À la carte accounting will not deliver globally consistent standards

Introduction

Ladies and gentlemen

It is my great pleasure to join you today. It is hard to believe that it has been exactly one year since my last visit to Tokyo, to celebrate the opening of the IFRS Foundation Asia-Oceania office.

I should point out from the outset that, as Chairman of the Trustees, I do not involve myself in the technical work of the IASB. You will, however, be pleased to know that Hans Hoogervorst, Chairman of the IASB, will be in Tokyo in February next year. I am sure he will provide you with a technical update at that time.

Today I would like to spend some time talking about the importance of our work to achieve a single set of high quality, global accounting standards and the remarkable progress towards this goal in the last ten years. I will also discuss the important role that this part of the world has played and continues to play in helping us to realise that goal.

Before I begin, however, I would first like to take the opportunity to welcome Joji Okada as a new Trustee of the IFRS Foundation. I know that Joji is a highly respected member of the Japanese business community and we have already benefitted from his wise advice.

I would also like to mention a familiar face to many of you—Noriaki Shimazaki. Noriaki served as one of our Trustees for many years and he has kindly agreed to remain involved in a slightly different capacity, as an unpaid adviser to the Foundation while we seek to further establish the Asia-Oceania office as a regional centre of excellence.

The case for global accounting standards.

So, I will begin at the beginning. I am old enough to remember the genesis of the whole move towards international accounting standards. Back in 1973, nine of the largest national accounting institutes came together to support the formation of the International Accounting Standards Committee, or IASC. The idea back then was for the major economies, including Japan, which was represented by the JICPA, and the US through the AICPA to work together to make their respective jurisdictional accounting standards fully compatible with the IASC's standards as the international point of reference[1].

The first Chairman of the IASC was Lord Henry Benson, who at that time served as President of the Institute of Chartered Accountants for England and Wales. In a speech in 1975, two years after the formation of the IASC, he said "I think we will see, during the next five years, great successes, the effects of which will not make themselves felt until the year 2000." He

[1] Agreement to Establish an International Accounting Standards Committee, London, 29 June 1973, signed by the chairs of national accounting institutes in Australia, Canada, France, Germany, Japan, Mexico, Netherlands, United Kingdom and Ireland, and United States.

continued, "Don't laugh when I mention the year 2000; 25 years is nothing in the life of a great profession".

Lord Benson's prediction was remarkable, because things turned out exactly as he had predicted. Unaware of the prediction, in 2000 I was Chairman of the IOSCO Technical Committee when it endorsed the core set of International Accounting Standards.

It was that decision that legitimised the use of international accounting standards by capital markets around the world.

At the same time, the prediction was, in another way, entirely wrong. 25 years after he made that statement, of the nine founding members of the IASC, none were using the IASC's standards. That is because the approach to international accounting standards before the IASB was similar to choosing from the à la carte menu in a restaurant. The standards contained plenty of options, and different jurisdictions would pick and choose aspects of the standards they liked and to develop their own alternatives where they disagreed with the international approach. Different jurisdictions had different preferences, so international comparability went out of the window.

That is why in 2001, the leadership of the old IASC, with the support by Europe, Japan, the US and the wider world gave up on the idea of using international standards as simply a reference for domestic standards and instead set out a bold vision whereby all countries of the world would adopt verbatim the same set of international standards, known as International Financial Reporting Standards, or IFRS. In other words, à la carte was out and replaced with sophisticated cuisine of the highest order that takes the best ingredients from around the world. The part-time IASC was replaced with a full-time and well-resourced IASB, and the rest is history.

Perhaps I am taking the food analogy a little too far, even for a Frenchman! However, there is a serious point. The reality is that, given the opportunity, every IFRS jurisdiction would like to choose from the à la carte menu; to tweak the IFRS standards to better reflect local preferences or accounting traditions within their own jurisdiction—a form of nostalgia accounting.

However, the basic premise of IFRS is what rational choice theorists call a 'dilemma of collective action'. If we all work together, taking into consideration our local knowledge and expertise, to develop a single set of standards of the highest quality, and if we all commit ourselves to abide by the outcome of the standard-setting process that takes into consideration global input gained along the way, then we are all better off. Yet, if some jurisdictions—particularly the larger ones—go back to the à la carte model then we should not be surprised that others will follow. Before we know it we are back with the old IASC model and everyone loses.

Difficult and sometimes unpopular as it may be, there really is no alternative. If you want global accounting standards that offer true international comparability to investors, and you want those standards to provide a high quality, level playing field for regulators and help

companies to reduce the costs of maintaining multiple sets of books and, more importantly, you want them to reduce the cost of capital by improving the credibility of their financial statements, then everyone must commit themselves to adopt the same, single set of high quality standards.

Some have argued that the concept of a single set of global accounting standards can be approached in an informal way by the dominant economies working together to eliminate differences in their respective standards. This is an appealing concept for many. After all, who wouldn't want the benefits of global standards while maintaining national GAAP?

Unfortunately, this is a false premise. You only need to look at the IASB and the FASB's decade-long convergence programme to see the practical difficulties of expecting two or more independent boards to independently come up with the same answer. If the IASB and the FASB could not come up with the same standards for the netting of derivative contracts, and has struggled to find a common loan loss impairment model, despite years of sitting around the same board table, then what chance is there for multiple boards to independently reach the same outcome?

By the way, while I'm not involved in technicalities, as a former securities regulator I am not always comfortable with the notion of cultural specificities in the accounting field. To me these do not always seem well founded: for example, prior to the financial crisis, banks around the world were able to keep massive investments in toxic derivatives off balance sheet by circumventing a host of very specific consolidation rules. Was this a reflection of a rule-based business culture or may it have instead been simply bad accounting?

The experience of the old IASC is instructive. "Those who cannot remember the past are condemned to repeat it", said the philosopher Santayana, and his words are still true. If the accounting preferences of France, Germany and the United Kingdom could be bridged by IFRS; then why not the EU, Japan, the United States and other parts of the world?

Progress towards IFRS as global standards

The IFRS model of a single set of global accounting standards has been a remarkable success. The decision by the European Union to undertake a wholesale adoption from 2005 gave IFRS credibility and critical mass, while important decisions in this and other regions has seen the number of IFRS jurisdictions continue to swell. For example, just in the past five years alone, over 25 countries have joined the IFRS family by requiring IFRS for all or most listed companies. These include Argentina, Brazil, Canada, Chile, Israel, Korea, Mexico, Russia, Taiwan and Ukraine.

We know this because earlier this year, we published the findings of a major piece of research into the use of IFRS around the world.

Of the 81 jurisdictions researched so far, nearly all have made a public commitment to supporting a single set of high quality global accounting standards, while 85 per cent of those jurisdictions have already mandated IFRS for all or most listed companies.

Those jurisdictions made very few modifications to IFRS, and where they did, the modifications affected only a few companies and were generally regarded as temporary.

To have achieved this in such a short period of time is an astonishing accomplishment. IFRS has now become established as a globally understood language of financial reporting, and that is not going to change.

Of course, there is still work to do. There are several large economies that are yet to fully adopt our standards. In the United States, the SEC decided in 2007 to permit non-US companies to report using IFRS. Today, more than 450 Foreign Private Issuers are reporting using IFRS as issued by the IASB, representing trillions of dollars in market capitalisation. This shows that IFRS is clearly a major player in US economics today.

The SEC has been a long-term supporter of our work to develop a single set of high quality global accounting standards, but it is fair to say that progress in the US has been slower than many of us would wish. The SEC's Chief Accountant Paul Beswick has spoken about a "softer transition" or a "change over time". I think that is what we should expect in the US. It may not happen overnight, but I do believe that we will get there eventually. American investors hold trillions of dollars of securities issued by IFRS companies; and investors in IFRS countries hold trillions of dollars of securities issued by American companies. The need for comparable financial information is undeniable.

China has chosen a strategy of convergence of its standards with IFRS for all listed companies. While the Chinese had, like many countries in the EU, a lot of catching up to do—as was certainly the case for France and Germany before them—and while there remains some work to do, China has already made remarkable progress and has reached substantial convergence with IFRS.

Japan, of course, is also yet to mandate a full transition to IFRS, but the dynamics of IFRS here continue to be very strong. Japan already permits the use of IFRS. Currently, 16 of Japan's largest multinationals are using IFRS for domestic reporting. The Japanese Business Association, the Keidanren, has estimated that in the very near future that number will increase to 60 Japanese companies reporting using IFRS, representing around 20 per cent of total market capitalisation of the Japanese Stock Exchange.

The market capitalisation of these companies is expected to be in the region of 75 trillion Yen, which is 750 billion US dollars—which is larger than the total market capitalisation of markets in many other countries such as Russia and Singapore. Recently, the Nikkei and the Tokyo Stock exchange announced their intention to create a new equity index, confirming that they would consider the use of IFRS in selecting the composition of the index.

We are also delighted to have received strong policy-level backing here in Japan. The Liberal Democratic Party has set a numerical target of 300 companies to use IFRS by 2016. Recent months have seen the announcement of three policies in Japan that will greatly aid those seeking to use IFRS here. These policies are the relaxation of conditions for the voluntary use of IFRS, the creation of a new set of Japanese accounting standards similar to

IFRS and the simplification of disclosure requirements for non-consolidated financial statements under Japanese GAAP.

We are of course, delighted to see such a number of positive steps being made to increase the number of companies using IFRS in Japan. We still hope, however, that these are seen in Japan as steps towards a full transition to IFRS as the single set of global accounting standards.

Japan has a leadership role to play in these developments

So clearly, IFRS is important to Japan. But Japan's leadership is also vital to our own success. As a nation you are well represented at all levels in our organisation. The Chairman of the IFRS Monitoring Board is my good friend Masamichi Kono, Vice-Commissioner of International Affairs of the Japanese Financial Services Agency. As Chairman of the Trustees I am ably supported by my colleague Aki Fujinuma, who has served us with distinction since 2005.

Earlier this year, Joji Okada succeeded Noriaki Shimizaki as a Trustee. I am very pleased that Noriaki continues to support our work as an adviser to the Asia-Oceania office here in Tokyo.

On the Board of the IASB, Japan is ably represented by Takatsugu Ochi and the technical staff are lucky enough to include several gifted Japanese accountants, while Kazuo Yuasa ably serves as a Member of the IFRS Interpretations Committee.

Japan has also been selected as one of the founding members of the Accounting Standards Advisory Forum, or ASAF. ASAF provides an important mechanism for strengthening our co-operation with the international standard-setting community and represents only one of the ways in which we are working to create a more inclusive, multilateral approach to standard-setting.

The ASAF has now met twice face to face and once via conference call. In only six months, ASAF has become one of the IASB's most important forums for dialogue with the standard-setting community. The group allows feedback to be discussed not only with the IASB itself but with other standard setters. The end result is that participants will understand much better the competing views, while the IASB is better able to incorporate this feedback into its own deliberations. Japan's input into this process will of course be invaluable, and we fully expect to continue receiving high quality input from ASBJ through ASAF and also in informal meetings. We have long counted on your support and I very much hope that we will be able to do so for the foreseeable future.

Asia-Oceania office

Since its opening exactly one year ago, the Asia-Oceania office, our first (and indeed only) office outside London, has played a key role in promoting widespread adoption of IFRS

across the Asia-Oceania region. It fulfils a vital function, linking the developed and high-growth economies of this region into the global accounting standard-setting process.

I should express from the outset our gratitude to the Japanese Financial Accounting Standards Foundation, led by the previous President Mr Hagiwara, for its remarkable generosity in helping us to do this. We would not be here without their support. I also want to thank the current President, Mr Kama, who has taken over Mr Hagiwara's leadership and continues to support us in the Asia-Oceania region.

The office has, in its first year, helped our stakeholders in Asia-Oceania to express their views on the IASB's projects through the co-ordination of numerous outreach events in the region.

This however, is just the beginning. We fully expect that in its second year, the Asia-Oceania office will also begin to undertake its own technical standard-setting activities, such as research projects. Such research will be central to determining the IASB's agenda, and will enable the IASB to identify important areas in need of attention, with the help of regional and national standard-setters.

Under the leadership of our office Director Mitsuhiro Takemura I have no doubt that the endeavours of the office in the coming years will prove to be a great success.

Close

Ladies and gentlemen, I will now draw to a conclusion.

As the first Chairman of the IASC said, twenty-five years is not a long time in the history of a great profession. Against this backdrop, it is even more remarkable what has been achieved in the short time since the IASB began its work in 2001.

It is reassuring that nobody has opposed the G20's objective, and the governments of the G20 have recently repeated their commitment to the goal of a single set of high quality accounting standards. But there are some voices in favour of a sort of decentralised process by which national regulators would work together with a view to either converge towards international standards, or not, according to so-called national specificities and interests. They would then choose whether or not to adapt their national standards accordingly. This would be a most regrettable step backwards.

I strongly believe that we must all remain focused on the ultimate goal of a single set of high quality global accounting standards, and I believe ASAF is the place where a truly international dialogue must help us to reach this objective. I also believe that Japan can play a major role in the speeding up of this dynamic, thanks to Japan's continued leadership. We are encouraged by your recent decisions and I believe that, thanks to Japan's commitment, we are closer to our goal than ever before.

I would like to thank the Financial Accounting Standards Foundation and its stakeholders for their full and continuing support of the activities of the IFRS Foundation. We look forward to continuing our work together.