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Next-generation EDINET and XBRL disclosure of material facts

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Executive Summary



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Japan's FSA plans to initiate XBRL disclosure of material facts that significantly influence investment decisions in addition to financial information that helps investors evaluate companies more efficiently. If this initiative is expanded to include Tokyo Stock Exchange TDnet timely disclosures it should contribute to improving market participants' operating efficiency and enhancing the Japanese equity market's transparency.

Disclosure of material facts that influence investment decisions

Investors primarily use financial information to evaluate companies, but they must also take into consideration corporate events of a magnitude sufficient to influence investment decisions. Examples of such events include equity offerings, acquisitions, and top-management personnel changes. Such information is defined by Article 166 of the Financial Instruments and Exchange Act (FIEA) as material facts that significantly influence investors' investment decisions. Put differently, the release of information about such material facts is likely to trigger an immediate share price reaction. Insiders are therefore prohibited from trading their companies' securities prior to the announcement of such information. Another important consideration for investors is the timing of their receipt of such information.

Such information is currently disclosed via the TDnet and EDINET disclosure systems respectively operated by the Tokyo Stock Exchange (TSE) and Financial Services Agency (FSA).

As defined by the FIEA, material facts are classified into several categories, including management decisions (e.g., dividend payments, equity issuance, stock buybacks, stock splits, stock swaps, stock transfers, mergers, business divestments, spinoffs, dissolutions), events (e.g., disasters, changes in major shareholders' shareholdings), and information on financial results. Disclosure of such material facts or tender-offer information via TDnet is deemed to constitute public disclosure. Listed companies consequently use TDnet to disclose such

information. Accordingly, financial results and other reports are submitted to TDnet before EDINET in compliance with stock exchange rules. Information on material facts is thus available first on TDnet. Additionally, the TSE requires timely disclosure of events that it defines as material to investors. Its definition of material events is broader than the FIEA's definition. Meanwhile, the FSA requires EDINET filings of extraordinary reports, securities offering registration statements, and notifications and reports related to tender offers by not only listed companies but also private companies¹⁾. For example, companies are required to file extraordinary reports in the event of changes in major shareholders' shareholdings, initiation or resolution of litigation, material disasters, and changes in external auditor or corporate officers.

NOTE

1) In addition to listed companies, private companies with 1,000 or more shareholders also are required to file security reports on EDINET.

Information material to investors

On TDnet, hundreds of material facts are disclosed every day, but they are disclosed in PDF files in a format similar to a press release. Unlike financial results, such information releases are unscheduled. They are consequently very difficult to continuously monitor.

When companies with large market capitalizations or heavily traded stocks disclose material facts, the disclosures tend to be reported in the media, but smaller companies' disclosures do not necessarily receive detailed media coverage. Additionally, disclosure of material facts is subject to a materiality threshold. In some cases, disclosure is not required if information's anticipated impact is deemed to be insignificant.

However, the standards by which the law and media judge materiality do not necessarily coincide with investors' materiality standards. For companies not covered in the media, investors must directly search for information on TDnet and/or EDINET and check corporate press releases for information that may be material to their investment decisions but not deemed a material fact. Such information gathering imposes a heavy burden on investors that own many stocks or invest in mid- and small-cap companies about which information is not readily accessible.

Next-generation EDINET

2) From June 25, 2012, the FSA's website was soliciting public comments on an EDINET system upgrade scheduled to take place in fiscal 2013. The scope of information subject to XBRL disclosure is slated to be enlarged in conjunction with the upgrade.

3) XBRL: eXtensible Business Reporting Language

4) Tags are character strings used to mark up documents in HTML, XML and other languages. Being an XML dialect, XBRL has tags for financial statement accounts. The tags convey the meaning of the account names.

5) English labels are one XBRL product. Tags have both English and Japanese labels. Users' computer systems can be configured to display report element titles in English.

6) A taxonomy (electronic template) is an XBRL file that defines reports' structure and the hierarchical relationship among financial statement accounts.

EDINET is scheduled to be upgraded in fiscal 2013²⁾. The FSA published proposed specifications for the upgraded system and solicited public comments on them during a one-month period from June 25, 2012. While the FSA currently requires XBRL³⁾ disclosure of only securities reports and other documents related to financial results, it plans to expand the scope of XBRL disclosure to documents disclosing material facts, including large-shareholding ownership reports, extraordinary reports, and filings related to tender offers.

Extraordinary reports are required to be filed when any of 34 statutorily prescribed events occurs as material facts. According to the proposal on which the FSA solicited public comments, XBRL tags⁴⁾ will be used to enable investors to identify the reason for extraordinary reports' filing without looking at the content of a PDF or other file. If English labels⁵⁾ are used, overseas institutional investors also would be able to ascertain the nature of the event that has occurred.

Future disclosure infrastructure's potential

Like EDINET, TDnet has since 2008 required financial statements in companies' earnings digests to be prepared in XBRL format. For this purpose, the TSE requires companies to use the XBRL taxonomy⁶⁾ issued by the FSA. Accordingly, even though companies' earnings digests released via TDnet and securities reports released via EDINET are prepared in different formats, users can access financial information as data using the same taxonomy. Users are conveniently able to initially obtain data when earnings digests are released and later obtain more complete data when the securities report is released.

If the scope of TDnet's XBRL disclosure is expanded to include not only existing earnings digests but also material facts and other information subject to timely disclosure requirements, disclosure information would be comprehensively available in data format through TDnet and EDINET combined. TDnet data on material facts could also be used by brokerages to check for insider buying or selling, and by asset management companies' back offices as a source of information on corporate actions.

Corporate action information is being converted to XBRL overseas. Most notably,

the US Depository Trust & Clearing Corporation (DTCC) has recently started to apply XBRL to corporate action information for ADRs (American depository receipts) after conducting a pilot test in 2011.

From a big-picture standpoint, expansion of XBRL disclosure to encompass material facts would not only improve market participants' operating efficiency but also greatly help Japan's equity market to increase transparency and gain trust from overseas.

The FSA will revise its XBRL taxonomy when launching its next-generation EDINET. TDnet will consequently require some type of system upgrade if it is to continue to use the FSA's taxonomy. As of July 31, 2012, the TSE had yet to announce whether it will adopt the same taxonomy as the next-generation EDINET. However, if the TSE upgrades its TDnet system to incorporate the FSA's updated taxonomy, the upgrade may be a good opportunity to expand the scope of TDnet's XBRL disclosure to include material facts and other such information. Even if the TSE does not upgrade TDnet in time to coincide with the EDINET upgrade, concerned parties should discuss this issue and improve the Tokyo market's infrastructure to boost confidence in the market.

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