

## Accounting in Japan: Some Aspects

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### Résumé de l'article

Nous remercions la Chaire des sciences comptables de l'École des Hautes Études Commerciales de Montréal de nous avoir autorisés à publier l'exposé donné par le professeur Iwanabe lors de son passage à l'École, le 8 novembre 1990. « La comptabilité au Japon : quelques aspects » trace l'évolution de cette discipline depuis la Seconde Guerre mondiale, quoi qu'il faille remonter au siècle dernier pour bien comprendre le système comptable japonais. L'auteur décrit les nouvelles influences américaines depuis 1950, mentionne l'instauration de normes de pratique (« Cost Accounting Standards »), décrit le développement de la gestion comptable et autres principes comptables ou méthodes de vérification. Il termine son exposé sur des statistiques concernant la profession comptable et sur les associations professionnelles.

# Accounting in Japan: Some Aspects <sup>1</sup>

by

Kozo Iwanabe <sup>2</sup>

*Nous remercions la Chaire des sciences comptables de l'École des Hautes Études Commerciales de Montréal de nous avoir autorisés à publier l'exposé donné par le professeur Iwanabe lors de son passage à l'École, le 8 novembre 1990. «La comptabilité au Japon : quelques aspects» trace l'évolution de cette discipline depuis la Seconde Guerre mondiale, quoiqu'il faille remonter au siècle dernier pour bien comprendre le système comptable japonais. L'auteur décrit les nouvelles influences américaines depuis 1950, mentionne l'instauration de normes de pratique ("Cost Accounting Standards"), décrit le développement de la gestion comptable et autres principes comptables ou méthodes de vérification. Il termine son exposé sur des statistiques concernant la profession comptable et sur les associations professionnelles.*

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One of the best ways of gaining a good understanding of today's accounting in Japan might be to observe the evolution of the system established after World War II. But this would not be enough. In order to understand the real situation, one needs to go back into the history of accounting before World War II.

I have stated that studying only the post-modernization period would not convey a complete picture of the history of accounting in Japan and that the pre-modernization period should also be referred

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<sup>1</sup>Cahier N° 4, published under the responsibility of the Chaire de sciences comptables of the École des Hautes Études Commerciales of Montreal. This text was the theme of a speech given by the author at the École des Hautes Études Commerciales on November 8, 1990.

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to. I have also said that Italian bookkeeping was conveyed to Japan in the late 16th century <sup>3</sup>.

However, considering the time and space at my disposal, I shall restrain myself to the evolution of accounting since the Meiji Era, which started in 1868.

## 1. Western-style bookkeeping In the Meiji Era

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When people talk about the history of accounting in Japan, they often set their starting point at the Meiji Era, which corresponded with the beginning of Japan's modernization. To be more exact, I shall start at the year 1873.

Yukichi Fukuzawa put out the first Western-style bookkeeping textbook, *Chooai-no-ho*, in June 1873. It was based on an original textbook on *Common School Bookkeeping* authored by Henri Beadman Bryant and Henry Dwight Stratton.

Also often referred to as the first book on double-entry bookkeeping published in Japan is *Ginkoo-boki-seihou*. This was a translation of *Bookkeeping of Banking* written by Alexander Allan Shand and published in December 1873 — the same year as Fukuzawa's book. Allan Shand, who was born in Scotland, came to Japan to enter the service of the Japanese Government. When the Bank of Japan was established, he was working for the Ministry of Finance and he delivered lectures on bookkeeping to bankers <sup>4</sup>.

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<sup>3</sup>Kozo Iwanabe, "A History of Sixteenth Century Accounting in Europe and Japan," *Social Science Review*, published by Saitama University, March 1986.

Kozo Iwanabe, "Bookkeeping in the Early Edo-Period and Italian Renaissance," *Social Science Review*, published by Saitama University, January 1987.

Kozo Iwanabe, "The Significance and the Contents of A Guide to Bookkeeping for Small Business," *Social Science Review*, published by Saitama University, March 1987.

Kozo Iwanabe, "The Bookkeeping at Katsurariyaku and a Mystery of History," *Social Science Review*, published by Saitama University, February 1988.

Kozo Iwanabe, "Accounting in Edo-Period and the Cultural Aspects," *Social Science Review*, published by Saitama University, March 1988.

Kozo Iwanabe, "The Propagation of Italian Bookkeeping to Japan," *Kaikei (Accounting)*, compiled by the Japan Society of Accounting, June 1989.

<sup>4</sup>Kojiro Nishikawa, *Nihon Boki-gaku Seisei-shi (The History of Bookkeeping in Japan)*, Yusho-do, 1982, 24.

Thus were bookkeeping textbooks from Europe and America translated and published in the early period of the Meiji Era, in the wake of Japan's westernization, concurrently with the introduction of Western-style bookkeeping under the direct influence of foreign accountants employed by the Meiji Government to set up accounting methods suitable to the new social regime.

## 2. Propagation of Western-style and Japanese-style bookkeeping

The establishment of commercial schools in Japan began in the 20th year of the Meiji Era (1887). Bookkeeping was taught in commercial schools and its propagation was promoted. But the environment was not yet ready to assimilate it and it was only in the second half of 1897 that the time became ripe for its propagation.

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In 1895, Naotaro Shimono published the first textbook on traditional Japanese bookkeeping, *Boki Seiri* (Detailed Method of Bookkeeping). In the same year, the Government carried out a reform of the Income Tax Law which had been enforced in 1887 and imposed a tax on corporate income. This helped create a background for a widespread knowledge of bookkeeping.

Meanwhile, merchants who had successfully established themselves in the Edo Period and become wealthy were still using traditional Japanese-style bookkeeping. Famous merchant families, such as the Tanabe family in Izumo Province and Homma family in Dewa Province, continued to use traditional bookkeeping methods. Most small merchants in local districts were also using Japanese-style bookkeeping, mainly Daifuku-cho bookkeeping methods, as late as the first half of 1945.

Despite the introduction of Western-style bookkeeping after the Meiji restoration, Japanese-style bookkeeping was still in general use. This means that people had no particular problems in carrying out business with the traditional Japanese-style bookkeeping. This can also be explained by the fact that Japanese bookkeeping and Western-style bookkeeping are both based on the double-entry system, despite differences in recording styles <sup>5</sup>.

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<sup>5</sup>Kozo Iwanabe, "Accounting in Edo-Period and the Cultural Aspects," *Social Science Review*, published by Saitama University, March 1988, 100-1.

### 3. Accounting regulations in Japan

The first financial statement made public in Japan was issued by the First National Bank under date of December 31, 1873. It was prepared on a Western-style bookkeeping basis, reflecting the fact that many national banks had adopted this basis in accordance with the law.

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But it was not until 1899 that Japan's accounting methods were generally systematized and that Western-style bookkeeping became established. In that year, the Commercial Code was promulgated. It contains articles that refer to accounting. For instance: merchants shall keep and compile commercial accounts, merchants shall submit them, merchants shall keep them in good order.

The commercial accounts referred to in the Code were, at that time, the inventory and the balance sheet. As a general rule, property was to be valued on a market value basis.

A peculiar feature of Japan's Commercial Code is that it was drafted under the direction of Karl Friedrich Herman Roesler, a German lawyer in the employ of the Meiji Government<sup>6</sup>. Consequently, there is a strong influence of Germany's old 1861 Commercial Code reflected in Japan's Commercial Code.

The Commercial Code was substantially amended in May 1950 — shortly after World War II. Since then, it was again amended in April 1962, April 1974, and June 1981. But the basic structure remains unchanged and is still holding on today.

Accounting functions were handled by in-house specialists and it was only in 1927 that professional accountants were given legal recognition. In that year, the Registered Public Accountants Law was promulgated. It instituted the first accounting profession in Japan.

In order to become a Registered Public Accountant, one had to register and pass an examination. Accounting graduates from a university or vocational college were exempted from the examination.

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<sup>6</sup>Kiyoshi Kurosawa, "100 Year History of Accounting Systematizing in Japan," *Kindai-kaiki Hyakunen (100 Year History of Modern Accounting)*, JAA, 1978, 21.

The Law was repealed in August 1948 when the Certified Public Accountants Law was promulgated.

#### 4. Accounting regulations before World War II

Before World War II there were special accounting regulations for certain industries, such as banks, insurance, electricity, railways, etc. These regulations prescribed the form in which the balance sheet, inventory and profit and loss statement were to be prepared.

But things were different in the case of other industries. There was no standard to be observed. In 1934, the Industrial Efficiency Bureau of the Ministry of Commerce and Industry issued a *Rule for the Preparation of Financial Statements* which standardized the form of financial statements and the titles and classification of items in the financial statements in those industries.

In addition, a *Rule for Manufacturing Cost Accounting* was issued in 1937 by the Financial Administration Council of the Ministry of Commerce and Industry.

Meanwhile, the Armed Forces of Japan also set up cost accounting standards. These aimed at the determination of prices for military procurement. In 1939, the Army issued *Guidelines for Cost Accounting in Army Factory for Military Supplies* and in 1940 the Navy issued *Rules for Cost Accounting In Army Factory for Military Supplies*. Some analysts point out that the former carry some German character while the latter are somewhat American in their character<sup>7</sup>. These two guidelines were later combined into *The Essentials of Cost Accounting*, issued in 1942 by the Planning Agency.

In 1940, the Army Ministry put out a *Guideline for Estimating an Optimum Rate of Profit*. The Ministry published in the following year (1941) a *Budgetary Control Guideline*, an *Administration Comparison Guideline*, and a *Financial Comparison Guideline*. Despite their excellent contents, these guidelines were not mandatory. Furthermore, the war situation got worse before corporations

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<sup>7</sup>Nobuo Kawai, "Development of Accounting System," *Sengo Kigyo-kaikei Seido no Tenkai* (Development of Corporate Accounting System in the Postwar Days), ed. N. Kawai and T. Terajima, Horitsu-bunkasha, 1983, 4.

had the leisure to plan production and put the guidelines into practice. It was therefore out of the question that they could find their permanent way into accounting methods.

## 5. Accounting regulations after World War II

Japan's accounting was mainly influenced by Germany's until the end of World War II. Since then, it has been directly influenced by American theory and practice.

100 In 1947, the General Headquarters of Allied Nations asked holding companies of financial groups to submit their financial statements. This was intended with a view to dismantling the Zaibatsu (financial group alignment).

As there were a number of obscure accounting items in the financial statements so submitted, the General Headquarters issued an *Instruction for the Preparation of Financial Statements of Manufacturing and Trading Companies* which aimed at standardizing the financial statements. This marked the starting point for the modernization and standardization of Japan's accounting along the American pattern <sup>8</sup>.

As I mentioned before, the Commercial Code was substantially amended in 1950. The German-type system of divided stock was abolished and the American-style authorized capital system was introduced instead.

The tax system was also amended. In 1947, the tax levying system was changed to a return filing system. The number of income taxpayers, which was 1.88 million in 1939, had increased to 18.85 million in 1947. Furthermore, the tax system underwent a great change in 1950 in the wake of Dr. Karl Shoup's recommendations of 1949. It was entirely reorganized, including the establishment of a Blue Return System under which taxpayers filing a return were required to submit financial statements with the bookkeeping documents attached.

In December 1949, the Business Accounting Investigation Committee of the Economic Stabilization Board submitted to the

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<sup>8</sup>See *supra* Note 7.5.

Government a *Guide to Bookkeeping for Small Business*. This guide, which had been prepared mainly by Torao Nakanishi and Tatsu Nabeshima, was intended as a guideline for small and medium-size enterprises <sup>9</sup>.

In July 1949, the same committee had released *Financial Accounting Principles (or Standards)*, a report prepared by leading accounting scholars headed by Kiyoshi Kurosawa. Although the opinions and proposals it contained were not mandatory, the report followed the General Headquarters' *Instruction*. Furthermore, it was adopted as a standard for Certified Public Accountants under the Certified Public Accountants Law which was introduced in line with the Securities and Exchange Law in 1948.

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Under these circumstances, the report came to exert profound influence on Japan's financial accounting and its leadership extended to big enterprises as well as smaller corporations.

## 6. Establishment of Cost Accounting Standards

In March 1948, the Price Agency established *Cost Accounting Standards* on the basis of the Price Control Regulations. As these were only a reworking of the *Guide for Cost Accounting* published by the Planning Agency in 1942 for the purpose of making price decisions in the wartime economy, there was a need for new cost accounting standards to match with the postwar restoration.

For this purpose, a Business Accounting Deliberation Council was set up by the Ministry of Finance in December 1950, with Tarao Nakanishi as Chairman. However, it was only in November 1962, or 12 years later, that the Council issued the new standards. Indeed, it had taken a long time.

The reason for this long delay was that the Council had to make lengthy and careful discussions — especially on how to coordinate the objectives of financial accounting and those of management accounting. The council took a long time reaching a final conclusion on this point.

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<sup>9</sup>Kozo Iwanabe, "The Significance and the Contents of A Guide to Bookkeeping for Small Business," *Social Science Review*, published by Saitama University, March 1987.



Another reason for the delay was the time spent on coordinating predetermined cost, including standard cost, and actual cost, for tax purposes.

The good thing about the standards is that the time and energy spent on their preparation enabled the Council to debate the issues thoroughly and set a new trend in management accounting. It produced a high quality report which meshed well with the existing *Financial Accounting Principles*. Indeed the *Cost Accounting Standards* held out against environmental changes in the Japanese economy and provided a strong support to Japan's high economic growth.

Meanwhile, the Japan Productive Center established a Cost Accounting Committee for Medium and Small-size Business, with Torao Nakanishi as Chairman. The Committee put out *Cost Accounting for Medium and Small-Size Business* in 1958. During the next decade, cost accounting standards for medium and small-size business — classified by type of business — were developed and made public <sup>10</sup>.

This led to a nation-wide movement to propagate the concept. As a result, cost awareness began to take root within Japan's medium and small-size enterprises and, through them, contributed much to support Japan's economy.

## 7. Development of management accounting

Toward 1935, industrial rationalization plans promoted by the Government led corporations, on an individual basis, to adopt budgeting systems. Although the trend spread among Japanese corporations, it was only in the 1950's, after World War II, that budgeting was adopted by corporations in a systematic form.

One of the factors which were conducive to the universal adoption of budgeting was that the Government and its agencies put forth guidelines for managerial control that centered around budgeting.

In 1951, the Rationalization Committee of the Ministry of Trade and Industry released *Internal Control Systems for*

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<sup>10</sup>Tatsuro Yamaguchi, "Postscript," *Keiei to Kaikei no Kihon-mondai (Basic Issues of Accounting and Management)*, ed. Tatsu Nabeshima, Chikura, 1986, 254.

*Corporations* at the request of the Government. The report recommended the introduction of American-style managerial methods.

The Industrial Structure Council of the Ministry of Trade and Industry issued one report after another in reply to questions raised by the Government: in 1960, *Profit Control by Divisional Organization*; in 1966, *Cost Management — New Concepts and Methods for Cost Reduction*; and in 1972, *Ideal Methods of Corporate Financial Policies*.

In an opinion released in 1972, the Council encouraged corporations to look at the concept of management from a different angle.

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They should free themselves from the conventional management philosophy which places too much emphasis on increasing profit by expanding market share. Recognizing that factors such as environmental pollution and consumer movements pose increasing difficulties for corporations, the Council stressed that each corporation should take into account the interests of local residents and consumers in formulating its objectives.

Professors Torao Nakanishi and Tatsu Nabeshima, who contributed much to the establishment of cost accounting standards, expressed their views on corporate management philosophy in *Today's Management Philosophy and its Features*, a book published by the Japan Productivity Center in 1965. They emphasized the social responsibility of corporations. They also explained in detail how management accounting can be a means of improving productivity. The book had a great deal of influence among Japan's industrial circles and became very helpful in educating Japanese management.

In addition, Professors Nakanishi and Nabeshima co-authored in 1973 a book attuned to the forthcoming age, *New Economic Trends and Corporate Management*. It was published by the Japan Productivity Center. The authors clearly explained the basic links between corporations and the national economy and between the national economy and the international economy. In 1975, the Japan Productivity Center celebrated its 20th anniversary by staging a public platform on "Productivity in the Forthcoming Age."

As you must be aware, Japanese management philosophy is based on corporate social responsibility and public service. This

concept, which originated with the Government and economic groups, was well understood by both management and labour unions. Thus, a new management philosophy was firmly established. It worked so successfully that Japan overcame the world recession that resulted from OPEC's crude oil price hike in 1973.

104 In the meantime, a study group made up of representatives from leading corporations was set up under the chairmanship of Professor Nakanishi. In 1969, the study group launched a study of coordinated computerized accounting information systems <sup>11</sup>. When Professor Nakanishi died in 1971, Professor Nabeshima succeeded him as Chairman. In 1987, the study group put forth a report on the results of its study. The report examines how management strategies have relevance to the development of new theory and practice in the middle of widespread office automation.

## 8. The Commercial Code and Financial Accounting Principles

Financial Accounting Principles in Japan have been orientated toward achieving correctness in the profit and loss statement, as advocated in the United States (dynamic accounting). In the U.S., profits and losses are calculated on an accrual basis and assets are valued on the historical cost basis. Contrarywise, the Commercial Code prescribed the inventory method of calculating income, as advocated by German accounting, and the valuation of assets at less than current prices.

At the time of their development, the Financial Accounting Principles were therefore at wide variance with the accounting methods prescribed in the Commercial Code.

When the Financial Accounting Principles were put into effect, it was strongly requested that they be given precedence over the accounting provisions of the Commercial Code, tax legislation and other related regulations. This resulted in numerous amendments to the computation rules in the Commercial Code. The historical cost basis was substituted as the basis of asset valuation and the lower of cost or market basis was also introduced. But those amendments

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<sup>11</sup>Torao Nakanishi, *Keiei-keizai-gaku Ronbun Sensyu (Selected Works of Dr. Torao Nakanishi)*, Chikura, 1980, 242.

did not resolve all the discrepancies between the Commercial Code and the Financial Accounting Principles.

In view of this, the Financial Accounting Principles were amended in 1963. This time, discrepancies were resolved in favour of the Commercial Code, an indication of the powerful status of the Code. The amendments were described in the preamble of the Principles.

In addition to weakening the leadership of the Financial Accounting Principles, this caused confusion in the practice of corporate accounting. For example, no regard was paid to the principle of consistency by all but the few enterprises which kept their accounts in compliance with the Commercial Code. Likewise, Article 287 of the Commercial Code dealing with reserve accounts was so widely applied that reserves for profit were sometimes created.

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Two amendment proposals were put forth, both of which were criticized. In 1974, the Financial Accounting Principles were amended in accordance with a revised draft of these proposals. The principle of consistency was reconfirmed, but reserves for profit continued to be allowed.

As regards the form of financial statements, the Principles were changed to stipulate the all-inclusive income concept and the rules in the Commercial Code were amended accordingly, the two sets of amendments being coordinated. In the 1981 amendments to the Commercial Code, all kinds of reserves for profit were prohibited and the special reserves under Article 287-2 were limited to expenses. The Financial Accounting Principles were partly amended accordingly, save for an item of liability reserves.

## **9. The Certified Public Accountants System in Japan**

Japan's Certified Public Accountants system started in July 1948 with the passing of the Certified Public Accountants Law, which replaced the Registered Public Accountants Law. The new designation was intended for professional accountants with a high standard of character and judgement.

Just three months before the Certified Public Accountants Law was adopted, so was the Securities and Exchange Law. This piece

of legislation was largely inspired from the American Securities and Exchange Law.

Japan's Securities and Exchange Law was adopted in the middle of a movement for the democratization of the securities and exchange business and disbandment of the *Zaibatsu* (financial group alignment). With the advent of the Law, all companies listed on a stock exchange became subject to audit and certification of their financial statements by an independent public accountant having no direct interest in the company.

106 The new audit and certification requirement under the Securities and Exchange Law made it necessary to put the corporate accounting and audit systems in viable condition. The following rules and regulations were issued accordingly: in July 1949, *Financial Accounting Principles* and in September 1950, *Audit Standards* and *Working Rules of Field Work*.

Based on these rules and standards, *Rules on Terminology, Form and Procedures for Preparation of Financial Statements* and *Rules for Audit and Certification of Financial Statements* became effective in January 1951. The audit of companies listed on a stock exchange started in July 1951. At that time, there were more or less 450 companies subject to audit, and the number of Certified Public Accountants was less than 400<sup>12</sup>.

In the beginning, auditors were putting the emphasis on the role of internal control and internal audit systems as checks on the reliability of the accounting system. Therefore, audits were partially carried out through unique methods. In December 1956, the *Audit Standards* were amended. The *Working Rules of Field Work* were also entirely revised and *Audit Reporting Standards* were put into effect. The full-scale audit of financial statements started in January 1957.

The Certified Public Accountants system experienced ups and downs in line with the expansion of companies and the ensuing increase in the number of companies subject to audit. The system thus began to take root in society.

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<sup>12</sup>Nihon Konin Kaikei-shi Kyokai (The Japanese Institute of Certified Public Accountants), *Konin Kaikei-shi Seido no Ayumi (The History of CPA System in Japan)*, 1983, 12.

During the second half of 1964, many companies went bankrupt one after another. The most remarkable case was that of Sanyo Tokushu kou (Sanyo Special Steel Co. Ltd.); the window-dressing that came to light caused a big social commotion.

This led to a revision of the CPAs Law in 1966. The Japanese Institute of CPAs was reorganized into a special corporate body and audit corporations were introduced.

Meanwhile, the Japanese economy was becoming international, capital transactions were becoming more liberal and the securities market was expanding. Things were changing dramatically around the securities market.

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In view of the changing business environment, the disclosure system was revised in March 1971 for the first time in 18 years and the provisions of the Securities and Exchange Law pertaining to rationalization were thoroughly revised. This was designed to strengthen the protection of investors.

In 1972, foreign corporation stocks were offered for public subscription for the first time in Japan. In 1973, a full-scale liberalization of capital was evolving and foreign companies began to be listed on Japan's securities market. As these movements gained momentum, the capital market became more and more international, causing Japanese CPAs to get more and more international-minded.

## 10. Japan's audit system

In Japan, audits are performed by CPAs. But an audit system existed under the Commercial Code before the Securities and Exchange Law was put into force. The Kansayaku, auditors appointed under the Commercial Code, were already performing audits. This raised the problem of how to bring the existing Kansayaku system in line with the new CPA system. It took a long time to resolve this problem.

In 1974, the audit provisions of the Commercial Code were amended. A new audit system was introduced. It required that all companies with a capital exceeding 500 million yen, whether or not governed by the Securities and Exchange Law, were subject to audit by an accounting (Kansayaku) auditor appointed under the Commercial Code as well as by a CPA or audit corporation. Along

with this amendment, the Kansayaku was given additional responsibility for operational auditing. Previously, he had been responsible only for financial auditing. (The application of the new rule was limited to companies with a capital exceeding 100 million yen.)

In this way, the audit under the Securities and Exchange Law and that under the Commercial Code came to meet each other in practice, and the audit system was thereby strengthened.

108 Even in those days, however, the appointment of the accounting auditor was subject to approval by two thirds of Kansayaku auditors and to a resolution of the Board of Directors. His term of office was not limited. The Board had the right to dismiss him by a resolution of two thirds of its members. There was still a big problem with the independence of the accounting auditor.

To solve this problem, the Commercial Code was amended in 1981 to require that both the accounting auditor or the Kansayaku auditor be appointed by a general meeting of shareholders. At the same time, the spectrum of companies to be audited by an accounting auditor was expanded to cover not only companies to which the Securities and Exchange Law was applicable, but also companies with a capital exceeding 500 million yen, as well as companies with liabilities amounting to more than 20 billion yen.

In 1965, the Minister of Finance referred the question of consolidated financial statements to the Business Accounting Deliberation Council. He was aiming at strengthening the audit system and his request was one of the measures he had in mind for this purpose. After various discussions, *Accounting Principles (or Standards) for Consolidated Financial Statements* were issued in 1975.

The preparation of consolidated financial statements and their audit by a CPA became effective in April 1977. In the first year of application of the new measure, that is the year ended March 1978, a total of 1,467 companies submitted negotiable securities statements. Out of these companies, a total of 494 were covered by the new measure and they had an average of 5.5 subsidiaries <sup>13</sup>.

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<sup>13</sup>See *supra* Note 12, 16.

The field of activities of Japanese CPAs has been extended from companies to schools. In 1970, the Private School Law was amended to cope with prevailing campus disturbances. At that time, *Accounting Standards for Schools* were issued by the Ministry of Education and school foundations which were receiving subsidies from the state and local public organizations were required to carry out prescribed accounting procedures and have their statements audited by a CPA.

In 1971, the Law was applied to universities and junior colleges which were under the authority of the Minister of Education, and its application was further extended to school foundations under the authority of a governor. In 1975, the Private School Promotion Subsidization Law was promulgated, which requires most private schools such as high schools, junior high schools, primary schools and kindergarten to have their financial statements audited.

As of July 25, 1990, the Japanese Certified Public Accountants Association had a membership of 8,701 Japanese, 18 foreigners and 99 audit corporations, totalling 8,818. In addition, there were 1,933 assistant CPAs registered as junior accountants. The number of companies which are submitting negotiable securities statements to the Ministry of Finance comprises 3,320 Japanese and 381 foreign entities as of August 1990.

## 11. Japan's tax accounting

There are two kinds of professional accountants in Japan, Certified Public Accountants (CPA) and Certified Tax Accountants (CTA). CPAs take care of the audit of large companies, while CTA handle tax services for small and medium-size companies. Certified Tax Accountants carry on an agency and tax consulting business, preparing tax documents and tax returns to be submitted to tax offices.

To qualify as a Certified Tax Accountant one has to pass an examination, or else be a lawyer or a CPA. He must also register with the Japanese Federation of Certified Tax Accountants' Association.

There are now 56,000 Certified Tax Accountants in Japan and they serve a population of 1,800,000 corporations and 1,300,000 individual businessmen.



As I mentioned before, Japan's accounting is governed by the Financial Accounting Principles and the Commercial Code. In addition, it is strongly influenced by tax rules. Depreciation is a case in point. It is computed under one of two methods (straight-line and declining balance) specified in the Income Tax Law, on the basis of such useful life as is determined in detail by a Finance Ministry Ordinance. The mining industry has the further choice of depreciating its assets under a production method.

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I would like to draw the attention to the fact that the useful life of depreciable assets is changing over the time as a reflection of the Government's high economic growth policies. If the useful lives fixed in 1947 are compared with those in effect in 1951, one will find them shortened by 20 per cent. This means that the revised useful life was shorter than the actual useful life. Useful lives were again reduced by 20 percent in 1961, and by a further 15 per cent in 1964. This action was taken in recognition of the obsolescence of facilities in an age of technical innovation. At the same time, it aimed at raising the ratio of depreciation in capital assets <sup>14</sup>.

Let me give another example of tax policy. In 1957, the Special Taxation Measures Law was promulgated in order to allow various kinds of tax advantages to certain industries, businesses or regions. These preferential tax treatments proved to be very useful to strengthen the economic power of companies. In 1965, the Corporation Tax Law was completely overhauled. All those laws are supplemented by Finance Ministry Ordinances <sup>15</sup>.

## 12. Academic accounting societies in Japan

Nowadays, most of the accounting scholars in Japan belong to the Japan Accounting Association. The Japan Accounting Association was established in 1937 by 90 accounting scholars from universities and high schools.

Another group, the Japan Society of Accounting, had been founded in 1917. It consisted chiefly of businessmen and had a total of 1,000 members. It was not an academic society in the strict

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<sup>14</sup>See *supra* Note 7, 24.

<sup>15</sup>Masato Kikuya, "Accounting and the Profession in Japan" (in English), *Bulletin of Nihon Junior College of Economic*, July 1990, 4.

meaning of this term, but a society to educate people and propagate the knowledge of accounting. Although the society is still issuing a magazine, *Accounting*, its activities virtually came to an end in 1943.

The Japan Accounting Association was established by and is composed of scholars only. It interrupted its activities in 1944 because of the war, but resumed them in May 1948. It has contributed much to the development of accounting in Japan from the postwar period to this day.

Its activities include a national assembly held once a year and regional meetings in six districts. At the national assembly, individual members used to present study reports freely. In addition, there were three thematic divisions: financial accounting, cost accounting and audit. Study reports were presented and discussions were made in each division.

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The Japan Accounting Association was the only academic accounting society until the Japan Cost Accounting Association was founded in December 1975. But from the time when its members exceeded 1,200, a specialized academic society was established for each division through the personal connections of leading scholars. As of September 1990, the number of members in the Japan Accounting Association is 1,649.

As for the Japan Cost Accounting Association, it aims at promoting academic activities among its members, consisting of scholars and businessmen, in the area of cost accounting, one of the most important fields of accounting.

In May 1978, the Japan Auditing Association was founded. It is said to have developed from a parent organization, Kansai Audit Association. It got its start as a pure auditing scholars' society, but it later opened its membership to audit practitioners with remarkable achievements as well as to law scholars who are interested in auditing. It also admits audit corporations as special members.

As far as I know, there are twelve accounting associations in Japan. But it seems that there must be more. Following is a list showing the name of each association and the year of its foundation.

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**Accounting Associations in Japan**

	<b>Name of academic society</b>	<b>Year of foundation</b>
<b>112</b>	• Japan Accounting Association	1937
	• Japan Cost Accounting Association	1975
	• Japan Auditing Association	1978
	• Accounting History Association	1982
	• Japan Association of Business Analysts	1984
	• Japanese Association for International Accounting Studies	1984
	• Japanese Bookkeeping Association (tentative name)	1985
	• The Japan Society for Social Science of Accounting	1986
	• Japan Corporate Social Accounting & Reporting Association	1988
	• Association of Accounting in Mathematics (tentative name)	1988
	• Association of International Studies for Public Sector Accounting (tentative name)	1989
	• Japan Tax Accounting Association	1989

**Afterwords**

I have given a general view on the historical development of Japan's accounting in terms of individual divisions, such as financial accounting, management accounting, auditing, etc. I have also given an outline of the professional accountants and associations of accounting scholars and practitioners. Accounting covers a wide sphere, and Japan's accounting developed in a particular environment indigenous to Japan.

The various accounting systems in place in Japan today are derived from accounting skills and theories developed in Europe and

the United States. So I am confident that accounting in Japan is playing as important a role in society as it is in other countries. Nowadays, people in Japan talk about the necessity of internationalization. They use the word *internationalization* here and there as a kind of slogan to describe what they think they should do.

Perhaps it is the wave of internationalization that carried me here to deliver this speech.