

Annual Report

June 2018

Certified Public Accountants and Auditing Oversight Board

About this Annual Report

Pursuant to Article 16 of the Certified Public Accountants and Auditing Oversight Board (CPAAOB) Rules of Operation as below, which is stipulated on the basis of Article 2 of the CPAAOB Cabinet Order, this Annual Report publishes the activities of the CPAAOB for FY2017 (from April 1, 2017, to March 31, 2018).

To better meet the needs of readers, the Report also includes information on activities taken before and after FY2017.

Note that FY2017 and this fiscal year refer to the period from April 1, 2017 to March 31, 2018, while PY2017 and this program year refer to the period from July 1, 2017 to June 30, 2018.

- The CPAAOB Rules of Operation

- Article 16 The CPAAOB shall, after the end of each fiscal year, publish its activities for that year, such as measures taken and the number of inspections conducted.

<<If you have any comments, etc., please contact the following address>>

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1 Overview of the CPAAOB

1.1 Certified Public Accountants and Auditing Oversight Board (CPAAOB)

The CPAAOB, government organization which has a council system, was established under the Financial Services Agency (FSA) in April 2004, based on Article 35, Paragraph 1 of the Certified Public Accountants Act (CPA Act) and on Article 6 of the Act for Establishment of the FSA.

The CPAAOB is comprised of the Chairperson and up to 9 Commissioners with understanding and knowledge of matters concerning CPAs who are appointed by the Prime Minister after the approval of both Diet houses. Most of the Commissioners serve part-time, but one of them can serve full-time. They are appointed for a term of three years (Articles 36, 37-2 and 37-3 of the CPA Act).

The Chairperson and Commissioners exercise authority independently. They shall not be dismissed against their will except for the reasons stipulated by the laws during their appointed terms (Articles 35-2 and 37-4 of the CPA Act).

The CPAAOB, comprising 10 members (newly-appointed Chairperson Toshiro Hiromoto, newly-appointed full-time Commissioner Takayuki Matsui, and eight part-time Commissioners, including three who have been newly appointed), has been launched for its fifth term (from April 2016 to March 2019) (See Annex, page 33).

The key responsibilities of the CPAAOB are as follows:

- Inspection of CPAs, audit firms, foreign audit firms, and the Japanese Institute of Certified Public Accountants (“JICPA”)

- Implementation of CPA Examinations

- Deliberation of disciplinary actions against CPAs and audit firms

1.2 Executive Bureau

The CPAAOB has an Executive Bureau to handle its administrative duties (Article 41, Paragraph 1 of the CPA Act).

The Executive Bureau is comprised of the Planning, Management and CPA Examination Office and the Monitoring and Inspection Office, led by the Secretary-General of the Executive Bureau. The Planning, Management and CPA Examination Office is in charge of implementing the CPA examinations, investigating

and deliberating on disciplinary actions against CPAs, etc., and coordinating general issues of the Executive Bureau. The Monitoring and Inspection Office is in charge of monitoring audit and attestation services provided by audit firms, etc. and the operation of the JICPA, and inspecting audit firms, etc., foreign audit firms and JICPA.

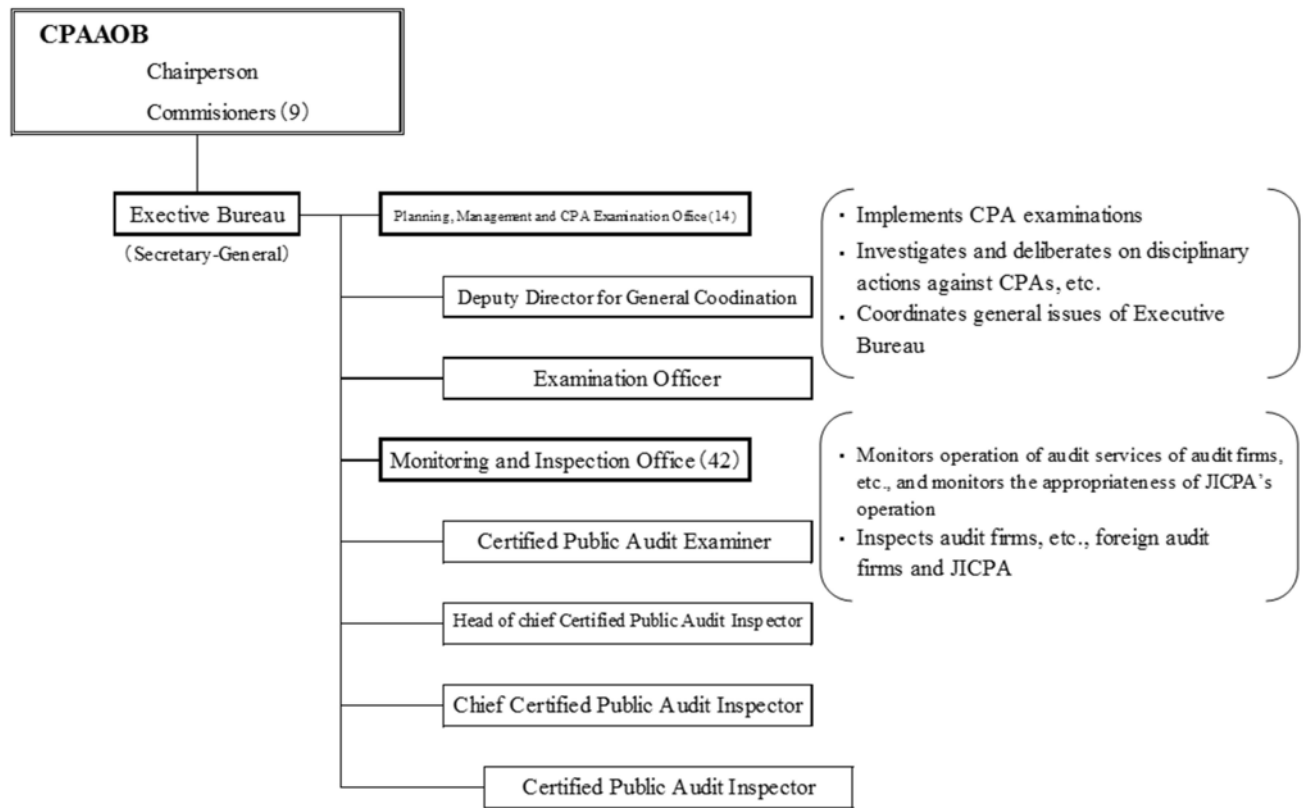
The Executive Bureau had 40 staff members when it was launched in April 2004. Its staff was steadily increased thereafter, to 14 in the Planning, Management and CPA Examination Office, and 42 in the Monitoring and Inspection Office: for a total of 56 staff members on March 31, 2018.

Staffing of the Executive Bureau

(Fiscal year-end basis)

| FY | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 ~ 2015 | 2016 ~ 2017 |
|--|------|------|------|------|------|------|------|------|-------------------|-------------------|
| Planning, Management and CPA Examination Office | 11 | 12 | 12 | 12 | 12 | 14 | 14 | 14 | 14 | 14 |
| Monitoring and Inspection Office | 29 | 29 | 31 | 35 | 39 | 41 | 44 | 43 | 42 | 42 |
| Head of Chief Inspector | - | - | - | - | - | - | - | - | - | 1 |
| Chief Inspectors | 4 | 4 | 4 | 4 | 5 | 5 | 7 | 7 | 7 | 6 |
| Inspectors | 18 | 18 | 20 | 24 | 26 | 28 | 28 | 27 | 26 | 26 |

Organization Chart of the CPAAOB



(Note) Figures in parentheses denote the number of personnel at the end of FY2017.

2 Oversight and Inspection of Audit Firms

2.1 Outline

Previously, the JICPA's quality control reviews (see Note) of audit firms had been self-regulated. However, from the perspective of ensuring the fairness and transparency of capital markets and establishing a market capable of gaining the trust of investors, and as a measure for enhancing and strengthening the monitoring and oversight functions over audit firms, the June 2003 revision of the CPA Act resulted in quality control reviews becoming statutory. Under the revision, the CPAAOB receives reports on the results of these reviews from the JICPA, examines them, and if the CPAAOB deems it necessary, requests additional information and conducts inspections.

Furthermore, for the purpose of ensuring the soundness of Japan's financial and capital markets, as a result of the June 2007 revision of the CPA Act, foreign audit firms that conduct audits of foreign companies subject to the disclosure regulations under the Financial Instruments and Exchange Act became subject to the inspections and supervision of Japan's authorities, and the CPAAOB was given the mandate to collect the relevant information and conduct on-site inspections.

Specifically, the authority related to the following matters has been delegated from the Commissioner of the FSA to the CPAAOB (Article 49-4, Paragraphs 2 and 3 of the CPA Act):

Business pertaining to the receipt of reports on the results of reviews by the JICPA on the operation of members' services (audit and attestation services) set forth in Article 2, Paragraph 1 of the CPA Act (Article 46-9-2, Paragraph 2 of the CPA Act)

Collection of reports and inspections on the JICPA, CPAs and audit firms, which are conducted in relation to the above mentioned reports (Article 46-12, Paragraph 1 and Article 49-3, Paragraphs 1 and 2 of the CPA Act)

Collection of reports and inspections on foreign audit firms, etc. (Article 49-3-2, Paragraphs 1 and 2 of the CPA Act)

As a result, the CPAAOB is required to examine quality control review reports, and, if the CPAAOB considers it necessary and appropriate in light of public interest or investor protection, to collect the relevant information and conduct inspections.

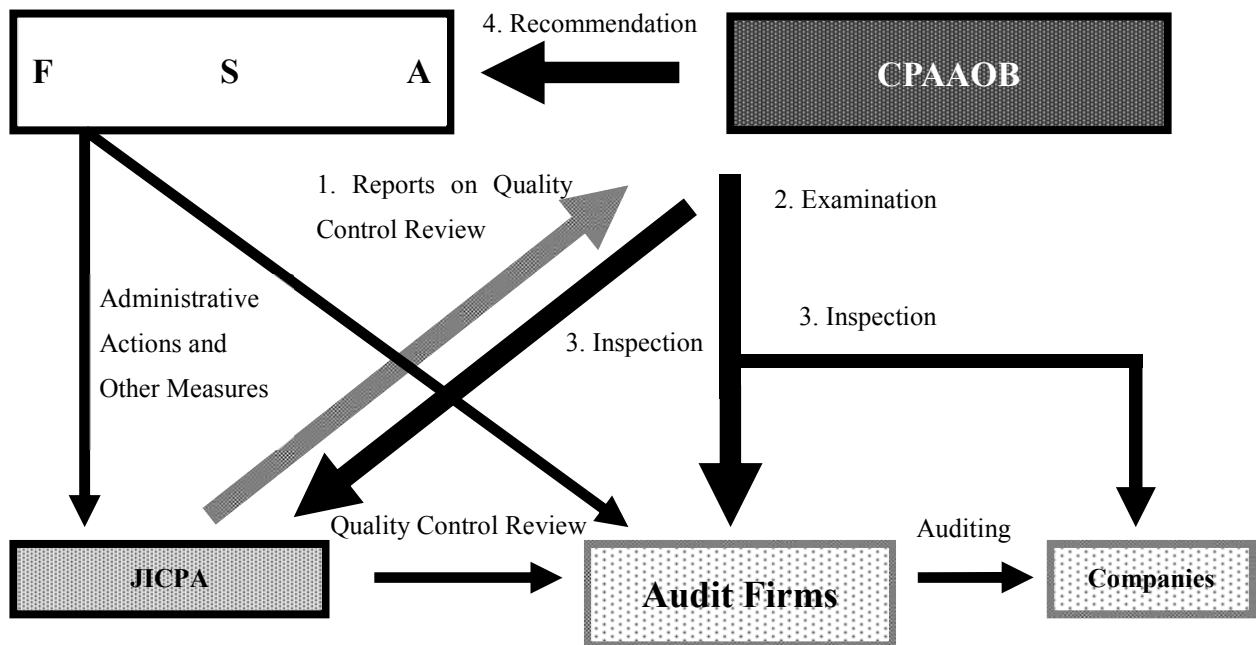
Furthermore, based on the results of examination or inspection, if the CPAAOB considers it necessary, it shall make a recommendation to the Commissioner of the FSA for administrative actions or other measures (Article 41-2 of the CPA Act).

(Note) Quality control reviews

Quality control reviews are performed by the JICPA pursuant to the CPA Act, according to which the JICPA shall review the status of the operation of services by members set forth in Article 2(1) of the Act. (Article 46-9-2(1) of the CPA Act).

Specifically, with the aim of maintaining and improving an appropriate quality level of audit service as well as maintaining and enhancing social confidence in auditing, the JICPA is obliged to review the status of the quality control of audits performed by audit firms and CPA offices (audit firms).

Outline of Oversight and Inspections



1. Reports on quality control review

Once every three years in principle (or once every two years, if the JICPA finds it necessary), the JICPA reviews and assesses an audit firm’s compliance with laws, regulations, audit standards, the JICPA’s rules, and other related regulations. The CPAAOB obtains reports on the results of those reviews.

2. Examination

The CPAAOB examines the JICPA’s reports and ascertains: (i) whether the quality control review system is being properly operated by the JICPA, and (ii) whether audit services are being properly provided by audit firms. The CPAAOB requests the submission of reports or other materials from audit firms, if in the course of its examination, the CPAAOB finds it necessary to do so.

3. Inspection

If the CPAAOB considers it necessary and appropriate in light of public interest or investor protection, it conducts inspections of audit firms (including entities which are audited by audit firms).

Furthermore, if the CPAAOB considers it necessary to do so from the viewpoint of securing the appropriate conduct of administration by the JICPA, it conducts inspections of the JICPA.

4. Recommendation

Based on the results of examination or inspection, the CPAAOB may make a recommendation to the Commissioner of the FSA for administrative actions or any other measures for securing fair operation of audit services by audit firms or that of administrative operations of the JICPA, when the CPAAOB considers it necessary.

Note: Regarding the collection of reports from and inspections on foreign audit firms, etc., refer to item (ii), Section 2.3.6 “A framework for information requirements and inspections on foreign audit firms, etc.” (see page 17).

2.2 Basic Policy for Monitoring Audit Firms

2.2.1 Basic Policy for Monitoring Audit Firms (Basic Policy for Examination and Inspection)

From the viewpoints of further improving the audit quality and improving the effectiveness of audits conducted by audit firms through examinations and inspections, the CPAAOB formulated and, published on May 13, 2016, the “Basic Policy for Monitoring of Audit Firms (Basic Policy for Examination and Inspection - To Ensure More Effective Auditing -“ for the fifth term (April 2016 to March 2019), based on the results of examinations and inspections during the first through the fourth terms (April 2004 to March 2016).

<Outline of the basic policies>

(i) Perspectives

The CPAAOB shall conduct effective and efficient monitoring (see Note) in light of the situation at audit firms, and work actively to ensure the credibility of audits by maintaining and enhancing audit quality.

In addition, the CPAAOB shall proactively provide useful information about industry-wide issues that resulted from analyzing information obtained from monitoring to the JICPA, the FSA, etc. as well as endeavor to expand the range of

information it publicly disseminates.

(Note) Monitoring includes both on-site monitoring, i.e. inspections, and off-site monitoring, which refers to activities other than inspections. These include obtaining information through the collection of reports, the exchange of opinions, etc.

(ii) Goals

The basic goal shall be to ensure proper operation of audit firms. In particular, given the fact that audit firms are primarily responsible for maintaining and enhancing audit quality, the CPAAOB shall conduct monitoring that is effective in encouraging audit firms to take action voluntarily.

The CPAAOB shall also focus not only on whether audit firms formally conform to audit standards, but also on whether they substantively serve to maintain and enhance audit quality. For example, it is important for them to have an appropriate level of professional skepticism designed to find out accounting fraud and so on.

(iii) Basic policy for off-site monitoring

The CPAAOB receives reports on the results of quality control reviews, which are conducted by the JICPA, and with regard to these reports, collects reports from and conducts interviews with audit firms, etc. when this is deemed necessary, and endeavors to make the collection and analysis of information more effective and sophisticated by exchanging opinions and cooperating with affiliate.

Furthermore, with the aim of accurately determining the circumstances and risks relating to audit firms and individual audit engagements, the CPAAOB utilizes the information it has obtained to conduct effective off-site monitoring that reflects the circumstances of audit firms. For example, it verifies the quality control reviews performed by the JICPA and collects information.

(iv) Basic policy on inspections

In addition to conducting effective and efficient inspections that reflect the risks and circumstances of audit firms, the CPAAOB endeavors to enhance the effectiveness of inspections by, for example, improving inspection methods.

The CPAAOB also strives to integrate inspections with off-site monitoring, and works to maintain and enhance audit quality at audit firms.

Given the role they play in the capital markets, the CPAAOB conducts periodic inspections of large-sized audit firms (see Note 1) and second-tier audit firms (see Note 2) based on reports of the results of quality control reviews.

The CPAAOB also conducts inspections of small and medium-sized audit firms (see Note 3) based on the results of quality control reviews as necessary.

(v) Policy on the provision of monitoring information

The basic policy is to contribute to maintaining and enhancing audit quality not only by informing audit firms and audited entities of audit quality control issues related to audit firms, but also by providing investors, etc. and other members of the general public with information on the outcomes of monitoring, including inspection results, in the form of reports, etc.

(Note 1) Large-sized audit firm is an audit corporation with 100 or more listed companies as audit clients and 1,000 or more full-time auditors. In this annual report, there are four such firms: KPMG AZSA LLC, Ernst & Young ShinNihon LLC, Deloitte Touche Tohmatsu LLC, and PricewaterhouseCoopers Aarata LLC.

(Note 2) Second-tier audit firm is an audit corporation that while not meeting the criteria for a large-sized audit firm nevertheless has a relatively large number of listed companies as audit clients. In this annual report, there are six such firms: Gyosei & Co., BDO Sanyu & Co., Grant Thornton Taiyo LLC, BDO Toyo & Co., PricewaterhouseCoopers Kyoto, and Yusei Audit & Co.

(Note 3) A small and medium-sized audit firm is an audit firm other than a large-sized or second-tier audit firm.

2.2.2 Basic Plan for Monitoring Audit Firms

Based on the Basic Policy for Monitoring Audit Firms, the CPAAOB formulates the Basic Plan for Monitoring Audit Firms, to provide a direction for monitoring in each program year.

The Basic Plan for Monitoring Audit Firms in the program year 2017 was formulated based on the circumstances described below and announced on July 26, 2017.

- In the wake of recent accounting scandals, confidence in audit has been questioned again. To address this situation, the Financial Services Agency (FSA) released the Principles for Effective Management of Audit Firms (“The Audit Firm Governance Code”) on March 31, 2017. Currently, large-sized audit firms, second-tier audit firms and some other firms are working to reorganize their governance environment for the improvement of the audit quality.
- There have been problems in internal controls including overseas group companies, for example, an accounting problem was reported recently at an overseas subsidiary of a listed company. Audit firms are thus required to thoroughly conduct specific assessment based on the actual state of business operations, including overseas operations, when they assess the internal

controls of their audited companies.

<Outline of the Basic Plan>

(i) Basic Plan Pertaining to Off-site Monitoring

(a) Examination of JICPA's quality control review

The CPAAOB will collectively examine the JICPA's policy and responses toward the improvement of the audit quality as a self-regulatory organization, mainly the quality control review system including the effectiveness of the quality control review. We will contribute to this examination through evaluation when receiving a review report from the JICPA and the examination of the results of the CPAAOB's inspection.

Furthermore, we will maintain effective cooperation between the CPAAOB and the JICPA, exchanging views on the preferable manner of quality control review that can lead to an effective improvement in practices and improvement in audit quality.

In addition, we will discuss the appropriate role sharing with the JICPA, taking into account the JICPA's efforts to improve the effectiveness of its quality control review.

(b) Collection of reports

▪ Continuous collection of reports from large-sized audit firms

The CPAAOB will continuously request them to provide quantitative and qualitative information in the collection of reports, which are necessary for the inspection of business management (governance) environment and service management environment.

After analyzing the information obtained through the collection of reports, we will use it to make our inspections more effective and efficient. At the same time, we will use the information for comparative analysis of large-sized audit firms and identification of issues commonly found across large-sized audit firms.

▪ Collection of reports from second-tier and small and medium-sized audit firms not subject to on-site inspections

Regarding the performance of audit engagements, we will collect reports from audit firms in a timely manner in order to encourage them to continue appropriate audit quality control.

Based on their individual characteristics, we will intensively examine the status of the development of the quality control system at the audit firms, the management policies of their leaders, revenue/financial structures,

organizational structures and human resources.

- Collection of reports on status of improvement after conducting inspections (follow-up)

After a certain period of time from the date of the notification of the inspection results, we will collect reports from the relevant audit firms to examine how much they have improved their quality control as necessary. If an audit firm is found through inspection to have deficiencies in its business operation and to be required immediate improvement, we will consider collecting a report on its improvement plan and the progress of the plan simultaneously with notification of the inspection results.

(ii) Basic Inspection Plan

we will conduct inspections with a focus on the below mentioned aspects according to the type of audit firm in this program year.

- (1) Whether the below items, which are prepared by audit firms to ensure and improve the quality control environment, are appropriate according to the size and characteristics of the audit firms:

- the basic management policy and measures related to business management
- measures for securing the fair execution of services, such as measures related to compliance with laws and regulations.

- (2) Whether audit firms implement acceptance and continuance of engagements, formulation of audit planning, and other audit procedures by implementing an appropriate assessment of business risk including the economic circumstances and the corporate environment surrounding the audited companies.

- (3) Whether audit firms subject to inspection take their own initiatives in addressing identification of the root causes of their deficiencies and taking actions for effective improvements through fundamental measures.

(a) Large-sized audit firms

Taking into account their role in the capital market and domestic and international trends related to supervision of auditors, we will cyclically inspect large-sized audit firms based on our evaluation results pertaining to the JICPA's quality control review.

We need to conduct inspection with more emphasis on large-sized audit firms' business management (governance) environment and service management environment.

We will conduct inspection with a focus on the below mentioned items in this program year.

- Inspection of procedures to take on new audit contracts, especially those pertaining to large-sized listed companies.
- Inspection of the status of internal control assessment of companies including overseas operations and group audits including overseas subsidiaries, etc.

We will conduct inspection from the standpoint of whether audit firms' operation control structure is effective, which is established and strengthened in response to the Audit Firm Governance Code.

Moreover, from the standpoint of strengthening follow-up to inspection, we will conduct a follow-up inspection in the following program year in order to check if the deficiency pointed out at the inspection in the previous program year is being steadily remedied.

(b) Second-tier audit firms

Taking into account the situation of the entities and an audit firm's business profile, we will cyclically inspect second-tier audit firms in light of their significance in the Japanese audit industry.

We will conduct inspection with a focus on the below mentioned items in this program year.

- Inspection with a focus on essential problems in the business operation by obtaining information with high importance related to quality control and engagements at the audit firm, taking into account the previous inspection results and the status of monitoring by overseas business partners, and paying attention to engagement risk.
- Inspection of business management environment and service management environment, such as unity as an organization, etc.

(c) Small and medium-sized audit firms

Regarding small and medium-sized audit firms, we will conduct inspection, mainly confirmation of the audit quality, such as audit firm's quality control environment and service management environment based on the intention and nature of the managing partner and the partners and the conformity of individual engagements with audit standards. We will conduct inspection as needed.

For this purpose, we will conduct inspection with a focus on the below mentioned items in this program year.

- Inspection with consideration of issues related to business operations and quality control attributable to a small and medium-sized audit firm's systems. Especially, inspection of business management environment and service management environment, including aspects such as unity as an organization,

etc.

2.3 Monitoring and Inspections of Audit Firms

Audit firms, using the name “certified public accountant”, may audit or attest financial documents for fees at the request of others (Article 2(1) of the CPA Act) and compile financial documents, examine or plan financial matters, or provide consulting services on financial matters for fees at the request of others (Article 2(2) of the CPA Act).

As of the end of FY2017, the number of registered certified public accountants totals 30,350, of which the number of CPAs belonging to large-sized audit firms is 11,016 or approximately 40% of the total and the number of audit firms totals 229.

(Reference)

| | End of FY2013 | End of FY2014 | End of FY2015 | End of FY2016 | End of FY2017 |
|---|------------------|------------------|------------------|------------------|------------------|
| Number of registered certified public accountants | 26,260 | 27,313 | 28,286 | 29,367 | 30,350 |
| Large-sized audit firms | 10,074 | 10,312 | 10,846 | 11,002 | 11,016 |
| Number of audit firms | 216 | 219 | 214 | 222 | 229 |

2.3.1 Quality Control Reviews by the Japanese Institute of Certified Public Accountants (JICPA)

(i) FY2016

In FY2016, the JICPA performed 101 quality control reviews of audit firms (71 audit firms (including 2 large-sized and 3 second-tier audit firms; 1 joint CPA office), and 30 CPAs). The conclusions are presented in the following table.

Conclusions based on the Results of Reviews (FY2016) (Number of audit firms)

| Category | Unqualified conclusion | | Qualified conclusion | | Disclaimer of Opinion | | Adverse Opinion | | Total (e) |
|------------|------------------------|-------|----------------------|-------|-----------------------|-----|-----------------|-----|--------------|
| | (a) | a/e | (b) | b/e | (c) | c/e | (d) | d/e | |
| Audit firm | 58 | 81.7% | 13 | 18.3% | — | — | — | — | 71 |
| CPA | 26 | 86.7% | 4 | 13.3% | — | — | — | — | 30 |
| Total | 84 | 83.2% | 17 | 16.8% | — | — | — | — | 101 |

(Note) 98 out of 101 cases include recommendations for improvement.

(ii) FY2017

In FY2017, the JICPA performed 96 quality control reviews of audit firms (72 audit firms (including 2 large-sized and 2 second-tier audit firms; 4 joint CPA offices), and 24 CPAs). As the table below shows, all had been performed by March 31, 2018.

Status of Implementation of Quality Control Reviews

| Date of quality control review | 2017 | | | | | | | 2018 | | | Total |
|--|------|------|------|------|------|------|------|------|------|------|-------|
| | Jun. | Jul. | Aug. | Sep. | Oct. | Nov. | Dec. | Jan. | Feb. | Mar. | |
| Number of audit firms reviewed for quality control | 0 | 13 | 17 | 1 | 16 | 24 | 17 | 7 | 1 | 0 | 96 |

Of the quality control reviews conducted in FY2017, 43 cases, the details of which had been approved by the Quality Control Committee, had been reported to the CPAAOB as of March 31, 2018. The conclusions of those reports were as follows.

- Unqualified conclusion: 41 cases (30 audit firms, 11 CPAs)
- Qualified conclusion: 2 cases (2 audit firms)

2.3.2 *Monitoring of Quality Control Reviews*

(i) Purpose

Monitoring is conducted for the purpose of confirming that audit firms are implementing quality controls and providing audit services appropriately, and in order to examine that the JICPA is investigating the audit quality controls implemented by audit firms and ensuring that audit firms make improvements where necessary.

(ii) Monitoring flow

The results of quality control reviews received from the JICPA are analyzed widely to determine whether there are any qualified items and to ascertain the details and number of deficiencies. The content of the improvement plans submitted to the JICPA by each audit firm are also analyzed. In addition, the appropriateness of the JICPA reviews are monitored.

To ensure that the results of monitoring that have been analyzed will contribute to making improvements effective and enhancing audit quality, they are used to select audit firms for inspection and audit firms from which reports will be collected (see (3) below) as well as when exchanging opinions with the JICPA.

Information obtained as a result of cooperation and opinion exchanges with related departments inside the Financial Services Agency and related organizations, etc.

such as the JICPA, securities exchanges, the Japan Audit & Supervisory Board Members Association, etc. is also used during monitoring.

(iii) Results of the analysis of quality control reviews in FY2016

Regarding audit firms subject to qualified items, more serious matters were pointed out than in FY2015. In some cases, for example, not only were there deficiencies in substantive procedures for audits of accounting estimates, but there were also qualified items going all the way back to the beginning of the audit process, such as deficiencies in the correction of audit plans.

With regard to quality-control-related findings, there were many cases of qualified items that were linked to the deficiencies of quality control systems of audit firms. Among the findings relating to individual audit engagements, for example, there were deficiencies in the “instructions provided by and supervision performed by audit managers and the review of audit documentation,” the “examination of audit engagements,” and “periodic inspections.”

As stated above, while improvements were seen, there remained cases where findings were not deep enough. In some cases, for example, only issues with documentation were pointed out, rather than deficiencies with audit procedures. And there were also situations where reports were not being applied in a flexible enough way. For example, there were few cases where the review period was extended.

Note that with regard to the FY2017 quality control reviews, analysis will be performed after all the reports have been received.

2.3.3. *Collection of Reports, from Audit Firms*

(i) Ongoing collection of reports from large-sized audit firms

In PY2017 the CPAAOB collected reports from all large-sized audit firms for the purpose of monitoring their business management (governance) environment and operations management environment and so on (reports were collected in July 2017). In addition to analyzing information obtained through these reports and employing the findings to ensure that inspections would be effective and efficient, the CPAAOB also used them to obtain overall understanding with regard to quality control at large-sized audit firms. The CPAAOB plans to continue collecting reports annually in the future.

(ii) Collection of reports from second-tier audit firms and small and medium-sized audit firms

Based on the PY2017 Basic Plan for Monitoring Audit Firms, the CPAAOB

collected reports from 51 audit firms for which it was deemed necessary to monitor improvements made by second-tier audit firms and small and medium-sized audit firms in response to quality control reviews and determine the situation with regard to business management environment, etc. at such firms (reports were collected in August 2017).

History of Collection of Reports

| | Record of Report Collection in PY2017 | | Record of Report Collection in PY2016 | |
|--------------------|---|--|---|--|
| | No. of firms undergoing report collection | No. of firms undergoing QC reviews in FY2016 | No. of firms undergoing report collection | No. of firms undergoing QC reviews in FY2015 |
| Audit firms | 51 | 101 | 83 | 83 |
| Audit firms (Note) | 47 | 71 | 57 | 57 |
| Individual firms | 4 | 30 | 26 | 26 |

(Note) Including CPA joint office

With regard to the collection of reports, some of the second-tier audit firms and small and medium-sized audit firms from which the results of FY2016 quality control reviews had been received were selected based on factors such as the importance of the review results. The collection of reports in PY2016 focused on comprehensive coverage, with the aim of identifying the situation in the entire sector.

(iii) Collection of reports on status of improvement after conducting inspections (follow-up)

In PY2017 the CPAAOB collected reports from three audit firms (including one that had also submitted a report in PY2016) that had been informed of the results of inspections in order to confirm the status of improvements made in response to deficiencies identified during inspections. Note that one of the three audit firms from which reports were collected was deemed to need to make rapid improvements. The CPAAOB is confirming the content of reports submitted by audit firms.

2.3.4 *Inspections of Audit Firms*

In PY2017 the CPAAOB conducted inspections of large-sized audit firms, second-tier audit firms, and small and medium-sized audit firms based on their situations and in accordance with the Basic Plan for On-site Inspections (see 2.2.2 (ii) above).

With regard to large-sized audit firms, inspections are generally performed once every two years, with a follow-up inspection conducted in the following program year. Specifically, the CPAAOB conducted ordinary inspections of two firms and follow-up inspections of two firms.

With regard to second-tier audit firms, inspections are generally performed once every three years. Specifically, the CPAAOB conducted inspections of two firms.

With regard to small and medium-sized audit firms, inspections are performed as necessary. Specifically, the CPAAOB conducted inspections of three firms.

During these inspections, the CPAAOB carried out inspections aimed at encouraging the audit firms to make effective improvements based not only on the direct causes of deficiencies but also on the analysis of the root causes of the deficiencies concerned and fundamental responses.

Status of commencement of inspections in most recent five years (as of March 31, 2018)

| FY/PY | 25 | 26 | 27 | 28 | 29 |
|------------------------------------|----|----|----|----|----|
| Large-sized audit firms | 2 | 2 | 2 | 4 | 4 |
| Second-tier audit firms | 2 | 1 | 1 | 2 | 2 |
| Small and medium-sized audit firms | 9 | 11 | 6 | 5 | 3 |
| Foreign audit firms | 0 | 1 | 0 | 1 | 0 |
| Total | 13 | 15 | 9 | 12 | 9 |

Note: From July 2016 periods have been changed to program years (July through the following June). Because PY2016 was the year in which this change was made, the data for it includes inspections conducted in April-June 2016.

2.3.5 Recommendations to the Commissioner of the Financial Services Agency (FSA)

As a result of inspection, the CPAAOB found that Aria Audit Corporation performed audit services in a grossly inappropriate manner. Pursuant to the provisions of Article 41-2 of the CPA Act, on June 8, 2017 the CPAAOB recommended that the Commissioner of the FSA take administrative actions and other measures against it.

2.3.6 Inspections and Oversight on Foreign Audit Firms

(i) Situation with foreign audit firms

When providing services overseas deemed to correspond to audit attestation services for financial statements submitted by foreign companies, etc. under the Financial Instruments and Exchange Act, parties providing such services shall notify the Commissioner of the Financial Services Agency in advance. The situation with foreign audit firms, etc. is as follows:

Situation with foreign audit firms, etc. (as of March 31, 2018)

| | Number of countries/regions | Number of audit firms, etc. |
|-------------------------|-----------------------------|-----------------------------|
| North America | 2 | 9 |
| Central & South America | 3 | 9 |
| Europe | 15 | 44 |
| Asia & Pacific | 10 | 27 |
| Middle East | 1 | 2 |
| Total | 31 | 91 |

(ii) A framework for information requirement and inspections on foreign audit firms, etc.

In relation to the treatment of foreign audit firms, etc., the CPAAOB collects reports from and conducts inspections of foreign audit firms, etc. in accordance with the “A Framework for Inspection/Supervision of Foreign Audit Firms, etc.” and the “Basic Guidelines on Information Requirements and Inspection of Foreign Audit Firms, etc.”

Under the above Framework and Guidelines, the CPAAOB will collect reports from foreign audit firms, etc. once every three years, in principle. It will then analyze the information submitted, and if it deems it necessary to conduct an inspection to confirm, for example, that operations regarded as equivalent to audit attestation services are being performed appropriately, it will conduct an inspection of the foreign audit firm, etc. concerned. However, with respect to information requirements and inspections regarding foreign audit firms, etc., the CPAAOB will generally rely on such actions by the competent authorities of the firms’ home jurisdictions (“foreign competent authorities”), instead of seeking to obtain information from or conducting inspections on firms themselves provided (a) audit and public oversight systems in the firms’ home jurisdictions are equivalent to those of Japan, (b) necessary information can be provided from the foreign competent authorities through appropriate arrangements of information exchange, and (c) reciprocity is ensured.

(iii) Information requirement to foreign audit firms

In accordance with the Framework and Guidelines described in (ii) above, the CPAAOB collected reports from foreign audit firms in FY2012 and FY2015. Furthermore, in PY2017, the CPAAOB asked the competent authorities in the country in which certain foreign audit firms, etc. were based to provide information on the situation with these audit firms, in accordance with the framework for exchanging information with competent authorities in these countries.

(Note) See “3.2. Bilateral cooperation” on p.31 for details of the information exchange framework.

(iv) Inspections of foreign audit firms, etc.

With regard to the foreign audit firms, etc. mentioned in (iii) above, based on the information submitted through the collection of reports in FY2015, the CPAAOB gave concrete consideration of inspection of the firms and endeavored to strengthen cooperation with the competent authorities in which the firms is located. The CPAAOB performed an inspection of one foreign audit firm, etc. in May 2017.

2.4 Dissemination of Information relating to Oversight and Inspection

2.4.1 Preparation and Publication of “Case Report from Audit Firm Inspection Results”

Since its establishment in April 2004, the CPAAOB has, from the viewpoint of serving the public interest and protecting investors, inspected audit firms and CPAs for ensuring and improving the quality of audits conducted in Japan. As part of these efforts, each year since 2008 the CPAAOB has compiled and published a Case Report containing its main findings with the goal of encouraging audit firms to act independently to ensure and improve quality. The CPAAOB has expanded the content of the Case Report each year. For example, the CPAAOB has indicated the “required action” that the CPAAOB expects to be taken with respect to audit quality.

The Case Report published on July 26, 2017 basically follows the structure of the previous year’s edition (published in July 2016), but has been updated to include, for example, the latest inspection cases, and the content has been made easier to understand. The key changes made are as follows:

- “I. Root Cause Analysis and Operation Management Environment”
The Case Report explains the relationships between governance and the root causes of deficiencies and gives examples of large-sized audit firms that are taking independent action to identify root causes.

- “III. Individual Audit Engagements”

Around 30% of the cases have been replaced with ones that relate to the most recent inspections. In “fraud in audits of financial statements,” the explanations of the inspection cases and important points have been expanded to reflect the growing importance of accounting fraud.

And to illustrate examples of proactive efforts by audit firms, which can serve as a reference to others, the section on “commendable initiatives” has been expanded to include, for example, initiatives taken to improve group audits.

The CPAAOB hopes that audit firms will refer to the identified deficiencies, causes, etc. presented in the Case Book when they perform self-inspections of individual audit engagements and the system of quality control. The CPAAOB also hopes that when a deficiency is discovered, the audit firm not only corrects the deficiency, but also investigates the root causes that led to the deficiency and endeavors to improve its quality controls.

The full text of the Case Report can be viewed on the CPAAOB’s website in both Japanese and English. The Japanese (original) version was made available on July 26, 2017, while the English version was published in December of the same year. The URLs are as follows:

Japanese: <http://www.fsa.go.jp/cpaaob/shinsakensa/kouhyou/20170726.html>

English: <http://www.fsa.go.jp/cpaaob/english/oversight/20171225/20171225.html>

2.4.2 Preparation and Publication of “Monitoring Report in 2017”

Since 2016, the CPAAOB has published Monitoring Reports to provide information about audit firms in an easy to understand form. These reports are not only for audit and accounting specialists but also for a non-specialized audience.

Under circumstances that the role of audit in capital markets is becoming increasingly important, it has become vital that the quality of audits performed by audit firms is appropriately assessed by market participants including shareholders, corporate insiders such as company auditors and corporate executives, and investors. The CPAAOB has intended to publish the reports for promoting market participants’ understanding of audit firms.

The 2017 edition report published on July 26, 2017, has included data that facilitates

understanding of the situations at audit firms, as have descriptions based on materials and information obtained by the CPAAOB through its monitoring activities, which include inspections and the collection of reports. The key changes made are as follows:

- Overall rating of the operation of audit firms
The CPAAOB gives overall ratings of audit firms with the aims of accurately conveying to audit firms the results of the assessments the CPAAOB has made through its inspections, and to help company auditors etc. better understand levels of quality control at audit firms.
- Environment for Supporting Audit Services
Audit firms provide support for the audit teams that carry out audit engagements to enable them to conduct deep-probing audits. Specifically, an overview of environment of support provided by quality control departments etc, and examples of cross-departmental management of risk information and the use of IT.
- Changes in auditors of listed companies
Regarding changes in auditors of listed companies, the number of changes in auditors of listed companies has been high during the last two years, when looking at data for the past five years, from June 2013 to June 2017. This report has also mentioned the reasons for changes and changes in audit fees before and after the changes.

The full text of the “Monitoring Report in 2017” can be viewed on the CPAAOB’s website in both Japanese and English. The Japanese (original) version was made available on July 26, 2017, while the English version was published in December of the same year. The URLs are as follows:

Japanese: <http://www.fsa.go.jp/cpaaob/shinsakensa/kouhyou/20170726/20170726.html>

English: <http://www.fsa.go.jp/cpaaob/english/oversight/20171225/20171225.html>)

2.4.3 Lectures, etc. on Inspection Results (the Case Report)

The CPAAOB chairperson and inspectors give lectures, etc. at workshops organized by the JICPA or other relevant organizations to lecture on inspection results (the Case Report) in order to contribute to making the performance of audit procedures more appropriate.

In PY2017, the CPAAOB delivered 12 lectures for CPAs at workshops held at the JICPA headquarters and 11 regional chapters across Japan from October to December 2017, to promote voluntary activities aimed at securing and improving audit quality. The CPAAOB also delivered two lectures for audit & supervisory board members at the Japan Audit & Supervisory Board Members Association (JASBA) in December 2017 so that the Case Report may be widely used to understand the conditions regarding external audits.

In addition, the CPAAOB placed introduction of the Case Report in the bulletins and other publications of relevant organizations such as the JICPA and the JASBA, so that audit firms, etc., can actively use the Case Report for reference purposes.

2.5 Cooperation with Relevant Organizations

To maintain and improve the quality of audits, it is important not only to secure the effectiveness of audits conducted by audit firms but also to share information on common audit-related challenges and have mutual understanding on issues by further enhancing cooperation with audit firms and companies subject to audit .

For this purpose, the CPAAOB exchanges opinions not only with the relevant FSA divisions but also with other relevant organizations, including the JICPA and stock exchanges.

2.5.1 Cooperation with Relevant Divisions of the FSA

The CPAAOB shared information and exchanged opinions with the Securities and Exchange Surveillance Commission concerning issues with the disclosures and audits of listed companies and with the Supervisory Bureau and the Inspection Bureau concerning issues with the audits of financial institutions since cooperation with relevant FSA divisions which investigate or inspect companies will enable more effective and efficient inspection, etc. The information acquired from sharing and exchanges of opinions was applied to monitoring.

Furthermore, the CPAAOB frequently shared information with the Coordination and Planning Division concerning the results of inspections of audit firms for which recommendations have been issued.

2.5.2 Cooperation with the JICPA

The CPAAOB, as a government authority, conducts monitoring to facilitate further improvements in the effectiveness of the JICPA's quality control reviews, and to ensure that audit firms fairly perform audit services. It is expected that, as a reviewer of the quality control reviews, the JICPA further improves the effectiveness of its reviews through enhancement of the review implementation environment to ensure that audit firms manage the quality of audits in a proper manner. Therefore, the CPAAOB addresses information sharing and enhancement of cooperation with the JICPA through discussions with the JICPA's executives and reviewers on problems identified through monitoring.

In PY2017, the CPAAOB exchanged opinions with the JICPA about measures to enhance quality control review, issues surrounding quality control reviews detected in the CPAAOB's inspections and the expansion in the disclosure of review findings.

2.5.3 Cooperation with Stock Exchanges

The CPAAOB cooperated with Stock Exchanges, self-regulatory organizations for listed companies, by exchanging opinions concerning internal-control issues identified through monitoring that are common to all listed companies, changes in auditors, etc. so that both parties can have the mutual understanding on issues.

2.5.4 Cooperation with the Japan Audit & Supervisory Board Members Association (JASBA)

The CPAAOB places importance on cooperation with company auditors who perform corporate governance for their companies in light of facilitating appropriate disclosure of financial information by companies. Therefore, the CPAAOB has verified communication between company auditors and auditors in inspections of audit firms. In addition, as a result of the revision of the Companies Act and the implementation of the Corporate Governance Code, the roles and duties of company auditors have become increasingly important.

Therefore, the CPAAOB exchanged opinions with the JASBA and discussed issues such as overall rating of the operation of audit firms and communication between company auditors and auditors in June 2017. The CPAAOB also provided information on deficiencies identified in inspections and problems, etc. at audit firms to company auditors through lecture meetings, etc. held by the JASBA.

2.6 Actions for issues in PY2017 and Next Challenges

2.6.1 Improvement of Effectiveness of Inspections Mainly for Large-sized Audit Firms

Recent accounting scandals have led to questions being raised again about the credibility of accounting audits. The CPAAOB published a report entitled “Improvement of Effectiveness of the CPAAOB Inspections – Mainly for Large-sized Audit Firms –” on March 24, 2016.

Based on this report, the CPAAOB conducted the follow-up inspections for large-sized audit firms in PY2017 just as it did during the previous program year.

The main aim of these inspections was not to identify more individual deficiencies, but rather to conduct investigations focused on the effectiveness of governance and voluntary effort for improvement implemented by audit firms, and to encourage large-sized audit firms to improve their ability to make improvements autonomously.

The CPAAOB has amended its inspection process for making inspections more effective and efficient. For example, the CPAAOB has requested information from audit firms (the prior collection of reports) and analyzed the information before on-site inspection.

Because the entities responsible for ensuring and improving audit quality are audit firms, the CPAAOB will continue to conduct inspections with a focus on encouraging audit firms to act autonomously to enhance audit quality also in PY2018.

2.6.2 Response to the Audit Firm Governance Code

On March 31, 2017 the FSA announced the “Principles for Effective Management of Audit Firms (The Audit Firm Governance Code),” and large-sized audit firms, second-tier audit firms, etc. have declared adopting the Code.

The CPAAOB is already focusing its investigations more on the business management (governance) environment as well as operations management environment. The CPAAOB will continue to verify the environment that has been established and strengthened by audit firms and because audit firms, particularly large-sized ones, are currently working to improve these systems in response to the Code.

2.6.3 Monitoring of Audit using IT and Group Audits

Recently, some large-sized audit firms and second-tier audit firms have strengthened

environments for managing risk information on a cross-department basis and their responses to group audits by international departments. Some are also supporting audit engagements by, for example, introducing IT tools for analyzing accounting data at audited companies. The adoption of IT, in particular, partly depends on development policies and investment trends of global audit networks. The CPAAOB has endeavored to obtain information of audit firm's efforts through opinion exchanges, etc. in PY2017.

Also in PY2018, the CPAAOB will continue to obtain information about these circumstances and will also find out about matters such as whether human resources that can cope with the increasingly deep and complex nature of audit methods have been secured and developed.

2.6.4 Ensuring Cybersecurity

Recently, audit firms have been introducing IT in audit engagements, such as by obtaining huge volumes of electronic data from companies and analyzing it in response to the increasing adoption of IT by companies and the digitalization of accounting data and transaction data. However, cybersecurity risk has increased with cyberattacks becoming increasingly sophisticated and large scale. Ensuring cybersecurity is an urgent task because the leakage of corporate information possessed by audit firms would have a significant impact on the reputation of audit firms.

With this understanding, the CPAAOB will exchange opinions and conduct interviews with mainly large-sized and second-tier audit firms to find out about their policies and structures relating to cybersecurity and their responses to cybersecurity risk also in PY2018. In this way, the CPAAOB will ascertain the situation and encourage audit firms to take appropriate action.

2.6.5 Ongoing Follow-up of Efforts by the JICPA to Improve the Functionality of Quality Control Reviews, etc.

Since its establishment, the CPAAOB, as a government authority, has set its objective to encouraging further improvement of quality control review by the JICPA.

In PY2017 the CPAAOB organized study sessions concerning quality control approaches that would lead to effective improvements and enhanced audit quality based on the CPAAOB inspections' findings. The results will be reflected in the FY2018 quality control reviews and PY2018 inspections.

Furthermore, the CPAAOB and JICPA will discuss the appropriate division of roles. These discussions will take into account efforts to enhance the effectiveness of the quality control reviews performed by the JICPA.

2.6.6 Strengthening the Dissemination of Information

(i) Communication of “Key Points”

The CPAAOB has broadened an obligation from large-sized audit firms to all audit firms to communicate the “Key Points” presented in inspection results notifications to company auditors, etc. of audited companies since PY2017.

(ii) Enrichment of Monitoring Report

Since the 2017 edition, the Monitoring Report has been published separately from the Case Report, and the 2018 edition will be further expanded to reflect the additional monitoring information that has been collected and accumulated.

2.6.7 Enhancing the CPAAOB Monitoring Structure for Addressing Challenges

The CPAAOB monitoring needs to appropriately adapt to the issues with audit firms described above and to the internationalization of accounting procedures, which is occurring as a result of factors such as the increasing overseas expansion of companies and the rise in the number of overseas transactions. The CPAAOB therefore believes it important to continue to enhance its monitoring system, including the procurement of personnel and the enhancement of its information collection and analysis system.

3 Cooperation with Relevant Organizations in Other Jurisdictions

3.1 Activities of the International Forum of Independent Audit Regulators (IFIAR)

3.1.1 Background

Triggered by accounting scandals such as at Enron and WorldCom in the United States (the U.S.A.), the need to ensure and improve the audit quality was recognized, and since 2002, audit oversight regulators independent from the accounting profession have been established in jurisdictions throughout the world.

Amid such circumstances, the first unofficial meeting of audit oversight regulators was held in Washington, D.C., in September 2004, organized by the Financial Stability

Forum (FSF) (now the Financial Stability Board (FSB)), for the purpose of sharing information among respective members' jurisdictions. The meeting was attended by nine jurisdictions: Japan, the U.S.A., the U.K., Germany, France, Italy, Canada, Australia, and Singapore. Subsequently, a series of further informal meetings were held. Momentum was gathered for the establishment of a permanent international forum, and at the fifth meeting of audit oversight regulators held in Paris in September 2006, formal approval was given for the establishment of the International Forum of Independent Audit Regulators (IFIAR). Its first Plenary Meeting was held in Tokyo in March 2007, hosted by the CPAAOB, and was attended by the audit oversight authorities of 22 jurisdictions.

According to the Charter adopted at the 4th Plenary Meeting, which was held in Cape Town in September 2008, the purpose of the IFIAR is to engage in activities i-iii below. Later, at the 13th Plenary Meeting held in Noordwijk in April 2013, the Charter was revised with the addition of iv below.

- i Sharing knowledge of the audit market environment and practical experience of independent audit regulatory activity with a focus on inspections of auditors and audit firms;
- ii Promoting collaboration and consistency in regulatory activity;
- iii Initiating and leading dialogue with other policy-makers and organizations that have an interest in audit quality; and
- iv Forming common and consistent views or positions on matters of importance to its Members, taking into account the legal mandates and missions of individual members.

3.1.2 Organization

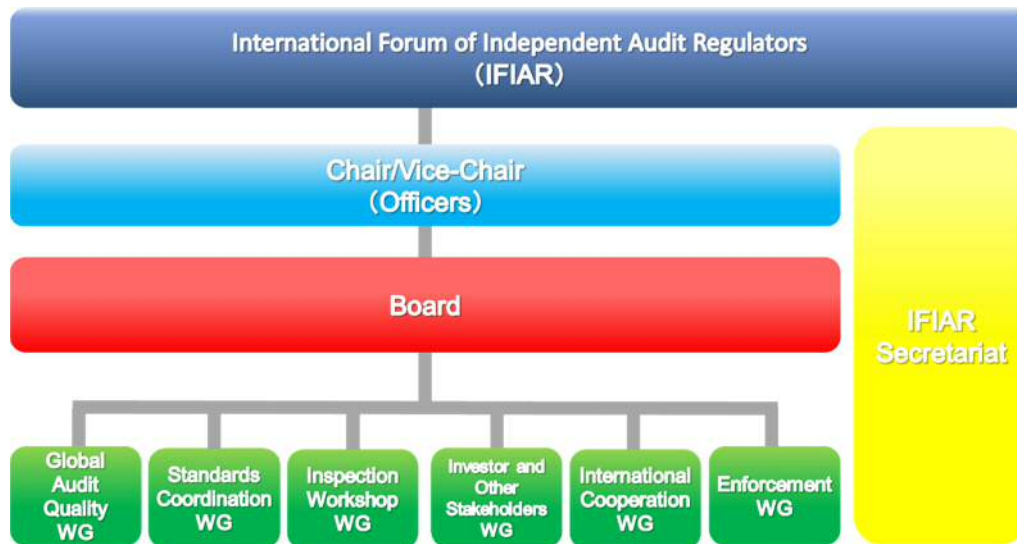
The IFIAR comprises audit oversight authorities from jurisdictions with eligibility for membership. As of March 31, 2018, the number of participating jurisdictions was 52.

Important decisions are made at the Plenary Meeting, in which audit oversight authorities from all member jurisdictions participate. The 17th Plenary Meeting was held in Tokyo in April 2017.

To enable the IFIAR to conduct its activities efficiently, the posts of Chair and Vice-Chair are assigned to individuals. As of March 31, 2018, the Chair country was Canada while the Vice-Chair country was Switzerland. Following the establishment of the permanent Secretariat in April 2017, the IFIAR Board, a new governing body comprising 15 board members, including Japan, was established, and the first meeting of the Board was held in Tokyo.

Furthermore, as of March 31, 2018 the IFIAR has six working groups. The purposes and activities are described in detail in 3.1.4 (ii).

IFIAR Organization Chart (as of March 31, 2018)



3.1.3 Establishment of IFIAR Secretariat in Tokyo

In recent years, the IFIAR grown rapidly from being a forum for the exchange of opinions among competent authorities in each jurisdiction to become an organization conducting practical activities as an international body. In addition, it is increasingly necessary for the IFIAR to enhance its relationships with other international organizations, including the Financial Stability Board (FSB), the International Organization of Securities Commissions (IOSCO) and the Basel Committee on Banking Supervision (BCBS). Under these circumstances, the establishment of a permanent secretariat was discussed at the Washington, D.C. 14th Plenary Meeting in April 2014.

From the viewpoint of international contribution to the improvement of audit quality through the IFIAR, improvement of Japan’s influence in international financial regulatory activities, including audits, and contribution to the establishment of Tokyo’s presence as an international financial center, in January 2015 the CPAAOB and the FSA ran for candidacy to host the Secretariat. The CPAAOB and the FSA, in cooperation with related ministries and agencies, sought support for Tokyo as the host country of the Secretariat from IFIAR’s other member authorities. Private-sector business groups, audit-related organizations, etc. also issued statements in support.

As a result of these efforts, a decision was made to establish the Secretariat in Tokyo at the 16th Plenary Meeting in London in April 2016, and the Secretariat opened in April 2017.

Furthermore, in December 2016 the Japan IFIAR Network was established by stakeholders in Japan for the purpose of supporting the activities of the Secretariat and raising awareness of audit quality in Japan.

3.1.4 *Activities*

i Activities of the Plenary Meeting

(i) 17th Plenary Meeting in Tokyo

The 17th Plenary Meeting was held in Tokyo from April 3 to 6, 2017, and was hosted by the CPAAOB and the FSA.

At the meeting, an opening ceremony of the Secretariat was held, and there was also a signing ceremony for the Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (MMOU), which was signed by representatives of audit oversight authorities from 22 jurisdictions. In addition, a report entitled “Audit Committees and Audit Quality: Trends and Areas for Further Consideration,” which was prepared by the Investors and Other Stakeholders Working Group was published.

There was also a discussion involving the Chairs of standards-setting bodies (International Auditing and Assurance Standards Board (IAASB) and International Ethics Standards Board for Accountants (IESBA)) and the Public Interest Oversight Board (PIOB) on how standards setting can contribute to enhancing audit quality. The CEOs of the six largest international audit networks (see Note) also discussed audit quality.

(Note) The six largest international audit networks are comprised of Deloitte Touche Tohmatsu, Ernst & Young, KPMG, PricewaterhouseCoopers, BDO and Grant Thornton.

(ii) Board

In 2015, the execution structure, which had hitherto been led by the Chair and the Vice-Chair, was overhauled in order to make the IFIAR function better as an international body. Agreement was reached to establish an execution structure based on a council system that is led by the member countries (board structure). As a result of these governance reforms, in April 2017 the IFIAR established the Board, and in

conjunction with this move, the Advisory Council, which had served as an advisory body to the Chair and Vice-Chair was scrapped. The Board is a decision-making organ comprising nominated members from eight authorities and elected members from up to eight authorities, to give a total of 16 members. Japan was officially made a nominated member in accordance with the selection procedures (points system) prescribed in the IFIAR Charter at the IFIAR Plenary Meeting held in April 2017.

The Board deliberates on the IFIAR's Strategic Plan and conducts high-level discussions on the administration of the IFIAR's operations. In FY2017, the Board meetings were held in Tokyo on April 7, in Toronto on October 19 and 20, and in Zurich on January 22 and 23, 2018.

(iii) Inspection Findings Report

Since 2012, with the aim of providing information on trends discovered during inspections by the member authorities, the IFIAR has compiled the results of inspections performed by member authorities of the six largest international audit networks in the form of an "Inspection Findings Report." This report contains aggregated inspection results in the two categories of quality control systems and individual audit engagements, and calculates the rate at which deficiencies were identified in each of the categories.

The sixth 2017 survey covered 42 authorities (as of March 31, 2018, the total number of IFIAR member jurisdictions was 52). The 2017 survey found that deficiencies were identified in 40% of individual audit engagements of listed companies inspected by the member authorities as a whole. This was slightly decreased from the 42% captured in the 2016 survey.

ii Activities of each working group

(a) Global Audit Quality (GAQ) Working Group

The aim of this working group (WG) is to exchange views with the six largest international audit networks on the quality control of global audits. The WG maintains dialogue with each network on such topics as the quality control systems of global audit networks, and shares information between authorities on improvements in quality control and on the organizational expansion of each network.

The WG had also proposed to have several authorities conduct multijurisdictional inspections of audit firms that are part of large audit networks in order to assess the effectiveness of group audits of multinational companies, and in 2015 and 2016

Japan (CPAAOB) took the lead in conducting the inspections.

The WG's meetings were held on October 16 to 18, 2017 in Toronto and on March 13 to 15, 2018 in Amsterdam. At these meetings, the participants discussed audit related topics such as data analytics initiatives at audit firms, culture, cybersecurity, and future action for reducing the rate of identified deficiencies.

(b) Standards Coordination Working Group

The aims of this WG include the exchange of views on the setting of international standards at the IAASB and IESBA and the preparation of comment letters in response to exposure drafts published by these standard-setting bodies.

(c) Inspection Workshop Working Group

This WG plans, coordinates and evaluates the IFIAR inspection workshop. This workshop is held every year for the purpose of skill training for inspectors and to share inspection methods and experiences.

At the first IFIAR Plenary Meeting in Tokyo in 2007, it was agreed that the inspection workshop would be held, led by the inspectors of the IFIAR members, for the purpose of sharing information on the inspection methods of audit oversight authorities and on issues related to inspections, as well as providing training for inspectors. Since then, the workshop has been held every year, with planning and coordination provided by this WG.

The 12th inspection workshop was held between February 20 and 22, 2018, and was hosted by the Sri Lanka Accounting and Auditing Standards Monitoring Board (SLAASMB). 112 inspectors and others participated from 41 jurisdictions, including Japan, and the CPAAOB sent two chief inspectors to serve as panelists.

(d) Investor and Other Stakeholders Working Group

The aim of this WG is to engage in dialogue with investors and other stakeholders as users of audit reports on issues such as the audit quality and what audit reports ought to be like. The WG also plans and coordinates the exchange of views with investor representatives at the IFIAR Plenary Meeting.

The WG has compiled a report entitled "Audit Committees and Audit Quality: Trends and Areas for Further Consideration," which was published as an IFIAR document on April 7, 2017.

(e) International Cooperation Working Group

The aim of this WG is to promote the practical exchange of information on regulations and inspections between audit oversight authorities, and it has been working on such tasks as establishing the MMOU.

The MMOU was finalized in June 2015, and at the Tokyo Plenary Meeting in April 2017, it was signed by audit oversight authorities from 22 jurisdictions, including the CPAAOB and the FSA.

The WG also conducts research on obstacles to international activities by audit firm partners, ways of utilizing supervisory colleges by audit oversight authorities, and so on.

(f) Enforcement Working Group

The aim of this WG is to promote cooperation between audit oversight authorities in the area of enforcement, including investigations, and facilitate exchange of information on enforcement regimes and developments in member jurisdictions, in order to enhance investor protection and improve audit quality.

Japan chaired this WG from its foundation in July 2013 until April 2017.

3.2 Bilateral Cooperation

In light of the globalization of corporate activities, ensuring the quality of audit procedures that, such as using the audit results of overseas audit firms in the audit of consolidated financial statements, has become globally more important than ever before. Moreover, enhancing cooperation with foreign audit oversight authorities has become indispensable for establishing a global audit oversight system. In addition to the participation in the activities at the IFIAR, for the purpose of sharing information on international audit firms and audits and inspections' issues, the CPAAOB has been also constantly exchanging views with audit oversight authorities from various jurisdictions and has been striving to build and enhance its bilateral cooperative relationships with foreign audit oversight authorities, including the establishment of a framework for exchanging information on audit oversight activities (see Note), to facilitate its examination and inspection activities.

Furthermore, the CPAAOB and the FSA exchanged the letters on cooperation in the area of audit oversight with the Chinese Ministry of Finance. As a result of this exchange of letters, information concerning audit oversight will be exchanged more

smoothly between Japan and China. It will also be possible for Japanese companies operating in mainland China to issue “Panda bonds” there.

(Note) Overseas authorities which have a framework for exchanging information on audit supervisory activities with the CPAAOB and FSA

- The U.S. Public Company Accounting Oversight Board (PCAOB)
- The Canadian Public Accountability Board (CPAB)
- The Audit Oversight Board of Malaysia (AOB)
- The Netherlands Authority for the Financial Markets (AFM)
- The Commission de Surveillance du Secteur Financier (CSSF)
- The U.K. Financial Reporting Council (FRC)
- The Haut Conseil du Commissariat aux Comptes (H3C)
- The Chinese Ministry of Finance

3.3 *Next challenges*

Given that the globalization of corporate activities has led to the advance of cross-border audit services, such as the use of the audit results by overseas audit firms in the audit of consolidated financial statements of internationally active companies, ensuring audit quality globally is a challenge.

Under these circumstances, special attention also needs to be paid to the quality control method in the whole network of international audit firms, the introduction of the data analysis method in audits, and the effects that the global economic and financial situation, etc. has on the audit quality.

Regarding international trends in discussion on accounting and audit systems, the CPAAOB believes it essential to analyze the potential impact of discussions conducted at international organizations and in multiple countries on audit firm activities and the CPAAOB’s operations, etc. and to take appropriate measures, as needed, including reflecting them in the CPAAOB’s inspections of audit firms.

It is therefore essential to continue to strengthen cooperation with audit oversight authorities in each jurisdiction and reinforce bilateral cooperation networks by making an active contribution to the activities of the IFIAR, which has established a Secretariat in Tokyo. Cooperation could involve sharing views on global audit-related issues, creating opportunities for person-to-person interaction, and so on. It will also be important to develop and secure globally-minded personnel who are capable of responding to these trends.

**List of Members of
Certified Public Accountants and Auditing Oversight Board
(CPA AOB)
(As of March 31, 2018)**

| | | |
|-----------------------------|------------------|--|
| Chairperson (full-time) | Toshiro Hiromoto | Professor Emeritus Hitotsubashi University |
| Commissioner (full-time) | Takayuki Matsui | Former Professor Graduate School of Professional Accountancy , Aoyama Gakuin University |
| Commissioner (part-time) | Akiko Kimura | Of Counsel Anderson Mori & Tomotsune Outside Corporate Auditor Fuji Electric Co., Ltd. Outside Corporate Auditor Daiichi Sankyo Co., Ltd. Outside Director Nomura Asset Management Co., Ltd. |
| Commissioner (part-time) | Yoshiko Sato | Executive Managing Director Japan Investor Relations Association |
| Commissioner (part-time) | Yoshihiro Tokuga | Vice-President and Professor, Kyoto University |
| Commissioner (part-time) | Yasuyuki Fuchita | Executive Fellow Nomura Institute of Capital Markets Research |
| Commissioner (part-time) | Keiko Mizuguchi | Counselor and Chief Analyst Japan Credit Rating Agency, Ltd. |
| Commissioner (part-time) | Kazunori Yagi | Advisor Yokogawa Electric Corporation Audit & Supervisory Board Member Yokogawa Bridge Holdings Corp. Audit & Supervisory Board Member TDK Corporation Outside Director OYO Corporation Audit & Supervisory Board Member Sojitz Corporation |

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| Commissioner (part-time) | Tatsumi Yamada | Partner KPMG AZSA LLC |
| Commissioner (part-time) | Keita Yoshida | Partner Deloitte Touche Tohmatsu LLC |