs of finance leases be classified as servicing of finance and not operating cash flow.

26 Taking a ‘use’ rather than a ‘source’ perspective the (re)payment of the principle should be classified as ‘investment’ and not “financing”, but in any event that would also require splitting the cash flow into different classifications: ‘investment’ and ‘operating’ rather than ‘financing’ and ‘operational’. Interest is not necessarily classified as an ‘operational’ cash outflow. SFAC 95 states that interest capitalized as part of the cost of an asset should be classified as an investing cash flow (FASB, 1987, fn. 7).

27 Usually, but not always, the periodic payments will be identical throughout the life of the agreement.

28 The issue of future replacement cost is ignored as it is assumed that the purchase cost of an equivalent asset will remain constant during the life of the lease agreement.
to anticipate the Idealised Financial Reporter cannot make those calculations.

But an Idealised Financial Reporter’s anticipatory deficit is even greater. The total financing charge of £30,000 would also have to be calculated for/at the end of each reporting period during the 5 year period. The reported periodic amounts would vary depending on the methods used (ASB, 1997c; FASB, 1976b; IASC, 1982). For instance, based on the example above, the ‘actuarial method’ would express the annual interest cash flows for the first and second last years of the lease as £12,211 and £3,419 respectively, whilst the ‘sum of the digits method’ would represent those annual cash flows as £12,000 and £3,000 respectively.\(^\text{29}\)

Each period amount calculating method requires, amongst other things, the use of the number of years of anticipated duration of the lease — by definition, impossible for an Idealised Financial Reporter.

At the extreme, perhaps, it could be argued that the repayments of the principle and the interest charge are both financing cash outflows so that an Idealised Financial Reporter could so classify the total cash payment to the lessee. Anticipation-based calculations would not be required. But that evasive move will not work for all composites. There are many other composite cash flows whose desegregated amounts would be allocated either to the ‘investment’ or to ‘operating’ classifications (FASB, 1987). Examples are: research plus development; fixed asset maintenance plus fixed asset construction/enhancement; inventory plus fixed asset expenditures; interest payments for operational plus capital development purposes. An examination below of some of the distinctions between ‘operating’ ‘investment’ cash flows illustrates the ineliminable role of anticipations in their construction. An Idealised Financial Reporter cannot classify these, and similar, composites either as disaggregated amounts or as a composite to a single classification. To split them would require impossible anticipation. For example, a separation of a research and development cash flow into operational and investment components would require a distinction between types degrees of risk/certainty of commercial and technical anticipations. But there is a prior, or higher level, constraint. The classifications themselves are anticipation-dependant. This would debar the location of even unseparated cash flows and non-composite cash flows which are (but unknowable as such by an Idealised Financial Reporter) ‘operating’ or ‘investment’ cash flows.

Central to the distinctiveness between the classifications ‘investment’ and ‘operating’ is the assumed effect/use of cash flows in the post-reporting period. For ‘operating’ cash flows the assumption is that their use has expired (expenses) or will expire in the short-term post reporting period (e.g. inventory). Whilst cash flows classified as ‘investment’ are either those which it anticipated will have longer-term use (e.g. capital expenditures) or which in the past had such a time horizon but no longer so do (e.g. proceeds of sale of facility).\(^\text{30}\) The two classifications are distinguishable from each other on the basis of the time horizons of their constitutive anticipations. Unable to anticipate, an Idealised Financial Reporter could not even conceive of these categories.

Yet, again we see that cash flow reports/statements have to rely on anticipation of events later than the events they are about. This the Idealised Financial Reporter cannot do. Not only profit and loss accounts and balance sheets but also cash flow statements are temporally incomplete. An essential component of their descriptions of what happened is derived from anticipations of events subsequent to the reported period. A cashflow statement (like a profit and loss account and a balance sheet) is a temporally open story. A story

\(^{\text{29}}\) It is possible to argue, as FASB does (1987, fn. 6), that in the first year there may be a three-way classification split. In addition to the financing and operating components, FASB states that advance payments or other amounts paid at or near to the time of the purchase (other than directly related debt such) are investment cash outflows.

\(^{\text{30}}\) These are just some of the anticipations necessary in making a distinction between ‘investment’ and ‘operating’ cash flows. At a more general level the classification of investment depends on the future-orientated ‘going concern assumption’ (discussed above). Without that positive anticipation many, or all, of what otherwise would be classified as ‘investment cash flow’ could not be so reported.
has to be more than an enumeration of events in serial order. Events are organized into an intelligible whole. In cash flow statements that organization is achieved through the classification of events. Without anticipation, even a minimal classification of cash flow events would not be possible.

4. Discussion

The analysis above suggests that there is knowledge of the past which could not have been observed by a witness — even by an Idealised Financial Reporter with ‘immaculate perception’. Financial reports are descriptions which have as truth-conditions, events which occur later than the periods reported on. They are outcomes of what is no longer and what is not yet. Projections are essential for representation of what ‘actually happened’. Financial reports must necessarily ‘look forward to the past’.

Uniformly theorizing ‘future events’ has contributed to confusion about time. Four types of future events are distinguished. (I) The conception of future events as necessarily involved in financial reports, for example the statement that: “x was a good investment”, made before the end of the investment’s life, assumes future events i.e. future benefits, call them past describing anticipated events, is radically different than: (II) enriching future events — future events which result in an enrichment or revision of understanding of past events, for example: “x proved to be a very wise investment”, or “an actor in the 1955 movie Bedtime for Bonzo was [later] a President of the United States” — statements which could not be made at the time of the first event; (III) predicted future events which are not part of descriptions of the past, e.g. “x will be a wise investment”, and, “that actor will become the President”; and (IV) caused future events — future events which are causally linked with past events e.g. “because of x investment there was y income”, and, “that actor’s memory helped him become President”. Causes cannot be witnessed as causes.

Descriptions of events of each of the three latter types may appear in accounts and specifically in what are sometimes colloquially called ‘financial reports’, but, unlike the first type, none is a necessary condition for financial reporting in the sense of that which ‘tells it like it was’ (ex post accounting). A future event cannot be a necessary condition for a past event (reverse causality); but anticipation of a future event may be a necessary condition for a description of a past event; and if so its occurrence is a necessary condition for a correct description of that past event.

4.1. Three discourses

Does it matter? An idealised notions of either closed ex post measurements of income and capital may have useful analytical roles as a heuristic device (cf. Harcourt, 1965), but attempts to use that absolute to describe, or prescribe, accounting practice confronts insuperable problems. Here the paper describes some of the problems which the assumption of the feasibility of closed ex post accounting generates in three literatures: income theory; reformist accounting polemics; and regulatory prescriptions.

4.1.1. Income theory

The theory and measurement of income [personal, corporate, societal, and national] has attracted a voluminous literature (Whittington, 1981) which has considered a range of issues including: ambit; effects of changing value of money; and usefulness. Much of that literature focuses only on future (ex ante) income and thus has not been concerned with ex post income measurement. But the conflation of the absolute distinction between the Past and Future with the temporal characteristics of feasible descriptions of the Past is apparent in a sub-set of income theory literature which has sought to discretely distinguish between ‘accounting’ and ‘economic’ concepts of income (and capital).31 In the main, but with fine exceptions,

31 The terms ‘accounting income’ and ‘economic income’ have also been used in other senses to distinguish between: (i) theories which reject or approve of the inclusion of unrealized gains in income (Most, 1982), and (ii) theories concerned with the income of business entities and that of individuals (Mitchell, 1995 [1967]).
that literature is dichotomised. It treats each of the two categories as internally uniform and entirely distinct from each other on the basis that the former is backward-looking, it only measures the past whilst the latter is forward looking, it anticipates the future. In contrast we have seen that past income cannot be measured without anticipations. Sometimes accounting income’ is also described as “objective” (in a realist, not a consensual sense) because it just measures the past, whilst ‘economic income’ is described as “subjective” (cf. Mitchell, 1995 [1967]). From the analysis above it is clear that “objective” is an inappropriate description of income (and capital) in financial reports. The future does not exist so that its various anticipations in financial reports cannot appropriately be described as “objective”.32

A variation on the dichotomised view is that having first contrasted “accounting income” with an ‘economic income’, the practice of accounting is then pejoratively described as confused, as an impure mixture of both notions of income/capital (cf. Hansen, 1962). But as we have seen, contrasting closed ex post [aka ‘accounting income’] and ex ante [aka ‘economic income’] is spurious as the former is an illusion, an impossibility. What is treated as confused is a consequence of necessarily incorporating anticipations into the measurement of ex post income and capital. Another variation has been to contrast the notion of closed ex post accounting, sometimes patronisingly said to characterise theoretically unsophisticated “accountants”, with an idealised, and lauded, notion of ex ante income one which unrealistically assumes certainty in the identification of future net cash flows. Much of the prescriptive accounting, finance, and other literature on discounted cash flow relies on the possibility of knowing future net cash flows (and other future events). This is a utopian notion of perfect knowledge, an unimplementable idea which ironically is often asserted in the name of the practical (for a recent example see Grant, 1995). But neither notions have descriptive or prescriptive validity. Two impossibilities are contrasted. Some of that literature has explicitly appealed to John Hicks’ notions of ex post and ex ante measurements of income and capital, treating ex post (in the language of this article) as temporally closed. But, ironically, a more careful reading of Hicks’ notion of ex post would have revealed that it is temporally open, not closed. Ex post measurements of income and capital are he accurately and evocatively states: “shrouded... in the mists of futurity” (Hicks, 1942, p. 177; 1973, p. 164).

4.1.2. Creative accounting literature

The literature critiqued above by failing to recognise the role of anticipation in ex post income/capital measurements contrasts ‘accounting’ and ‘economic’ income on mistaken grounds. The second type of literature considered acknowledges the use of anticipations in financial reporting but, overly committed to the idealisation of closed ex post accounting, it fails to distinguish adequately between legitimate and illegitimate anticipations (cf. Griffiths, 1986; Jameson, 1988; Smith, 1992). It calls for the prohibition of ‘creative’ accounting (and sometimes the reform of regulatory institutions) on the grounds that whilst financial reports should, and could, contain only true information they often intentionally, although legally, include at which is untrue.33

The central flaw in this literature is not its assumption that financial reports may be deliberately ‘massaged’ or ‘distorted’ — they sometimes are (Basu, 1997; FASB, 1980 pp. 56/7) — but in assuming that non-judgement based financial reports are possible. Its critique is based on the idea of knowable absolute truth. A rigorous distinction is drawn between the imaginary and the real. On the basis of the presupposition that specific accounting methods, known to both account preparers and their critics, can produce accounts that can wholly rely on facts the literature asserts that different approaches are intentionally used to

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32 The terms “objective” and “subjective” are now passé, but the sense in which the literature uses them will be apparent.

33 A variation is the financial analysis literature which excessively claims that it is possible to adjust/re-calculate financial reports so that the effects of judgements are eliminated. White, Sondhi and Fried, for example, state that they “have designed their book to lead the financial statement user through the labyrinth of financial reporting [to make] adjustments [which will] discern substance over form” (1994:2,3).
provide accounting representations which diverge from, or conceal what is known by the preparers to be the truth (cf. Griffiths, 1986; Jameson, 1988; Smith 1992). With good faith it is assumed that uncreative accounts can be produced.

Many of the techniques described in the ‘creative accounting’ literature manifestly rely on the anticipation of future events. These include capitalisation of costs; contingent liabilities; deferred consideration; pension fund surplus; extraordinary items; pre-acquisition write-down and brand accounting (e.g. Smith, 1992). An intention to mislead, bad faith, is not a necessary condition of untrue financial statements. The same temporal openness that facilitates the intentional production of untrue accounts characterises all financial statements. All ex post reporting is unavoidably creative in the sense of requiring some imaginary. What is not present, that is that which must be anticipated, may be plausibly or implausibly, may be honestly or dishonestly, represented through anticipation, but cannot be truthfully re-presented. The ideal of closed ex post accounting may have a regulative role, but it is diversionary or unattainable when it is treated as the achievable aim of reform programs or adjustment procedures. The property of temporal closedness requires the fulfilment of conditions which simply cannot be fulfilled.

4.1.3. Regulatory bodies

Creative duality — the ineliminability of anticipations from financial reports and yet the potential for the intentional use of anticipations to mislead, is a major descriptive/prescriptive problem for financial regulatory bodies. On the one hand it wants to reduce, and ideally eliminate, opportunities for such manipulations. On the other hand specific descriptions of permitted methods of measurement cannot avoid acknowledging the need to incorporate anticipations.

In their attempts to cope with creative duality, regulatory bodies have resorted to three discursive strategies: denial; acknowledgement; and constraints. These are outlined below.

4.1.4. Denial

The ordinary notion of time privileges a particular idea of presence. That which is represented, if it is true, re-presents that which exists/exited as chronologically dated. A representation is or was ‘in the now’ but it cannot be in the future as that does not yet exist. The strategy of denial, i.e. that financial reports of the past cannot include that which has not or is not present, is most evident within documents which set out the ‘principles for’ or the ‘qualitative characteristics of’ such reports. Documents of this type are often generically described as the ‘conceptual frameworks’ (cf. FASB, 1976b; Macve, 1981; Power, 1989) of financial regulatory bodies. In the main denial is indirect, that is, the characterisations of financial reports excludes the possibility of including non-presence and thus anticipations. Amongst the qualitative characteristics of accounting information listed by the FASB is “representational faithfulness” defined as “correspondence or agreement between a measure or description and the phenomenon it purports to represent” (FASB, 1980). “Faithful representation” is also listed by ASB as a “qualitative characteristic... of the content” of financial reports. It adds that: “[i]f information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance” (1996, p.15). A report on future events published by five regulatory bodies34 states that “All events that are recognised in an entity’s financial statements for a particular period should reflect underlying events that have occurred during the period” and “it should be noted that the definitions of assets and liabilities refer to real-world assets and liabilities” (FASB, 1994 p. 2, fn. 2).

Less frequently the denial is direct or explicit. An example is the assertion in the U.K Accounting Standards Board’s Statement of Principles that “[f]inancial statements attempt to capture in financial terms the effects on the entity of events occurring up to a certain date; they do not anticipate future events” (ASB, 1995, para. 4.12). The first clause in that sentence is a correct description of the aim of ex post financial statements. The second clause is presented as a consequence of the first. But as the analysis above has demonstrated the second description does not flow from the first,

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34 See footnote 12.
rather the first is not possible without the second, and yet that necessity is denied. However, unlike the creative accounting polemics — discussed above — regulatory bodies have specified in detail many required, permitted or prohibited methods of calculation of particular types of anticipated transactions or conditions. Because of the impossibility of attaining the regulative ideal of closed ex post accounting, the denial of anticipation is an incomplete strategy.

4.1.5. Acknowledgement

Even within the ‘conceptual frameworks’ there are, in varying degrees, acknowledgements of the unavoidability of anticipations in descriptions of past events. For instance: “[t]he definition of an asset requires that there be some opportunity for future benefit...[and]...revisions of judgements made in earlier periods are a normal feature of reporting under conditions of uncertainty” (ASB, 1995 paras.3.0, 6.33); “[e]stimates resting on expectations of the future are often needed in financial reporting...their major use...is to measure financial effects of past transaction or events” (FASB, 1978, para.21); and “[v]irtually every accrual and deferral contains an explicit or implicit assumption about the occurrence or outcome of future events”. But, acknowledgements, retreats from the ideal of closed ex post accounting are even more apparent in many of the documents (often called “statements” or “standards”) in which the regulatory bodies specify the required or prescribed methods of measurements. Many of these documents are peppered with descriptions of required or permitted methods of calculation which cannot be made without anticipations. This necessity is, for example, made explicit in SSAP 2:

The main difficulty in applying the fundamental accounting concepts arises from the fact that many business transactions have financial effects spreading over a number of years. Decisions have to be made on the extent to which expenditure incurred in one year may reasonably be expected to produce benefits in the form of revenue in other years and should therefore be carried forward, in whole or in part; that is, should be dealt with in the closing balance sheet, as distinct from being dealt with as an expense of the current year in the profit and loss account because the benefit has been exhausted in that year. All such decisions require consideration of future events of uncertain financial effect, and to this extent an element of commercial judgement is unavoidable in the assessment (ASC, 1971).

4.1.6. Restrictions

As we have seen there are conflicts within regulatory body pronouncements between denial and acknowledgement of the necessity of making anticipations in the construction of financial reporting measurements. The denials reflects the stated objective of restricting ex post financial reports to descriptions of the past but the failure of denial — as evident in the acknowledgements — is a consequence of trying to do so within the chronological notion of time. The legitimate desire to restrict ex post financial reporting to descriptions of the past and yet the unavoidable inclusion of anticipations is accommodated in constraints or restrictions placed on the characteristics of permitted anticipations. Through these specifications the ideal of closed ex post accounting is maintained whilst the necessity to make anticipations is facilitated.

As we saw in the discussion above of creative accounting, anticipations potentially provide a major opportunity for bad faith creative accounting. Unable to prohibit anticipations — without which financial reporting would be impossible — regulatory bodies seek to constrain and specify the characteristics and limits of the financial reporting imagination. The permitted use of future events in calculation of past conditions is restricted to what was described above in the four-way classification of future events as: “past describing anticipated events”. That is, whilst the description of the past events requires anticipation of future events, those future events are limited to those which are necessary to describe the past. The formal description above of open ex post accounting was that event $E_2$ (which has not occurred at the time of $E_1$) is a necessary condition for a description of $E_1$ (made at or after the time of $E_1$, but before the time of $E_2$). But events of the type $E_2$ are not arbitrarily chooseable. Just as descriptions of events of the type $E_1$ require those of the type $E_2$ what may be legiti-
mately be regarded as an E₂, an anticipated event, requires, an E₁. This places a critical constraint on what may be used as a future event for financial reporting purposes. As ASB succinctly describes it:

[T]here must be some past event that triggers the recognition of a change in the entity’s assets and liabilities, even though the measurement of this change may reflect views on the amount of benefits that will flow to or from the entity in the future (ASB, 1995, para. 4.12).

If, for example, no future benefits are anticipated from a past expenditure it is treated as an expense of the past period. If future benefits are anticipated then a necessary but not sufficient regulatory condition is satisfied (cf. ASC, 1989; FASB, 1985).

5. Conclusions

One way of writing financial reports would be to wait until long after the events to be described and the future events upon which those descriptions also rely had passed. But financial reporting must necessarily be impatient. Although describing what is past it constitutes an eminently open inquiry. Financial reports are not mere records, not the equivalent of pointing. They are descriptions of the past made before all that is essential for such accounts has happened. Financial reports necessarily include descriptions of the past events which refer to at least two-time separated events though they only describe (or are only about) the earliest event to which they refer. Effects do not precede causes, but descriptions of events can precede their causes. There are descriptions in financial reports which although applied to present/past events do so only on the assumption that a future event(s) occurs and which will retrospectively be untrue of those objects if the future anticipated in making the description of the past fails to materialise.

The past is necessarily viewed from the perspective of an imagined future. Imagination has a prominent and ineliminable role in financial accounts of the past. The end of a financial reporting story is in the future. There are non-presences, not-yets, might never-be, at the heart of descriptions of the past. In essence, financial reporting is necessarily incomplete. If R is a description of an event E₁-N, there will always be some aspect(s) true of E₁-N, call it G, which can be witnessed or retrospectively described. If, however, we subtract “E₁-N was G” from “E₁-N was H” there will be a residue of events not witnessed at the time the description of E₁-N was made (Danto, 1985).35,36

The analysis above showed that the temporal structures of financial reporting are not identical with those of ordinary notions of time. Yet, something important is stated by that idea of time as simply a succession of events. Every event is ‘datable’ once it is located within that framework. We rely on it for the idea of lapse of time, the measurement of intervals by fixed units of duration (including periodization), the notion of simultaneity, and an anonymous and communal ‘public time’. Calenders and clocks govern our schedules. Our birth is an event of the past that no longer exists and our death a future event that has not yet taken place. But something is also perverted by it (Ricoeur, 1988). The ‘thickness’ of a described event lies both in its temporal isolation and yet its continuity (McSweeney, 1994 in Hopwood & Miller, 1994).

In this paper we have sought to show that financial reporting (for a maker/writer and for a reader) must not only, as it were, look back but also forwards. Financial reporting is never a mere record or grasping of something, but always requires, as the discussion above of anticipation and retroactive change suggests, what Augustine

35 An implication of this analysis is that there are limitations on the adequacy of contemporaneous ethnographic, anthropological, or other field-study reports of accounting (or indeed anything else). Knowledge that is contemporaneously knowable may in many circumstances be useful, indeed be vital, but the argument in this paper is that there is knowledge which is available uniquely only in retrospect. It cannot be observed by a witness. It is misguided therefore to believe that temporal (and spacial) proximity to actions (as for example in field studies) necessarily is always superior.

36 As this paper has sought to limit discussion of the interpretative properties of description to that of its temporal character the conceptual asymmetry between the systems of thought available to witnesses and those used later by re-describers is ignored.
called an [entangled] triple present (the present of the past, the present of the present, the present of the future)(in Ricoeur, 1984). Future, present, and past mutually determine one another as parts of a narrative whole (Carr, 1986). These three ecstases of a plural unity of temporality together with an chronological sense of time constitute the dual, unconflatable temporal structures of financial reporting. Those events which are temporally accounted for in financial reports are not isolated past events, but configurations which extend projection. In so far as the future is open, so too are descriptions of the past.

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