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GLOBAL ECONOMICAL CRISIS AND ACCOUNTANCY STANDARDS

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Abstract in original language:
Hospodářská krize odhalila nedostatky v účetních metodách používaných finančními institucemi například v spojených státech se ozývají hlasy žádající změnu metod poživených při zaúčtování nelikvidních aktiv změna metod by měla pomoci zlepšit vypovídající schopnost účetnictví . Panuje přesvědčení že účetnictví používající mark-to-market postup při zaúčtování je adekvátní v případě aktivních účtu ale je nevyhovující v případě nelikvidního trhu.

Key words in original language:
IFRS - Mezinárodní standardy účetního výkaznictví; IASB - mezinárodní výbor účetnických standardů; IAS - Mezinárodní účetní standardy; SEC - US komise obchodování s cennými papíry ; NASBA - Národní asociace státního výboru pro účetnictví; NYSSCPA - The New York státní sdružení certifikovaných účetních-

Abstract:
The crisis unveiled discrepancies within the accountancy methods used by financial institutions for example in the US there are voices calling for a change in the way the financial institutions account for illiquid assets to help stem the financial crisis. There is a believe that mark-to-market accounting is totally appropriate for tradable assets in a liquid market, however there are opinions that in illiquid market, fair value accounting is problematic.

Key words:
IFRS - International Financial Reporting Standards; IASB - International Accounting Standards Board; IAS - International Accounting Standards; SEC - U.S. Securities and Exchange Commission; NASBA - The National Association of State Boards of Accountancy; NYSSCPA - The New York State Society of Certified Public Accountants

One of the striking features of this financial crisis and of the severe global recession which it has caused is how much they have surprised us, how poor we have been at foreseeing even the short-term future.

With a few noteworthy and commendable exceptions, most apparent experts – central bankers, regulators, treasury officials, academic economists and bankers themselves – did not recognize, in the boom years up to 2007, that we were heading for disaster. Indeed the record is full of expert speeches explaining how financial innovation had dispersed the holding of credit risks and increased financial resilience. The financial institutions ignored altogether the basis of conservative approach towards lending money and started to provide loans without a sufficient guarantee,

What is surprising is how poor was our predictive ability even once we were a year into the financial crisis, in summer and autumn 2008.

Very few foresaw in early September 2008 that between 15 September and 10 October the global money market would seize up almost completely, forcing major banks across the world to rely on central bank liquidity support and government recapitalization for survival. The world seemed to change in four weeks. The financial institutions had huge amounts of money deposited in loans, stocks and other financial products which price was artificially over estimated.

Most of us have been surprised how long it has taken to restore confidence in the global banking system given the huge public interventions and the clear commitment, confirmed by action, that after Lehman Brothers no other systemically important bank or investment bank will be allowed to fail, for if the chain of bankruptcies' continued then the impact would be devastating.

The IMF World Economic Outlook of October 2008 was still forecasting 3% global growth in 2009 and a return to 4.7% to 2010: the latest forecast is a global contraction of 1.3% in 2009 and global growth of 1.9% in 2010. In October Japan was still anticipated to grow 0.5% in 2009: the forecast is now a contraction of 6.25%. We knew that the financial crisis would hit economies with large financial sectors, but most experts did not anticipate, even six months ago, how big the impact would be on global trade and on manufacturing demand and output. The crisis demonstrated the fragility of the financial institutions and uncovered many faulty practices deeply rooted in the system. The regulators in the US and EU are considering the introduction of new set of lows and regulations in order to rectify the situation.

The crisis has therefore brutally illustrated two facts which we should always have known, but which were easy to ignore in what seemed like the golden years of the Great Moderation.

First that banking systems, because they perform maturity transformation – lending long and borrowing short – depend crucially on confidence in banks and between banks, which if lost can take a long time to recover. And that the most important risks in banking are systemic not idiosyncratic: illiquidity in one bank or securitised credit market having potential impacts on the behaviour and liquidity of others, lack of confidence in one bank or securitised credit market potentially draining confidence and liquidity from others.

And second, that if the banking system is impaired huge economic loss can result. Ben Bernanke's 'Essays on the Great Depression' illustrates the pivotal role that banking system failure played, alongside the collapse in nominal demand, in creating the Great Depression. Recent IMF research illustrates that recessions which followed banking crisis were on average much deeper and longer lasting than those where banking failure was absent. And the historic lessons from crises, focused on classic on-balance sheet banking, apply perhaps even more so in a system characterized by a significant role for securitized credit. The potential for irrational exuberance and then irrational despair is inherent in all financial markets, rooted in collective action problems, principal agent relationships, and human psychology. But whereas the market economy seems able to absorb without too great harm a boom and bust in, for instance, a large element of the equity market – e.g. the internet boom of 1996 to 2001 – irrational exuberance and then reversal in the price of securitized credit held on the trading books of banks is far more disruptive.

Those lessons carry major implications for the future regulation of the banking and credit intermediation system.

The crisis faces us with two key challenges:

how best to manage the macro economy in the short term, minimizing the scale and depth of the recession; and how to create a more robust banking system for the future.

The answer to the first lies partly in macroeconomic policy, action to maintain nominal demand through fiscal policy, classic monetary policy and if necessary quantitative easing. It also requires action to accelerate the return to health of the banking system, where by health we mean not just the absence of failure, but the ability to extend sufficient credit to the real economy. That has required a mix of recapitalization, funding guarantees and tail risk insurance, informed by stress tests which deliberately consider future scenarios more severe than we expect to arise. The purpose of stress tests indeed is to inform policy decisions on bank support packages which ensure that the stress scenario never in fact occurs.

The crisis unveiled discrepancies within the accountancy methods used by financial institutions for example in the US there are voices calling for a change in the way the financial institutions account for illiquid assets to help stem the financial crisis. There is a believe that mark-to-market accounting is totally appropriate for tradable assets in a liquid market, however there are opinions that in illiquid market, fair value accounting is problematic. It is perhaps exacerbating problems Many banks blame fair value accounting, also known as mark-to-market, which requires assets be valued at market prices, for billion of dollars in write-downs on mortgage assets in the subprime crisis. But for illiquid mortgage assets, banks have to value assets at fire- sale prices in the market turmoil, but may not plan to sell the assets now and their value could grow in the future. In EU the situation differs from the US the EU has relaxed mark-to-market accounting to ease requirements for marking down investment to help banks have more healthy balance sheets.

What the European Union has done is to moderate some effects of fair value accounting in illiquid market circumstances. This is what has not been done in the US thus contributing to the current problems. The international account standards represent a factor which can in future prevent the repetition of the current crises.

Thanks to the severity and longevity of the global financial crisis, progress toward U.S. conversion with international financial reporting standards (IFRS) appears to be slowing, and support for the change seems to be cooling despite criticism that the different standards applied were the reason behind huge financial loses of the financial institutions in the US.

Some recent comments filed with the SEC protest moving forward with IFRS in the U.S. in the current economic climate.

Others noted challenges with the road map for implementation proposed last year by the SEC. The commenter's all expressed support for a single, comprehensive set of international accounting standards, but many said the SEC's proposed road map would either not further that goal, or would in fact inhibit the achievement of a global set of standards. Therefore a discussion between the relevant parties must take place in order to determine common approach and to provide a frame work in which all the parties can provide their suggestions.

These opinions surfaced after the SEC extended its comment deadline on the proposed road map until April 20. The SEC issued the road map on November 14. The proposal would set

2011 as the date for the SEC to decide whether to phase in IFRS in the U.S., with large, midsize, and small public companies adopting it in 2014, 2015, and 2016, respectively.

The Financial Accounting Standards Board and its parent organization also told the SEC to take it slow, recommending the creation of an advisory committee to study the issue.

The New York State Society of CPAs said in its comments submitted on the 5th of March that "it would be reasonable to conclude that the monetary and human capital costs of the transition to IFRS could be burdensome to entities with limited resources and prohibitive for some smaller entities, even over a period of many years."

Because of the NYSSCPA said "due consideration should be given to the ability of market participants to institute a change as costly and pervasive as the adoption of IFRS." The society recommends the SEC focus on narrowing the differences between IFRS and U.S. generally accepted accounting principles (GAAP) before moving to a decision to impose mandatory adoption. The extra cost of enforcing IFRS will present a financial burden to many companies specially the small companies, thus the financial aspect is considered as the main obstacle

Despite these comments, NYSSCPA said eligibility for early adoption should be broadened because the current plan may not facilitate ultimate adoption by all.

The SEC's road map would allow early adoption by the 20 largest U.S. companies with an international presence in their industries and who already must comport most of their financial reports in other countries with IFRS.

Several other commenter's echoed the theme of financial crisis and poor financial position of many companies, both of which could make a required IFRS conversion ill-timed.

Others pointed out that altering the timing may be enough to permit conversion to proceed. The consultancy company Ernst & Young comments indicated that it "fully supports" the proposed road map. However, the current schedule might not leave enough time for 2014 implementation by the largest companies.

E&Y suggested reducing the number of years for which companies must provide reconciliations between IFRS and U.S. GAAP prior to 2014, or consider delaying the 2014 start date for large filers if experience after 2011 shows problematic transition issues.

The National Association of State Boards of Accountancy (NASBA) stated that there may be constitutional issues for non-public companies if the U.S. adopts IFRS standards. U.S. GAAP currently applies to both public and non-public companies in the U.S. NASBA said if the SEC adopts IFRS for public companies it is unclear what will result for private companies, or non-issuers.

Financial reporting standard-setting for non-issuers is a state right, not a federal one, NASBA pointed out. "It is not likely that the states would accept the IASB (International Accounting Standards Board), a non-U.S. organization, as the one to set standards for U.S. non-issuers."

NASBA recommended that FASB and IASB should continue their convergence efforts "rather than move towards adoption of or transition to IFRS." Adopting IFRS outright could reduce FASB to a "rubber stamp" operation, NASBA said, noting that FASB and IASB have

been vital in developing high-quality financial reporting in the U.S. and "should be continued in their present roles of setting financial reporting standards for U.S. issuers and non-issuers."

A report issued by the Financial Executives International's Financial Executives Research Foundation (FERF) and Resources Global Professionals concurs that early adoption may be difficult due to road map constraints. "International Financial Reporting Standards: A Project Plan for U.S. Companies" included input by 30 U.S.-based public companies. It noted that whether the SEC decides in 2011 to make IFRS adoption mandatory will be a crucial milestone.

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