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THE ACCOUNTING PROFESSION IN ASIA -- WHERE WE ARE TODAY AND WHERE WE WILL BE IN THE YEAR 2000

by

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What I am going to talk about tonight is Obsolescence: obsolescence of human beings; obsolescence of me; and obsolescence of yourself unless, and it is a big unless, you pay attention to my coming recommendations to "go international."

I will be talking about the environment we are in based on the thesis that the emergence of the economy in Asia Pacific is going to result in the growth of sophistication in that part of the world which will have a significant impact on their accounting profession. Of even greater interest to the people here tonight is that I believe it is going to have a great impact on the United States economy and on the United States accounting profession. Consequently, not doing anything about it will not be an option available to the people in the room tonight. You will either have to take up the challenge with regard to developments in the Asia Pacific area that impacts us, or you will lose.

If that sounds a little somber, I hope it does sound that way. It is one way I hope to get your attention this evening.

The subsections of what I am going to talk about are:

1. Where did the accounting profession come from?
2. What is happening in the Asia Pacific area that makes these developments worthwhile reviewing?
3. I will give you a little tour of the Asia Pacific area dealing with the economies there and how they interact with the accounting profession in that part of the world.
4. Finally, I will be bold enough to make a few predictions on where I think it will impact the United States.

Evolution of Accounting Profession

With regard to the accounting profession, it started in Italy with the double entry bookkeeping system. From there we can trace it to Scotland and the emergence of the excellence of the Scottish Institute of Chartered Accountants. From Scotland we go to England and from England to the colonies. Since the United States is one of the colonies, it leads to the influence on the United States. Great advancement in the US. profession came in the 1930's because of the recession and the legislation enacted that dealt

with accounting-related issues.

History now becomes important when you look at the Far East. If you look at countries like Hong Kong, Malaysia, and Singapore you have accounting professions that really have copied what was going on in the United Kingdom.

In the case of Japan, Korea and Taiwan (because of the economic influence of the United States) you also have a heavy influence in those countries with regard to the United States accounting profession. But if the United States and the United Kingdom have had such a significant impact on those countries should there be any real differences between what we are familiar with and the accounting profession in the Far East? The answer is "Yes."

The reason is the transportation of the accounting profession from the U.K. and the U.S. to the Far East was not perfect. The question that really comes to mind is: "Are there any human factors which perhaps make what goes on in the United States not transportable intact to the Asia Pacific accounting profession?" The answer comes in part from the economic developments in the Far East.

What Is Going On In Asia Pacific?

The recent edition of the "Financial Times" talks about the economic growth in the Far East. That newspaper is saying that the Mediterranean is history, the Atlantic Ocean is "now," but the Pacific Ocean is the future. Why is that? The reason is economies have gone from being based on commodities to the industrial society of manufacturing, and then on to the information society. That development has happened at a time when information has become a strategic asset. Why is that important? It is important for a country -- like Japan -- that has no real natural resources except its people. It is a country which, for every logical reason in the old days, could not obtain the position it has in the world today. It was little other than a pile of rocks, if you will, but the "people factor" positions them to be where they are today. Countries are no longer dependent so much on iron ore and similar natural resources. Information is now an important natural resource.

Another important economic development is the "triad" between London, New York, and Tokyo. From a financial center standpoint, the shift to Japan has come about for a simple reason. What do you think Japan is doing with all the money it gets from selling automobiles to the United States? They take it back to Japan and what do they do with it? Kenichi Ohmae of McKenzie and Company in Japan has written a book called "Triad Power." In that book he has traced what happens to the flow of money.

Japan cannot consume all the cash it receives from selling those automobiles, video cassette recorders and similar products; rather, since it is one of the high savings countries of the world, it sends this money back to the United States to companies who borrow. As a result, Japanese flow of cash to the United States is one of the reasons why the U.S. interest rates are so low. This is an over simplification of what is actually going on, but it does make a point. The point is that Japan is a financial center just because it is processing so much of the liquidity on a global basis.

Another economic factor is our interdependence. We talk about the fact that there are global products. When I have a chance to discuss the Far East issue, I generally put on a screen a picture of Michael Jackson with a Japanese face. I say "This is the real Michael Jackson." Everyone laughs and shakes their head "no." The fact of the matter is there is no country I have ever spoken in where the audience does not know Michael Jackson. He is an international commodity and, as a result, presents in a way the fact that there-is emerging a global economy. There is emerging an environment in which you product plan for Asia as well as North America, as well as Latin America, as well as Europe. You cannot be a competitor in the international environment unless you do so.

This interdependence and global product creation come smack against a people situation where the cultures are different. You have different people trying to accommodate themselves to this global

environment. That makes for a real change even though the world is trying to homogenize its products.

One last matter from an economic standpoint is Robotics. I visited a factory in Japan some time ago where robots made robots. Someone has said, "It is funny when robots sweep up behind humans, but it is less funny when humans sweep up behind robots." However, because of economic developments in the Far East, the question is becoming "What will be the use of the human being?" This is a very unnerving development in today's world.

The conclusion that you can draw is that there will always be a need for human beings because, even in historical terms, rationality has enabled the human being to protect itself from larger animals over the centuries. There will be a demand for quality of people but perhaps not for quantity. As someone has said, "If you are a country like China these days, it may not be a good century in which to get caught with a billion extra people." The ability to challenge or create an environment for those people is becoming-more difficult.

Impact On The Accounting Profession

This sets a background which says the Asia Pacific area is emerging in a sophisticated way and that sophistication is going to involve very energized human beings. It is rising in an environment where globality will dominate and the ability to shut out other people from your environment will become much more difficult. Does this mean for the accounting profession? One of the things that it should mean is we are in need of a common accounting language, I've had the privilege to study and work under Professors Briloff and Saxe; we've all looked for that rationalization of accounting concepts. However, I wouldn't hold my breath until it happens. We are still dealing with an environment where the movement of information across borders is happening in a way which is not yet at the stage where the Tower of Babel -- from an accounting standpoint -- has been brought to an irreducible minimum.

Another element we are finding is the cultural difference of people in the accounting profession. The audit function entails asking questions, challenging and inquiring -- not from the standpoint of the other person not telling the truth -- but just saying "I have an obligation as an independent person to make an inquisition and as a result from that, a judgment."

In the 1950s and 1960s when several Big 8 accounting firms sent American auditors to Japan, there was a great deal of difficulty in getting American type auditors functioning within the Japanese environment. The Japanese were not used to the inquiry that goes with American-type auditing. To be more specific, when a younger auditor from a U.S. firm was told that the answer he received from a superior didn't make sense (and he had to go back out and re-ask the question) the very thought of a young person challenging someone old enough to be his father was quite traumatic. For that reason, the cultural differences in Asia relating to the accounting profession challenge the people.

The environment is certainly different than that in the United States. In the accounting profession in many countries the relationship between the client and the accounting firm, between the accounting firm and the public, and between the client and the Ministry of Finance (i.e. government) tends to be quite different than that in Japan.

In some countries, there is limitation on the accounting profession. There are two basic reasons:

1. The accounting profession is not looked at in some countries as being important.
2. It is considered to be important but there are limitations on the extent of their obligations should the results of the clients' business be deficient.

Another difference is the relevance of the new move of accounting firms to the Far East. I have mentioned the United States/United Kingdom base for the Far East. But if you take the situation like SGV (a very large Philippine-based accounting firm) and its recent merger with Arthur Andersen, it

reflects an intention on the part of Arthur Andersen to develop a distribution system in that part of the world. This movement of people into the Asia Pacific area is dramatically changing the accounting profession.

Tour of Asia Pacific

Earlier I had promised a tour of Asia Pacific. Let me review a couple of countries in Asia which I have selected because they represent different points of view from an accounting profession standpoint.

Let's start with Hong Kong. This is a country that would have the greatest amount of UK influence. Over time, however, that has changed from a political as well as economic standpoint. It is a country where the "old boy" network mentioned in the Clavel book "Noble House" has been pre-eminent. But that is true not only in the writing of novels but also in the performance of business. The accounting profession is well respected in Hong Kong.

But Hong Kong is now a country at the crossroads of its existence. It has been in existence for a long period of time, but is only now beginning a formalized continuing professional education program and monitoring it. In the case of Hong Kong, we have a country which will be blending with the People's Republic of China. I see it as illustrating a situation where its accounting profession will have to be reconstructed dramatically. What is the future look for the people of Hong Kong? The answer is: the mainland. So let us take a look at China itself.

China has an imbalance of its population and the accounting profession with a population of one billion people and approximately only one thousand qualified accountants!

With the political upheaval in the past many professionals such as doctors, lawyers and accountants had to do labor in the fields. This puts the country in a position where they don't really have an accounting profession of great strength at this time. What is the significance of this factor?

If you look at a country this size in 1986 environment, how do you start an accounting profession? They are starting with the idea of lower level finance people in China studying with non-Chinese people and then returning to China and sit for their examinations. One element in this environment then becomes "Who do you have that can sit for the examination?". China is trying to tap into the technology of the western world. They view it as being transferable to the people in China. That is an experiment worth watching because Chinese people are very hard working and this work ethic should enable them to stimulate a transfer of technology from the western world to China.

The China solution is not to bring in U.S. or U.K. type of people. They are going to develop their own kind of accounting profession. This is producing certain difficulties, although I think they are short term, i.e., one or two decades. The difficulty stems from the joint ventures between Chinese created organizations and American firms or Swiss firms or Japanese firms. These are needed due to the type of accounting services that the companies in China do not perform but which are provided by hundreds of thousands of people in the global accounting profession today. It will be interesting to see to what extent joint venturing between the eastern world and the western world will develop.

Now let's go from China to a country that's much smaller -- Singapore. What is happening in Singapore is the development of the accounting profession very closely tied in with its economic environment. Singapore is a country that has enjoyed growth always close to 7, 8 or 9 percent in real terms every year. However, the recent recession hit them quite badly. As a result there emerged a tremendous price competition with regard to accountants in Singapore, as well as other businesses. The result of that price competition has been stress at the foundation of the accounting profession in Singapore. That profession is world class because of the high quality of people in the profession. However, when that kind of talent is placed into tight fee situations, it presents problems. What we see in Singapore today is a profession that has not yet been able to cope with free competition -- and I wouldn't exclude United States on that

statement. What has happened in the short term is an attempt at peer review. That's worth noticing because the idea of one accounting firm reviewing another accounting firm is a significant development whose time has not yet come in all of Asia. Singapore, at least, is trying to make a start at it.

Let's now take a look at Korea. It presents another point of view. While it is not as small as Singapore nor as old as Hong Kong nor as big as China, the thing that makes Korea different is the way clients are obtained by the accounting firms. The Ministry of Finance has imposed a point system whereby for every CPA on your staff you get a certain number of points. Then with these points added up for your firm, you are able to allocate to them in the process of obtaining clients, i.e. each client is worth a certain number of points. This is certainly dissimilar to what we have in the United States, but what it does do is give the Ministry of Finance some control of the distribution of clients among the accounting firms. Basically, the MOF wants the distribution to be of such a nature that it does not lead to aggressive price competition. It stands for quality of accounting service to clients and for that one has to give them credit. It is intended to spread the talent in the accounting profession over a range of clients and not allow any one accounting firm to get a dominant position in the accounting market.

Moving from Korea, let us take a look at Japan. Japan is a most sophisticated business environment today. If you look at this week's magazine, "The Economist," it shows a picture of a large Samurai looking at a little Uncle Sam with the caption saying, "I am richer than you are." What do you think the accounting profession is like in Japan? Is it a profession quite like that in the United States because our economies are similar in terms of sophistication? Or is it a situation like China that's just getting started with a thousand people? Let me give you a few statistics. To become a CPA in Japan you have to pass three sets of examinations. The passing rate on the first exam is a fairly high 70%. However, the passing rate on the second exam is lower — 10%, and finally in the third examination the passing rate is only 20%. Consequently, after squeezing that many people through that many examinations you wind up with a profession that consists of only about 8,000 CPAs, only adding about 300 new CPAs to the accounting profession every year.

How would you like to be the recruiting person for these people? If you think of a profession of the type we have in the United States, the comparison with the Japanese profession is staggering. In 1948 the AICPA was created but it was only in 1966 that the Ministry of Finance created a mechanism called "Audit Corporation." They had stepped back and looked at the accounting profession in the early 1960s and, because of the things I was describing, they saw if we were ever going to have a good size profession in Japan they had to create mass. They had to generate some bigger accounting organizations because up to 1966 the audits of even the largest Japanese companies were done by sole practitioner CPAs. It was a personal appointment. However, when one client amounts to a substantial percentage of the income of the CPA, the matter of independence becomes important. The issue at that point in time in Japan was the question "what are they trying to accomplish?" In the context of what the CPA is required to do, they have a commercial code in Japan that requires all financial statements to be reported on by an examiner. That's the good news. However, he need not be independent and in many cases that individual may even be an employee of the company! As a result the Ministry of Finance has now created requirements that certain size companies (500 billion yen and above) have to be audited by an audit corporation or at least the auditor of the firm has to be assisted by an audit corporation.

They are still not completely in good shape yet because the audit corporations themselves, in many cases, are an aggregation of what we would call sole proprietorships in the United States. The situation in the United States was like this years ago but the firms now are more homogeneous. In the Japanese environment the identification of a client with an individual partner (and staff in the firm with that partner) is still a very close one. In fact, in the case of some of the major Japanese audit corporations little swapping of staff among different partners takes place. They do share the central costs of running the firm, but there is still a great amount of individuality among the partners in the audit corporations in Japan.

Consequently, in painting a picture of the profession in one of the major economies of the world today,

we have a profession at a different level of sophistication than what we find in the United States. But what will the impact be of these points I have mentioned about Japan on the United States. I think there are several and they provide challenges for people in this room.

Predictions for the Future

First, I predict that accounting professions in the Far East are going to reflect the protectionism we are seeing in the economies of the world today. Psychologically, we have not recovered (and I am including the United States in that statement) from the 1973-74 recession. One can be very outward going, very international in thinking when you don't have to worry so much about what the other person's products are going to do to your environment. I think that the United States as a country has responded poorly to the international challenges that emerged after the recession. It remains to be seen whether, as a country, we will respond to that challenge in a more mature way or just circle the wagons, hold on until the year 2000, and try to conduct "business as usual."

There is a sentiment in the United States of that nature. What I am saying in different words is that there will be reflected in the accounting profession in the Asia Pacific area protectionism in the accounting profession if we start with protectionism from the business environment as a whole.

For example, why can't a U.S. CPA become a CPA in Japan? Why can't a US. CPA become one of the celebrated 1,000 in China? Why don't they let us take the CPA exam? The answer might very well be, "Fine, how would you like to have millions of new CPAs in the state of California?" Why don't we swap CPA certificates? When it becomes a question of expanding the CPA certificates in the United States, we get a little less charitable, we are a little less willing to give certificates to non-U.S. people. There is one challenge for the United States coming from Asia Pacific.

Secondly, I predict the accounting professions in these Asian countries are going to become much more significant once they are able to assimilate the technology whether it be from the United States, the United Kingdom, Canada, Germany or wherever. These countries have a chance to build very strong national professions that are very clearly Korean, Chinese or Japanese in nature. For that reason the human element I spoke about earlier becomes quite important.

I have written an article for "International Management" in which I discussed the question of what was going to happen to the influx into the United States of the Oriental population. I think it is just great! The European movement to the United States over 100 years ago has made the United States great. If you see a Korean person or a Vietnamese person or a Chinese person catching up to you in the US. economy, the advice I give is that you are going to have to train harder and run faster. The basic result of my article was a question: "Can we beat Japan?" The answer I gave was "Yes" because our Japanese are going to be better than their Japanese! I believe the United States is going to attract the best Oriental people, will train them and will assimilate them into the American environment. We will change them and they will change us. But I think we can provide an environment for them to make the United States grow. The globalism I was talking about earlier will be a thing the United States can use as a competitive advantage for upgrading our population.

I also predict that, from an accounting profession standpoint, we have to expect the United States to begin more and more to accept audits of non-U.S. accounting firms. I don't mean lowering standards; I mean they will be upgrading their performance. I would bet that the SEC will realize that the quality of work done in some of the environments I have been talking about will be of such quality that there would be no reason not to accept it other than for purely protectionism reasons. This will provide us with a challenge in the American accounting profession. If we cannot meet the competition then we don't deserve to win.

Next I see in the Far East a continuation of the control of the accounting profession by the government or some public sector element. I would prefer to see it in the private sector but my crystal ball does not

go out that far. There is nothing to say it has to be in the private sector.

I believe there are certain advantages the Chinese have for making an outstanding accounting profession. They are extremely patient people. At a recent meeting I had with a Korean gentleman, he indicated that compared to the Chinese, the Koreans and Japanese are not patient at all; nor are the Americans. The Chinese are willing to wait a longer period of time. Their timeframe is certainly longer than the United States. If you keep in mind that the Chinese were eating from dishes when the Americans were still swinging from trees it should put our histories in perspective. The last couple of centuries in China are just snapshots in terms of what I am talking about. The Chinese are people to be admired because of their industry. I think they are also ones who can provide significant competition in the accounting profession sign-in the Asia Pacific area.

Finally, the globalism that I talked about in terms of global products and global people is the development in Asia that will happen quicker than it happened in the North American and South American continents. By globalism I don't mean U.S. companies going to Asia. We are beyond those days when the large accounting firms in the United States and the U.K. sent people out to the Far East to teach people how to audit. We are beyond the stage where you have to have residents there from outside the country in order to run that accounting practice. This globalism really means that, given the fact that there is no time difference in reality between information that relays from London to New York to Tokyo, the financial markets of the world have become one. In the banking business, there is a person in one of the major New York-based commercial banks who has indicated that banking is no longer the obtaining of funds at a certain cost and lending it on with a mark up margin. He indicated that there is practically no space between the time I know I can get money at 9% and the person to whom I would lend it knows it can be obtained at 9%. What does this mean? It means that information compresses the time factor for the movement of physical things and even the movement of liquidity. It means that financial services, with banks being financial advisors, have provided sophisticated value added services which are now going to be a most important activity in the Asia Pacific area. Banks are not going to be movers of assets; they are going to be financial consultants.

A Final Thought

With this tour of the Asia Pacific area I'd like to leave you with one idea on how to find out what is going to happen in the future. Go to California. We tend to sit in New York feeling we are in the center of international business; however, California is an interesting part of the world. Friends of mine from Asia Pacific and Europe look at California to give clues as to what is going on in the minds of people in the United States as a country. There is a lot of experimentation in California. The different things that they do give clues as to what will be going on in the United States in the future. I think for your success you have to pay attention to Asia and as part of that process I think the Asian influence in California give us an opportunity to get a microscopic view of the way the United States is going and the way Asia is going.

If what I have said tonight is confusing you a bit, I am glad. Asia Pacific is not neat and tidy and structured and organized. It is a hodge-podge of different and sometimes conflicting movements; but that is the real world! If at any time you feel that it is getting too complicated for you to think about and you want to go back to the "good old days," I strongly urge you to resist that feeling! I don't think that is an option you will have available because as I have mentioned earlier, if you want to vegetate and behave like machines, you have to remember the admonition I made earlier! The robots are coming!

