

Roadmap to Future Mandatory Application of International Financial Reporting Standards (IFRS) in Japan From the Perspectives of Financial Statement Preparers*

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This paper seeks to contribute to the discussion on the future mandatory application of International Financial Reporting Standards (IFRS) using data from a questionnaire-based survey administered to financial statement preparers, that is, management in Japan. The important findings of this paper are as follows. The majority of Japanese companies consider that the domestic markets are more important than overseas markets; the most important differences between IFRS and Japanese standards are goodwill, comprehensive income, and the recognition of revenue; it is expected that IFRS would be applied only in consolidated financial statements or in both consolidated and parent companies' separate financial statements; and the lack of legislation making it mandatory is the main reason why IFRS has not been adopted by Japanese companies. Overall, this paper found that Japanese management is prudent and passive regarding IFRS adoption, leaving room for further discussions on the future mandatory application of IFRS in Japan.

Keywords: International Financial Reporting Standards (IFRS), Japanese Generally Accepted Accounting Principles (GAAP), convergence

Introduction

The current research attempts to investigate issues concerning the adoption of International Accounting Standards (IAS) or International Financial Reporting Standards (IFRS) from the perspectives of financial statement preparers.

The "Interim Report: Application of International Financial Reporting Standards (IFRS) in Japan" (the "Interim IFRS Roadmap") was published on June 30 (described in Section 3), which was based on the exposure draft published on February 4, 2009. After investing efforts for 10 years on producing high-quality accounting standards that reflect the Japanese way of conducting business and the exploration of ways to converge with global financial reporting standards, Japan has apparently taken a critical step forward towards adopting IFRS.

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The main points of the report concern the voluntary adoption of IFRS in consolidated financial statements, starting with the fiscal year ending on March 31, 2010, for “companies with global financial/operating activities” and the possibility of mandatory application of IFRS in Japan.

As we know, the approach to achieving a single set of global accounting standards is two-pronged: adoption and convergence. Japan and the US have been regarded as examples of convergence countries. However, the Interim IFRS Roadmap indicates a future approach where IFRS can be used and Japan would adopt IFRS in some manner in the future. Therefore, the issuance of the initial IFRS draft roadmap would signify far-reaching regulatory changes that would require some important issues be considered and dealt with. For example, before the final decision on mandatory adoption is made, questions such as whether to adopt IFRS in both consolidated financial statements and non-consolidated financial statements or in consolidated financial statements alone, what kinds of companies should be required to prepare financial statements in compliance with IFRS, what are the incentives for and obstacles preventing companies from implementing IFRS, and other related questions should be answered on the basis of a comprehensive investigation. Since these issues are very pertinent for financial statement preparers, it is relevant to explore their understanding of IFRS and their opinions regarding the adoption of IFRS and the preparations for its application.

The authors conducted a survey investigating leading Japanese companies’ views on the IFRS application before the publication of the initial IFRS roadmap, when Japan was deliberating over convergence and adoption. The authors aimed to provide evidence for or against the adoption of IFRS from the perspective of financial statement preparers. However, the result of the survey is also relevant at this time because it refers to the issues proposed in the Interim IFRS Roadmap. The result of the survey is expected to provide implications for setting future standards regarding the mandatory application of IFRS and to provide evidence for establishing, training, and supporting the program with regard to the application of IFRS in Japanese companies.

Section 2 first introduces the context for Japan’s move towards IFRS adoption to indicate the importance of strategic structuring of an accounting system based on a comprehensive understanding of the situation of Japanese companies and their accounting contexts. Section 3 specifies the significance of the Interim IFRS Roadmap and important issues concerning adoption that is to be considered. Section 4 considers the most important influential factors that affect the accounting practices of Japanese companies, the features of Japanese accounting, and the differences between IFRS and Japanese Generally Accepted Accounting Principles (GAAP) that have a direct bearing on the problems concerning the application of IFRS in Japanese companies. Section 5, based on the analysis in Sections 3 and 4, investigates Japanese managers’ opinions on issues concerning IFRS application and the perceived proper way of application. Finally, Section 6 identifies some problems facing companies and provides concluding remarks.

Background: Accounting Development Towards Adoption

Since 1997, the Japanese government had decided on the basic policy regarding the Japanese Financial Big Bang in an attempt to sweep away the lack of transparency that was said to characterize the Tokyo market and to improve its globalization by constantly focusing on global standards instead of domestic logic. In the following decade, Japan extensively reformed its accounting system and commercial code to achieve international standards, well known as the “Accounting Big Bang.” Although with these reforms, Japanese accounting became quite similar to the IAS/IFRS, some differences in specific accounting standards continue to exist.

However, since there was no clear strategy for structuring the accounting system, the regulator's opinion regarding IAS/IFRS adoption kept changing. In 2002 and 2003, the Japanese Financial Services Agency, Ministry of Justice, and Nippon Keidanren¹ expressed negative opinions regarding the adoption of IAS/IFRS. In contrast, there appeared an international trend of convergence with IAS/IFRS during the same period and this trend spread. On October 29, 2002, the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) jointly issued a memorandum of understanding which formalized their commitments to the convergence of the US and IAS. Moreover, during the following year, that is, 2005, which might be seen as the beginning of a new era for financial reporting, IAS and IFRS were adopted in European Union (EU) countries. In keeping with this trend, in March 2005, a joint project on the convergence of Japanese GAAP and IFRS was established in Japan to analyze and discuss the equivalence of Japanese GAAP and IFRS (Koga & Rimmel, 2007). Nippon Keidanren changed its opinion in favor of convergence with IAS in 2006, three years after it expressed a negative opinion regarding adoption. However, there was still no real progress. In 2007, with the publication of the US Securities and Exchange Commission's (2007a; 2007b) concept release on allowing US issuers to prepare financial statements in accordance with IFRS (the concept release) and its proposal, acceptance from foreign private issuers of financial statements prepared in accordance with IFRS without reconciliation to US GAAP, Japan found itself falling behind in the global trend. Therefore, generally speaking, after the Big Bang, Japan seemed to lag behind its European and US counterparts in converging with IAS/IFRS. The changing opinion of the regulator was apparently owing to the external influences of international trends and the lack of a strategy based on the comprehensive understanding of the state of Japanese companies and their accounting environments.

The Publication of the Interim IFRS Roadmap

A major step towards Japan's adoption of IFRS is the publication of the "Interim IFRS Roadmap" which indicates that the attitude of the Financial Services Agency (FSA) towards the adoption of IFRS is positive. The Business Accounting Council (BAC), a key advisory body to the commissioner of the FSA, approved the roadmap for the adoption of IFRSs in Japan. Sir David Tweedie, chairman of the IASB, said the following on the announcement of the adoption of IFRSs in Japan (IASB, 2009):

This is a landmark decision, both for Japan and for IFRSs. For Japan, it signals the eventual adoption of IFRSs. For the IASB, adoption of IFRSs by the world's second largest national economy underscores the truly global nature of IFRSs and the acceptance of these standards by all major economies.

In the Interim IFRS Roadmap, continuing convergence has been emphasized. At the same time, the directions for Japanese GAAP are indicated, including topics on issues concerning the application of IFRS in Japan and the required approach. These issues include the optional application and considerations for the mandatory application of IFRS in Japan, for example, scope and methods for mandatory application, treatment of non-consolidated financial statements, etc..

One of the arguments for the adoption of IFRS is that adopting IFRS can improve the comparability of accounting information and transparency. The mission of IASB is to develop a single set of high-quality global

¹ Nippon Keidanren (Japan Business Federation) is an umbrella economic organization born in May 2002 through the amalgamation of Keidanren (Japan Federation of Economic Organizations) and Nikkeiren (Japan Federation of Employers' Associations). Its membership comprises 1,285 companies, 127 industrial associations, and 47 regional economic organizations (as of March 29, 2012).

accounting standards that are accepted worldwide. Though IFRS enables improved comparability, it should be noted that comparability should not be confused with uniformity, because comparability means that similar things should look alike and different things should look different (Barth, 2008). It is obvious that major international differences exist in accounting practices and the possible causes of differences may not be completely eliminated even if adopting the IAS (Alexander & Nobes, 2009). Therefore, IFRS, if to be adopted in Japan, must faithfully reflect the economic reality of businesses and trade practices in Japan, as well as in the global financial and capital market. Hence, the continuing convergence is still emphasized in the Interim IFRS Roadmap.

On the other hand, though the Interim IFRS Roadmap indicates acceptance of IFRS, several problems still need to be tackled, including the above issues indicated in the report because of the existing differences between IFRS and Japanese GAAP and the cause of the differences which may not be eliminated entirely. As we know, accounting standards can be regarded as fully functional only if financial reports are appropriately prepared. Therefore, when the manner of adoption, especially mandatory application, is to be determined, the features of Japanese accounting, situation of Japanese companies, difference between IFRS and Japanese GAAP, and other related issues should be understood, just as the Interim IFRS Roadmap makes clear:

... Japan must be prepared to take on the issue of mandatory application of IFRS from a broad range of perspectives, defining the path to be taken in the case of making the use of IFRS by a certain range of Japanese companies mandatory, while attending to the various aforementioned conditions in Japan and abroad... (Business Accounting Council, 2009, p. 16)

The Features of Japanese Accounting

In this section, the authors will analyze the major environmental factors that influence companies' accounting practices, particularly, the factors that directly influence the incentive to implement IFRS, features of Japanese accounting, and the major differences between IFRS and Japanese GAAP, in order to acquire an understanding of the relevant issues that must be considered in making the final decision on whether and how IFRS should be complied with.

First, a large list of possible causes of international differences can be found in the writings of previous researchers (e.g., Choi & Meek, 2005; Nobes & Parker, 2008). For example, the most frequently referred factors that may influence accounting development are cultures, legal environment, providers of finance, taxation, professionalization of the accounting profession, and other external influences such as the economy, political events, and international influences. Although international influence seems to be the most significant factor spurring the adoption of IFRS worldwide, the countries with a strong equity market and those with weak equity market accounting standards do not seem to follow the prevailing trend.

Among all the above factors affecting accounting development, the main variable apart from international influences that explain the most important international differences in financial reporting is the financing system, or particularly, the providers of finance. In countries where the capitals provided by banks or family companies are very important, the banks or family companies may nominate directors and thus be able to obtain restricted information and affect decisions. In this case, the need for published information is much lesser because of this access to private information. In other countries where the major sources of corporate finance have been the share capital and loan capital provided by large numbers of private investors, especially foreign investors, there is a relatively strong requirement for unbiased information regarding the success of a

business and its state of affairs. It is reasonable to assume that companies with different capital structures may have different opinions on IFRS.

Japan seems to be a unique case. It has a fairly important equity market, although not as important as that in the US or the UK. Furthermore, many Japanese companies own shares in each other, and therefore, the total number of listed companies and market value is exaggerated when making an international comparison. Thus, an understanding of the major finance resource of Japanese companies and their perceptions of the importance of domestic and foreign equity markets is beneficial when deciding if there is a need for mandatory adoption.

Second, Japanese accounting has both German and American features. The Japanese accounting system largely consists of a commercial code borrowed from Germany during the late 19th century, overlaid with US-style securities laws imposed during the late 1940s. Japanese accounting standards are characterized as rule-based, which are similar to US GAAP, in contrast to IFRS which is characterized as principle-based. In converging an accounting standard with IFRS, there are two approaches: the “principle-based approach” and the “rule-based approach”. Under the former, the accounting standards are established on the bases of general principles and the professional judgments of the financial statements makers, whereas, under the latter, the accounting standards are established on the basis of more detailed and clear rules. Continuing convergence with IFRS should resolve the conflict between rule-based and principle-based accounting standards. On the other hand, complete adoption of IFRS may mean a change from rule-based to principle-based accounting standards that are assumed to have a great impact on financial statement preparers.

Third, the major difference in accounting standards between IFRS and Japanese GAAP concerns the recognition of revenue, research and development (R&D), financial instruments, lease accounting, etc.. These differences are rooted in the basic accounting ideas of the two sets of accounting standards. The basic ideas of IFRS are principle-based, financial position-focused statement, and fair value accounting, whereas those of Japanese accounting are rule-based and attach great importance to income statements. Although the resulting concrete differences in standards hold different levels of importance for Japanese companies, there is value in understanding the relative importance of each of the differences in accounting standards.

Investigation of Managers’ Opinions on IFRS Adoption

With the above considerations in mind, the authors conducted a survey to determine the necessity of adoption and the possible problems concerning adoption from the perspectives of financial statement preparers. In this paper, the authors referred to the chief financial officers (CFOs) and accounting managers of Japanese companies and asked questions to investigate their understanding of and opinions towards IFRS adoption and the present situation of IFRS application in Japanese companies using a postal questionnaire.

Structure of Investigation Questionnaire

Since the provider of finance is one of the most important factors influencing the accounting practice, it is helpful to know the capital structure and major finance sources of investigated companies. It is also relevant to understand how the accounting managers are prepared for adoption, for example, to explore how important they consider the difference between domestic accounting standards and IFRS to be, how would they prefer IFRS to be adopted, the present adoption of IFRS in their companies, and the difficulties or other considerations relating to the application of IFRS. Furthermore, if IFRS is to be adopted, the contradiction between rule-based Japanese accounting and principle-based IFRS should be resolved. It is also important to

understand the accounting managers’ opinions on principle-based and rule-based accounting, because the character of accounting standards directly affects managers’ judgments and their accounting practices. Therefore, the questionnaire comprised four parts:

- (1) Major finance sources and users of financial statements;
- (2) Attitudes towards and opinions on the adoption of IFRS;
- (3) The present situation of IFRS application;
- (4) The convergence approach of accounting standards.

Sample Selection and Collection of Responses

The sample selection and collection of responses of each investigation are summarized as follows. The investigation selected 500 companies of which 67 are Japanese companies having the rank of a Fortune Global 500 in 2007. The questionnaires were sent to the CFOs or senior managers of these companies in 2008. One hundred and fifteen useful responses were received (the response rate was 23%), of which 57 are Japanese companies (response rate 89%). In the current paper, the authors analyze only the data of Japanese companies. The companies that are permitted to apply IFRS voluntarily and those that may be required to apply IFRS to their financial statements in the Interim IFRS Roadmap are those that conduct global financial or business activities. The investigated companies fall within the category of optional application or future mandatory application of IFRS.

Results and Analysis

The respondent percentages reported in this paper are based upon the total number of responses to the questions. The design of the questionnaire permits multiple answers for some questions. Consequently, the combined responses for some questions may exceed 100%.

Major finance sources and users of financial statements. The first question asked the managers’ views concerning the importance of domestic and overseas stock markets to their companies and the importance of the stock market and bond market. A 5-point Likert scale was used for measurement where “1” = Not important at all, “3” = Not so important, and “5” = Very important.

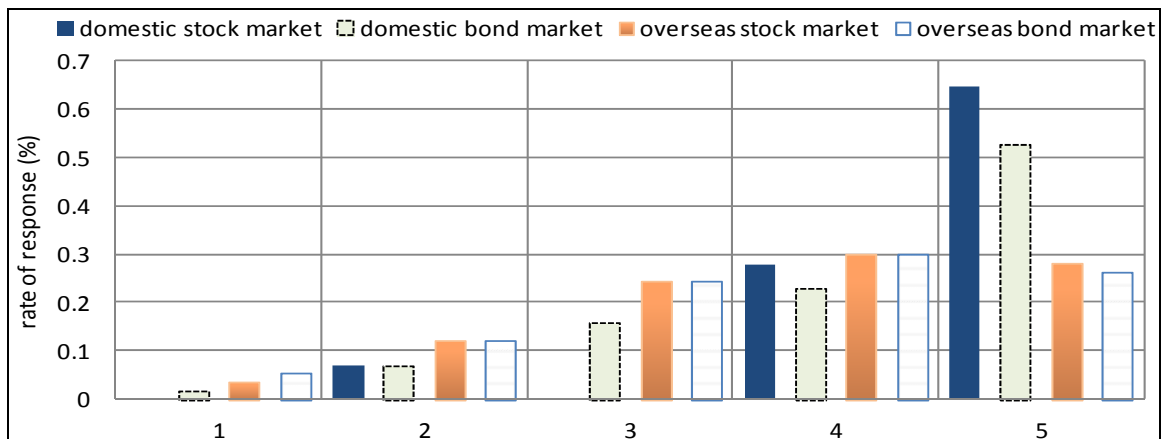


Figure 1. The managers’ views on the importance of markets in Japan.

As shown in Figure 1, the domestic market was regarded by the largest category, 65% of respondents, as being very important to their business activities. Some 42% of respondents indicated that the domestic bond

market was very important. Overall, 23% of respondents rated the overseas stock market as either important or very important. Though the majority of respondents rated the overseas markets as not being of the same importance as the domestic markets, in general, they regarded the overseas market as important (see Figure 1 and Table 1).

Table 1

The Managers' Views on the Importance of Markets in Japan

Market	The average point	Sample company
Domestic stock market	4.501	<i>n</i> = 57
Domestic bond market	4.175	<i>n</i> = 57
Overseas stock market	3.614	<i>n</i> = 56
Overseas bond market	3.544	<i>n</i> = 56

Note. A 5-point Likert scale was used: "1" = Not important at all, "3" = Not so important, and "5" = Very important.

The perception that domestic markets are more important than overseas markets may suggest that Japanese companies give little attention to overseas users of financial statements, which may lead to a lack of incentive to adopt IFRS. To confirm this, the second question in the questionnaire used a 5-point Likert scale as previously described to determine how CFOs or senior managers view the importance of financial statements to various users (see Figure 2 and Table 2).

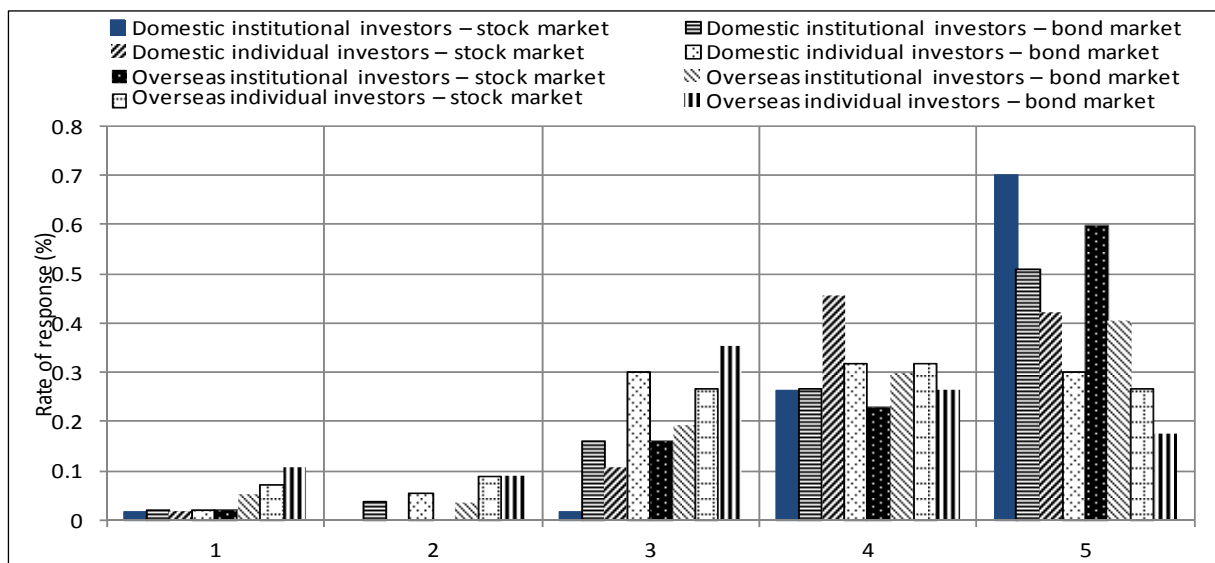


Figure 2. The managers' views on the importance of financial statements to various users in Japan.

Table 2 shows that the entire set of respondents think that financial statements are important to most users (the average point > 3). Generally, the respondents assessed financial statements as being more important to domestic investors than to overseas investors. However, financial statements are important even for overseas investors. Overall, as can be seen in Figure 2, 42% of the respondents think that financial statements are very important to individual investors in the stock market, whereas 70% think that the financial statements are very important to institutional investors. However, concerning investors in the overseas stock market, 60% of respondents think that financial statements are important to institutional investors, whereas only 26% regard them as very important to individual investors.

Table 2

Comparison of the Managers' Views on the Importance of Financial Statements to Various Users in Japan

Investor and market	The average point	Sample company
Domestic institutional investors—stock market	4.632	<i>n</i> = 57
Domestic institutional investors—bond market	4.158	<i>n</i> = 56
Domestic individual investors—stock market	4.263	<i>n</i> = 57
Domestic individual investors—bond market	3.839	<i>n</i> = 56
Overseas institutional investors—stock market	4.386	<i>n</i> = 57
Overseas institutional investors—bond market	3.982	<i>n</i> = 56
Overseas individual investors—stock market	3.614	<i>n</i> = 57
Overseas individual investors—bond market	3.321	<i>n</i> = 56

Note. A 5-point Likert scale was used: “1” = Not important at all, “3” = Not so important, and “5” = Very important.

The authors did a similar survey in 1997, and by comparing the results, they found that the managers' perceptions that financial statements were most important to domestic institutional investors compared with other users remained unchanged over the past decade (Hu, 2012).

The authors also investigated the foreign ownership of each company. Approximately, 10% of the respondents stated that their overseas investment is 0%; 48% of respondents, the largest group, stated that foreign ownership is within “1%-10%”; 12% of respondents chose “11%-20%”; 20% of respondents chose “21%-40%”; and 10% of respondents said that their foreign ownership is “over 40%”.

Attitudes Towards and Opinions on the Adoption of IFRS

The fourth question asked the respondents about their preferences with regard to how IFRS is adopted. There were three options: (1) only adopt IFRS or US GAAP; (2) use both IFRS (for overseas use) and Japanese GAAP (for domestic use); and (3) use international accounting standards as supplementation to Japanese GAAP. Forty one percent of respondents preferred to adopt only IFRS as the basic financial statements standards. Another 29% of the respondents preferred to use IFRS as a supplementation to Japanese GAAP. Only 11% selected the use of both IFRS and Japanese GAAP, which might because of the high costs of using double standards and the complication of usage.

Then, the survey asked the respondents for their understanding of the difference between IFRS and Japanese accounting standards.

Table 3

The Managers' Views on the Importance of Differences Between Japanese GAAP and IFRS

Accounting standard	The average point	Accounting standard	The average point
Goodwill	4.636	Allowance	3.545
Comprehensive income	4.327	Fixed tangible assets	3.509
The recognition of revenue	4.018	Consolidated/South Pacific Commission (SPC)	3.491
Business combination	3.981	Investment property	3.364
R&D	3.857	Foreign currency	3.127
Financial instrument	3.636	Lease	2.873
Impairment*		Employee payment*	

Notes. (1) A 5-point Likert scale was used: “1” = Not important at all, “3” = Not so important, and “5” = Very important; (2) *: Additional indication by respondents.

The results show that the differences between Japanese GAAP and IFRS, which are thought to be the most important, are the standards for goodwill, comprehensive income, and recognition of revenue (see Table 3). The differences in accounting standards for business combinations and R&D are also regarded as important. In addition to those listed in the questionnaire, some respondents indicate that significant differences in accounting standards for impairment and payment to employees are also important (see Table 3).

The authors also asked respondents to state their opinions on the change concerning the application of IFRS five years from now. As can be seen in Table 4, most of the respondents expected that IFRS would be increasingly used only in consolidated financial statements or in both consolidated and the parent company's separated financial statements. A minority of the respondents expected that IFRS would be adopted only in the parent company's account or in a supplementary disclosure as well. If the expectation of these respondents is correct, they will need to plan for the switch to IFRS.

Table 4

The Managers' Views on the Expectation of Future Application of IFRS

Expectation of future application of IFRS	The average point	Sample company
Application only in consolidated financial statements	1.582	<i>n</i> = 55
Application only in parent company's separate financial statements	2.321	<i>n</i> = 53
Application in both consolidated and parent company's separate financial statements	1.855	<i>n</i> = 55
Application only in supplementary disclosure	2.472	<i>n</i> = 53

Note. A 5-point Likert scale was used: "1" = Not important at all, "3" = Not so important, and "5" = Very important.

The survey then asked whether the respondents agreed with the statement that it would be difficult to change from Japanese GAAP to IFRS. As can be seen in Table 5, 55% of respondents thought that it would be difficult to change from Japanese GAAP to IFRS.

Table 5

The Managers' Views on Whether Changing From Japanese GAAP to IFRS Would Be Difficult

The managers' view	Strongly agree	Agree	Slightly agree	Disagree	Strongly disagree
The percentage of responded companies	7.14%	21.43%	26.79%	35.71%	8.93%

The Present Situation of IFRS Application

Only two out of 57 respondents from the usable sample reported that they were adopting IFRS when asked. Another two Japanese companies answered that they were going to adopt IFRS though they were not using it at that moment². However, the vast majority (93.0%) of the respondents noted that IFRS was not being adopted and they were not sure whether they would adopt it in the future.

The respondents who indicated that they were not yet adopting IFRS were questioned to explore the main reasons why IFRS was not being adopted. The reasons suggested by these respondents are as follows: (1) The cost is too high (10.5% of the respondents); (2) The staff training system is inadequate (24.5% of the respondents); (3) The international accounting standards are inconsistent with Japanese accounting standards (38.5% of the respondents); (4) There is little benefit from the adoption of international accounting standards (22.8% of the respondents); (5) Adopting IFRS is not a legal requirement (52.6% of the respondents); and (6)

² Note that even though the Japanese government (FSA) decided to adopt IFRS voluntarily from 2010, there was only one company which did adopt IFRS in 2010 (Hu, 2011).

Other reasons (14.0% of the respondents). Multiple choices were permitted and respondents could cite other reasons than those listed. Clearly, the lack of legal requirement for adopting IFRS was found to be the main reason for the uncertainty regarding the future adoption of IFRS.

The authors then used the 5-point Likert scale to measure the respondents' perceived importance concerning the benefit of adopting IFRS (see Table 6). The expected benefits are that: (1) It will improve the trust and understanding of securities investors; (2) It will improve the trust and understanding of bond investors; (3) It will make it easier to issue securities in international markets; (4) It will reduce the costs of raising bond capital; (5) It will improve the international image of the company; (6) It will reduce the barriers to listing in overseas stock markets; and (7) It will reduce the cost of creating financial statements. The majority of the respondents perceive that the most important benefits of IFRS adoption are the greater ease of issuing securities in international markets (61%), the improved trust and understanding of securities investors (58%), and the reduced barriers to listing in overseas stock markets (51%). It is obvious that the greatest benefit of IFRS adoption is related to international markets, international status, and international fund-raising. Only 9% of respondents think that the reduced cost of making financial statements is an important or very important factor.

It is interesting that the perceived benefits have changed over the years (Hu, 2012). To be specific, respondents in the 2008 investigation thought more negatively about IFRS adoption and they perceived less benefits than those did in 1997. For example, in 1997, Japanese managers regarded improving the trust and understanding of stock investors as a very important benefit, whereas in 2008 they did not ascribe great importance to it. One of the reasons for this may be that managers have fully realized the achievement of accounting convergence towards IFRS through the Accounting Big Bang after 1997.

Table 6

The Managers' Views on the Perceived Benefits of IFRS Adoption

Perceived benefit of IFRS adoption	The average point	Sample company
Improve the trust and understanding of stock investors	3.754	<i>n</i> = 57
Improve the trust and understanding of bond investors	3.684	<i>n</i> = 57
Make it easier to issue securities in international markets	3.930	<i>n</i> = 57
Reduce the cost of raising bond capital	3.246	<i>n</i> = 57
Improve the international image of the company	3.474	<i>n</i> = 57
Reduce the barriers to list in overseas markets	3.790	<i>n</i> = 57
Reduce the cost of making financial statements	2.263	<i>n</i> = 57

Note. A 5-point Likert scale was used: "1" = Not important at all, "3" = Not so important, and "5" = Very important.

Then, the questionnaire asked the accounting managers to state their perceptions of the relationship between cost and benefit. The respondents displayed some skepticism regarding the benefits of IFRS adoption. Indeed, 64% of the respondents thought that cost would exceed benefit, whereas 15% indicated that cost would almost equal benefit. Only 1.8% expected that benefit would exceed cost (see Table 7).

Table 7

The Managers' Views on the Cost-Benefit Analysis of IFRS Adoption

The managers' views	Benefits greatly exceed costs	Benefits slightly exceed costs	Benefits equal costs	Costs lightly exceed benefits	Costs greatly exceed benefits
The percentage of responded companies	1.82%	20.00%	14.55%	40.00%	23.64%

The Convergence Approach of Accounting Standards

Furthermore, as for the approach—either principle-based or rule-based approach—to adopting IAS, 60% of respondents regard the principle-based approach as more appropriate. The main reason given is that the accounting under principle standards reflects the substance of the economy and it is easier to implement IFRS in practice, because detailed rules may impede the use of IFRS in a Japanese context. In contrast, only 25% think the rule-based approach is better, with the main argument being that the accounting method is clearly prescribed so that it is easier to comply with in practice and the comparability of accounting information would be improved.

Conclusions and Discussion

The present research investigated issues concerning the application of IFRS in Japan from the perspectives of managers of Japanese companies, that is, the preparers of financial statements.

In the first three sections of the paper, the authors have indicated that the provider of finance and the differences in the basic idea and concrete standards between IFRS and Japanese GAAP might influence the financial statements preparers' application of IFRS. These aspects should be considered when the scope and approach of a mandatory application of IFRS are being decided. By investigating the major finances of leading Japanese companies, the managers' opinions on adoption, the present adoption by Japanese companies, and reasons for non-adoption were determined:

(1) Over half of the largest companies in the sample have rather low foreign ownership (less than 10%). It is obvious that the greatest benefit of IFRS adoption is related to international markets, international status, and international fund-raising. Thus, the Japanese companies expressed an assessment that financial statements are more important to domestic investors than to overseas investors. Though the majority of the respondents rated the overseas markets as being less important than the domestic markets, in general, they still regard overseas financing markets as important;

(2) The major differences in accounting standards concern the recognition of revenue, R&D, leases, and financial instruments, whereas the differences thought to be the most important by Japanese companies are standards for goodwill, comprehensive income, and the recognition of revenue. The differences in accounting standards for business combinations and R&D are also regarded as important;

(3) Most of the respondents expected that IFRS would be increasingly used only in consolidated financial statements or in both consolidated and parent companies' separated financial statements;

(4) The main reasons why Japanese companies have not adopted IFRS include the lack of a legal requirement that IFRS be adopted, inconsistencies between IFRS and Japanese GAAP, and inadequate training systems. The reason why Japanese companies display a negative attitude towards IFRS adoption may be that the Japanese managers expect that the application of IFRS would be difficult. Furthermore, with the convergence of Japanese standards with IFRS in 2008, Japanese companies became more confident about preparing their financial statements under the domestic standards than before. They assume that even without adopting IFRS, they can gain the trust and understanding of investors. Further, Japanese managers expected that the cost of IFRS adoption would exceed the benefit;

(5) Principle-based accounting is thought to be superior to rule-based accounting by managers of Japanese companies.

The above survey results provide some implications for regulation consideration and training programs. The following points require the attention of regulators. First, though the globalization of the Japanese economy and the filtering of global standards (accounting standards, corporate governance) have steadily progressed, Japanese companies remained prudent and passive regarding IFRS adoption. This may be partially owing to the relatively low foreign ownership in leading Japanese companies. Although the investigated companies are all leading companies in Japan, the fund-raising policies and the proportion of foreign ownership vary. The initial IFRS roadmap suggests a phase-in approach based on criteria such as the gross market value of each company—a scheme proposed in the US roadmap. The survey result suggests that the phase-in approach based on both foreign ownership and gross market value criteria would be better, as the greatest benefit of IFRS adoption is related to international markets, international status, and international fund-raising.

Second, one of the most important considerations concerning the adoption of IFRS is that the cost of adoption is expected to exceed the benefit. The adoption of IFRS not only influences accounting practice but also has an effect on other aspects of business, such as the operating process, management system, and strategy making. For example, the authors know that there are differences in the two sets of accounting standards, one of which concerns standards for revenue recognition. In Japanese GAAP, sales revenue is recognized at the time of shipment, whereas IFRS prescribes that sales revenue can be recognized when the risk and benefit of the goods have been transferred to the buyer so that the revenue may not be recognized at the time of shipment. If IFRS is implemented, Japanese companies that have recognized sales revenue on a shipment basis may have to change the time of revenue recognition. This may result in changes to the internal control system, information system, distribution system of the company, and the amount of yearly sales revenue, which may further influence the business plan and strategy. These costs are beyond the direct costs related only to the accounting system. Cost-benefit trade-off is one of the most important considerations of preparers of financial statements. Thus, it should also be an important issue for consideration in deciding on mandatory application.

Furthermore, lack of a training system has been an important reason for Japanese companies' cautious attitudes towards IFRS. The training should not only concentrate on the detailed accounting standards but also include content concerning the total influence that IFRS adoption may have on the entire business. Moreover, principle-based accounting standards are regarded by a majority of the companies as reflecting economic substance and are thus regarded as superior. However, it requires a higher judgment capacity on the part of financial statement preparers. This not only requires a comprehensive training program but also increases the cost of adoption.

In addition, the investigated companies have indicated several differences in accounting standards that are important to their companies' goodwill, comprehensive income, and recognition of revenue, which implies that in making a decision on mandatory application, that is, whether to apply IFRS as developed by the IASB or to make partial modifications or exclusions of IFRS, not only the content of IFRS but the status of the setting of IFRS needs to be reviewed but also a careful investigation of the influence on Japanese companies must be conducted.

The current paper is written mainly from the perspectives of financial statement preparers. There are other perspectives that should be considered when deciding on the scope and methods of IFRS application, for example, the perspectives of accounting information users, auditors, and other interested parties. In addition, research shows some evidences that the adoption of IFRS itself does not lead to high-quality information. Therefore, adoption will not necessarily lead to increased transparency and the trust of accounting information.

Effective enforcement combined with high-quality standards leads to high value-relevant information. A strong equity market is connected with strong investor protection. Overall, the international value relevance of accounting information studies provides some supports for the argument that accounting information is more value relevant in countries having strong legal protection of outside investors (Habib, 2007). Japan has a unique equity market and accounting system that is discussed in Section 4. Therefore, adoption of IFRS should be further supplemented by consideration of enforcement, which can be analyzed in future papers.

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