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# **COST ACCOUNTING IN JAPAN: HISTORICAL EVOLUTION, CONTEMPORARY PRACTICES AND BEHAVIOURAL DIMENSIONS**

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## **Abstract**

The current research aims to shed light on cost accounting in Japan. It begins by providing a historical introduction to cost accounting in Japan, including the most important standards issued since the 1930s, the reasons for their change, and their role in the Japanese national economy. This is followed by a description of the Japanese cost accounting system, its most important functions and objectives, and the role cost accounting has played in practical human resources education in Japan, such as universities and academic institutions. Furthermore, a space is devoted to presenting cost accounting techniques, Japanese society's preferences for the most important of these techniques, and the reasons behind these preferences. The research also highlights the behavioural aspects practiced by Japanese companies and how to motivate workers to decrease costs rather focusing on the control of cost. It also examines the key features of cost accounting management as a collaborative method and a common language between the firm, its clientele, and dealers.

**Keywords:** Japanese cost accounting systems, job costing system, sales costing system, objectives and functions of Japanese cost accounting, standard costing method.

## **Introduction**

Before World War II, Japanese cost accounting systems were influenced by those of UK and Germany. After the war, they also received their share of influence from the United States. Therefore, it is said that the process of establishing Japanese cost accounting standards owes much to Western influence. However, it is difficult to discern this influence in contemporary practice, as we find Japanese cost accounting systems completely different from those found in Germany, the USA, UK, and several EU states. This is due to the nature of Japanese society, which has devised a unique management strategy based on concepts and principles that it has added over time, such as collectivism, participation, quality, continuous improvement, and continuous innovation. This has achieved rapid economic growth for Japan, placing the country among the advanced industrial nations. Historical Introduction

The literature agrees (Kurosawa, 1943; Ota, et al., 1983; Yoshikawa, 2001): Historically, the process of establishing Japanese cost accounting standards went through three stages. The first stage involved the Navy and Army establishing their rules of cost accounting in 1937, when the Sino-Japanese War broke out. This was followed by rules in 1939 and 1940. It is worth noting that these standards were intended to control munitions prices. Unfortunately, however, these rules caused problems for the entire industrial sector, leaving the Japanese government in need of a comprehensive accounting rule. As of April 1942, the Guide to Manufacturing Cost Accounting was issued to replace the Navy and Military cost accounting rules. Such manual was intended to regulate product rates and rise management efficacy because of The Second World War. The ensuing stage was revolving around the issuing of the rule of cost control accounting for the aim of price regulation and control, effective since 2 March 1948. After Japan suffered an economic slump following WWII, the economy gradually stabilized, and the administration created determinations to convalesce efficiency. A remarkable result of this procedure was the presentation of a contemporary structure for cost accounting. In 1962, regulations were issued in the Cost Accounting Standards (Yoshikawa, 2001), which Japanese managers in the Japan Cost Accounting Association sometimes utilised to distribute expenses founded on employment prices, even though labour costs embody merely a minor fraction of the entire charges. This distribution was built to emphasis project locomotive engineer' devotion on growing production throughout mechanisation and manipulating workers.

### **Key Goals and Operational Functions of Cost Accounting in Japan**

Japanese cost management is essentially one of the most important operational tools for engineers and middle and lower-level managers, as the importance of cost stems from the control and routine decision-making process. Japanese management is characterized by a strong orientation of cost accounting toward behavioural aspects, motivating employees to reduce costs from their own positions rather than controlling costs. Notably, cost accounting operates as an integrated package of Modern operational systems and costing techniques are represented by applying just-in-time model (JIT) creation, quality control, and target costing. (Okano, 2005) The function of auditors and accountant in Japanese corporations was largely administrative, and indispensable preparation and controller purposes were vicarious to trade companies, workshops, industry partitions, which have entertained relative autonomy.

Japanese managers prefer to use cost accounting to deliver physical non-financial, and supply active knowledge, unlike US executives who favour world-wide and monetary measures. Cost accounting/management systems are also decentralized to provide seamless services on demand. Japanese accountants aim to divide the company's main objective into smaller objectives that express the company's strategic plan. These smaller objectives are distributed among employees to achieve the main objective. Japanese cost accounting thus appears as a tool for global competitiveness and strategy. The decentralized system is also embodied in cost accounting through finance centres, which form groups divided according to machinery or manufacturing, sales, and support departments into smaller groups of five to ten people, whose task is to inventory. Costing was based on a straight estimation scheme, and cost administration pointers such as efficacy per hour and contrast of real vs. premeditated

incomes were utilised. The impression was that contractors and the corporation must raise together, rather than the corporation rising at the cost of contractors. A renewed "collectivist" philosophy appeared in this area, and Japanese cost accounting appeared to be addressing. There is a common understanding within and outside the company. Therefore, some see cost accounting/management as a common language between buyers and suppliers, and as a practical learning tool because employees are trained primarily internally and through job rotation, rather than at universities. Technical departments in Japanese executive management also contribute to accounting tasks, with engineers contributing to cost reduction programs.

### **Traditional Japanese Cost Accounting Systems**

There are two predominant systems in Japanese cost accounting. The author (Yoshikawa, 1989) reports that records from more than 88 of the 137 companies in the study sample showed two systems: job costing and sales costing. The second, more common, is based on batch costing, which is believed to have originated in Deutschland (Accounting Study Office of Kobe University, 1984). It is basically implemented to all types of light industries, such as food and chemicals, and heavy industries, such as automobiles.

Product cost is determined by adding the entire unswerving prices of the procedure desirable billed combined charges. Yoshikawa (2001) provide a worthy illustration of how to calculate product costing. Namely, it is predictable that creation X is factory-made throughout procedures A (forming), B (foundry), and C, and product Y throughout procedures A, B, and D. Hence, the charges of product X strongminded by the lot costing scheme are the entire straight prices of procedure C and the joint costs allocated to processes A and B. The costs of product Y are the direct costs of process D and the joint costs allocated to processes A and B. One of the key causes for or the popularity of batch costing systems in Japan is the preoccupation of manufacturers with developing economical production systems.

### **Japanese Cost Accounting Techniques**

Companies listed on the Japanese Stock Exchange have committed to using the issued cost accounting standards in disclosing their financial statements. In this regard, we utilized the results of a study (Kawano, 2014), whose results we divided into three questions: First, what is the preferred costing method for Japanese companies? What are the companies' justifications for using the selected costing method? Do Japanese companies use costing methods that are supportive of the primary method used by companies? Participants' responses revealed that 68% of those surveyed by the author between 2011 and 2014 use standard costing. A significant feature of this study is that its results revealed a much higher percentage than previous studies of the usage of typical cost accounting and how to categorise variances based on subtracting actual costs from standard costs.

The answers to the second question, which focused on the reasons for using standard cost accounting, were divided into two parts. The first included the responses of 53 companies, representing 56%, regarding cost control and reduction. The second part included the responses of 16 companies, representing 17%, regarding the purpose of preparing planning budgets. The third part indicated that 13% of respondents had attempted to use ABC as a

specific tool for studying costs. Some businesses, clinics, banks, and home-grown communal institutes (gas, water, transport networks, hospitals, electricity, etc.) have also endeavoured to utilize the ABM/ABC system to manage costs and expenses. Though, they occasionally misinterpret the spirit of this system. The Osaka City Waterworks Bureau has unconfined cost information by cost centre (waterworks activities) annually since 2005, and the bureau calls its costs ABC. However, the technique actually implemented is nothing but a meek combination of costs by cost centre, not ABC (source: <http://www.city.osaka.lg.jp/suido/page/0000017062.html>).

The literature (Okano and Suzuki, 2007) links “Japanese cost accounting to accounting and management techniques commonly used by Japanese firms, most notably target costing practices, which Toyota is considered the first to comprehensively develop. By studying Toyota, Okano & Suzuki argue that the achievement of several foremost Japanese companies is attributable to main descriptions explicit to Japan in running accounting practices. The Japanese literature also indicates that various protuberant scholars maintain that target costing is neither costing nor accounting, but rather a recurrent and give-and-take communication strategy and act that allows whole revenue management and planning (Tani, et al. 1993; Tanaka, 1989; Sakurai, 1997; Monden & Hamada, b1993; Kato, 1994).

In this regard, researchers (Yoshikawa, 1994, 2001; McMann & Nanni 1995) conclude that the concepts of “cultural” and “social” are what add specificity. For Japanese management, this point should be understood considering Japanese management's efforts to develop what is called "on-the-job training" (OJT), for instance, as a device that enables unceasing development. In the late 20<sup>th</sup> century, Japanese companies also introduced the Just-in-Time (JIT) production system and Kaizen costing, which focuses on continuous improvement practiced by employees at their work sites daily.

However, there is a group with a different view (Tsuji, 1971), who argues that Japanese accounting literature indicates that most cost accounting techniques are imported from the West. He goes on to explain that if we exclude the cultural and social concept of target costing, it appears to be a mathematical formula: Target selling price - Target profit = Target cost (Sakurai, 1989; Tanaka, 1995; Yoshikawa et al., 1994). It has also been found that the progress of control over and above limits and average costs has conventionally been reviewed in straight connection to the prominence of scientific management (Solomons, 1952; Epstein, 1978).

The quality control system (Odaka, et al., 1993; Ishikawa, 1984) is considered key features of Japanese expansion. It is characterized by being a day-to-day practice rather than a focussed or specialised custom. Japanese management aims to construct each worker in A corporation aware of its goals and plans, particularly in the area of costs, must contribute from its position and area of expertise, and through the execution of its daily duties, to reducing costs, shortening delivery times, and working professionally and skilfully, adhering to pre-established measurements and standards to maintain quality and reliability, which ultimately contributes to quality.

Japanese management also distinguished itself by not linking the performance evaluation of employees and managers to quality management but rather linking it to the contribution of individuals to continuous improvement, cost reduction, shorter delivery times, and reliability.

(Okano and Suzuki, 2007) argue that Total Quality Control (TQC), methodically expressed by US trait regulator specialist A. V. Feigenbaum, was announced in Japan. Compared to its practice in the United States, TQC was a stand-alone system, employing specialized personnel, and based on arithmetical approaches that combined the thoughts of W. A. Shewhart exclusively on quality assurance and control.

Primarily, in Japan, TQC was pondered in the communications division, nonetheless it was subsequently indorsed in numerous diverse subdivisions throughout CCS organisation choices prearranged by Allied Power's H.Q., Public Infrastructures Division (Goto, 1999). Ultimately, TQC grown into a cooperation-wide quality control (CWQC) scheme that incorporates roughly all workers. Mr. Taiichi Ono of Toyota also occupies a pivotal role through his involvement in a report tour in the US, which focussed on the undertakings of cost accounting practices to cultivate Japanese production centre systems and progress the Japanese control systems. Upon his return, he contributed to the development of these methods and laid the foundations of what we know today as the Just-in-Time (JIT) system.

Okano and Suzuki (2007) show that at NEC, additional thoughtful efforts were created to implement normal costing. In 1953, the corporation established a 'double standard costing system,' which separated the aim of standard costing into two key fragments: one for record assessment (Accounting for financial reporting) and the other for managerial accounting (cost management). For the latter, however, NEC dedicated on accountability accounting, organisation by exclusion, and koto-mai management (i.e., before special effects hit or fundamental organisation). First, accountability accounting required responses to enquiries concerning who was accountable for what variance and cost. The second key notion, 'management by exception,' was, as is usually comprehended, the basis of technical Management based on cost analysis. Standards, comprising recognising the causes of deviancies from the standard. Third, the focus of koto-mai management was on examining causative associations, which was considered indispensable for planning a supplementary consistent and proficient manufacture system in the following phase. Given the fact that costs once incurred become irrecoverable, koto-mai management proved indispensable compared with ordinary standards, which could later be established as the thought of kaizen (unceasing development) costing.

It is difficult to discuss cost accounting techniques without examining Toyota's experience (Toyota Motor Corporation, 1987), which in 1950 founded the concept of "maintenance costing" to maintain low vehicle costs within the scope of periodic financial accounting. Applying the notion of maintenance costing necessitated the recognition and creation of diverse standards, predominantly standard cost figures, which, in Toyota's rapports, embodied "standard costing." In the early 1960<sup>s</sup>, the management of Toyota company distributed the cost management procedure into three main phases: kaizen costing, maintenance costing and target costing, intriguing a distinctive approach to all these three phases. As of 1961, the car maker commenced developing the Kaizen costing procedure by means of enhancing programs to considerably decrease defect costs, for example claims costs, damage costs and rework costs along with and by implementing value analysis and value engineering (henceforth as VE/VA)<sup>19</sup>, which transported dealers into the cooperative industrial process.



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### **Integrating management practices and methods with cost accounting at the company level**

Japanese companies have used some management methods and practices in a manner that is integrated with cost accounting, most notably Hoshin Kanri (Ueno & Scarbrough, 2016), "a management methodology extensively expended among Japanese producers as from the 1960<sup>s</sup>. It is a supervision methodology related to Total Quality Control (TQC). In short, it is an intricate and complex plan that incorporates a company's dream, route, objectives, and strategies. The Hoshin Kanri approach is basically employee-driven and relies on a bottom-up approach (managers) to communicate operational results daily. Many companies have contributed to the development of the Hoshin Kanri approach, for example Panasonic NEC in the 1980<sup>s</sup> and Bridgestone in the 1970<sup>s</sup>.

Furthermore, Japanese corporations incorporate management by mean of objectives with Hoshin Kanri to credibly interconnect objectives to employees and middle-level and operational managers, achieving continuous improvement in organizational performance. In this regard, the Hoshin Kanri system is supported by an enterprise resource planning (ERP) system to support planning and deliver timely feedback to various parts of the organization.

### **Japanese Cost Accounting: Between Western Influence and Indigenous Innovation**

At first glance, Japanese cost accounting systems have been historically influenced by before World War II systems in the Britain and Deutschland, and in the aftermath of World War II systems in America. However, upon inspecting and probing into the practical reality, it is difficult to find features or characteristics that indicate this influence. Writers and researchers attribute this matter to two concepts that distinguish Japanese society: the cultural dimension and the social dimension, which are embodied through collectivism, participation, quality, improvement, and continuous innovation.

Japanese companies adhered to cost accounting standards. Over time, the most important purposes for which these standards were established were price control, long-term planning and budgeting, and cost management, which represents one of the most important operational tools serving engineers and middle and lower management. Japanese cost accounting includes two basic systems: job costing and cost of sales. The latter is more common and is based on batch costing. Cost accounting records for administrative purposes differ from those in European countries. Direct materials are charged directly to the product, while indirect costs are charged according to the cost allocation rates.

The second type of cost accounting records is used for preparing financial statements and is like those in Europe. A high percentage of listed Japanese companies prefer standard costing for two reasons: the first is for the purpose of controlling and reducing costs, and the second is for preparing planning budgets. A small percentage of companies also support this with the ABC costing system and the ABC/ABM cost management system. Japanese cost accounting is associated with important methods and practices, most notably target costing, total quality control, Kaizen costing, and JIT. Japanese management aims to use this combination to reduce product costs, and even if this goal is not achieved, it is useful in cost management.

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