I. Overview of the Audit Sector

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A. CPAs

1. Introduction of the CPA system

The origin of the Japanese CPA system is the Accountants Act, which was enacted in 1927. With the economic and social reconstruction and democratization proceeding after the end of World War II, the Accountants Act was abolished, and the CPA system was introduced in 1948 for the purpose of ensuring the reliability of financial statements by determining the qualifications of audit and accounting experts whose primary duty is audit and attestation. Specifically, the Securities and Exchange Act was promulgated in 1947, requiring companies that issue or solicit investment in shares, corporate bonds or other securities to submit reports. The issuer of listed securities is required to obtain audit attestation from certified public accountants (CPAs) by the full overhaul of the 1948 Securities and Exchange Act (currently the Financial Instruments and Exchange Act (FIEA)) as well as the promulgation/enforcement of the Certified Public Accountants Act (CPA Act).

Accordingly, the Certified Public Accountants Management Committee was established to conduct CPA examinations, etc. (becoming the CPA Examination and Investigation Board in 1952 after a transfer of jurisdiction and expanded/restructured into the current Certified Public Accountants and Auditing Oversight Board in 2004). The Corporate Accounting Principles were released in 1949, and the Audit Standards in 1950.

The present CPA Act clearly sets out the mission and professional responsibilities of CPAs as given below. CPAs must always be self-aware of this mission and these professional responsibilities in performing their duties regardless of audit attestation services or non-audit services.

“The mission of certified public accountants, as professionals on 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 documents and any other information concerning finance from an independent standpoint, thereby contributing to the sound development of the national economy” (Article 1).

“A certified public accountant shall always maintain his/her dignity, endeavor to acquire knowledge and skills, and provide services with fairness and integrity from an independent standpoint” (Article 1-2).

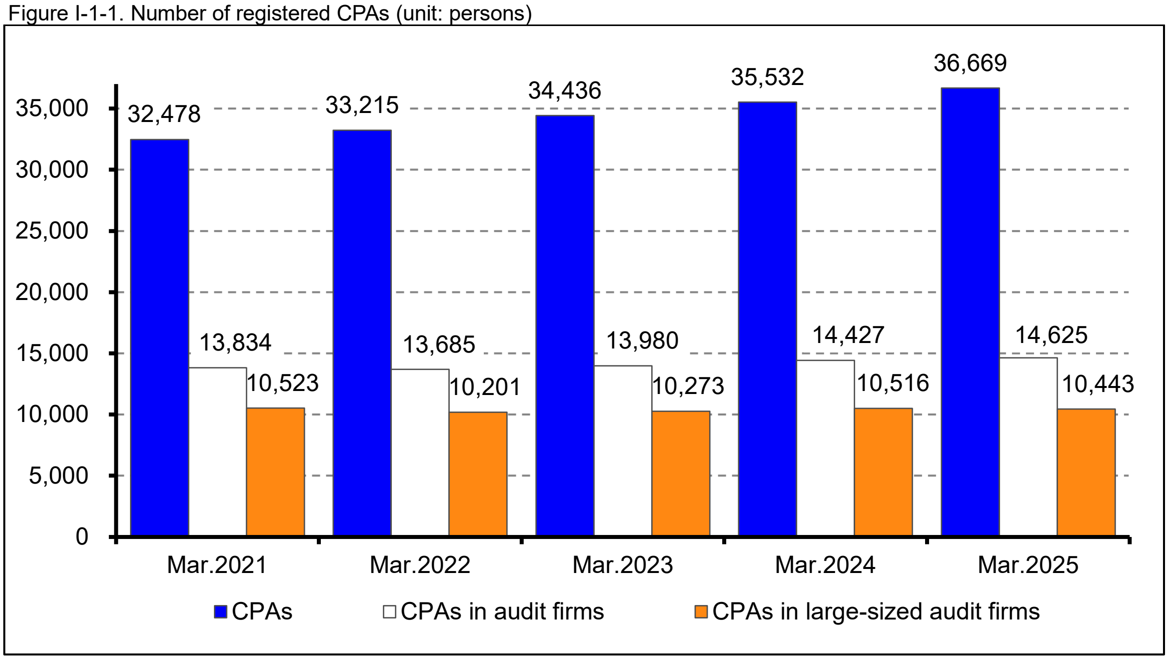
2. CPAs

To become a certified public accountant, a person must pass the certified public accountant examination, satisfy certain requirements (business assistance, professional accountancy education program, etc.), and be registered on the roster maintained by the Japanese Institute of Certified Public Accountants (JICPA) (Articles 3, 17, and 18 of the CPA Act).

The number of registered CPAs has been gradually increasing over the past few years. However, but the number of CPAs working at audit firms has not increased as much as the number of registered CPAs. The ratio of the number of CPAs working at audit firms to the total number of registered CPAs has been declining year by year, and continued to decline from 42.6% at the end of March 2021 to 39.9% at the end of March 2025. Of the registered CPAs belonging to audit firms, around 70% at large-sized audit firms (Figure I-1-1).

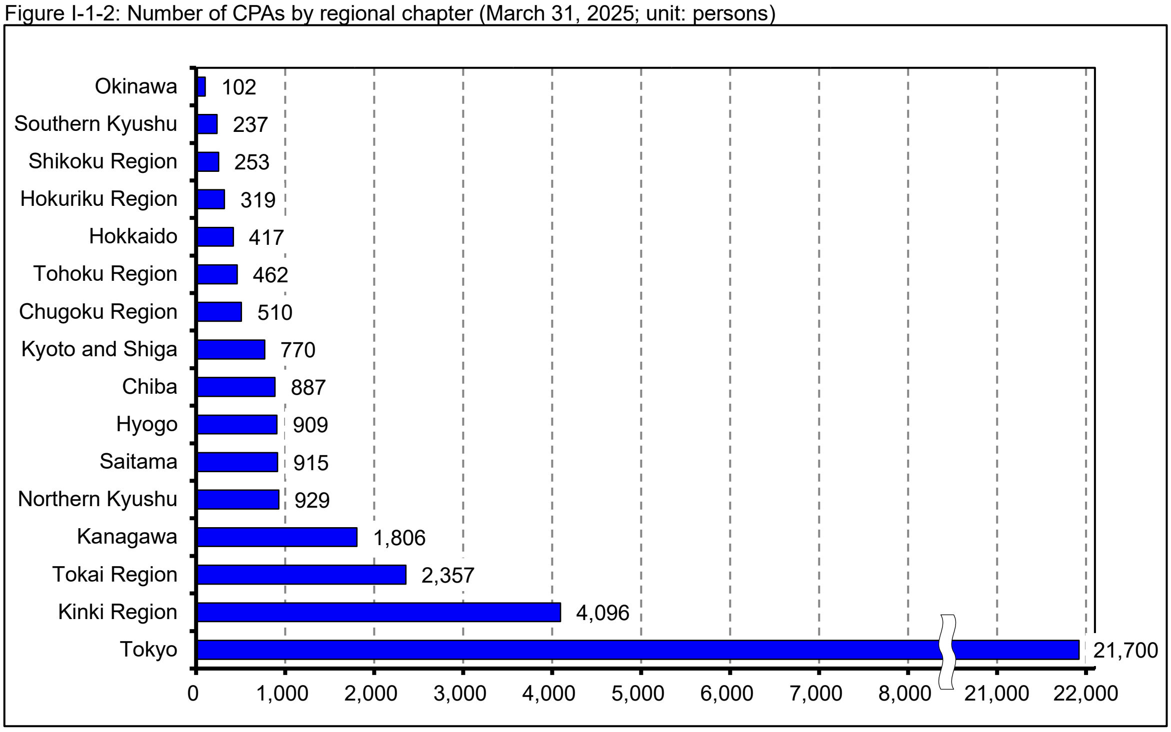
CPAs must be members of the JICPA (Article 46-2 of the CPA Act) and must belong to a regional chapter, i.e., one of the JICPA branches established across Japan (16 regional chapters as of March 31, 2025). Around 70% of CPAs are based in the Tokyo metropolitan area (Tokyo, Kanagawa, Saitama, Chiba) (Figure I-1-2).

Figure I-1-1. Number of registered CPAs (unit: persons)



(Source) Prepared by the CPAAOB based on data from the JICPA

Figure I-1-2: Number of CPAs by regional chapter (March 31, 2025; unit: persons)



(Source) Prepared by the CPAAOB based on data (e.g. survey of numbers of members) from the JICPA

■ Initiatives to improve the attractiveness of audit service ■

The number of registered CPAs increased from 24,964 at the end of March 2013 to 36,669 at the end of March 2025 (46.9% increase). On the other hand, the number of personnel working at audit firms has not increased as much as the number of registered personnel, from 12,799 at the end of March 2013 to 14,625 at the end of March 2025 (14.3% increase). With the growing needs for audits in terms of both quality and quantity, there are concerns about a shortage of personnel in charge of audits. Improving the attractiveness of audit services and securing audit professionals are not issues unique to Japan and many countries are taking action.

International Federation of Accountants (IFAC) states that the factors that caused personnel difficulties for small and medium-sized audit firms are now affecting the audit industry as a whole; specifically, (I) declining the number of applicants, (ii) increasing the opportunities for employment in other fields, and (iii) concerns about achieving work-life balance and flexible working styles. In Japan as well, the increase in mechanical and monotonous work, long working hours, and inability to realize the results of one's own work are reported as reasons why accountants do not find audit attractive.

By classifying the above factors into (I) decline in motivation and incentive to engage in audit services or to belong to audit firms, (ii) increase in workload due to the refinement of audit standards and manuals, and (iii) increase in opportunities for employment in other fields, we would like to introduce the efforts of audit firms to increase the attractiveness of engaging in audit services and to secure personnel engaging audit services.

(I) Initiatives to address declining motivation and incentive to engage in audit services or to belong to audit firms
・Flexible timing of promotion, including earlier promotion for capable staff and promotions that take into account the preference for work-life balance;
・Diversifying career paths (creating the promotion paths allow for the acquisition of expertise in addition to the promotion path from staff to partners);
・Compile a variety of work styles and share them across the firm;
・Providing work opportunities for non-audit work, such as tax and advisory services, as well as expanding opportunities for short-term secondments to external organizations and interdepartmental transfers;
・Enhancing communication within small groups and mentoring programs, etc.

(II) Efforts to address workloads associated with the refinement of audit standards and manuals
・Leveling of work through centralized management of assignments handled by each partner/staff
・Greater flexibility in working locations and hours through remote work and flexible working hours
・Improving efficiency by introducing IT system and transferring operations to a service delivery center (an organization established to perform non-judgemental tasks such as sending and collecting balance confirmation letters), mainly undertaken by large-sized audit firms

(III) Initiatives to respond to the increase in employment opportunities in other fields
In recent years, the fields in which CPAs play an active role have expanded, and there are a growing number of careers in which CPAs can make a tangible contributions to organizations and society, such as CFOs and accounting managers of business companies, consulting firms, and NPOs. Under these circumstances, the message that "audit is a social infrastructure that ensures the fairness of capital markets," which has been a source of attraction for audit services, is said to have become relatively less convincing. Audit firms are also promoting initiatives such as those mentioned in (I) above with the aim of providing CPAs with an opportunity to experience their own growth. On the other hand, if CPAs play an active role on the side of the preparers of financial statements, there is an expectation that the appropriateness of the financial statements prepared will increase, so that the firms show a certain degree of understanding towards young CPAs who wish to advance their careers outside of the firm. Large-sized audit firms and some mid-tier audit firms have introduced an initiative called "alumni" to encourage CPAs who are active in such business companies to return to audit engagements by maintaining and strengthening relationships with their retirees. This initiative provides opportunities for exchanging information between retirees and between retirees and incumbents, as well as for rehiring retirees or introduce part-time audit engagement opportunities, thereby

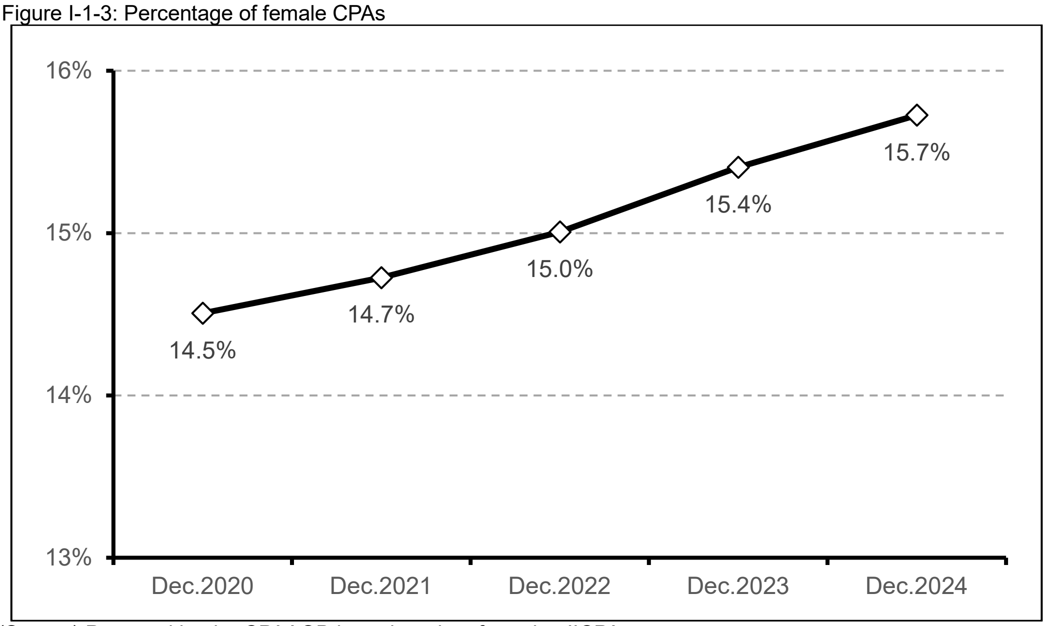
encouraging them to return to auditing work. With regard to retirees from other firms, each audit firm recruits mid-career professionals regardless of their original firm, and expects them to be immediately engaged in audit engagements. Furthermore, audit firms' compensation tends to be less favorable than that of business companies and consulting firms. It is not easy for audit firms to increase audit fees, which are the source of their salaries. However, at large-sized audit firms, there have been cases of salary increases for senior staff, who tend to have higher turnover rates than other levels.

Some large-sized audit firms are planning to expand the scope of audit and assurance beyond financial information to include third-party evaluation of information security, AI assurance, and evaluation of governance effectiveness. As a measure to develop diverse human resources for the future, large-sized audit firms are providing training and establishing internal qualification systems for specialist knowledge in the fields of sustainability and digital fields such as generated AI and data analysis. We expect that these initiatives, which provide employees with a wide range of growth opportunities, will also lead to increased attractiveness of audit profession.

3. Percentage of Female CPAs

The percentage of women among the total number of registered CPAs is gradually increasing (Figure I-1-3), and at the end of 2024 the figure reached 15.7%, which is the same as the level for female tax accountants[1]. On the other hand, it is still lower than the percentages of female attorneys and female CPAs in the UK[2].

Figure I-1-3: Percentage of female CPAs



(Source) Prepared by the CPAAOB based on data from the JICPA

[1] According to "2024 Survey on Women's Participation in Policy and Decision-making Processes" by the Cabinet Office's Gender Equality Bureau, the percentage of female tax accountants was 15.8% at the end of March, 2024, and the percentage of female attorneys was 20.2% at the November 1st, 2024.

[2] According to the UK Financial Reporting Council's "Key Facts and Trends in the Accountancy Profession 2023," there are several CPA institutes in the UK, and the average female membership for them is 38%.

■ Efforts to gender diversity ■

The Japanese Institute of Certified Public Accountants (JICPA) intends to increase the share of successful female examinees to 30% by 2030 and the share of female members and semi-members to 30% by 2048. And it is promoting arrangements to further empower female CPAs, such as the use of maiden names, support for employment and return to work, exemption or relief from continuing professional development (CPD) and membership fees during absence from work for childbirth, childrearing and other reasons. There are some large-sized audit firms that are setting KPIs such as the share of female executives, nurturing female executives and providing support for female CPAs at each life stage, holding training sessions and seminars to develop an organizational culture to accept diverse working styles, and offering support for creating networks.

Large-sized audit firms are also promoting initiatives such as setting KPIs for the ratio of women in management positions, etc., supporting women's career development, supporting various life stages such as childcare and nursing care, encouraging male employees to take childcare leave, and supporting the establishment of networks among female employees. According to the Audit Quality Reports of large-sized audit firms, the average proportion of female partners is around 9%, while the average proportion of female managers (senior managers, managers, etc.) is around 21%.

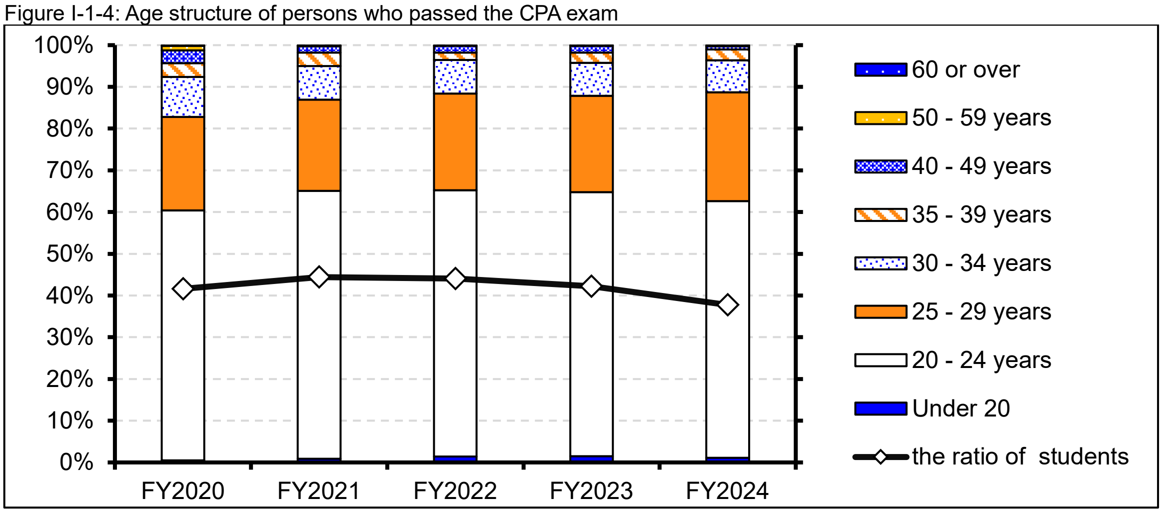
The JFSA, together with the JICPA, has published a pamphlet titled "Activity Fields for CPAs and Exam Passers," which disseminates messages from female CPAs about the attractiveness and motivation of CPAs and their career plans, with an eye to increasing the number of women taking the CPA exam.

The ratio of successful examinees by gender for the 2024 CPA Examination was 6.17% for female examinees (7.90% for male examinees), which was lower than the 2023 Examination. However, the ratio of successful female examinees was 22.4%, a slight increase from the previous year, and the number of successful female examinees also increased from the previous year. In recent years, the number of females submitting applications for the examination and passing the examination has been showing an upward trend.

4. Age Structure of Persons who Passed the CPA exam

Breaking down the age structure of persons who passed the CPA examinations, we see that the largest age group is 20-24 years. People in this group accounted for 61.5% of those who passed it in 2024. The ratio of students (excluding persons enrolled in courses at vocational schools etc.) is the highest by occupation. Among them, despite on the decline, the proportion of university (including junior colleges) students were 37.7% in the 2024 examinations (Figure I-1-4). The number of university student applicants continues to increase (6,559 in the 2022 Examination, 6,740 in the 2023 Examination, and 6,901 in the 2024 Examination).

Figure I-1-4: Age structure of persons who passed the CPA exam



(Source) Prepared by the CPAAOB based on data from the CPAAOB survey of persons who passed the CPA exam

■ Initiatives to review the operation of the CPA examination ■

The CPA exam is the initial step in the process of selecting and developing CPAs. Approximately 20 years have passed since the CPA exam took its current form in 2006, and the number of CPA exam takers has increased to over 20,000 per year. The number of registered CPAs has more than doubled from approximately 16,000 as of the end of March 2006 to approximately 36000 as of the end of March 2025. Thus, the number of accounting professionals in society as a whole has been steadily increasing.

Under these circumstances, in the CPA examination, the pass rate of the short-answer examination has declined as the number of examinees has increased, while the pass rate of the essay examination has been relatively high. Therefore, there are issues in terms of the positioning and roles of the short-answer examination and the essay examination, and there are concerns about ensuring the qualities and abilities of the passers.

Specifically, since the pass rate of the short answer exam is too low and questions with high points per question have a large impact on the pass / fail, it is considered that there are many people who cannot pass the short answer exam even if they have a systematic understanding of the necessary knowledge. In addition, since the pass rate of the essay exam is relatively high and the amount of description is reduced in some subjects, it is considered that there are people who can pass the exam even if they have not been sufficiently trained in the necessary thinking skills and applied skills. Furthermore, the circumstances surrounding CPAs are changing, and it is considered necessary to respond to the situation where the required knowledge and skills are expanding, such as the relationship with English and IT, and the consideration of the disclosure and assurance system of sustainability information.

In light of this situation, the CPAAOB formulated and published "Rebalancing the CPA Exam- Review of the Exam Administration Framework and Question Content for a More Accurate Assessment of Examinees' Abilities" ("Rebalancing the Exam") in June 2025 in order to more accurately assess the abilities of examinees.

(Follow the link below)
https://www.fsa.go.jp/cpaaob/kouninkaikeishi-shiken/20250612.html

The following measures will be taken to balance the studies.

(1) Adjustment of the pass rate between the short answer and essay tests [Implemented from 2027 Exam]

Increase the number of applicants for the essay test (the number of persons who pass the short-answer test) in order to ensure more appropriate competition in the essay test (raising the criteria for passing the essay test).

(ii) Adjustment of the allocation of points per question for the short-answer examination [Implemented from the 2026 Exam]

- In the short-answer exam subjects with calculation questions (Financial Accounting and Management Accounting), the number of questions has decreased due to time constraints, so the number of questions will be increased to narrow the gap in the allocation of points per question (and the time will be adjusted accordingly).

(iii) Responses to issues related to the production of examination questions and proficiency assessment

- In the essay test, questions that require a certain amount of description will be given. [Corresponding from the 2026 Exam]

- We will also consider appropriate point conversion methods for elective subjects and the creation of tests (English, disclosure and assurance of sustainability information, IT, etc.) in accordance with the expansion of the knowledge and skills required of CPAs.

B. Audit Firms

Audit firms numbered 2,419 at the end of March 2024, but they vary by service and business format. Audit and attestation services cover both statutory audits and non-statutory audits. Statutory audits are CPA audits required by the law. When CPA audits were first introduced, the only statutory audits were FIEA audits, but thereafter CPA audits under the Companies Act were introduced, and then educational corporation audits under the Act on Subsidies for Private Schools. There are now a multitude of statutory audits, including audits of labor unions, credit unions, credit associations, agricultural cooperatives, social welfare corporations and medical corporations, etc. Further explanation of audit and attestation services is provided on C. Audited Companies, 1. Types of Audit and Attestation Services.

There are three types of entities providing audit and attestation services: audit firms, partnerships, and solo practitioners. Audit firms are established pursuant to the CPA Act for the purpose of organizationally performing audit and attestation services. When the audit firm system was forged in 1966, the tasks involved in audit and attestation services had increased in volume and complexity as corporations subsequently grew larger in scale and management became more multifaceted. Additionally, numerous incidents of fraudulent accounting were occurring at the time, bringing into question the raison d'être of CPAs. The system of audit firms was therefore introduced to improve audit quality for promoting the conduct of organizational audits.

The CPAAOB classifies audit firms by scale into large-sized audit firms, mid-tier audit firms, and small and medium-sized audit firms (Figure I-2-1). CPAAOB mainly monitors those audit firms conducting FIEA audits of domestic listed companies[3].

Figure I-2-1: Classifications of audit firms (as of March 31, 2024)

	Audit Firm	Number of Firms
Large-sized audit firms		4
Mid-tier audit firms		4
Small and medium-sized audit firms		2,411
(Breakdown)	Small and medium-sized audit firms	(279)
	Partnerships (Note 1)	(49)
	Solo practitioners (Note 1, 2)	(2,083)

(Note 1) The number of audit offices in fiscal 2023 (book closing date from April 1, 2023, till March 31, 2024) listed in copies of audit summaries or audit implementation reports submitted to the JIPCA.

(Note 2) In order for solo practitioners to conduct an audit for a listed company it is required by the CPA Act and each exchange's securities listing regulations to conduct the audit jointly with other CPAs, etc.

(Source) Prepared by the CPAAOB based on data from the JICPA

1. Organizational Structure of Audit Firms

Audit firms are established through investment by persons including five or more CPAs, and their defining characteristics are that the persons who invested (partners) are directly engaged in

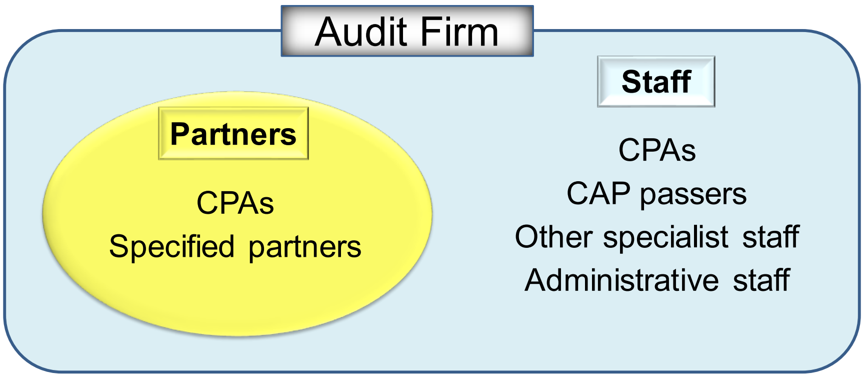
[3] Registration as a registered auditor of listed companies etc. is required to audit listed companies. For information on the registration system for listed company auditors, see "IV. Responses to Changes in the Global Environment Surrounding Audits, 1. Trends Surrounding Small and Medium-sized Audit FirmsI".

management and that they ensure organizational discipline via mutual monitoring. Some audit firms comprise only partners, but those of a certain scale ordinarily employ CPAs (CPAs who have not invested in order to become partners of the audit firm), CPA examination passers (persons who have passed the CPA exam but have not been registered as CPAs after undergoing practical training and providing assistance with audit work), and other experts as staff.

In the past, partners of audit firms were limited to CPAs, but in today's more sophisticated economy and society, partners are required to have a wide range of knowledge and experience including management, law, IT, pension mathematics to ensure appropriate operational management of the audit firm and to provide effective organizational audit services. Accordingly, as a result of legal revisions in 2007, a "specified partner system" allowed non-CPAs to be partners at an audit firm. However, CPAs must comprise at least 75% of the audit firm's partners if specified partners join the firm. In FY2024 large-sized audit firms had 165 specified partners among a total of 1,886 partners.

The personnel composition of an audit firm is outlined below (Figure I-2-2), and explained in more details in "III. Operation of Audit Firms, A. Operations Management System, 3. Human Resources of Audit Firms".

Figure I-2-2: Personnel composition at audit firms



(Source) Prepared by the CPAAOB with reference to page 55 of "New CPA/Audit firm Audit System - Ensuring Fair Financial/Capital Markets" (Dai-Ichi Hoki Co., Ltd., 2009), Yuichi Ikeda and Hidenori Mitsui, ed.

	Large-sized audit firm	Mid-tier audit firm	Small and medium-sized audit firm
Partners	Approx.240 up to approx. 570	Approx. 40 up to 100	Up to approx. 50(Note2)
Full-time staff	Approx. 3,300 up to approx. 7,700	Approx. 210 up to 950	Up to approx. 110(Note2)

(Note1) See "Figure III-1-3: Characteristics of each type of audit firm" (page 65) for Characteristics of organizational structure based on audit firm size.
(Note2) The fiscal years of small and medium-sized audit firms cover a wide range of months, and the figures for FY2024 have not yet been compiled. For this reason, small and medium-sized audit firms are included up to FY2023. Excluding an audit firm whose number of partners and full-time staff members is much higher than others.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

In response to the increasing complexity and internationalization of corporate activities at domestic listed companies, especially major ones, audit firms grow bigger. The large-sized audit firms responsible for the majority of audits of major listed companies have workforces exceeding several thousand people; even mid-tier audit firms now have more than 200 people.

As audit firms grow in scale, they necessitate introducing job classification system defined by abilities, experience, etc. for effective management of organization. (Figure I-2-3). It is standard practice for personnel to move up the ranks from staff and senior staff to manager, senior manager and, if selected, to partner. In recent years, some large-sized audit firms hire a larger number of audit assistants (staff without qualifications relating to financial statement audits, such as a qualification of CPA) to reduce the workload of CPAs and enable them to concentrate on duties requiring professional judgment.

The expanding size of audit firms and the increasing complexity of their organizational administration has made the difficulty of ensuring audit quality even more apparent. In response to this situation, Principles for Effective Management of Audit Firms (the Audit Firm Governance Code) formulated in March 2017 was revised in March 2023. As a result of this revision, audit firms registered on the list of listed company auditors are now required to establish a framework for conducting operations in accordance with the Audit Firm Governance Code and a framework for disclosing substantial information. As for the situation of amendments of Audit Firm Governance Code, refer to III. Operation of Audit Firms A. Operations Management System 2. Efforts in Response to Audit Firm Governance Code.

Figure I-2-3: Professional hierarchy, required skills, and primary trainings in a large-sized audit firm

	Staff	Senior Staff	Manager	Senior Manager	Partner
Roles	Perform of audit practice under the guidance and supervision of superiors; in the case of seniors, supervising engagement teams performing audits of small and medium-sized enterprises, depending on their experience		Oversight of audit teams		Overall suprivision of all audit engagements and involvement in management of the audit firm
Skills required	Specialist knowledge on audit practices, accounting and audits		Management skills in staff mentoring and coordination with audited companies, as well as problem solving skills		High level of skill as a audit supervisor
Primary training	Trainings related to annual accounting audits, fraud prevention, global audit, IT, sustainability etc.				
	Audit procedure training, etc.	Management training, specialty-specific training, etc.			

(Note) For details, see “III. Operation of Audit Firms, A. Operations Management System, 4. Organizational Structure for Providing Audit Services” and “5. Organizational Structure for Supporting Audit Services”.
(Source) Prepared by the CPAAOB

2. Development of Quality Management Structures and Responses by Audit Firms

To ensure audit quality, it is important that audit firms develop and operate appropriate quality control structures to serve as a foundation for having their partners perform audit services properly.

"Standards on Quality Control for Audits" were formulated for audit and attestation services in 2005, and revised in November 2021 in association with the "Quality Control Standards for Audits," the International Standard on Quality Management (ISQM) 1 (ISQM1: Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements), which is an international quality management standard, and other standards were newly established or revised. Audit firms need to comply with professional ethics in their services other than audit and attestation services as well.

The Revised Standards on Quality Control for Audits (hereinafter referred to as the "Revised Standards") require individual audit firms to introduce the system of quality management based on a risk-based approach, under which they should

a. set their own quality objectives,
b. distinguish quality risks that hinder the achievement of such quality goals and assess them one by one,
c. determine policies or procedures for dealing with those assessed quality risks and implement them, and
d. make improvements based on the root cause analysis of defects, if any.

Additionally, the Revised Standards state that the system of quality management should include the following as component elements:

a. Process to assess risks of the audit firm;
b. Governance and leadership;
c. Professional ethics and independence;
d. Conclusion and renewal of audit engagements;
e. Implementation of services;
f. Resources for operational management of the audit firm;
g. Information and communication;
h. Monitoring of the system of quality management and improvement process; and
i. Succession among audit firms.

Furthermore, the Revised Standards newly require the top officer in charge of an audit firm's system of quality management to evaluate the system at least once a year by setting a base date and draw a conclusion as to whether the system provides reasonable assurance to the audit firm that the purpose thereof is surely achieved.

The Revised Standards are effective for audits of financial statements for a business year or an accounting period starting on or after July 1, 2023 (for audit firms other than large audit firms under the CPA Act, for a business year or an accounting period starting on or after July 1, 2024).

According to interviews with large-sized audit firms, they are moving ahead of the ISQM1, which went into effect in December 2022, in cooperation with the global networks. They are receiving risk assessment tools from the global networks and are adding evaluation items based on the Revised Standards' own requirements while taking into account the quality goals and quality risks set by global networks.

Regarding the operation of the system of quality management, at many large-sized audit firms, the persons responsible for each division have process owners identify quality risks and policies and procedures for dealing with risks, and assess risks under the steering committee, which comprehensively manages responses to quality risks. Some firms have person in charge of monitoring compliance with the Revised Standards from independent standpoint.

The number of quality goals, quality risks, and policies and procedures to address these risks varies from firm to firm ranging from 15 to 144 in quality goals, 117 to 320 in quality risks, and 536 to 1,296 in policies and procedures to address the risks.

The timelines for the evaluation of the system of quality management also vary between firms, and the reporting time of evaluation results spread over the period from February 2024 to November 2024. Regarding the overall evaluation results, at all firms, the chief responsible officer for the system of quality management concludes that the system of quality management provides reasonable assurance that the objectives of the system are being achieved.

Through the operation and monitoring of the system of quality management, all large-sized audit firms are aware of the challenge of making system of quality management known to engagement teams, as this encourages engagement teams that actually operate some processes of the system of quality management to take autonomous actions.

Some large-sized audit firms also face challenges in further enhancing the collection and analysis of risk information in order to improve the accuracy of identifying high-risk audit engagements and control processes as well as monitoring viewpoints.

According to reports collected during PY2024, mid-tier audit firms are taking action based on risk assessment tools provided by their global networks. Three of mid-tier audit firms have been applying the Revised Standards since July 1, 2023 and the rest of mid-tier audit firm has also started to apply since July 1, 2024. Regarding the risk assessment process, similar to large-sized audit firms, they are developing the quality goals, quality risks and the policies and procedures based on the items shown in the global network's tool as well as adding evaluation items based on the Revised Standards' own requirements. Regarding the overall evaluation results, at three firms which have applied the Revised Standards since July 1, 2023, the chief responsible officer for the system of quality management concludes that the system of quality management provides reasonable assurance that the objectives of the system are being achieved.

In addition, as part of the efforts to penetrate and establish the system of quality management in the workplace, meetings and training sessions such as partner meetings are held. Some mid-tier audit firms have stated a quality management committee held once every three months, with at least one member from each regional office participating.

Mid-tier audit firms are aware of the following issues relating to the operation and monitoring of system of quality management: (1) it is difficult to assess the degree of implementation of response measures if sufficient time is not allowed until the evaluation base date for response measures developed during the term; (2) a certain amount of effort is required for coordination among departments in responding to matters requiring improvement that cut across multiple departments; and (3) through the operation and monitoring of system of quality management, it is necessary for engagement teams to operate implemented measures while continuously running the PDCA cycle.

Small and medium-sized audit firms have also begun applying the Revised Standards. According to the results of the collection of reports from 52 small and medium-sized audit firms in PY2024[4], approximately 25% of the audit firms surveyed required the most time to set quality objectives as part of their risk assessment process when applying the Revised Standards; approximately 20% required the most time to establish rules concerning governance and leadership; and approximately 15% required the most time to review all quality management rules.

The Revised Standards also require audit firms to perform root cause analysis of deficiencies identified in their system of quality management and implement improvement activities to address the deficiencies.

Small and medium-sized audit firms have been analyzing the root causes of improvement recommendations pointed out in the JICPA Quality Control Reviews even before the implementation of the Revised Standards began (See details in 3. Report of JICPA Quality Control Review). According to reports collected in PY2024, many small and medium-sized audit firms cited the following as root causes:

- There was a lack of understanding of the level required by the current auditing and quality management standards and the high level of discipline required in the registration of listed company auditors.
- The establishment and operation of a quality management environment was inadequate due to a lack of an attitude and organizational culture that emphasizes quality management, as well as the priority given to the performance of individual audit engagements.
- There was a lack of education and training within the firm, as well as a lack of information sharing across the firm on matters pointed out by the JICPA, etc. and fraud cases involving companies other than the audited company.

On the other hand, there were some cases where the root cause was attributed to personal qualities

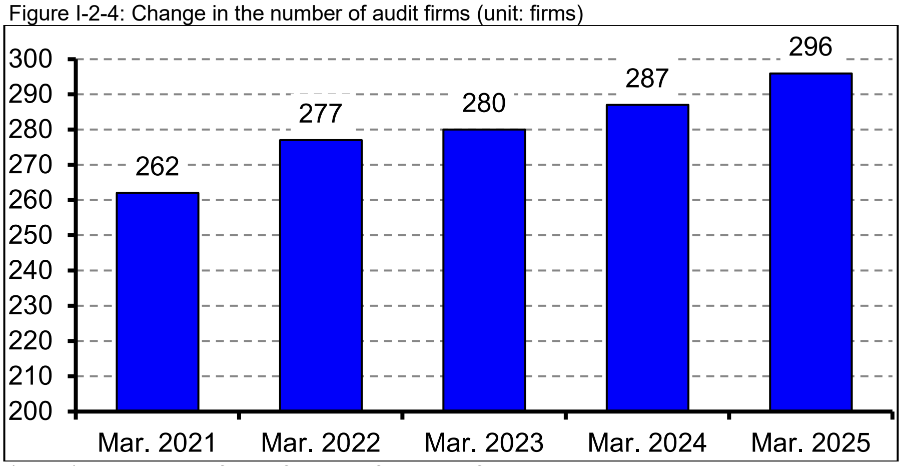
[4] It should be noted that the collection of reports was answered based on information as of June 30, 2024, which may be different from the current situation.

such as errors in awareness and judgment by the engagement team and engagement partners, etc., as well as some cases where superficial reasons such as insufficient review of audit documentation were pointed out in the collection of reports. Thus, there were challenges in conducting sufficient and appropriate root cause analysis.

3. Number of Audit firms

The number of audit firms has been on an upward trend in recent years. As of March 31, 2025, there were 296 firms, and 5 firms disappeared as a result of dissolution and 14 were established in the period April 2024 - March 2025, ending up with a net increase by 9 firms (Figure I-2-4) year on year. See "4. Mergers of Audit Firms" for details on mergers from FY2021 onwards.

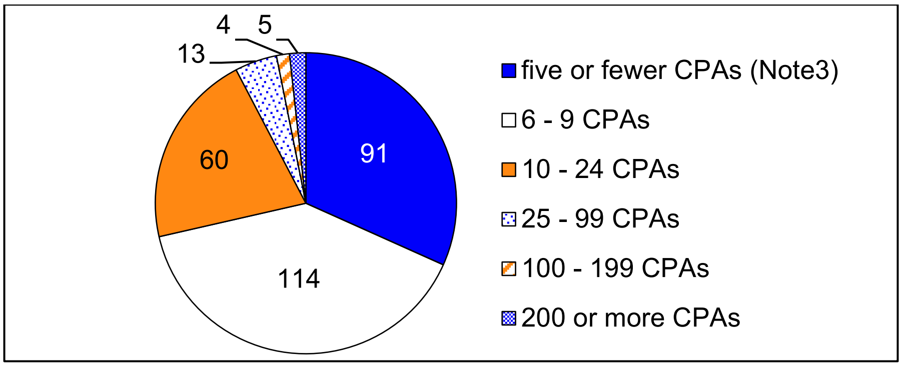
Figure I-2-4: Change in the number of audit firms (unit: firms)



(Note1) The number of audit firms as of the end of March and 2021 2022 are adjusted based on the data obtained after publishing the previous Monitoring Report.
(Note2) The number of limited liability audit firms[5] as of the end of March 2025 was 36.
(Source) Prepared by the CPAAOB based on data (e.g. survey of numbers of members) from the JICPA and reports of individual audit firms. The list of limited liability audit firms is published on the FSA website.

Classification by the number of full-time CPAs belonging to each audit firm reveals that firms with fewer than 25 CPAs make up over 90% of the total (Figure I-2-5).

Figure I-2-5: Number of audit firms by scale in terms of full-time CPAs (FY2024; unit: firms)



(Note 1) The number of full-time CPAs is the total of partners who are CPAs and full-time staff who are CPAs.
(Note 2) Data on 287 audit firms (excluding dissolved and disappearing firms during the period) was collected from operational reports submitted by these firms in FY2024. The timing of the submission of the business reports of each audit firm differs depending on the financial year, and for the sake of compiling the data for this report, information for 2022 is used for small and medium-sized audit firms (the same applies to the subsequent figures).
(Note 3) An audit firm where the number of partners who are CPAs drops to four or fewer should be dissolved, but six months is granted

[5] An audit firm in which individual partners assume unlimited joint and several liability only with respect to audit attestation (specified attestation) in which the partners are involved as designated limited liability partners, and other operations are the responsibility of the partners within the scope of their contributions

as suspended term as stipulated in the CPA Act.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

4. Mergers of Audit Firms

There have been 8 mergers of audit firms since FY2020 (Figure I-2-6). The main reasons for mergers were to reinforce management infrastructure and to expand business.

Figure I-2-6: Audit firms involved in mergers from FY2020 (March 31, 2025)

FY	Surviving firm	Disappearing firm
2020	Ark LLC	Kinki Daiichi Audit Corporation
	Nishi-Nihon Audit Corporation (Kowa Audit Corporation)	Hibiya Audit Corporation
2021	Yasaka Kaikeisha Audit Corporation	Keihin Audit Corporation
2022	Kyoritsu Audit Corporation	Shinmei Audit Corporation
	Moore Shisei Audit Corporation (Moore Mirai Audit Corporation)	Kisaragi Audit Corporation
	SKIP Audit Corporation	Godai Audit Corporation
2023	Souken Nichiei Audit Corporation (Fujimi Audit Corporation)	Seinan Audit Corporation, Nagoya Audit Corporation
	PricewaterhouseCoopers Aarata LLC (PricewaterhouseCoopers Japan LLC)	PricewaterhouseCoopers Kyoto Audit Corporation
2024	(No mergers)	

(Note) Names in parentheses show the new name after merger as of March 31, 2025.
(Source) Prepared by the CPAAOB from materials made publicly available by audit firms

Reports collected from mid-tier audit firms in PY2024 showed that many of them considered mergers as an option for their future business strategies. The collection of reports from small and medium-sized audit firms (involving 52 firms) in the same program year found that around 48% of small and medium-sized audit firms said they would consider a merger if they could find a good partner.

5. Financial Condition (Operating Revenue, Proportion of Audit and Attestation Services and Non-audit and Attestation Services)

Audit firms offer not only audit and attestation services but – non-audit services such as assurance services other than audit and attestation services and financial advisory services (support for initial public offerings, introduction of IFRS, organizational realignment and so forth).

Operating revenues over the five years until FY2024 (FY2023 in the case of small and medium-sized audit firms) showed an uptrend all at large-sized, mid-tier and small and medium-sized audit firms (excluding the impact of the merger between PwC Aarata and PwC Kyoto).

Revenues from audit and attestation services roughly accounted for 70% of operating revenues at large-sized audit firms, while the ratio was about 95% and 90% respectively at mid-tier and small and medium-sized audit firms (Figure I-2-7). For audit firm groups' operating revenues, see "III. Operation of Audit Firms, A. Operations Management System, 9. Domestic Audit Firm Groups".

Characteristics of audit firms, classified by size, are as follows:

a. Large-sized audit firms

The ratio of audit service and attestation revenues, which has been around 75% for large-sized audit firms as a whole. Seeing the ratio of each large-sized audit firm, the ratio has ranged between 60% and 85% at three of the four firms, but at the remaining firm it has hovered at around 50%.

Large-sized audit firms operate certain extent of non-audit services based on their organizational policy that “performing non-audit services provides their personnel with opportunities to acquire a wide variety of business experiences to grow”, “a broad range of experiences and knowledge through non-audit services serves to enhance audit quality”, and “non-audit service is effective for attracting talent”.

b. Mid-tier audit firms

Audit and attestation service revenues have been rising at all firms, and the ratio of them in operating revenues has mostly maintained a level over 90%.

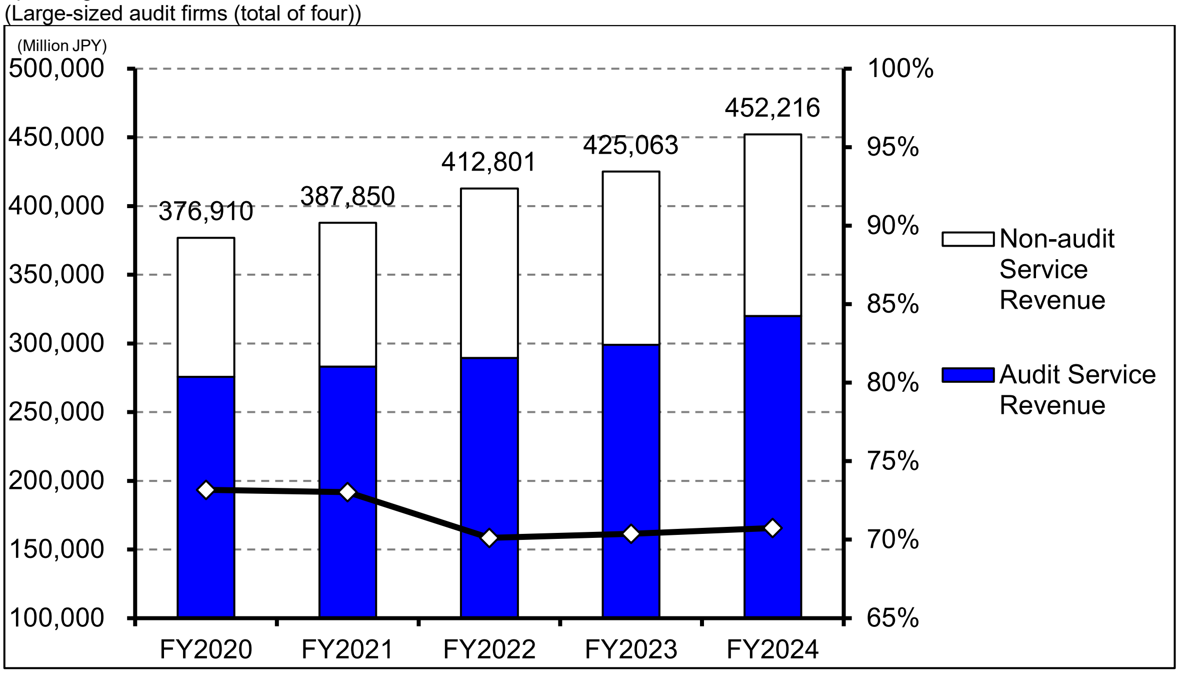
As mid-tier audit firms' business is centered on audit and attestation services, they provide non-audit services that are considered useful when conducted together with audit and attestation services or only within a limited range based on their individual circumstances, including available staff members.

c. Small and medium-sized audit firms

The ratio of audit and attestation service revenues has been around 90%.

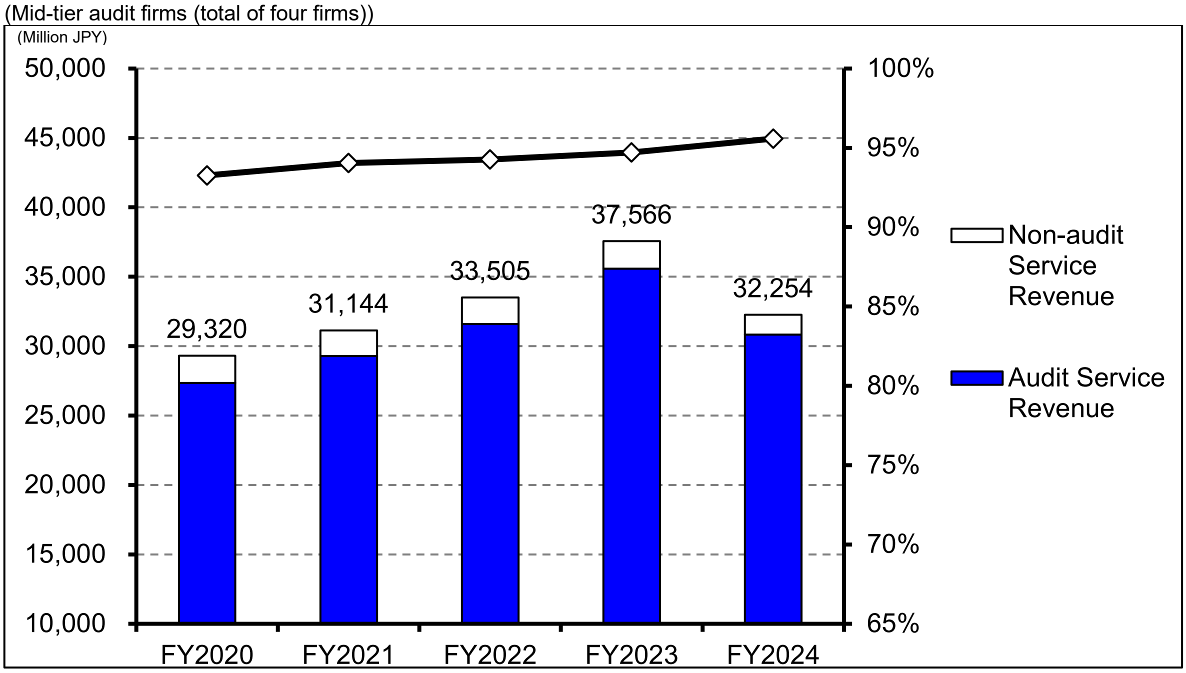
The operating revenues of small and medium-sized audit firms are moderate on the whole, but some of the largest firms in this category are expanding their business through newly concluding audit engagements with companies for which mainly large-sized audit firms cancelled audit engagements. In particular, since 2021, the number of companies audited by small and medium-sized audit firms has increased due to changes in auditors, resulting in a significant increase in revenue from audit and attestation services. For changes in accounting auditors, see "III. Operation of Audit Firms, E. Acceptance of New Audit Engagements and Changes of Accounting Auditors".

Figure I-2-7: Operating revenues, breakdowns of operating revenues, and proportions of audit and attestation service revenues to total operating revenues
(Large-sized audit firms (total of four))



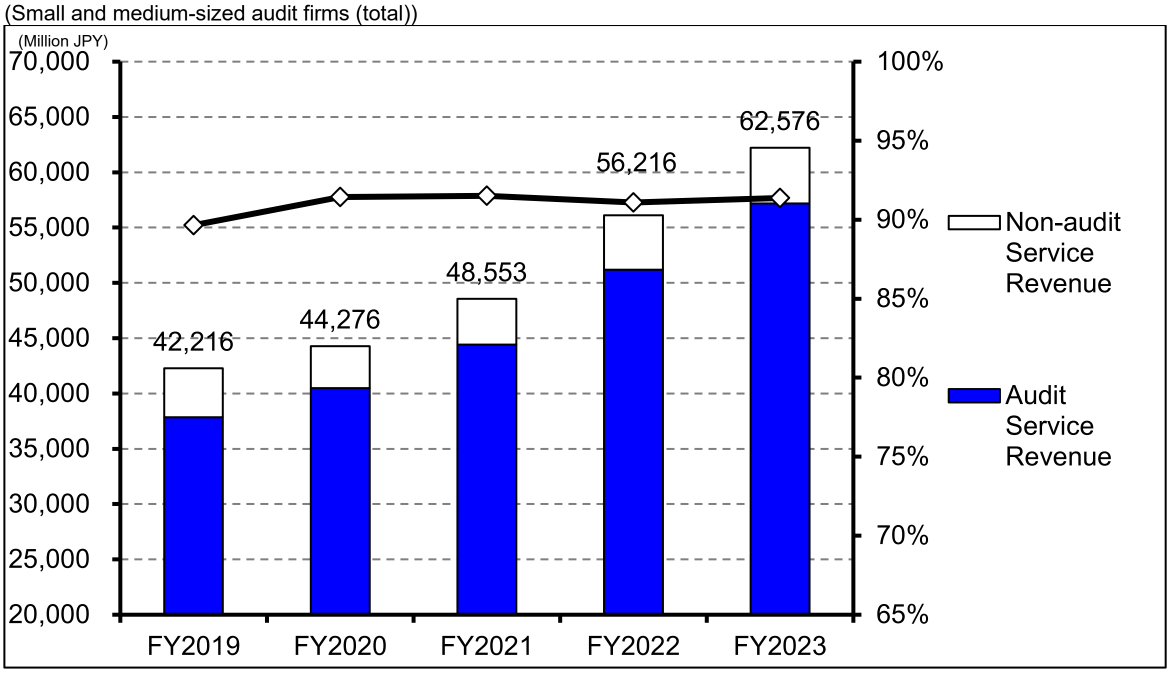
(Note 1) The business reports for FY2020 through 2023 are prepared for the financial year before the establishment of PwC Japan and does not take into account the effects of the merger of PwC Arata and PwC Kyoto.
(Note 2) Revenues and the components thereof increased in FY2024 due to the effects of the establishment of PwC Japan LLC (merger of PwC Aarata and PwC Kyoto).
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

(Mid-tier audit firms (total of four firms))



(Note) While figures for FY2020 through 2023 include PwC Kyoto, revenues and the components thereof decreased in FY2024 due to the effects of the exclusion of PwC Kyoto as a result of its merger with PwC Aarata.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

(Small and medium-sized audit firms (total))



(Note) As fiscal year-end varies widely among small and medium-sized audit firms, their results in FY2024 have yet to be tallied. This report therefore covers their results through FY2023 (from April 2023 through March 2024). The number of small and medium-sized audit firms differs each fiscal year. For FY2023, the results of 271 firms were tallied.

(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

C. Audited Companies

1. Types of Audit and Attestation Services

As previously noted in "B. Audit Firms", audit and attestation services include statutory audits, which are based on such laws as the FIEA, the Companies Act, the Act on Subsidies for Private Schools, and the Labor Union Act and non-statutory audits whose objectives and content are decided by the parties involved. The types of audit and attestation services provided by audit firms are shown below (Figure I-3-1).

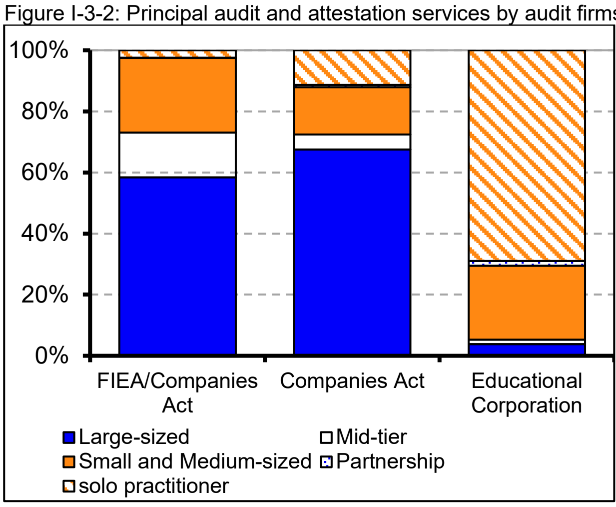
Figure I-3-1: Types of audit and attestation services by audit firm

Type	Statutory audits						Non-statutory audits	Total
	FIEA / Companies Act	FIEA	Companies Act	Act on Subsidies for Private Schools	Labor Union Act	Other		
Number of companies	4,093	291	5,543	1,540	433	4,498	5,729	22,127
Percentage	18.5	1.3	25.0	7.0	2.0	20.3	25.9	100.0

(Note 1) The number of audited companies has been aggregated from operational reports submitted by audit firms in FY2023
(Note 2) "FIEA/Companies Act" denotes operations where audit and attestation under both the FIEA and Companies Act are required, while "FIEA" and "Companies Act" denote operations where audit and attestation under the respective act only is required.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

Audit firms, partnerships and solo practitioners are the entities that provide audit and attestation services. Looking at the entities providing audit and attestation services, about 60-70% of FIEA/Companies Act audits and Companies Act audits are conducted by large-sized audit firms, while about 70% of educational corporation audits are conducted by solo practitioners (Figure I-3-2).

Figure I-3-2: Principal audit and attestation services by audit firms' types (unit: companies)



Type		FIEA/Companies Act	Companies Act	Educational Corporation
Audit firms		4,137	5,496	1,407
(Breakdown)	Large-sized	(2,478)	(4,215)	(180)
	Mid-tier	(626)	(310)	(71)
	Small and medium-sized	(1,033)	(971)	(1,156)
Partnership		7	43	74
Solo practitioner		103	709	3,295

(Note 1) Data was aggregated from audits conducted from the term ended April 2023 to the term ended March 2024. The figures do not match with the figures in Figure I-3-1 because the collection period is different.
(Note 2) The figures in the column "FIEA/Companies Act" include services requiring audit and attestation only under the FIEA, in addition to services requiring audit and attestation under the FIEA and the Companies Act.
(Source) Prepared by the CPAAOB based on data from the JICPA

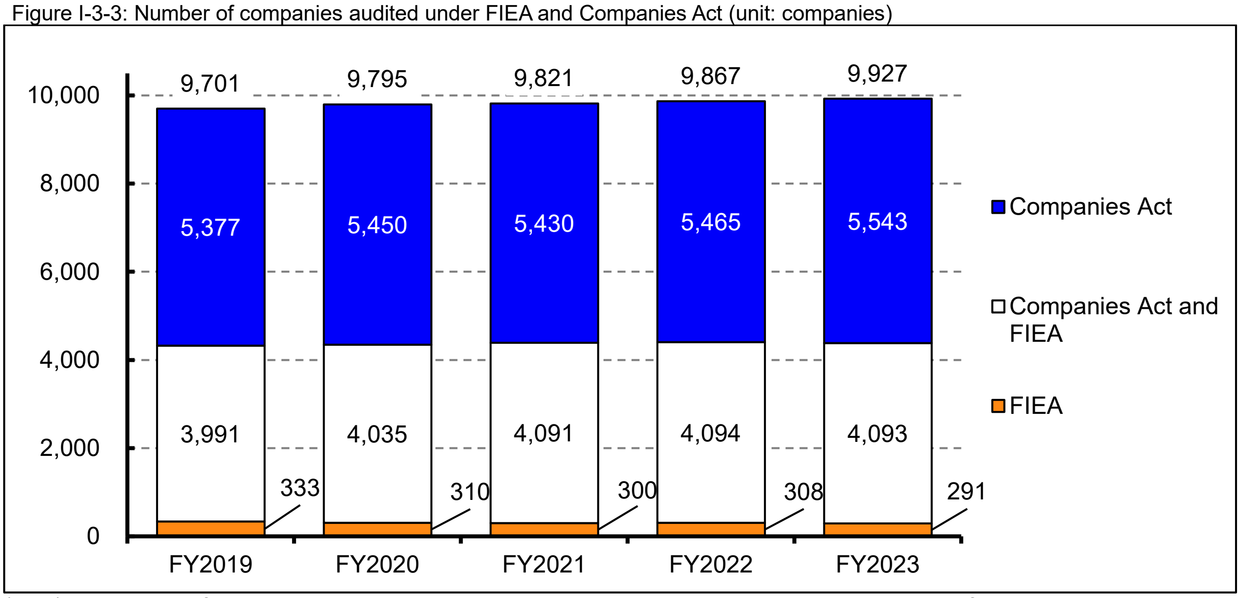
2. FIEA and Companies Act Audits

The results of analysis of audited companies etc. and listed companies that are subject to statutory audits under the FIEA and the Companies Act are as follows:

a. Number of companies audited under the FIEA and the Companies Act and share by scale of audit firm

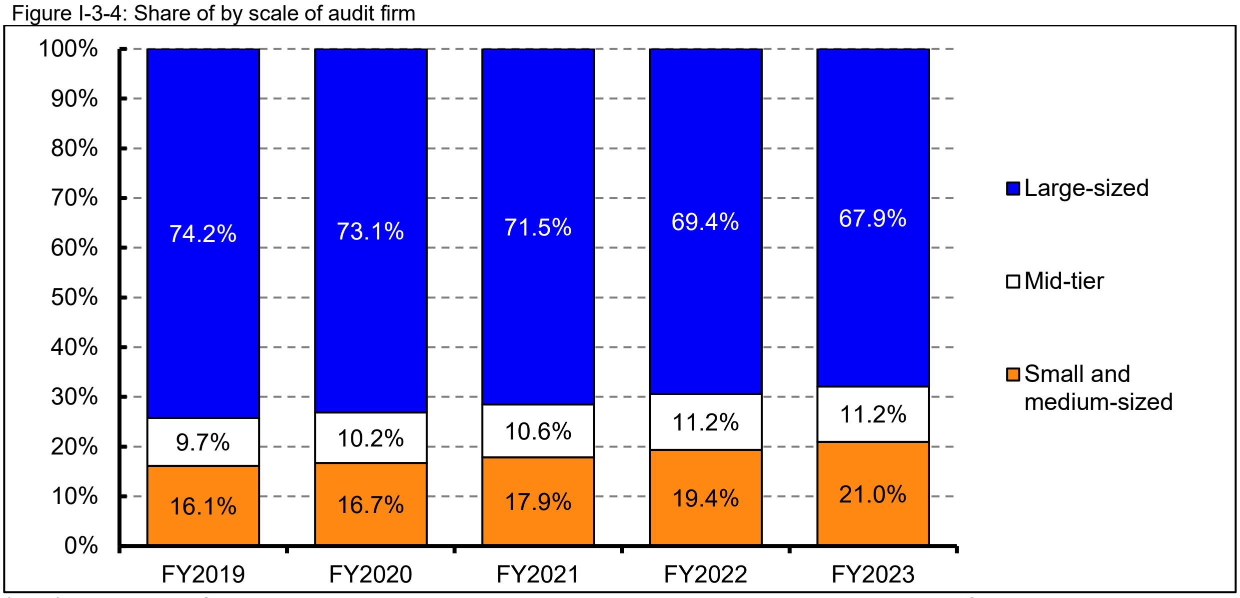
There has been no significant change in the number of companies audited under the FIEA or the Companies Act (Figure I-3-3). With regard to share by scale of audit firm, large-sized audit firms' share has been going down, mid-tier and small and medium-sized audit firms' share have been going up annually (Figure I-3-4).

Figure I-3-3: Number of companies audited under FIEA and Companies Act (unit: companies)



(Note) The number of audited companies is compiled based on operational reports submitted by audit firms.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

Figure I-3-4: Share of by scale of audit firm



(Note) The number of audited companies is compiled based on operational reports submitted by audit firms.
(Source) Prepared by the CPAAOB based on operational reports submitted by audit firms.

b. Share of listed domestic companies by scale of audit firms

The auditors of 3,930 domestic listed companies at the end of FY2023 are as follows.

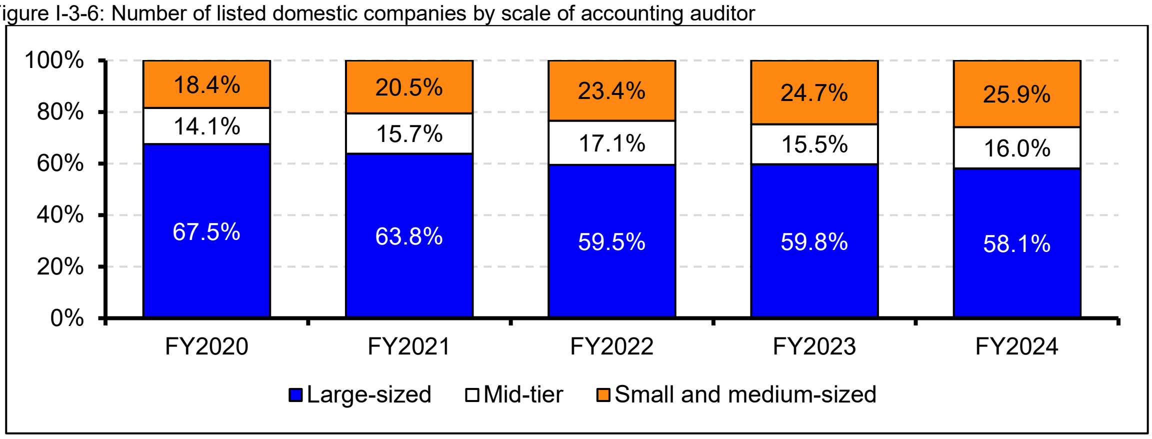
Figure I-3-5: Number and market capitalization of listed domestic companies by scale of auditor (as of the end of March 2025)

	Domestic listed companies	
	Number of companies	Market capitalization (billion yen)
large-sized audit firms	2,278	904,812.3
Mid-tier audit firms	627	23,640.3
Small and medium-sized audit firms	1,017	27,569.2
Total	3,922	956,021.9

(Source) Prepared by the CPAAOB based on data from Quick and exchanges

Although large-sized audit firms have been gradually reducing their share on the basis of the number of companies, they still audit approximately 60% of listed domestic companies and approximately 90% on the basis of market capitalization, a trend that has continued from the past. This is likely due to the fact that listed domestic companies with large market capitalizations tend to have large, complex, and international operations, and their audits require a large number of audit personnel and diverse expert capabilities, making it difficult for audit firms other than large-sized audit firms to handle such audits (Figures I-3-6 and I-3-7).

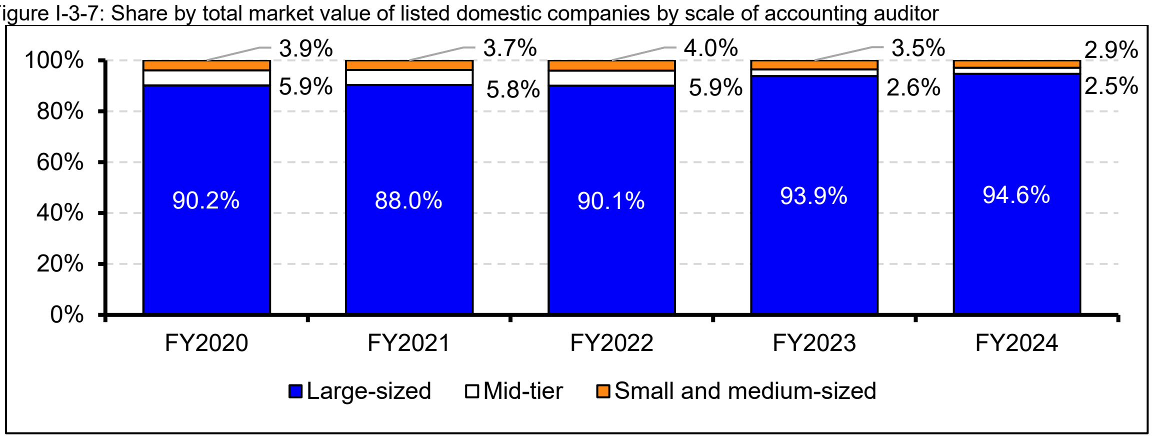
Figure I-3-6: Number of listed domestic companies by scale of accounting auditor



(Note) The number of listed domestic companies audited by mid-tier audit firms up to FY2022 is the total of five audit firms: Gyosei & Co., BDO Sanyu & Co., Grant Thornton Taiyo LLC, Crowe Toyo & Co, and PwC Kyoto. The numbers of listed domestic companies audited by mid-tier audit firms after FY2023 are the total of four audit corporations: Gyosei & Co., BDO Sanyu & Co., Grant Thornton Taiyo LLC, and Crowe Toyo & Co., due to the merger of PwC Arata and PwC Kyoto in December 2023.

(Source) Prepared by the CPAAOB based on data from Quick and exchanges

Figure I-3-7: Share by total market value of listed domestic companies by scale of accounting auditor



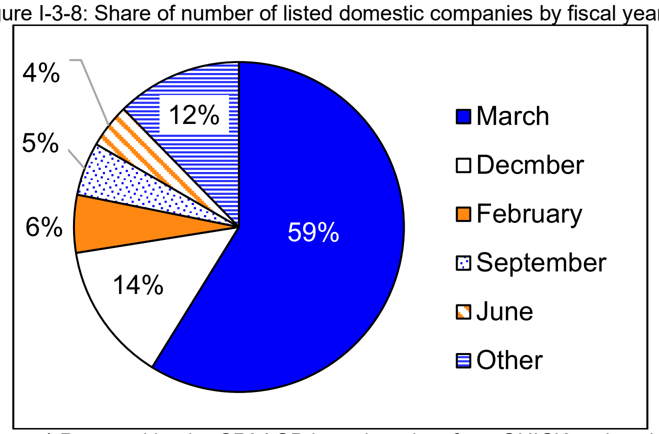
(Note) The number of listed domestic companies audited by mid-tier audit firms up to FY2022 is the total of five audit firms: Gyosei & Co., BDO Sanyu & Co., Grant Thornton Taiyo LLC, Crowe Toyo & Co, and PwC Kyoto. The numbers of listed domestic companies audited by mid-tier audit firms after FY2023 are the total of four audit corporations: Gyosei & Co., BDO Sanyu & Co., Grant Thornton Taiyo LLC, and Crowe Toyo & Co., due to the merger of PwC Arata and PwC Kyoto in December 2023.

(Source) Prepared by the CPAAOB based on data from Quick and exchanges

c. Number of listed domestic companies and total market value by fiscal year-end

59% of listed domestic companies close their books at the end of March, and that they account for 80% of the total market capitalization. This fact explains why audit operations are heavily concentrated in specific periods (Figures I-3-8 and I-3-9).

Figure I-3-8: Share of number of listed domestic companies by fiscal year-end (March 31, 2025) (unit: companies)

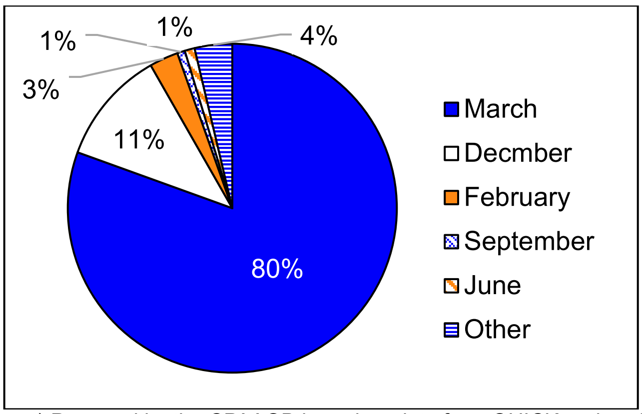


March	2,307
December	536
February	222
September	205
June	169
Other	483
Total	3,922

(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

Figure I-3-9: Share of market value of listed domestic companies by fiscal year-end (March 31, 2025)

(unit: hundred million JPY)



March	7,697,633
December	1,073,356
February	271,076
September	72,355
June	93,038
Other	352,758
Total	9,560,219

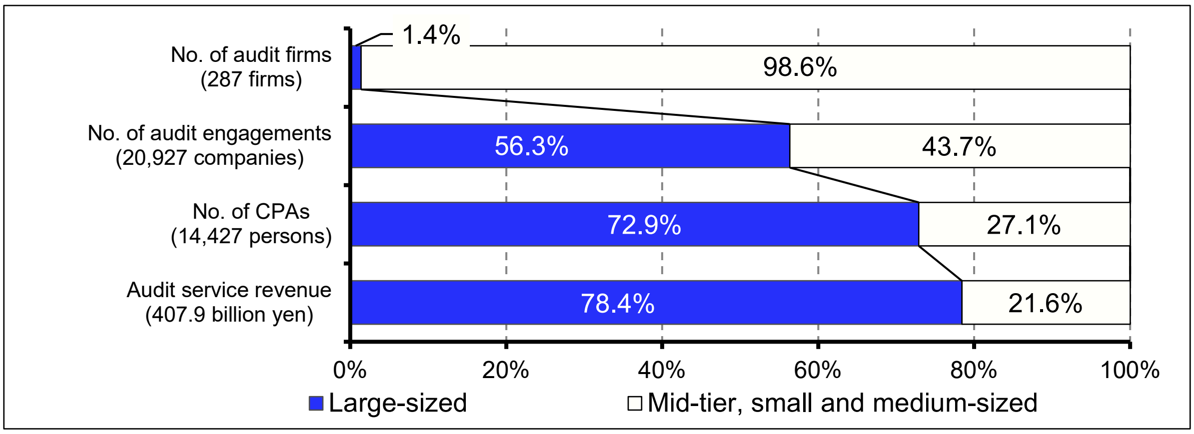
(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

■ Share of large-sized audit firms ■

Among the 287 audit firms as of the end of FY2023, large-sized audit firms accounted for a large portion of the number of audit and attestation engagements, the number of CPAs and audit and attestation service revenues.

The share of large-sized audit firms in the number of audit and attestation engagements, audit service revenues and other categories has been on the decline in recent years as a result of operations management related to the continuation of their audit service contracts. See "III. Operation of Audit Firms, E. Acceptance of New Audit Engagements and Changes of Accounting Auditors".

< Share by category of audit firm (FY2023) >



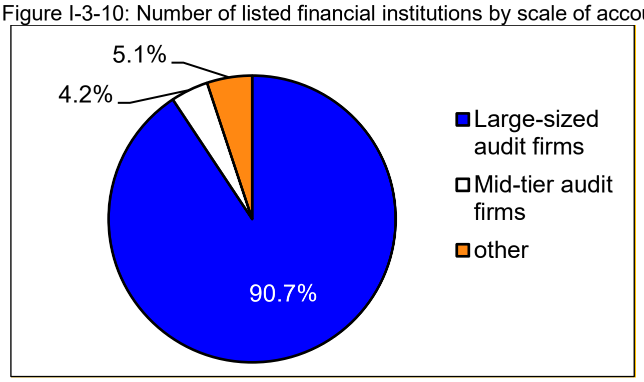
(Note) Compiled based on FY2023 JICPA member data and operational reports submitted by audit firms

3. Audits of Financial Institutions

90% of listed financial institutions (118 companies) were audited by large-sized audit firms, and in terms of market capitalization, large-sized audit firms handled 99%. So compared with all domestic listed companies, large-sized audit firms' share presented a further increase (Figures I-3-10 and I-3-11). For information about domestic listed firms as a whole, see "2. FIEA and Companies Act Audits".

To cope with accounting and audit practices that are designed to the listed financial institutions, large-sized audit firms are establishing departments specializing in financial services in their audit operations divisions, and some mid-tier audit firms have established support systems that specialize in handling inquiries about the accounting procedures of financial institutions.

Figure I-3-10: Number of listed financial institutions by scale of accounting auditor (As of March 31, 2025)

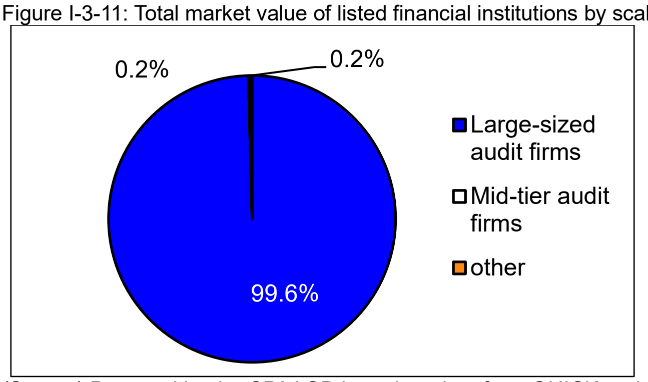


(unit: companies)

Large-sized audit firms	107
Mid-tier audit firms	5
Small and medium-sized audit firms, partnerships and solo practitioners	6
Total	118

(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

Figure I-3-11: Total market value of listed financial institutions by scale of accounting auditor (As of March 31, 2025)



(unit: hundred million JPY)

Large-sized audit firms	1,112,514
Mid-tier audit firms	2,377
Small and medium-sized audit firms, partnerships and solo practitioners	2,278
Total	1,117,171

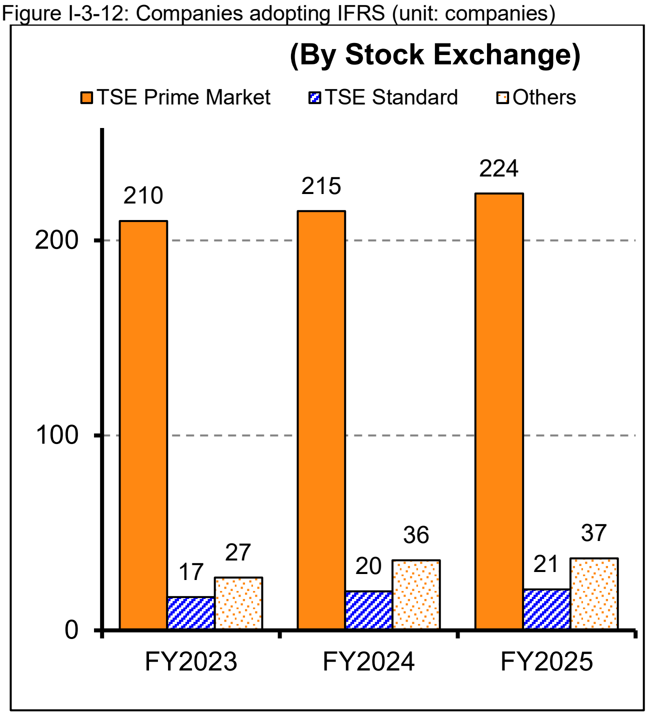
(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

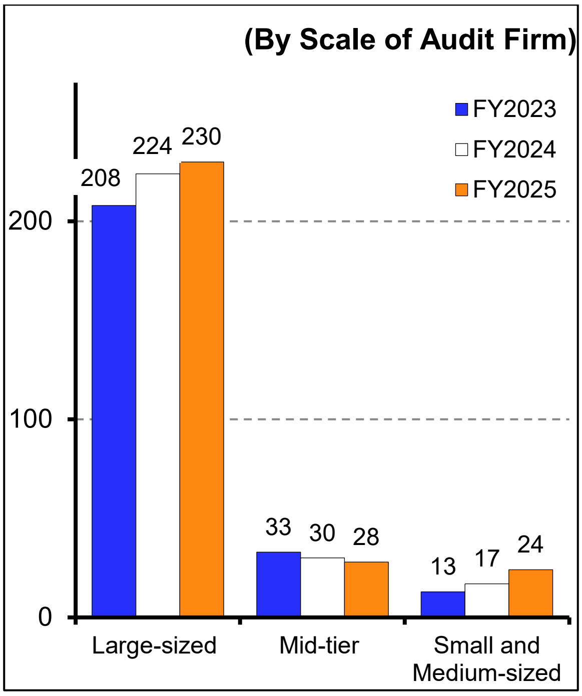
4. Companies Adopting IFRS

The following figures show the listing markets for companies that have adopted IFRS and the scale of the accounting auditors for these companies as of the end of March 2025 (Figures I-3-12).

The majority of companies that have adopted IFRS are listed on the Prime Section of the Tokyo Stock Exchange, and many of them operate internationally. Audit contracts are concentrated in large-sized audit firms which collaborate with large global networks. A similar situation is seen with companies that have decided to adopt IFRS (companies in which the business execution body has decided to adopt IFRS and has disclosed this decision to the public) (Figure I-3-13).

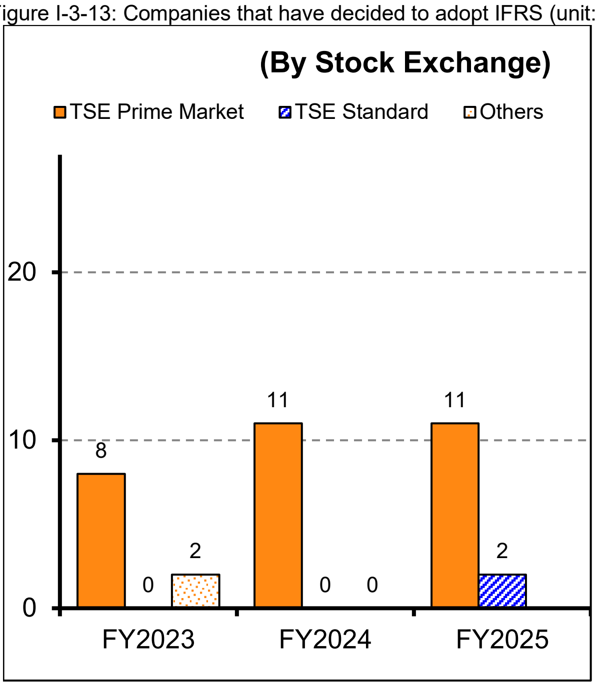
Figure I-3-12: Companies adopting IFRS (unit: companies)

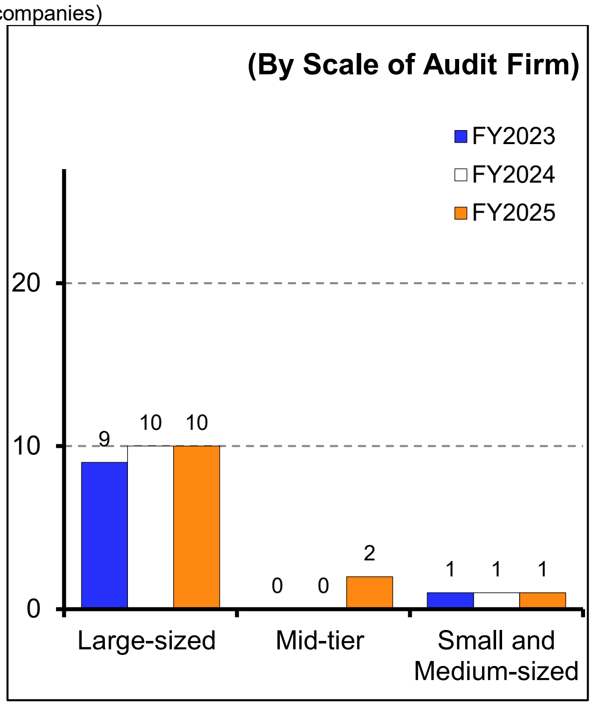




(Note) PwC Arata and PwC Kyoto merged on December 1, 2023 to form PwC Japan, and the former PwC Kyoto is classified as a large-sized audit firm for the fiscal year ended March 31, 2006 in the status of Scale of Audit Firm.
(Source) Prepared by the CPAAOB based on data from exchanges

Figure I-3-13: Companies that have decided to adopt IFRS (unit: companies)





(Note) PwC Arata and PwC Kyoto merged on December 1, 2023 to form PwC Japan, and the former PwC Kyoto is classified as a large-sized audit firm for the fiscal year ended March 31, 2006 in the status of Scale of Audit Firm.
(Source) Prepared by the CPAAOB based on data from exchanges

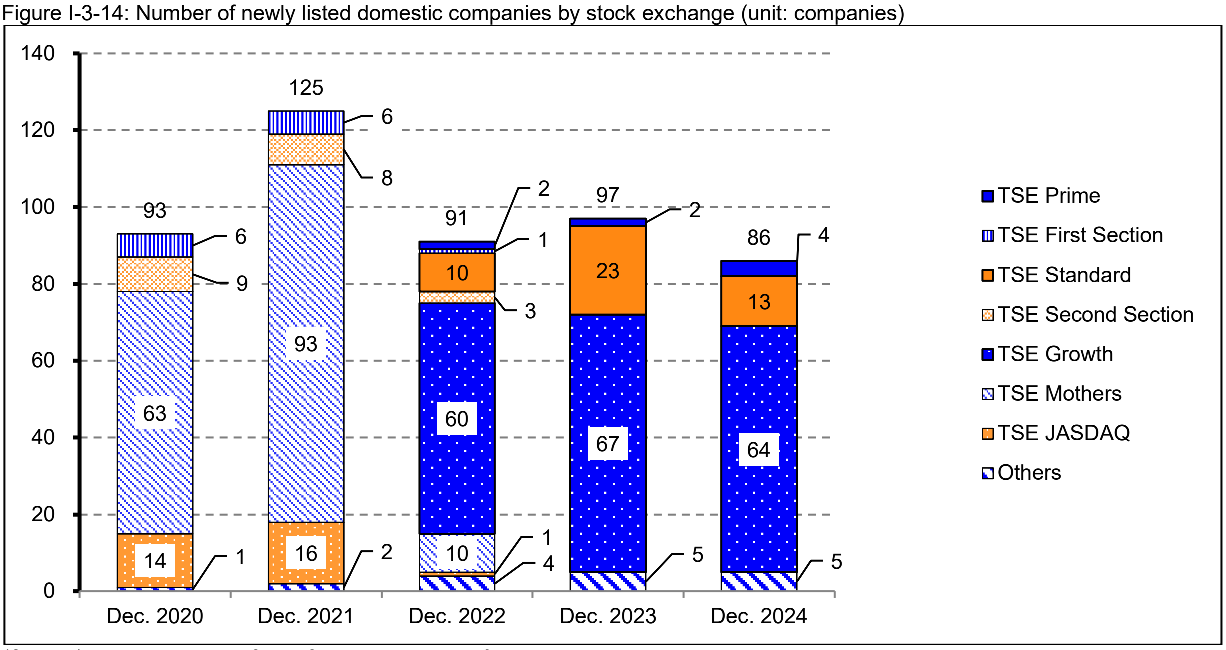
5. Audits of Initial Public Offerings

The number of IPOs (excluding listings on the Tokyo Pro Market) for the period from January 2024 to December 2024 (hereinafter referred to as the "year through December 2024") came to 86, which has decreased from the previous year. Listings on the Tokyo Stock Exchange Standard and Growth market were particularly large in number (Figure I-3-14).

Seeing shares by size of audit firms, large-sized audit firms maintain a large share (Figure I-3-15). However, the shares held by each of the large-sized audit firms have changed, which likely reflects changes in the business operation policies and IPO related operations embedded in each firm. For information about the organizational structures, etc. of audit firms regarding the acceptance of IPO audit engagements, see "III. Operation of Audit Firms, A. Operations Management System, 4. Organizational Structure for Providing Audit Services".

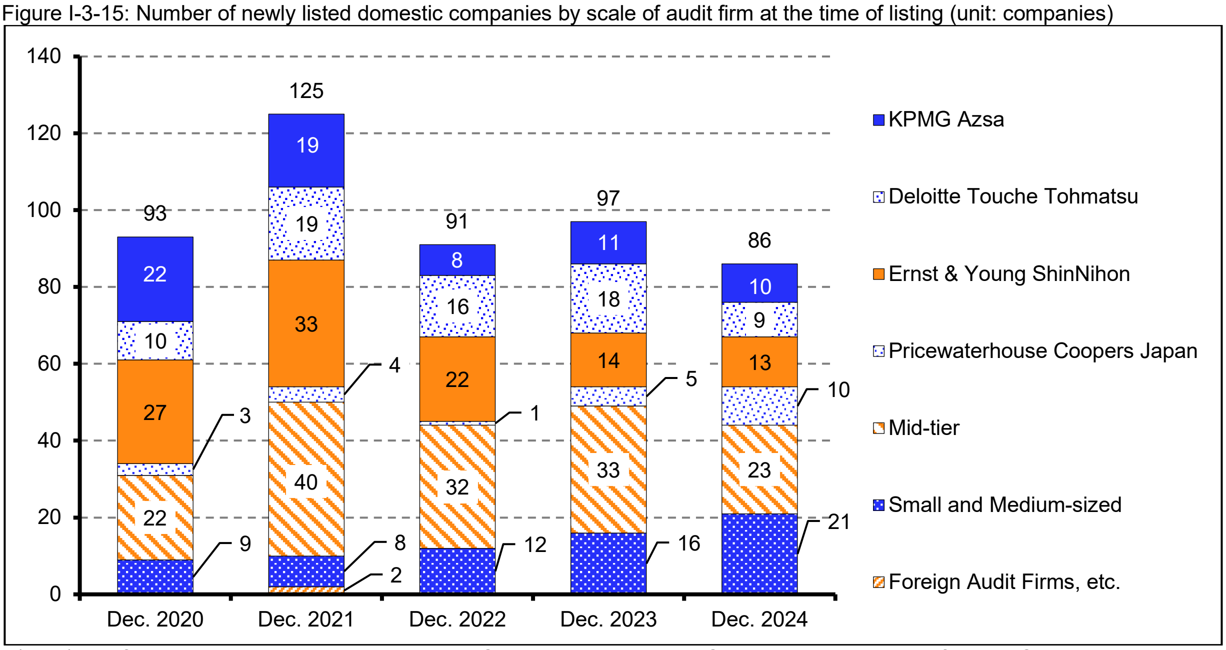
As of December 31, 2024, the share of large-sized audit firms was 49%, which is almost the same as the previous year. On the other hand, while the share of mid-tier audit firms declined from 34% to 27%, the share of small and medium-sized audit firms increased from 16% to 24%.

Figure I-3-14: Number of newly listed domestic companies by stock exchange (unit: companies)



(Source) Prepared by the CPAAOB based on data from exchanges

Figure I-3-15: Number of newly listed domestic companies by scale of audit firm at the time of listing (unit: companies)

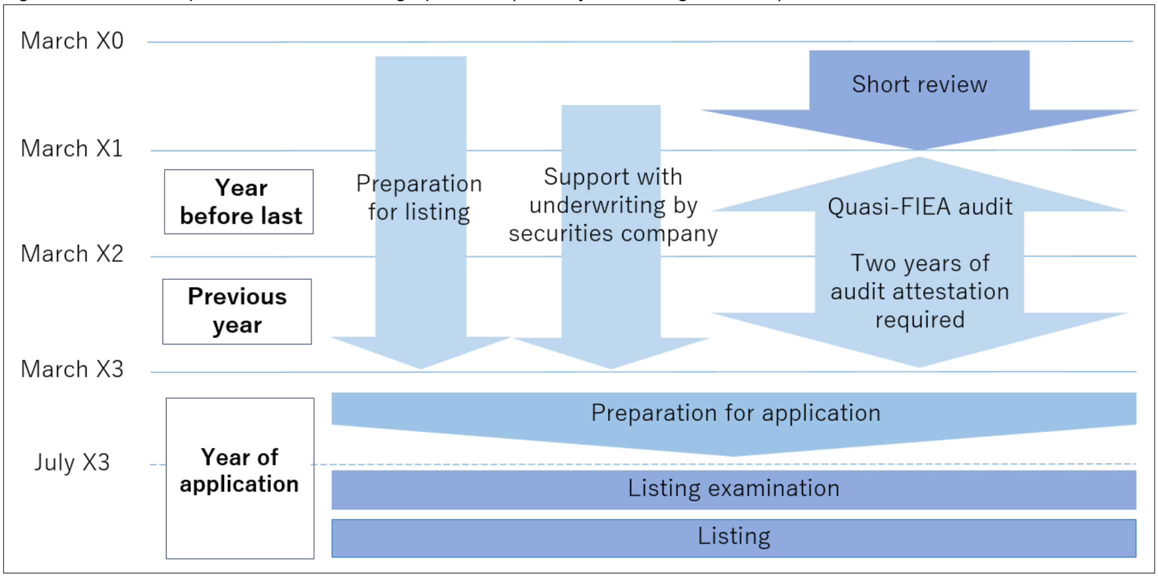


(Note) As of December 1, 2023, PricewaterhouseCoopers Aarata and PwC Kyoto were merged to form PwC Japan. As a result, the company that PwC Kyoto before the merger was involved in the IPO is classified as a mid-tier firm.
(Source) Prepared by the CPAAOB based on data from exchanges

Most audit firms regard the acceptance of IPO audit engagements as a part of their mission of audit firms since assisting with IPOs contributes not only to companies' growth but also to socioeconomic development.

However, IPO audits often entail a relatively high audit risk, such as vulnerable internal control structure of the audited company, and there are cases where improper accounting had already been practiced by the time of IPO. Accordingly, Many audit firms have a policy of more carefully considering engagement risks than usual when accepting IPO audit engagements.

Figure I-3-16: Example of schedule leading up to IPO (Fiscal year ending in March)



(Source) Prepared by the CPAAOB

■ IPO support services ■

Article 192-2, paragraph of the FIEA stipulate that for listing, a company needs to have its financial statements audited for the two years prior to the year in which it will be listed (application year). (This type of audit is described as "quasi-FIEA audit"). Furthermore, before concluding a quasi-FIEA audit contract, a short review is conducted so as to identify and resolve issues ahead of listing. This is the typical workflow when preparing for listing. Companies often ask CPAs and audit firms for support with conducting the short review and resolving issues, and CPAs and audit firms accept these engagements as non-audit work. The IPO-related support services that CPAs and audit firms provide as non-audit work include the following:

- Short reviews
- Support with establishing management structures
- Support with establishing internal control structures
- Support with speeding up bookclosing procedures
- Support with preparing listing application documentation

According to the collection of reports from small and medium-sized audit firms (all of which are small and medium-sized audit firms, covering 52 firms), the percentage of responses that audit firms "provide audit services" or "provide non-audit services" to IPO preparation companies was 65% of all responses in PY2023, but increased to 72% in PY2024. As indicated by the aforementioned shares by size of audit firm at the time of listing, opportunities for small and medium-sized audit firms to provide services to IPO preparation companies are on the rise. In addition, some small and medium-sized audit firms have continued to achieve significant growth due to their management policies focusing on providing services to IPO preparation companies.

The CPAAOB will continue to examine whether there are any problems with the provision of audit services to IPO preparation companies, etc. through inspections and the collection of reports from small and medium-sized audit firms.