IV. Responses to Changes in the Global Environment Surrounding Audits

IV. Responses to Changes in the Global Environment Surrounding Audits

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, while the number of listed domestic companies in Japan has been declining, the trend of changing accounting auditors from large-sized audit firms to mid-tier and small and medium-sized audit firms has continued. In particular, small and medium-sized audit firms currently provide audit services to approximately 28% of listed domestic companies (around 1,050 companies on a company basis). Moreover, the number of newly listed domestic companies appointing such firms as their accounting auditors has increased year by year. Accordingly, the role expected of these firms in the capital markets has become increasingly important.

Against this backdrop, the Quality Control Standards became fully applicable to audits of fiscal years beginning on or after July 2024. In addition, the JICPA Code of Ethics, which was amended in July 2022 to strengthen regulations related to independence, was further revised in July 2024 with respect to the definition of engagement teams, provisions relating to group audit engagements, and other matters. As a result, small and medium-sized audit firms are required not only to establish systems to provide audit services to listed domestic companies but also to appropriately implement and operate the system of quality management and respond to strengthened independence requirements concerning audit fees, non-audit fees, fee dependency, and the concurrent provision of non-assurance services.

Furthermore, small and medium-sized audit firms face challenges in securing and developing human resources and maintaining financial resources, particularly in response to the digitalization of audit services, including the digitalization of audit documentation, the increasing complexity of audit procedures relating to areas such as crypto-assets, and the expansion of service areas, including assurance over sustainability-related information.

Moreover, in light of changes in the economic and social environment surrounding accounting audits, including the expansion of the base of auditors for listed domestic companies, the CPA Act was revised in May 2022 and introduced a statutory Registration System for Auditors of Listed Companies. Under the Revised Ordinance for Enforcement of the CPA Act, audit firms conducting audits of listed companies are required to establish systems for enhanced information disclosure and to conduct business operations in accordance with the Audit Firm Governance Code (revised in March 2023). These requirements became applicable to small and medium-sized audit firms registered as auditors of listed companies from the beginning of the first accounting period of audited companies commencing on or after July 1, 2024.

In addition, cases have emerged in which accounting fraud had been committed since the initial public offering application stage at listed domestic companies audited by small and medium-sized audit firms, raising concerns regarding the quality of audits performed by such firms.

2. Response by the JICPA to Small and Medium-Sized Audit Firms

a. Operational status of the Registration System for Auditors of Listed Companies

The registration of audit firms conducting audits of listed domestic companies had previously been administered by the Quality Control Committee of the JICPA as part of its self-regulatory activities. However, following the introduction of the statutory Registration System for Auditors of Listed Companies on April 1, 2023, Review for Application Review, Review for Revocation of Registration, and deliberations on matters necessary for the operation of the system have been conducted by the Registration Review Committee for Auditors of Listed Companies (“Registration Review Committee”), which consists of seven members, including three JICPA members and four non-members.

The Registration System for Auditors of Listed Companies is designed to contribute to the reliability of financial audits by:

(i) Registering audit firms conducting audits of listed companies on a legally mandated list of auditors of listed companies (“List of Auditors of Listed Companies”),
(ii) Requiring a high level of discipline from registered auditors of listed companies (“Registered Auditors of Listed Companies”),
(iii) Requiring the JICPA to verify through confirmation of eligibility, whether Registered Auditors of Listed Companies are fulfilling such responsibilities, and
(iv) Revoking registrations when necessary.

The JICPA receives applications from audit firms seeking registration (“Applicant Firms”) and conducts a Review for Application Review to assess the status of their systems of quality management. The JICPA also conducts confirmations of eligibility through the Quality Control Review, including the Review for Application Review, to determine whether the Applicant Firms or Registered Auditors of Listed Companies have systems sufficient to fairly and appropriately perform audit attestation services relating to the financial statements of listed companies. Based on the results of these reviews and confirmations of eligibility, the Registration Review Committee decides whether the registration should be approved or revoked.

In June 2023, the JICPA published the Eligibility Confirmation Guideline, which outlines viewpoints and criteria for review teams to consider when confirming eligibility. At the same time, Applicant Firms and Registered Auditors of Listed Companies are expected to conduct self-assessments against the conditions set out in the Eligibility Confirmation Guideline, and if any deficiencies are identified, to promptly develop and implement voluntary improvement measures. This Guideline was subsequently revised in August 2024 and June 2025 to reflect, among other things, the application of the Revised Quality Control Standards, discussions within the Registration Review Committee, and experience gained through Quality Control Review. These revisions included the reorganization of items and the addition of new viewpoints and criteria.

Audit firms that were conducting audits of listed companies as of April 1, 2023 were designated as

Deemed Registered Auditors of Listed Companies (“Deemed Registered Auditors”) under transitional measures and were permitted to continue providing audit attestation services until September 30, 2024. The JICPA stated that, from October 1, 2024, such firms would be categorized either as “Firms to be examined by the Registration Review Committee” or as “Firms whose registration applications were denied but that continued to audit listed companies.” On July 3, 2025, the JICPA announced that it had completed the Reviews for Application Review of all Deemed Registered Auditors. Accordingly, after that date, the only remaining Deemed Registered Auditors were the “Firms whose registration applications were denied but that continued to audit listed companies.”

The Registration Review Committee held a total of 40 meetings between April 2023 and June 2026. During this period, 130 audit firms (including 10 firms that newly applied for registration and were not Deemed Registered Auditors) were registered on the List of Auditors of Listed Companies. As of the end of June 2026, one audit firm remained a Deemed Registered Auditor. On July 2, 2026, however, it was announced that a temporary accounting auditor would be appointed at the listed audited company for which the successor accounting auditor had not yet been determined, and it was confirmed that this Deemed Registered Auditor would no longer perform the audit engagement. As a result, the number of Deemed Registered Auditors has fallen to zero[50].

b. Framework for supporting small and medium-sized audit firms

(i) Small Medium Practices Policy Committee

The Small Medium Practices Policy Committee considers measures to facilitate the smooth performance of services provided by small and medium-sized audit firms and to promote continuous improvement. The following committees have been established under this Committee:

[Audit and Ethics Standards Subcommittee]

- Considers publications and guidance materials to support appropriate compliance with the JICPA Code of Ethics, auditing standards and guidelines, and other relevant requirements, with the aim of maintaining and enhancing audit quality.

[IT Support Subcommittee for Small and Medium-Sized Audit Firms]

- Assesses the status of IT infrastructure development and the use of IT-based audit methodologies.
- Provides support for the enhancement of IT infrastructure, including cybersecurity measures, and for the development of audit tools utilizing information technology.

[International Affairs Subcommittee]

- Monitors developments in international standards through discussions conducted by the International Ethics Standards Board for Accountants (IESBA) and the International Federation of Accountants (IFAC) and shares information with small and medium-sized audit firms at an early stage to facilitate the smooth implementation of international standards.
- Communicates views from the perspective of small and medium-sized audit firms on matters

[50] Although this event occurred shortly after the end of the FY2025 inspection year, it is reflected here because of its close relevance to the circumstances discussed above.

that may affect audit practice in Japan.

[Accounting Subcommittee]

- Supports the application of accounting standards, including IFRS, prepares disclosure and presentation checklists for annual securities reports, and develops training materials related to audit responses associated with enhanced corporate disclosure requirements.

[Sustainability Information Support Committee for Small and Medium-Sized Audit Firms]

- Collects and provides information necessary to help small and medium-sized audit firms appropriately address sustainability-related information and other emerging reporting matters.

(ii) Small and Medium-Sized Audit Firms Liaison Council

The Small and Medium-sized Audit Firms Liaison Council operates on a voluntary membership basis and, in principle, is open to small and medium-sized audit firms conducting audits of listed companies. As part of efforts to maintain and enhance the quality of audit firms and audit engagements, the Council provides information and support on an ongoing basis. The following subcommittee and two working groups have been established under the Council:

[Subcommittee on Strengthening the Foundations of Small and Medium-sized Audit Firms]

- Established to promote various initiatives undertaken by the JICPA, in a robust and organized manner, to strengthen the operational foundations of small and medium-sized audit firms.
- Determines overall policies for enhancing disclosures and strengthening firm foundations and monitors various support measures aimed at strengthening those foundations.

[Working Group on Auditor Recruitment and Development]

- Established to support the recruitment and development of personnel at small and medium-sized audit firms.
- Prepares recruitment brochures for small and medium-sized audit firms and distributes them to professional schools, universities, and accounting colleges, and organizes networking events for young CPAs working at small and medium-sized audit firms.

[Working Group on Audit Firm Support]

- Established to support improvements in audit quality and enhance consultation services for small and medium-sized audit firms.
- Operates a consultation desk for matters relating to compliance with the Guideline for the Confirmation of Eligibility, and plans and administers interactive training programs aimed at improving audit quality.

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

The JICPA, primarily through the Small Medium Practices Policy Committee and the Small and Medium-Sized Audit Firms Liaison Council, implements various initiatives to strengthen the operational foundations of small and medium-sized audit firms that audit listed companies and other public interest entities. These initiatives include: (i) support for enhanced transparency and disclosure; (ii) support for improving audit quality and enhancing consultation functions; (iii) support for

digitalization; (iv) support for implementation of the revised Quality Control Standards; (v) training programs relating to the revised JICPA Code of Ethics; (vi) support for recruitment and development of personnel; (vii) maintenance of directories of overseas firms; (viii) dialogue with capital market stakeholders; and (ix) regular opinion exchange meetings. The principal initiatives are outlined below.

(i) Support for enhanced transparency and disclosure

- Prepared and published the Guidance for Preparing Annual Reports on Audit Quality Management and conducted training sessions through regional chapters.
- Reviewed draft (dry-run) versions of annual reports on audit quality management and provided feedback on the results.
- Conducted reviews of the finalized annual reports on audit quality management and collected related data.
- Compiled common observations and good practices identified across multiple audit firms and shared them with member firms of the Small and Medium-Sized Audit Firms Liaison Council.
- Held study sessions with external experts on topics such as the Audit Firm Governance Code and published the related materials on the JICPA website.
- Established a consultation desk to respond to inquiries relating to disclosure matters.
- Supported the preparation of video messages from firm leadership to facilitate implementation of the Audit Firm Governance Code.
- Established the “Top Message Website for Small and Medium-sized Audit Firms Auditing Listed Companies”, which publishes firms’ annual reports on audit quality management, information on the application of the Audit Firm Governance Code, and explanatory documents together with leadership messages and related videos.

(ii) Support for improving audit quality and enhancing consultation functions

- Conducted interactive training programs designed to improve audit quality while also strengthening individual consultation functions. Topics covered in FY2025 included audit firm quality management, evaluation of systems of quality management, organization and retention of audit documentation, information security, audit execution (including IT audits), risk assessment and response procedures, audit of accounting estimates, and group audits.
- Conducted training programs tailored to small and medium-sized audit firms, including seminars on audit risk and accounting fraud, updates on auditing and quality management standards, IFRS, and sustainability-related matters.
- Established a consultation desk to provide advice on the development of appropriate audit firm governance and operational structures.

(iii) Support for digitalization

- Held regular IT Community meetings to facilitate information sharing on the introduction of IT infrastructure and audit tools, with participation typically ranging from 200 to 300 IT professionals and practitioners.

- Established a consultation desk to advise on audit firm infrastructure, including IT environments and the digitalization of electronic audit documentation.
- Conducted surveys on the status of IT infrastructure, digital transformation (DX), and the use of generative AI, and shared the results through the IT Community.

(iv) Support for recruitment and human resource development

- Prepared, published, and distributed the recruitment brochure Employment Guidebook for Small and Medium-sized Audit Firms.
- Organized networking events for young CPAs working at small and medium-sized audit firms.
- Beginning in FY2026, plans to provide training programs for audit assistants who have not passed the CPA Examination, in cooperation with the Accounting Education and Learning Foundation.

(v) Regular dialogue and exchange of views

- Held a number of roundtable meetings between the JICPA President, Vice Presidents and Executive Board Members responsible for supporting small and medium-sized audit firms, and representatives of such firms.
- Gathered views and feedback on challenges faced by individual firms and communicated the JICPA's expectations regarding firm scale and organizational capacity necessary to maintain an appropriate level of audit quality.

d. Support within the audit industry involving the JICPA

The Audit Confirmation Center GK, established through joint investment by large-sized audit firms, provides a digitalization platform for balance confirmation procedures that focuses on standardizing and improving the efficiency of audit operations, accelerating confirmation procedures, and ensuring a high-level of security. Traditionally, the process required sending, responding to, and collecting confirmation letters in paper form. However, by utilizing this platform, it has become possible to send electronic confirmation letters and receive responses via the web.

The electronic confirmation letters cover balances such as accounts receivable and payable, bank transaction balances, and securities transaction balances. As of June 2026, the platform was being used by more than 160 audit firms, including approximately 80 small and medium-sized audit firms. One factor that may have contributed to the increased adoption of the platform among small and medium-sized audit firms is the regular dissemination of information on the platform through the IT Community organized by the JICPA.

The Audit Digital & Innovation Consortium LLC (ADIC), established through joint investment by one mid-tier audit firm, two small and medium-sized audit corporations, and one business corporation, provides small and medium-sized audit corporations with a shared IT infrastructure environment that enables the use of electronic audit working paper systems, as well as digital transformation tools designed to enhance the effectiveness and efficiency of audit engagements.

ADIC was established with the advice and cooperation of the JICPA, and the JICPA continues to

support the development of a shared IT infrastructure environment for small and medium-sized audit firms through the provision of information, exchange of opinions, and other forms of assistance.

In addition, the Audit Firms Support Association (AFSA), a general incorporated association established in April 2024 by three mid-tier audit firms and two small and medium-sized audit firms as members, aims to enhance the quality of audit firms and supports their efforts to meet the requirements set forth in the Audit Firm Governance Code and other relevant standards. Its membership consists of audit firms engaging in audits of listed companies. Specifically, the AFSA provides services including independent third-party advice to members, responses by specialists in accounting, auditing and related fields to members' inquiries seeking professional opinions, and support for improvement measures in response to significant findings identified through external inspections. The AFSA also plans to provide support for training related to accounting, auditing, ethics, and other professional matters in the future. The JICPA works in cooperation with the AFSA in providing support to small and medium-sized audit firms aimed at enhancing audit quality.

3. Response by the CPAAOB

The 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 receive the necessary support on a medium- to long-term basis, and that the administrative authority should promote proactive quality management by audit firms through CPAAOB inspections, while supporting the efforts of the JICPA.

As part of its efforts to support small and medium-sized audit firms, the CPAAOB delivered a lecture for the managements of small and medium-sized audit firms in a program entitled *"Strengthening Organizational and On-site Capabilities of Audit Firms"* organized by the Accounting Education and Training Organization, a general incorporated foundation. During the lecture, the CPAAOB explained its expectations regarding sound organizational management.

In addition, the CPAAOB has published the Case Report from Audit Firm Inspection Results and has presented these case studies at training sessions organized by regional chapters of the JICPA. Furthermore, based on the Basic Policy for Monitoring in the 8th Term, the CPAAOB continues to place emphasis on inspections of small and medium-sized audit firms while also supporting their efforts through lectures delivered at seminars and training programs organized by relevant organizations.

B. Recent Trends in Auditing

1. Trends in International Auditing and Assurance Standards and Ethical Standards

The International Auditing and Assurance Standards Board (IAASB) and the IESBA, both established within the International Foundation for Ethics and Audit (IFEA)[51], are engaged in the development of international audit standards, assurance standards, and ethics standards.

Recent major revisions to the International Standards on Auditing (ISA) issued by the IAASB include revised ISA240 (The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements). In March 2025, the IAASB Board approved the finalization of the revised standard, which is effective for audits of financial statements for fiscal years beginning on or after December 15, 2026. The revised ISA240 clarifies the auditor's role and responsibilities in relation to fraud in financial statement audits. It requires auditors to communicate with management and those charged with governance regarding fraud, and to identify matters that they consider to be of particular importance in the audit of the current-periods financial statements as Key Audit Matters.

The revised ISA570 (Going Concern), which was finalized at the IAASB Board meeting held in December 2024 and published in April 2025, is effective for audits of financial statements for fiscal years beginning on or after December 15, 2026. The revised ISA570 requires management's assessment of going concern to cover a period of at least 12 months from the date of approval of the financial statements and requires the auditor's report to include a statement setting out the auditor's conclusion regarding the appropriateness of the going concern basis of accounting.

In addition, in response to calls for integrated project addressing audit evidence and responses to assessed risks, the IAASB decided at its Board meeting in December 2024 to launch a project to revise ISA330 (The Auditor's Responses to Assessed Risks), ISA500 (Audit Evidence) and ISA520 (Analytical Procedures) simultaneously. The project is intended to (i) strengthen auditors' exercise of professional judgment and professional skepticism, (ii) promote greater consistency in audit practice and auditor behavior, and (iii) encourage the use of technology in obtaining audit evidence and assessing its sufficiency and appropriateness. The IAASB aims to finalize the revised standards by December 2026.

Recent developments in international assurance standards issued by the IAASB include the ISSA5000, *General Requirements for Sustainability Assurance Engagements*, which was approved for finalization at the IAASB's September 2024 Board meeting and formally issued in November 2024. ISSA5000 is effective for sustainability assurance engagements relating to periods beginning on or after December 15, 2026, and for engagements as at a specific date on or after December 15, 2026. The standard is designed to be profession-agnostic and applies to all sustainability assurance practitioners, whether professional accountants or otherwise, and to both limited and reasonable assurance engagements.

Recent developments in the IESBA Code of Ethics include the IESBA's approval of revisions to the IESBA Code at its December 2024 Board meeting. Following this approval, the IESBA published in

[51] An organization established in 2022 to replace the International Federation of Accountants (IFAC) as the parent body of the IAASB and IESBA, reflecting the view that standard-setting bodies should be independent from professional accountancy organizations. The transfer of the IAASB and the IESBA to the IFEA was implemented in January 2023.

January 2025 the *International Ethics Standards for Sustainability Assurance Engagements (including International Independence Standards) and Other Revisions to the IESBA Code Relating to Sustainability Assurance and Reporting*, as well as the Revisions to the *IESBA Code Relating to the Use of the Work of an External Expert*. The first introduces, among other changes, a new Part 5 that establishes ethics and independence requirements for sustainability assurance engagements meeting specified criteria and applies to all assurance practitioners, including those who are not professional accountants. The second provides guidance on evaluating the competence, capabilities, and objectivity of external experts whose work is used in situations where expertise other than that possessed by professional accountants or sustainability assurance practitioners is required. The above revisions to the IESBA Code, other than those relating to value chain components, are effective for sustainability assurance engagements covering periods beginning on or after December 15, 2026, or for sustainability-related information reported as of a specific date on or after December 15, 2026. The provisions relating to value chain components are effective for sustainability assurance engagements covering periods beginning on or after July 1, 2028, or for sustainability-related information reported as of a specific date on or after July 1, 2028.

2. Revision of the JICPA Code of Ethics

The JICPA has revised its Code of Ethics in response to changes in the domestic regulatory framework, while also taking into account revisions to the IESBA Code.

In the July 2022 revision, the JICPA undertook a fundamental restructuring of the framework of the JICPA Code of Ethics by integrating the guidance on independence, conflicts of interest, and non-compliance with laws and regulations (NOCLAR) into the JICPA Code of Ethics.

In addition, the independence requirements were strengthened. With respect to fees, where the audit client is a PIE, audit firms are required to disclose fee-related information, including audit and non-audit fees. Furthermore, where fees from a PIE audit client exceed, or are likely to exceed, 15% of the audit firm’s total fees for two consecutive years, an engagement quality review prior to the issuance of the auditor’s report is required as a safeguard, and disclosures relating to fee dependency is also required. Moreover, where fee dependency on a PIE audit client exceeds, or is likely to exceed, 15% for five consecutive years, the auditor is required to resign from the engagement after issuing the auditor’s report for the fifth year.

With respect to non-assurance services, the revised JICPA Code of Ethics provides that, where the audit client is a PIE, the audit firm or network firm shall not provide non-assurance services that may create a self-review threat.

Reflecting the revisions to the JICPA Code of Ethics, the Cabinet Office Ordinance on Audit Certification of Financial Statements, etc. was also amended to require the disclosure, in the auditor’s report, of information relating to fees received by the CPAs or audit firm (including persons and entities within the same network) from the audited entity, including its consolidated and non-consolidated subsidiaries.

The July 2024 revisions primarily included: (i) provisions relating to the definitions of listed entities and PIEs; (ii) provisions relating to the definition of engagement teams and group audit engagements; and (iii) provisions relating to technology (including amendments replacing the term “confidentiality obligation” with “confidentiality”). In addition, the July 2025 revisions introduced, among other changes, new ethical requirements applicable when the JICPA members provide tax planning services, including services involving tax planning, strategy development, and advice.

Further proposed revisions to the JICPA Code of Ethics were published in April 2026. The principal proposals include: (i) the introduction of new ethical requirements for sustainability assurance engagements; and (ii) new provisions relating to the use of the work of external experts.

3. Other Trends in Financial Reporting Systems

a. Responses to individual cases

Shares of domestic company A (Company A), a Japanese company whose principal business was the development and provision of services utilizing generative AI technology, were listed on the Tokyo Stock Exchange Growth Market in October 2024. In April 2025, the Securities and Exchange Surveillance Commission commenced a compulsory investigation of Company A on suspicion of false statements in its annual securities reports. In response, Company A established a third-party committee to investigate the possibility that its sales revenue had been overstated. In July 2025, Company A disclosed the investigation report received from the third-party committee, which revealed, among other findings, that most of the reported sales revenue from the fiscal year ended December 31, 2021, through the fiscal year ended December 31, 2024 was fictitious and lacked underlying economic substance. Subsequently, in August 2025, the Tokyo Stock Exchange delisted Company A’s shares.

An accounting fraud case involving Company A significantly undermined confidence in the financial reporting system. Notable features of the case included the use of circular transactions through sales agents, a change of audit firm during the IPO preparation process, and the inclusion of false information in the financial statements and other documents submitted as part of the listing application, which ultimately resulted in the company obtaining approval for listing.

In light of these characteristics, it was recognized that close cooperation among the principal gatekeepers involved in the IPO process, namely the stock exchange, the lead underwriter, and the audit firm, was essential. These gatekeepers were therefore expected to strengthen their capabilities in reviewing and auditing fraud-related risks and to promote information dissemination and awareness-raising activities directed at companies preparing for listing.

In December 2025, the TSE and JPX-R issued a report entitled *“Exchange Responses in Light of Accounting Fraud Cases at the Time of Initial Public Offerings.”*[52] The report stated that the Exchange would:

[52] JPX-R, “Exchange Responses in Light of Accounting Fraud Cases at the Time of Initial Public Offerings” https://www.jpx.co.jp/news/1020/t13vrt000000ciom-att/t13vrt000000cirn.pdf

(i) strengthen listing examinations based on identified fraud risks, including verifying the identity ad substance of suppliers and customers in business models that rely heavily on agents in view of the risk of circular transactions, and confirming with predecessor auditors the circumstances surrounding any change of audit firm during the IPO preparation period;
(ii) strengthen reviews of whistleblowing systems and enhance the collection and sharing of fraud-related information, including confirming the establishment of internal whistleblowing systems at IPO applicant companies and, in cooperation with IPO-related stakeholders, promoting awareness of the Exchange's whistleblowing channels among officers and employees of companies preparing for listing;
(iii) enhance awareness-raising activities for management, including strengthening communications with senior executives of IPO applicant companies regarding the responsibilities associated with being a listed company, with emphasis on integrity and fraud prevention, and confirming the effectiveness of frameworks for preventing fraud through interviews with outside directors and corporate auditors conducted a part of the listing examination process;
(iv) strengthen cooperation with IPO-related stakeholders; and
(v) improve the capabilities of the self-regulatory organization to assess fraud risks in listing examinations.

In March 2026, the Japan Securities Dealers Association published the "Guidelines for Underwriting Examinations in Light of Accounting Fraud Cases at the Time of Initial Public Offerings."[53] The guidelines identify matters to which lead underwriters should pay particular attention when conducting underwriting examinations. These include (i) procedures responsive to fraud risks, such as reviewing the status of suppliers, customers, subcontractors, and advertising activities, confirming, through discussions with predecessor auditors, the circumstances surrounding any change of auditors, and conducting interviews where concerns arise regarding management integrity or the issuer's responses during the underwriting review process; (ii) confirming the adequacy of internal whistleblowing arrangements and responding to information relating to fraud or misconduct, including reviewing the establishment of internal whistleblowing systems and the extent to which whistleblowing channels have been communicated within the organization; and (iii) making inquiries of representative directors, corporate auditors, and independent officers.

In January 2026, the JICPA published *"Initiatives to Enhance the Reliability of Audits Conducted by Registered Auditors of Listed Companies and Other Entities,"*[54] in which it announced measures including the strengthening the monitoring of Registered Auditors of Listed Companies and the enhancement of members' competencies through training programs. On the same date, the JICPA also issued *"Audit Responses in Light of Accounting Fraud Cases at Newly Listed Companies and*

[53] Japan Securities Dealers Association, "Guidelines for Underwriting Examinations in Light of Accounting Fraud Cases at the Time of Initial Public Offerings" https://www.jsda.or.jp/shijyo/seido/jishukisei/web-handbook/105_kabushiki/files/20260318_shinkijoujouhikiukeshinsa.pdf
[54] JICPA, "Initiatives to Enhance the Reliability of Audits Conducted by Registered Auditors of Listed Companies and Other Entities" https://jicpa.or.jp/news/information/files/5-99-0-2-20260126.pdf

Other Entities (Notice),"[55] which sets out considerations for audit engagements relating to companies seeking an initial public offering. These considerations include the evaluation of risks arising from auditor changes and new client acceptance, understanding the entity's business model, identifying and assessing fraud risks, responding to assessed risks, maintaining professional skepticism regarding management integrity, consulting on technical matters, and communicating with corporate auditors and audit committees. In addition, in March 2026, the JICPA published *"Treatment of Confidentiality Obligations in Relation to Interviews Conducted by Stock Exchanges and Other Organizations in Connection with Initial Public Offerings."*[56] This publication explains confidentiality provisions that may be included in audit engagement letters to enable auditors to respond appropriately to interviews conducted by stock exchanges and other relevant organizations.

Furthermore, in response to a series of accounting fraud cases involving listed Japanese companies, including Company A, the JICPA has advocated enhancing the content of the management confirmation letter submitted together with annual securities reports and other disclosure documents in order to strengthen management's awareness of its responsibility for appropriate disclosure.

The CPAAOB is closely monitoring the impact of the implementation of the measures introduced in response to accounting fraud cases at the time of initial public offerings, including their implications for audit practices.

b. Submission of the Annual Securities Report Prior to the Shareholders' Meeting

In March 2025, the Minister for Financial Services issued a request titled *"Appropriate Information Disclosure Prior to the Shareholders' Meeting"* to all listed companies. The request indicated that the most desirable timing for submitting the annual securities report would be at least three weeks prior to the shareholders' meeting. However, taking into account the practical burden on companies, the request encouraged companies to begin by considering submission a day or several days before the meeting.

In June 2025, the FSA presented materials at the third meeting of the Liaison Council for Preparing the Environment for Disclosure of Annual Securities Reports Prior to Shareholders' Meetings. According to the materials, out of 2,262 listed domestic companies with the fiscal year ended March 2025, 1,241 companies indicated that they plan to disclose their annual securities reports prior to the shareholders' meeting, representing 54.9% of the total.

According to large-sized audit firms, among listed domestic companies with the fiscal year ended on March 2026, the number of companies planning to disclose their annual securities reports prior to their shareholders' meetings increased by approximately 40% compared with the previous year. While the majority of these companies plan to disclose their annual securities reports one or two days before their shareholders' meetings, an increasing number are expected to make such disclosures more than one week in advance.

[55] Same as footnote 52.
[56] JICPA, "Treatment of Confidentiality Obligations in Relation to Interviews Conducted by Stock Exchanges and Other Organizations in Connection with Initial Public Offerings" https://jicpa.or.jp/specialized_field/files/0-53-0-2-20260318.pdf

Large-sized audit firms have expressed the following views regarding the impact of disclosing annual securities reports prior to the shareholders' meeting on audit operations:

- There are concerns that, if annual securities reports are disclosed substantially earlier than the current practices of disclosure only a few days before shareholders' meetings, audit schedules would need to be significantly accelerated. This could cause audit work for listed audit clients to become concentrated within a limited period and raise concerns about securing sufficient audit resources and maintaining audit quality.
- As the audit period for annual securities reports may need to be shortened, it will be necessary not only to identify audit procedures that can be performed earlier, but also to advance discussions and resolve issues relating to new disclosure requirements and emerging topics earlier than in the past.
- Listed audit clients should consider the scheduling of shareholders' meetings and the preparation of annual securities reports from the perspective of overall optimization and establish an appropriate framework for cooperation with their auditors, based on an agreed reporting and audit timetable.
- Even where listed audit clients advance their reporting schedules, audit firms generally consider it feasible to accelerate the corresponding audit schedules.
- If annual securities reports are disclosed one or two days before shareholders' meetings, the impact is not expected to be significant. However, if disclosure is advanced to as early as three weeks before shareholders' meetings, changes in the preparation timetable for annual securities reports may affect the manner in which audit engagements are conducted.
- For audit teams responsible for listed audit clients planning to disclose annual securities reports more than one week before shareholders' meetings, firms have individually confirmed the status of their responses, including why disclosure was being accelerated, whether sufficient measures have been implemented in advance in cooperation with the companies to ensure adequate audit resources, and whether plans existed for further accelerating disclosure or moving toward integrated disclosure of annual securities reports and business reports for the following year.
- If filing dates are accelerated excessively, there is a concern that insufficient time may be available to perform year-end audit procedures. Although audit firms intend to respond through the earlier performance of audit procedures and greater digitalization, some consider that postponing the dates of shareholders' meetings may be necessary to ensure that sufficient audit time is available.

Some large-sized audit firms also expressed the view that, if annual securities reports are expected to be disclosed more than three weeks before shareholders' meetings, relevant government agencies and other stakeholders would need to make further efforts to create an environment conducive to the integrated disclosure and consolidation of annual securities reports and business reports, as well as to the postponement of shareholders' meeting dates.

Large-sized audit firms described their responses to, and views on, the integrated disclosure and consolidation of annual securities reports and business reports, and the related impact on audit engagements, as follows:

- Dedicated portal sites have been established to provide their personnel with the latest information and to make available materials for communication with listed audit clients.
- Cross-functional project teams comprising personnel responsible for contracts, accounting and disclosure, auditing, and engagement quality reviews have been established within the quality management divisions to support audit teams in responding to integrated disclosure initiatives.
- Support is being provided to listed audit clients that plan to implement integrated disclosure or postpone shareholders' meeting dates.
- Where listed audit clients seek advice on integrated disclosure and consolidation, audit firms determine an appropriate response on a case-by-case basis, taking into account each client's circumstances and the potential implications for the audit engagement, etc.
- As progress toward integrated disclosure and consolidation among listed audit clients remains limited, audit firms are continuing to address matters individually while also developing tools such as standard contractual documentation and disclosure checklists.
- During the first year of transition to integrated disclosure, additional efforts are expected to be required, including the reorganization of disclosure information and the adjustment of audit schedules. From the second year onward, however, efficiencies in the audit process and a more balanced distribution of audit hours are expected as a result of document consolidation.
- Consolidating disclosure documents into a single reporting package is expected not only to improve audit efficiency but also to reduce the burden on listed audit clients in preparing disclosure materials, thereby facilitating the disclosure of annual securities reports before shareholders' meetings.

The CPAAOB will continue to monitor the impact of the disclosure of annual securities reports prior to shareholders' meetings, as well as the integrated disclosure and consolidation of annual securities reports and business reports, on audit engagements and related practices.

■ Introduction of New Lease Accounting Standards ■

A lease transaction refers to an arrangement in which a company rents and uses a specific asset such as a building, machinery, or vehicle for a fixed period. In this arrangement, the leasing company owns the asset, and the company ("the lessee") obtains the right to use the asset by paying lease fees.

In Japan, the accounting standards for lease transactions were established in 2007 with the issuance of the Accounting Standard for Lease Transactions (ASBJ Statement No. 13) and the Guidance on Accounting Standard for Lease Transactions (ASBJ Guidance No. 16). These standards, collectively referred to as the "former lease accounting standards," were consistent with international accounting standards at the time.

Under the former lease accounting standards, lease transactions were classified into finance leases and operating leases. A finance lease is a transaction in which a leasing company purchases an asset on behalf of the lessee and leases it to the lessee, where cancellation during the lease term is not permitted and substantially all of the acquisition cost of the asset and related expenses are recovered through lease payments. An operating lease is a lease transaction that has characteristics similar to those of an ordinary rental agreement. Under the former standards, only finance leases were recognized as assets and liabilities on the balance sheet.

However, in January 2016, the IASB issued IFRS 16 *"Leases,"* which requires lessees to recognize all lease transactions as assets and liabilities on the balance sheet. As a result, differences arose between Japanese accounting standards and international standards, particularly in the recognition of liabilities. This discrepancy raised concerns about potential issues in international comparability. In response, the Accounting Standards Board of Japan (ASBJ) began developing a new accounting standard that would require lessees to recognize all lease transactions as assets and liabilities on the balance sheet. Since March 2019, ASBJ has conducted extensive deliberations on this matter.

In September 2024, the ASBJ issued the Accounting Standard for Leases (ASBJ Statement No. 34) and the Guidance on Accounting Standard for Leases (ASBJ Guidance No. 33) (collectively referred to as the "new lease accounting standards"). Under the new lease accounting standards, entities are, in principle, required to recognize on the balance sheet all assets and liabilities arising from leases. The standards also replace the term "lease transactions" with "leases. The new lease accounting standards apply to companies subject to disclosure under the FIEA, including listed domestic companies, their subsidiaries and affiliates, as well as large companies under the Companies Act. The standards will be effective from the beginning of the consolidated fiscal year or business year starting on or after April 2027, with early adoption permitted from the beginning of the fiscal year or business year starting on or after April 2025.

Under the new lease accounting standards, the definition and identification criteria for leases have been revised. A transaction is identified as a lease based on three key considerations: (1) whether the asset can be specifically identified, (2) whether the party has the right to obtain economic benefits from the asset, and (3) whether the party has the right to direct the use of the asset.

As a result, companies subject to the new standards must begin by collecting relevant contracts and reviewing each contract to determine whether it constitutes a lease. They are also required to maintain documentation of their assessments and conclusion regarding whether a contract is a lease. This requirement is expected to be particularly burdensome for companies operating multi-store business models, such as retailers and restaurant operators, as a large number of leasehold property contracts that have previously accounted for as rental transactions may need to be assessed and may be determined to constitute leases under the new standards.

Accordingly, companies subject to the new lease accounting standards are required to implement accounting systems and revise their business processes in order to identify transactions within the scope of the new standards and ensure appropriate accounting treatment in accordance with those standards. In particular, identifying transactions subject to the new standards is expected to impose a significant workload on affected companies. In light of these circumstances, although early adoption has been permitted for fiscal years beginning on or after April 2025, few companies have elected to adopt the standards early.

In preparation for the implementation of the new lease accounting standards, companies subject to the standards are expected to make prompt and thorough preparations. At the same time, audit firms must respond to the increased scope of contracts subject to audit, the greater complexity of accounting treatments, and the resulting increase in audit workload, while also enhancing their professional expertise as auditors. In addition, as the use of generative AI is expected in areas such as the identification and evaluation of transactions subject to the standards, developments relating to its utilization will also warrant close attention.

C. Trends in Sustainability Disclosure and Assurance

1. Trends in the Development of Disclosure and Assurance Frameworks for Sustainability-related Information

Until recently, sustainability-related information has been disclosed primarily on a voluntary basis through integrated reports and other corporate publications. However, in Japan, disclosure of sustainability-related information in annual securities reports became mandatory for fiscal years ending on or after March 31, 2023. As the specific content of such disclosures has largely been left to the judgment of individual companies, concerns have been raised regarding the comparability of disclosed information. Consequently, efforts to establish disclosure standards have progressed both domestically and internationally. At the international level, the ISSB issued the IFRS Sustainability Disclosure Standards (ISSB Standards)[57] in June 2023. In response, jurisdictions around the world have been developing regulatory frameworks aligned with these standards. In Japan, the Sustainability Standards Board of Japan (SSBJ) published sustainability disclosure standards in March 2025 that are functionally aligned with the ISSB standards (SSBJ Standards).

Third-party assurance is also considered beneficial for enhancing the reliability of sustainability-related information. Against the backdrop of growing demand for a global benchmark capable of supporting consistent, high-quality assurance of sustainability-related information, the IAASB issued ISSA 5000 in November 2024. Although ISSA5000 is designed to be applicable to all assurance practitioners and not limited to CPAs and audit firms, it requires compliance with quality management standards at least equivalent to ISQM1 and ethics and independence requirements at least equivalent to the IESBA Codes as fundamental prerequisites for the delivery of high-quality sustainability assurance engagements that serve the public interest.

Given these circumstances, the Financial System Council's Working Group on Disclosure and Assurance of Sustainability-related Financial Information (Sustainability WG) conducted discussions on the future framework for sustainability-related disclosure and assurance in Japan. The Sustainability WG published an Interim Discussion Paper in July 2025, followed by its Final Report in January 2026.

The Interim Discussion Paper proposed a phased approach requiring Prime Market-listed companies meeting specific market capitalization thresholds to prepare annual securities reports in accordance with the SSBJ Standards.[58] Reflecting this proposal, the Cabinet Office Ordinance on Disclosure of Corporate Affairs and related regulations were amended in February 2026.

The Final Report presented the broad direction of the assurance framework, including: (i) mandatory assurance beginning one year after the initial application of the SSBJ Standards; (ii) limitation of the scope of assurance during the first two years to specified sustainability-related information,[59] with

[57] IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* (IFRS S1) and IFRS S2 *Climate-related Disclosures* (IFRS S2)
[58] Taking into account the periods for preparation for companies, the implementation roadmap provides for mandatory application of the SSBJ Standards beginning with fiscal years ending on March 2027 for companies with a market capitalization of JPY 3 trillion or more, March 2028 for companies with a market capitalization of JPY 1 trillion or more, and March 2029 for companies with a market capitalization of JPY 500 billion or more.
[59] During the first two years, the scope of assurance is limited to disclosures relating to Scope 1 and Scope 2 greenhouse gas (GHG) emissions, governance, and risk management.

possible expansion after the third year in light of international developments and other factors; and (iii) adoption of limited assurance as the required assurance level, with no planed transition to reasonable assurance. The Report also proposed a registration system for assurance providers. Under this framework, both audit firms and non-audit firms would be eligible for registration, provided that they satisfy prescribed registration requirements and perform assurance engagements in accordance with international standards such as ISSA5000. In addition, the Report outlined key registration requirements, including the establishment of appropriate personnel and system of quality management, and indicated that the FSA would be responsible, at least initially, for the inspection and oversight of registered assurance providers.

Following these recommendations, legislative efforts have also progressed. In April 2026, a bill to amend the FIEA and related legislation was submitted to the 221st session of the National Diet as part of the process toward institutionalizing the new framework. Furthermore, with respect to third-party assurance, the Sustainability Assurance Subcommittee was established under the Business Accounting Council in April 2026 to deliberate on and examine the development of standards that are aligned with international standards. The Subcommittee has since been conducting broad-based discussions regarding the framework for assurance standards and related requirements that would be equivalent to internationally recognized standards.

While regulatory frameworks for the disclosure and assurance of sustainability-related information have continued to develop in other jurisdictions, there have also been moves to review and simplify such frameworks in response to concerns about increasing compliance costs for companies and potential impacts on international competitiveness.

For example, in the European Union, the Corporate Sustainability Reporting Directive (CSRD), which entered into force in January 2023, requires the disclosure of sustainability-related information and the provision of limited assurance by an independent third party. The requirements began to apply to certain companies from the 2024 financial year. Subsequently, in February 2025, the European Commission published the Omnibus Package, a set of legislative proposals aimed at simplifying sustainability-related regulations, and until February 2026, these proposals have been progressively approved and adopted by the European Parliament and the Council of the European Union. As a result, a number of measures were introduced, including the simplification of the European Sustainability Reporting Standards (ESRS), a reduction in the number of companies subject to the requirements through revisions to the applicable thresholds, and the postponement of the implementation timeline for companies that had not yet become subject to the reporting obligations. In addition, the European Union clarified that it would not proceed with a future transition from limited assurance to reasonable assurance.

In the United States, the SEC adopted its final rule on climate-related disclosure in March 2024. However, implementation of the rule was suspended following a series of legal challenges. Subsequently, under the current Republican administration, momentum grew for a reconsideration of

climate-related disclosure requirements, and in May 2026, a proposal was published to rescind the rule.

Meanwhile, in Australia, regulatory initiatives have continued to advance, including the introduction of mandatory climate-related disclosures and the development and implementation of third-party assurance standards.[60] As a result, approaches to sustainability-related disclosure and assurance are becoming increasingly diverse across jurisdictions. Developments among IFIAR member jurisdictions are discussed in "I. Monitoring by the CPAAOB, C. Cooperation with International Organizations Related to Auditing, 1. Participation in International Discussions through IFIAR, d. Responses to the Institutionalization of Sustainability-related Disclosure and Assurance".

2. Response by Audit Firms

Given their experience in providing assurance through financial statement audits, audit firms are expected by investors and other stakeholders to play an important role in the reliability of sustainability-related information. The following section outlines developments in sustainability assurance practices among audit firms, categorized by firm size.

a. Large-sized Audit Firms

Large-sized audit firms, either directly or through their group entities, provide advisory services relating to sustainability-related disclosures as well as voluntary assurance engagements on sustainability-related information. To support these activities, they have established dedicated functions responsible for promoting sustainability assurance engagements, facilitating collaboration between audit practices and specialists in non-financial reporting, and providing opportunities for audit professionals to participate in sustainability assurance engagements in order to gain practical experience in this area.

With respect to assurance procedures under ISSA5000, audit firms have been developing methodologies and guidance in collaboration with their global networks. In some cases, Japanese professionals have been assigned to global development teams responsible for designing assurance methodologies. Many firms have also begun using global platforms and tools developed within their networks to improve the efficiency and standardization of sustainability assurance engagements. In addition, firms have been progressively enhancing their quality management frameworks for sustainability assurance engagements, including the establishment of dedicated functions responsible for oversight and quality management.

Large-sized audit firms generally have more advanced human resource development programs than mid-tier and small and medium-sized audit firms. Many have established structured training programs that combine formal learning with practical experience and require audit professionals to complete these programs as part of the firms' mandatory training requirements. Some firms have also introduced internal certification programs for sustainability disclosure and assurance professionals.

[60] In Australia, mandatory disclosure requirements currently apply only to climate-related information. The assurance standards have been developed based on ISSA5000, which covers assurance engagements for all types of sustainability-related information. The framework requires limited assurance initially and provides for a future transition to reasonable assurance.

b. Mid-tier Audit Firms

Mid-tier audit firms generally intend to perform sustainability assurance engagements directly, rather than through group entities, and have established dedicated departments, committees, or other organizational structures to promote such services. Many firms are considering the systems, internal policies, and procedures necessary to undertake sustainability assurance engagements. Approximately half of the firms have undertaken voluntary assurance engagements relating to sustainability-related information. In addition, some firms utilize advisory entities within their groups to provide support services for sustainability-related disclosures, enabling them to accumulate practical experience and expertise through such engagements. To strengthen human resources, firms are fostering personnel with specialized sustainability-related knowledge through internal training programs and support personnel in obtaining external sustainability-related qualifications.

Mid-tier audit firms also actively collaborate with global networks, including the collection of information on international developments and the provision of training materials. Some firms receive support from their global networks or from member firms in other jurisdictions with established expertise in sustainability assurance, including assistance in developing methodologies and conducting engagements. Others, however, report that they do not receive such support from their global networks.

c. Small and Medium-sized Audit Firms

Through the collection of reports conducted in PY2025, the CPAAOB examined the status of initiatives relating to assurance engagements for non-financial information.[61] Reports collected from the firms showed that a substantial majority of firms responded that they were either “interested in assurance engagements relating to non-financial information but have not yet undertaken specific consideration” or “not interested in such engagements and do not intend to provide them even if approached by clients.” Many firms explained that they had not commenced detailed consideration because none of their audit clients were currently subject to mandatory third-party assurance requirements. Other firms cited resources constraints as a challenge to undertaking such work.

On the other hand, firms that responded that they were “interested in assurance engagements relating to non-financial information and were conducting specific internal assessments, including information gathering,” tended to be undertaking initiatives similar to those of mid-tier audit firms, although they had not yet accepted any such assurance engagements. For example, most of these firms reported collecting information on domestic and international developments and developing personnel with specialized expertise. Specific initiatives included participation in training programs organized by the JICPA or global networks, in-house training sessions involving external experts, and support for personnel seeking external sustainability-related qualifications. Some firms also participate in committees established by the JICPA, such as the Sustainability Information Support Committee for Small and Medium-sized Audit Firms. From an organizational perspective, several firms have established project teams or committees to examine issues associated with providing sustainability

[61] The collection of reports covered 44 small and medium-sized audit firms.

assurance engagements and to consider the development of the necessary internal infrastructure.

In July 2025, the JICPA established the Sustainability Capacity Building Council as the body responsible for promoting competency development relating to sustainability-related disclosure and assurance engagements among CPAs. The Council is currently considering measures to develop the knowledge, skills, and competencies necessary for CPAs to perform sustainability assurance engagements and related services appropriately.

In April 2026, the Council launched the JICPA Professional Program in Sustainability, a structured training framework designed to enable CPAs to systematically acquire the sustainability-related expertise expected of the profession. The JICPA develops and offers training courses aligned with the Program for its members. In addition, the JICPA makes such training courses available to audit firms that have established systematic training frameworks, including firms that already conduct training under comprehensive programs for the development of sustainability-related competencies in collaboration with member firms within their global networks. Participants who complete all courses required under the Program are eligible to receive a certificate of completion upon application. Large-sized audit firms have been steadily aligning their existing internal training programs with the JICPA Professional Program in Sustainability. Active utilization of the Program is also expected among mid-tier and small and medium-sized audit firms.