2026 Monitoring Report Key Points

July 2026

Certified Public Accountants and Auditing Oversight Board



Overview of the 2026 Monitoring Report

Refer to P1

Purpose of Publication

■ This report is intended for a broad audience, including audit and accounting professionals, market participants, students, and working professionals, and aims to enhance understanding of the importance of audits through accessible and relevant information on the CPAAOB's monitoring activities and developments in the audit environment.

Composition

■ This report comprises the following four sections (I – IV). The structure of this report has been partially revised starting with this edition.

I. Monitoring by the CPAAOB	II. Overview of the Audit Sector	III. Operation of Audit Firms	IV. Responses to the Changes in the Global Environment Surrounding Audits
• Revisions to the CPAAOB's Monitoring Approach for Audit Firms • Overview of the CPAAOB's Monitoring Framework, Including Inspections • Cooperation with International Audit and Oversight Organizations	• Overview of the audit sector as a whole through presenting the developments of the number of CPAs, audit firms, and audited companies etc.	• Operation of audit firms including the structure, digitalization, and group audit • Current situation of change of auditors, and trend of audit fees change caused by auditor change	• Trends in institutional reforms in light of recent changes to the audit environment

* Include topics that will attract readers' interest in columns within each section.

Revision of the Approach to the Monitoring of Audit Firms (1/2)

Refer to P8-9

Mission and Responsibilities of the CPAAOB

- Enhancing investor confidence in Japan's capital markets by improving audit quality and ensuring the reliability of CPA audits, thereby enhancing the fairness and transparency of Japan's capital markets.

Changes in the Environment Surrounding Audits and Audit Firms

- Increase in accounting fraud cases disclosed by listed companies, including high-profile cases

  (Note) Following the amendment of the Certified Public Accountants Act (effective in 2023), the CPAAOB has been empowered to conduct verification regarding false or unjust attestation.

- While the range of audit firms auditing listed companies continues to expand, CPAAOB inspections have identified cases among small and medium-sized audit firms where quality management systems were not satisfactory, raising concerns that weaknesses in organizational infrastructure could affect audit quality.

- On the other hand, large-sized audit firms audit companies accounting for more than 90% of the total market capitalization of listed companies in Japan, making it necessary to maintain and improve audit quality in light of their importance to the capital markets. In addition, auditing methods are becoming increasingly sophisticated and diverse due to the introduction of AI systems and audit tools developed by their global networks, requiring closer monitoring of audit firms' operational management and quality management systems.

It is important to conduct monitoring more appropriately in accordance with the circumstances and risks of audit firms.

⇒Revision of the Approach to Monitoring*

* Monitoring includes both on-site monitoring (inspections) and off-site monitoring.

"Basic Policy for Monitoring Audit Firms" sets out the objectives of the CPAAOB's monitoring activities and the underlying principles guiding them. Reflecting this review, the Basic Policy was revised in July 2026.

Revision of the Approach to the Monitoring of Audit Firms (2/2)

Refer to P9-11

Revision Details

- By timely and accurately understanding developments and risks surrounding audits and audit firms and conducting effective and efficient inspections based on such information, off-site and on-site monitoring will be more organically integrated.

Inspections

- Risk-based inspections (Where prompt confirmation is required, inspections may be conducted on an ad hoc basis irrespective of the standard inspection cycle.)
- Verification of suspected false or unjust attestation

<Standard Inspection Frequency by Size of Audit Firm>

Large-sized

- Full-scope and follow-up inspections, together with year-round monitoring using both on-site/off-site monitoring methods, including targeted reviews focusing on specific aspects of quality management systems and horizontal reviews on specific themes
  (Previously: inspections once every two years.)

Mid-tier

- Inspections once every two years in principle. (No change.)
- For firms whose quality management status has improved and whose business operations remain consistently satisfactory, a review of inspection frequency will be considered in light of their risk profile and quality management status.
  Consideration will also be given to applying an inspection approach similar to that used for large-sized audit firms, taking into account their global networks and quality management practices.

Small and Medium-sized

- Risk-based selection of audit firms based on the status of their operations and other factors, and increase in the number of inspections

Off-site Monitoring

Information Gathering and Analysis

- Timely identification of audit-firm risks based on JICPA Quality Control Reviews, together with information gathering and analysis regarding the introduction of IT and AI and corrections to audited companies' financial results.

Improvement Follow-up

- Enhanced follow-up through collection of reports and other measures for audit firms whose business operations are not considered satisfactory, promoting effective remediation.

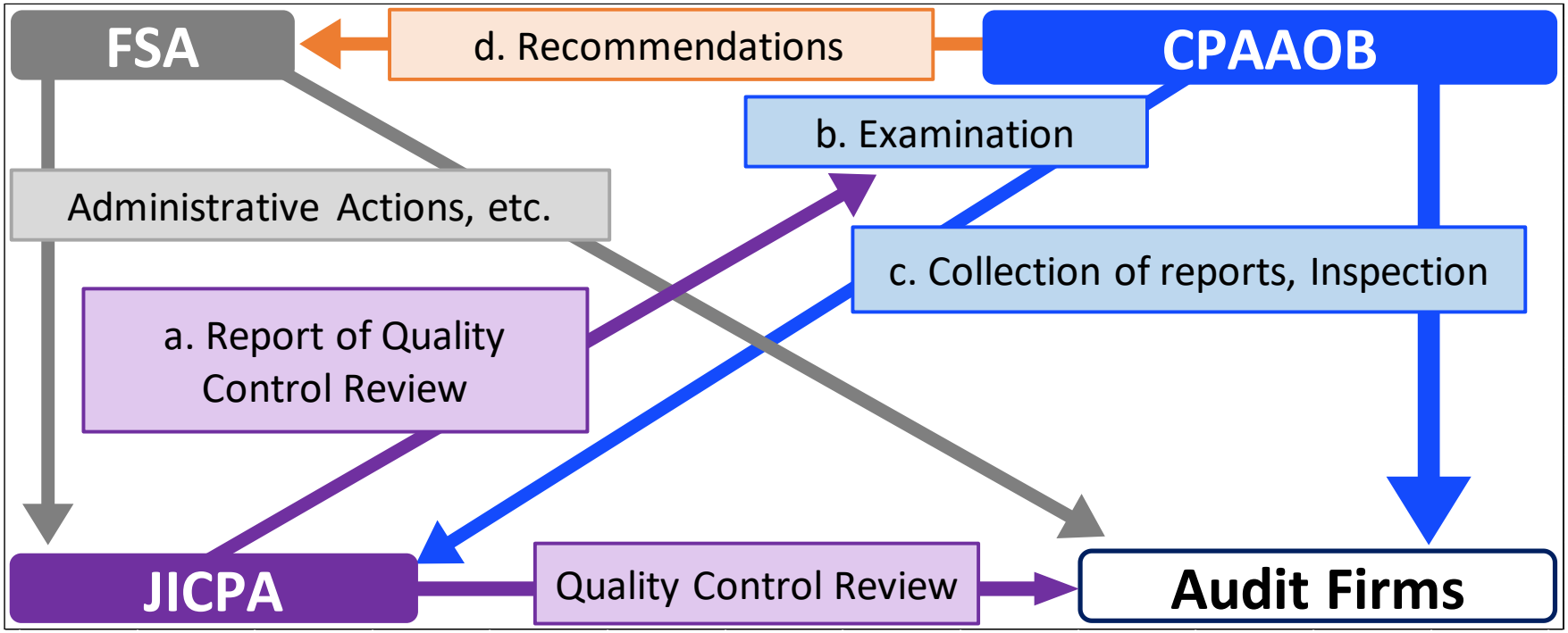
Reflecting the above revisions, the CPAAOB published "*Basic Plan for Monitoring Audit Firms for the PY2026*" on July 17, 2026, setting out the priority areas and other key matters for monitoring activities.

The CPAAOB Monitoring

Refer to P17

Overview of the CPAAOB Monitoring

- Based on the JICPA Quality Control Reports, (a.)
- The CPAAOB assesses whether the JICPA has carried out the Quality Control Reviews properly and whether the audit firms have properly performed its audit services. (b.)
- When deemed necessary, the CPAAOB collects reports from the JICPA and audit firms and conducts inspections. (c.)
- If it finds it to be necessary as results of inspections, the CPAAOB recommends administrative actions or other measures to the FSA Commissioner. (d.)



Overall Ratings

Refer to P32-33

- Based on the inspection results, the operational management of each audit firm is classified into one of five rating categories, and the resulting classification is notified to the firm as its overall rating. Upon notification, audit firms are required to disclose the rating to the audit and supervisory board members of audited companies (since PY2016).
- No audit firm was classified in the highest rating category, “Satisfactory”. All firms were classified as “Generally satisfactory with minor deficiencies” or below.
- Small and medium-sized audit firms tended to be rated lower than large-sized and mid-tier audit firms. This may partly be because the CPAAOB selects audit firms to be inspected on a risk basis.

Overall Rating	Details	Large-sized Audit Firms	Mid-tier Audit Firms	Small and Medium-sized Audit Firms
Satisfactory (Overall rating: 1)	Given when the operations of the audit firm are deemed to be satisfactory	–	–	–
Generally satisfactory with minor deficiencies (Overall rating:2)	Given when there are issues that need to be fixed, but the operations of the audit firm are deemed to be satisfactory overall	4	–	–
Unsatisfactory due to presence of significant deficiencies that need to be fixed (Overall rating: 3)	Given when the operations of the audit firm are deemed to be unsatisfactory	–	4	2
Unsatisfactory and in need of immediate remediation in operations management system (Overall rating: 4)	Given when the operations of the audit firm are deemed to be unsatisfactory and in need of immediate remediation	–	1	5
Extremely unsatisfactory (Overall rating: 5)	Material deficiencies with the quality management and audit engagements were identified and voluntary remediation cannot be expected to be implemented by the audit firm (recommendation is made to the FSA Commissioner)	–	–	10

(Note1) The above figures are tabulated based on inspections that terminated from PY2021 to PY2025.
(Note2) Regular inspections take place once every two years in the case of large-sized audit firms, once every three years in the case of mid-tier audit firms (until PY2025), and as necessary in the cases of small and medium sized audit firms.
(Note3) For audit firms that underwent regular inspections multiple times during the relevant period, results of the latest inspection are tabulated.

Cooperation with International Audit and Oversight Organizations

Refer to P37-46

Participation in International Discussions through IFIAR

- IFIAR was established in September 2006 as a forum for independent audit regulators. Since its inception, the CPAAOB and the FSA have been active members of IFIAR, contributing to the improvement of global audit quality.
- As an IFIAR Board member, the CPAAOB and the FSA leads dialogues with the six largest global audit networks and contributes to the various WGs* and TFs**. Japan also supports IFIAR as the host jurisdiction of the IFIAR Secretariat.

* Working Group, ** Task Force

Major IFIAR Activities Related to Recent International Developments in Auditing

Inspection Findings Survey

- IFIAR annually compiles and publishes inspection findings reported by member regulators relating to the system of quality management and audit engagements of the six largest global audit networks.
- IFIAR engages with the six largest global audit networks to encourage them to undertake root cause analyses, develop remediation measures, and continuously monitor the effectiveness of those measures.

Use of Technology in Auditing

- Drawing on dialogue with the six largest global audit networks and the sharing of supervisory practices among member regulators, IFIAR discusses issues such as the impact of technology on audit quality and related accountability challenges.
- In April 2026, IFIAR published a report outlining key considerations for regulators in monitoring audit firms' governance and oversight of technology tools.

Trends in Private Equity Investment in Audit Firms

- In recent years, IFIAR has examined the rapid growth of private equity investment in audit firms, particularly in Europe and North America, through stakeholder interviews and research.
- Japan and the Netherlands serve as co-chairs of this initiative and are leading discussions on IFIAR's response to these developments.

Institutionalization of Sustainability Reporting and Assurance

- IFIAR members share knowledge and practical experience regarding sustainability assurance frameworks and supervisory approaches.
- In 2025, IFIAR conducted a survey of member regulators on the implementation of sustainability reporting and assurance regimes, as well as the development of related supervisory and inspection frameworks. In June 2026, IFIAR published a fact sheet summarizing the survey findings.

Cooperation with Foreign Audit Regulators

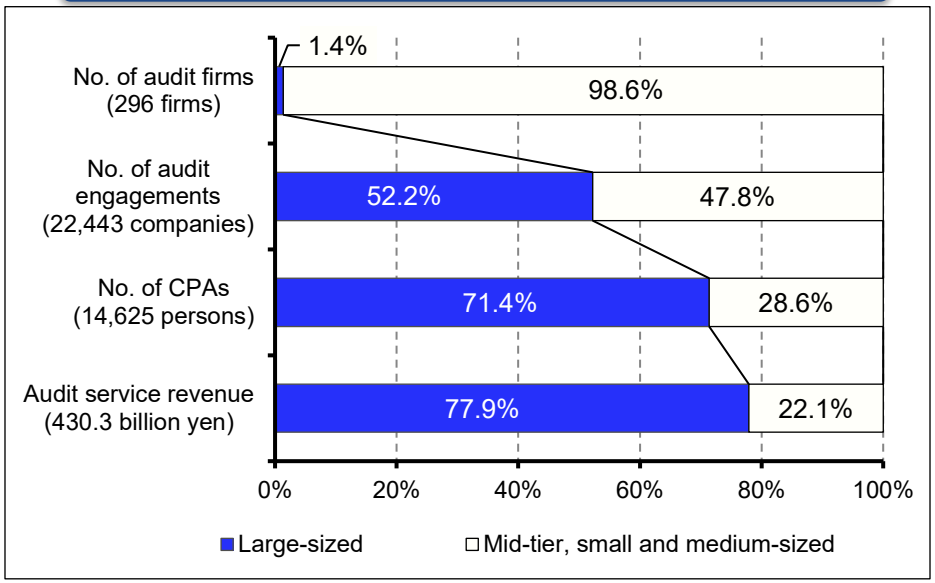
- The CPAAOB also places importance on strengthening bilateral and regional relationships. The CPAAOB actively participates in meetings and regional forums organized by other audit regulators, sharing Japan's audit oversight challenges and initiatives.
- Participation in such forums is important for gaining a multifaceted understanding of international regulatory developments, region-specific perspectives, and emerging trends in practice and research, and for appropriately reflecting international discussions in Japan's audit oversight activities.

Concentration of Audit Engagements at Large-Sized Audit Firms

Refer to P65-67

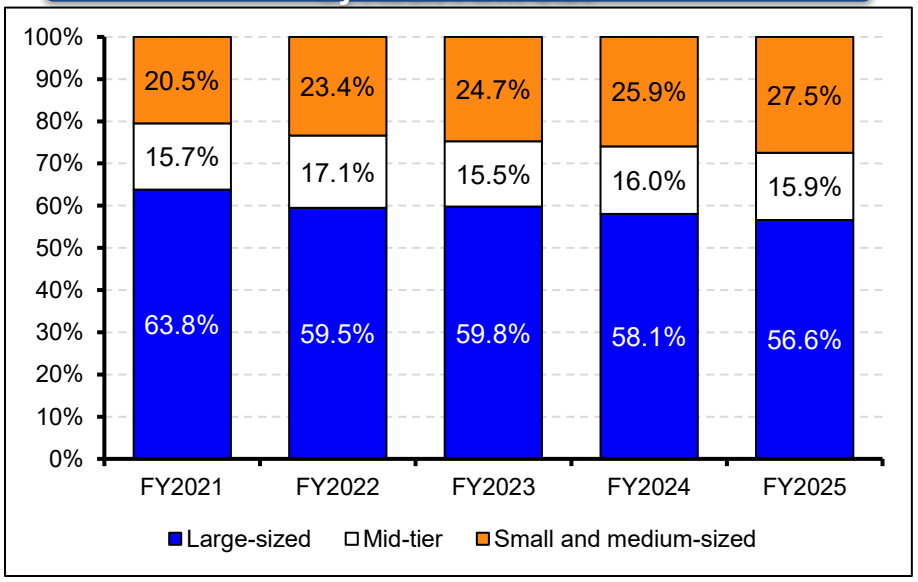
- Approximately 78% of audit service revenue is concentrated in the large-sized audit firms.
- In recent years, the share of large-sized audit firms has been declining in terms of both the number of audit engagements and audit service revenue.
- Similar market concentration is observed in the United States and the United Kingdom.

Market Share by Audit Firm Type (FY2024)



(Note) Compiled based on FY2024 JICPA member data and business reports submitted by audit firms

Number of Listed Domestic Companies by Audit Firm Size



(Note) Prepared by the CPAAOB based on data from Quick and Exchanges

Market Share of Big4 Global Networks in Audit Engagements for Major Listed Companies (Based on Number of Companies)

Refer to P 108-109

	Japan	United States	UK
Market Share of Big4 Global Networks	97%	99%	87%

(Note) Market shares calculated by CPAAOB based on the following stock indices:
Japan: Nikkei225
United States: S&P 500
UK: FTSE 350

Development and Implementation of Systems of Quality Management by Audit Firms

Refer to P55-58

System of Quality Management (SoQM)

- All audit firms started to apply the Quality Control Standards for Audits to audits of financial statements for business years or accounting periods on or after July 1, 2024, which were revised to reflect ISQM1*.
- Audit firms are required to comply with professional ethics not only in audit engagements but also in non-audit services.

* International Standard on Quality Management 1

Progress at Audit Firms

Large-sized / Mid-tier

- Incorporate the components of SoQM required under the Standards through the addition of evaluation items and other measures, based on the quality objectives and quality risks established by global networks.
- Continue efforts to promote the penetration and establishment of SoQM throughout their firms, while its operation and monitoring are becoming increasingly established.

Small and Medium-Sized

- Develop quality objectives, quality risks, and related policies and procedures by utilizing tools published by the JICPA.
- Progressively publish evaluation results of SoQM, recognizing that evaluation dates differ among audit firms, with some firms concluding that identified deficiencies are significant but not pervasive.
- Address challenges including securing sufficient resources for quality management activities and selecting quality objectives, quality risks, and related policies and procedures that are appropriate to the size and characteristics of the firm.
- Need to steadily operate the PDCA cycle by promptly identifying matters requiring improvement, analyzing root causes, and implementing necessary remedial actions through the firm's own evaluation process for SoQM.

Monitoring of the Systems of Quality Management

Refer to P118-120

Periodic Inspections of Audit Engagements

- Procedures performed to confirm that audit engagements comply with the audit firm's SoQM. Conducted periodically on completed engagements for each engagement partner (e.g., once every three years).
- The number of inspections, reviewers, and tools used varies depending on audit firm size.
  - ✓ Around 50-170 reviewers at large-sized audit firms, 15-40 at mid-tier audit firms, and 1-20 at small and medium-sized audit firms.
- Regardless of firm size, inspection results and identified deficiencies are shared with partners and staff through internal training and other channels to raise awareness.
- Inspection results are reflected in partner evaluations at large and mid-tier audit firms, as well as some small and medium-sized audit firms, to enhance the effectiveness of audit quality improvement efforts.

Utilization of Global Networks

- The Big4 global networks require their member firms to comply with detailed quality management standards and audit manuals established by the global network. To confirm whether member firms comply with these requirements and whether periodic inspections and individual audit engagements are performed in accordance with them, global reviews are conducted.
- Outside the Big4, requirements to comply with globally developed audit manuals are generally less stringent, and there are substantial differences in the scope, methodology, and frequency of global reviews.

Monitoring Before Audit Opinion Issuance

- Conduct monitoring of audit engagements before the audit opinion is issued to identify quality management issues and encourage engagement teams to take timely corrective actions.
- Often focus such monitoring on high-risk audit areas, including fraud risk.

Use of Technology in Audit

Refer to P99-102

Utilization of AI in Audit Engagements

- Audit firms, especially large-sized audit firms, are increasingly incorporating AI into audit engagements. Firms are using AI trained on auditors' expertise and experience as well as generative AI to enhance the efficiency and effectiveness of audit procedures, including financial data analysis and document reviews.
- Key challenges in the use of AI include data accuracy, algorithmic bias, lack of transparency in decision-making, data confidentiality, and AI hallucinations.
- Audit firms need appropriate controls over AI use. CPAs should have a basic understanding of data science and machine learning and should not rely uncritically on AI-generated outputs.

Examples of IT Utilization in Audit Engagements

[Legend] ○ Implemented / In use, ▲ Currently under implementation (incl, only some firms have adopted the tool, — Not implemented

Category	Type of Tool	Large-sized Audit Firms	Mid-tier Audit Firms
Infrastructure and Practice Management	Electronic audit working paper systems	○	○
	File-sharing systems	○	▲
	Audit databases	○	—
Analytics and Audit Support	Journal entry analysis tools	○	○
	Supporting document matching tools	○	▲
	Accounts receivable/payable confirmation systems	○	▲
	Disclosure document review tools	▲	▲
Automation	Robotic Process Automation (RPA)	○	▲
AI and Advanced Analytics	AI for fraud prediction using historical financial information	○	▲
	Generative AI for internal inquiries (e.g., firm rules and audit manuals)	○	▲
	Natural language processing for document digitization and analysis	▲	▲
	Generative AI for assisting with audit working paper drafting (AI agents)	▲	—
	AI for fraud prediction using non-financial information	Under development	—
Other Technologies	Use of blockchain technology	○	—
	Drones for improving the efficiency of physical inventory observations	Under development	—

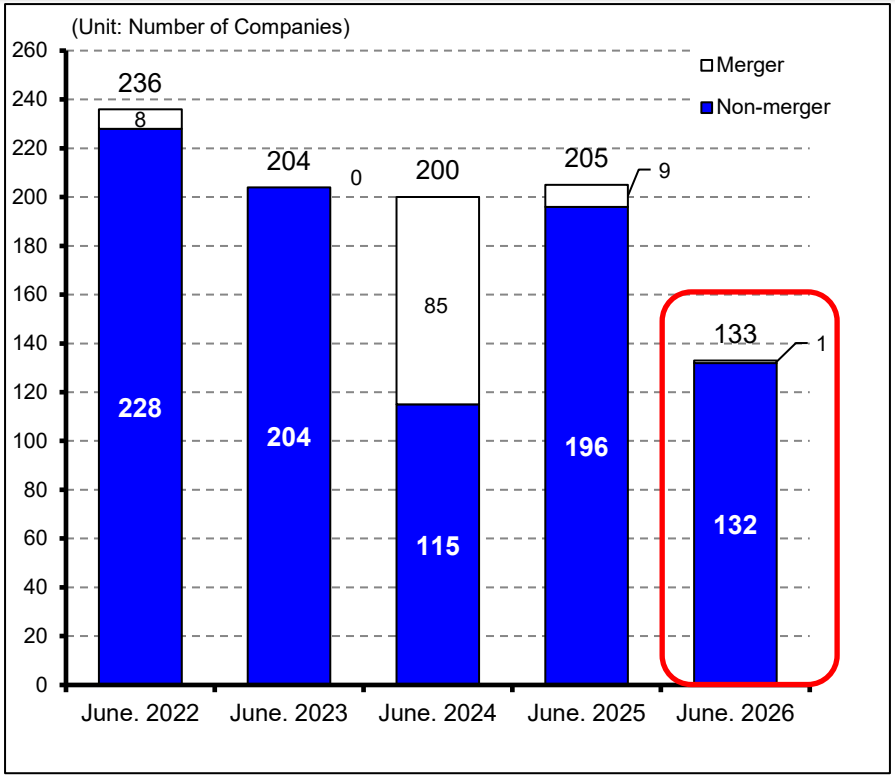
(Note) Prepared by the CPAAOB based on information obtained through the collection of reports

Changes of Accounting Auditors (1/3)

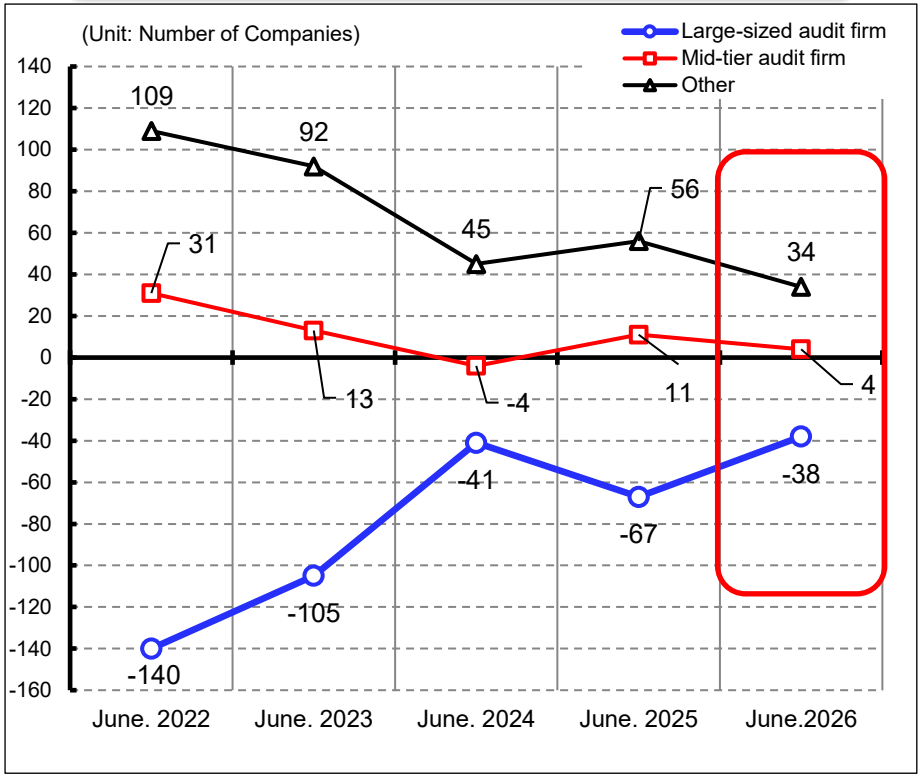
Refer to P125-127

- Decline in auditor changes compared with the year ended June 2025, with the number of changes returning toward historical levels after peaking in the year ended June 2022, suggesting a stabilization of auditor switching activity.
- Continued trend of companies changing auditors from large-sized audit firms to mid-tier audit firms or small and medium-sized audit firms, despite a decrease in the overall number of auditor changes.

Listed Domestic Companies Changed Audit Firms



Changes by Audit Firm Size



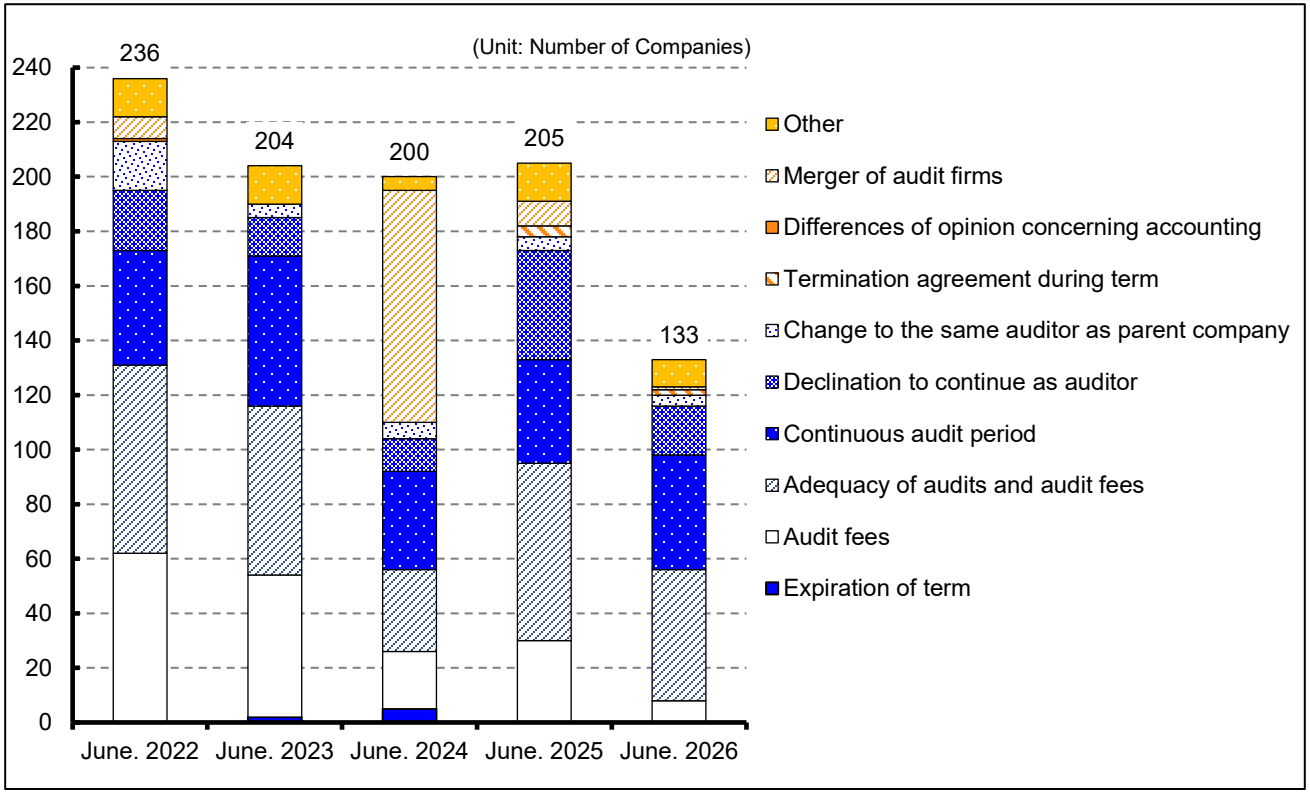
(Note) The figures above show the number of companies that had decided on an incoming auditor by the end of June of each period, based on timely disclosures of listed domestic companies.

Changes of Accounting Auditors (2/3)

Refer to P127-128

- Audit fee increases, the appropriateness of audit services in light of the company's business scale and the reasonableness of audit fees, and prolonged auditor tenure as key factors behind audit changes.
- Notable increase in cases of current auditors declining to continue engagements because of the anticipated increase in audit workload arising from changes in the audit environment, coupled with difficulties in securing sufficient personnel to perform the engagement.

Reasons for Changes in Accounting Auditors by Listed Domestic Companies



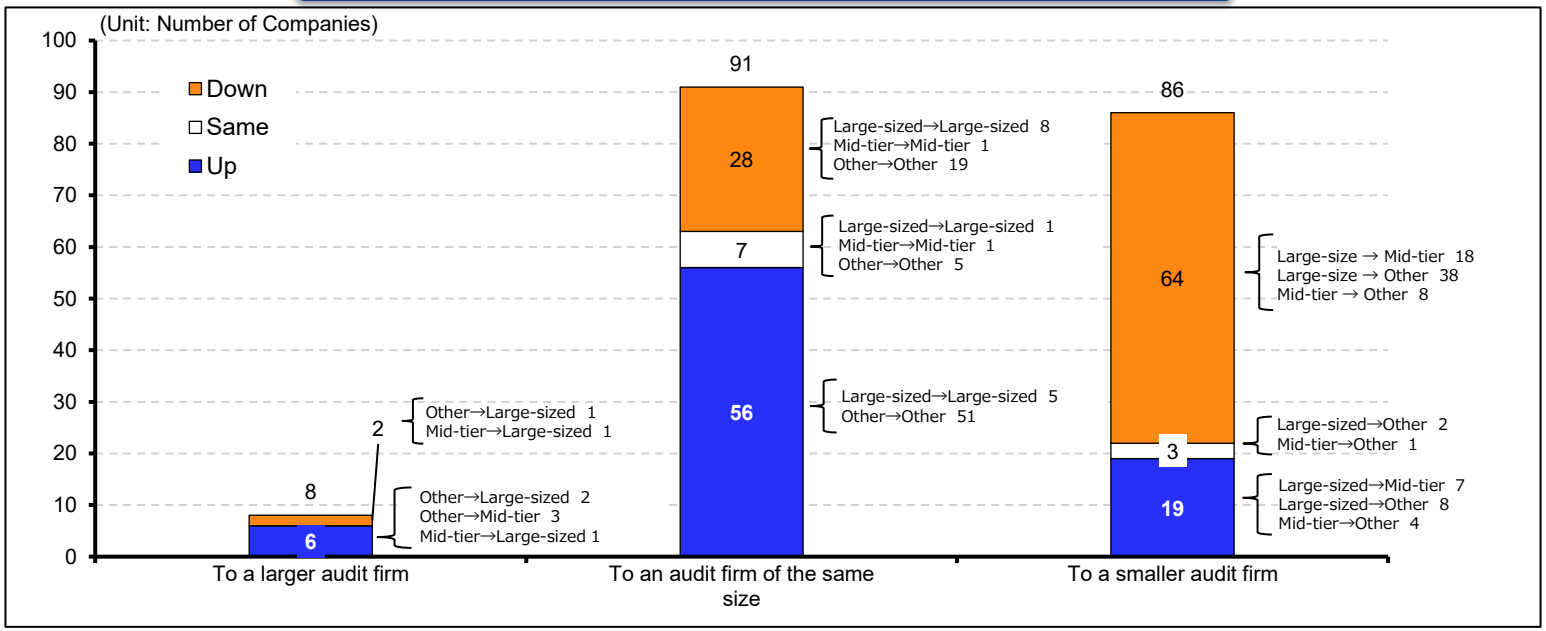
(Note1) Complied based on timely disclosures by listed domestic companies choosing new auditors by the end of June each year.
(Note2) In the case of two or more reasons disclosed, the classification was made based on principal reasons.

Changes of Accounting Auditors (3/3)

Refer to P132-134

- In PY 2025, even in cases of changes to smaller audit firms, increases in audit fees were observed more frequently than in the previous fiscal year.
  - ✓ This is considered to reflect situations in which audited companies prioritized audit services from auditors better suited to their business scale and accepted higher audit fees. The findings suggest a shift in which lower audit fees do not necessarily follow a change to a smaller audit firm.
- Audit fees also increased in substantial numbers in changes to audit firms of the same size, particularly between small and medium-sized audit firms.
  - ✓ Given the increasing number of cases in which incumbent auditors have declined to continue audit engagements, audited companies may have accepted the audit fees proposed by successor auditors to secure a prompt replacement.

Audit Fees Following Changes in Accounting Auditors



(Note1) Based on changes in accounting auditors between July 2023 and June 2024 where the audit fees before and after the changes were publicly disclosed.
(Note2) Prepared by the CPAAOB based on timely disclosures of changes in accounting auditors and security reports submitted by June 2025
(Note3) Breakdowns of these changes are shown in the graph.

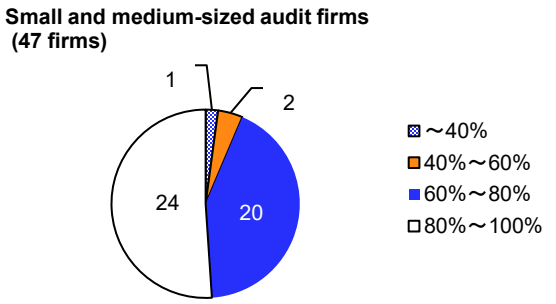
Side Businesses of Partners and Part-Time Personnel

Refer to P90-92

Side Businesses of Partners

- Large-sized audit firms generally do not permit partners to engage in side businesses with tax accountant offices or private practitioner offices.
- Practices vary among mid-tier audit firms, but even where side businesses are permitted, partners, including those with side businesses, spend more than 90% of their working hours on audit firm activities.
- Most small and medium-sized audit firms permit side businesses, as many partners already operate their own tax accountant offices when joining the firm.

Audit Firms by % of Partner's Allocation Time in Firm Operations

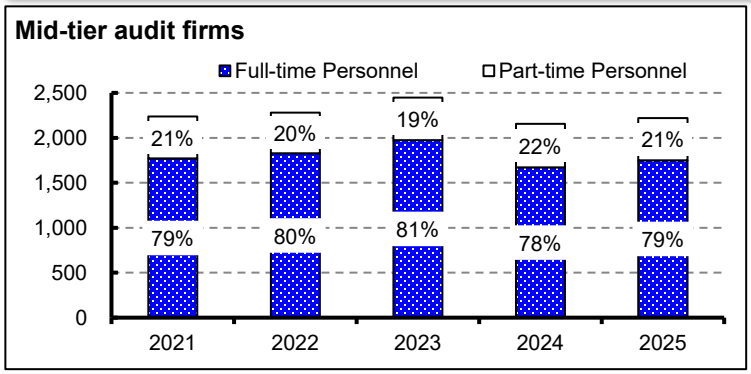


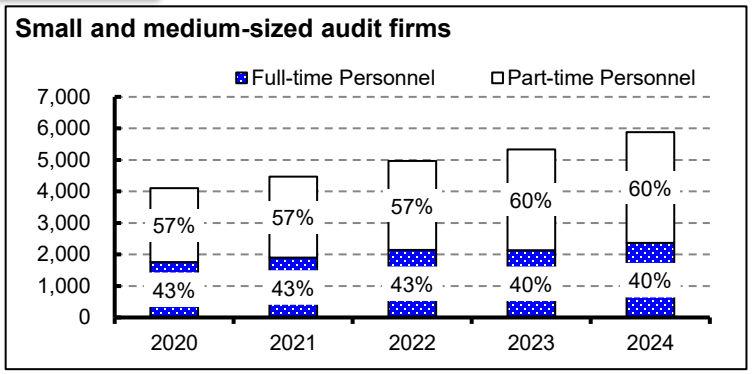
(Note) Prepared by the CPAAOB based on partner's declarations collected through the inspections and collection of reports

Part-Time Personnel

- In small and medium-sized audit firms, part-time personnel have consistently accounted for around 60% of total personnel, reflecting a reliance on part-time audit assistants in firm operations.

Number of Full-time and Part-time Personnel (unit: persons)





(Note) Prepared by the CPAAOB based on business reports submitted by audit firms.

Trends Surrounding Small and Medium-Sized Audit Firms

Refer to P138-144

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

Operation of the Registration System for Auditors of Listed Companies

- The Registration Review Committee for Auditors of Listed Companies reviews applications for registration and cancellation of registration, and deliberates on matters relating to the operation of the registration system.
- Assesses the status of the audit firm's system of quality management through Review for Application Review when the firm applies for registration. Decisions on registration and cancellation are made by the Registration Review Committee based on the results of confirmation of eligibility conducted through the Quality Control Review system.
- Clarified the viewpoints and criteria for confirmation of eligibility through the issuance and revision of the *Guideline for Confirmation of Eligibility of Audit Firms Engaged in the Audit of Listed Companies*. Audit firms are expected to conduct self-assessments based on the Guideline and voluntarily address any identified deficiencies.
- In July 2025, the review of deemed registered auditors under the transitional measures was completed. As of the end of June 2026, 130 audit firms had been registered.

Support Measures for Small and Medium-Sized Audit Firms

- Led by the Small and Medium Practices Policy Committee and the Small and Medium-Sized Audit Firms Liaison Council, the JICPA provides support for information disclosure, audit quality improvement, digitalization, compliance with the revised Quality Control Standards and the JICPA Code of Ethics, and talent recruitment and development.
- In collaboration with organizations across the audit profession, the JICPA promotes audit infrastructure enhancements, including electronic confirmations, electronic audit documentation systems, and support for compliance with the Audit Firm Governance Code.

Response by the CPAAOB

- Key points of the revised Quality Control Standards state that the administrative authority should strive to ensure proactive quality management by audit firms through inspections by the CPAAOB, while supporting the efforts of audit firms and the JICPA.
- The CPAAOB continues to place emphasis on inspections of small and medium-sized audit firms, while also supporting them by delivering lectures at seminars and training sessions organized by relevant institutions.

Trends in Financial Reporting Systems

Refer to P149-151

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

- In March 2025, the Minister for Financial Services requested all listed companies to consider filing annual securities reports before shareholders' meetings. While filing at least three weeks in advance was identified as the most desirable timing, companies were encouraged, in light of practical implementation burdens, to start by filing one or a few days before the meeting.
- According to large-sized audit firms, the number of listed domestic companies planning to file annual securities reports before shareholders' meetings for the fiscal year ending March 2026 is expected to increase by approximately 40% from the previous year. While most plan to disclose one or two days before the meeting, the number planning to disclose more than one week in advance is also expected to increase.

Impact of filing annual securities reports prior to the shareholders' meeting on audit operations of large-sized audit firms	Responses to the integrated disclosure and consolidation of annual securities reports and business reports at large-sized audit firms
➢ Earlier pre-shareholders' meeting disclosure may accelerate audit schedules and concentrate audit work, creating challenges for audit resources and quality. Earlier audit procedures and enhanced communication with audit clients are therefore required. ➢ Listed audit clients need to optimize overall schedules and work closely with auditors. Where excessive acceleration could adversely affect audit engagements, postponing shareholders' meeting dates may also be necessary where appropriate.	➢ Develop support measures for audit teams by providing the latest information and establishing cross-functional project teams within quality management divisions. ➢ Provide support tailored to each listed audit client planning to adopt integrated disclosure. ➢ While additional efforts are expected in the first year of transition, integrated disclosure is expected to improve the efficiency of both disclosure and auditing and facilitate disclosure prior to shareholders' meetings over time.

- 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 the consolidation of annual securities reports and business reports, on audit engagements and related practices.

Trends in Financial Reporting Systems and Sustainability Disclosure and Assurance

Refer to P147-149, 153-157

Actions Taken by Relevant Stakeholders in Response to IPO-Related Accounting Fraud Cases

- An accounting fraud case identified shortly after an IPO revealed several notable features, including circular transactions through sales agents, a change of audit firm during the IPO preparation process, and false information in listing application documents.
- In response, the TSE, JPX-R, JSDA, and JICPA announced policy measures. Recognizing the importance of close cooperation among stock exchanges, lead underwriters, and audit firms as key IPO gatekeepers, these organizations encouraged enhanced review and audit capabilities to address fraud risks, as well as strengthened information-sharing and awareness-raising activities for IPO candidates.

Sustainability Disclosure and Assurance

- In Japan, the Financial System Council's Working Group on Disclosure and Assurance of Sustainability-related Financial Information has outlined the direction of the sustainability disclosure and assurance framework through its Interim Discussion Paper (July 2025) and Final Report (January 2026). Legislative measures are being developed accordingly.
- The Sustainability Assurance Subcommittee under the Business Accounting Council is discussing assurance standards and related requirements aligned with international standards, including ISSA 5000.
- Large-sized audit firms are expanding sustainability-related advisory services and voluntary assurance engagements through their network firms, strengthening collaboration with sustainability specialists, and providing practical experience to audit professionals. They are also developing ISSA 5000-based assurance methodologies and tools in collaboration with their global networks, with Japanese professionals contributing to these initiatives. At the same time, they are enhancing their quality management frameworks for sustainability assurance engagements.

(Note) TSE: Tokyo Stock Exchange, JPX-R: Japan Exchange Regulation, JSDA: Japan Securities Dealers Association, ISSA: International Standard on Sustainability Assurance