

EU-JAPAN BUSINESS DIALOGUE ROUND TABLE  
WORKING PARTY 2 ACCOUNTING AND TAX ISSUES

**WORKING PARTY 2 ACCOUNTING AND TAXATION**

**ACCOUNTING ISSUES**

**2 - E - 1**

**KEY POINTS OF RECOMMENDATIONS**

- (i) We understand that the Committee of European Securities Regulators ('CESR') has been asked to present technical advice on equivalence of IAS/IFRS and third country Generally Accepted Accounting Principles ('GAAP') and that the European Commission takes a final decision considering both CESR's advice and the actual impact on the economy. We ask that the European Commission decides after careful consideration to minimise the cost and inconvenience to users and providers of J-GAAP following receipt of CESR's final technical advice.
- (ii) In addition we ask that the European Commission makes every effort to adopt a prompt decision, well before the 1 January 2007 deadline, on the equivalence of J-GAAP.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

In our report last year we recognised the need to examine the question of equivalence between International Accounting Standards/International Financial Reporting Standards ('IAS/IFRS') and third party GAAPs and we commented that we wished to add our voice to those of other stakeholders calling for broad-based and urgent discussion of the issue. We welcome the European Commission's decision to refer the matter to CESR.

Since we reported, CESR's draft technical advice has been presented as a consultation paper. CESR found that the GAAPs of the US, Canada and Japan were equivalent to IAS/IFRS. However the advice identified four areas of significant variance between J-GAAP and IAS/IFRS. As matters stand at present, the elimination of these variances will require companies using J-GAAP in the EU after 1 January 2007 to file separate accounts for the areas in question.

**2 - E - 2**

**KEY POINTS OF RECOMMENDATIONS**

Given that the European Union's Emissions Trading Scheme ('ETS') is now in operation, we ask the European Commission to endorse widely accepted accounting rules on emissions rights.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

In advance of the introduction of ETS on 1 January 2005, the International Financial Reporting Interpretations Committee ('IFRIC') issued a draft interpretation to guide accounting treatment of emission rights.

This was not endorsed by the European Financial Reporting Advisory Group ('EFRAG'), which provides technical advice to the European Commission. Thus a new interpretation has to be presented by IFRIC.

**2 - EJ - 1**

**KEY POINTS OF RECOMMENDATIONS**

We ask that the public authorities in Japan and the European Union make steady progress towards adoption and implementation of IAS/IFRS.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

We recognise IAS/IFRS has been adopted in the EU with the exception of certain provisions in fair value accounting for financial instruments.

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We note that the Accounting Standards Council is examining how financial documents based on IAS/IFRS are positioned in terms of the Japanese legal system and look forward to early results from this important work.

**2 – EJ - 2**

**KEY POINTS OF RECOMMENDATIONS**

We ask the public authorities to observe closely the process of rule setting and revision by IASB and to have regard for the interests of companies and investors (whether European or Japanese) in the opinions they transmit to the IASB, in particular in its Performance Reporting project.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

We welcome and support the progress that has been achieved in adopting IAS/IFRS. We have registered in earlier recommendations our concern that the opinions of business users of accounting standards, as distinct from those of technical experts and standards setters, do not always appear to be as fully reflected as we should wish, and we reiterate that concern here, in view of development in discussion of Performance Reporting project.

The IASC is now reviewing its governance and we welcome efforts of the EC and the Government of Japan that published their views on such matters as due processes to set accounting standards in the IASB.

**2 – EJ – 3**

**KEY POINTS OF RECOMMENDATIONS**

Concerning research on the introduction of reports on internal control over financial reporting, we ask that both governments sufficiently discuss the function of internal control, correlating with each mechanism to improve credibility of financial reporting, such as corporate governance, audits on financial statements and oversight over companies and independent auditors.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

In Japan, introduction of management's assessment and auditors' attestation on companies' internal control over financial reporting has been discussed by the Accounting Standards Council. On the other hand, the EU proposed to adopt International Standards on Auditing (ISA) for statutory audits of financial statements and International Auditing and Assurance Standards Board (IAASB), which sets ISA, considers possibility to put reporting on internal control on its agenda.

In the US, which introduced such system earlier, while it was appreciated that reinforcement of internal control reviews contributes deterrent effect on accounting frauds to some extents, it was also pointed out that costs of compliance were far higher than anticipated. It is necessary to carefully examine the balance of benefits and costs, reflecting needs in the capital market, and deliberate attitude should be taken to introduce such mechanism.

**2 – EJ – 4**

**KEY POINTS OF RECOMMENDATIONS**

Recognising that convergence of international standards of accounting, auditing, and disclosure is an objective, we ask that the public authorities adopt mutual recognition as a short-term target on a course toward convergence in the future.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

We fully support convergence of standards of accounting, auditing, and disclosure and we recognise that this is an objective that will take some time to achieve because sufficient discussion and building consensus among participants in the market are

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necessary. To eliminate practical obstacles quickly for smooth capital financing, even at a stage that convergence is not completed, we ask that the public authorities adopt timely mutual recognition as a short-term target on a course toward convergence in the future under the condition that those standards fulfil common minimum standards.

**TAX ISSUES**

**2 – E – 3**

**KEY POINTS OF RECOMMENDATIONS**

We welcome the news that the European Commission intends to present in 2006 a Communication on the Member States bilateral tax treaties and ask that the European Commission use this opportunity to encourage the Member States to revise those treaty provisions concerned with the reduction of certain withholding taxes and to enter into common agreements with the Government of Japan in order to realise fully the benefits of the single market.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

The income tax treaty between the USA and Japan has come into effect in January 2005. The main feature of the revision is the reduction, or elimination of certain withholding taxes. We hope that it can be replicated in relations between the GOJ and the EU's Member States.

We believe that the relevant treaties between Japan and the Member States would benefit from renewal. For example, the treaties with Germany, Italy and the UK are over 30 years old. We welcome that the Netherlands and the United Kingdom have started to negotiate with Japanese tax authorities to revise their tax treaties in 2004.

We recognise that the Member States and not the Commission decide taxation. We ask the Commission to take whatever steps it can to invite the Member States to ensure that there is consistency between new treaties they may agree with the GOJ. The integrity of the single market would be damaged if there were to be significant differences between Member States' treatments of withholding taxes.

**2 – J – 1**

**KEY POINTS OF RECOMMENDATIONS**

We ask that the government of Japan quickly reform the consolidated tax system, allowing the carrying forward of tax losses in subsidiaries incurred before the system came into effect, exempting revaluation of subsidiaries at the initiation, and allowing tax deduction of transfers between consolidated entities.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

We believe that the GOJ should reform the system because discriminatory treatments of consolidated taxation remain though the 2% surtax was abolished.

**2 – J – 2**

**KEY POINTS OF RECOMMENDATIONS**

In order to promote mutual investment between the EU and Japan, the BDRT asks the Government of Japan to reduce or eliminate certain withholding taxes.

**ADDITIONAL INFORMATION IN SUPPORT OF RECOMMENDATIONS**

Last year we noted that the Governments of Japan and the USA reached agreement in November 2003 to revise the income tax treaty between their two countries with the intention of reducing or eliminating certain withholding taxes. We welcomed this decision and hoped that it could be replicated in relations between the GOJ and the EU's Member States. We repeat this request.