The Global CFO

By Ramona Dzinkowski

In the past two years, American CFOs have been faced with more change, greater complexity, and arguably more stress than in any other period of U.S. history. Sarbanes-Oxley has seen to that. But for CFOs outside the U.S., the world has also become an increasingly complicated place. While the European Union remains intensely focused on meeting the requirements of accounting standards harmonization in 2005, the pressure of international convergence in markets, currencies, and business practices around the globe continues to change the way companies operate both at home and outside their traditional borders.

Last October, more than 300 CFOs from 22 countries gathered at the Palazzo Corsini in Florence, Italy, for the 35th World Congress of the International Association of Financial Executives Institutes (IAFEI). The IAFEI represents more than 32,000 senior financial executives around the world. Not surprisingly, the agenda was weighted toward concerns over globalization, the pressing issues surrounding accounting standards harmonization and adoption in the EU, and last, but certainly not least, how CFOs are coping with complexity in a converging business environment.

A VIEW FROM TOKYO

One of the key issues on the table was the role of the U.S. in the world economy and its influence on setting business standards in foreign markets. According to Toyoo Gyohten, president of the Japan Association for CFOs, president of the Institute for International Monetary Affairs, and senior advisor to the Bank of Tokyo-Mitsubishi Ltd., the "western" model may not be the best approach in a diverse world. His general assumption was that convergence to western business models will lead to more efficient and effective world markets, and most would agree. Yet he also noted that this model hasn't always produced the best results—witness Enron, WorldCom, and others. In his words:

"It cannot be denied that a certain amount of efficiency will be obtained when there is free competition in pursuit of maximum profit; however, there is no assurance that it can do that while containing the explosion of unbridled greed. It is true that many corrective measures have been planned and implemented to stop the scandals. But there is hardly any evidence that the correction has been completed. In all markets in the world, there is a recognition that a single effort to converge to a crude form of capitalistic market will not produce the best result."

Under these circumstances, Gyohten suggests, the structure of local markets and the regulations that govern them should be uniquely suited to the national cultural, political, and business environment they serve. At the same time, he also recognizes that doing business internationally—moreover, raising money on international capital markets—is highly dependent on the free flow of information and a common basis for understanding the underlying economic realities of the firm, regardless of country of origin. Furthermore, it's the public's demand for information that is both changing and unifying global business practices. He explains:

"Today, thanks to sophisticated information technology, all taxpayers, workers, shareholders, and consumers can enjoy access to the same information internationally and globally. Naturally this enhances the people's demand for greater transparency and accountability. It has forced a fundamental change in political and corporate management. Political leaders and corporate CEOs can no longer maintain their authority by way of monopolizing information as their predecessors used to do. They have to establish their authority on the basis of transparency and accountability. This is globalization."

This is the crux of the debate. In order to meet the demands of transparency and accountability, should there be one system of doing business, with common market structures, business cultures, and corporate governance rules and standards? Alternatively, should we strive for international diversity based upon existing business cultures, practices, and political and market structures? It's true that efficient capital markets will attract investors. But it's also true that, thus far, the diversity of nations has helped define their competitive advantages and hence their ability to compete in global markets.

For CFOs outside the U.S., the issue becomes what impact convergence will have on the competitive capabilities of their organizations. What will happen if their countries resist this trend, and what new strengths and weakness will be uncovered in the process?

These aren't easy questions to answer, particularly when there are other and arguably more pressing issues that will have a sudden and direct impact on a company's financial statements—namely, the convergence of international accounting standards.

TROUBLE IN THE EU

This brings us to the second major issue on the table at the Congress—accounting convergence.

The panel discussion of experts headed up by Alberto Giussani, senior partner at PricewaterhouseCoopers, member of the Advisory Committee of the International Accounting Standards Board (IASB), and professor of economics at the Catholic University of Milan, showed that as CFOs in Europe approach the 11th hour for adopting the International Standards for Financial Reporting (ISFR), many problems and concerns remain. Here are a few of them.

Comparability and Taxation: First, in brief, the ISFR will likely pertain only to consolidated accounts (as opposed to individual accounts) for the foreseeable future due to the tax implications of using ISFR for individual accounts. This limits the comparability aspect of the standards. Furthermore, since applying ISFR to individual accounts would require countries to revise and harmonize their tax systems, comparability is likely to be a long way off.

Language: Second, there is a significant language issue. The ISFR have to be translated from English into the local languages of the EU countries. Giussani explained:

"These international standards are designed and written in English, but sometimes not in plain English but, rather, in very complicated English. Fortunately, the IASB has recently deliberated that in the future they will use plain English rather than a Shakespearean one, which will become easier. But with the accession of 10 new countries, the number of languages will increase dramatically. All these standards need to be published concurrently in all the official languages of the enlarged EU. This means that the time for having these standards available in each language will greatly expand."

Also related to the language problem is the fact that until the standards are translated into the language of the local courts, they aren't likely to be considered legally valid.

EU Endorsement: Third is the issue of EU endorsement. The EU has reserved the right to endorse all of these standards when they are published in the languages of the EU countries. This again means a time lag. There is also the issue of partial endorsement, which is particularly relevant in the case of International Accounting Standard (IAS) 39, "Financial Instruments: Recognition and Measurement." Partial endorsement suggests that companies may describe compliance and noncompliance in different ways, and this will ultimately have implications for the language used in the auditors' report.

Principles vs. Rules: Fourth, the complexity of the ISFR and the detailed implementation guidance has called into question whether or not the standards move accounting in the EU from the principles-based system on which it was established, to a U.S.-style rules-based system and all the problems associated with it.

Producers of Accounting Standards Are Prolific: Another concern is the frequency and sheer volume of amendments being made to the standards as well as the number of corresponding interpretations. In addition to the amount of administrative work this causes for companies, when the IAS replace the local GAAP, the constant changes to the rules will have a dramatic impact on tax planning.

SURVIVING GLOBALIZATION THE ITALIAN WAY

Meanwhile, in addition to the challenges of converging business models and harmonized accounting standards, CFOs still have to face unique business pressures within their own companies. In one of the last sessions of the Congress, the delegates were introduced to a company that has to completely rethink the way it does business in order to compete in the current and evolving global market—Fiat.

Fiat Group of Italy has been fighting its way through a prolonged period of internal economic and political chaos. The magnitude of its financial losses over the past six years is overshadowed only by the astonishing rate at which it loses CEOs. In the past 30 months, Fiat has seen five CEOs come and go. With dismal results exacerbated by a revolving door to the executive suite, the company is in a state of emergency.

Fiat's latest CEO, Sergio Marchionne, a Canadian/Italian chartered accountant (CA) and lawyer, is determined to steer the company through these complicated times. He says, "Fiat is in a very delicate period of transition from a rather vast industrial conglomerate of the 1990s to a group that is becoming much more focused on the automotive business as a way of life."

The structural problems endemic to the company are perhaps the greatest threat to its survival and to the survival of others like it. Notes Marchionne, "Fiat is an inward-looking organization. It does not assess itself in comparative terms. But, more fundamentally, I don't think it looks at the marketplace as the gauge by which success should be determined. For whatever reason, it lost its commitment to operational excellence. It is not a well-run organization today. It's improving, but it's not well run and is truly complex. The role of the centre and the way in which it interacts with the field is unclear, and, perhaps more importantly, it's very slow. It does not move fast enough, it does not react to market demand fast enough. Fiat doesn't adjust to the vagaries of the market in the way in which our competitors do."

Marchionne's strategy for survival reflects the impacts of globalization on companies around the world who have had to re-examine their raison d'etre under pressures to survive. He explains:

"The advantage we gain in our economic system just means increased competition from the other side. Whatever advantage we gain is incredibly short lived. If this is true, then the way in which you run and manage businesses has to drastically change. This issue of turbulence is a key issue that faces not only Fiat but faces every other type of concern in the world. It is a permanent factor in the way in which resources get allocated, and it is the only way in which we can legitimize the concept of competition within the organization. We can't focus on sustainable competitive advantage because that's going to be competed away. You need to be able to change your stamina in the marketplace at an increasing rate. That is fundamentally a big shift from broad plans that delineate strategic intent going forward five years. You know the minute that you issue them the marketplace has changed so drastically that you're going to have to reallocate resources in order to meet the market shift."

THERE'S HOPE

The 35th World Congress of IAFEI ended on a note of optimism and increased understanding of the complexities facing organizations today. It also became clear that CFOs everywhere wanted to ensure that their companies could uphold a standard of excellence in financial management and reporting that would allow them access to the resources in capital markets around the world. At the same time, all agreed, there are many challenges ahead. ■

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