

Application of International Financial Reporting Standards (IFRS) in Japan (Summary)

This is a summary of the interim report, that was agreed upon at the meeting of the Planning and Coordination Committee of the Business Accounting Council (BAC), an advisory body to the Commissioner of the Financial Services Agency, on June 11, 2009.

Areas for consideration in deciding the potential use of IFRS

To ensure that sufficient preparations are made, which will lead to the smooth application of IFRS, it is critical that the future prospect is shown, while it may vary depending on the progress made in a number of areas, including preparations in accounting practice. Therefore, constituencies are strongly encouraged to make proactive efforts in the following areas:

i) The quality of IFRS

For IFRS to function well at each stage of the financial reporting process, it is important to ensure that IFRS appropriately reflect business practices in Japan and fairly represent the economic reality of Japanese businesses. It is also important that IFRS are sufficiently examined, taking into account current global market developments.

ii) Language in the application of IFRS

It is necessary that IFRS are appropriately translated into Japanese and an authentic Japanese translated version can be made available.

iii) Due process for and governance over setting of IFRS

It is necessary to ensure that due-process taken at the International Accounting Standards Committee Foundation (IASCF) and governance of the IASCF will be improved. Such improvement includes, among others, improved accountability

to regulators and market participants, and enhanced feedback regarding standards settings to stakeholders.

The recent decision of the IASCF to revise their Constitution in January 2009 with regard to the establishment of the Monitoring Board marked a critical starting point for the enhanced governance; thus efforts should be made so that the Monitoring Board will function as expected. It is also important that the IASCF continues steady efforts toward improvement of its governance, which include upgrading Standards Advisory Council and securing a stable source of funds-raising.

iv) Education and training of IFRS

It is important that stakeholders such as investors, preparers, auditors, regulators and academics take sufficient measures so that they can understand and utilize IFRS appropriately.

v) Involvement in setting of IFRS and governance of IASCF

In order to further improve the quality of Japanese GAAP and to increase the participation concerning the settings of IFRS, it is essential to enhance the function of the Accounting Standards Board of Japan (ASBJ) and to secure a broad-based stable source of funding to the ASBJ and the IASCF. It is important that a wide range of stakeholders, such as preparers, investors and auditors, also proactively and effectively participate in the standard setting process from an early stage, if necessary, in collaboration with foreign stakeholders.

vi) XBRL

The number of IFRS data items in the taxonomy published by the IASCF is by far smaller than that of Japanese GAAP taxonomy, and the IFRS taxonomies are not compatible with the Japanese language or the Japanese electronic reporting system (Electronic Disclosure for Investors' NETwork, or EDINET). Therefore, the IFRS taxonomies should be further developed by global efforts so that the XBRL reporting at EDINET under IFRS may be possible by the time the use of IFRS becomes mandatory, if it is decided to do so.

Optional use of IFRS

i) Scope of companies

It is appropriate that IFRS are allowed as a basis for the consolidated financial statements by listed companies whose financial or operational activities are conducted internationally. In that case, such companies are required to be sufficiently prepared for IFRS reporting. It is appropriate to decide whether to enhance the scope to include large-scale listed companies well recognized in the market, by carefully examining the developments in the setting of IFRS, etc.

ii) Parallel disclosure

For companies choosing the option to use IFRS, it is appropriate to also require disclosure of Japanese GAAP financial information corresponding to the current and previous year, in the first year of IFRS application. On an on-going basis, however, considering the costs and benefits of parallel disclosure, it would be appropriate to consider a simpler and more effective measure, including qualitative and quantitative disclosure comparing significant differences between IFRS and Japanese GAAP when applicable.

iii) IFRS for optional use

In principle, the text of IFRS for optional use should be the IFRS as promulgated by the International Accounting Standards Board (IASB).

iv) Timing

It is appropriate that the use of IFRS is allowed from the fiscal year ending in March 2010.

Mandatory use of IFRS

If it is decided to make the use of IFRS mandatory, a roadmap should be drawn with detailed steps so that stakeholders can make preparations well in advance.

i) Timing to decide the mandatory application

In deciding whether to make the use of IFRS mandatory, it is necessary to examine the progress made in tackling the issues mentioned, as well as the experience gained from the application of IFRS during the optional use period. Especially, as IFRS are under an intensive review to address the issues being revealed during the current global financial crisis, it is necessary to examine whether IFRS are of high quality and whether it could be consistently applied under future economic developments on a sustainable basis. In the meantime, the decision regarding the mandatory use of IFRS is aimed to be made around 2012, although it should be noted that the timing may be moved back or forward depending on the abovementioned situation.

ii) Scope of companies and transitions

Taking into account the benefit of promoting international comparability, it is considered to be appropriate at this stage that the mandatory use of IFRS is only applied to consolidated financial statements of listed companies. If it is decided to make the use of IFRS mandatory in the future, the transition may be made either by the “Big-Bang” approach or phase-in approach based on the size of the companies. Yet, it is important to ensure a sufficient preparation period of at least three years. (The mandatory use will start from 2015 or 2016 if the decision is made in 2012.) In addition, before making a decision on the mandatory use of IFRS, the situation of the IFRS setting process, including due process, needs to be assessed in order to decide whether to accept the text of IFRS as promulgated by the IASB or to make amendments or omissions to such text.

iii) International convergence of accounting standards

For IFRS to be applied in Japan, it is essential that Japanese GAAP and IFRS further converge, with regard to other issues in addition to existing differences, and that further progress is made concerning their practices. Therefore, stakeholders are strongly encouraged to make further efforts toward promoting the international convergence.