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Accounting for the fictitious: A Marxist contribution to understanding accounting's roles in the financial crisis

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ABSTRACT

This paper presents a contribution to the debates surrounding the culpability of accounting in the recent financial crisis. It adopts a Marxist theoretical perspective concentrating mainly on Marx's work on fictitious capital. Fictitious capital is any form of investment (for example bonds, stocks, derivatives, and collateralized debt obligations) which is based upon the *expectation* of future returns. According to Marx while fictitious capital is useful to capitalism, it cannot create value – only human labour can do that. The recent crisis was exacerbated by the significant amounts of investment which were made in extreme forms of fictitious capital. The paper argues that the accounting profession's adoption of financial economic rationalities meant that it helped to animate the form of financialised neo-liberalism which dominated at the time of the crisis. The accounting profession and accounting academia have implemented and propagated technologies and rationalities which enabled, legitimised, and drove the activities of business in general and financial institutions in particular in the run up to and since the crisis. While, accounting could be seen as being complicit in the crisis, it is important to remember that it was a capitalist crisis. The intuitional structures of accounting mean that it is susceptible of being captured by the most powerful in society.

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> The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually slaves to some defunct economist. Madmen in authority, who hear voices in the air are distilling their frenzy from some academic scribbler a few years back.
>
> Keynes (1936, p. 383)

> . . .it has long been evident to dispassionate observers that individual capitalists operating in their own self-interest are prone to behave in such a way as to collectively drive capitalism deeper into crisis. The same can be said of the various factional interests that periodically dominate political and economic power: the bonus-hungry bankers and financiers who now set so much of the agenda in Washington and London . . . Individuals and factions pursuing their own particular interests have almost always signally failed to produce a cogent political agenda to stabilise, let alone revive, an ailing capitalist system.
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> Harvey (2011, p. 275/6)

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In the wake of arguably the worst economic crisis in 80 years, a new debate is gradually opening up about the culpability of accounting in the crisis (Hopwood, 2009). In particular, significant concerns have been raised about the roles of fair value accounting, auditing, off-balance-sheet financing and accounting regulation (Arnold, 2009; Gup & Lutton, 2009; Hatherly, 2013; Krumwiede, 2008; Laux & Leuz, 2009; Magnan & Markarian, 2011; Sikka, 2009; Whittle, Carter, & Mueller, 2014). At a very basic level one might ask how it could be that large financial institutions with recently audited financial statements showing positive net assets and no audit qualifications could fail so dramatically or require such massive government bail-outs. Following the bail-outs and failures the press was quick to make allusions to Marx but as Kunkel (2011) states; this is a "shallow revival" of Marxist theory perhaps best exemplified by a piece in the UK conservative Spectator Magazine by the Archbishop of Canterbury,[1] Rowan Williams (2008), in which he argued that placing too much trust in the market had become a kind of "idolatry." Williams reminded readers of Karl Marx's criticism of laissez-faire capitalism, noting, "He was right about that, if about little else." This Marxist revival has picked up upon some interesting facets of Marx's work, notably its crisis tendencies but Keynesianism appears to set the left-boundary of economic debate in the press (Kunkel, 2011).

This essay argues that a deeper reading of the work of Marx, especially his work on credit and fictitious capital, can enable a stronger understanding of the crisis and could play a central role in the conceptual discussions about accounting and its role in the crisis. This paper draws upon David Harvey's writings (2006, 2010, 2011) and Marx's work on the labour theory of value and the credit system including fictitious capital (Marx, nd, 1967, 1973). The use of Marxist theorisation is not new in accounting. For example, Marxist theory has been used to develop a social history of accounting change (e.g. Armstrong, 1985, 1987; Bryer, 2000a, 2000b, 2005, 2006a; Toms, 2005). Other accounting research has used Marxist theory to develop an understanding of contemporary issues in accounting. For example, in the Special Issue on human rights, in Critical Perspectives on Accounting, several papers draw upon Marxist theory (see for example, Cooper, Coulson, & Taylor, 2011; Sikka, 2011). Marxist theory has been used to comprehend accounting's functions in terms of control over the labour process (Arnold, 1988; Cooper & Taylor, 2000; Saravanamuthu & Tinker, 2003; Spence & Carter, 2011) and deal with contemporary issues like accounting's functions in privatisation (see for example, Arnold & Cooper, 1999; Toms, Beck, & Asenova, 2011). In terms of the argumentation in this paper, a body of work has been developed which argues that Marx's labour theory of value is superior to marginalist economic theory as the foundation for describing and explaining the role and practices of financial reporting in capitalism (Bryer, 1994, 1999a; Martin, 1998). This paper builds upon this body of work by using Marxist theory as a counterweight to financial economic theory which, as will be argued in more detail in the paper, provided the ideological and theoretical underpinning of the structures and activities which enabled impelled and legitimated the events which led to the financial crisis. Financial economics ideas (positive accounting theory, efficient markets hypothesis, agency theory and so on) dominate the field of academic accounting as well as the field of accounting practice.

The crisis demonstrated that financial economic theory serves the interests of some more than others, for while a few individuals were enriched before and by the crisis, it has had a profoundly destructive impact on the majority.[2] Although financial economic theory has been empirically falsified[3] and continues to wreak havoc and destruction it is very difficult to overcome. For this reason several theorists have described financial economics as zombie economics (see for example, Fine, 2008a, 2008b; Martin, 2002; Quiggin, 2012). This is not simply a question of theoretical niceties; in practice, in 2014, financial institutions and government policies (whose activities are underpinned by financial economics' rationalities) continue to impoverish the lives of the majority of people.

Two aspects of Marxist theory are particularly pertinent for the arguments in this essay – the labour theory of value and fictitious capital. In Marxism only human labour (work) can create value.[4] Fictitious capital is any form of investment (for example bonds, stocks, derivatives, and collateralized debt obligations) which is based upon the *expectation* of future returns. Since the expected returns might be produced in the future, they do not currently exist, and, so are fictitious. Marx explains that fictitious capital (especially stocks and credit) serves several important functions under capitalism, not least in terms of enabling capitalist expansion. But, if investment flows to forms of fictitious capital which are not based upon the creation of value, this will, sooner or later, provoke an economic crisis. The flow of money into forms of fictitious capital which are purely speculative and not part of the value creation process (although incredibly profitable for some) exacerbated the recent crisis (see Chabrak, 2014).

The paper is structured as follows. After a deeper consideration of fictitious capital, the paper outlines the form of economic theory, described in the paper as financial economics, which has underpinned neo-liberalism and prioritised the expansion of the markets for fictitious capitals. Next, the paper turns to the impact of financial economics on both professional and academic accountants. Although academic accounting and finance departments provided an incubator for the development of financial economics, the ideology of financial economics is founded upon a belief in unfettered markets and so is against accounting regulation and so presented a challenge to the profession. This is followed by a brief explanation

[1] The Archbishop of Canterbury is the senior bishop in the Church of England.

[2] See for example, http://wearethe99percent.tumblr.com which sets out personal narratives of ordinary Americans who have played by the rules, worked and studied hard, bought homes for their families, and now feel abandoned and betrayed by the system in which they supported.

[3] This appears to be the case for the majority of activities which are informed by financial economic thought. Quiggin (2012) argues that the US and UK governments are making policy decisions on the basis that the fiscal multiplier is substantial and negative so cutting expenditure will increase output. This claim has no theoretical basis and flawed empirical support.

[4] This is not to argue that technology is unimportant. Technology is also created by human labour and can be described as "dead labour". Even the most sophisticated machinery has to be operated by humans.

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