

Oxford Report (Summary)

The Impact of IFRS on Wider Stakeholders of Socio-Economy in Japan

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<For accurate and further information, please consult the original texts in the Report. For any inquiry, details of the Report and collaboration, please contact Tomo Suzuki (Tomo.Suzuki@sbs.ox.ac.uk).>

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1. Background of the Report

(1) Neutral point of view - political biases eliminated as much as possible.

- Self-sustained inquiry from purely academic perspectives (since 2000).
- Robust attitude to eliminate interests of specific stakeholders. No endowed chairs / professorship.
- Japan's responses to IFRS evaluated on the basis of comparisons with other countries.

(2) Proven record of contribution to policy-making in various countries

- Significant contribution to policy-making in India, China, Malaysia, Indonesia and other countries.

(3) Up-to-date information about international developments

- Well-developed information network encompassing China, India, Commonwealth and European countries.
- Maintaining arm's length distance with both Continental Europe and the United States.
- Access to the IASB. Information gathering and analysis of future developments through frequent and informal communication.
- Close communication with and access to first-class academics around the world.

(4) UNIAS methodology

- Rather than pursuing "truth" or "solution", it is aimed at "fostering communication and discussions," by overcoming "rhetoric".
- Improvement on previous research methods. Combination of socio-economic and political point of views and statistical method.
- Analytical method based on "procedural objectivity" in a long-term dialectic process, analyzing influences of "rhetoric" of IFRS.
- A research period of over 12 years based on strategically planned interviews with around 1,000 stakeholders.

2. Rhetoric used by IASB - Responses from main jurisdictions

<IASB's use of rhetoric>

IASB's skillful use of rhetoric

- 'High quality', 'transparency', 'fair value', 'comparability', 'global standard', etc.
- From 'harmonisation' (mutual recognition) to 'convergence', and then to 'adoption' without anyone noticing it.



<How jurisdictions have responded>

While countries initially responded positively to IASB's uses of rhetoric, they have gradually become aware of disparities between the rhetoric and reality. It has by now been clearly recognised that that adoption of IFRS is problematic. The ideal form of international harmonisation is now considered, drawing on detailed analysis of impact on socio-economies.

Europe: While having pursued "adoption", reduction of cost of capital is not recognised. Response through careful design of market structures and audit (implementation and practice). Pushback against introducing MoU project items including financial instruments standards.

US: Having made clear in Work Plan that there are significant issues in terms of co-ordination with domestic legal and regulatory systems, the US is learnt to maintain the US GAAP. Examining costs and benefits and due process. Further delays in convergence expected.

China: Never "Adoption." "Convergence" has already been substantially been completed – is the official position.

India: Initially planned full convergence for all listed companies. Concerns have been raised through impact analyses (inter alios, Suzuki & Jain, 2011). Resulted in only soft convergence and 8 carve-outs.

3. Changes in international contexts, and reactions to IFRS / IASB

<Domestic analysis>

- Historical significance of Japan's accounting system: Elements embedded in Japan's institutional design such as calculation of "taxable income based on financial statements approved by shareholders", and "conservatism".
→ Becoming dysfunctional through expanded use of fair value accounting.
- "Three Fundamental Concerns" arising from premature use of IFRS. Potentials of "decreased transparency and comparability", "Dis-coordination within related socio-economic systems", and "undesirable behaviour of unsophisticated investors"
- Significance for the "other" stakeholders than investors: Existence of various concerns among companies already using IFRS, manufacturing, non-listed companies, specific industries, related institutions, including taxation and company law is suggested.
- "Pro-IFRS group" vs. "Anti-IFRS group": Different degrees of awareness. While pro-IFRS group does not rate merits of IFRS-adoption highly, anti-IFRS group has serious concerns over mandatory adoption of IFRS.
- How Japan's decision-makers have responded: Decision made in the FSA's Interim Report (June 2011) is considered appropriate, reflecting new international contexts. Need for shared proactive co-operation with IASB.

<International analysis: short-medium term (5-15 years)>

- IASB's "Agenda Consultation" and proposed amendments to "Due Process Handbook". Demands for "Period of Calm," and appropriate evaluation of economic impact of standards.
- Relationship with US. Possibility of further delay in MoU projects.
- IASB's "Use of IFRS" = "convergence" and "carve-outs." → Less convergence efforts. Possible divergence at an appropriate level.
- Need to listen to voices from the practitioners to determine if accounting standards are practical and substantially useful (true empiricism).
- Involvement of emerging economies. Possibility of South-North Problems, and eventual dysfunction of IASB (The "United Nations" phenomenon – unable to make effective decisions).

4. Policy recommendations for Japan – Need for short to medium term (5-15 years) response, in order to prevent "Quiet Revolution"

<Domestic response>

- Further cost-benefit analysis.
- More items on the agenda of Business Accounting Council, such as merits of IFRS for listed companies, appropriate input into proposed amendments to IASB Due Process Handbook. Cross-ministerial deliberations, close co-operation between relevant stakeholders, ensuring consistent response.
- Restricted application of IFRS to consolidated financial statements alone; i.e., no application of IFRS to non-consolidated financial statements, to prevent unnecessary international influence on domestic institutional and regulatory framework
- Need for analysis of related institutional and regulatory systems: e.g., Quarterly reporting and auditing.
- Importance of new market design of stock exchanges.
- Need to carefully examine the relationship with company law (regulation of profit distribution), tax law, other related institutions, and commercial and contractual practices.
- Priority to be given to enabling management of mature economy and sustainable economic activities.

<International response>

- Need for pro-active international response. Strict and uncompromising attitude against undemocratic rhetoric when lacking evidence.
- Increasing voluntary use of IFRS. Continuation of pro-active convergence, based on merit. Active intellectual contribution to IASB's activities including contribution of human resources.
- Appropriate understanding of potential re-emergence of "Legend" problem.
- Co-operation with China, India, South Korea and other countries. Need to identify common agenda among Asian countries. Effective use of IASB's Asia-Oceania satellite office in Tokyo.
- Need for actions for increasing medium to long term corporate values involving all relevant stakeholders (e.g., through introduction of integrated reporting).
- Internationalisation of auditors. Truly international accounting personnel.

UNIAS Project believes that premature, strong-form mandatory adoption of IFRS should not be supported in Japan.

1. Table of Contents

Section 1 Background

- A brief review of Japan's modern accounting history – Accounting for socio-economy
- The viewpoint of the report - i.e., not narrowly for “investors” alone, but for broad socio-economic communities.

Section 2 Objectives • research approach • structure

- To evaluate the impact of global standardization of accounting on a variety of stakeholders in Japan, and present data / evidence for policy discussion.
- A long-term dialectic interview method and a comprehensive review of the literature

Section 3 The history, theory, and effect of “the financial reporting for investors”

- Transparency and comparability are actually damaged due to principles-based fair value accounting
- The label of “high quality global standards,” misleads many, especially un-sophisticated investors
- Above factors can create an artificial reality in a world of short-term investment behaviour, and degrade objective, transparent and comparable accounting data.

Section 4 Impact on other stakeholders

- From the viewpoint of production and operation, rather than finance, such potential distortions have already caused serious concerns among top Japanese companies (e.g., Goodwill accounting, and R&D accounting).
- Impact on the Bank and Insurance industries.

Section 5 Politics of accounting standards setting

- The false impression of mandating “Adoption” was created through highly effective rhetoric by pro-IFRS businesses and political camps, which damaged the quality of social communication in the process of policy making.
- A potential of a single set of the global standards depends on several important parameters including evidence (and not rhetoric) of IFRS leading to higher quality accounting in some clearly understood and measurable fashion.
- All stakeholders collaborate to enhance proactive rather than reactive efforts towards international convergence.

Section 6 Summary and Recommendation

2. Research Approach

We conducted approximately 1,000 units of interviews with a variety of stakeholders including ministers of relevant departments, accounting standards board members, executives of multinational companies and small local businesses, over an extended time period (2000-12) that included the whole life-span of the IASB.

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We have also conducted a comprehensive review of the literature (637 articles in Japanese and 72 academic papers in English) to guide our interpretations of the interview data.