INTERNET INITIATIVE JAPAN INC
Form 6-K
August 10, 2006

FORM 6-K
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Report of Foreign Private Issuer

Pursuant to Rule 13a-16 or 15d-16 under
the Securities Exchange Act of 1934

For August 10, 2006
Commission File Number: 0-30204

Internet Initiative Japan Inc.
(Translation of registrant's name into English)

Jinbocho Mitsui Bldg. 1-105 Kanda Jinbo-cho, Chiyoda-ku, Tokyo 101-0051, Japan

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F:

Form 20-F [X] Form 40-F [ ]

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1): ____

Note: Regulation S-T Rule 101(b)(1) only permits the submission in paper of a Form 6-K if submitted solely to provide an attached annual report to security holders.

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7): ____

Note: Regulation S-T Rule 101(b)(7) only permits the submission in paper of a Form 6-K if submitted to furnish a report or other document that the registrant foreign private issuer must furnish and make public under the laws of the jurisdiction in which the registrant is incorporated, domiciled or legally organized (the registrant's "home country"), or under the rules of the home country exchange on which the registrant's securities are traded, as long as the report or other document is not a press release, is not required to be and has not been distributed to the registrant's security holders, and, if discussing a material event, has already been the subject of a Form 6-K submission or other Commission filing on EDGAR.

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes [ ] No [X]

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-____________

EXHIBIT INDEX

Exhibit	Date	Description of Exhibit
1	2006/08/09	IIJ Announces First Quarter Results for the Year Ending March 31, 2007
2	2006/08/09	Overview of Financial Results for the Three Months Ended June 30, 2006 (Consolidated) - English Translation of the Results in the form defined by the Tokyo Stock Exchange

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Internet Initiative Japan Inc.

Date: August 10, 2006 By: /s/ Koichi Suzuki

Koichi Suzuki
President, Chief Executive Officer and
Representative Director

EXHIBIT 1

IIJ Announces First Quarter Results for the Year Ending March 31, 2007; Year-over-Year Increase in Revenues and Profits, Affected by Favorable Trends

TOKYO--(BUSINESS WIRE)--Aug. 9, 2006--Internet Initiative Japan Inc. (NASDAQ: IIJI, Tokyo Stock Exchange Mothers: 3774) ("IIJ"), one of Japan's leading Internet-access and comprehensive network solutions providers, today announced its financial results for the first quarter of the fiscal year ending March 31, 2007 ("FY2006").(1)

Highlights of First Quarter FY2006 Results

-- Revenue totaled JPY 12,437 million ($108.6 million), an increase of 25.9% from 1Q05.

-- Operating income was JPY 559 million ($4.9 million), an increase of 126.6% from 1Q05.

-- Net income was JPY 734 million ($6.4 million), an increase of 17.8% from 1Q05.

Target for FY2006(2)

-- We maintain our initial target for full FY2006 that we announced on May 10, 2006.

Overview of 1st Quarter of FY2006 Financial Results and Business Outlook(2)

"FY2006 started strongly as revenues from both outsourcing services and systems integration grew substantially," said Koichi Suzuki, President and CEO of IIJ. "Overall revenues increased 25.9% and operating income jumped 126.6% in 1Q06 compared to 1Q05, although our first quarter is historically weakest due to seasonal fluctuations in Japanese corporate spending. The Japanese economy continues to recover and, as a result, we see a greater willingness for Japanese companies to invest in information systems. At the same time, our corporate customers are increasingly recognizing the importance of Internet technology in helping them increase business efficiency and competitiveness. Internet technology became one of the key components of their business operations and consequently they need and demand highly reliable and safe Internet-related services. IIJ has accumulated extensive Internet technological expertise more than a decade, and it is now being validated that IIJ is correctly positioned to meet the growing demand from corporate customers. We are working hard to continue our expansion by developing additional services, particularly in the fields of outsourcing, Internet VPN and Internet security along with favorable business environment."

"In 1Q06, we had an improvement in our financial results", said Akihisa Watai, CFO of IIJ. "At the Ordinary General Shareholders' Meeting held on June 28, 2006, the reductions of the Company's additional paid-in capital and common stock in the non-consolidated financial statements under generally accepted accounting principles in Japan were resolved and became effective on August 4, 2006. The reductions did not result in any changes to the number of shares of common stock outstanding, total shareholders' equity or our earning per share targets for FY2006. The reductions have not affected our consolidated financial statements under accounting principles generally accepted in the United States ("U.S. GAAP") due to the difference in accounting principles between Japan and the United States."

1st Quarter FY2006 Financial Results

Operating Result Summary (JPY in millions)

	1Q06	1Q05	YoY % change
Total Revenues	12,437	9,880	25.9%
Total Costs	10,134	8,118	24.8%
SG&A Expenses and R&D	1,744	1,516	15.1%
Operating Income	559	247	126.6%
Income before Income Tax Expense	999	682	46.5%
Net Income	734	623	17.8%

Revenues

Revenues in 1Q06 totaled JPY 12,437 million, an increase of 25.9% from JPY 9,880 million in 1Q05.

Revenues (JPY in millions)

	1Q06	1Q05	YoY % change
Total Revenues:	12,437	9,880	25.9%
Connectivity and Value-added Services	5,864	5,767	1.7%
Systems Integration	6,032	3,840	57.1%
Equipment Sales	541	273	98.1%

Connectivity and Value-added Services ("VAS") revenues were JPY 5,864 million in 1Q06, an increase of 1.7 % compared to 1Q05. The increase is mainly due to an increase in revenues from various types of value-added services, which was caused by an increase in demand for outsourcing services.

SI revenues increased 57.1% to JPY 6,032 million in 1Q06 compared to 1Q05. The increase was mainly due to an increase in one-time revenues from the design, construction and consultation of networks, as well as a continuous increase in monthly recurring revenues from network operation and maintenance.

Equipment sales revenues were JPY 541 million in 1Q06, an increase of 98.1% compared to 1Q05.

Cost and expense

Cost of revenues was JPY 10,134 million in 1Q06, an increase of 24.8% compared to 1Q05.

Cost of Revenues (JPY in millions)

	1Q06	1Q05	YoY % change
Cost of Revenues:	10,134	8,118	24.8%
Connectivity and Value-added Services	5,070	4,964	2.1%
Systems Integration	4,581	2,910	57.4%
Equipment Sales	483	244	98.2%

Cost of Connectivity and VAS revenues was JPY 5,070 million in 1Q06, an increase of 2.1% compared to 1Q05.

Cost of SI revenues was JPY 4,581 million in 1Q06, an increase of 57.4% compared to 1Q05. The increase was mainly due to an increase in systems integration projects.

Cost of Equipment Sales revenues was JPY 483 million in 1Q06, an increase of 98.2% compared to 1Q05. The increase was mainly due to an increase in equipment sales.

Sales and marketing expenses were JPY 790 million in 1Q06, an increase of 2.9% compared to 1Q05. The increase was mainly due to an increase in expenses along with the business expansion.

General and administrative expenses were JPY 915 million in 1Q06, an increase of 28.1% compared to 1Q05. The increase was mainly due to an increase in personnel expenses principally related to recruitment of new graduates, an increase of recruiting expenses and expenses related to changes in office layouts.

Operating income

Operating income was JPY 559 million in 1Q06, an increase of 126.6% compared to 1Q05. The increase was mainly due to the increase of revenues from higher-margin value-added services and systems integration.

Other income and others

Other income in 1Q06 was JPY 440 million, an increase of 1.1% from JPY 435 million in 1Q05. The increase included a gain from sale of available-for-sale securities of JPY 478 million.

Net income was JPY 734 million in 1Q06, an increase of 17.8% compared to 1Q05. The increase was mainly due to an increase in operating income. The income tax expense in 1Q06 increased to JPY 149 million compared to 1Q05, mainly due to income tax payable related to taxable income of our consolidated subsidiaries. The equity in net loss of equity method investees increased compared to 1Q05 mainly due to an increase of equity method loss from the newly established equity method investee.

1st Quarter FY2006 Business Review

Analysis by Service

Connectivity and Value-added Services

For dedicated access services, customers continued to shift to higher speed and the number of contracts for broadband services increased as customers connected their branch offices and shops over Internet VPN.

The number of contracts for dedicated access services increased by 3,080 to 15,354 compared to 1Q05. The contracted bandwidth increased by 84.5Gbps to 225.4Gbps compared to 1Q05.

Dedicated access service revenues were JPY 2,616 million, a decrease of 4.8% compared to 1Q05. The decrease is mainly related to a decrease by JPY 234 million in interconnection revenues between IIJ's network and Asia Internet Holding Co., Ltd. ("AIH"), our former equity method investee, because AIH was merged into IIJ in October 2005.

Dial-up access service revenues were JPY 607 million in 1Q06, a decrease of 13.1% compared to 1Q05, mainly due to the decrease in revenues from services for individual customers, such as IIJ4U, as well as the discontinuance of services of certain large customer to which we provided our services as OEM.

VAS revenues were JPY 1,741 million in 1Q06, an increase of 25.5% compared to 1Q05. The increase was due to an increase in revenues from various types of services. We recorded an increase in revenues from network-related outsourcing services such as the rental service of SEIL, our in-house developed routers and SEIL Management Framework ("SMF"), the central management system of SEIL, server-related outsourcing services such as outsourcing of e-mail systems and data center related services. The increase in revenues from SEIL rental service and SMF reflects an increase of multi-site connection projects with Internet-VPN.

Other revenues were JPY 900 million in 1Q06, a decrease of 3.6% compared to 1Q05.

As a result, revenues from Internet connectivity and value-added services in 1Q06 were JPY 5,864 million, an increase of 1.7% compared to 1Q05. The gross margin for Internet connectivity and value-added services in 1Q06 was JPY 794 million, a decrease of 1.1% compared to 1Q05. The gross margin ratio of Internet connectivity and value-added services was 13.5% in 1Q06.

Number of Contracts for Connectivity Services

	1Q06	1Q05	YoY Change
Dedicated Access Service Contracts	15,354	12,274	3,080
IP Service (Low Bandwidth: 64kbps-768kbps)(3)	74	65	9
IP Service (Medium Bandwidth: 1Mbps-99Mbps)(3)	673	637	36
IP Service (High Bandwidth: 100Mbps-)	182	131	51
IIJ T1 Standard and IIJ Economy	76	208	(132)
IIJ Data Center Connectivity Service	264	234	30
IIJ FiberAccess/F and IIJ DSL/F (Broadband Services)	14,085	10,999	3,086
Dial-up Access Service Contracts	596,628	677,207	(80,579)
Dial-up Access Services, under IIJ Brand	61,222	66,125	(4,903)
Dial-up Access Services, OEM(4)	535,406	611,082	(75,676)
Total Contracted Bandwidth	225.4Gbps	140.9Gbps	84.5Gbps

Connectivity and VAS Revenue Breakdown and Cost (JPY in millions)

	1Q06	1Q05	YoY %Change
Connectivity Service Revenues	3,223	3,446	(6.5%)
Dedicated Access Service Revenues	2,616	2,747	(4.8%)
IP Service (5)	2,046	2,166	(5.5%)
IIJ T1 Standard and IIJ Economy	62	134	(53.7%)
IIJ FiberAccess/F and IIJ DSL/F (Broadband Services)	508	447	13.7%
Dial-up Access Service Revenues	607	699	(13.1%)
Under IIJ Brand	420	466	(9.8%)
OEM	187	233	(19.8%)
VAS Revenues	1,741	1,388	25.5%

Other Revenues	900	933	(3.6%)
Total Connectivity and VAS Revenues	5,864	5,767	1.7%
Cost of Connectivity and VAS	5,070	4,964	2.1%
Backbone Cost (included in the cost of Connectivity and VAS)	872	864	0.9%
Connectivity and VAS Gross Margin Ratio	13.5%	13.9%	--

Systems Integration

Revenue from systems integration was JPY 6,032 million in 1Q06, an increase of 57.1% compared to 1Q05. The increase was mainly due to consistent increases in monthly recurring revenues from outsourced operations, and an increase in revenues from one-time systems integration. The revenues from outsourced operations increased by 22.9% compared to 1Q05. The revenues from one-time systems integration increased significantly by 132.9% compared to 1Q05, partly due to projects carrying over from the previous quarter. The gross margin for SI in 1Q06 was 24.0%.

Systems Integration Revenue Breakdown and Cost (JPY in millions)

	1Q06	1Q05	YoY % Change
Systems Integration Revenues	6,032	3,840	57.1%
Systems Integration	2,778	1,193	132.9%
Outsourced Operation	3,254	2,647	22.9%
Cost of Systems Integration	4,581	2,910	57.4%
Systems Integration Gross Margin Ratio	24.0%	24.2%	--

Equipment Sales

Revenue from equipment sales was JPY 541 million in 1Q06. The gross margin ratio for equipment sales in 1Q06 was 10.8%.

Equipment Sales Revenue and Cost (JPY in millions)

	1Q06	1Q05	YoY % Change
Equipment Sales Revenues	541	273	98.1%
Cost of Equipment Sales	483	244	98.2%
Equipment Sales Gross Margin Ratio	10.8%	10.9%	--

Other Financial Statistics

Other Financial Statistics (JPY in millions)

	1Q06	1Q05	YoY % change

Adjusted EBITDA(6)	1,666	1,261	32.2%
CAPEX, including capital leases(7)	842	533	57.9%
Depreciation and amortization	1,107	1,014	9.2%

Reconciliation of Non-GAAP Financial Measures

The following table summarizes the reconciliation of adjusted EBITDA to net income according to the consolidated statements of income that are prepared in accordance with U.S. GAAP and presented in Appendix 1:

Adjusted EBITDA (JPY in millions)		
	1Q06	1Q05
Adjusted EBITDA	1,666	1,261
Depreciation and Amortization	(1,107)	(1,014)
Operating Income	559	247
Other Income	440	435
Income Tax Expense	149	38
Minority Interests in Earnings of Subsidiaries	(43)	(24)
Equity in Net Income (Loss) of Equity Method Investees	(73)	3
Net Income	734	623

The following table summarizes the reconciliation of capital expenditures to the purchase of property and equipment according to the consolidated statements of cash flows that are prepared and presented in accordance with U.S. GAAP in Appendix 3:

CAPEX (JPY in millions)		
	1Q06	1Q05
Capital Expenditures	842	533
Acquisition of Assets by Entering into Capital Leases	406	320
Purchase of Property and Equipment	436	213

Target

We maintain our initial target that we announced on May 10, 2006 for the annual fiscal year as follows:

(JPY in millions)

Income from Operations before Income Tax Expense, Minority Interests and Equity in

Revenues	Operating Income	Net Income (Loss) of Equity Method Investees	Net Income
55,000	3,200	6,300	5,000

Presentation

On August 10, 2006, IIJ will post a presentation of its results on its Web site. For details, please access the following URL: http://www.iij.ad.jp/en/IR/

About Internet Initiative Japan Inc.

Founded in 1992, Internet Initiative Japan Inc. (IIJ, NASDAQ: IIJI, Tokyo Stock Exchange Mothers: 3774) is one of Japan's leading Internet-access and comprehensive network solutions providers. The company has built one of the largest Internet backbone networks in Japan, and between Japan and the United States. IIJ and its group of companies provide total network solutions that mainly cater to high-end corporate customers. The company's services include high-quality systems integration and security services, Internet access, hosting/housing, and content design.

Statements made in this press release regarding IIJ's or management's intentions, beliefs, expectations, or predictions for the future are forward-looking statements that are based on IIJ's and managements' current expectations, assumptions, estimates and projections about its business and the industry. These forward-looking statements, such as statements regarding FY2006 revenues and operating and net profitability, are subject to various risks, uncertainties and other factors that could cause IIJ's actual results to differ materially from those contained in any forward-looking statement. These risks, uncertainties and other factors include: IIJ's ability to maintain and increase revenues from higher-margin services such as systems integration and value-added services; the possibility that revenues from connectivity services may decline substantially as a result of competition and other factors; the ability to compete in a rapidly evolving and competitive marketplace; the impact on IIJ's profits of fluctuations in costs such as backbone costs and subcontractor costs; the impact on IIJ's profits of fluctuations in the price of available-for-sale securities; the impact of technological changes in its industry; IIJ's ability to raise additional capital to cover its indebtedness; the possibility that NTT, IIJ's largest shareholder, may decide to exercise substantial influence over IIJ; and other risks referred to from time to time in IIJ's filings on Form 20-F of its annual report and other filings with the United States Securities and Exchange Commission.

(1) Unless otherwise stated, all financial figures discussed in this announcement are prepared in accordance with U.S. GAAP. All financial figures are unaudited and consolidated. For all 1Q06 results, translations of Japanese yen amounts into US dollars are solely for the convenience of readers outside of Japan and have been made at the rate of JPY 114.51 = US$1.00.

(2) This Overview and Business Outlook contains forward-looking statements and projections such as statements regarding FY2006 revenues and operating and net income that are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those expressed or implied by these statements. These risks and uncertainties include, but are

not limited to, the factors noted at the end of this release and to the risk factors and other information included in IIJ's annual report on Form 20-F, filed with the SEC on July 11, 2006, as well as other filings and documents furnished to the Securities and Exchange Commission. IIJ plans to keep this press release publicly available on its Web site (www.iij.ad.jp), but may discontinue this practice at any time. IIJ intends to publish its next Overview and Business Outlook in its 2Q06 earnings release, presently scheduled for release in November 2006.

(3) Including IPv6 Services.

(4) OEM services provided to other service providers.

(5) IP Service revenues includes revenues from Data Center Connectivity Service.

(6) Please refer to the Reconciliation of Non-GAAP Financial Measures below.

(7) Please refer to the Reconciliation of Non-GAAP Financial Measures below.

Appendix 1

Internet Initiative Japan Inc.
Quarterly Consolidated Balance Sheets (Unaudited)
(As of June 30, 2006 and March 31, 2006)

	As of June 30, 2006			As of March 31, 2006	
	Thousands of U.S. Dollars	Thousands of Yen	%	Thousands of Yen	%
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	114,322	13,091,020		13,727,021	
Accounts receivable, net of allowance for doubtful accounts of JPY 29,084 thousand and JPY 23,411 thousand at June 30, 2006 and March 31, 2006, respectively	53,649	6,143,361		11,962,304	
Inventories	6,192	709,047		851,857	
Prepaid expenses	16,033	1,835,908		1,031,325	
Other current assets, net of allowance for doubtful accounts of JPY 30,850 thousand and JPY 33,250 thousand at June 30, 2006 and March 31, 2006, respectively	1,548	177,320		214,121	
Total current assets	191,744	21,956,656	52.3	27,786,628	54.8
INVESTMENTS IN AND ADVANCES TO EQUITY METHOD INVESTEES, net of loan loss valuation allowance of JPY 16,701					

thousand and JPY 16,701 thousand at June 30, 2006 and March 31, 2006, respectively	9,563	1,095,058	2.6	1,162,971	2.3
OTHER INVESTMENTS	50,747	5,811,019	13.8	8,020,705	15.8
PROPERTY AND EQUIPMENT--Net	85,330	9,771,187	23.3	10,299,496	20.3
INTANGIBLE ASSETS--Net	5,547	635,152	1.5	632,594	1.2
GUARANTEE DEPOSITS	13,576	1,554,601	3.7	1,549,653	3.1
OTHER ASSETS, net of allowance for doubtful accounts of JPY 39,657 thousand and JPY 40,980 thousand at June 30, 2006 and March 31, 2006, respectively	10,285	1,177,744	2.8	1,252,942	2.5
TOTAL	366,792	42,001,417	100.0	50,704,989	100.0

	As of June 30, 2006			As of March 31, 2006	
	Thousands of U.S. Dollars	Thousands of Yen	%	Thousands of Yen	%
LIABILITIES AND SHAREHOLDERS' EQUITY					
CURRENT LIABILITIES:					
Short-term borrowings	46,721	5,350,000		4,555,000	
Long-term borrowings--current portion	11,801	1,351,342		1,989,963	
Payable under securities loan agreement	4,332	496,080		999,600	
Capital lease obligations--current portion	30,192	3,457,253		3,003,914	
Accounts payable	33,070	3,786,846		10,107,942	
Accrued expenses	4,644	531,849		540,027	
Other current liabilities	17,919	2,051,859		1,702,208	
Total current liabilities	148,679	17,025,229	40.5	22,898,654	45.2
LONG-TERM BORROWINGS	2,349	269,000	0.6	290,000	0.6
CAPITAL LEASE OBLIGATIONS --Noncurrent	35,132	4,022,923	9.6	4,980,659	9.8
ACCRUED RETIREMENT AND PENSION COSTS	2,138	244,823	0.6	223,332	0.4
OTHER NONCURRENT LIABILITIES	5,958	682,291	1.6	827,086	1.6
Total Liabilities	194,256	22,244,266	52.9	29,219,731	57.6
MINORITY INTEREST	11,194	1,281,860	3.1	1,263,320	2.5
COMMITMENTS AND CONTINGENCIES	--	--	--	--	--
SHAREHOLDERS' EQUITY:					
Common-stock--authorized, 377,600 shares; issued and outstanding, 204,300 shares at June 30, 2006 and authorized, 377,600					

shares; issued and outstanding, 204,300 shares at March 31, 2006	147,008	16,833,847	40.1	16,833,847	33.2
Additional paid-in capital	232,287	26,599,217	63.3	26,599,217	52.5
Accumulated deficit	(252,788)	(28,946,811)	(68.9)	(29,680,482)	(58.5)
Accumulated other comprehensive income	35,571	4,073,276	9.7	6,553,594	12.9
Treasury stock--777 shares held by an equity method investee at June 30, 2006 and March 31, 2006, respectively	(736)	(84,238)	(0.2)	(84,238)	(0.2)
Total shareholders' equity	161,342	18,475,291	44.0	20,221,938	39.9
TOTAL	366,792	42,001,417	100.0	50,704,989	100.0

(Note)

(1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

(2) IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers of shares of common stock authorized, and issued and outstanding, and shares held by an equity method investee in this table are calculated with the assumption that the stock split was made at the beginning of FY2005. IIJ issued 12,500 new shares of common stock for public offering when it listed on the Mothers market of TSE in December 2005.

Appendix 2

Internet Initiative Japan Inc.
Quarterly Consolidated Statements of Income (Unaudited)
(For the three months ended June 30, 2006 and June 30, 2005)

	Three Months Ended June 30, 2006			Three Months Ended June 30, 2005	
	Thousands of U.S. Dollars	Thousands of Yen	% of total revenues	Thousands of Yen	% of total revenues
REVENUES:					
Connectivity and value-added services:					
Dedicated access	22,844	2,615,890		2,746,900	
Dial-up access	5,301	606,995		698,670	
Value-added services	15,207	1,741,318		1,387,893	
Other	7,857	899,726		933,120	
Total	51,209	5,863,929		5,766,583	
Systems integration	52,676	6,031,963		3,840,075	
Equipment sales	4,729	541,545		273,438	

Total revenues	108,614	12,437,437	100.0	9,880,096	100.0
COST AND EXPENSES:					
Cost of connectivity and value-added services	44,273	5,069,730		4,963,835	
Cost of systems integration	40,008	4,581,313		2,910,262	
Cost of equipment sales	4,218	483,015		243,699	
Total cost	88,499	10,134,058	81.5	8,117,796	82.2
Sales and marketing	6,898	789,932	6.3	767,801	7.8
General and administrative	7,988	914,711	7.4	713,917	7.2
Research and development	347	39,684	0.3	33,904	0.3
Total cost and expenses	103,732	11,878,385	95.5	9,633,418	97.5
OPERATING INCOME	4,882	559,052	4.5	246,678	2.5
OTHER INCOME:					
Interest income	27	3,049		2,101	
Interest expense	(935)	(107,002)		(109,377)	
Foreign exchange gains	6	690		8,030	
Gain on other investments--net	4,176	478,186		488,758	
Other--net	569	65,181		45,721	
Other income-- net	3,843	440,104	3.5	435,233	4.4
INCOME FROM OPERATIONS BEFORE INCOME TAX EXPENSE, MINORITY INTERESTS AND EQUITY IN NET INCOME (LOSS) OF EQUITY METHOD INVESTEES	8,725	999,156	8.0	681,911	6.9
INCOME TAX EXPENSE	1,300	148,874	1.2	38,111	0.4
MINORITY INTERESTS IN EARNINGS OF SUBSIDIARIES	(380)	(43,574)	(0.3)	(23,855)	(0.2)
EQUITY IN NET INCOME (LOSS) OF EQUITY METHOD INVESTEES	(638)	(73,037)	(0.6)	2,729	0.0
NET INCOME	6,407	733,671	5.9	622,674	6.3

	Three Months Ended June 30, 2006		Three Months Ended June 30, 2005
	Thousands of U.S. Dollars	Thousands of Yen	Thousands of Yen

BASIC WEIGHTED-AVERAGE NUMBER OF SHARES		203,989	191,547
DILUTED WEIGHTED-AVERAGE NUMBER OF SHARES		204,230	191,547
BASIC WEIGHTED-AVERAGE NUMBER OF ADS EQUIVALENTS		81,595,702	76,618,779
DILUTED WEIGHTED-AVERAGE NUMBER OF ADS EQUIVALENTS		81,692,077	76,618,779
BASIC NET INCOME PER SHARE	31	3,597	3,251
DILUTED NET INCOME PER SHARE	31	3,592	3,251
BASIC NET INCOME PER ADS EQUIVALENT		8.99	8.13
DILUTED NET INCOME PER ADS EQUIVALENT		8.98	8.13

(Note)

(1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

(2) IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers of shares of common stock authorized, and issued and outstanding, and shares held by an equity method investee in this table are calculated with the assumption that the stock split was made at the beginning of FY2005. IIJ issued 12,500 new shares of common stock for public offering when it listed on the Mothers market of TSE in December 2005.

Appendix 3

Internet Initiative Japan Inc.

Quarterly Condensed Consolidated Statements of Cash Flows (Unaudited)

(For the three months ended June 30, 2006 and June 30, 2005)

	Three Months Ended June 30, 2006		Three Months Ended June 30, 2005
	Thousands of U.S. Dollars	Thousands of Yen	Thousands of Yen
OPERATING ACTIVITIES:			
Net income	6,407	733,671	622,674
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	9,669	1,107,155	1,013,745
Provision for (reversal of) doubtful accounts and advances	30	3,413	(5,339)
Gains on other investments--net	(4,176)	(478,186)	(488,758)

Foreign exchange losses (gains)	29	3,284	(6,278)
Equity in net loss (income) of equity method investees	638	73,037	(2,729)
Minority interests in earnings of subsidiaries	381	43,574	23,855
Deferred income tax	184	21,054	18,343
Others	300	34,300	51,618
Changes in operating assets and liabilities:			
Decrease in accounts receivable	50,719	5,807,822	1,621,419
Increase in inventories, prepaid expenses and other current and noncurrent assets	(5,549)	(635,408)	(738,757)
Decrease in accounts payable	(53,019)	(6,071,242)	(1,132,992)
Increase in accrued expenses, other current and noncurrent liabilities	2,290	262,210	50,697
Net cash provided by operating activities	7,900	904,684	1,027,498
INVESTING ACTIVITIES:			
Purchase of property and equipment	(3,810)	(436,264)	(213,485)
Purchase of short-term and other investments	(2,438)	(279,230)	(299,311)
Purchase of subsidiary stock from minority shareholders	(241)	(27,559)	-
Proceeds from sales and redemption of other investments	4,212	482,348	514,460
Payment of guarantee deposits--net	(49)	(5,562)	(39,210)
Other	(6)	(726)	(5,450)
Net cash used in investing activities	(2,332)	(266,993)	(42,996)
FINANCING ACTIVITIES:			
Proceeds from issuance of short-term borrowings with initial maturities over three months	37,988	4,350,000	-
Repayments of long-term borrowings	(5,760)	(659,621)	(208,654)
Proceeds from securities loan agreement	4,332	496,080	-
Repayments of securities loan agreement	(8,729)	(999,600)	(199,120)
Principal payments under capital leases	(7,859)	(899,879)	(766,807)
Net decrease in short-term borrowings with initial maturities less than three months	(31,045)	(3,555,000)	(1,246)
Net cash used in financing activities	(11,073)	(1,268,020)	(1,175,827)

EFFECT OF EXCHANGE RATE CHANGES ON CASH	(50)	(5,672)	11,236
NET INCREASE (DECREASE) IN CASH	(5,554)	(636,001)	(180,089)
CASH, BEGINNING OF EACH PERIOD	119,876	13,727,021	5,286,477
CASH, END OF EACH PERIOD	114,322	13,091,020	5,106,388
ADDITIONAL CASH FLOW INFORMATION:			
Interest paid	795	91,001	95,390
Income taxes paid	1,970	225,563	128,764
NONCASH INVESTING AND FINANCING ACTIVITIES:			
Acquisition of assets by entering into capital leases	3,542	405,621	319,828

(Note)
(1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

CONTACT: IIJ Corporate Communications
Taisuke ONO, +81-3-5259-6500
ir@iij.ad.jp
http://www.iij.ad.jp/

EXHIBIT 2

(English Translation)

Overview of Financial Results for the Three Months Ended June 30, 2006
(Consolidated)
(Prepared in accordance with Generally Accepted Accounting Principles in the United States of America ("U.S. GAAP"))

August 9, 2006

Company name Internet Initiative Japan Inc.

("IIJ", stock code number: 3774, the Mothers Market of the Tokyo Stock Exchange ("TSE")) (URL http://www.iij.ad.jp/)

Contacts Company representative: Koichi Suzuki, President and Representative Director
Person-in-charge: Akihisa Watai, Director and CFO
TEL: (03)-5259-6500

1. Items regarding Preparation of Quarterly Consolidated Financial Results

(1) Standard used for preparation of the quarterly consolidated financial statements: Standard for Preparation of Interim Consolidated Financial Statements

(2) Changes in accounting method from the most recent fiscal year: No

(3) Changes in scope of consolidation and equity method: No

2. Overview of Financial Results for the Three Months Ended June 30, 2006
(April 1, 2006 through June 30, 2006)

(1) Consolidated Results of Operations

(Amounts less than one

	Total Revenues		Operating Income		I
	Millions of Yen	%	Millions of Yen	%	Mi
Three months ended June 30, 2006	12,437	25.9	559	126.6	99
Three months ended June 30, 2005	9,880	--	247	--	68
(For reference) Year ended March 31, 2006	49,813		2,411		5,37

	Basic Net Income per Share	Diluted Net Income per Share
	Yen	Yen
Three months ended June 30, 2006	3,597	3,592
Three months ended June 30, 2005	3,251	3,251
(For reference) Year ended March 31, 2006	24,301	24,258

(Notes)

1) Equity in net income (loss) of equity method investees was equity in net loss of JPY 73 million, equity in net income of JPY 3 million and equity in net loss of JPY 14 million for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, respectively.

2) The weighted-average number of shares of common stock outstanding (consolidated) was 203,989, 191,547 and 195,613 for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, respectively. IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers are calculated with the assumption that the stock spilt was made at the beginning of the year ended March 31, 2006. The numbers are calculated with the number of IIJ shares of common stock outstanding deducted by the number of IIJ's shares owned by IIJ's equity method investee multiplied by IIJ's ownership in the equity method investee.

3) The percentage figures for the total revenues, operating income and others for the three months ended June 30, 2006 show an increase or decrease compared to the same quarter in the last fiscal year. As IIJ began to prepare the financial statements for three months ended June 30 as required by TSE for the three months ended June 30, 2005, IIJ does not show the percentage figures for the total revenues, operating income and others for the three months ended June 30, 2005.

4) The potential shares did not have a dilutive effect for the three months ended June 30, 2006.

5) In this document, income before income tax expense represents income from operations before income tax expense, minority interests and equity in net income (loss) of equity method investees in IIJ's consolidated financial statements.

(Consolidated Results of Operations for the three months ended June 30, 2006 (from April 1, 2006 to June 30, 2006))

a. Overview of Financial Results

IIJ had a favorable start to the year ending March 31, 2007. Despite the fact that our first quarter is historically weakest due to seasonal fluctuations in Japanese corporate spending, both revenues and profits increased significantly for the three months ended June 30, 2006 compared to the three months ended June 30, 2005 due to the significant increase in systems integration and outsourcing services.

In general, with the recovering trend of the Japanese economy, corporate investments on network have continued to rise. Under this business environment, revenues from systems integration, such as network design, construction, operation and maintenance, and value-added services ("VAS") such as security-related services, and outsourcing of email-related system and data center services, are steadily increasing.

As a result, for the IIJ Group's consolidated results of operation for the three months ended June 30, 2006, total revenues amounted to JPY 12,437 million, an increase of 25.9% compared to the three months ended June 30, 2005. Operating income amounted to JPY 559 million, an increase of 126.6% compared to the three months ended June 30, 2005. Income before income tax expense amounted to JPY 999 million, an increase of 46.5% compared to the three months ended June 30, 2005 and net income amounted to JPY 734 million, an increase of 17.8% compared to the three months ended June 30, 2005.

b. Analysis of the Results of Operations

1) Revenues

Revenues for the three months ended June 30, 2006 totaled JPY 12,437 million, an increase of 25.9% compared to the three months ended June 30, 2005.

	Three Months ended June 30, 2006	Three Months en 30, 2005
	Millions of Yen	Millions of

Connectivity and VAS	5,864
Systems Integration	6,032
Equipment Sales	541
Total Revenues	12,437

Connectivity and VAS revenues were JPY 5,864 million for the three months ended June 30, 2006, an increase of 1.7% compared to the three months ended June 30, 2005. Although revenues from Internet connectivity services decreased, revenues from various types of VAS increased due to an increase in demand for outsourcing services.

SI revenues increased by 57.1% from the three months ended June 30, 2005 to JPY 6,032 million for the three months ended June 30, 2006. The increase was mainly due to an increase in revenues from network system outsourcing and maintenance which generated recurring revenues and increase in one-time revenues from network design, construction and consultation.

Equipment sales revenues were JPY 541 million for the three months ended June 30, 2006, an increase of 98.1% compared to the three months ended June 30, 2005.

2) Cost of Revenues

The cost of revenues was JPY 10,134 million for the three months ended June 30, 2006, an increase of 24.8% compared to the three months ended June 30, 2005.

	Three Months ended June 30, 2006	Three Months en 30, 2005
	Millions of Yen	Millions of
Connectivity and VAS	5,070	
Systems Integration	4,581	
Equipment Sales	483	
Total Cost of Revenues	10,134	

The cost of connectivity and VAS revenues was JPY 5,070 million for the three months ended June 30, 2006, an increase of 2.1% compared to the three months ended June 30, 2005.

The cost of SI revenues increased by 57.4% to JPY 4,581 million for the three months ended June 30, 2006 from the three months ended June 30, 2005, mainly due to an increase in revenues from systems integration.

The cost of equipment sales revenues was JPY 483 million for the three months ended June 30, 2006, an increase of 98.2% compared to the three months ended June 30, 2005.

3) Sales and Marketing Expenses

Sales and marketing expenses were JPY 790 million for the three months ended June 30, 2006, an increase of 2.9% compared to the three months ended June 30, 2005. The increase was mainly due to an increase in expenses from the business expansion.

4) General and Administrative Expenses

General and administrative expenses were JPY 915 million for the three months ended June 30, 2006, an increase of 28.1% compared to the three months ended June 30, 2005. The increase was mainly due to an increase in personnel expenses principally related to the recruitment of new graduates, an increase of recruiting expenses and expenses related to changes in office layouts.

5) Operating Income

Operating income was JPY 559 million for the three months ended June 30, 2006, an increase of 126.6% compared to the three months ended June 30, 2005. The increase was mainly due to the increase in gross margin, which was caused by the increase in revenues from value-added services and systems integration.

6) Other Income and Others

Other income for three months ended June 30, 2006 was JPY 440 million, an increase of 1.1% compared to the three months ended June 30, 2005. The increase included a gain from sale of available-for-sale securities of JPY 478 million.

7) Net Income

Net income for the three months ended June 30, 2006 was JPY 734 million, an increase of 17.8% compared to the three months ended June 30, 2005. The income tax expense for the three months ended June 30, 2006 increased to JPY 149 million compared to the three months ended June 30, 2005, mainly due to an increase of income tax payable related to taxable income of our consolidated subsidiaries. The equity in net loss of equity method investees totaled JPY 73 million for the three months ended June 30, 2006 due to an increase of equity method loss from the newly established equity method investee.

c. Analysis by Service

1) Internet Connectivity and Value-added Services ("VAS")

For dedicated access services, a number of corporate customers have increased their bandwidth and the number of contracts of broadband services increased with an increase of multi-site connection projects. However, the revenue from dedicated access services decreased by 4.8% to JPY 2,616 million mainly related to a decrease by JPY 234 million in interconnection revenues between IIJ's network and Asia Internet Holding Co., Ltd. ("AIH"), our former equity method investee, because AIH merged into IIJ.

Dial-up access service revenues were JPY 607 million for the three months ended June 30, 2006, a decrease of 13.1% compared to the three months ended June 30, 2005. The decrease was mainly due to the decrease in revenues from services for individual customers, such as IIJ4U, as well as the discontinuance of services of a large customer to which we provided our services as OEM.

VAS revenues were JPY 1,741 million for the three months ended June 30, 2006, an increase of 25.5% compared to the three months ended June 30, 2005 due to an increase in revenues from various types of services. We recorded an increase in revenues from network-related outsourcing services such as the rental service of SEIL, our in-house developed routers and SEIL Management Framework ("SMF"), the central management system of SEIL, server-related outsourcing services such as outsourcing of e-mail systems and data center related services. The increase in revenues from the SEIL rental service and SMF reflects an increase of multi-site connection projects.

Other revenues were JPY 900 million for the three months ended June 30, 2006, a decrease of 3.6% compared to the three months ended June 30, 2005.

As a result, revenues from Internet connectivity and VAS for the three months ended June 30, 2006 were JPY 5,864 million, an increase of 1.7% compared to the three months ended June 30, 2005. The gross margin of Internet connectivity and VAS was JPY 794 million, a decrease of 1.1% compared to the three months ended June 30, 2005 and the gross margin ratio was 13.5%.

[Connectivity and VAS Revenue Breakdown and Cost]

	Three Months Ended June 30, 2006	Three Months June 30, 2
	Millions of Yen	Millions of
Connectivity and VAS Revenues	5,864	
Dedicated Access Service Revenues	2,616	
Dial-up Access Service Revenues	607	
VAS Revenues	1,741	
Other Revenues	900	
Cost of Connectivity and VAS	5,070	
Backbone Cost (included in the cost of Connectivity and VAS)	872	
Connectivity and VAS Gross Margin Ratio	13.5%	

2) Systems integration ("SI")

Systems integration revenues for the three months ended June 30, 2006 were JPY 6,032 million, an increase of 57.1% compared to the three months ended June 30, 2005. The increase was mainly due to an increase of 22.9% in revenues from network system outsourcing and maintenance, which will generate recurring revenues, and a significant increase of 132.9% in revenues from one-time systems integration projects, partly due to projects carrying over from the previous quarter. The gross margin ratio for SI was 24.0%.

[Systems Integration Revenue Breakdown and Cost]

	Three Months Ended June 30, 2006	Three Months June 30, 2
	Millions of Yen	Millions of
SI Revenues	6,032	
Systems Integration	2,778	
Outsourced Operation	3,254	
Cost of SI	4,581	
SI Gross Margin Ratio	24.0%	

3) Equipment sales

Equipment sales revenues for the three months ended June 30, 2006 were JPY 541 million. The gross margin of equipment sales was JPY 59 million and the gross margin ratio was 10.8%.

[Equipment Sales Revenue and Cost]

	Three Months Ended June 30, 2006	Three Months June 30, 2
	Millions of Yen	Millions of
Equipment Sales Revenues	541	
Cost of Equipment Sales	483	
Equipment Sales Gross Margin Ratio	10.8%	

(2) Changes in Consolidated Financial Position (Amounts less than one

	Total Assets	Shareholders' Equity	Equity-to-Assets Ratio
	Millions of Yen	Millions of Yen	%
As of June 30, 2006	42,001	18,475	44
As of June 30, 2005	33,744	10,187	30

(For reference) As of March 31, 2006	50,705	20,222	39

(Note)

The number of shares of common stock outstanding (consolidated) was 203,989, 191,489 and 203,989 as of June 30, 2006, June 30, 2005 and March 31, 2006, respectively. IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers are calculated with the assumption that the stock spilt had been made at the beginning of the year ended March 31, 2006. The numbers are calculated with the number of IIJ shares of common stock outstanding reduced by the number of IIJ's shares owned by IIJ's equity method investee multiplied by IIJ's percentage ownership in the equity method investee.

(3) Consolidated Cash Flows

(Amounts less than o

	Net cash provided by operating activities	Net cash provided by (used in) investing activities	Net cash provided by (used in) financing activiti
	Millions of Yen	Millions of Yen	Millions of Yen
Three months ended June 30, 2006	905	(267)	(1,268)
Three months ended June 30, 2005	1,027	(43)	(1,176)
(For reference) Year ended March 31, 2006	6,559	1,805	39

(Note)

As for the cash flows, the effect of exchange rate changes on cash was JPY (6) million, JPY 11 million and JPY 38 million for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, respectively.

(Qualitative Information Regarding Changes in Consolidated Financial Position)

The balance of cash as of June 30, 2006 was JPY 13,091 million (the balance of cash as of June 30, 2005 was JPY 5,106 million).

(Net cash used in operating activities)

Net cash provided by operating activities was JPY 905 million for the three months ended June 30, 2006 (the net cash provided by operating activities was JPY 1,027 million for the three months ended June 30, 2005). An increase or decrease of accounts receivable and accounts payable offset an increase in operating income due to an increase in revenues from value-added services and systems integration.

(Net cash used in investing activities)

Net cash used in investing activities was JPY 267 million for the three months ended June 30, 2006 (the net cash used in financing activities was JPY 43 million for the three months ended June 30, 2005). Purchases of short-term and other investments of JPY 279 million and property and equipment of JPY 436 million offset proceeds of JPY 482 million from sales and redemption of short-term and other investments.

(Net cash used in financing activities)

Net cash used in financing activities was JPY 1,268 million for the three months ended June 30, 2006 (the net cash used in financing activities was JPY 1,176 million for the three months ended June 30, 2005). Repayments of securities loan agreement of JPY 1,000 million, principal payments under capital leases of JPY 900 million, and repayments of long-term borrowings of JPY 660 million offset proceeds of JPY 795 million from issuance of short-term borrowings and proceeds of JPY 496 million from securities loan agreement.

3. Target of Consolidated Financial Results for the Year Ending March 31, 2007 (April 1, 2006 through March 31, 2007)

(Amounts less than one milli

	Total Revenues	Operating Income	Income before Incom Tax Expense
	Millions of Yen	Millions of Yen	Millions of Yen
Interim period ending September 30, 2006	25,000	1,000	2,600
Year ending March 31, 2007	55,000	3,200	6,300

(Reference) Net income per share for the year ending March 31, 2007, based on the target above: JPY 24,511

(Notes)

1) Statements made in this press release regarding IIJ's or management's intentions, beliefs, expectations, or predictions for the future are forward-looking statements that are based on IIJ's and managements' current expectations, assumptions, estimates and projections about its business and the industry. These forward-looking statements, such as statements regarding revenues and operating and net profitability of the year ending March 31, 2007, are subject to various risks, uncertainties and other factors that could cause IIJ's actual results to differ materially from those contained in any forward-looking statement. These risks, uncertainties and other factors include: IIJ's ability to maintain and increase revenues from higher-margin services such as systems integration and value-added services; the possibility that revenues from connectivity services may decline substantially as a result of competition and other factors; the ability to compete in a rapidly evolving and competitive marketplace; the impact on IIJ's profits of fluctuations in costs such as

backbone costs and subcontractor costs; the impact on IIJ's profits of fluctuations in the price of available-for-sale securities; the impact of technological changes in its industry; IIJ's ability to raise additional capital to cover its indebtedness; the possibility that NTT, IIJ's largest shareholder, may decide to exercise substantial influence over IIJ; and other risks referred to from time to time in IIJ's filings on Form 20-F of its annual report and other filings with the United States Securities and Exchange Commission.

(Qualitative Information regarding Targets for Consolidated Financial Results)

IIJ maintains its target for consolidated and non-consolidated financial results for the year ending March 31, 2007 that we announced on May 10, 2006.

4. Reference Information

At the Ordinary General Shareholders' Meeting held on June 28, 2006, the reductions of additional paid-in capital of JPY 21,980,395 thousand and common stock of JPY 2,539,222 thousand were resolved to eliminate the accumulated deficit in the non-consolidated financial statements under generally accepted accounting principles in Japan. The resolution became effective on August 4, 2006. As a result, the common stock was reduced to JPY 14,294,625,054, the additional paid-in capital was reduced to JPY 0 and the accumulated deficit was eliminated in the non-consolidated financial statements. However, due to the difference in accounting principles between Japan and the United States, the accumulated deficit has not been eliminated and the common stock and additional paid-in capital have not been reduced in our consolidated financial statements under U.S. GAAP.

5. Quarterly Consolidated Financial Statements
(From April 1, 2006 through June 30, 2006)

(1) Quarterly Consolidated Balance Sheets

		As of June 30, 2006			As of June 30, 2005
	Notes	Thousands of U.S. Dollars	Thousands of Yen	%	Thousands of Yen
ASSETS					
CURRENT ASSETS:					
Cash		114,322	13,091,020		5,106,388
Short-term investments		--	--		304,628
Accounts receivable, net of allowance for doubtful accounts of JPY 29,054 thousand, JPY 35,482 thousand and JPY 23,411 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively	3	53,649	6,143,361		5,792,808
Inventories		6,192	709,047		265,286

Prepaid expenses		16,033	1,835,908		1,263,409	
Other current assets, net of allowance for doubtful accounts of JPY 30,850 thousand, JPY 19,000 thousand and JPY 33,250 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively		1,548	177,320		80,797	
Total current assets		191,744	21,956,656	52.3	12,813,316	
INVESTMENTS IN AND ADVANCES TO EQUITY METHOD INVESTEES, net of loan loss valuation allowance of JPY 16,701 thousand, JPY 31,378 thousand and JPY 16,701 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively	3	,563	1,095,058	2.6	677,035	
OTHER INVESTMENTS	2,5	50,747	5,811,019	13.8	7,882,229	
PROPERTY AND EQUIPMENT--Net	4	85,330	9,771,187	23.3	9,155,981	
INTANGIBLE ASSETS--Net		5,547	635,152	1.5	560,288	
GUARANTEE DEPOSITS	4,5	13,576	1,554,601	3.7	2,091,237	
OTHER ASSETS, net of allowance for doubtful accounts of JPY 39,657 thousand, JPY 375,989 thousand and JPY 40,980 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively		10,285	1,177,744	2.8	564,153	
TOTAL		366,792	42,001,417	100.0	33,744,239	1

		As of June 30, 2006			As of June 30, 20
	Notes	Thousands of U.S. Dollars	Thousands of Yen	%	Thousands of Yen
LIABILITIES AND SHAREHOLDERS' EQUITY					
CURRENT LIABILITIES:					
Short-term borrowings	5	46,721	5,350,000		4,723,387
Long-term borrowings--current portion	5	11,801	1,351,342		3,187,023
Payable under securities loan agreement	5	4,332	496,080		1,530,400
Capital lease obligations--current portion	4	30,192	3,457,253		2,718,759
Accounts payable	3	33,070	3,786,846		3,665,233
Accrued expenses		4,644	531,849		523,478
Other current liabilities		17,919	2,051,859		918,829
Total current liabilities		148,679	17,025,229	40.5	17,267,109
LONG-TERM BORROWINGS	5	2,349	269,000	0.6	870,342
CAPITAL LEASE OBLIGATIONS --Noncurrent	4	35,132	4,022,923	9.6	3,950,359
ACCRUED RETIREMENT AND PENSION COSTS		2,138	244,823	0.6	169,460

	Notes					
OTHER NONCURRENT LIABILITIES		5,958	682,291	1.6	246,818	
Total Liabilities		194,256	22,244,266	52.9	22,504,088	
MINORITY INTEREST		11,194	1,281,860	3.1	1,053,212	
COMMITMENTS AND CONTINGENCIES	6	--	--	--	--	
SHAREHOLDERS' EQUITY:						
Common-stock--authorized, 377,600 shares; issued and outstanding, 204,300 shares at June 30, 2006, authorized, 377,600 shares; issued and outstanding, 191,800 shares at June 30, 2005 and authorized, 377,600 shares; issued and outstanding, 204, 300 shares at March 31, 2006		147,008	16,833,847	40.1	13,765,372	
Additional paid-in capital		232,287	26,599,217	63.3	23,637,628	
Accumulated deficit		(252,788)	(28,946,811)	(68.9)	(33,811,378)	(1
Accumulated other comprehensive income		35,571	4,073,276	9.7	6,679,555	
Treasury stock--777 shares held by an equity method investee at June 30, 2006, June 30, 2005 and March 31, 2006, respectively		(736)	(84,238)	(0.2)	(84,238)	
Total shareholders' equity		161,342	18,475,291	44.0	10,186,939	
TOTAL		366,792	42,001,417	100.0	33,744,239	1

(Note)

1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

2) IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers of shares of common stock authorized, and issued and outstanding, and shares held by an equity method investee in this table are calculated with the assumption that the stock split was made at the beginning of the year ended March 31, 2006. IIJ issued 12,500 new shares of common stock for public offering when it listed on the Mothers market of TSE in December 2005.

(2) Quarterly Consolidated Statements of Income

		Three Months Ended June 30, 2006			Three Months Ende June 30, 2005	
	Notes	Thousands of U.S. Dollars	Thousands of Yen	% of total revenues	Thousands of Yen	% o tot reve
REVENUES:	3					

Connectivity and value-added services:						
Dedicated access		22,844	2,615,890		2,746,900	
Dial-up access		5,301	606,995		698,670	
Value-added services		15,207	1,741,318		1,387,893	
Other		7,857	899,726		933,120	
Total		51,209	5,863,929		5,766,583	
Systems integration		52,676	6,031,963		3,840,075	
Equipment sales		4,729	541,545		273,438	
Total revenues		108,614	12,437,437	100.0	9,880,096	100
COST AND EXPENSES:	3,4					
Cost of connectivity and value-added services		44,273	5,069,730		4,963,835	
Cost of systems integration		40,008	4,581,313		2,910,262	
Cost of equipment sales		4,218	483,015		243,699	
Total cost		88,499	10,134,058	81.5	8,117,796	82
Sales and marketing		6,898	789,932	6.3	767,801	7
General and administrative		7,988	914,711	7.4	713,917	7
Research and development		347	39,684	0.3	33,904	0
Total cost and expenses		103,732	11,878,385	95.5	9,633,418	97
OPERATING INCOME		4,882	559,052	4.5	246,678	2
OTHER INCOME:						
Interest income		27	3,049		2,101	
Interest expense		(935)	(107,002)		(109,377)	
Foreign exchange gains		6	690		8,030	
Gain on other investments--net	2	4,176	478,186		488,758	
Other--net		569	65,181		45,721	
Other income-- net		3,843	440,104	3.5	435,233	4
INCOME FROM OPERATIONS BEFORE INCOME TAX EXPENSE, MINORITY INTERESTS AND EQUITY IN NET INCOME (LOSS) OF EQUITY METHOD INVESTEES		8,725	999,156	8.0	681,911	6
INCOME TAX EXPENSE		1,300	148,874	1.2	38,111	0
MINORITY INTERESTS IN EARNINGS OF SUBSIDIARIES		(380)	(43,574)	(0.3)	(23,855)	(0
EQUITY IN NET INCOME (LOSS) OF EQUITY METHOD INVESTEES	3	(638)	(73,037)	(0.6)	2,729	0
NET INCOME		6,407	733,671	5.9	622,674	6

		Three Months Ended June 30, 2006		Three Months Ende June 30, 2005
	Notes	Thousands of U.S. Dollars	Thousands of Yen	Thousands of Yen
NET INCOME PER SHARE	8			

BASIC WEIGHTED-AVERAGE NUMBER OF SHARES		203,989	191,547
DILUTED WEIGHTED-AVERAGE NUMBER OF SHARES		204,230	191,547
BASIC WEIGHTED-AVERAGE NUMBER OF ADS EQUIVALENTS		81,595,702	76,618,779
DILUTED WEIGHTED-AVERAGE NUMBER OF ADS EQUIVALENTS		81,692,077	76,618,779
BASIC NET INCOME PER SHARE	31	3,597	3,251
DILUTED NET INCOME PER SHARE	31	3,592	3,251
BASIC NET INCOME PER ADS EQUIVALENT		8.99	8.13
DILUTED NET INCOME PER ADS EQUIVALENT		8.98	8.13

(Note)

1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

2) IIJ conducted a 1 for 5 stock split effective on October 11, 2005. The numbers of shares of common stock authorized, and issued and outstanding, and shares held by an equity method investee in this table are calculated with the assumption that the stock split was made at the beginning of the year ended March 31, 2006. IIJ issued 12,500 new shares of common stock for public offering when it listed on the Mothers market of TSE in December 2005.

(3) Consolidated Statements of Shareholders' Equity

Consolidated statements of shareholders' equity for three months ended June 30, 2006 (Unit: Thous

	Shares of Common Stock Outstanding (Including Treasury Stock) (Shares)	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulat Other Comprehen Income
BALANCE, APRIL 1, 2006	204,300	16,833,847	26,599,217	(29,680,482)	6,553,
Net income				733,671	
Other comprehensive loss, net of tax					(2,480,
Total comprehensive income					
BALANCE, JUNE 30, 2006	204,300	16,833,847	26,599,217	(28,946,811)	4,073,

Consolidated statements of shareholders' equity for three months ended June 30, 2006 (Unit: Thous

	Shares of Common Stock Outstanding (Including Treasury Stock) (Shares)	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulat Other Comprehen Income
BALANCE, APRIL 1, 2006	204,300	147,008	232,287	(259,196)	57,
Net income				6,407	
Other comprehensive loss, net of tax					(21,
Total comprehensive income					
BALANCE, JUNE 30, 2006	204,300	147,008	232,287	(252,788)	35,

(Note)

1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

Consolidated statements of shareholders' equity for three months ended June 30, 2005 (Unit: Thous

	Shares of Common Stock Outstanding (Including Treasury Stock) (Shares)	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulat Other Comprehen Income
BALANCE, APRIL 1, 2005	191,800	13,765,372	23,637,628	(34,434,052)	8,690,
Net income				622,674	
Other comprehensive income, net of tax					(2,010,
Total comprehensive income					
Purchase of common stock by an equity method investee					
BALANCE, JUNE 30, 2005	191,800	13,765,372	23,637,628	(33,811,378)	6,679,

Consolidated statements of shareholders' equity for the fiscal year ended March 31, 2006 (Unit: T

	Shares of Common Stock Outstanding (Including Treasury Stock) (Shares)	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulat Other Comprehen Income
BALANCE, APRIL 1, 2005	191,800	13,765,372	23,637,628	(34,434,052)	8,690,
Net income				4,753,570	
Other comprehensive loss, net of tax					(2,136,
Total comprehensive income					
Issuance of common stock, net of issuance cost	12,500	3,068,475	2,961,589		
Purchase of common stock by an equity method investee					
BALANCE, MARCH 31, 2006	204,300	16,833,847	26,599,217	(29,680,482)	6,553,

(4) Quarterly Condensed Consolidated Statements of Cash Flows

	Three Months Ended June 30, 2006	
	Thousands of U.S. Dollars	Thousands of Yen
OPERATING ACTIVITIES:		
Net income	6,407	733,671
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,669	1,107,155
Provision for (reversal of) doubtful accounts and advances	30	3,413
Gains on other investments--net	(4,176)	(478,186
Foreign exchange losses (gains)	29	3,284
Equity in net loss (income) of equity method investees	638	73,037
Minority interests in earnings of subsidiaries	381	43,574

Deferred income tax expense (benefit)	184	21,054
Others	298	34,300
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable	50,719	5,807,822
Increase in inventories, prepaid expenses and other current and noncurrent assets	(5,549)	(635,408
Increase (decrease) in accounts payable	(53,019)	(6,071,242
Increase in accrued expenses, other current and noncurrent liabilities	2,289	262,210
Net cash provided by operating activities	7,900	904,684
INVESTING ACTIVITIES:		
Purchase of property and equipment	(3,810)	(436,264
Purchase of short-term and other investments	(2,438)	(279,230
Investment in an equity method investee	--	--
Purchase of subsidiary stock from minority shareholders	(241)	(27,559
Proceeds from sales and redemption of other investments	4,212	482,348
Acquisition of a newly controlled company, net of cash acquired	--	--
Refund (payment) of guarantee deposits--net	(49)	(5,562
Other	(6)	(726
Net cash provided by (used in) investing activities	(2,332)	(266,993
FINANCING ACTIVITIES:		
Proceeds from issuance of short-term borrowings with initial maturities over three months and long-term borrowings	37,988	4,350,000
Repayments of long-term borrowings	(5,760)	(659,621
Proceeds from securities loan agreement	4,332	496,080
Repayments of securities loan agreement	(8,729)	(999,600
Principal payments under capital leases	(7,859)	(899,879
Net decrease in short-term borrowings with initial maturities less than three months	(31,045)	(3,555,000
Proceeds from issuance of common stock, net of issuance cost	--	--
Net cash provided by (used in) financing activities	(11,073)	(1,268,020
EFFECT OF EXCHANGE RATE CHANGES ON CASH	(49)	(5,672
NET INCREASE (DECREASE) IN CASH	(5,554)	(636,001
CASH, BEGINNING OF EACH PERIOD	119,876	13,727,021
CASH, END OF EACH PERIOD	114,322	13,091,020
ADDITIONAL CASH FLOW INFORMATION:		

Interest paid	795	91,001
Income taxes paid	1,970	225,563
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Acquisition of assets by entering into capital leases	3,542	405,621
Exchange of common stock investment due to merger:		
Market value of common shares acquired	--	
Cost of investment	--	
Acquisition of business and a company:		
Assets acquired	--	
Cash paid	--	
Liabilities assumed	--	

(Note)

1) The U.S. dollar amounts represent translations of yen amounts at the rate of JPY 114.51 which was the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York prevailing as of June 30, 2006.

Standard for Preparation of Consolidated Financial Statements for the three months ended June 30, 2006

1. The Terminology, Form, and Preparation Methods for the Consolidated Financial Statements for the three months ended June 30, 2006

   The consolidated financial statements for the three months ended June 30, 2006 have been prepared under the accounting principles, procedures and ways of presentations requested for the issuance of American Depository Receipts ("ADRs") and others (generally accepted accounting principles in the United States of America ("U.S. GAAP"), including Accounting Research Bulletins ("ARB"), Accounting Principles Board ("APB") Opinions, Statement of Financial Accounting Standards ("SFAS") and related interpretation guidelines) in accordance with the provisions of article 81 "provisions for the terminology, form, and preparation methods for interim consolidated financial statements" (Ministry of Finance, ordinance No. 24, 1999).

   IIJ registered issuance of ADRs under the United States Securities and Exchange Commission ("the United States SEC") and list IIJ's ADRs on NASDAQ market in August 1999. Accordingly, IIJ regularly files its annual report on Form 20-F in English with the United States SEC, including consolidated financial statements in English prepared under U.S. GAAP, in accordance with Rule 13 of the U.S. Securities Exchange Act of 1934, as amended.

2. Main Differences in Preparation of Financial Statements in Accordance with Japan's Provisions and Principles for Interim Consolidated Financial Statements

   The main differences between the consolidated financial statements for the three months ended June 30, 2006 prepared under U.S. GAAP and the consolidated financial statements for the three months ended June 30, 2006 prepared in accordance with the Japan's provisions and principles for interim consolidated financial statements and the impact of the financially material items on income from operations before income tax expense, minority interests and equity in net income (loss) of equity method investees ("income before income tax expense") (the impact by an amendment to the financial statements prepared under U.S. GAAP) are as follows:

(1) Differences in the Composition of the Quarterly Consolidated Financial Statements

The quarterly consolidated financial statements under U.S. GAAP are composed of quarterly consolidated balance sheets, quarterly consolidated statements of income, quarterly consolidated statements of shareholders' equity and quarterly consolidated statements of cash flows and notes to the financial statements.

(2) Differences in the Presentation of the Quarterly Consolidated Financial Statements

Equity in net income (loss) of equity method investees is shown as an independent item in the quarterly consolidated financial statements after income before income tax expense.

(3) Differences in Accounting Standards

a. Income tax expense

Income tax expenses are accounted for in accordance with SFAS No. 109. Changes in the deferred income tax asset valuation allowance that relate to the tax effect of unrealized gains and losses on available-for-sale securities have been recorded as a separate component of other comprehensive income.

b. Lease transactions

The Company accounts for significant lease transaction agreements that fulfill the requirements for capitalized leases as stipulated by SFAS No. 13, in accordance with SFAS. As a result, finance lease transactions, other than those that recognize transfer of ownership to the lessee, are treated as purchased. In the three months ended June 30, 2006, this accounting treatment of lease transactions resulted in a JPY 6,452 thousand reduction in income before income tax expense.

c. Cost of issuance of common stock

The cost of issuing of common stock is accounted for as an expense related to capital transactions and is deducted from additional paid-in capital. In the three months ended June 30, 2006, this accounting treatment resulted in a JPY 8,906 thousand increase in income before income tax expense.

d. Retirement benefit accounting

Unfunded retirement benefits and noncontributory defined benefit pension plans are accounted for in accordance with SFAS No. 87. In the three months ended June 30, 2006, this accounting treatment resulted in a JPY 130 thousand decrease in income before income tax expense.

e. Comprehensive income

Comprehensive income is accounted for in accordance with SFAS No. 130, "reporting comprehensive income." SFAS requires additional disclosure of information in consolidated financial statements. In the three months ended June 30, 2006, this accounting treatment did not result in any change in income before income tax expense.

(4) Difference in the Way Diluted Net Income per Common Share is accounted for in the Quarterly Consolidated Financial Statements

Diluted net income per common share is accounted for in accordance with SFAS No. 128. In accordance with SFAS, the test of potential common shares that have dilutive effects should be conducted over three months. In the accounting principles in Japan regarding calculation of net income, the test should consider the period from the beginning of a fiscal year to the end of the quarter as one period. As a result, there might be a difference in the result of the test depending on the average of the share price during the period.

In the three months ended June 30, 2006, there was no difference mentioned above.

Notes to Quarterly Consolidated Financial Statements

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Internet Initiative Japan Inc. ("IIJ"), a Japanese corporation, was founded in December 1992 to develop and operate Internet access services and other Internet-related services in Japan and is 29.7 percent owned by Nippon Telegraph and Telephone Corporation ("NTT") and its subsidiary, NTT Communications Corporation as of June 30, 2006. IIJ and consolidated subsidiaries (collectively, the "Company") provide Internet access services throughout Japan and into the United States of America and into the rest of Asia. The Company provides Internet-related systems integration, such as systems consultation, design, development, construction and operations and maintenance. The Company also provides systems integrations or sell equipment to supply equipment to construct systems, and provide other miscellaneous Internet access-related services.

The Company manages its business and measures results based on a single Internet-related services industry segment. Substantially all revenues are from customers operating in Japan.

Certain Significant Risks and Uncertainties

The Company has available-for-sale securities of JPY 4,288,015 thousand at June 30, 2006, and believes that the fluctuations in stock price of available-for-sale securities could have a material adverse effect on the Company's future financial position, results of operations or cash flows.

The Company relies on telecommunications carriers for significant portion of network backbone, and Nippon Telegraph and Telephone East Corporation ("NTT East"), Nippon Telegraph and Telephone West Corporation ("NTT West"), electric power companies and their affiliates for local connections to customers. The Company believes that its use of multiple carriers and suppliers significantly mitigates concentrations of credit risk. However, any disruption of telecommunication services could have an adverse effect on operating results.

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash investments, accounts receivable and guarantee deposits. The Company believes that the risks associated with accounts receivable is mitigated by the large number of customers comprising its customer base.

Summary of Significant Accounting Policies

Basis of Presentation

IIJ maintains its record in accordance with generally accepted accounting principles in Japan. Certain adjustment and reclassifications have been incorporated in the accompanying consolidated financial statements to conform to U.S. GAAP. These adjustments were not recorded in the statutory accounts.

Consolidation

The quarterly consolidated financial statements include the accounts of IIJ and all of its subsidiaries, Net Care, Inc. ("Net Care"), IIJ Technology Inc. ("IIJ Technology"), IIJ Financial Systems Inc. ("IIJ FS") and IIJ America, Inc. ("IIJ America"), which have first quarters ending June 30, except for IIJ America. IIJ America's first quarter end is March 31 and such date was used for purposes of preparing the quarterly consolidated financial statements as it is not practicable for the subsidiary to report its financial results as of June 30. There were no significant events that occurred during the intervening period that would require adjustment to or disclosure in the accompanying quarterly consolidated financial statements. Significant intercompany transactions and balances have been eliminated in consolidation. Investments in companies over which IIJ has significant influence but not control are accounted for by the equity method. For other than a temporary decline in the value of investments in equity method investees below the carrying amount, the investment is reduced to fair value and an impairment loss is recognized.

A subsidiary or equity method investee may issue its shares to third parties at amounts per share in excess of or less than the Company's average per share carrying value. With respect to such transactions, the resulting gains or losses arising from the change in ownership are recorded in income for the year in which such shares are issued.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Significant estimates and assumptions used are primarily in the areas of impairment loss on advances to equity method investees, valuation allowances for deferred tax assets, allowance for doubtful accounts, and estimated lives of fixed assets. Actual results could differ from those estimates.

Revenue Recognition

Revenues from customer connectivity services consist principally of dedicated Internet access services and dial-up Internet access services. Dedicated Internet access services represent full-line IP services and standard-level IP services (T1 Standard and IIJ FiberAccess/F Service). Dial-up Internet access services are provided to both enterprises and individuals (IIJ4U). The term of these contracts is one year for dedicated Internet access services and generally one month for dial-up Internet access services. All these services are billed and recognized monthly on a straight-line basis.

Value-added service revenues consist principally of sales of various

Internet access-related services such as firewall services. Value-added services also include monthly fees from data center services such as housing, monitoring, and security services. Other revenues under connectivity and value-added services consist principally of call-center customer support and Wide-area Ethernet services to construct networks that connect multiple operational sites for customers. The terms of these services are generally for one year and revenues are recognized on a straight-line basis during the service period.

Initial set up fees received in connection with connectivity services and value-added services are deferred and recognized over the contract period.

Systems integration revenues consist principally of the consultation of Internet network systems, design, development or construction and related maintenance, monitoring and other operating services. The period for the development of the systems or designs is less than one year and revenues are recognized when network systems and equipment are delivered and accepted by the customer under the completed contract method. The development of the Internet network systems or design includes multiple element arrangements such as consultation, planning, systems design, and construction services, and equipment and software purchased from third parties. When the equipment or system is delivered prior to other elements of the arrangement, revenue is deferred until other service elements are completed and accepted by the customer. Maintenance, monitoring, and operating service revenues are recognized ratably over the separate contract period, which is generally for one year.

Systems integration service is subject to the Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board ("FASB") Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables" which was adopted as of April 1, 2004.

Equipment sales are reported on a gross or net basis in accordance with EITF Issue No. 99-19 "Reporting Revenue Gross as a Principal versus Net as an Agent". Revenues are recognized when equipments are delivered and accepted by the customer.

Cash and Cash Equivalents

Cash and cash equivalents include time deposits and readily marketable securities with original maturities of three months or less.

Allowance for Doubtful Accounts

An allowance for doubtful accounts is established in amounts considered to be appropriate based primarily upon the Company's past credit loss experience and an evaluation of potential losses in the receivables outstanding.

Other Investments

In accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," all marketable equity securities are classified as available-for-sale securities, which are accounted for at fair value with unrealized gains and losses excluded from earnings and reported in accumulated other comprehensive income (loss). The cost of securities sold is determined based on average cost.

The Company reviews the fair value of available-for-sale investments on a regular basis to determine if the fair value of any individual investment has declined below its cost and if such decline is other than temporary. If the decline in value is judged to be other than temporary, the cost basis of the investment is written down to fair value. Other than temporary declines in value are determined taking into consideration the extent of decline in fair value, the length of time that the decline in fair value below cost has existed and events that might accelerate the recognition of impairment. The resulting realized loss is included in the consolidated statements of operations in the period in which the decline was deemed to be other than temporary.

Non-marketable equity securities are carried at cost as fair value is not readily determinable. If the value of a security is estimated to have declined and such decline is judged to be other than temporary, the security is written down to the fair value. Determination of impairment is based on the consideration of such factors as operating results, business plans and change in the regulatory, economic or technological environment of the investees. Fair value is determined as the Company's interest in the net assets of investees.

Inventories

Inventories consist mainly of network equipment purchased for resale and work-in-process for development of Internet network systems. Network equipment purchased for resale is stated at the lower of cost, which is determined by the average-cost method, or market. Work-in-process for development of network systems is stated at the lower of actual production costs, including overhead cost, or market. Inventories are reviewed periodically and items considered to be slow-moving or obsolete are written down to their estimated net realizable value.

Leases

Capital leases, which meet specific criteria noted in SFAS No. 13, "Accounting for Leases", are capitalized at the inception of the lease at present value of the minimum lease payments. All other leases are accounted for as operating leases. Lease payments for capital leases are apportioned to interest expense and a reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Operating lease payments are recognized as an expense on a straight-line basis over the lease term.

Property and Equipment

Property and equipment are recorded at cost. Depreciation and amortization of property and equipment, including purchased software and capitalized leases, are computed principally using the straight-line method based on either the estimated useful lives of assets or the lease period, whichever is shorter.

The useful lives for depreciation and amortization by major asset classes are as follows:

	Range of useful lives
Data communications, office and other equipment	2 to 15 years
Leasehold improvements	3 to 15 years
Purchased software	5 years
Capitalized leases	4 to 7 years

Impairment of Long-Lived Assets

Long-lived assets consist principally of property and equipment, including those items leased under capital leases. The Company evaluates the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". There were no impairment loss for long-lived assets for the three months ended June

30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006.

Goodwill and Intangible Assets

In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets", goodwill (including equity-method goodwill) and intangible assets that are deemed to have indefinite useful lives are not amortized, but are subject to impairment testing. Impairment testing is performed annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The Company performs annual impairment tests on March 31.

Pension and severance indemnities plans

The Company has pension plans and /or severance indemnities plans. The cost of the pension plans and severance indemnities plans are accrued based on amounts determined using actuarial methods, in accordance with SFAS No. 87, "Employers' Accounting for Pensions".

Income Taxes

The provision for income taxes is based on earnings before income taxes and includes the effects of temporary differences between assets and liabilities recognized for financial reporting purposes and income tax purposes and operating loss carryforwards. Valuation allowances are provided against assets that are not likely to be realized.

Foreign Currency Transactions

Foreign currency assets and liabilities, which consist substantially of cash and accounts payable for connectivity leases to international carriers denominated in U.S. dollars, are stated at the amount as computed by using quarter-end exchange rates and the resulting transaction gain or loss is recognized in earnings.

Derivative Financial Instruments

All derivatives are recorded at fair value as either asset or liabilities in the balance sheet in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 138 and No. 149 (collectively, "SFAS No. 133"). In accordance with SFAS No. 133, the Company designated interest swap contracts as a hedge of the variability of cash flows to be paid related to interest on floating rate borrowings (cash flow hedge) and the effective portion of the derivative's gain or loss is initially reported as a component of other comprehensive income and subsequently reclassified into earnings when the underlying transaction affects earnings. The ineffective portion of the gain or loss is reported in earnings immediately. The Company enters into contracts to hedge interest rate risks and does not enter into contracts or utilize derivatives for trading purposes.

Stock Sprits

On August 4, 2005, IIJ's board of directors approved a five-for-one split of IIJ's common stock. Shareholders of record on August 31, 2005 received an additional common share. The stock split was effective on October 11, 2005. In order to reflect this split, information pertaining to the number of shares of common stock and net income per share has been restated in the accompanying financial statements and related notes.

Stock-based Compensation

The Company accounts for stock-based compensation in accordance with SFAS No. 123R, "Accounting for Stock-Based Compensation" from this quarter. SFAS No. 123R requires compensation expense for stock options and other share-based payment to be measured and recorded based on the instruments' fair value. The Company adopted SFAS No. 123R and the related FASB Staff Positions on April 1, 2006 by using modified prospective application, which requires recognizing expenses for options granted prior to the adoption date equal to the fair value of unvested amounts over the remaining vesting period. The portion of these options' fair value attributable to vested awards prior to the adoption of SFAS No. 123R is never recognized.

As all existing granted stock-based awards of the Company have vested, the adoption of SFAS No. 123R did not have any impact on the Company's consolidated financial position or results of operations.

Research and Development and Advertising

Research and development and advertising costs are expensed as incurred.

Advertising

Advertising costs are expensed as incurred.

Basic and Diluted Net Income per Share

Basic net income per share is computed by dividing net income by the weighted-average number of shares of common stock outstanding during the quarter. Diluted net income per share reflects the potential dilutive effect of stock options. (See note 8 - Basic and Diluted Net Income per Share)

Other Comprehensive Income (Loss)

Other comprehensive income (loss) consists of translation adjustments resulting from the translation of financial statements of a foreign subsidiary, unrealized gains or losses on available-for-sale securities and gains or losses on cash flow hedging derivative instruments.

Segment Reporting

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," establishes standards for reporting information about operating segments. Operating segments are defined as components of an enterprise that engages in business activities from which it may earn revenues and incur expense and for which separate financial information is available that is evaluated regularly by the chief operation decision maker in deciding how to allocate resources and in assessing performance.

The Company provides a comprehensive range of network solutions to meet its customers' needs by cross-selling a variety of services, including Internet connectivity services, value-added services, systems integration and sales of network-related equipment. The Company's chief operating decision maker, who is IIJ's President and Representative Director, regularly reviews the revenue and cost of sales on a consolidated basis and makes decisions regarding how to allocate resources and assess performance based on a single operating unit.

New Accounting Standards

In June 2006, the FASB issued FASB Interpretation ("FIN") No. 48, "Accounting for Uncertainty in Income Taxes," which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." This interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in quarterly financial statements, disclosure, and transition. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of adopting this interpretation.

2. OTHER INVESTMENTS

Pursuant to SFAS No. 115, all of the Company's marketable equity securities, principally marketable shares of common stock of Japanese companies, were classified as available-for-sale securities. Information regarding the securities classified as available-for-sale at June 30, 2006, June 30, 2005 and March 31, 2006, is as follows:

(Unit: Thousands of Yen)

	As of June 30, 2006			
	Cost	Unrealized gains	Unrealized losses	Fair value
Available-for-sale--				
Equity securities	220,184	4,067,848	17	4,288,015

	As of June 30, 2005			
	Cost	Unrealized gains	Unrealized losses	Fair value
Available-for-sale--				
Equity securities	212,219	6,711,169	2,530	6,920,858

	As of March 31, 2006			
	Cost	Unrealized gains	Unrealized losses	Fair value
Available-for-sale--				
Equity securities	222,807	6,552,623	42	6,775,388

The following table provides the fair value and gross unrealized losses of the Company's investments, which have been deemed to be temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2006, June 30, 2005 and March 31, 2006:

(Unit: Thousands of Yen)

As of June 30, 2006

	Less than 12 months		12 months more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Marketable equity securities	1,363	17	--	--	1,363	17

	As of June 30, 2005					
	Less than 12 months		12 months more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Marketable equity securities	47,200	2,530	--	--	47,200	2,530

	As of March 31, 2006					
	Less than 12 months		12 months more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Marketable equity securities	1,338	42	--	--	1,338	42

The Company regularly reviews all of the Company's investments to determine if any are other-than-temporarily impaired. The analysis includes reviewing industry analyst reports, sector credit ratings and volatility of the security's market price.

Proceeds from the sale of available-for-sale securities were JPY 480,806 thousand, JPY 514,460 thousand and JPY 3,240,805 thousand for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, respectively. Gross realized gain of JPY 478,186 thousand, JPY 511,421 thousand and JPY 3,222,397 thousand were included in other income (expense) for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, respectively.

The aggregate cost of the Company's cost method investments totaled JPY 1,523,004 thousand, JPY 961,371 thousand and JPY 1,245,317 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively.

Losses on write-down of investments in certain marketable and nonmarketable equity securities, included in other income (expense), were recognized to reflect the decline in value considered to be other than temporary, totaled JPY 22,663 thousand and JPY 29,513 thousand for the three months ended June 30, 2005 and for the year ended March 31, 2006, respectively. Gain on exchange of securities of JPY 35,450 thousand and JPY 4,806 thousand, included in other income (expense), in the three months ended June 30, 2005 and the year ended

March 31, 2006, respectively, represented a non-monetary gain upon the exchange of marketable common shares in a merger transaction.

In Japan, there is a market in which participants lend and borrow debt and equity securities without collateral from financial institutions under agreement known as lending and borrowing debt and equity securities contracts. Under the agreement, the Company loans equity securities without collateral. The Company has loaned JPY 216,000 thousand and JPY 324,000 thousand of available-for-sale securities to the financial institution as of June 30, 2006 and March 31, 2006, respectively.

3. INVESTMENTS IN AND ADVANCES TO EQUITY METHOD INVESTEEES

IIJ utilizes various companies in Japan and neighboring countries to form and operate its Internet business. Businesses operated by its equity method investees include connectivity services in Asian countries (Asia Internet Holding Co., Ltd. ("AIH" through September 2005), multifeed technology services and location facilities for connecting high-speed Internet backbones (Internet Multifeed Co., "Multifeed"), Web page design services (atom Co., Ltd., "atom"), and data center services in Asian countries (i-Heart Inc., "i-Heart").

The aggregate amounts of balances and transactions of the Company with these equity method investees as of June 30, 2006, June 30, 2005 and March 31, 2006 and for each of the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006 were summarized as follows:

	As of June 30, 2006	As of June 30, 2005	As of March 31, 2006
Accounts receivable	46,559	110,435	253,208
Accounts payable	13,039	94,810	17,804
	From April 1, 2006 to June 30, 2006	From April 1, 2005 to June 30, 2005	From April 1, 2005 to March 31, 2006
Revenues	123,503	308,627	1,286,275
Cost and expenses	36,075	283,200	656,184

During each of the three months ended June 30, 2006, and June 30, 2005 and the year ended March 31, 2006, the Company did not receive any dividends from its equity method investees.

The Company's investments in and advances to these equity method investees and respective ownership percentage at June 30, 2006, June 30, 2005 and March 31, 2006 consisted of the following:

	As of June 30, 2006		As of June 30, 2005		As of March 31, 2006	
	Ownership (%)	Thousands of Yen	Ownership (%)	Thousands of Yen	Ownership (%)	Thousands of Yen
AIH	--	--	26.69	265,460	--	--
Multifeed	29.44	352,648	28.58	264,219	29.44	317,144
atom	40.00	99,675	40.00	106,521	40.00	116,974
Internet Revolution Inc.	30.00	585,291	--	--	30.00	676,795
Other		57,444		40,835		52,058
Total		1,095,058		677,035		1,162,971

Advances of JPY 34,545 thousand, JPY 19,868 thousand and JPY 34,545 thousand to an equity method investees, net of loan loss valuation allowance was included in the balances, as of June 30, 2006, June 30, 2005 and March 31, 2006, respectively.

4. LEASES

The Company enters into, in the normal course of business, various leases for domestic and international backbone services, office premises, network operation centers and data communications and other equipment. Certain leases that meet one or more of the criteria set forth in the provision of SFAS No. 13, "Accounting for leases" have been classified as capital leases and the others have been classified as operating leases.

Operating Leases

The Company has operating lease agreements with telecommunications carriers and others for the use of connectivity lines, including local access lines that customers use to connect to IIJ's network. The leases for domestic backbone connectivity are generally either non-cancelable for a minimum one-year lease period or cancelable during a lease period of three years, with a significant penalty for cancellation (35%). The leases for international backbone connectivity during one-year lease period are substantially non-cancelable. The Company also leases its office premises, for which refundable lease deposits are capitalized as guarantee deposits, and certain office equipment under non-cancelable operating leases which expire on various dates through the year 2008 and also leases its network operation centers under non-cancelable operating leases.

Refundable guarantee deposits as of June 30, 2006, June 30, 2005 and March 31, 2006 consist of as follows:

	As of June 30, 2006	As of June 30, 2005	As of March 31, 2006
Head Office	1,185,307	1,744,949	1,185,307
Sales and subsidiaries offices	314,253	298,457	308,494
Other	55,041	47,831	55,852
Total refundable			

guarantee deposits	1,554,601	2,091,237	1,549,653

Lease expenses related to backbone lines for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006 amounted to JPY 871,856 thousand, JPY 863,705 thousand and JPY 3,516,322 thousand, respectively. Lease expenses for local access lines for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, which are only attributable to dedicated access revenues, amounted to JPY 1,143,812 thousand, JPY 1,131,358 thousand and JPY 4,558,382 thousand, respectively. Other lease expenses for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006 amounted to JPY 1,040,676 thousand, JPY 871,848 thousand and JPY 3,653,766 thousand, respectively.

The Company has subleased a part of its office premises. Lease expenses mentioned above have been reduced by sublease revenues totaling JPY 111,021 thousand and JPY 435,224 thousand for the three months ended June 30, 2005 and the year ended March 31, 2006, respectively.

Capital Leases

The Company conducts its connectivity and other Internet-related services by using data communications and other equipment leased under capital lease arrangements. The fair values of the assets upon execution of the capital lease agreements and accumulated depreciation amounted to JPY 14,529,403 thousand and JPY 7,338,962 thousand at June 30, 2006, JPY 12,740,593 thousand and JPY 6,265,906 thousand at June 30, 2005 and JPY 14,458,667 thousand and JPY 6,819,503 thousand at March 31, 2006, respectively.

As of June 30, 2006, future lease payments under non-cancelable operating leases, including the aforementioned non-cancelable connectivity lease agreements (but excluding dedicated access lines which the Company charges outright to customers), and capital leases were as follows:

	As of June 30, 2006		
	Connectivity lines operating leases	Other operating leases	Capital leases
Through June 30, 2007	12,798	1,345,745	3,457,253
July 1, 2007 and thereafter	0	1,115,777	4,022,923

5. BORROWINGS AND CONVERTIBLE NOTES

Short-term borrowings at June 30, 2006, June 30, 2005 and March 31, 2006 consist of bank overdrafts. Short-term borrowings bear fixed-rate interest and their weighted average rates at June 30, 2006, June 30, 2005 and March 31, 2006 were 1.050 percent, 1.375 percent, and 1.375 percent, respectively.

Long term borrowings as of June 30, 2006, June 30, 2005 and March 31, 2006 consisted of the following:

(Unit: Thousands of Yen)

	As of June 30, 2006	As of June 30, 2005	As of March 31, 2006
Unsecured long-term loans payable to banks, maturing at various dates through calendar 2007. Interest is payable at a variable rate. Weighted average interest rates were 2.169 percent, 1.946 percent and 2.206 percent at June 30, 2006, June 30, 2005 and March 31, 2006, respectively.	353,000	937,000	374,000
Unsecured long-term loans payable to banks (secured in 2005), maturing in calendar 2006. Weighted average interest rates were 1.857 percent and 1.710 percent at June 30, 2005 and March 31, 2006, respectively.	--	1,450,000	600,000
Unsecured long-term loans payable to banks (secured in 2005), maturing at various dates through calendar 2007. Interest is payable at a variable rate based on TIBOR. All of interest is converted to a fixed interest rate through interest rate swap contracts. Weighted average interest rates were 1.174 percent, 1.132 percent and 1.130 percent at June 30, 2006, June 30, 2005 and March 31, 2006, respectively.	1,150,000	1,400,000	1,150,000
Long-term installment loans payable at various dates through calendar 2007. Interest rates were 2.55 percent at June 30, 2006, June 30, 2005 and March 31, 2006.	117,342	270,365	155,963
Total	1,620,342	4,057,365	2,279,963
Less current portion	(1,351,342)	(3,187,023)	(1,989,963)
Long-term borrowings less current portion	269,000	870,342	290,000

The Company entered into interest rate swap contracts to manage its interest rate exposure resulting in a fixed interest rate for a portion of its long-term debt.

On March 14, 2003, the Company entered into a long-term installment loan agreement with a leasing company to finance the payment for rental deposits given to other lessor for its new head office. The principal of the loan is JPY 117,342 thousand, JPY 270,365 thousand and JPY 155,963 thousand at June 30, 2006, June 30, 2005 and March 31, 2006 and the loan is secured by a first priority pledge against a claim for the guarantee deposits of JPY 1,146,039 thousand at June 30, 2006.

The Company entered into bank overdraft agreements with certain Japanese banks for which the unused balance outstanding as of June 30, 2006, June 30, 2005 and March 31, 2006 was JPY 5,620,000 thousand, JPY 1,891,613 thousand and JPY 3,210,000 thousand.

Since August 2004, the Company has been a party to a securities loan agreement with a certain Japanese financial institution. The available-for-sale securities loaned to the financial institution were JPY 632,700 thousand, JPY 1,910,200 thousand and JPY 1,230,000 thousand, and the cash received in return was JPY 496,080 thousand, 1,530,400 thousand and 999,600 thousand at June 30, 2006, June 30, 2005 and March 31, 2006, respectively. These transactions were accounted for as secured borrowings and the cash received was recorded as payable under the securities loan agreement and securities lent were recorded as other investments. The agreement requires the Company to provide certain marketable securities as collateral at the commencement of the transaction. The Company is required to make a partial repayment or receive additional borrowings depending on the market value of securities pledged. The Company paid the interest on the payables at a variable rate, which was 0.37 percent, 0.6349 percent and 0.37 percent as of June 30, 2006, June 30, 2005 and March 31, 2006, respectively.

6. COMITMENTS AND CONTINGENT LIABILITIES

In December 2001, a class action complaint alleging violations of the federal securities laws was filed against the Company, naming IIJ, certain of its officers and directors as defendants, and underwriters of IIJ's initial public offering. Similar complaints have been filed against over 300 other issuers that have had initial public offerings since 1998 and such actions have been included in a single coordinate proceeding in the Southern District of New York. An amended complaint was filed on April 24, 2002 alleging, among other things, that the underwriters of IIJ's initial public offering violated the securities laws (i) by failing to disclose in the offering's registration statement certain alleged compensation arrangements entered into with the underwriters' clients, such as undisclosed commissions or tie-in agreements to purchase stock in the after-market, and (ii) by engaging in manipulative practices to artificially inflate the price of IIJ's stock in the after-market subsequent to the initial public offering. On July 15, 2002, the Company joined in an 'omnibus' motion to dismiss the amended complaint filed by the issuers and individuals named in the various coordinated cases. In June 2003, the Company approved a settlement with the plaintiffs in this matter. IIJ, along with the settling issuer defendants, filed a motion seeking the court's preliminary approval of the settlement. The court granted preliminary approval of the settlement on February 15, 2005, subject to certain modifications. On August 31, 2005, the court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The court also appointed the Notice Administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members beginning on November 15, 2005, The settlement fairness hearing took place on April 24, 2006. If the court determines that the settlement is fair to the class members, the settlement will be approved. The settlement releases IIJ and the individual defendants for liability for the conduct alleged in the action. Under the settlement, the Company agreed to assign away, not assert, or release certain potential claims the Company may have against IIJ's underwriters. Approximately 260 defendant issuers participated in this settlement. As to financial impact on the Company, the settlement provides that the class members will be guaranteed $1 billion in recoveries by the insurers of the issuers. In addition to IIJ's portion of the proposed settlement, some of the continuing legal expenses incurred in connection with the partial settlement would be borne by IIJ's insurer based on the settlement agreement and an individual agreement between IIJ and IIJ's insurer. Consequently, the Company believes that there will be no significant financial impact on the Company as a result of this matter.

In addition to the foregoing, the Company is a party to other suits and claims that arise in the normal course of business. The negative adverse outcome of such suits and claims would not have a significant impact on the financial statements.

In January 19, 2006, IIJ entered into a joint venture agreement regarding the establishment and management of Internet Revolution Inc. ("i-revo") with Konami corporation. In the agreement, IIJ committed an additional contribution for capital investment or working capital to i-revo of up to JPY 90,000 thousand for the period from November 2006 to April 2007.

7. DERIVATIVE AND OTHER FINANCIAL INSTRUMENTS Interest Rate Swap Agreement

The Company is exposed to changes in interest rates that are associated with long-term bank borrowings. The Company's policy on managing the interest rate risk is to hedge the exposure to variability in future cash flows of floating rate interest payments on the long-term bank borrowings. In order to reduce cash flow risk exposures on floating rate borrowings, the Company utilizes interest rate swap agreements to convert a floating rate borrowing to a fixed rate borrowing.

The Company is also exposed to credit-related losses in the event of non-performance by counterparties to interest rate swaps, but it is not expected that any counterparties will fail to meet their obligations, because counterparties are internationally recognized financial institutions.

Changes in fair value of interest rate swaps designated as hedging instruments are reported in accumulated other comprehensive income during the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006. These amounts subsequently are reclassified into interest expense as a yield adjustment in the same period in which the hedged bank borrowings affect earnings. The term, notional amount, and repricing date of interest rate swaps exactly match those of the long-term borrowings. The swap terms are "at the market," so they have zero value at inception. Thus, there was no ineffectiveness recognized in earning for the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006. For the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, net derivative loss of JPY 751 thousand, JPY 752 thousand and JPY 10,008 thousand were reclassified to interest expense, respectively.

Approximately JPY 6,988 thousand of accumulated other comprehensive loss related to the interest rate swaps are expected to be reclassified as an adjustment to interest expense as a yield adjustment of the hedged bank borrowings within the next 12 months.

8. BASIC AND DILUTED NET INCOME PER SHARE

The basic and diluted net income per share in the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006 is as follows:

	From April 1, 2006 to June 30, 2006	From April 1, 2005 to June 30, 2005	From April 1, 2005 to March 31, 2006
Numerator:			

Net income (JPY thousand)	733,671	622,674	4,753,570
Dilutive effect (JPY thousand)	--	--	--
Diluted net income (JPY thousand)	733,671	622,674	4,753,570
Denominator:			
Basic weighted average number of shares of common stock outstanding	203,989	191,547	195,613
Effect by stock option	241	--	342
Diluted weighted average number of shares of common stock outstanding	204,230	191,547	195,955
Basic net income per share	3,597	3,251	24,301
Diluted net income per share	3,592	3,251	24,258

For the three months ended June 30, 2006, the three months ended June 30, 2005 and the year ended March 31, 2006, the number of the potential common shares excluded from the computation of diluted net income per share because the exercise prices of the options were greater than the average market price of the common shares was 975, 2,700 and 975 at June 30, 2006, June 30, 2005 and March 31, 2006, respectively.

9. SUBSEQUENT EVENTS

The reductions of additional paid-in capital of JPY 21,980,395 thousand and common stock of JPY 2,539,222 thousand to eliminate accumulated deficit for purposes of reporting under the Corporation Law in its non-consolidated financial statements, approved by IIJ's shareholders at the 14th Ordinary General Shareholders' Meeting held on June 28, 2006 became effective on August 4, 2006.

(5) Others No applicable item.