The Impact of Voluntary IFRS Adoption[1) on Japanese Public Companies

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Abstract

This paper presents the current status of voluntary IFRS adoption in Japan and explains the factors that have led public companies to adopt these international standards. This research provides an in-depth analysis of the situation in Japan and provides some figures to support the findings. The goal of this paper is to conduct a preliminary study of Japanese companies that have adopted IFRS. Additionally this paper determines reasons for the voluntary adoption of IFRS by Japanese public companies through the analysis of major differences between Japanese GAAP ("JP GAAP") and IFRS. The purpose of this paper is to contribute to international debate and enhance the current understanding of voluntary IFRS adoption in Japan and the practical issues related to the adoption.

I. Current status of voluntary adoption of IFRS in Japan

Eligible Japanese companies have been permitted to use the designated IFRS in their consolidated financial statements, in lieu of JP GAAP, since 2010. At the current, the Financial Services Agency of Japan ("FSA") has stated that all IFRS and IFRIC interpretations published by the IASB are specified as "Designated IFRS."[2) Therefore, the designated IFRS are the same as current IFRS. In addition, the eligibility for voluntary IFRS adoption initially required domestic Japanese companies meet strict guidelines[3). These conditions were amended in October 2013

Keywords: Voluntary, Adoption, IFRS, Differences, JP GAAP, IFRS, Public companies, first-time adoption

1) IFRS means International Financial Reporting Standards, which is a set of accounting standards developed by an independent, not-for-profit organization called the International Accounting Standards Board (IASB).

2) The Present Policy on the Application of IFRS (IFRS)

3) Original Rule, which was enacted in 2010, indicates that eligible domestic companies have to meet both of 1 and 2 below. It was quite difficult to become eligible domestic companies.

(1) All of the following requirements shall be met:
- Shares issued by the company are listed on a Securities Exchange in Japan.
- The company discloses in its Annual Securities Reports information regarding specific efforts to ensure appropriateness of its consolidated financial statements.
- The company allocates executives or employees with ample knowledge about Designated IFRS and has in place a structure that enables it to properly prepare consolidated financial statements in accordance with Designated IFRS.

(2) The company, its parent, a related company, or the parent of the related company shall either:
- Disclose under laws and regulations of a foreign jurisdiction periodically as required thereby,

and, nowadays, public companies only need meet the following conditions.

1. The company must demonstrate that it has given its best effort in preparing the Annual Securities Reports to ensure the quality and appropriateness of consolidated financial statements.
2. The company must allocate executives or employees with ample knowledge of the Designated IFRS and ensure there is a structure in place that enables the proper preparation of consolidated financial statements in accordance with Designated IFRS.

Consequently, more than 4,000 public companies are eligible to voluntarily adopt IFRS in Japan[4]. As of August 2014, 45 Japanese companies have either adopted IFRS or have publicly announced their intention to do so[5]. When compared with the 4,000 public companies that are eligible for voluntary IFRS adoption, these 45 companies[6] seem somewhat insignificant, however; the aggregated market value of these 45 companies comprises approximately 13.7 percent of the market capitalization on the Tokyo Stock Exchange ("TSE") in August, 2014. Figure 1 shows the changes in the voluntary adoption of IFRS in Japan.

On May 23, 2014, the Liberal Democratic Party of Japan ("LDP") released the "Japan Revival Vision"[7] and declared their intention to increase the number of voluntary IFRS adopters to 300 public companies before the end of fiscal 2016. Even with this significant increase, these 300 companies will account for less than 10% of listed companies on the TSE. LDP assumes that the aggregated market values of these 300 companies will be over 50% of the aggregated market capitalization on the TSE, since major Japanese global enterprises will take the initiative in adopting IFRS.

This paper firstly elaborates on the historical background of IFRS adoption in Japan and the possibility of mandatory adoption in the future. Next, the major differences between JP GAAP and IFRS are compared at the point of first-time adoption within Japan. An analysis of the fore mentioned 45 companies which have adopted IFRS in place of JP GAAP follows. Finally, the opening statement of financial position at the date of transition to IFRS and the first year financial statements under IFRS are analyzed. Based on these procedures, the effects of voluntary IFRS adop-

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documents on its business conditions prepared in accordance with IFRS;

- disclose under rules set by a foreign security exchange markets periodically as required thereby, documents on its business conditions prepared in accordance with IFRS; or
- Own a foreign subsidiary whose capital is equal to or exceeds the equivalent of two billion Japanese yen.

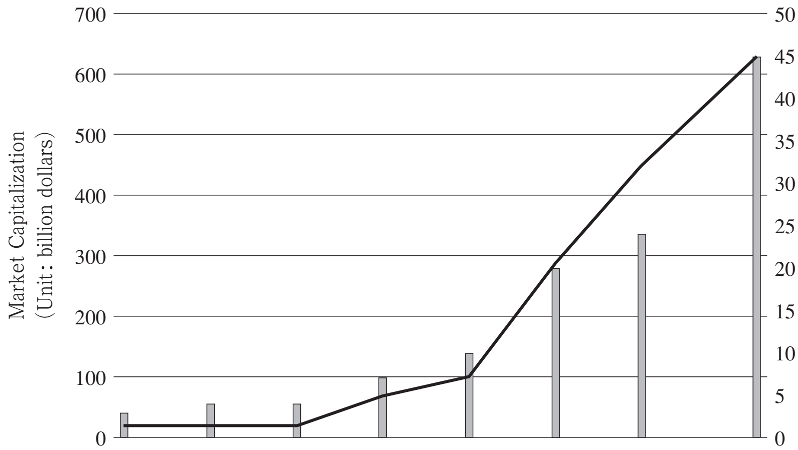
4) Please refer to http://www.ifrs.org/Alerts/Publication/Pages/Japan-IFRS-profile-revised-February-2014.aspx as of August 21, 2014

5) Please refer to http://www.tse.or.jp/listing/ifrs/list.html as of August 21, 2014

6) This number includes Skylark Co., Ltd., which plan to list on TSE in October, 2014. Therefore, Skylark is not included in the market capitalization figures.

7) "Japan Revival Vision", Liberal Democratic Party of Japan - Japan Economic Revival Headquarters, May 23, 2014

Figure 1　Change of voluntary adoption of IFRS in Japan[8]



	Dec-10	Jun-11	Dec-11	Jun-12	Dec-12	Jun-13	Dec-13	Aug-14
Number of Company	3	4	4	7	10	20	24	45
Market Capitalization	20	20	20	70	100	290	450	630

tion by Japanese public companies can be readily identified.

II. Historical Background of IFRS adoption in Japan

In this section, the historical background of IFRS adoption in Japan is explained. In 2005, the Accounting Standards Board of Japan ("ASBJ") and the International Accounting Standards Board ("IASB") held their initial meeting on the joint project for convergence of accounting standards.

In 2006, the ASBJ began meeting with the Financial Accounting Standards Board ("FASB") periodically, in pursuit of global convergence.

In 2008, the European Commission announced that JP GAAP was found to be equivalent to IFRS as adopted by the European Union. ASBJ completed the short-term project in the Tokyo Agreement.

In 2009, the Business Accounting Council ("BAC"), which is an advisory body to the FSA, issued the "Opinion on the Application of IFRS in Japan (Interim Report)." The interim report requested the establishment of the IFRS Council, which is a private sector promotion council to address Japan's roadmap towards IFRS implementation.

In 2011, the ASBJ and the IASB jointly announced their achievements under the Tokyo Agreement and their plans for closer co-operation. The IFRS Foundation decided to establish an

8) This chart was originally presented by Mr. Takatsuki Ochi of board member of IASB at the annual meeting of Japan Accounting Association on September 6, 2014. I tried to update the original chart to use this paper.

Asia-Oceania liaison office in Tokyo. Subsequently, the office received approval to begin operations in November, 2012.

In 2013, the BAC published the Present Policy on the Application of IFRS (the "Present Policy"), which stated the need for a process of endorsing IFRS to increase voluntary IFRS adoption in Japan. Furthermore, it was determined that the ASBJ be expected to perform the process expeditiously.

Following the publication of the Present Policy, the ASBJ established the "Working Group for the Endorsement of IFRS", which started its deliberations in August 2013.

In July 2014, the ASBJ issued the Exposure Draft on "Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRS and the ASBJ Modifications"[9]. The Exposure Draft on JMIS indicated that JMIS would accept all IFRS except for accounting for goodwill and other comprehensive income.

In other words, under JMIS, Japanese public companies may amortize goodwill periodically and may use recycling of items of other comprehensive income and profit or loss.

Consequently, in the near future, Japanese public companies will be entitled to use one of the four following sets of accounting standards in their consolidated financial statements, subject to certain eligibility requirements.

- JP GAAP
- IFRS (designated)
- JMIS
- US GAAP[10]

This research assumes that the 4 accounting standards will be converged to pure IFRS. It is unlikely that Japanese public companies will be required to adopt IFRS mandatorily in the near future, since the United States of America has not yet committed to IFRS adoption[11]. The number of companies voluntarily adopting IFRS has unquestionably increased within Japan. Japan is likely to converge JP GAAP with IFRS, essentially becoming an IFRS adopter, without the necessity of mandatory adoption.

Of course, IFRS are not permitted for statutory filings such as separate standalone financial statements within Japan.

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9) Please refer to https://www.asb.or.jp/asb/asb_e/endorsement/exposure_drafts/index.jsp

10) In case companies file form 20 F to SEC and prepare the consolidated financial statements under US GAAP, they are permitted to prepare the consolidated financial statements under US GAAP for the purpose of Japanese public filing.

11) I guess so based on the presentations of Mr. Atsushi Kogasaka of vice chairman of ASBJ at the annual meeting of Japan Accounting Association, which was held on September 6, 2014.

III. Major differences between JP GAAP and IFRS

As previously explained in the above sections, the ASBJ and IASB have been converging their accounting standards since 2005. Nowadays, there are not many differences between JP GAAP and IFRS. ASBJ indicated that the items identified as "issues for which there significant differences in the fundamental thinking on accounting standards" include the following[12]:

(a) Non-amortization of goodwill

(b) Items related to recycling of items of other comprehensive income and profit or loss

(c) Scope of fair value measurement

(d) Capitalization of development costs

ASBJ indicated only fundamental differences and, therefore, Japanese companies have to familiarize themselves with other major differences. Issues of significant importance include; accountings for tax, depreciation methods for fixed assets, consolidation and business combinations. It is also vital to understand the significant differences in presentation and disclosures methods including footnote information.

In this section, major practical differences between JP GAAP and IFRS, regarding accounting recognitions and measurements, are discussed. It is not necessary to discuss the presentation and disclosure issues in this paper, since retained earnings and the net income of companies are not influenced by these presentation and disclosures differences. Japanese stakeholders are generally interested in the retained earnings and net income, as opposed to the presentation.

The primary differences consist of the following items.

(1) Revenue recognition

Under IAS 18, revenue should be recognized when all 5 criteria[13] are met. Under JP GAAP, there are no specific requirements and revenue is recognized in accordance with the "Realization principle". It is customary for Japanese companies to recognize sales when inventory is shipped, in conformity with Japanese Tax Law.

12) Foreword to the Exposure Draft on "Japan's Modified International Standards (JMIS): Accounting Standards Comprising IFRS and the ASBJ Modifications" ASBJ, 31 July 2014

13) IFRS provides five criteria for identifying the critical event for recognizing revenue on the sale of goods.
(1) Risks and rewards have been transferred from the seller to the buyer
(2) The seller has no control over the goods sold
(3) Collection of payment is reasonably assured
(4) The amount of revenue can be reasonably measured
(5) Costs of earning the revenue can be reasonably measured

（2） Employee benefits

There are no significant differences between JP GAAP and IFRS in this sector of accounting because costs are usually recognized on an accrual basis. IFRS require so-called ‘non-recycling’ for the measurement of net defined benefit liabilities (asset) (IAS 19 Employee Benefits). Non-recycling means that there will be no reclassification adjustments (recycling) for items previously recognized in other comprehensive income. As long as this is known, the difference significantly impact Japanese companies.

（3） Depreciation methods of fixed assets

Under IAS 16, the depreciation method used reflects the pattern in which the asset’s future economic benefits are expected to be consumed. Under JP GAAP, the definition is same. Actually, under IAS 16, many companies use straight-line method. However, many Japanese companies[14] still use declining-balance method in conformity with JP GAAP or Japanese Tax Law.

（4） Amortization and impairment testing of goodwill

Amortization: Under IFRS, goodwill is not amortized. Under JP GAAP, goodwill is recognized as an asset and amortized on a systematic basis over a period in which effects are expected to occur, not to exceed 20 years.

Impairment testing: Under IFRS, even if impairment indicators do not exist, companies have to perform impairment test annually. Under JP GAAP, just in case impairment indicators exist, the one-step approach requires that impairment loss (if any) must be calculated.

（5） Fair value measurement of financial assets

Under IFRS 9, the measurement of fair value for equity investments is the general rule and cost is the exception. While under JP GAAP, unlisted financial instruments are measured at cost. Therefore, many financial instruments are often measured at cost in Japan.

（6） Recoverability of deferred tax assets

The accounting for current tax and deferred tax under JP GAAP is not fundamentally different from IFRS. However, with respect to assessing the recoverability of deferred

14） Based on the eol database, 1875 listed companies still use declining-balance method for machinery as of March 31, 2014.

tax assets, JP GAAP provides detailed guidelines. Under these guidelines, entities are classified into five categories, mainly based on past performance, to determine the recoverability of the deferred tax assets. This guideline seems to be ultraconservative, compared to IFRS. IFRS require substantial judgment as there is no specific guidance.

(7) Provisions for special repairs under JP GAAP and Tax

Under IAS 16, when each major inspection is performed, its cost is recognized in the carrying amount of the item of property, plant, and equipment as a replacement if the recognition criteria are satisfied. If necessary, the estimated cost of similar future inspection may be used as an indication of what the cost of the existing inspection component was when the item was acquired or constructed. Therefore, under IFRS, companies cannot accrue special provisions for repairs. Under JP GAAP, special repair provisions are given as an example of non-current liabilities. The amount of provision which relates to the current period is recognized as a current period profit or loss.

(8) Accrued vacation pay

Under IAS 19, the expected cost of short-term compensated absences (vacation pay) is recognized as the employees render service that increases their entitlement or, in the case of non-accumulating absences, when the absences occur, and includes any additional amounts an entity expects to pay as a result of unused entitlements at the end of the period. Under JP GAAP, there are no specific requirements.

(9) Customers loyalty programs

Under IFRIC 13, customer loyalty programs are accounted for as multiple-element arrangements. The entity allocates some of the consideration to the award credits and defers the recognition of revenue until such award credits are redeemed or forfeited. Under JP GAAP, there are no specific requirements. In general, the entity recognizes the full amount of revenue at initial recognition. This includes the award credits and accounts for the estimated future cost of supplying the awards. These expenses are accrued at the end of the reporting period as a provision and selling, general and administrative expenses.

(10) Capitalization of research and development cost

Internally generated research and develop cost are generally expensed under JP GAAP, which is different from IFRS which requires the capitalization of development costs when certain criteria are met.

IV. Why do Japanese public companies voluntarily adopt IFRS?

As mentioned in previous sections, there are several substantial differences between JP GAAP and IFRS. Therefore, in cases where Japanese public companies adopt IFRS, these companies have to bear costs related to the application by multinational companies which consist of changing the internal systems to make them compatible with the new reporting standards, training costs, etc. In spite of this disadvantage, these 45 Japanese companies in our study have implemented IFRS or have publicly announced their intention to do so.

In this section, the advantages of adopting IFRS on a voluntary basis are discussed.

Relating to the advantages of adopting IFRS, KEIDANREN (Japan Business Federation)[15] established the task force in August 2012 for the purpose of identifying practical solutions and disadvantages offered by them. The task force researched the reasons why Japanese public companies adopted or planned to adopt IFRS voluntarily. The resulting report on the reference cases for practical solutions to voluntary adoption of IFRS was released on January 15, 2014.

The report summarized the reasoning for these companies voluntary adoption, as follows.

1. Advantages of voluntary IFRS adoption from the external standpoint
   (1) Increased comparability with foreign companies in the same line of business. Consequently, Japanese companies can easily procure foreign funds from overseas capital markets.
   (2) Unfortunately, JP GAAP is not a popular global standards, even though the EU approved JP GAAP as an equivalent. There are several risks to using JP GAAP continuously. Nowadays, foreign stock ownership ratios are increasing in the Japanese stock markets. In instances where U.S. shareholders' ratio is over 10% if such companies acquire another large company, the Securities and Exchange Commissions ("SEC") may require the company file Form F-4[16]. In such a case, the company has to prepare the consolidated financial statements under US GAAP or IFRS. This is quite tedious work for companies, which have already prepared the consolidated financial statements in accordance with JP GAAP.
   (3) Investors, especially foreign investors, view at IFRS adoption favorably.

15) KEIDANREN (Japan Business Federation) is a comprehensive economic organization with a membership comprised of 1,309 representative companies of Japan, 112 nationwide industrial associations and 47 regional economic organizations (as of July 1, 2014).

16) Form F-4 is an American Form used to register securities in connection with business combinations and exchange offers involving foreign private issuers, which are owned over 10% by US shareholders. These activities include mergers & acquisitions, going-private transactions, rights offerings, and other similar deals conducted by foreign entities

2. Advantages of voluntary IFRS adoption from the internal standpoint

(1) When companies prepare consolidated financial statements in accordance with IFRS, it is more useful for management.

(2) Since Japanese parent companies normally have many foreign subsidiaries, the adoption of IFRS means that all group companies will unify their local accounting principles to IFRS. The unification of accounting principles has brought about the enhancement of consolidated financial information, strengthening corporate governance and operational efficiency of the corporate group.

(3) When the companies adopt IFRS, they are able to unify the external and the internal indexes. Thus, enhancing budget control, operation efficiency, and reducing duplicate costs.

KEIDANREN explained that many leading companies in Japan have considered adopting IFRS based on the above advantages, in spite of increased costs.

V. IFRS first-time voluntary adoption for Japanese public companies

When Japanese public companies decide to voluntarily adopt IFRS, the companies have to follow IFRS 1, "First-Time Adoption of IFRS". That is to say, IFRS 1 is the standard that is applied during preparation of a company's first IFRS-based financial statements. This standard was created to help companies transition to IFRS and provide practical accommodations which are intended to make first-time adoption cost-efficient. It also supports application guidance for addressing difficult conversion topics. Therefore, all Japanese companies, which adopt IFRS, or plan to, will have to prepare their first IFRS-based Financial Statements ("first IFRS Financial Statement ("F/S") in accordance with IFRS 1"). Under IFRS 1, the companies have to retrospectively apply all IFRS standards that are effective as of the reporting date of the first IFRS F/S, when they prepare these financial statements. In addition, IFRS 1 requires these companies to:

(a) Identify the first IFRS financial statements

(b) Prepare an opening statement of financial position at the date of transition to IFRS

(c) Select accounting policies that comply with IFRS and apply those policies retrospectively to all of the periods presented in the first IFRS F/S

(d) Consider whether to apply any of the optional exemptions from retrospective applications

(e) Apply the mandatory exception from retrospective applications

(f) Make extensive disclosures to explain the transition to IFRS

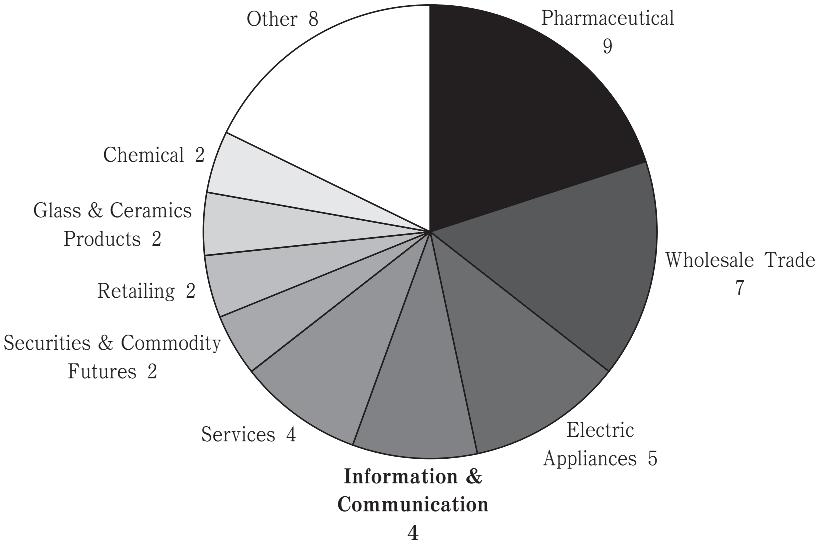
As mentioned above, the exemption provides limited relief for first-time adopters, mainly in areas where the information needed to apply IFRS, retrospectively, might be challenging to obtain. However, there are no exceptions from the requirements of IFRS disclosures, and Japanese companies have experienced or may experience challenges in collecting new information and data for retrospective footnote disclosures. In addition to this, Many Japanese public companies will need to make changes to existing accounting policies to comply with IFRS. As mentioned in the previous section, there are several major differences between JP GAAP and IFRS. Japanese public companies implementing IFRS 1 may be required to perform calculations or collect information that was not previously required under JP GAAP. These requirements are a substantial burden for Japanese public companies preparing their first IFRS F/S.

In the following section, the impact of IFRS 1, “First-Time Adoption”, on Japanese companies is evaluated.

VI. Empirical Analysis of 19 public companies which have voluntarily shifted from JP GAAP to IFRS

To better understanding the current situation concerning voluntary IFRS adoption by Japanese public companies, some significant figures have been generated and analyzed. As indicated in the previous sections, the 45 Japanese companies have either implemented IFRS or have publicly announced their intention to do so. Figure 2 demonstrates analysis of the 45 companies by industry.

Figure 2　Analysis 45 companies by industry



Notes
1　In the pharmaceutical industry, 6 of the top 10 companies decided to adopt IFRS voluntarily. Sales amounts for these 6 companies represent over 70% of the top 10 companies’ sales.
2　In the wholesale trade industry, these 7 companies represent all of major *Sogoshosha,* which trade in a wide range of products and materials, except for Toyota Tsusho.

As was explained in previous sections, KEIDANREN indicated several advantages from external or internal standpoints. If the analyses of these advantages are correct, the 45 companies should have significantly more foreign subsidiaries, compared to other public companies in Japan. In addition, the foreign stockholding ratio of these companies should also be higher than other Japanese publically traded companies.

These Analyses have led to the following conclusions.

(*a*) *Comparison of numbers of foreign subsidiaries*

A Business activity survey report[17] indicated that Japanese companies have 7.2 foreign subsidiaries on average. Based on these calculations, these 45 companies have approximately 66 foreign subsidiaries on average.

(*b*) *Comparison of foreign stockholding ratio*

A stock condition survey[18] of TSE indicated that the average foreign stockholding ratio of Japanese public companies is 30.3% as of March 31, 2014. Based on calculations, the average foreign stockholding ratio for these 45 companies is 34.62 % as of March 31, 2014.

As a result of this research, it can be concluded that the analysis of advantages, which were reported by KEIDANREN, are reasonable.

Among the 45 companies, 27 companies have already initiated use of IFRS as of March 31, 2014. It was thought that these 27 companies had applied IFRS 1 and, therefore, based on the IFRS 1 information, the compilation of GAAP differences was possible. For that purpose, annual reports for these 27 companies were obtained and the financial statements were analyzed to determine the impact of IFRS adoption. However, it was later found that 2 of the companies did not apply IFRS 1, since sets of IFRS financial statements for these 2 companies were made available to owners or external parties in the preceding year[19]. Furthermore, 6 of them had originally prepared consolidated financial statements in accordance with U.S. GAAP, not JP GAAP.

Consequently, an analysis of the consolidated financial statements for the remaining 19 companies was performed to determine the impact of voluntary IFRS adaption.

Table 1 shows the 19 public companies that have voluntarily shifted from JP GAAP to IFRS.

As has been mentioned in previous sections, there are many differences between JP GAAP and IFRS. Perhaps most notably, the differences related to accounting recognitions and measure-

17) This report issued by Ministry of Economy, Trade and Industry on December 26, 2013

18) 2013 Stock condition survey, issued by Tokyo Stocks Exchange on June 19, 2014.

19) Please refer to IFRS 1.3

Table 1　The 19 public companies voluntarily shifted from JP GAAP to IFRS

Company Nam[20]	Transition date	First-year of adaption
HOYA CORPORATION	1-Apr-08	31-Mar-09
Nippon Sheet Glass Company, Limited	1-Apr-10	31-Mar-10
JAPAN TOBACCO INC.	1-Apr-10	31-Mar-11
DeNA Co. Ltd.	1-Apr-11	31-Mar-12
Anritsu Corporation	1-Apr-11	31-Mar-12
SBI Holdings Inc.	1-Apr-11	31-Mar-12
Monex Group Inc.	1-Apr-11	31-Mar-12
Sojitz Corporation	1-Apr-11	31-Mar-12
CHUGAI PHARMACEUTICAL CO.LTD.	1-Jan-12	31-Dec-12
Rakuten Inc.	1-Jan-12	31-Dec-12
NEXON Co. Ltd.	1-Jan-12	31-Dec-12
SoftBank Corp.	1-Apr-12	31-Mar-13
Asahi Glass Company, Limited	1-Jan-12	31-Dec-12
Takeda Chemical Industries, Ltd.	1-Apr-12	31-Mar-13
Astellas Pharma Inc.	1-Apr-12	31-Mar-13
Ono Pharmaceutical Co., Ltd.	1-Apr-12	31-Mar-13
Sosei Group Corporation	1-Apr-12	31-Mar-13
DAIICHI SANKYO COMPANY LIMITED	1-Apr-12	31-Mar-13
ITOCHU ENEX CO.LTD.	1-Apr-12	31-Mar-13

ments are most important for companies and investors since these differences impact retained earnings (net income) for companies have recently adopted IFRS. For evaluating the impact of these differences, the variations evident in first-time IFRS adoptions were compiled from these 19 companies. Data from opening balance sheets at the IFRS transition dates and first- year IFRS F/S were obtained to determine which items impact the retained earnings of companies having recently implemented IFRS. Table 2 demonstrates the summary of significant GAAP differences for these 19 companies.

Through the above research of GAAP differences, the following findings emerged.

(1) *Optional exception of cumulative exchange differences at first-time adoption*

Exchange differences, which arose from translation of foreign subsidiaries, were recognized as separate components of equity. At the transition date, the cumulative amounts of these exchange differences were principally recalculated and charged to profit and loss, retrospectively. However, the retrospective recalculation proved quite challenging for the companies, and it was not cost-effective. Therefore, IFRS 1 D 12-13 permitted cumulative exchange differences

20) Company name represents the registered English name under the commercial registration act in Japan. Therefore, the name is sometime different from common name.

Table 2 The summary of significant GAAP differences for these 19 companies

Items	Numbers of companies	
	Transition date	First-year
Optional exception of cumulative exchange differences at first-time adoption	15	15
Depreciation method and useful year	12	12
Employee benefits	10	10
Accrued vacation pay	10	10
No amortization of goodwill	—	14
Capitalization of research and development cost	8	8
Provisions for special repairs	7	7
Revenue recognition	5	5

Note
Except for the above items, there are several other differences which were recognized by less than 4 companies. These items were omitted from this paper.

at the transition date to be recorded as null, and registered against the retained earnings. This application had a tremendous impact on Japanese public companies, due to excessive fluctuations in the exchange rate for the Japanese yen over the past 20 years. As listed in table 2, 15 companies applied the optional exception of cumulative exchange differences. At the transition dates, these 15 companies transferred cumulative exchange differences under JP GAAP to the retained earnings under IFRS. The aggregated amount of these differences decreased of 1,577,206 million yen, which represents 25% of the aggregated amount of retained earnings under IFRS at the transition dates. Furthermore, 4 of these 15 companies sustained negative retained earnings at the transition dates, due to these effects.

(2) *Depreciation method and useful year*

As has been mentioned previously, many Japanese companies still use the declining-balance method in conforming to Japanese Tax Law. The declining-balance method normally does not reflect the pattern in which the asset's future economic benefits are expected to be consumed. Therefore, the 12 companies changed their depreciation method from declining-balance method to straight line method or reconsidered their useful years. The aggregated effects of these differences were 121,582 million yen and 129,509 million yen at the transition dates and for the first-year of IFRS, respectively. 129,509 million yen represents 12% of the aggregated net income for these 12 companies over the first-year. For minimizing these impacts, the listed companies, which plan to adopt IFRS in the near future, changed their depreciation method from the declining-balance method to the straight-line method under JP GAAP. As of March 31, 2013, 70 listed companies[21)] changed their deprecation method from the declining-balance method to the straight-line method.

(3) *Employee benefits*

There are no significant differences in this sector of accounting between JP GAAP and IFRS. However, the JP GAAP was amended by ASBJ in May 2012 and went into effect as of March 31, 2014. Therefore, the financial statements under JP GAAP for the first-year (before 2013) were prepared in conformity with the former accounting standards, which had several differences from IFRS. Consequently, 10 companies recognized these differences. Since these differences were solved after April 1, 2014, no further investigation was performed in regard to employee benefits.

(4) *Non-amortization of goodwill*

Under IFRS, goodwill is not amortized. Under JP GAAP, goodwill is recognized as an asset and amortized within 20 years. In table 2, the 14 companies stopped amortizing goodwill for the first-year in conformity with IFRS. The aggregated amount of non-amortization was 247,552 million yen, which represented 21% of the aggregated net income for the 14 companies during the first-year.

(5) *Accrued vacation pay*

Customarily in Japan, many Japanese companies do not recognize accrued vacation pay, since Japanese employees do not generally take long vacation and the unused vacation days are not reimbursed by their employers. As indicated in table 2, 10 companies recognized accrued vacation pay at the transition dates and first-year. The aggregated amount of that accrued vacation pay was 35,954 million yen and 27,864 million yen at transition dates and first-year, respectively. These amounts are immaterial to both the retained earnings and the net income.

(6) *Capitalization of research and development cost*

As mentioned previously, internally generated research and develop cost are often expensed under JP GAAP, as oppose to IFRS which requires the capitalization of development cost when certain criteria are met. In the table 2, the 8 companies from the study capitalized their research and development costs. The aggregated total capitalized R&D costs were 292,205 million yen and 271,099 million yen, respectively. These amounts have had huge impacts on

21) Weekly Report on Financial Accounting No. 3126 reported 70 companies changed their depreciation method from declining-balance method to straight-line method, among all listed companies for the year ended March 31, 2013.

net income. Actually, the aggregated amount of 271,099 million yen represents 65% of aggregated net income for 8 of these companies for the first year.

(7) *Provisions for special repairs*

Some companies, especially manufacturers, accrue special provisions for repairs under JP GAAP. In cases where the companies have applied IFRS, these provisions have to be reversed. As indicated in table 2, the 7 companies reversed the provisions for special repair or other similar provisions at the transition dates and first-year. The aggregated amounts of these reversals of allowance for special repair were 14,406 million yen and 20,036 million yen at transition dates and first-year, respectively. These amounts are immaterial to the retained earnings or net income.

(8) *Revenue recognition*

As described in table 2, the 5 companies adjusted the timing of revenue recognition. The aggregated totals for these revenue recognition adjustments were 27,252 million yen and 28,261 million yen at transition dates and first-year, respectively. These amounts are immaterial to both retained earnings and net income. However, it is of note that 13 companies[22] changed their revenue recognition policy from delivery based to inspection based under JP GAAP. Presumably this step was taken to allow the public companies to adjust their revenue recognition policy before adopting IFRS.

VII. Conclusion

The voluntary adaption of IFRS is a first step towards the perfect endorsement of IFRS in Japan. The voluntary adoption of IFRS has helped enhance the comparability of financial information between Japanese companies and foreign competitors. Furthermore, voluntary adoption has improved the quality of disclosures, as indicated in previous sections above.

One of the main advantages derived from the voluntary adoption IFRS is that Japanese companies can easily raise funds in overseas capital markets, since they have increased their financial comparability with foreign companies in the same line of business. This has been confirmed by the empirical data shown in the research figures above.

Two other primary advantages which derive from the voluntary adoption of IFRS are the ability to unify both external indexes for public announcements and internal indexes for business man-

22) Weekly Report on Financial Accounting No. 3126 reported 13 companies changed their revenue recognition policy from delivery basis to inspection basis, among all listed companies for the year ended March 31, 2013.

agement, since we know that IFRS are unified standards. These unifications have brought about effective budget controls, promoted more efficient operation and avoided cost duplications. This was also confirmed through the empirical figures. To enjoy these advantages, Sogoshosha have decided to adopt IFRS voluntarily.

In addition to the fore mentioned bonuses, there are several major differences between JP GAAP and IFRS worth mentioning. Analysis of differences from 19 adopted companies found that the key differences for Japanese companies are（ⅰ）Optional exception of cumulative exchange differences at first-time adoption,（ⅱ）Non- amortization of goodwill,（ⅲ）Capitalization of research and development cost, and（ⅳ）Depreciation method and useful year. To take advantage of benefits from（ⅱ）and（ⅲ）benefits, many major pharmaceutical companies decided to have voluntarily adopted IFRS.

The path towards the mandatory adoption of IFRS is still a long way off for Japan. The voluntary adoption of IFRS in Japan is likely to continue increasing at a substantial rate for the foreseeable future and Japan will ultimately be seen as a guiding forerunner among countries adopting pure IFRS.

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Discussion of the Presentation by Professor OZAWA Yoshiaki

This session discussed the five questions below. Although these questions are concerned with basic matters, they helped participants expand their understanding about the current status of IFRS. Since the International Academic Seminar is designed to invite the experts from a wide range of fields from accounting to other areas concerning economics and business administration, we made it a point not to let discussions between the presenter and discussant become technical. In the years ahead, however, we expect that experts in South Korea and Japan will have more in-depth discussions about international accounting standards.

1. Why do you think only 45 Japanese companies have adopted IFRS, despite the magnitude of market capitalization?

Many Japanese companies believe IFRS adoption as an extremely costly process, involving consultancy fees and replacement of whole systems. Many companies think that the introduction of IFRS is not beneficial enough for them to justify all these costs. The main reason for this image of IFRS is that companies strongly believe that changing depreciation methods (to the straight-line method) and compliance with the revenue recognition standards are very painstaking processes.

2. What do you think Japanese companies will increase to adopt IFRS by issuing JMIS?

I personally believe that few companies will adopt JMIS. As you know, under JMIS, the companies have to amortize goodwill periodically and have to use recycling of items of other comprehensive items as profit or loss. I think these exceptional treatments from IFRSs would not provide enough benefits for the companies to decide to adopt JMIS.

3. What do you think is the difference between IFRS and JMIS? In particular, what are the special reasons for accounting for goodwill and other comprehensive income in the Japanese context?

These two are the items Japan proposed to IFRS and asked for a change of standards. I think that Japan added these items to JMIS to make its own position clearer.

4. Which accounting method do you think is conservative, IFRS or JPGAAP?

I don't know which is conservative. Each of them has conservative aspects.

5. Why do you think there are industrial differences among firms adopting IFRS for the first time? Specially, why has the pharmaceutical and wholesale trade industries adopted IFRS?

Many competitor of pharmaceutical companies are in Europe and such European companies use IFRS. They make a lot of investments in R & D to develop new drugs, and Japanese companies needed to adopt IFRS to avoid suffering a comparative disadvantage. General trading companies have many subsidiaries around the world; some major trading houses have over 800 overseas subsidiaries. Such companies are believed to have had no choice but to adopt IFRS in order to have common, companywide accounting standards.

(Discussion by NAKAMURA Tsunehiko, Associate Professor of Business Administraion at Momoyama Gakuin University)