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Preface

This book presents the results of Polish-Ukrainian scientific cooperation. It contains the papers prepared for the 10th international conference “Quantitative Methods in Accounting and Finance”. Accounting and finance face nowadays many challenges. They require both an international and local approach, they need to be considered from the theoretical and practical point of view, and they also encourage general and specific analysis.

Support from quantitative methods is needed in order to discover, implement and verify new finance and accounting trends, methods and instruments. The research papers which are part of this book present different aspects of accounting and finance combined with a quantitative, in particular Econometric, approach.

Some of the papers focus on methodology of measurement, estimation and forecasting of financial phenomena, especially those related to investment processes. Others address specific problems of accounting such as accounting solutions for different branches, legal issues of accounting, responsibility and reporting. An alternative approach was also undertaken and the roles of a narrative and culture in accounting were presented.

The variety of papers selected for this issue ensures the complexity of the book. It provides theoretical as well as empirical material which can be used in further research and in business practice, particularly in accounting and finance. We hope that the content of the book provides a starting point for scientific discussion and practical changes.

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WHY NARRATIVES IN ACCOUNTING?

SKĄD NARRACJE W RACHUNKOWOŚCI?

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Summary: For years financial and management accounting reports were based primarily on “hard” numbers. Extensive written descriptions and explanations were not common in practice. However, in recent decades there has been a significant shift towards “softer” and more narrative communication in accounting. The purpose of the paper is to identify and describe the determinants of the development of accounting narratives in practice, and to explain why narratives are gaining in importance in the accounting communication. The paper presents the links between accounting and language, and then the development of accounting narratives is described and factors determining the use of narratives are identified and discussed.

Keywords: accounting, language, narratives.

Streszczenie: Przez lata raporty generowane w ramach rachunkowości finansowej i zarządczej wykorzystywały głównie twarde dane liczbowe. Ekstensywne słowne opisy i objaśnienia nie były powszechnie stosowane w praktyce. Jednak w ostatnich dekadach można zauważyć znaczny krok w kierunku bardziej miękkiej i narracyjnej komunikacji w rachunkowości. Cele artykułu to identyfikacja i opis determinant rozwoju narracji w rachunkowości w praktyce oraz wyjaśnienie, dlaczego narracje zyskują na znaczeniu w komunikacji w rachunkowości. Artykuł przedstawia związki rachunkowości z językiem, a następnie koncentruje się na rozwoju narracji w rachunkowości. Zidentyfikowano i przedyskutowano główne czynniki warunkujące ten proces.

Słowa kluczowe: rachunkowość, język, narracje.

*The narratives of the world
are numberless.*

Roland Barthes

1. Introduction

Accounting is commonly called the “language of business” as it enables communication between the preparers and the users of accounting information.

Accounting is also a tool for describing and constructing the image of the economic reality in which an entity operates [Masztalerz 2013]. While natural language reflects phenomena in the real world, accounting reflects phenomena in the business world [Jain 1973]. Accounting communication may be also referred to as a process of creating and sharing meaning [Jack, Davison, Craig 2013].

For years, accounting reports were based primarily on “hard” numbers, and accounting communication was equal to providing information. Extensive written descriptions and explanations were not common in practice. However, in recent decades there has been a significant shift towards “softer” and more narrative communication in accounting. This “narrative turn” in accounting gives rise to new research challenges and perspectives [Beattie 2014; Brennan, Merkl-Davies 2013].

The paper addresses selected linguistic and communication issues in accounting. The main purpose is to identify and describe the determinants of the development of accounting narratives in practice, and to explain why narratives are (and probably will be) still gaining in importance in the process of accounting communication processes. It is mainly a theoretical paper, based on literature review and the content analysis of text documents (standards, guidelines, reports). The paper is structured as follows. Section 2 presents briefly the links between accounting and language, adopting the structural, functional, semiotic, and social approach. Then another linguistic issue in accounting, namely the use and role of natural language in accounting, is outlined. Section 3 deals with the development of accounting narratives. Key factors determining the increasing use of written narratives are identified and discussed. The conclusion and final remarks are presented in the final part of the paper.

2. Accounting and language

It is commonly said that accounting is the language of business. For years this sentence has been repeated like a mantra by accounting theorists and practitioners, because accounting, like a natural language, is both a tool for describing, presenting or even constructing a picture of reality, and a tool of communication.

According to M. Masztalerz [2013], the links between accounting and language may be analysed by adopting four different approaches:

- structural (is accounting a real language? what is its structure? does it share the characteristics of a natural language?),
- functional (is accounting a communication tool like a natural language?),
- semiotic (is accounting a system of signs? what are the semantic, syntactic and pragmatic problems of accounting as a semiotic system?),
- social (is accounting language a social or cultural phenomenon? is it a social product or construct? what is its role in particular communities? how does the accounting language function in society and culture?).

There is also the second face of linguistic issues in accounting, namely the use and role of natural language (and thus also narratives) in accounting, which may be

considered, *per analogiam*, by using four approaches to accounting as a language. Firstly, under the structural approach, natural language is used in accounting in order to name, classify, and reflect the economic transactions and other phenomena that need to be taken into consideration while preparing financial and management accounting reports. Secondly, under the functional approach, language and text are used in order to facilitate the communication process and to provide comprehensive and understandable information from senders to receivers. Thirdly, under the semiotic approach, the use of language is required for constructing meaning(s), and creating a real or imagined picture of the economic reality in which an entity operates, or even to manage the impression of the users of information. Finally, under the social approach, language is used in the accounting communication process in order to integrate the members of a community (e.g. within an organization), or to accumulate knowledge (e.g. within professional accountants), but it may also be a tool for constructing the reality (this issue is strongly emphasized by critical researchers). The links between accounting and language are synthesized in Table 1.

Table 1. Table title table title and table title?

Approach	What is accounting as a language?	What is the use of language in accounting?
Structural	Accounting is a language as it has similar structure and characteristics.	Language is used in order to name, classify and reflect economic reality.
Functional	Accounting is a communication tool and performs all language functions.	Language is used in order to communicate information from senders to receivers.
Semiotic	Accounting is a system of signs and as such it has syntactic, semantic and pragmatic dimensions.	Language is used in order to construct meaning(s), to create a real or imagined picture of the reality.
Social	Accounting is a socio-cultural phenomenon and construct.	Language is used in order to integrate the members of a community, or to accumulate knowledge, or even to construct the reality.

Source: own study.

3. From numbers to words – the accounting communication (r)evolution

The importance of language in accounting communication has increased significantly in recent decades. Contemporary accounting, both in its theoretical and practical dimension, can no more be simply regarded as a technical and number-based discipline. It has been constantly developing in a rather “soft” and text-based direction [Brennan, Merkl-Davies 2013]. Accounting written narratives appear, for instance, in annual reports, financial statements, management commentaries, social responsibility and sustainability reports, integrated reports, intellectual capital reports, management accounting and performance reports, national and international

accounting standards and other regulations, principles and guidelines issued by numerous professional accounting bodies, accounting textbooks, papers, articles and monographs. There are several reasons why language and narratives have been systematically gaining in importance in the processes of accounting communication (Figure 1).

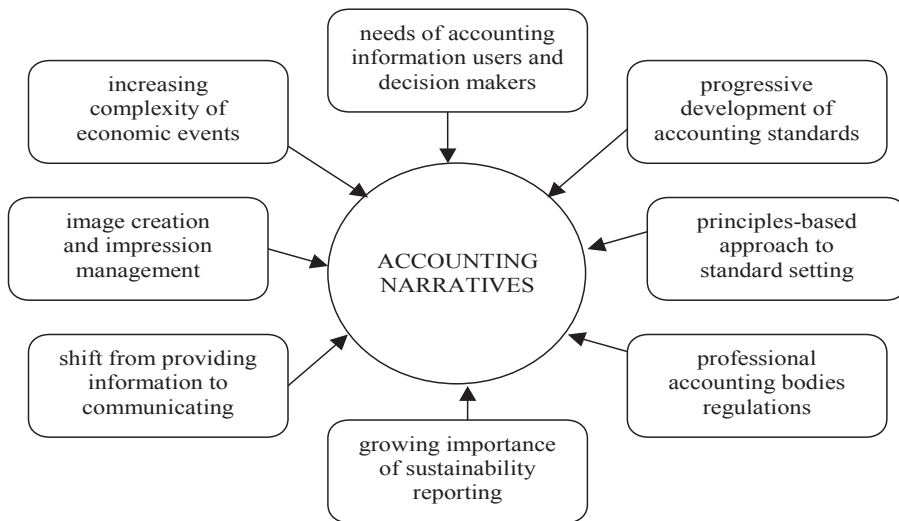


Fig. 1. Determinants of the development of narratives in accounting

Source: own study.

Firstly, the **increasing complexity of economic phenomena** [Beattie 2014], i.e. economic transactions and other events, requiring an accounting treatment involves the necessity of giving additional written explanations in order to ensure intelligibility. The accounting narratives in textbooks, standards or reports aim to enable the in-depth understanding of those complex phenomena. A given number in a financial statement may be insufficient for the information user if the nature of the related item or phenomenon is not clearly described and explained, and the underlying measurement or presentation assumptions are not provided.

The increasing complexity of economic phenomena had a significant impact on the **growing needs of accounting information users** and decision makers [Beyer et al. 2010; Beattie, Pratt 2002], who want to understand the determinants of a company's financial position and performance, so they expect not only relevant the information, but also intelligible explanations to be included in corporate reports. Around each enterprise there are groups of stakeholders interested in different aspects of the organization's performance. If an organisation aims to fully satisfy their information needs, some relevant explanatory narratives must be included in the financial statements, reports or other messages containing accounting information.

In response to the growing needs of the accounting information users, many professional accounting bodies have been (and undoubtedly will be) issuing standards, principles, guidelines, and other regulations or statements which may be considered as accounting narratives themselves, but on the other hand, they have also a significant impact on the use of language in accounting communication practice. The most visible example is the **progressive development of accounting standards**, particularly the International Financial Reporting Standards (IFRS). Since 2001 the International Accounting Standards Board (IASB) has issued an average of over one new standard *per annum*, not to mention the renewals of numerous formerly published standards (IAS). Currently, along with all the accompanying documents such as the bases for conclusions, implementation guidance, illustrative examples, interpretations and a practice statement, the complete text of the IFRS has more than 3,500 pages, and it will undoubtedly grow in the future. The influence of the IFRS on the use of narratives in annual reports results from at least two reasons. On the one hand, the IFRS have been requiring from entities more and more compulsory written disclosures in the notes to the financial statements (in order to present and explain accounting policies, judgments, estimations etc.), and on the other hand, since the publication of the IFRS practice statement *Management Commentary* in 2010, the IASB has been encouraging entities to prepare this non-binding narrative report providing a context within which to interpret the entity's position, performance and progress. The IASB assumes that management has a unique perspective on the enterprise and that perspective has value for other users of financial reports. The major objective of the management commentary is to supplement the financial statements with additional explanations of the amounts presented in the financial statements and the conditions and events that shaped that information, and to complement the financial statements with financial and non-financial information about the entity's position, performance and progress. Management commentary should communicate information about the enterprise's economic resources and explain the main trends and factors that are likely to affect the enterprise's future performance, position and development. All that information requires narrative disclosure.

Another reason for the increase in using narratives in the accounting communication is the **principles-based approach to standard setting** [Alexander, Jermakowicz 2006; Masztalerz 2012]. According to this approach, accounting standards are not designed to regulate the accounting treatment of all possible particular phenomena or events (as it is in case of the rules-based standards), but rather to indicate general principles focused on achieving accounting objectives. The application of the principles-based standards in the preparation of financial statements requires the regular use of professional judgment [Bennett, Bradbury, Prangnell 2006], and hence the use of verbal descriptions in order to explain accounting policies and all underlying assumptions and estimations to the information users. W. Smieliauskas [2013], outlines the role of argumentation in justifying the fairness of presentation in the financial statements, and argues that reasoning in natural language is essential in the environment of principle-based accounting.

Not only the financial reporting standards strengthen the role of narratives in the process of accounting communication. This is also the case of particular **professional accounting bodies regulations**. The *Global Management Accounting Principles* (GMAP) issued in 2014 by two international professional bodies – Chartered Institute of Management Accountants (CIMA) and American Institute of Certified Public Accountants (AICPA) – may serve as a blinding example. The document was designed to guide management accounting practice and includes four principles: Communication provides insight that is influential; Information is relevant; Impact on value is analysed; and Stewardship builds trust. According to CIMA and AICPA [2014, p. 6], “numbers usually require explanation [and] management accounting helps organisations translate numbers into meaningful narrative analysis”. The GMAP stress the importance of verbal description in management accounting reports as narratives make the accounting information more understandable for its users.

The next reason for the increasing use of verbal descriptions in the process of accounting communication is the **growing importance of sustainability reporting**, which is a natural consequence of the growing importance of sustainable development and the concept of corporate social and environmental responsibility [Mazurowska 2015]. In recent years, several bodies have published documents containing guidelines and principles for organizations interested in reporting social and environmental issues. An illustrative example is the International Integrated Reporting Framework published in 2013 by the International Integrated Reporting Committee (IIRC). According to IIRC [2013, p. 7], “an integrated report is a concise communication about how an organization’s strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value”. Integrated reporting encompasses such elements as organizational overview and external environment, governance, business model, risks and opportunities, strategy and resource allocation, performance, outlook, and the basis of preparation and presentation [IIRC 2013, pp. 24-29]. An integrated report contains both quantitative and qualitative information as each provides the context for the other: numbers and indicators need narrative explanation in order to ensure effective communication, as well as narratives need numbers and indicators in order to support and justify the verbal commentary.

What is a common feature for many recent pronouncements made by different accounting and reporting professional bodies, is the focus on communication. This explicit **shift from providing information to communicating** results in a much greater use of narratives in internal and external reporting. Although communication is commonly referred to as the process of transferring information from the sender to the recipient, this view is sometimes undermined. According to B. Ollivier [2007], communication should not be considered solely in terms of transferring messages from the addresser to the addressee, since the messages are continually subject to (re)interpretation by their users. As mentioned above, contemporary regulations and guidelines issued by professional accounting and reporting bodies (e.g. CIMA, AICPA, IIRC) put a lot of emphasis on communication. For example, in 2008 the

American Institute of Management Accountants (IMA) published a new definition of management accounting, which undermines the traditional role of management accountants as information providers and stresses their active and partnering role in decision-making. According to IMA [2008, p. 2], management accountants provide the conceptual framework for converting data into information and fulfil the role of enabler and strategic business partner along the entire information value chain. In turn, CIMA and AICPA [2014, p. 8], define management accounting as “the sourcing, analysis, communication and use of decision-relevant financial and non-financial information to generate and preserve value for organisations”. The GMAP strongly emphasize the importance of communication because “management accounting begins and ends with conversations” [CIMA, AICPA 2014, p. 9]. By communicating insightful information at all stages of the decision-making processes, management accounting leads to better decisions. The method and style of communication should be tailored to the information users, to the decision under discussion and to different decision styles. In order to improve the users’ understanding, management accounting should rely largely on explanatory narratives enabling deeper insight into the entity’s financial and non-financial position, performance and prospects.

The last but not least reason why accounting narratives have been gaining in importance is related to the **image creation and impression management** [Brennan, Guillamon-Saorin, Pierce 2009; Merkl-Davies, Brennan 2011; Brennan, Merkl-Davies 2013]. Every entity (be it a company, a manager, a standard setter, a textbook author, a professional body etc.) is naturally interested in presenting the best possible image of its position, performance and prospects. N.M. Brennan and D.M. Merkl-Davies [2013], argue that impression management can play a role in restoring reputation, image or legitimacy in times of crisis or change. As far as financial reporting is concerned, this goal may be achieved by using creative or aggressive accounting methods (in the area of measurement, disclosure and presentation of specific items or transactions), what leads to the apparent improvement of the entity’s financial position and performance reported in financial statements. Nonetheless, the impression management in accounting communication refers rather to the use of narratives and visuals in order to make and give the desired sense and meaning of the accounting information, and to influence the reader’s perception, understanding and (re)actions.

4. Conclusion

For years, accounting communication was based primarily on numbers. The effective communication between preparers and users of the accounting information required good knowledge of the accounting language itself (“dictionary and grammar”), for instance, definitions of accounting terms, journal entries rules, financial statement structure, measurement methods etc. Additional written explanations were not widely used. However, as it is shown above, written narratives have gained in importance in the process of accounting communication. This is a considerable shift from “accounting

is the language of business” towards “language is used in accounting”. This is also a shift from “providing information” towards “communication of meaning”.

The development of narratives in accounting is determined by several factors. Eight of them have been presented above. The increasing complexity of economic reality has an impact on the needs of accounting information users and decision makers. Professional accounting bodies and standard setters do not stop issuing new regulations and guidelines in order to satisfy these needs. Most frequently, all these regulations require from the information preparers a considerable effort in the verbal description of the reported numbers. Contemporary accounting is thus much more explanatory and “user-friendly” than before. Nonetheless, there is a risk of manipulation. But this is another paper.

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