

How come we outsourced accounting, company law and auditing?

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The [Telegraph](#) has noted:

PIRC has calculated the amount of bad debts the banks may have to write off in coming years but have yet to subtract from profits, together with other items such as deferred bonuses not booked.

HSBC, which is the biggest bank by assets, was shown to have £10.4bn of hidden losses, the Royal Bank of Scotland has £9.4bn, and Barclays has £7.3bn. Lloyds Banking Group has £2.5bn and Standard Chartered £2.2bn. Together the undeclared losses total £31.8bn.

The research shows the distorting impact the accounting rules, which allow bad loans to remain hidden, have on bank results. PIRC applied old-style UK GAAP accounting rules, which applied for 100 years until 2005, to the figures released in the 2012 banks' accounts.

This is the course the work of my old friend and ally Tim Bush who is a long term critic of International Financial Reporting Standards , and rightly so.

How did this happen? How could it be that banks can have their accounts signed off when they are so very obviously not true and fair because they include losses that everyone knows will happen but which are not anticipated? The answer is in those four words International Financial Reporting Standards.

IFRS replaced UK GAAP - a century old tradition in 2005. OK, it was partly the EU's fault - I accept that - but the project would not have existed without the Big 4. The Big 4 accountants - PWC, KPMG, Deloitte and Ernst & Young - wanted IFRS to suit its clients. And it wanted it for another reason - because the related auditing standards that they also drove through changed their obligations to report.

The combination has been lethal for our economies. First of all as the rules of the [IAASB](#) (International Auditing and Assurance Standards Board), which now sets auditing standards and which is also Big 4 dominated, [says, an audit is](#):

The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with IASs and relevant ethical requirements enables the auditor to form that opinion.

The wording is not a chance: the emphasis is on compliance with the financial reporting framework first; the consequence of being true and fair is assumed to follow, but is consequential, not the goal. So, true and fair was defined by these firms as ticking the boxes, not whether there was an actual true and fair view. The old rules of prudence, for example, which required that auditors did, come what may, anticipate losses went out of the window.

And that was deliberate, of course. The Big 4 wanted to curry favour with their clients. Anticipating profits reduced profits and that reduced directors bonuses, so that would never do, especially in banking. So IFRS abandoned the principle of prudence and its so called 'anticipated loss' model i.e. you wrote a debt off when you realised it was unlikely not to pay. Instead in came a "realised loss' model which meant you only wrote a loss off when it actually could not pay. That's what's deferred the loss recognition process which PIRC have identified. And having a convenient change in the auditing rules to say an audit only meant box ticking, not that the accounts could be relied on to show a true and fair view in any reasonable auditor's judgement, let all banks sweep bad news under the carpet.

The result is bank accounts have been misstated, I suggest deliberately.

The further result is some of our banks may now or have been insolvent when they have claimed otherwise.

And some may have been or may still be paying dividends that could be illegal.

And, of course, they won't lend because they know all of this.

As do the Big 4, who created the system so bankers could have their bonuses. And the Big 4 could have big fees.

That's how it works.

And the real question is - how come we outsourced accounting, company law and

auditing regulation to the Big 4 so they could rig the system in this way and entirely outside democratic control?