Chapter VI

Korea's New Accounting Standards and its Impact on APEC

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1. Introduction

Starting in FY1999, Korea implemented the new corporate accounting standards. Because most major companies in Korea begin their fiscal year on January 1st, most commercial transactions after that date will be recorded under the new standards. The new procedures are a part of the corporate accounting system reform associated with Korea's acceptance of IMF rescue funds. This study aims to show what led Korea to reform its corporate accounting standards and the impact the change has had on related sectors. This study also tries to show the impact Korea's new accounting standards will have on other APEC members and the APEC process. The rest of the paper is organized as follows: Section 1 surveys the change in Korea's corporate accounting standards. Section 2 shows reactions of related sectors---government, firms and accountants---to the change. Section 3 considers the relationship between Korea's new accounting standards and the APEC process. The last section summarizes and concludes.

2. Korea's New Corporate Accounting Standards

2.1 IMF Conditionalities

In November of 1997, to avoid a possible national default caused by a sudden decrease in foreign exchange holdings, Korea applied for emergency loans from the IMF and the World Bank. The IMF approved a line of credit totaling about 21 billion

Table 1 Agreements between the Korean Government and IMF
(Initial Letter of Intent dated December 3, 1997)

Size of Financial Support	･More than 55 billion US dollars---IMF $ 21billion, World Bank $ 10 billion, ADB $ 4 billion, Japan $ 10 billion, United States $ 5 billion, United Kingdom + France + Germany + Canada + Australia $ 5 billion).
Macro-economy	･Growth rate: 3% in 1998. ･Inflation rate: 5% in 1998. ･Tight monetary control. ･Current Deficit: Below 1% of GDP (about $5billion). ･Public Finance: Balanced, or a slight deficit.
Monetary Policy	･Maintain a flexible exchange rate policy (de facto acceptance of the won's depreciation). ･Close troubled financial institutions, especially 9 merchant banks. ･Pass financial sector reform bills to help develop independence of Bank of Korea and consolidate supervision of all banks. ･Allow mergers and acquisitions of financial institutions by foreigners and 100% participation for merchant banks. ･Develop a disposal plan for two distressed banks, Cheil Bank and Seoul Bank. ･Inject public funds into the recoverable institutions. ･Reform accounting standards, disclosure rules, and prudential standards according to international best practices. ･Respect the commercial orientation of bank lending---eliminate government intervention in banks' lending policy.
Corporate Governance	･Develop trade liberalization and improve the import certification procedures. ･Allow a maximum of 55% foreign ownership for listed companies by the end of 1998. ･Liberalize firms' direct foreign borrowing. ･Reform accounting standards, disclosure rules, and prudential standards according to international best practices. ･Eliminate directed lending and rescuing of individual corporations. ･Maintain the "real-name" financial transaction system. ･Create measures that encourage restructuring corporate finances (reduce high debt-equity ratio corporations, develop domestic capital markets, and change the system of cross guarantees within conglomerates).
Others	･Expand the Employment Insurance System. ･Publish and disseminate data on foreign debt and foreign exchange reserves. ･Do not impose further foreign exchange controls. ･Open the IMF Seoul office for quarterly quantitative performance monitoring.

Source: Government of the Republic of Korea, Letter of Intent submitted to IMF, December 3, 1997.

US dollars, and other international financial institutions, such as the World Bank, approved about 14 billion US dollars. Major developed economies also declared financial support for Korea, and the amount of the declared credit line totaled more than 23 billion US dollars. Including the financial support approved by international financial institutions, the total size of the international financial support for Korea amounted to 58.3 billion US dollars (See **Table 1**). This amounted to 13% of Korea's GDP in 1997.

As for the IMF loans, the total amount of the Fund's commitment far exceeded the credit line of the reserve tranche and the credit tranche set for Korea, and the government applied for structural adjustment loans (SAL). Under this scheme, the beneficiary is subject to strict and extensive macro economic control. The World Bank's structural adjustment loan requires similarly tight control. The requirements imposed by the IMF are often called "IMF conditionalities." **Table 1** summarizes the initial IMF conditionalities imposed on Korea, as expressed in the first letter of intent submitted from the Korean government to the IMF.

The ultimate goal of the IMF's tight economic control is to reduce the current account deficit and consequently improve the foreign exchange reserve position. The IMF conditionalities for Korea are broadly classified into the following four categories: macroeconomic controls, financial sector reform, corporate governance reform, and reform in other areas. The contractionary macroeconomic controls are meant to serve as an immediate way of shrinking imports by decreasing domestic demand. As shown in **Table 1**, the GDP growth rate would be capped at 3% in 1998. This was quite a reduction for Korea compared with its high growth performance until then, which had averaged about 7% per year.

However, for the middle- and long-term stabilization of the economy, more structural, rather than technical, remedies have long been called for. In this regard, the rest of the conditionalities---financial sector reform, corporate governance reform, etc---are more important than macroeconomic policies for sustained growth. These reforms were expected to serve as substantial medication on the Korean economy's chronic problems---the economy's strong tendency to hold excess production capacity as a result of the unsound financial sector and the cross debt guarantee[1] practice within chaebols (big conglomerates). Improving corporate accounting standards was one of the most important reform measures in the IMF conditionalities. It was mentioned both in the financial sector reform and in the corporate governance sections. It became compulsory for Korea to improve its corporate accounting standards according to the international best practice to enhance the transparency of the financial sector and the corporate sector, especially chaebols.

2.2. Background leading up to the Changes in Accounting Standards

Regulated Financial Sector, Chaebols, and Excess Capacity

The Korean financial sector has overwhelmingly been under the control of the government. In 1961, the Park Chung-hee administration nationalized major banks. Throughout his reign, using policy lending through the banks, the government promoted strategic industries of the time. In this process, there was no need for the banks to screen the lending projects by themselves, nor serious need to consider profitability of the banking business. Such attitudes still remain in the financial sector.

As for the chaebols' side, the problem was their intrinsic desire for "self-augmentation." They competed with other chaebols in terms of sales, production, etc. Until recently, the chaebols' best policy was to draw funds from banks as much as possible because procuring funds bound chaebols' activities. Hence, chaebols made full use of the cross debt guarantee practice between the affiliates of an individual conglomerate. This practice enabled an unprofitable chaebol subsidiary to borrow a huge amount of funds backed by debt guarantees of fellow subsidiaries.

The self-augmenting of chaebols and the lack of screening capability in the banking sector combined to create a loose lending practice for chaebol investment projects. If a chaebol firm applied for bank loans claiming that the firm was going to launch or expand their projects related to the government's industrial promotion policy, banks almost automatically offered funds. They assumed that the government would

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[1] According to Financial Supervisory Commission (February 10, 1999), the total amount of the top five Chaebols was 21.4 trillion won (approximately 17 billion US dollars). This figure totaled about 4.8% of the year's GDP.

subsidize, explicitly or implicitly, and the conglomerate would repay if the indebted subsidiary bankrupt. This led to excess production capacity in the national economy as a whole and eventually ignited the economic crisis.

Loose Accounting Standards and the Korean Economy's Chronic Problems

What role did accounting standards play in Korea's past economic growth? On the chaebols' side, loose regulations dealing with the consolidated financial statements of corporate groups hindered external inspections of a chaebol's financial condition. For chaebols, the primary reason for the intra-group manipulations, such as cross debt guarantee practices and intra-group transactions, was to expand the external size of themselves and to arbitrarily relocate profits. However, at the same time, external inspections concerning the real profitability of a chaebol became more and more difficult as the network of intra-group manipulation became more complicated.

Broadly speaking, inadequate corporate accounting systems created four major obstacles for external analysts trying to explore the real profitability of a chaebol. Firstly, as mentioned above, the coverage of the old consolidated financial statements was only limited. Consolidated financial statements were mandatory only for certain share-holding companies[2], and any natural person, such as "the owner" of a chaebol, was exempt from reporting consolidated financial statements. Secondly, even though consolidated information was partially available, intra-group transactions and investments were not presented in a matrix form. Forming an analysis matrix for a chaebol required analysts to use a considerable effort. Of course, very often, part of the consolidated information was missing because of the incomplete coverage of consolidated financial statements. Thirdly, financial statements that chaebol firms submitted did not necessarily reflect the truth. In the past many chaebol firms selected auditors from ex-workers or other individuals related to the chaebol. Even when an external audit was performed, the client firms' interest influenced the audit results reported by accounting firms. Fourthly, the historical value principle on asset

[2] Under the old standards, a share-holding company with more than a 50% share or the biggest share-holding company with more than a 30% share are obliged to report consolidated financial statements. If a natural person held a large share of a company, he or his group was not obliged to report consolidated financial statements.

evaluation under the old corporate accounting standards caused the accumulation of historical losses. This applied to both chaebols and the financial sector. Because of this, for example, failures in investment projects could carry over to consecutive years, or plunges in the firm's asset value (such as real estate) or potential increases in debt (such as debt expressed in foreign currencies) were not immediately reflected in financial statements. All these hindered external analysts from issuing early warnings about the possibility of firms going bankruptcy,[3] such as the chaebol bankruptcies of Kia and Hanbo. Also, the lack of transparency in banks' financial state might have led to rapid capital withdrawal from Korea in the 4th quarter of 1997.

2.3. Outline of the New Corporate Accounting Standards

In reaction to the agreement with the IMF, the Korean government started to revise its corporate accounting standards. The final goal of the reform is to increase the welfare of the investors by disseminating corporate finance information in Korea. The reform is quite drastic, and the procedure is now under way. The main elements of the new accounting standards are as follows: (1) introduce the combined financial statements to corporate groups, especially chaebols; (2) require market value evaluation of assets and debts in the term-end; and (3) restrict individual firms from changing their accounting policies. All these amendments went into effect January 1st, 1999. Also, they are consistent with International Accounting Standards (IAS) 27 and other international best practice[4]. See **Table 2** for a summary of the new corporate accounting standards.

The combined financial statements[5] are expected to serve as a powerful tool to reveal the real value and profitability of each chaebol. The combined financial

[3] The government shares the view that the lack of information about chaebols led to a series of large bankruptcies. See Korea Institute of Certified Public Accountants (November 1998).

[4] Kwon Tae-il, Deputy vice President, Security Supervisory Board, commented about the amended Standards for Corporate Accounting Standards, "These new standards are some of the most strict in the world." (*Hangug Gyeonjae Shinmun*, December 12,1998)

[5] Combined financial statements consist of the following: combined balance sheet, combined income statement, and combined cash flow statement. Groups obligated to report combined financial statements have to report the statements for the current year and the previous year.

Table 2. Major Changes in Korea's Corporate Accounting Standards

Items	**Old standard**	**New standard**	**Effect on firms**
Foreign Exchange Conversion Loss or Gain	Depreciation for various budget years.	Depreciation in the current budget year only.	Net profit (loss) may vary more due to foreign exchange factors.
Payment Guarantee by Financial Institutions	Allowances are not necessary.	Allowances are mandatory.	May lead to decreases in equity capital of banks, security brokers, merchant banking corporations (*ch'onghab geumyung sa*), and insurance companies.
Evaluation loss of the Share in the Security Market Stabilization Fund	Out of balance.	In balance.	May lead to a decrease in equity capital of security brokers.
Asset Evaluation	Based on historical value.	Based on market value, revised every term-end.	Expected to impede parent companies' support of subsidiaries through real estate transactions.
Derivatives	Contents are disclosed in footnotes.	Reflected directly in income statements.	Net profit (loss) may fluctuate more.
Investment Securities	Historical value evaluation is possible.	Reflect net profit (loss) of the stock-issuing firms.	Net profit (loss) will vary more for stock-holding firms with many subsidiaries.
Change in Accounting Policy	Permitted.	Strictly restricted.	Impede arbitrary adjustment of net profit.
Loss in Sales Credit	Disposed by decreasing assets only.	Partly reflected by increasing debts.	Debt-equity ratio will increase.
*Financial Statements for Corporate Groups	Consolidated Statements (may not cover all affiliates of a chaebol)	Combined Statements (wider coverage, to be reported by a chaebol)	Need to expose a grand view of a chaebol.
*Intra-group Balances and Transactions	Transactions within a chaebol may be counted multiple times.	Intra-group transactions are eliminated in the combined financial statements. Details are disclosed in footnotes.	Shrinking a chaebol affiliate's external size, and blocking arbitrary transfers of profit between chaebol subsidiaries.

Remarks: An asterisk (*) indicates that the item is pertinent to the renewed Standards for the Combined Financial Statements, which was promulgated from the Securities and Futures Commission on October 21, 1998. Other items are pertinent to the renewed Corporate Accounting Standards promulgated from the Financial Supervisory Commission on December 11, 1998.
Sources: Authors' compilation using Hanguk Gyeung-jae Shinmun(12/12/1998) and Korean Institute of Certified Public Accountants (November 1998).

statements are based on the Standards for the Combined Financial Statements promulgated on October 21, 1998. Under the new Standards, a corporate group ultimately controlled by one person must report the combined financial statement for the group. In reality, such corporate groups refer to chaebols. Under the old Standards, as mentioned above, because of the narrow definition of the control over a corporate group, many chaebol firms were not subject to consolidation. In the new Standard, the definition of a controlled corporate group corresponds with the official definition of a chaebol, which is 30 major conglomerates annually appointed by the Fair Trade Commission, based on Article 21, Enforcement Order of Monopoly Regulation and Fair Trade Act. The new Standards require a corporate group to disclose information about all domestic and foreign affiliates that are under its effective control, once the group has been officially designated as a chaebol. Assuming that the chaebol affiliates under common control form a single economic entity, all the intra-group transactions and balances are canceled out, and the combined statements identify the amount of transactions and balances solely with firms outside of the chaebol. Also, intra-group transactions and balances, such as ownership interests, cross debt guarantees, intra-group borrowings, and intra-group sales, are footnoted under the new Standards.

The amended Corporate Accounting Standards, promulgated on December 11, 1998 regulate the market value principle of asset and debt evaluation. As mentioned above, under the old Standards which used the historical value principle, any unrealized loss or gain might not be reflected in the financial statements, and because of this, it was not easy for external analysts to estimate the present value and profitability of a firm. Under the new Standards, a reporting firm shall re-evaluate all the major assets and debts at market value and record re-evaluation losses or gains accordingly. Specifically, the new Standards will more clearly show the impact of a firm’s debt denominated in foreign currencies and real estate holdings on the firms’ financial position. Thus, the market value principle enables external analysts, specifically domestic banks and foreign investors, to better estimate the ability of a firm to make payments. This principle and the requirements of the combined financial statements for chaebols combine to display the present value and profitability of a chaebol as a whole.

The amended Corporate Accounting Standards also regulates the strict restriction on firms' changing their accounting policies. This regulation implies that it becomes difficult for firms, especially chaebol affiliates, to transfer profits and losses between them as a part of chaebol-wide profit manipulation. Also, this restriction is expected to enhance the consistency and comparability of financial statements, and it will eventually facilitate investors.

2.4. Problems with the New Accounting Standards

The combined financial statements reported from a chaebol will provide useful information on the chaebol. However, the new Standards are not necessarily beneficial in all occasions. Broadly speaking, the new Standards have two major loopholes.

Firstly, the Standards for Combined Financial Statements include a waiver clause for reporting with combined financial statements. Section 7-B-1 of the new Standards waives the combined financial statements requirement if one subset of a corporate group whose controlling company is obligated to report the consolidated financial statements represents 80 percent of the total group assets. In other words, if the existing consolidated financial statements cover substantial part (80%+) of a chaebol, the chaebol is free from reporting with combined financial statements, which require more information to be disclosed.

Secondly, government appointment of chaebols possibly changes year by year. Legally, chaebols are defined as the top-30 conglomerates in terms of total assets. Therefore, small conglomerates are sometimes appointed as chaebols, but sometimes not. This means that the continuity of the accounting information can be violated for small chaebols. With the progress of the "big deal" (industry exchange between chaebols as a part of 'firm-value revitalization' campaign), we can expect that the total assets of an individual conglomerate to fluctuate quite largely.

Nevertheless, it is too early to judge whether or not the new Standards are invalid because of the loopholes. We need to observe how many of the top-30 chaebols report with a combined financial report respecting the sprit of the new Standards. Some chaebols do not want to reveal the information reported on the combined financial statements, but some chaebols may not mind disclosing more information to external analysts. Also, we need to observe how much damage the discontinuity of the combined financial statements for small conglomerates will bring about. Larger conglomerates, such as the top-five conglomerates, will probably stay in the top 30 chaebols. Therefore, the main benefit of the combined financial statements will probably be maintained, regardless of small conglomerates' yearly entry into and exit from the number of appointed chaebols.

3. Is Korea Ready for the New Accounting Standards? ---Reaction of Related Sectors---

Theoretically speaking, the drastic reform to Korea's corporate accounting standards will bring about some gains, especially on the investors' side. In Korea, it was almost a consensus that improved accounting standards would bring about benefits to the economy. For example, it would lower external borrowing rates, increase inward investment flows, etc. However, in reality, not all the economic entities welcomed the drastic change in the corporate accounting standards. This was partly because the accounting standards reform was carried out with short notice and only after the introduction of IMF funds in late 1997. The accounting standards reform even bothered those who faced a harsh competition---Korean firms competing with other countries for foreign investment and Korean accountants competing with foreign accountants for domestic clients. The following sub-sections introduce the reaction of major related sectors---government, firms, and accountants[6].

3.1. Government

In the process of implementing the corporate accounting standards reform, the government consistently played a central role. The Securities and Futures Commission took the initiative to form the Standards for the Combined Financial Statements. For the Standards for Corporate Accounting Standards, the Security Supervisory Board was mainly in charge of the revising work. In the process, they also maintained close contact with the Fair Trade Commission, which is in charge of

[6] The description in sub-sections 2.1-3 is based on interviews the author conducted in Seoul in December of 1998.

monitoring chaebols' monopolistic behavior. Officially speaking, their attitude toward the new Standards was, naturally, quite positive. They stressed the merits of introducing new and improved Standards that would increase information disclosure and decrease the financial costs of Korean firms through increased capital inflow. They also insisted that greater financial information about firms would help issue early warnings against large bankruptcies.

However, we need to remember that the government itself did not originally initiate the reform. A major part of the reform came about only after the introduction of the IMF funds. When the amended Corporate Accounting Standards passed the Financial Supervisory Commission on December 11, 1998, young accountants affiliated with the Security Supervisory Board anonymously said in relief, "If Korea hadn't received the emergency IMF funds, the quick and thorough change in accounting standards would have been impossible" (Hangug Gyeongje Shinmun 12/12/98). This type of comment clearly shows that IMF conditionalities were the most powerful driving force in the reform process.

3.2. Firms

The new corporate accounting standards require firms, especially chaebol affiliates, to report financial statements according to the international best practice. However, at least when the authors made a research trip to Korea in December 1998, it seemed that firms were not really ready for the drastic change in corporate accounting standards.

The new Standards came into effect with the start of the fiscal year of 1999. Because most Korean firms start their fiscal year on January 1st, this implies that most firms had to start recording transactions and evaluating assets and debts using the new standards since January 1st, 1999 . However, the Standards for Combined Financial Statements and the amended Corporate Accounting Standards were not promulgated until October and December, 1998, respectively. Firms complained that they were not given sufficient time to prepare for replacing their internal accounting systems. According to an interview with a mid-level corporate group, the group planned to record the transactions using its current system for the first several months of FY 1999; and thereafter, the group will start recording the transactions using the new accounting system compatible with the new accounting standards. Also, by the end of FY 1999, the group needs to convert huge amounts of transaction records from the old standards to those compatible with the new standards. Considering the fact that the current economic crisis severely hit most of the chaebols, the cost of replacing their accounting systems is not negligible.

Firms admitted that disclosure might improve borrowing rates for financially healthy firms. However, in reality very few healthy firms exist, in terms of international standards, in Korea. Instead, they are worried about the adverse impacts the market value principle in asset and debt evaluation will have on their profit figures. Currently, Korean firms are experiencing difficult times due to three major factors brought about by the economic crisis---the plunges in foreign exchange rates[7] and real estate prices, and a higher rate of bankruptcy. The devaluation considerably increases the won-denominated figure of external debts[8]; the plunge in real estate prices and high rate of corporate bankruptcy potentially decrease the value of assets. The market valuation principle forces Korean firms to directly reflect such negative impacts on their financial statements for FY 1999. Firms worry that revealing “the truth” will scare foreign investors away and that fund raising would become even more difficult.

3.3. Accountants

One accountant interviewed during the authors’ research trip said accountants did not welcome the new Standards very much. The reason was simple; their income would not increase very much compared with the complicated work necessary after the introduction of the new Standards. Accountant’s fees, as he projected, would not rise remarkably mainly because of competition with foreign accountants. The current accounting reform is pertinent to internationalizing the domestic standards, and many thought the profitability of the domestic audit market might be taken away by foreign accountants. Regarding external audits of financial institutions, Section 28 of Korea’s

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[7] The average won exchange rate for 1998 was 1401 won per U.S. dollar. This was about a 43% devaluation compared with the average in 1996.

[8] The total external liabilities as of January 31, 1999 was 57.25 billion U.S. dollars for the domestic banks and 41.17 billion U.S. dollars for the domestic non-banking sectors. For details, see Ministry of Finance and Economy (March 19, 1999). The compound private external liabilities corresponded to about 31% of the total GDP in 1998.

initial Letter of Intent to the IMF clearly stated, "Financial statements of large financial institutions will be audited by internationally recognized firms.[9]" This statement seemed to affect the accountants' client companies, and the domestic audit market has gradually consolidated into several influential accounting firms.

4. Accounting Standards Reform and its Implication to the APEC Process

So far, we have surveyed the recent reform in Korea's corporate accounting standards. Although some of the economic entities are not ready to transition to the new accounting standards, many admit that improving the standards will enhance Korea's economic welfare in the long run. As mentioned above, benefits from Korea's accounting standards reform will possibly come from facilitating trade and investment.

The Facilitation of trade and investment along with liberalization is an ultimate goal of APEC as well. This section considers the relationship between Korea's introduction of new corporate accounting standards and its implications on the APEC process.

4.1. Alignment of Standards in APEC-TILF

The APEC Osaka Action Agenda (OAA) set out 14 areas in which the member economies should make efforts to improve trade and investment liberalization and facilitation (TILF). **Table 3** lists these 14 APEC-TILF components. The Committee for Trade and Investment (CTI) carries out the APEC-TILF. The Committee also has corresponding TILF sub-committees under it. In 1996, member economies unilaterally announced their individual action plans (IAPs) on liberalization and facilitation, and member economies revise IAPs and review[10] their implementation once a year. Individual members can decide the pace of liberalization and facilitation

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[9] According to the Ministry of Finance and Economy (December 1998), the Financial Supervisory Commission was going to select domestic accounting firms which maintained cooperation with influential foreign accounting houses. And the Committee was going to appoint them as "internationally recognized accounting firms," which could audit large Korean financial institutions.

[10] Several attempts have been made to externally evaluate IAPs and their implementation. One example

Table 3. APEC-TILF Components

1. Tariffs
2. Non-Tariff Measures
3. Services
4. Investment
5. Standard and Conformance
6. Customs Procedures
7. Intellectual Property Rights
8. Competition Policy
9. Government Procurement
10. Deregulation
11. Rules of Origin
12. Dispute Mediation
13. Mobility of Business People
14. Implementation of the Uruguay Round Outcomes

expressed in the IAP, considering its domestic and external circumstances. Among the 14 APEC-TILF components, the reform to accounting standards will have the closest relationship with the standard and conformance area.

The principal objectives of the Sub-Committee for Standard and Conformance (SCSC) are to[11]:

(1) encourage alignment of members' standards with international standards;

(2) achieve mutual recognition among APEC economies of conformity assessment in regulated and voluntary sectors;

(3) promote cooperation for technical infrastructure development in order to facilitate broad participation in mutual recognition arrangements in both regulated and voluntary sectors; and

(4) ensure the transparency of the standards and conformity assessments of APEC economies.

SCSC works mainly in primary and secondary industries. Specifically, it has worked on manufacturing standards and agricultural products standards. Also member countries will work on a certain service-industry-related areas, such as mutual recognition of medical standards[12].

4.2. Possibility of Including Accounting Standards Reform into APEC-SCSC

The activity of the APEC-SCSC has not covered financial or monetary systems, and has been rather centered in manufacturing related areas. Accounting standards

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is Yamazawa (1997).

11 Refer to the SCSC web page at http://www.apecsec.org.sg/committee/standards.html

12 Japan will give foreign manufacturers of pharmaceuticals and medical devices opportunities to state their opinions in the relevant councils in 1999. Also, the range of acceptable foreign clinical test data for pharmaceuticals was expanded in August 1998. See Ministry of Foreign Affairs, Japan (1998).

have not been covered, either. However, is it relevant to include accounting standards in the APEC-SCSC activities? The authors think it is possible and advisable.

Harmonization of certain financial or monetary systems will possibly induce a large amount of friction or resistance from the concerned groups. For example, harmonization or alignment of currency systems, like currency unification into the EURO in the EU, will not proceed smoothly. This is partly because these types of adjustments touch upon the identity or sovereignty of a nation. Also, in APEC's context, such harmonization or alignment will often bind members, and this conflicts with the non-binding principle of APEC. However, harmonizing accounting systems may not conflict with the non-binding principle as much as other financial and monetary harmonization.

One example of worldwide harmonization in the financial area can be found in the laws on checks and bills. In the 1930s, major countries of the time agreed to harmonize their domestic laws on checks and bills. Related to the activities of APEC-SCSC, as we saw, the liberalization and facilitation activities gradually expand into services and related sectors. Also, APEC-ECOTECH (Economic and Technical Cooperation) deals with standards of a service sector[13].

Specifically, how relevant was Korea's introduction of new corporate accounting standards? When we compare Korea's accounting standards reform and the four objectives of APEC-SCSC, we know that Korea's reform conforms significantly to the APEC-SCSC objectives.

Harmonization to the international standard and transparency are the central objectives of Korea's accounting standards reform. Korea's reform fulfills the mutual recognition goal, at least partially. Internationalizing the Korean corporate accounting standards will facilitate circulation of Korean firms' financial statements in developed economies. Technical cooperation is under way, and Korea is accepting foreign (mainly American) accountants to deal with the internationalized audit system---especially for large financial institutions.

4.3. Applicability of Accounting Standards Reform to Other APEC members

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13 APEC-ECOTECH has a project titled "Vocational Teacher Standards and the Formulating Method," proposed by China and handled by APEC-HRDWG (Human Resource Development Working Group). Details about the project can be obtained from the following web site.
http://www.apecsec.org.sg/scsc/scsc.html

In the process of Korea's corporate accounting standards reform, domestic economic entities did not accelerate Korea's quick and drastic reform. Instead, external interests, such as the IMF, generated the momentum for the reform process. Korea's widespread unpreparedness to the transition of the accounting system widely observed in Korea by and large stemmed from the rash due to the IMF conditionalities.

However, on the other hand, harmonized accounting standards will possibly enhance trade and investment. The financial statements prepared in accordance with international standards will raise the international credibility of the reporting firms, and consequently help increase international trade. Similarly, enhanced credibility of the reporting firms through improved financial statements will possibly increase both inward FDI and portfolio investment. It also may avoid panic-stricken capital flight. All these will serve to stabilize the economy. The relative magnitude of benefits from reforms would be larger for small economies, especially for developing economies that have more room for reform. Avoiding capital flight would be especially appealing, considering the Asian economic crisis spread widely and quickly partly because of a lack of credibility in banking sectors etc. And it should be added that the concerted action by various countries would generate a synergy effect.

Therefore, to fully benefit from improving the corporate accounting standards, countries should proceed with reforms primarily according to their own agenda. But, at the same time, they should consider the possible synergy effect brought about by the collective action by multiple countries. In this situation, they should recall the concerted unilateralism principle of APEC.

If member countries worry about internal friction raised from the accounting system reform, including accounting standards in the APEC process would help. In the APEC process, the reform pledge becomes international, but it is still non-binding.

5. Summary and Conclusion

In reaction to the IMF conditionalities, Korea quickly and drastically reformed its corporate accounting standards by the end of 1998. Korea's new standards are now among the most strict set of standards in the world. This drastic change took place as part of corporate governance reform, which especially targeted reforming chaebols and improving the credibility of Korean financial institutions. The corporate accounting standards reform consists of, among others, the following three main elements: (1) the combined financial statements will have wider coverage than the existing consolidated statements, (2) firms will use the principle of market value to evaluate assets and debts, and (3) it will prohibit firms from arbitrary changing important accounting policies. These reforms try to remedy the shortcomings brought about by chaebols---such as over-expansion through cross-debt guarantee practices. Although several loopholes exist (such as the 80% rule for consolidated financial statements) in the current reform, the reforms will create substantial long-term benefits.

Economic entities seemed unprepared, and those which faced harsh competition seemed rather embarrassed at the change in the corporate accounting standards. Firms worried about the cost of transitioning and the overreacting of investors caused by the additional disclosures required under the new standards. Accountants also faced international competition because the government plans to call on internationally recognized accounting firms to audit large financial institutions.

Considering the side effects of Korea’s rushed transition to meet the standards and the possible long-term gain due to improved accounting standards, it is advisable to include accounting standards reform in the APEC process. Specifically, APEC-SCSC should expand its scope to include accounting standards. In the APEC-wide work of improving the accounting standards of member countries, they should recall the APEC principle of concerted unilateralism. By doing so, member countries can proceed with reforms according to their own agenda, but at the same time the pledge to improve the accounting system becomes international, which can pressure countries to implement the reform processes. Also, APEC activities dealing with accounting standards should be carried out in the close coordination with other international bodies concerned with accounting standards, such as the International Accounting Standards Committee (IASC).

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