(Reference) Case Report from Audit Firm Inspection Results

Recent Trends in Audit Firms

(Monitoring Report in Fiscal 2016)

July 2016

Certified Public Accountants and Auditing Oversight Board

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Introduction

The Certified Public Accountants and Auditing Oversight Board ("CPAAOB") has prepared *Activities of the Certified Public Accountants and Auditing Oversight Board,* as a summary of the CPAAOB's activities. The CPAAOB has also prepared and issued *Case Report from Audit Firm Inspection Results* ("case report"), a compilation of examples of deficiencies identified in inspections, every year.

The case report has been widely used, mainly by audit firms. However, at the same time, we have received opinions from readers that, as the contents are highly technical and extensive, readers other than professional accountants have difficulty understanding the contents.

As the role of auditing has increasingly grown in importance in the capital market, it also has become important to have an appropriate assessment of quality control at audit firms for many parties including enterprises and shareholders. Under these circumstances, the CPAAOB has prepared *Recent Trends in Audit Firms (Monitoring Report in Fiscal 2016)* to provide information on the status of audit firms for not only professional accountants but also other readers in a plain way. We hope you will use it together with the case report.

(Fiscal 2016 Edition)

We issued the Monitoring Report in Fiscal 2016 as reference materials of the case report, since we have compiled information that will help you to understand the status of audit firms based on materials and publicly available information that the CPAAOB gathered.

In the future, we would like to enhance the contents further including information on the CPAAOB's monitoring activities as much as possible and issue the Monitoring Report separately from the case report.

(Definition terms)

- The term *Act* refers to Certified Public Accountants Act.
- The term *audit firm* refers to an audit corporation, a joint office or a sole practitioner.
- The term *JICPA* refers to the Japanese Institute of Certified Public Accountants.
- The term *FIEA* refers to Financial Instruments and Exchange Act.
- The term *TSE* refers to Tokyo Stock Exchange.

Outline of Laws and Regulations and Various Systems Regarding Audit Firms

We hereby explain the system of certified public accountants and audit corporations, which are subject to this report, and the details of their services.

We also describe JICPA, which guides and supervises its members and manages administrative work regarding the registration of audit firms.

1. Certified Public Accountant System

The mission of certified public accountants, as professionals of auditing and accounting, shall be to ensure matters such as the fair business activities of companies, etc. and the protection of investors and creditors by ensuring the reliability of financial information and any other information concerning finance from an independent standpoint, thereby contributing to the sound development of the national economy (Article 1 of the Act).

A person who desires to be a certified public accountant shall pass the certified public accountant examination and meet certain requirements (internship and professional accountancy education program), and shall have his/her name registered on the certified public accountants list, which is maintained at the Japanese Institute of Certified Public Accountants (Article 3, 17 and 18 of the Act).

2. Audit Corporation System

An audit corporation refers to a corporation that is incorporated jointly by certified public accountants to conduct audit attestation in an organized manner. In this case, the persons who intend to be its partners shall include five or more persons who are certified public accountants (Article 34-7 (1)). Moreover, an audit corporation shall, when it has been incorporated, notify the prime minister (his/her authority shall be delegated to the commissioner of the Financial Services Agency in accordance with Article 49-4; the same shall apply hereinafter) to that effect after its incorporation (Article 34-9-(2)).

An audit corporation shall design an operation control system to perform its services fairly and properly and shall submit a business report to the prime minister each fiscal year.

The CPAAOB classifies audit firms into the following three categories according to the scale of their business.

Large-scale audit firms (Major audit corporations)	Second-tier large-scale audit firms (Quasi-major audit corporations)	Small and medium-sized audit firms
Audit firms that have more than 100 engagements with listed companies and have more than 1,000 full-time audit professionals.	Audit firms other than major audit corporations that have a relatively large number of listed companies	Small and medium-sized audit firms (audit firms other than major and quasi-major audit corporations), joint office or sole practitioners

The following table shows specific names of audit corporations.

(As of July 2016)

(Major audit corporations)	(Quasi-major audit corporations)
Deloitte Touche Tohmatsu LLC Ernst & Young ShinNihon LLC KPMG AZSA LLC PricewaterhouseCoopers Aarata LLC	BDO Sanyu & Co. BDO Toyo & Co. Grant Thornton Taiyo LLC GYOSEI & CO. PricewaterhouseCoopers Kyoto YUSEI Audit & Co.

(Audit corporation names listed in alphabetical order.)

In the following chapter, *Design of Quality Control System by Audit Corporations and Outline of Monitoring*, we will describe the operation control system that an audit corporation shall design.

3. Services Provided by Certified Public Accountants and Audit Corporations

The services provided by certified public accountants and audit corporations are prescribed by the Act as follows.

- Audit and Attestation Services: Audit or attest financial information for fees upon the requests of others. Only certified public accountants and audit corporations can perform audit and attestation services (Article 2-1)
- Non-Audit and Attestation Services: Prepare financial statements, investigate or plan financial matters, or advise on financial matters for fees upon the requests of

others, using the title of a certified public accountant or an audit corporation (Article 2-2).

4. Japanese Institute of Certified Public Accountants (JICPA)

The purpose of JICPA shall be to maintain the professional attitude of certified public accountants, to give guidance, to liaise with, to supervise its members in order to achieve the improvement and progress of the services set forth in Article 2 (1), and to maintain the registration of certified public accountants and specified partners (Article 43).

A certified public accountant or an audit corporation shall become a member of JICPA (Article 46-2) and needs to be registered with the relevant Regional Chapter of JICPA (16 Regional Chapters nationwide as of July 2016).

Design of Quality Control System by Audit Corporations and Outline of Monitoring

In this chapter, we describe the broad outline of an important element for assessing the quality of audit engagements—the design of a quality control system by audit corporations. Then, we explain quality control (QC) reviews and inspections of audit firms as a system to ensure the quality of audit engagements.

1. Design of a Quality Control System by Audit Corporations

An audit corporation shall design an operation control system pursuant to the provisions of a Cabinet Office Ordinance in order to perform its services fairly and properly. The operation control system shall include the design and the implementation of a policy on quality controls (Article 34-13 (1), (2)).

The quality controls mentioned above are specifically prescribed as taking the necessary measures for preventing situations that would impair the reasonableness, appropriateness and credibility of services concerning the below matters. (Article 34-13 (3), Ordinance for Enforcement of the Certified Public Accountants Act, Article 26)

Compliance of professional ethics and independence
Acceptance and continuance of engagements
Employment, education, training, evaluation, and appointment of partners and other professionals
Performance of engagements and engagement quality control reviews

The Business Accounting Council has also set *Quality Control Standards for Audit*, which define the quality control that audit firms and audit practitioners who perform audit engagements shall comply. When performing audits based on the FIEA, audit firms and audit practitioners are required to conform to the *Quality Control Standards for Audit*. (Cabinet Office Ordinance on Audit Certification of Financial Statements, etc. Article 3 (3), Cabinet Office Ordinance on the System for Ensuring the Adequacy of Documents on Financial Calculation and of Other Information Article 1 (3))

Following the above, JICPA has set *Quality Control for Audit Firms* (Quality Control Standards Committee Statement No.1) as rules related to quality control that audit firms (members of JICPA) shall comply with.

The items included in *Quality Control for Audit Firms* are as follows:

Application and compliance of related requirements
Composition of quality control systems
Responsibilities for quality controls
Professional ethics and independence
Acceptance and continuance of engagements
Employment, education, training, evaluation, and assignment of professionals (assignment of the engagement team)
Performance of engagements (consultation, engagement quality control reviews, differences in audit judgments, and audit documentations)
Monitoring of quality control systems (monitoring of the audit firm's policy and procedures related to the quality control, assessment of identified deficiencies, communication and remediation, appeal of an objection and raising of a doubt)
Documentation of the quality control system
Transfer of audit engagements between audit firms
Joint audit

JICPA has also set *Quality Control Related to Audit Engagements* as the rules related to quality control that audit practitioners who perform audit engagements shall comply with. (Auditing Standards Committee Statement 220)

We explain the acceptance and continuance of engagements, engagement quality control reviews, and monitoring of the audit firm's policy and procedures related to the quality control as items related to this report.

i) Acceptance and continuance of engagements

Audit firms shall set the policy and procedures for the acceptance and continuance of engagements with audit clients. (Quality Control Standards Committee Statement No.1 (25))

Specifically, the following conditions must be met.

Audit firms have capabilities and aptitudes to perform audit engagements including time and human resources.
Audit firms can comply with the rules regarding related professional ethics.
Audit firms have to consider the integrity of audit clients and to ensure that there are not significant concerns about the acceptance and continuance of engagements.

ii) Engagement quality control reviews

Audit firms shall, in principle, set the policy and procedures for engagement quality control reviews to objectively assess audit procedures, important audit judgments, and audit opinions issued by the engagement team in expressing audit opinions at all audit engagements. (Quality Control Standards Committee Statement No.1 (34))

Specifically, it is necessary to be prescribed for the execution of the following.

Discussion with an engagement partner about important issues
Review of financial statements and auditor's report draft
Consideration of important judgements made by engagement teams and the audit documentation regarding the conclusion
Assessment of the audit opinion and the appropriateness of the auditor's report draft

iii) Monitoring of the audit firm's policy and procedures related to quality control

Audit firms shall set the process for the monitoring of the quality control system to rationally ensure that the policy and procedures related to the quality control system are appropriately and sufficiently designed and effectively operated. (Quality Control Standards Committee Statement No.1 (47))

The above includes monitoring by the audit firms themselves and global reviews by international audit network firms.

2. QC Reviews and Inspections of Audit Firms

i) Quality control review by JICPA

A quality control review shall be conducted by JICPA to monitor the status of the operation of audit and attestation services set forth in Article 2 (1) that is provided by Article 46-9 (2). JICPA investigates the status of audit quality control by audit firms and makes recommendations for improvement to audit firms as necessary.

JICPA shall, periodically or as needed, report the results of QC review to the prime minister (the authority delegated to CPAAOB pursuant to Article 49-4).

ii) Inspections by CPAAOB

From the standpoint of establishing capital markets that investors trust through ensuring the fairness and transparency of the market, CPAAOB receives and inspects the quality control review reports from JICPA. As necessary, CPAAOB conducts on-site inspection of audit firms and JICPA.

If inspections reveal that JICPA failed to conduct its quality control review appropriately, or that audit quality control by audit firms was significantly insufficient and did not conform to laws and regulations, CPAAOB may make recommendations to the prime minister (FSA commissioner) concerning administrative guidance or any other measure to be taken in order to assure proper operations of the audit services. (Article 41-2)

For details of the above, please refer to *Activities of the Certified Public Accountants and Auditing Oversight Board* (June 2016).

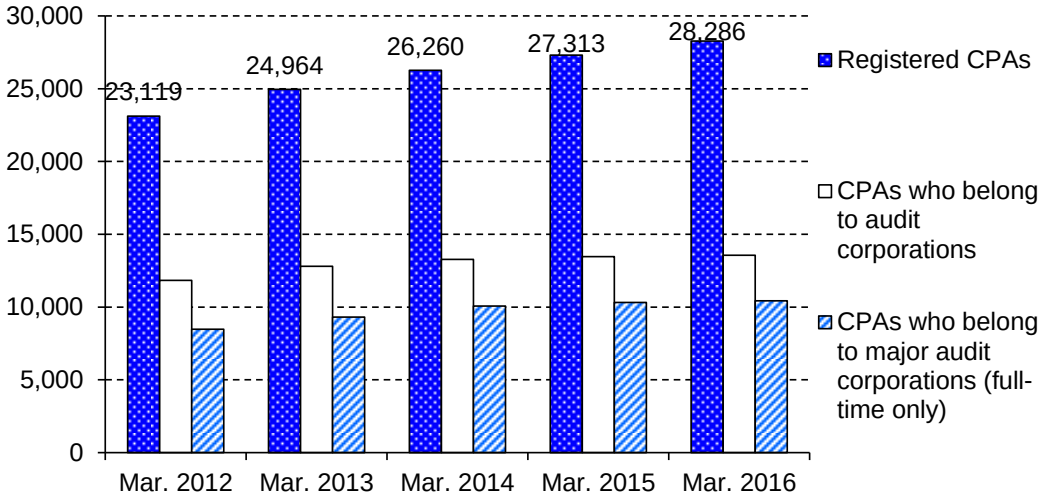
I. Overview of Certified Public Accountants

The changes in the number and age composition of registered certified public accountants and the number of certified public accountants by regional chapters are shown below.

The number of registered certified public accountants has been gradually increasing for several years, while the number of certified public accountants who belong to audit corporations has remained flat. (Fig. I-1)

Regarding the number of certified public accountants by regional organization, the majority are located in the metropolitan regions and a few are based in regions outside the major cities. (Fig. I-3)

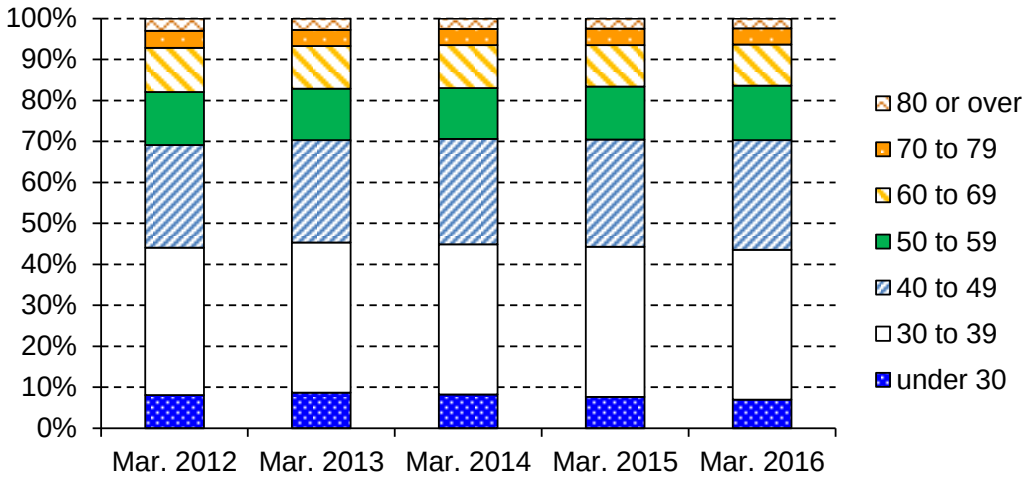
Fig. I-1 Change in the number of registered certified public accountants



(Source) JICPA, CPAAOB[1] (The number of certified public accountants who belong to major audit corporations is calculated by totaling the number of certified public accountants of each audit corporation during the above periods).

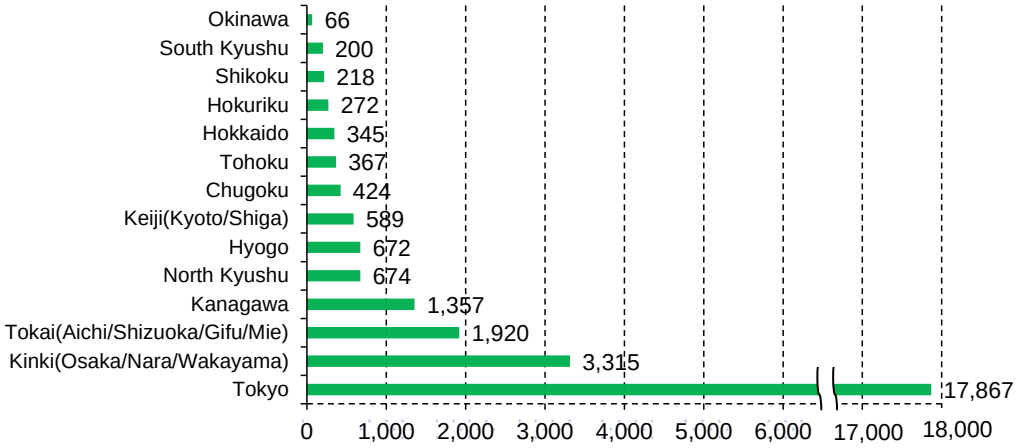
[1] CPAAOB in the above Source refers to data obtained by CPAAOB that was prepared by using materials regarding audit firms.

Fig. I-2 Change in the age composition of registered certified public accountants



(Source) JICPA

Fig. I-3 Number of certified public accountants by regional chapters



(Source) JICPA (as of the end of March 2016; in April 2016, the Saitama and Chiba Chapters were separated from the Tokyo Chapter)

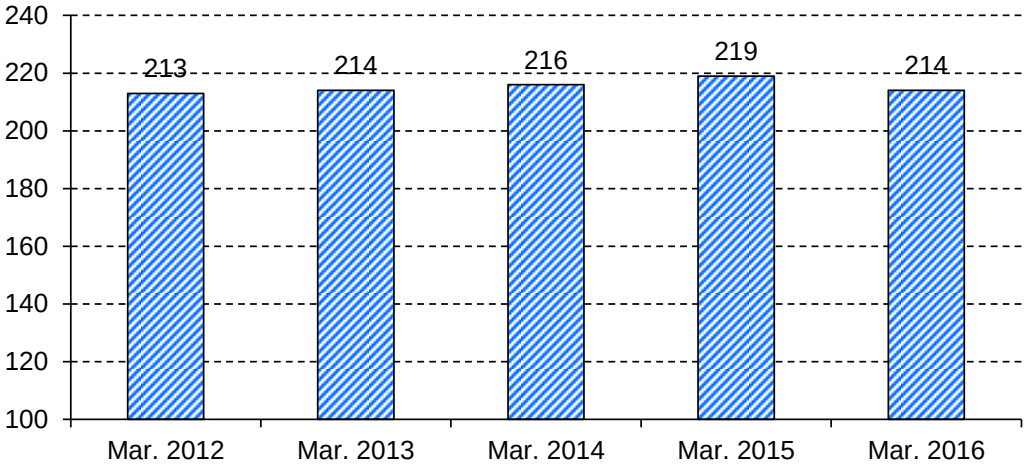
II. Overview of Audit Corporations

1. Overview of Audit Corporations

(1) Change in the Number of Audit Corporations

The number of audit corporations has not changed significantly for several years. (Fig. II-1-1)

Fig. II-1-1 Change in the number of audit corporations



(Source) JICPA

(2) Change in the Personnel Composition and Average Age of Staff in Audit Corporations

The change in the number of partners and full-time employees and the average age of partners and full-time employees (Fiscal Year 2014[2]) and the number of part-time employees (Fiscal Year 2014) at audit corporations (according to the size of audit corporations) are shown below.

Regarding the composition of personnel according to the size of audit corporations, the percentage of partners is higher at small and medium-sized audit corporations compared to major audit corporations and quasi-major audit corporations, since an audit corporation shall have five or more partners. (Fig. II-1-2)

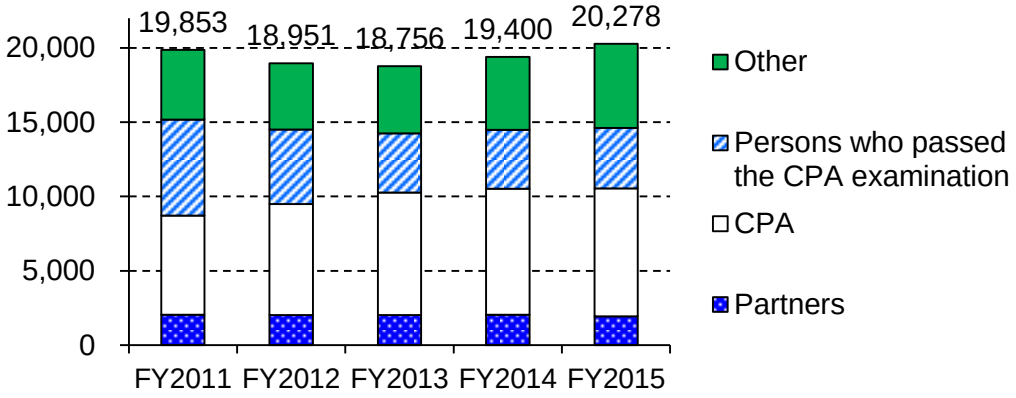
[2] In this report, “Fiscal Year” refers to the fiscal year ended March, unless otherwise noted.

Furthermore, the average age of partners and full-time employees at small and medium-sized audit corporations tends to be higher compared to major audit corporations and quasi-major audit corporations. (Fig. II-1-3)

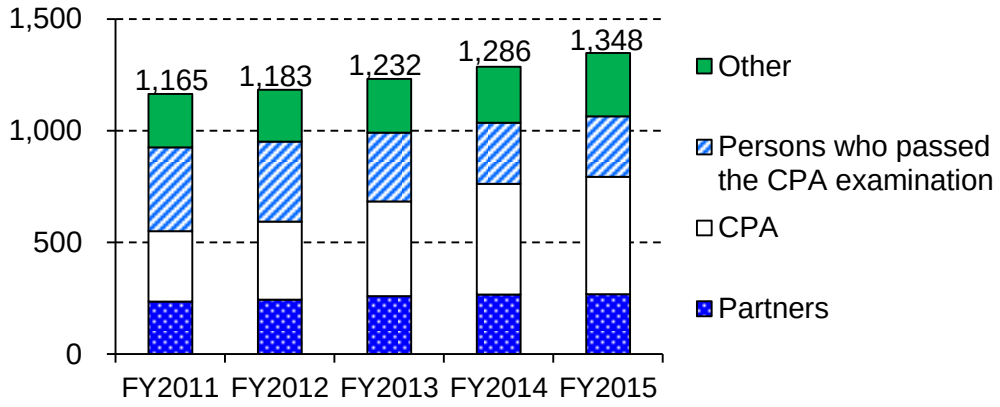
The percentage of part-time employees tends to be higher at small and medium-sized audit corporations. (Fig. II-1-4)

Fig. II-1-2 Change in the number of partners and full-time employees

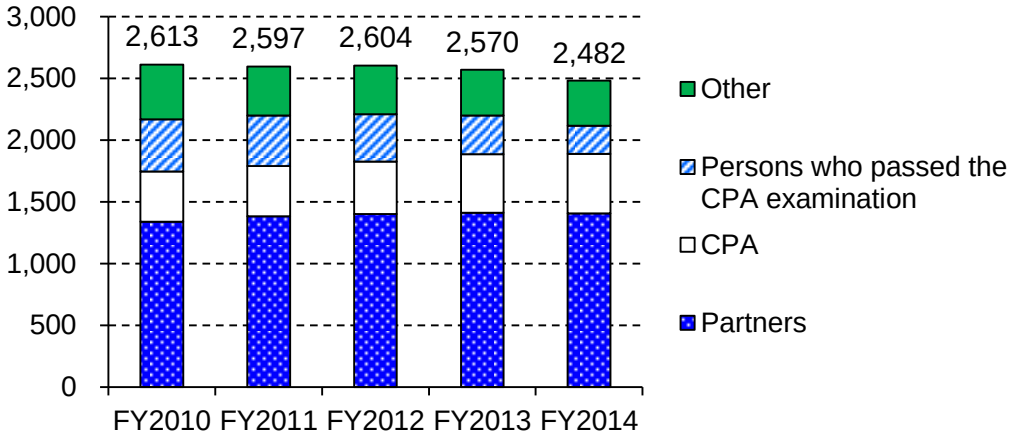
Major audit corporations (total of four audit corporations)



Quasi-major audit corporations (total of six audit corporations)

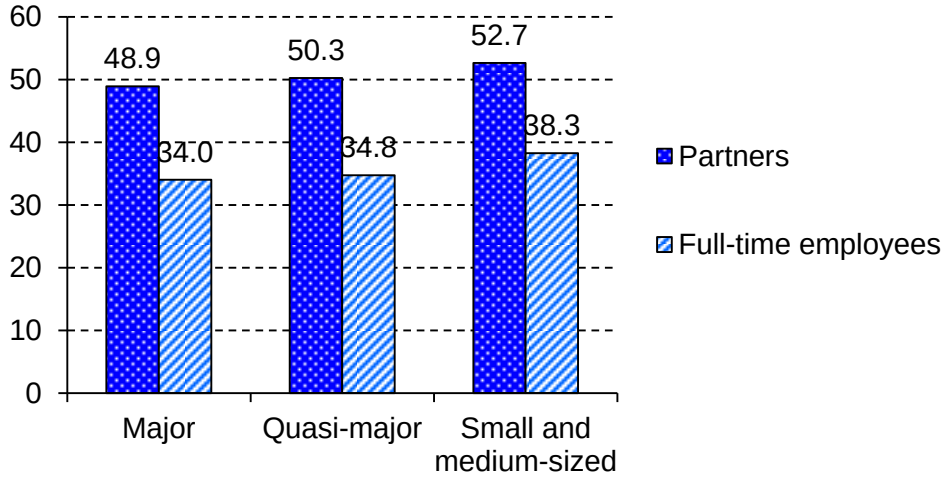


Small and medium-sized audit corporations (total)



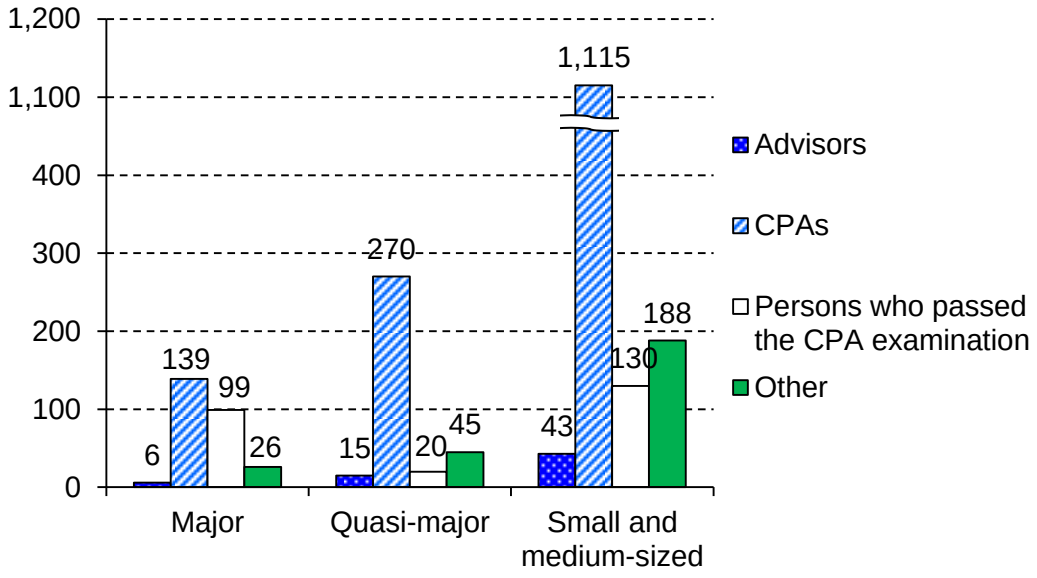
(Source) CPAAOB (The number of personnel at each audit corporation for the above fiscal years is added up. Regarding major and quasi-major audit corporations, the data is gathered up to Fiscal Year 2015. Regarding small and medium-sized audit corporations, the data is gathered up to Fiscal Year 2014.)

Fig. II-1-3 Average age of partners and full-time employees (Fiscal Year 2014)



(Source) CPAAOB (Average age calculated based on the average age of personnel at each audit corporation in Fiscal Year 2014)

Fig. II-1-4 Number of part-time employees (Fiscal Year 2014) (unit: persons)



(Source) CPAAOB (The number of personnel at each audit corporation in Fiscal Year 2014 is added up.)

2. Overview of Services Provided and Operating Revenues

Audit corporations provide audit and attestation as exclusive services. In addition, they provide non-audit services including support for initial public offerings, support for the implementation of International Financial Reporting Standards, and consulting services, such as financial-related advisory services for business reorganization.

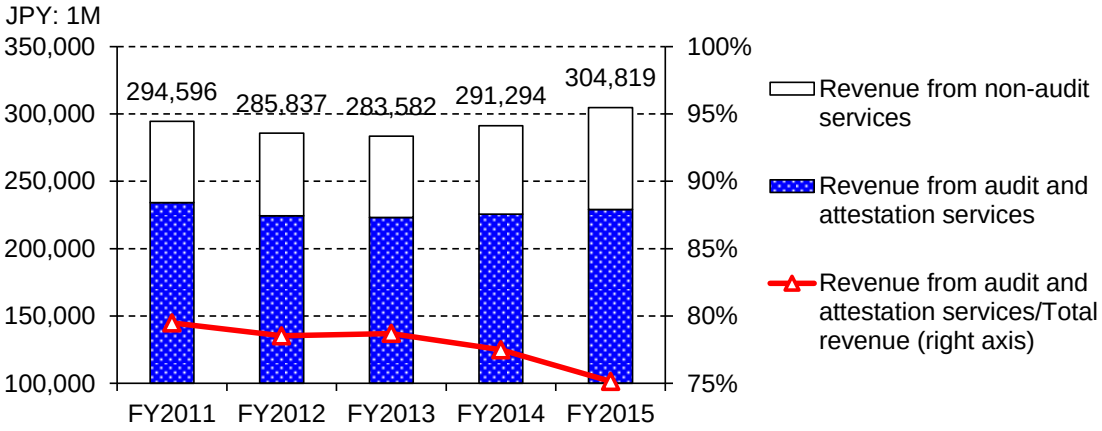
The breakdown of operating revenue and the change in the percentage of revenue from audit and attestation services at audit corporations are shown below.

The percentage of revenue from non-audit services is higher at major audit corporations compared to quasi-major audit corporations and small and medium-sized audit corporations. Furthermore, the percentage of revenue from audit and attestation services has been declining at major audit corporations.

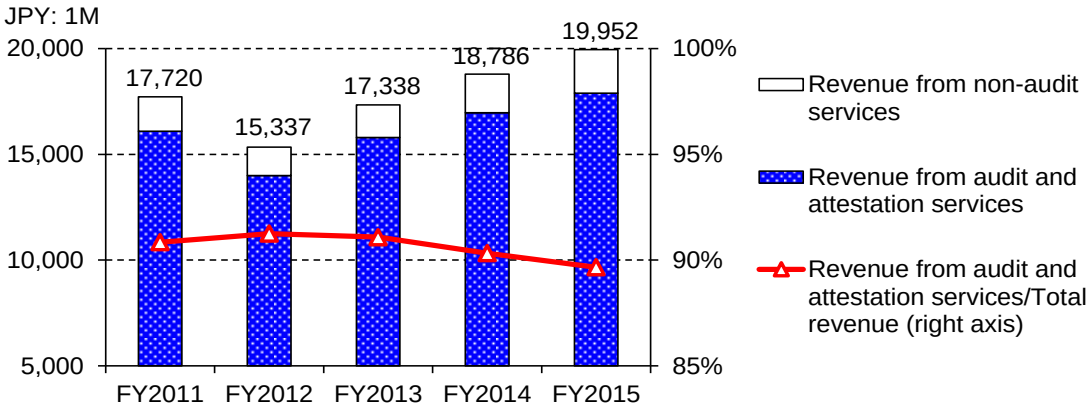
Meanwhile, dependence on audit and attestation services is high at quasi-major audit corporations and small and medium-sized audit corporations. The percentage of revenue from audit and attestation services exceeds around 90% of total operating revenue. (Fig. II-2)

Fig. II-2 Breakdown of operating revenue and the change in the percentage of revenue from audit and attestation services

Major audit corporations (total of four corporations)

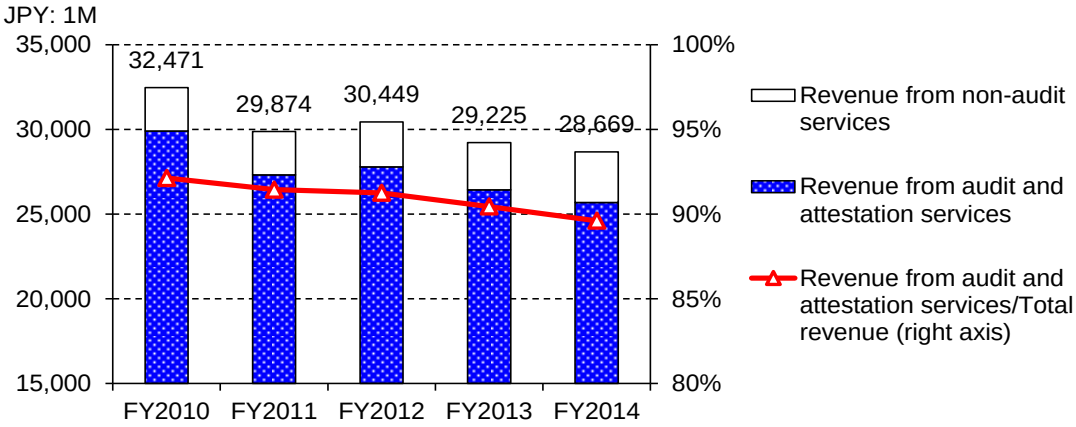


Quasi-major audit corporations (total of six audit corporations)



(Note) In FY2012, one audit corporation accounted for operating revenue for only three months due to the change of the fiscal year end.

Small and medium-sized audit corporations (total)



(Source) CPAAOB (Operating revenues of each audit corporation for the above fiscal years are added up. Regarding major and quasi-major audit corporations, the data is gathered up to Fiscal Year 2015. Regarding small and medium-sized audit corporations, the data is gathered up to Fiscal Year 2014.)

3. Overview of Audit Corporation Group

Most of the major audit corporations and quasi-major audit corporations use common logos and brands, and mutually cooperate to form business alliances[3] with their group firms. In general, audit corporation groups include audit corporations, tax corporations, consulting firms that perform financial due diligence, valuation and fraud investigations, and advisory firms that provide financial advisory services for M&A deals.

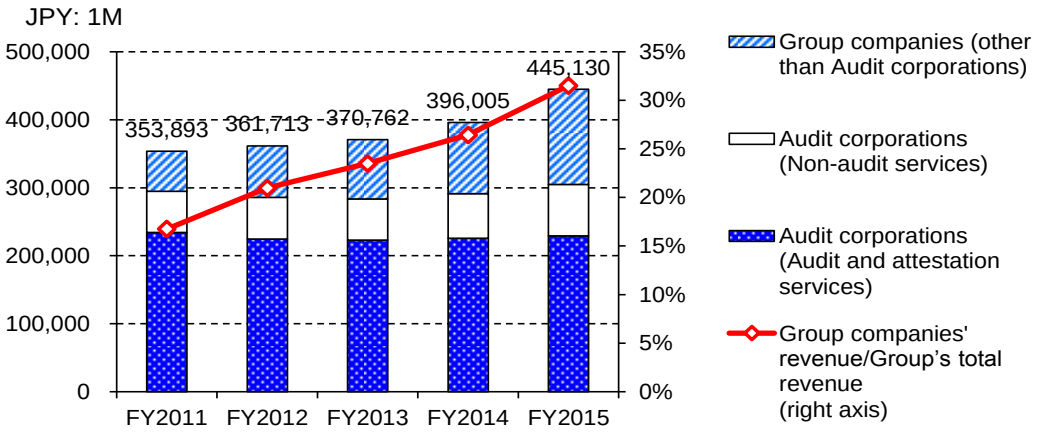
The changes in operating revenue of the entire audit corporation groups and the percentage of operating revenue from corporations other than audit corporations to the operating revenue of the entire audit corporation groups are shown below. Since most small and medium-sized audit corporations do not belong to audit corporation groups, we describe only major audit corporations and quasi-major audit corporations.

In major audit corporation groups, operating revenue from corporations other than audit corporations has been increasing. The percentage of operating revenue from corporations other than audit corporations to the operating revenue of the entire audit corporation groups has also been growing sharply. Meanwhile, in quasi-major audit corporation groups, operating revenue from audit corporations account for the most part of the operating revenue of the entire audit corporation groups. There is a significant difference in the constitution of a group between major audit corporations and quasi-major audit corporations. (Fig. II-3)

[3] Several audit corporations belong to the same international audit network firms. In such case, we treat them as different audit corporation groups.

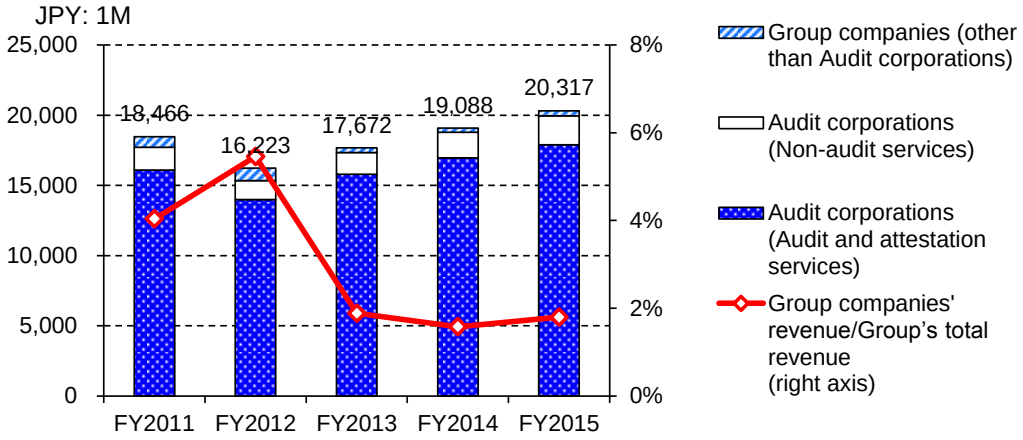
Fig. II-3 Changes in operating revenue of the entire audit corporation groups and the percentage of operating revenue from corporations other than audit corporations to the operating revenue of the entire audit corporation groups

Major audit corporations (total of four corporations)



(Note) Operating revenue of audit corporation groups does not include operating revenue of tax corporations.

Quasi-major audit corporations (total of six audit corporations)



(Note) In FY2012, one audit corporation accounted for operating revenue for only three months due to the change of fiscal year end.

(Source) CPAAOB (Operating revenues of each audit corporation group for the above fiscal years are added up.)

4. Overview of Alliance with International Audit Networks

Major audit corporations, quasi-major audit corporations, and some small and medium-sized audit corporations belong to international audit networks and are network firms that constitute networks in order to effectively perform audits of entities that have branches and overseas subsidiaries and receive know-how, such as audit manuals from the networks.

(1) Overview of Belonging to International Audit Networks

The status of audit corporations that belong to international audit networks by size is shown below. All of the major audit corporations and quasi-major audit corporations belong to international audit networks. Meanwhile, a number of small and medium-sized audit corporations have also joined international audit networks. (Fig. II-4-1, Fig. II-4-2)

Fig. II-4-1 Status of audit corporations that belong to international audit networks[4]

Number of audit corporations

Major audit corporations	4
Quasi-major audit corporations	6
Small and medium-sized audit corporations	23
Total	33

(Source) CPAAOB (Status of alliances formed by each audit corporation surveyed for FY2014)

Fig. II-4-2 List of international audit networks to which major audit corporations and quasi-major audit corporations belong

Audit corporation	International audit network
Deloitte Touche Tohmatsu LLC	Deloitte Touche Tohmatsu Limited
Ernst & Young ShinNihon LLC	Ernst & Young Global Limited
KPMG AZSA LLC	KPMG International Cooperative
PricewaterhouseCoopers Aarata LLC	PricewaterhouseCoopers International Limited
BDO Sanyu & Co.	BDO International Limited
BDO Toyo & Co.	BDO International Limited

[4] Small and medium-sized audit corporations that form collaborative alliances with overseas audit corporations are included in small and medium-sized audit corporations.

Audit corporation	International audit network
Grant Thornton Taiyo LLC	Grant Thornton International Limited
GYOSEI & CO.	Nexia International Limited
PricewaterhouseCoopers Kyoto	PricewaterhouseCoopers International Limited
YUSEI Audit & Co.	Crowe Horwath International

(Source) Compiled from publicly disclosed materials as of the end of June 2016

(2) Relationships with International Audit Networks

While network firms that constitute international audit networks can use the networks' logos and names, mutually introduce business, and receive know-how, they are responsible for quality controls. The responsibilities and their degree vary depending on the size of the international audit networks. In general, the bigger the size of the international audit network, the bigger the impact that the network has on its members.

Major audit corporations have independently belonged to four major international audit networks and have established close relationships. Specifically, they not only have the right to use the networks' logos and names, but are also involved in the operation of the networks, for instance, their chief executive officers are members of the important committees of the networks.

Major audit corporations have also received audit manuals and audit tools based on the manuals from the international audit networks. They have performed audits in accordance with the audit manuals based on the networks' standards. Moreover, they have implemented standards and procedures set by the networks for rules related to other quality controls, such as engagement quality control reviews and independence.

Major audit corporations have regularly received the global reviews of the international audit networks to maintain the quality of audit at the level required by the networks, mainly for individual audit engagements. Some audit corporations regard the global reviews as a regular cyclical inspection of engagements or part of it.

All quasi-major audit corporations belong to international audit networks. However, the degree of alliance significantly varies depending on the size of the networks.

Some have formed alliances with international audit networks at the same level as major audit corporations, but others have formed a moderate alliance in which they only have the right to use the networks' logos and names, receive introduction of audit engagements in each country, and do not receive audit manuals. Although all audit

corporations have received global reviews of the international audit networks, their frequency and contents vary greatly.

International audit networks to which small and medium-sized audit corporations belong only allow their members to use their logos and names, and to be introduced to audit engagements in network firms' countries. Many of them do not provide audit manuals or perform global reviews.

5. Forms of Engagement Quality Control Review

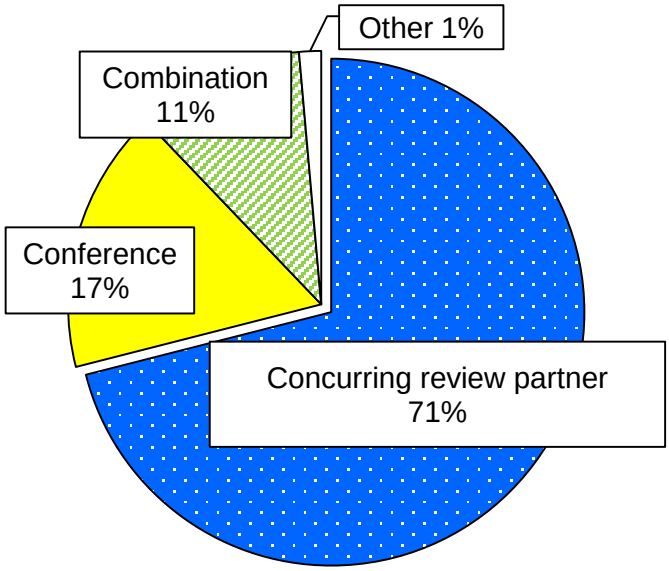
There are three forms of engagement quality control review by audit corporations: i) the concurring review partner form—a review is performed by a partner other than the engagement partner; ii) the conference form—a review is performed under the council system; and iii) the combination form—a review is performed by a concurring review partner, and any important matters in expressing audit opinions, which are clarified in advance, are discussed and reviewed at the council. The forms of review are shown below. (Fig. II-5)

In the past, many major audit corporations performed reviews with the conference method. However, currently, many of them have conducted reviews by the combination form.

Many quasi-major audit corporations adopt the combination form just like major audit corporations.

Many small and medium-sized audit corporations adopt the concurring review partner form, but not a few audit corporations perform reviews by the conference form. In addition, if there are disagreements between the engagement team and an engagement quality control reviewer even in a case where the concurring review partner form is adopted, many audit corporations perform the reviews at the Partners' Meeting if they consider it necessary. However, the matters to be discussed during such reviews at the Partners' Meeting vary depending on audit corporations.

Fig. II-5 Forms of Review (FY2014)



(Source) CPAAOB (The situation of each audit corporation surveyed for FY2014)

III. Overview of Audit

1. Overview of Entities

Audit and attestation services by audit firms are mainly statutory audits in accordance with the FIEA or the Companies Act.

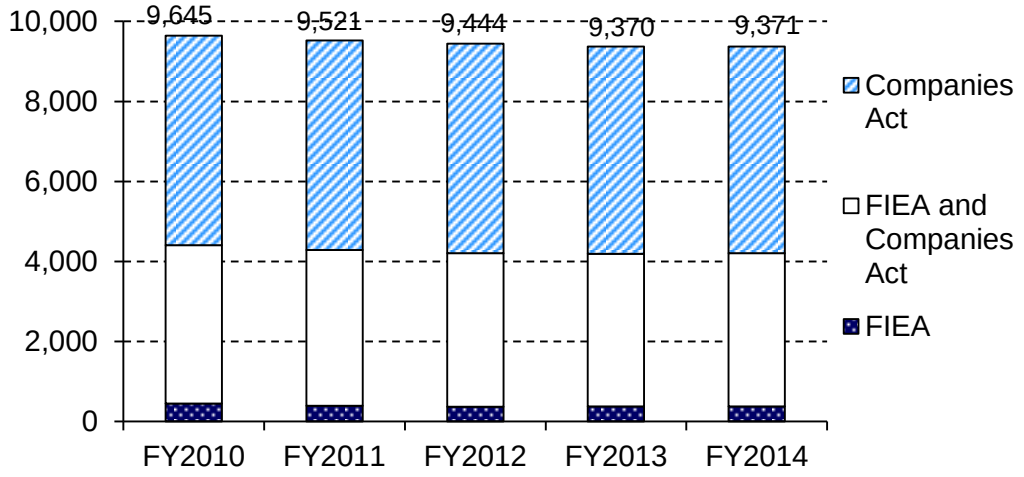
The change in the number of entities that are audited for FIEA or the Companies Act purposes and the number and market capitalization of listed entities (as of the end of March 2016) by the size of audit firms are shown below.

Although the number of the entities that are audited under FIEA or the Companies Act has not changed greatly, the number has been slightly diminishing. (Fig. III-1-1)

Major audit corporations have audited 73% of listed entities. Particularly, since the audit of large entities tends to be performed by major audit corporations, the proportion of the market capitalization of listed entities audited by major audit corporations is more than 90% of the total market capitalization of listed entities. (Fig. III-1-2, III-1-3)

Moreover, 67% of listed entities have a fiscal year ending March. Since the proportion of the market capitalization of such entities is approximately 80% of the total market capitalization of all listed entities, audit engagements are concentrated in a particular period. (Fig. III-1-4, III-1-5)

Fig. III-1-1 Change in the number of entities that are audited for the purposes of the FIEA or Companies Act



(Source) CPAAOB (The number of the entities audited by each audit corporation for the above fiscal years is calculated.

Fig. III-1-2 Number of audited listed entities by the size of audit firms

Number of audited listed entities

Major audit corporation	2,656
Quasi-major audit corporation	397
Small and medium-sized audit firms	577
Total	3,630

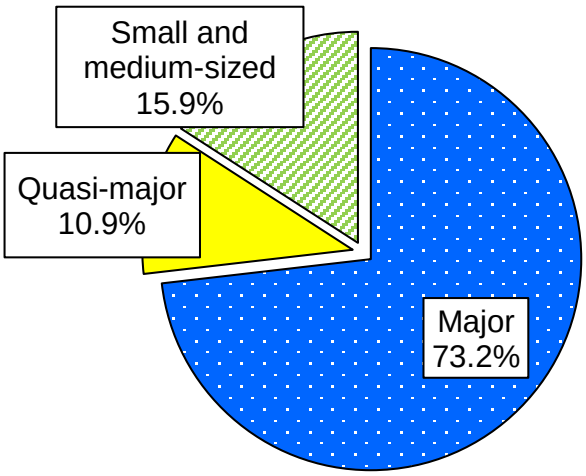


Fig. III-1-3 Market capitalization of listed entities by size of audit firms

JPY: 1M

Major audit corporation	484,655,522
Quasi-major audit corporation	25,563,182
Small and medium-sized audit firms	19,948,289
Total	530,166,993

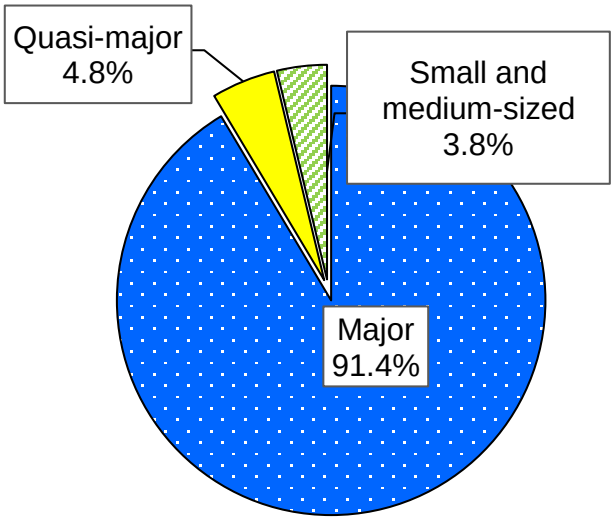


Fig. III-1-4 Number of audited listed entities by fiscal-year-end

	Number of audited listed entities
FY ended Mar.	2,444
FY ended Dec.	376
FY ended Feb.	202
Other	608
Total	3,630

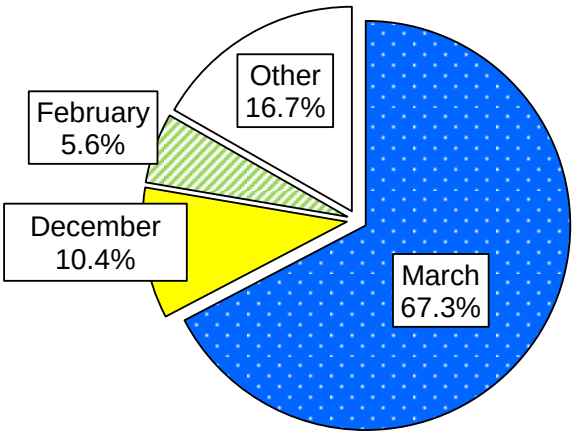
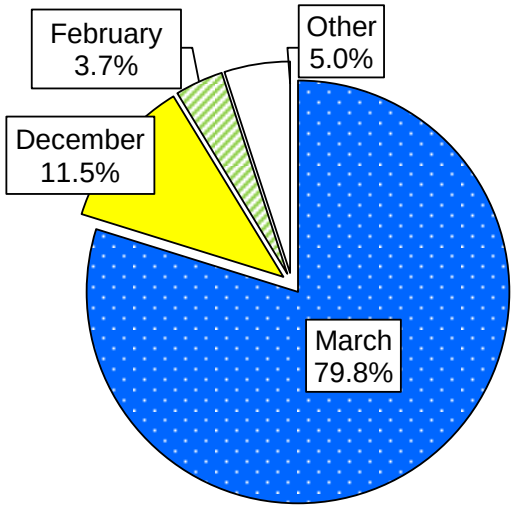


Fig. III-1-5 Market capitalization of listed entities by fiscal-year-end

	JPY：1M
FY ended Mar.	423,074,061
FY ended Dec.	60,922,594
FY ended Feb.	19,534,581
Other	26,635,756
Total	530,166,993



(Source) Based on the materials released by the stock exchanges as of the end of March 2016.

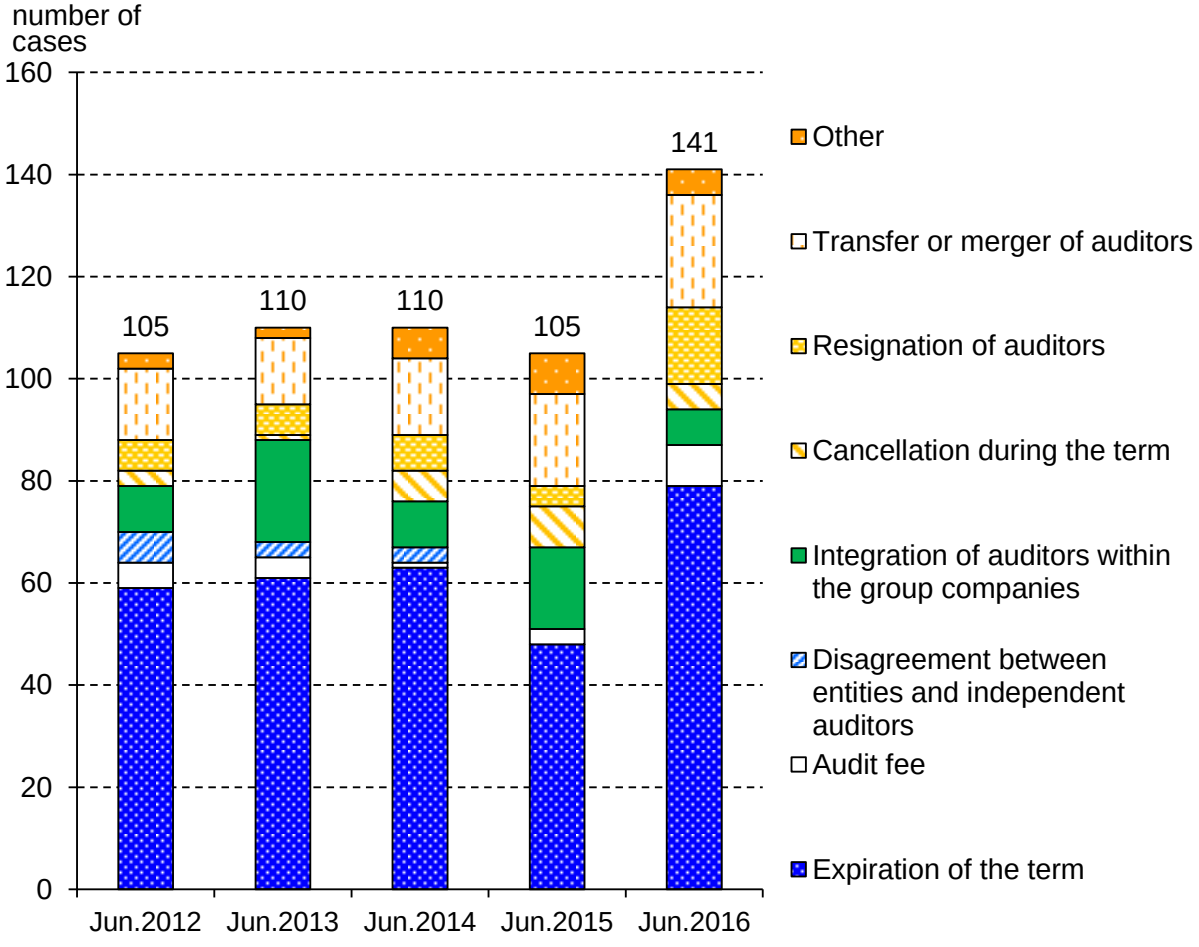
2. Overview of Replacement of Independent Auditors

The change in the reasons for replacement of independent auditors by listed companies, the transfer of independent auditors by the size of audit firms, and the audit fees following the replacement of independent auditors are shown below.

According to timely disclosure, the expiration of the term comes on the top of the list of the reasons for replacement of independent auditors. The integration of independent auditors among the group companies is also on the list. In June 2016, replacement resulting from the resignation of independent auditors increased. (Fig. III-2-1)

Regarding the net increase or decrease in the transfer of independent auditors, major audit corporations, and small and medium-sized audit firms, had been replaced by quasi-major audit corporations. However, in June 2016, major audit corporations showed a net decrease, while small and medium-sized audit firms showed a net increase. (Fig. III-2-2)

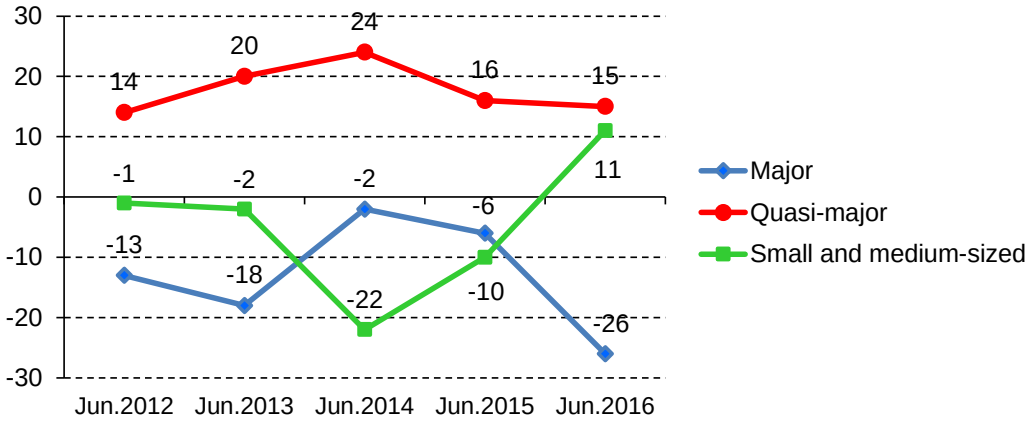
Fig. III-2-1 Change in the reasons for replacement of independent auditors by listed companies



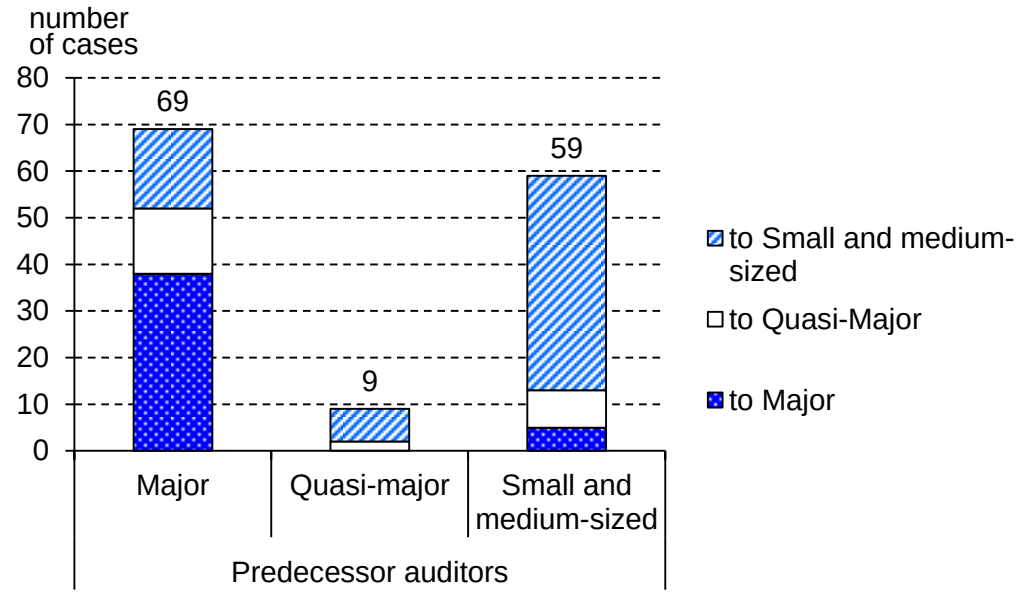
(Source) Timely disclosure on the replacement of independent auditors

Fig. III-2-2 Transfer of independent auditors by the size of audit firms

(Net increase or decrease by the size of audit firms)



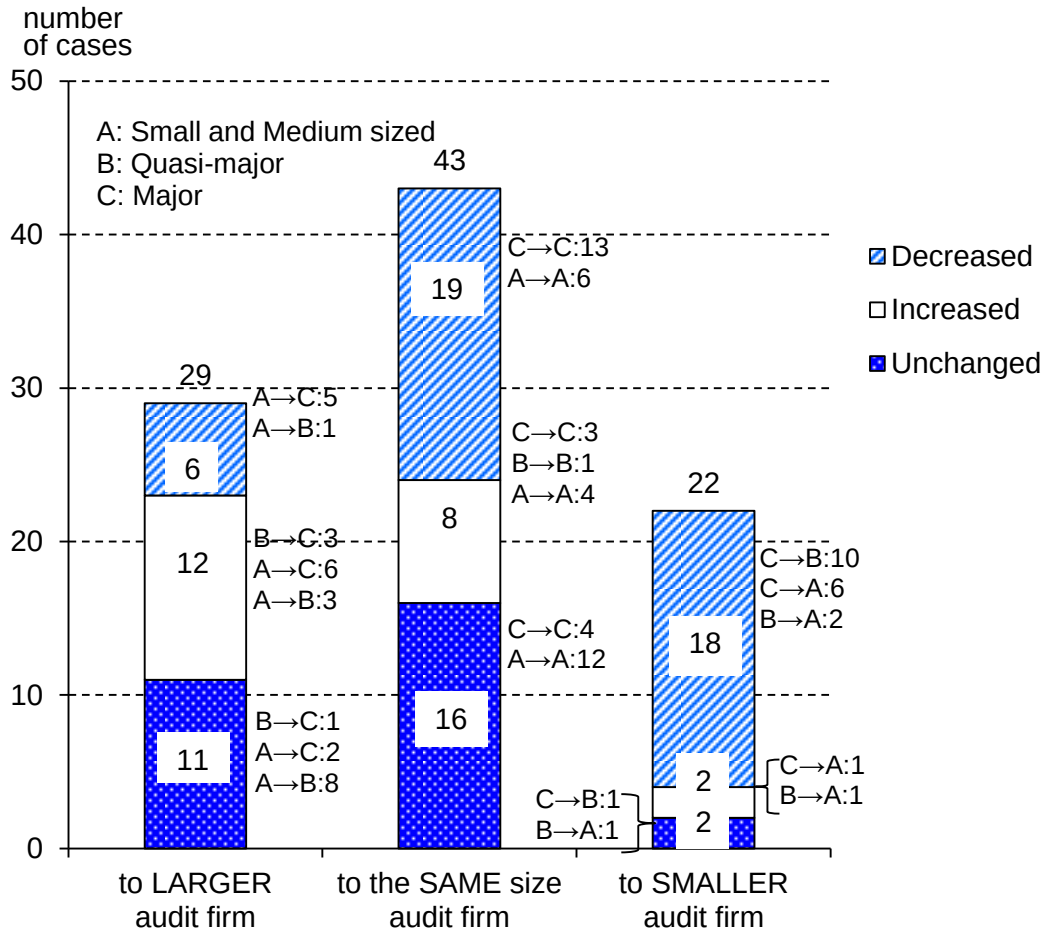
(Transfer among audit firms [FY June 2016])



(Source) Timely disclosure on the replacement of independent auditors

Regarding the increase or decrease in audit fees following the replacement of independent auditors, there were many instances in which fees were not changed or increased upon replacement with larger audit firms. Moreover, in half of the cases, fees decreased upon replacement with audit firms that are the same size as the predecessors. Meanwhile, in almost all cases, fees decreased upon replacement with smaller audit firms. (Fig. III-2-3)

Fig. III-2-3 Change in audit fees following the replacement of independent auditors



(Source) Timely disclosure on the replacement of independent auditors
(Note 1) Calculated audit fees following the replacement of independent auditors of listed entities that are publicly disclosed for the year from January 31 to December 31, 2014. A change of one million yen or more in fees is regarded as an increase or decrease.
(Note 2) The breakdown of changes is shown in graph form.

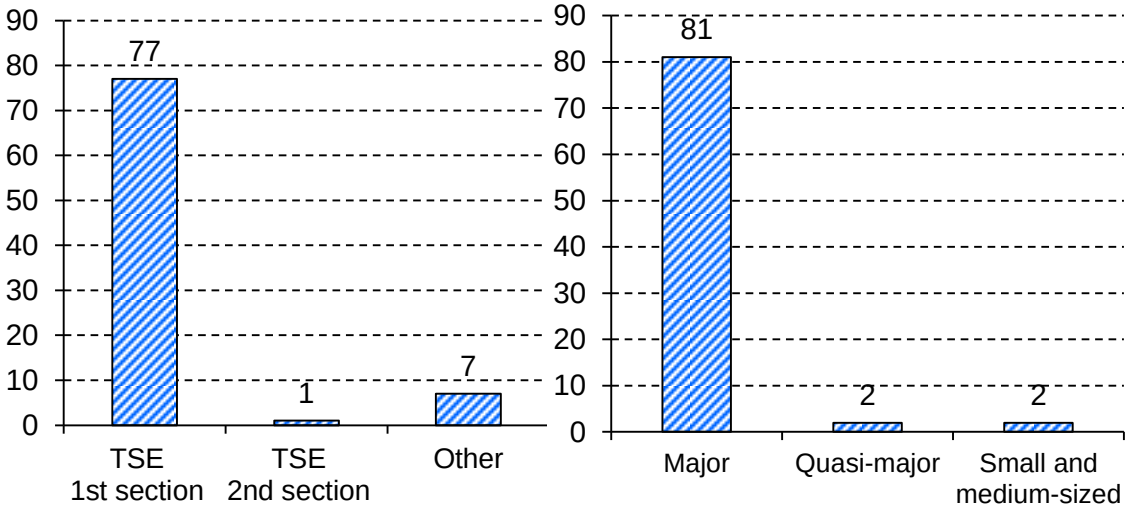
3. Overview of Audit Related to Various Systems

(1) Overview of Audits for Entities that adopt IFRS

Most of the entities that adopt IFRS are listed on the first section of the Tokyo Stock Exchange and the majority of their independent auditors are major audit corporations. The situation is the same for entities that plan to adopt IFRS. (Fig. III-3-1, Fig. III-3-2)

Fig. III-3-1 Entities that adopt IFRS

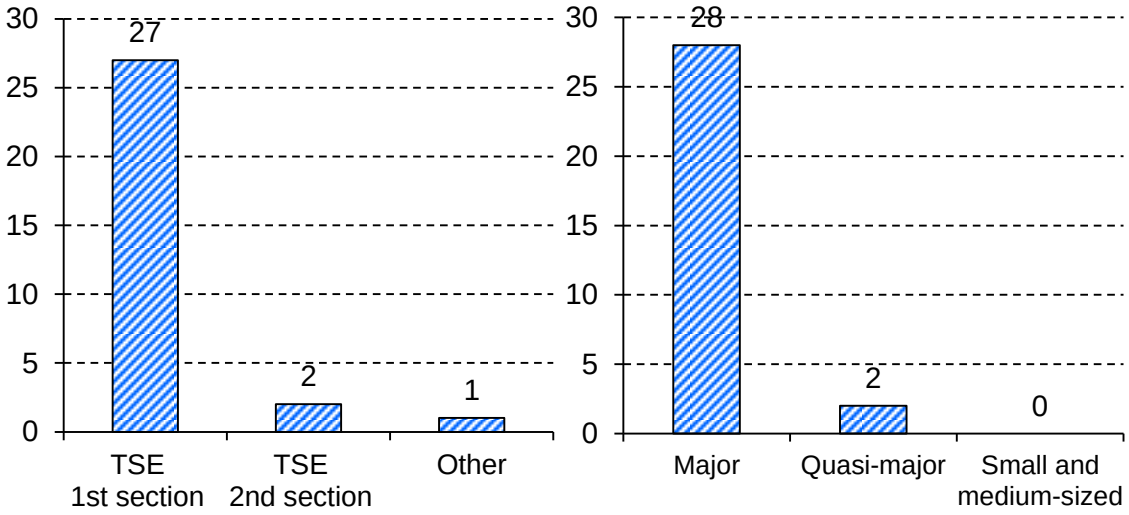
(Situation by market) (Situation by size of independent auditors)



(Source) Based on the materials released by the stock exchanges as of the end of June 2016

Fig. III-3-2 Entities that plan to adopt IFRS

(Situation by market) (Situation by size of independent auditors)



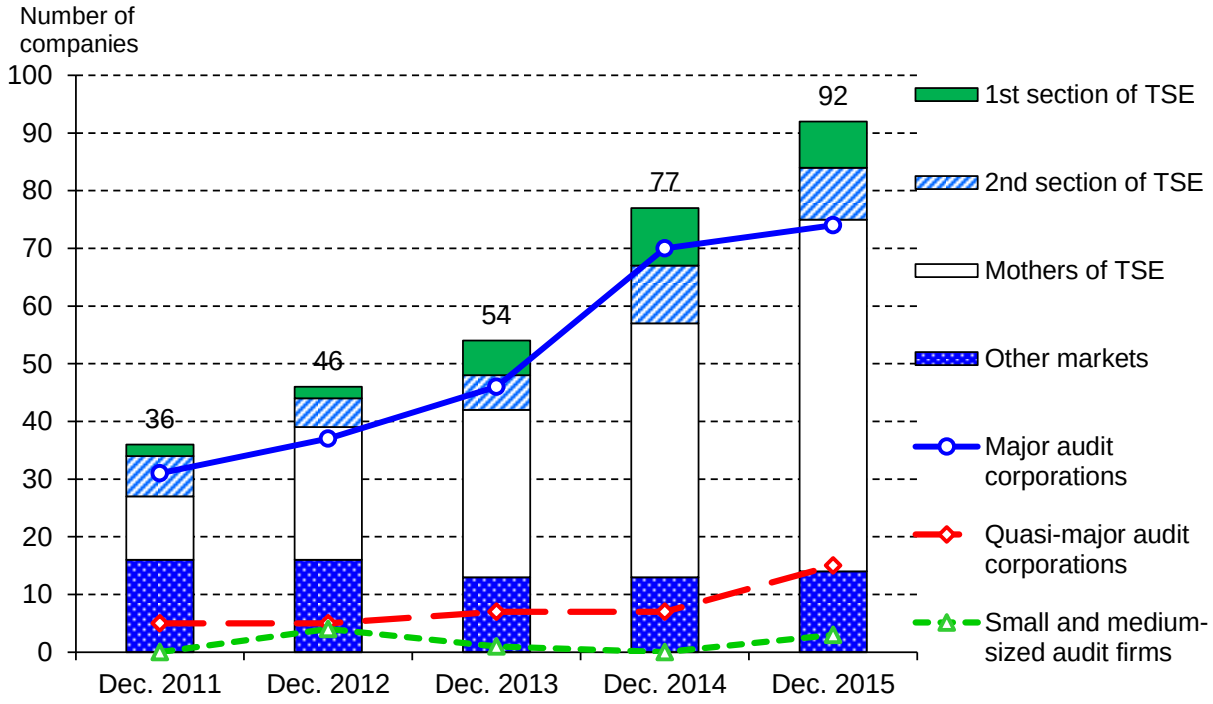
(Source) Based on the materials released by the stock exchanges as of the end of June 2016

(2) Overview of Audit Engagements for Initial Public Offering

The number of initial public offerings has been increasing over the most recent five years. Particularly, the number of companies listed on the Mothers has grown substantially.

Regarding the change in the size of audit firms at initial public offering, most of them have been major audit corporations. However, the number of quasi-major audit corporations increased for the year ended December 31, 2015. (Fig. III-3-3)

Fig. III-3-3 Changes in the number of initial public offerings and the size of their audit firms



(Source) Based on the materials released by the stock exchanges