IV. Responses to Changes in the Global Environment Surrounding Audits

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A. Trends surrounding small and medium-sized audit firms

1. Changes in the environment surrounding audits by small and medium-sized audit firms

In recent years, there has been a continuing trend of changing accounting auditors for audits of listed domestic companies from large-sized audit firms to mid-tier/small and medium-sized audit firms. As of the end of June 2023, the number of listed companies audited by small and medium-sized audit firms had increased by a net 92, indicating that the role of small and medium-sized audit firms as auditors of listed domestic companies is increasing.

In addition, quality control standards were revised to require the introduction of a quality control system based on a risk-based approach in order to maintain and improve audit quality. In order to strengthen independence, the Code of Ethics was also revised, and regulations on remuneration dependence on specific companies (15% rule)[17] and prohibition of providing non-assurance services that may cause self-reviews were introduced.

In light of these changes in the environment surrounding accounting audits, in order to ensure the reliability of accounting audits, discussions in the Advisory Council on the Systems of Accounting and Auditing highlighted the importance of supporting small and medium-sized audit firms that are working to improve their audit quality so as to broaden the base of audit service providers. They also highlighted the need to consider institutional frameworks that require a high degree of discipline in audits of listed companies and promotion of acceptance of the Audit Firm Governance Code. Among the issues highlighted, issues related to the CPA system were discussed by the Certified Public Accountant System Subcommittee of the Financial System Council, and a report, which includes the introduction of a legal registration system for audits of listed companies and system development for audit firms of listed companies through acceptance of the Audit Firm Governance Code, was published.

A bill to partially revise the Certified Public Accountants Act was submitted to the Diet on March 1, 2022, and was promulgated on May 18, 2021. In addition, the Order for Enforcement of the CPA Act and the Ordinance for Enforcement of the CPA Act were revised and promulgated on January 25, 2023 as a system development necessary for the enforcement of the revised CPA Act.

As a result of the above amendments to the CPA Act, audit firms that audit listed companies are required to accept the Audit Firm Governance Code. Therefore, in October 2022, the Expert Committee on the Audit Firm Governance Code was reopened, and the Code was revised to require effective disciplines suited to the scales and characteristics of audit firms, and was published on March 24, 2023.

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[17] A rule concerning audits of business entities with a high degree of social impact (PIEs) that stipulates that if the degree of dependence on fees (the proportion of fees received from a particular company to the total income of the audit firm) exceeds 15% for two consecutive years, the auditor must disclose this fact, and if the degree of dependence on fees exceeds 15% for five consecutive years, the auditor must in principle resign.

2. Response by the JICPA to small and medium-sized audit firms

In response to 1. above, the JICPA is responding to changes in the environment surrounding audits of small and medium-sized audit firms from three perspectives: (i) confirmation of eligibility through quality control reviews following the introduction of the legal registration system for auditors of listed companies, (ii) enhancement of information disclosure by small and medium-sized audit firms, and (iii) support for strengthening the foundations of small and medium-sized audit firms. In particular, through (ii) and (iii), the JICPA is accelerating efforts to strengthen the management fundamentals of small and medium-sized audit firms, which will lead to improvements in audit quality.

a Confirmation of eligibility through quality control reviews in connection with the introduction of the legal registration system for auditors of listed companies, etc.

In accordance with the revision of the CPA Act, the JICPA is required to conduct quality control reviews to confirm whether the operational control systems of registered auditors are in compliance with laws and regulations, etc. for conducting audits of listed companies, etc. fairly and appropriately (hereinafter referred to as "confirmation of eligibility"). This confirmation of eligibility is to confirm the status of the development of systems set forth in Articles 87 and 93 through 96 of the Ordinance for Enforcement. For example, with regard to the obligation set forth in Article 93 of the Ordinance to evaluate the status of business quality control and to develop a system to publish the results of the evaluation, the JICPA considers that (I) if it has not been published, or (ii) if the published matters significantly differ from the actual situation of registered auditors, it is a breach of legal obligations, and decides whether to revoke the registration. The JICPA uses quality control reviews as a method of "confirmation of eligibility." Quality control reviews are now expected to play an important role and responsibility in determining whether a firm can be registered to conduct audits of listed companies and the status of the development of operational control systems. Therefore, quality control reviews are required to verify the effectiveness of audit firms' quality control systems, including their governance systems, needs to be verified more rigorously and in depth.
Registration of audit firms, etc. that conduct audits of listed companies had been carried out by the Quality Control Committee, which had been responsible for the review system. On April 1, 2023, the Quality Control Oversight Board was established. The board is comprised of a total of seven members, three of which are members of the JICPA and four of which are non-members. The board specializes in screening registrations of audit firms, etc. that conduct audits of listed companies. From now on, further transparency and objectivity will be given to screening of registrations on the list of listed company auditors and decisions on cancellation of registrations.

b Enhancement of information disclosure by small and medium-sized audit firms

Audit firms that conduct audits of listed companies, etc. are now required to comply with Article 93 (Evaluation and Publication of Status of Quality Control of Services, etc.), Article 95

(Publication of Status of Business Management, etc.), and Article 96 (Organizational Operation) of the amended Ordinance for Enforcement of the CPA Act. In line with this, the JICPA has decided to enhance information disclosure by audit firms through letting them prepare "Annual Report on Audit Quality Management" (hereinafter referred to as the "Annual Report"). The Annual Report is prepared and published under self-regulations separately from the "Explanatory Documents" required under the CPA Act, and the content thereof is in principle at the discretion of each audit firm.

The JICPA believes that the preparation and publication of annual reports is meaningful in that small and medium-sized audit firms voluntarily disclose information relating to six fundamentals (quality control, organization and governance, human resources, IT/digital, finance, and international matters), and market participants are expected to deepen their understanding of audit firms through annual reports. In addition, the JICPA believes that information disclosure from the perspective of capital markets will have small and medium-sized audit firms work harder than ever to improve their audit quality, leading to further improvements in quality control systems. The JICPA has established the Practices Policy Committee for Small and Medium-sized Audit Firms and the Small and Medium-sized Audit Firms Liaison Council, and is implementing various support measures to achieve these goals.

c Support for strengthening the fundamentals of small and medium-sized audit firms

The JICPA accelerate efforts to strengthen the business fundamentals of small and medium-sized audit firms and improve audit quality through enhancement of information disclosure and various support measures. These efforts are led by the Practices Policy Committee for Small and Medium-Sized Audit Firms and the Small and Medium-Sized Audit Firms Liaison Council, and represented as follows.

- Publication of guidance for revised Quality Control Standards
  For QCSCS, Practical Guidance No.3 (Q&A on Quality Control and Engagement Quality Control Reviews for Audit Firms and Audit Engagements) and Practical Guidance No.4 (Tools for Quality Control at Audit Firms) were published.
- Training for Compliance with the revised Code of Ethics
- Opinion Exchange Meeting with Capital Market Participants
- Support for recruitment and training of small and medium-sized audit firms
- Maintenance of overseas office directory
- Interactive training for small and medium-sized audit firms
  In order to foster and support small and medium-sized audit firms and strengthen the individual consultation function, former reviewers of quality control reviews serve as lecturers, and opinions and information are exchanged and shared through Q&As and discussions with the participation of a small number of firms.
- Support for digitalization of small and medium-sized audit firms

Identifying the state of IT infrastructure development and the use of IT-based audit methods at small and medium-sized audit firms. Providing support for the development of IT infrastructure, including cybersecurity measures, and the development of IT-based audit tools. Specific digitalization support measures include the establishment of a shared IT infrastructure environment (support for the creation of a platform for use by small and medium-sized audit firms of an electronic audit documentation system) and hosting of IT communities (networking among IT personnel at small and medium-sized audit firms).

- Holding regular meetings to exchange opinions with small and medium-sized audit firms, etc.

3. Response by the CPAAOB

The revised Quality Control Standards, as "Points to Note Regarding Implementation of the Revised Quality Control Standards," state that it is particularly important for small and medium-sized audit firms to be provided with necessary support from a medium - to long-term perspective, and that the administrative authority should strive to ensure proactive quality control by audit firms through inspections by the CPAAOB, while supporting the efforts of the JICPA. The CPAAOB is making efforts to place greater emphasis on inspections to small and medium-sized audit firms based on the Basic Policy for Monitoring Audit Firms for the 7thTerm.

B. Recent Trends with Auditing

1. Trends in international auditing standards and ethical standards

The International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA), both established within the International Federation of Accountants (IFAC), are engaged in the development of international auditing standards and ethics standards. Recent major revisions to the International Standards on Auditing (ISA) established by the IAASB include the revision of "Quality Management for an Audit of Financial Statements " (ISA220) and the revision of "Quality Control for Firms that perform audits and reviews of financial statements, and other assurance and related engagements " (ISQC1) to "International Standard on Quality Management 1" (ISQM1) and "International Standard on Quality Management 2" (ISQM2). ISQM1 was adopted on December 15, 2022, and ISQM2 and ISA220 were adopted on audits for fiscal years beginning on or after December 15, 2022. In addition to the development of assurance standards for sustainability reporting, the Board is currently considering revisions to "Fraud" (ISA240) and "Going Concern" (ISA570), which are scheduled for finalization in March 2025 and December 2024, respectively. Revisions to audit evidence (ISA500) are scheduled for finalization in June 2024. The revisions to ISA500 reflect changes in the sources, volume, and diversity of information available to audited companies and auditors as a result of advances in technology.

Recent revisions to the IESBA Code of Ethics include a revision related to "Objectivity of Engagement Quality Reviewer and Other Appropriate Reviewers" in January 2021 in response to the ISQM2, which newly added provisions related to the objectivity of EQC reviewers, etc., a revision related to non-assurance service provisions of the Code in April 2021 in order to strengthen the independence of auditors and prohibit the provision of non-assurance activities to audited companies, and a revision related to fee-related provisions of the Code in April 2021 in order to strengthen the independence of auditors and improve transparency of information related to compensation. In addition, the IESBA published "Revisions to the Definitions of Listed Entity and Public Interest Entity in the Code " in April 2022, which requires the local bodies responsible for the adoption of the Code to consider the definition of PIEs in light of the circumstances of each jurisdiction beginning with audits for financial years beginning on or after December 15, 2024 (early adoption possible). In response to the revision of "Special Considerations-Audits of Group Financial Statements (including the Work of Component Auditors) " (ISA600), the IESBA published a revision to strengthen and clarify independence applicable to communication regarding independence among individuals ,firms involved in group audits, group auditors and component auditors.

2. Revision of the Code of Ethics by JICPA

Referring to revisions made to the IESBA Code of Ethics, the JICPA amended its Code of Ethics in July 2022 by integrating the original Code of Ethics with three sets of guidelines on Independence, Conflicts of Interest, and Non-Compliance, as well as by adding and modifying a number of individual rules.

Major additions and modifications to individual rules include matters related to compensation and non-assurance activities.

In response to the revision of the Code of Ethics, audit firms are required to disclose information related to audit fees (audit fees, non-audit fees, and fee dependency) when the client of an audit engagement is a business entity with a high degree of social impact ("PIE").The Cabinet Office Ordinance on Audit Certification of Financial Statements, etc. ("Audit Certification Ordinance") was also revised to require audit firms to add matters concerning the fees that CPAs or audit firms (including those who belong to the same network as these firms) receive from audited companies (including consolidated subsidiaries and non-consolidated subsidiaries) as descriptions in audit reports. In principle, the revised Audit Certification Ordinance shall be applied to audit certification of financial statements, etc. for business years, etc. starting on or after April 1, 2023.

In addition, the code of ethics regulation in cases where a firm's fees are highly dependent on the client for certain audit engagements was strengthened.

For example, in cases where the firm's fee dependence on PIEs exceeds or is likely to exceed 15% for two consecutive years, post-audit opinion review, which was previously allowed.is not allowed, and pre-audit opinion review and disclosure of fee dependency are mandatory. Also, in cases where the firm's fee dependence on PIEs continues to exceed or is likely to exceed 15% for five consecutive years, the firm is required to resign after the fifth annual opinion.

For non-assurance engagements, if the client of the audit engagement is a PIE, the audit firm or network firm must not provide non-assurance engagements that could be subject to self-review as a disincentive (prior to the revision, provision of non-assurance engagements was allowed according to materiality determinations and applicable safeguards). And the content of communications from audit firms to company auditors has been enhanced so that prior approval from company auditors for providing non-assurance service is required.

3. Other trends in financial reporting systems

a Changes in quarterly disclosure system

The quarterly reporting system was legislated in June 2006. However, in recent years, economic and social conditions have changed significantly, and the demand for reviewing framework of company’s information disclosure is observed. Under these circumstances, the importance of non-financial information related to medium - to long-term corporate value has increased in corporate disclosure. On the other hand, it is pointed out that there are overlaps between quarterly reports based on the FIEA (Quarterly Securities Report) and those based on exchange rules (Quarterly Earnings Report (Tanshin)), and such reports should be reviewed from the viewpoint of cost reduction and efficiency. In light of this, the Disclosure Working Group of the Financial System Council indicated in June 2022 that, in first and third quarters, the quarterly reports would be consolidated into a single quarterly report. The Group Report in December 2022 put together the following recommendations concerning specific consolidation of quarterly reports.

- For the time being, quarterly earnings reports will be made mandatory across the board. Going forward, making them voluntary will be continuously under consideration from a wide range of perspectives while monitoring the progress made in enhancing timely disclosure.
- With respect to the content of disclosure, matters for which investors' requests are particularly strong (segment information, cash flow information, etc.) shall be added based on the matters disclosed in the quarterly financial results.
- Auditor reviews will be at the companies' discretion and will be required for a certain period of time in the event of accounting irregularities or internal control deficiencies.
- Deliberate and malicious misstatements, such as those aimed at market fluctuations, may be subject to penalties under the FIEA.
- For listed companies, the interim report will require the same level of content and review by auditors as the current second quarter report.
- The period for public inspection of interim reports under the FIEA will be extended to five years.

Among these proposals, the FSA submitted to the Diet in March 2023 a bill to partially amend the FIEA and other related laws to address matters that require amendments to the FIEA. The bill is under review as of the end of June.

b Internal Control Reporting System

More than 15 years have passed since the internal control reporting system was introduced in 2008, and it is believed that this system has had some effect in improving the reliability of corporate financial reporting. On the other hand, there have been some cases in which material deficiencies that should be disclosed outside the scope of management's assessment of internal controls have become clear, and in which sufficient reasons were not disclosed when the evaluation of the effectiveness of internal controls was corrected. There are concerns about the effectiveness of the internal control reporting system, such as whether management has not appropriately considered the importance of the impact on the reliability of financial reporting when examining the scope of evaluation of internal controls.

In addition, in its Issues Paper published in November 2021, the Advising Council on the Systems of Accounting and Auditing stated that from the perspective of developing an environment for conducting high-quality accounting audits, it was necessary to analyze the design and operation of internal controls with regard to the internal control reporting system, and to promote discussions toward improving the effectiveness of internal controls as necessary, while taking into account the progress of international discussions on internal controls and risk management, such as the revision of the report on the basic framework of internal controls by the COSO (Committee of Sponsoring Organizations of the Tredway

Commission) in the United States.

Against this background, the Internal Control Standard Committee of the Business Accounting Council published "Revision of Standards and Practice Standards for Management Assessment and Audit concerning Internal Control Over Financial Reporting (Council Opinion)f" in April 2023.

As for the main points of revision, for example, regarding the basic framework of internal controls, based on the revision of the COSO Report, the importance of considering fraud risk when evaluating risks and matters to be considered have been clarified, and the growing importance of controls related to outsourced IT services has been described. Regarding the evaluation and reporting of internal controls over financial reporting, the revised Standard indicates that the following indicators should not be automatically applied when management determines the scope of assessment of internal controls: "approximately 2/3 of sales, etc." and "three accounts of sales, accounts receivable, and inventories," which are exemplified; it is appropriate to describe in the internal control report the reasons for judgment regarding the scope of assessment of internal controls by management; and regarding the audit of internal controls over financial reporting, the revised Standard indicates that it is important to utilize audit evidence obtained in the process of auditing financial statements and to have appropriate discussions with management in order to conduct an effective internal control audit.

In light of the above revisions, the "Cabinet Office Ordinance Partially Amending the Cabinet Office Ordinance on the System for Ensuring the Appropriateness of Documents on Financial Calculation and Other Information" was published in June 2023. The ordinance adds new matters to be included in the internal control report, etc. as follows:

Internal control report: If a material deficiency that should be disclosed was reported in the previous fiscal year, describe the status of corrective measures to the material deficiency as a supplementary note in the internal control report.

Corrected internal control report: When the assessment of the effectiveness of internal controls is subsequently corrected, the specific background and reason for the correction shall be included in the corrected internal control report.

Internal control audit report: If the company states that internal controls are not effective as a result of evaluating internal controls in the internal control report, the auditor includes this fact in the auditor's opinion in the internal control audit report.

In addition, the following issues were raised during deliberations by the Internal Control Standard Committee and will be addressed as medium - to long-term issues.

- The treatment of non-financial information such as sustainability in the internal control reporting system should be considered based on domestic and overseas discussions.
- Whether or not to adopt direct reporting should be discussed in light of the nature of internal control audits.

- With regard to enhancing the disclosure of the internal control audit report, whether or not to adopt, for example, "Key Audit Matters" related to internal controls should be considered in light of progress in disclosure in the internal control report.
- The audit of the corrected internal control report is currently not required. However, the way how the auditor is involved should be considered.
- Administrative monetary penalty and penal provisions should be reviewed in order to clarify the responsibility of management and to deal with management override of internal controls.
- Alignment between the FIEA and the Companies act, such as stipulating obligations to build internal control in Companies Act, is necessary. In the future, stipulations regarding internal control of the Companies Act and the FIEA should be integrated so that comprehensive judgments can be made covering the four objectives of internal controls.
- In the written confirmation by the company representative concerning the appropriateness of the content of the securities report, it may be appropriate to consider enhancing the content of statements related to internal controls.
- If the FIEA aims to promote extraordinary disclosure instead of periodic disclosure, we should be conscious of internal control even for extraordinary reports.

C. Trends in Sustainability Disclosure and Assurance

1. Trends in sustainability disclosure

In recent years, emphasis has been placed on sustainability in corporate management and investors' investment decisions, and non-financial information related to medium - to long-term corporate value has become increasingly important. On January 31, 2023, the FSA announced revisions to its Cabinet Office Ordinance on Disclosure of Corporate Affairs, etc., which will result in the following new disclosures and enhanced disclosures regarding corporate information prior to the "Status of Accounting" in securities reports and registration statements for the fiscal years ending on or after March 31, 2023.

・A new section titled "Views and Initiatives on Sustainability" has been added to the "Description of Businesses" section. Companies should describe their operations in accordance with four components consistent with international frameworks: "governance," "risk management," "strategy," and "indicators and targets." The terms "governance" and "risk management" are mandatory. Each company should describe "strategy" and "indicators and targets" according to its own assessment of materiality in the framework of "governance" and "risk management."

・As human capital disclosure, the Company shall describe the policy on human resource development including ensuring diversity of human resources, the policy on the internal environment, and the details of indicators related to such policy in "Strategy" and "Indicators and Targets" in the "Description Column" of Sustainability Information. These descriptions are required regardless of their materiality.

Under the Act on Promotion of Women's Participation and Advancement in the Workplace, companies that regularly employ more than 300 workers are required to publish one of eight items, including the ratio of women in managerial positions, and one of seven items, including the ratio of male and female employees taking childcare leave. In addition, from July 2022, companies are required to disclose the gender pay gap from the first fiscal year ending after June 2022. Under the Act on the Welfare of Workers who Take Care of Children or other Family Members including Child Care and Family Care Leave, companies that employ more than 1,000 workers are required to publish the percentage of male employees taking childcare leave from April 2023. Companies falling under this requirement are required to enter the figures for the submitting company and each consolidated subsidiary in "Employees."

・In the "Status of Corporate Governance, etc." section, companies are required to describe the activities of the Board of Directors, the Nomination Committee, the Compensation Committee, etc. (frequency of meetings, specific matters to be discussed, attendance), the effectiveness of internal audits (dual reporting, etc.), and an outline of business alliances with companies issuing cross-shareholdings.

In the above "Views and Initiatives on Sustainability," it was decided that climate change-related measures should be stated when a company judges them to be important, taking into account the business category and management environment, etc. The Disclosure Working Group of the Financial System Council stated that since GHG emissions are an effective indicator that contributes to constructive dialogue between investors and companies, it is expected that companies will actively disclose emissions in Scope1 and Scope2[18] in particular, while judging the materiality.

The mainstream of sustainability disclosure has been voluntary disclosure, such as integrated reports. However, disclosure standards that stipulate specific disclosure content are being discussed in Japan and overseas.

Internationally, the International Sustainability Standards Board (ISSB) finalized Standard S1 (IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information) and Standard S2 (IFRS S2 Climate-related Disclosures) in June 2023. These standards are to be applied from financial years beginning on or after January 2024. In May 2023, ISSB launched a public consultation by issuing a request for information on its priority agenda for future standards development. The request for information listed biodiversity and human capital as candidates for new research and standards-setting projects. ISSB plans to develop a two year work plan, beginning in 2024, based on the results of the request for information. In Europe, the Corporate Sustainability Reporting Directive (CSRD) published in April 2021 was finalized in November 2022, and the European Sustainability Reporting Standard (ESRS), the specific disclosure standard for the CSRD, is under consideration. Non-EU corporate groups with significant net sales in the EU market are

[18] Classification of greenhouse gas emissions by type of emissions. Scope1 means direct emissions by the company itself; Scope 2 means indirect emissions from the use of electricity, heat, or steam supplied by other companies; and Scope 3 means indirect emissions (emissions by other companies related to the company’s activities) other than those in Scope 1 and Scope 2

required to report in accordance with the ESRS or a recognized equivalent third country standard beginning with the 2028 financial year. In the United States, the Securities and Exchange Commission published draft rules in March 2022 mandating climate-related disclosures, which are being considered.

In Japan, the Sustainability Standards Board of Japan (SSBJ) has started development of standards equivalent to ISSB S1 standards (Japanese S1 standards) and S2 standards (Japanese S2 standards). The aim is to publish an exposure draft by the end of March 2024 and finalize it by the end of March 2025. If the target is met, early application will be possible from the fiscal year starting on or after April 1, 2025 at the latest (for companies whose fiscal year ends in March, it will be the fiscal year ending March 2026).

2. Trends in assurance on sustainability disclosures

It is also useful for investors and other stakeholders to set standards for the disclosure of sustainability information so that disclosure of each company has a certain degree of consistency, and increase the reliability of information through assurance by a third party. In recent years, with the background of increasing interest in a sustainable society, financing that proclaims sustainability, such as ESG investment, has increased, while society is paying attention to information dissemination that may cause mislead among stakeholders, such as greenwashing.

Regarding third party assurance on sustainability information, in Europe, a proposal has been made to introduce limited assurance for listed companies with 500 or more employees in fiscal year 2024, for other listed companies (excluding small and medium-sized enterprises) in fiscal year 2025, and for listed small and medium-sized enterprises (excluding micro-enterprises) in fiscal year 2026, along with reporting based on the CSRD, and to shift to reasonable assurance in the future. In the United States, the Securities and Exchange Commission (SEC) has published a draft regulation mandating climate-related disclosures, under which limited guarantees on GHG emissions for Scope1 and Scope2 are required from fiscal year 2024 for large-scale early filing companies and from fiscal year 2025 for early and non-early filing companies, and shift to reasonable assurance after two years is planned.

With regard to assurance standards, the International Auditing and Assurance Standards Board (IAASB) is developing a new comprehensive assurance standards (ISSA 5000) specifically for sustainability assurance, to be finalized by September 2024. This standard will be built on existing standards and guidance, such as the revised ISAE 3000 ("Assurance Engagement Other than Audits or Review of Historical Financial Information "), with a view to making them available to professional accountants as well as parties other than professional accountants. The International Ethics Standards Board for Accountants (IESBA) is also working on developing ethics and independence standards for sustainability reporting and assurance, to be finalized by the end of 2024. These standards will be built on existing ethics rules and will be available to professional accountants as well as parties other than professional accountants.

As for assurance providers, according to a survey of 1350 global companies in 21 jurisdictions, including G20 countries, Hong Kong, and Singapore, conducted through 2021, 43% of assurance providers are not audit firms.

In Japan, due to growing demand from investors for reliability of sustainability information, companies aim to voluntarily obtain assurance. In June 2022, the Disclosure Working Group of the Financial System Council reported that assurance over sustainability information needs to be considered over the medium term for the following reasons:

・The disclosure standards that are the basis for assurance are still under discussion internationally.

・Specific discussions will be held in the future regarding assurance standards for sustainability-related information.

・There are various opinions about appropriate assurance service providers from the viewpoint of knowledge, expertise, independence, etc.

In its December 2022 report, the Group recommended that the scope of assurance to be provided, the providers of guarantees, and the standards and levels of assurance be consistent with international standards.

According to a survey conducted by the Financial Services Agency on assurances for sustainability information provided to Nikkei 225 companies (as of June 2022), 65% of companies obtained assurance, and about half of them are provided assurance services by organizations other than audit firms or audit firm affiliated companies. In addition, when the Financial Services Agency interviewed ISO certification bodies, they commented that, as the demand for third party assurance for sustainability information is expanding, there is a shortage of personnel with the necessary skills and experience, and that if reasonable assurances are required in the future, the shortage of personnel will further expand.

Effective from the year ended March 31, 2022, the revised ASCS 720 clarifies and requires audit firms to take actions regarding their roles in relation to the examination of whether there are material differences among financial statements, the knowledge obtained through the audit process by the auditor and other statements (information other than financial statements and their audit reports).

Audit firms' responses regarding assurance of sustainability information are as follows:

Large-sized audit firms, either by themselves or through their group companies, provide advisory services on sustainability information. They also provide assurance services on sustainability information as accredited assessment bodies of the Japanese Association of Assurance Organizations for Sustainability Information[19]. In addition, they have established departments to promote sustainability information assurance services, collect information in Japan and overseas, disseminate the collected information within the firm, and train staff. Some of them are developing systematic mandatory training programs or establishing a sustainability disclosure assurance

[19] The Japanese Association of Assurance Organizations for Sustainability Information is general incorporated association. Its predecessor, the Japan Environmental Information Review Association was established in 2005 for the purpose of ensuring the reliability of reviews of environmental reports and contributing to the improvement of the reliability of environmental reports by realizing efficient and effective reviews. Six institutions are accredited as assessment bodies by this association.

accreditation system.

Mid-tier audit firms are endeavoring to gather information and implement initiatives within the firm, however the degree of such efforts varies by firm. Some mid-tier audit firms have established subcommittees to gather information and develop a documentation system for assuring non-financial information in preparation for providing services. On the other hand, some mid-tier audit firms are not actively expanding non-audit services and are considering providing services to the extent possible in response to client requests.

Some small and medium-sized audit firms have not considered the assurance of sustainability information because their clients have not consulted with them and the firm's resources do not allow for the assurance of non-financial information.

In April 2023, the JICPA published the "Action on the Basic Policy on Capacity Development for Sustainability" as a report on the results of a study on measures to steadily advance efforts to develop CPA capabilities related to sustainability. The report includes the basic policy on capacity development for sustainability, sustainability-related knowledge and capabilities required of CPAs, a syllabus on sustainability education, and future action.

■ Green Washing ■

"Greenwashing" is a term coined by combining the word "green," which conjures the idea of consideration for the environment, with the word "whitewashing," which conjures the idea of consideration for deception and being superficial. The term refers to the act of disseminating fraudulent information that appears to be environmentally conscious, and encouraging purchases of products and investments.

Examples of green washing have been pointed out widely, not limited to finance. In recent years, however, with the rapid increase in sustainable investment such as ESG investment and green bonds, there are concerns about the occurrence of financial products that are provided in a manner that could be misunderstood as sustainability-related investment products.

In an effort to avoid greenwashing, the Sustainable Finance Disclosure Regulation (SFDR) is being applied to a wide range of market participants, including asset managers, in Europe, and the IESBA published a Q & A in October 2022 to address concerns about greenwashing.

In Japan, the FSA revised its comprehensive supervisory guidelines for Financial Investment Business Operators in March 2023 to add a point of caution regarding disclosure of ESG investment trusts. Greenwashing is also said to occur due to differences in ESG ratings and data among providers. The FSA published the "Code of Conduct for ESG Evaluation and Data Providers" in December 2022.