

# I. Overview of the Audit Sector

## **I. Overview of the Audit Sector**

### **A. CPAs**

#### **1. Introduction of the CPA system**

A certified public accountant system was introduced in Japan in 1948. The Securities and Exchange Act was promulgated in 1947, requiring companies that issue or solicit investment in shares, corporate bonds or other securities to submit reports. The issuer is required to obtain audit attestation from certified public accountants (CPAs) by the full overhaul of the 1948 Securities and Exchange Act (now the Financial Instruments and Exchange Act (“FIEA”)) as well as the promulgation/enforcement of the Certified Public Accountants Act (“CPA Act”).

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

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

“The mission of certified public accountants, as professionals on auditing and accounting, shall be to ensure matters such as the fair business activities of companies, etc., and the protection of investors and creditors by ensuring the reliability of financial documents and any other information concerning finance from an independent standpoint, thereby contributing to the sound development of the national economy.” (Article 1)

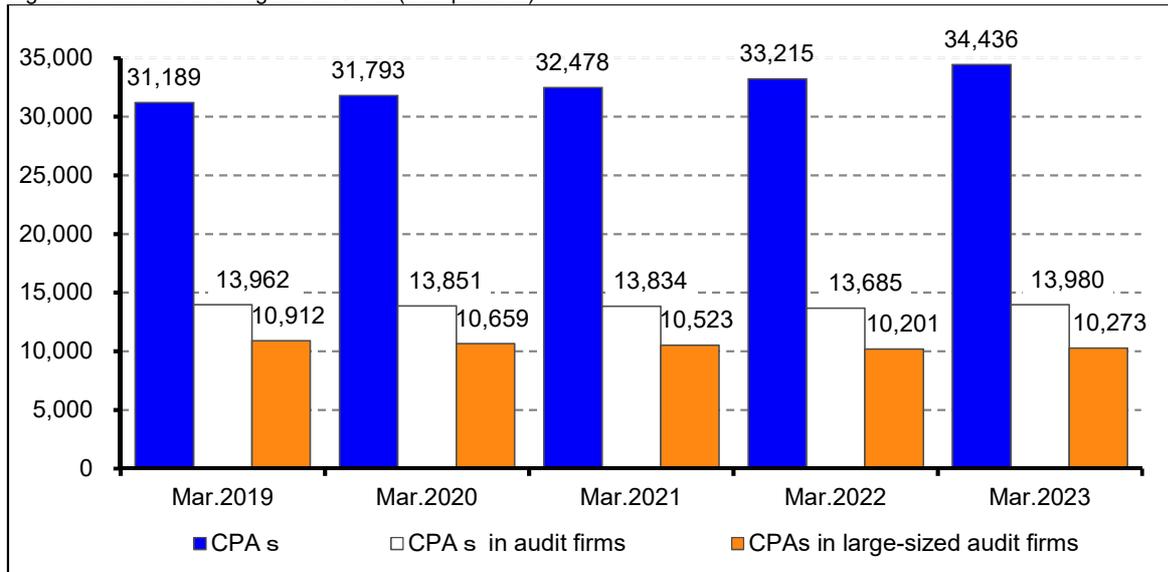
“A certified public accountant shall always maintain his/her dignity, endeavor to acquire knowledge and skills, and provide services with fairness and integrity from an independent standpoint.” (Article 1-2)

#### **2. CPAs**

The number of registered CPAs has been gradually increasing over the past few years. However, the number of the registered CPAs belonging to audit firms has stayed flat and their proportion of the overall total of registered CPAs has dropped year by year from 44.8% at the end of March 2019 to 40.6% at the end of March 2023. Of the registered CPAs belonging to audit firms, around 70% at large-sized audit firms (Figure I-1-1).

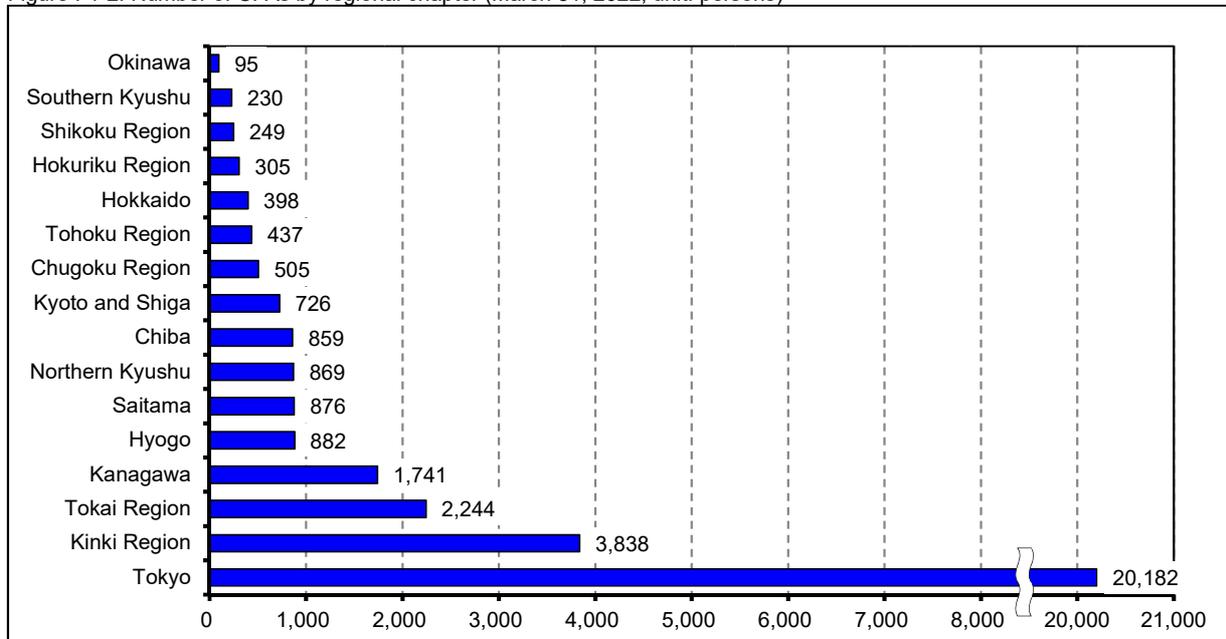
CPAs must be members of the JICPA (Article 46-2 of the CPA Act) and must belong to a regional chapter, i.e., one of the JICPA branches established across Japan (16 regional chapters as of March 31, 2023). Around 70% of CPAs are based in the Tokyo metropolitan area (Tokyo, Kanagawa, Saitama, Chiba) (Figure I-1-2).

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



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

Figure I-1-2: Number of CPAs by regional chapter (March 31, 2022; unit: persons)



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

### 3. Percentage of Female CPAs

The percentage of women among the total number of registered CPAs is gradually increasing (Figure I-1-3), and at the end of 2022 the figure reached 15.0%, which is the same as the level for female tax accountants<sup>1</sup>. On the other hand, it is still lower than the percentages of female attorneys and female CPAs in the UK and US<sup>2</sup>.

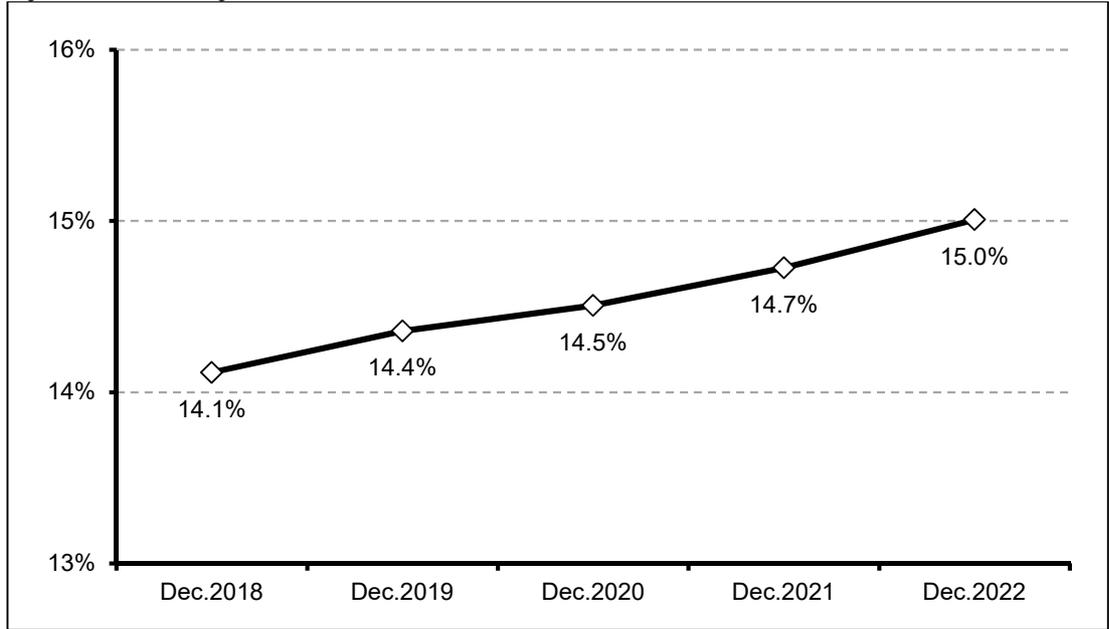
<sup>1</sup> According to “2022 Survey on Women’s Participation in Policy and Decision-making Processes” by the Cabinet Office’s Gender Equality Bureau, the percentage of female tax accountants was 15.2% at the end of March, 2022, and the percentage of female attorneys was 19.6% at the end of September, 2022.

<sup>2</sup> The percentage of female CPAs in the U.S. and the U.K. is as follows:

US: According to a survey of employment at accounting firms in 2020 conducted by the AICPA and included in its “2021 Trend Report,” the percentage of females is 46%.

UK: According to the Financial Reporting Council’s “Key Facts and Trends in the Accountancy Profession 2022,” there are several CPA institutes in the UK, and the average female membership for them is 37%.

Figure I-1-3: Percentage of female CPAs



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

■ Efforts to ensure empowerment of female CPAs ■

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

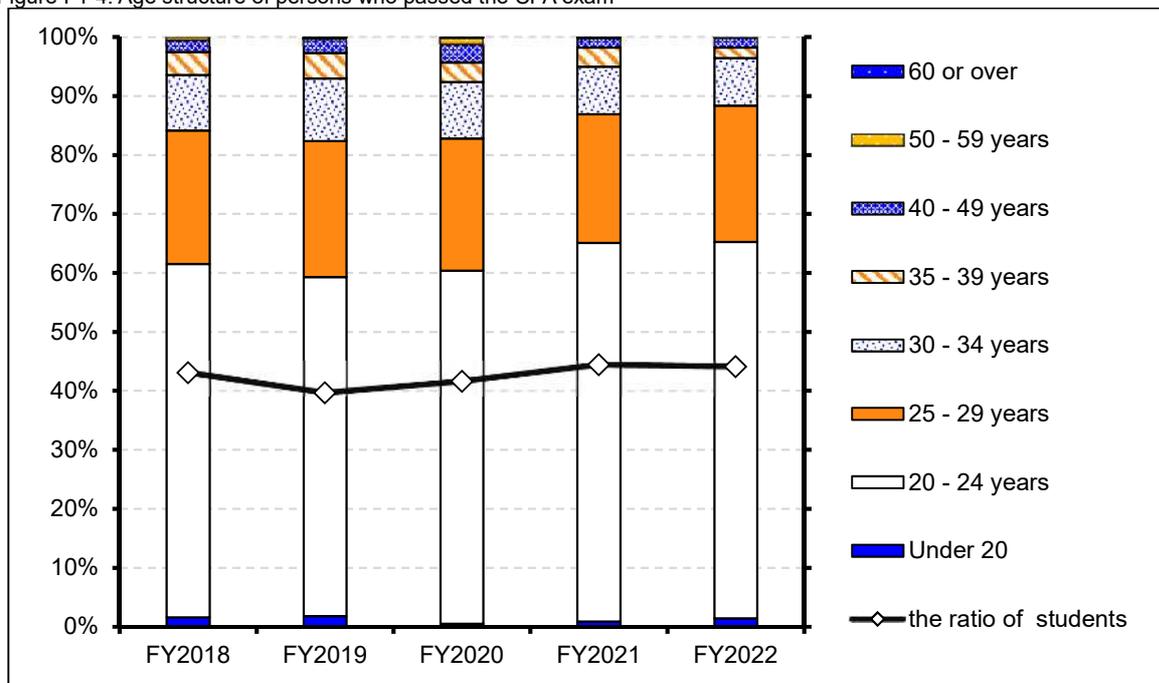
The amended CPA Act that was enacted in April 2023, lifted the restriction on services based on the marital relationship of audit firms' partners. When the spouse of an audit firm's partner serves as an officer, etc. of a company, the audit firm was conventionally prohibited from offering audit and attestation services to the relevant company. However, through the review, the restriction on services becomes applicable only when the relevant partner becomes involved in audit and attestation services. This is expected to facilitate the diversification of partners as well as to expand opportunities for female CPAs to exercise their abilities.

To encourage more females to take the CPA examination, the CPAAOB disseminates female CPAs' messages about the attractiveness and worthiness of their work and career plans through lectures at high schools and universities and the pamphlet of the CPA examination. In 2022, 22.5% of all successful examinees were women. The ratio of successful female examinees was 6.74%, while 8.1% for male examinees. Although these ratios of successful female examinees decreased in 2022 compared to the previous year, the number of successful female examinees increased. Females submitting applications for the examination and passing it has been showing an upward trend in recent years. .

#### 4. Age Structure of Persons who Passed the CPA exam

Breaking down the age structure of persons who passed the CPA examinations, we see that the largest age group is 20-24 years. People in this group accounted for 63.8% of those who passed it in 2022. As for occupation, the ratio of students (excluding persons enrolled in courses at vocational schools etc.) is the highest. Among them, the proportion enrolled in universities (including junior colleges) was 44.1% in the 2022 examinations (Figure I-1-4).

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



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

## B. Audit Firms

Audit firms, i.e., CPA firms engaged in providing audit and attestation services, numbered 2,407 at the end of March 2022, but they vary by service and business format.

Audit and attestation services cover both statutory audits and non-statutory audits. Statutory audits are CPA audits required by the law. When CPA audits were first introduced, the only statutory audits were FIEA audits, but thereafter CPA audits under the Companies Act were introduced, and then educational corporation audits under the Act on Subsidies for Private Schools. There are now a multitude of statutory audits, including audits of labor unions, credit unions, credit associations, agricultural cooperatives, social welfare corporations and medical corporations, etc. A more detailed explanation of audit and attestation services is provided on page 21 ("C. Audited Companies, 1. Types of Audit and Attestation Services").

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

The CPAAOB classifies audit firms by scale into large-sized audit firms, mid-tier audit firms, and small and medium-sized audit firms. The firms were classified as shown below based on their size and the audit services they provide (Figure I-2-1), and the CPAAOB mainly monitors those audit firms conducting FIEA audits of domestic listed companies (except for foreign companies ,the same hereafter).

Figure I-2-1: Classifications of audit firms (as of March 31, 2022)

Audit firm	Number of firms	Statutory audits			Non-statutory audits
		FIEA audits (Note 4)	Companies Act audits	Other	
Large-sized audit firms	4	○	○	○	○
Mid-tier audit firms	5	○	○	○	○
Small and medium-sized audit firms	2,398	○(Note 4)	○	○	○
(Breakdown)	Small and medium-sized audit firms	(267)			
	Partnerships (Note1)	(54)			
	Solo practitioners (Note 1)	(2,077)			

(Note 1) The number of audit offices in fiscal 2021 (book closing date from April 1, 2021, till March 31, 2022) listed in copies of audit summaries or audit implementation reports submitted to the JIPCA.

(Note 2) The symbol "○" in the table above means that audits concerned can be conducted.

(Note 3) Audit firms are required to register as Auditors of Listed Companies to audit listed domestic companies.

(Note 4) For solo practitioners to provide audit and attestation services to listed companies, they are required by law and each exchange's securities listing regulations to provide them jointly with other CPAs, etc.

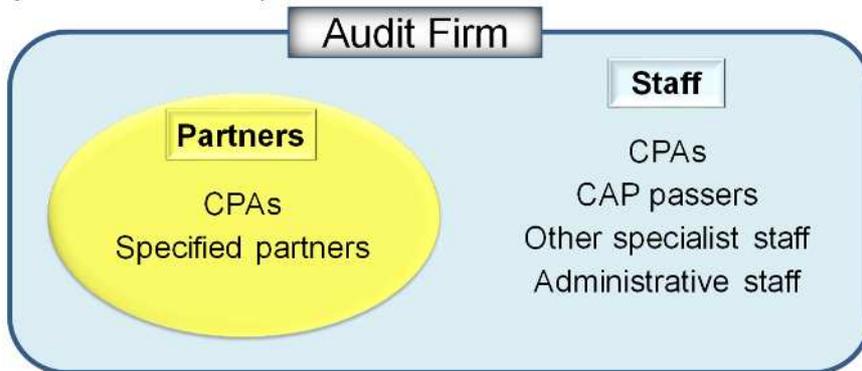
# 1. Organizational Structure of Audit Firms

Audit firms are established through investment by persons including five or more CPAs, and their defining characteristics are that the persons who invested (partners) are directly engaged in management and that they ensure organizational discipline via mutual monitoring. Some audit firms comprise only partners, but those of a certain scale ordinarily employ CPAs (CPAs who have not invested in order to become partners of the audit firm), CPA examination passers (persons who have passed the CPA exam but have not been registered as CPAs after undergoing practical training and providing assistance with audit work), and other experts as staff.

In the past, partners of audit firms were limited to CPAs, but in today's more sophisticated economy and society, partners are required to have a wide range of knowledge and experience including management, law, IT, pension mathematics to ensure appropriate operational management of the audit firm and to provide effective organizational audit services. Accordingly, as a result of legal revisions in 2007, a "specified partner system" allowed non-CPAs to be partners at an audit firm. However, CPAs must comprise at least 75% of the audit firm's partners if specified partners join the firm. In FY2022 large-sized audit firms had 141 specified partners among a total of 1,990 partners.

The personnel composition of an audit firm is outlined below (Figure I-2-2), and explained in more detail in "III. Operation of Audit Firms, A. Operations Management System, 3. Human Resources of Audit Firms." (page 62).

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



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

	Large-sized audit firm	Mid-tier audit firm	Small and medium-sized audit firm
Partners	Approx. 180 up to approx. 600	Approx. 30 up to 100	Up to approx. 40(Note2)
Full-time staff	Approx. 2,600 up to approx. 6,900	Approx. 200 up to 800	Up to approx. 90(Note2)

(Note1) See "Figure III-1-3: Characteristics of each type of audit firm" (page 55) for Characteristics of organizational structure based on audit firm size.

(Note2) Excluding an audit firm whose number of partners and full-time staff members is much higher than others.

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

As audit firms grow in scale, they necessitate introducing job classification system defined by abilities, experience, etc. for effective management of organization. (Figure I-2-3). It is standard practice for personnel to move up the ranks from staff and senior staff to manager, senior manager and, if selected, to partner. In recent years, some large-sized audit firms hire a larger number of audit assistants (staff without qualifications relating to financial statement audits, such as a qualification of CPA) to reduce the workload of CPAs and enable them to concentrate on duties requiring professional judgment. The expanding size of audit firms and the increasing complexity of their organizational administration has made the difficulty of ensuring audit quality even more apparent. In response to this situation, Principles for Effective Management of Audit Firms (the Audit Firm Governance Code) were formulated in March 2017, and are now being adopted, particularly by large-sized audit firms and mid-tier audit firms. As for the situation of amendments of Audit Firm Governance Code, refer to III. Operation of Audit Firms A. Operations Management System 2. Efforts in Response to Audit Firm Governance Code (page 56).

Figure I-2-3: Professional hierarchy in a large-sized audit firm

	Staff	Senior Staff	Manager	Senior Manager	Partner
Roles	Personnel who perform audit practice, under the guidance and supervision of superiors and seniors who may, depending on their experience, supervise engagement teams performing audits of SMEs (Small and Medium-sized Enterprises)		Personnel who oversee audit teams		Personnel who oversee all audit engagements and are involved in the management of the firm
Skills required	Specialist knowledge on audit practices, accounting and audits		Management skills in staff mentoring and coordination with audited companies, as well as problem solving skills		High level of skill as a audit supervisor
Primary training	Annual accounting audits training, Fraud prevention training, Global training, etc.				
	Audit procedure training, etc.		Management training, specialty-specific training, etc.		

(Note) For details, see "III. Operation of Audit Firms, A. Operations Management System, 4. Organizational Structure for Providing Audit Services" (page 67) and "5. Organizational Structure for Supporting Audit Services" (page 69).

## 2. Development of Quality Control Structures and Responses by Audit Firms

To ensure audit quality, it is important that audit firms develop/administer appropriate quality control structures to serve as a foundation for having their partners perform audit services properly. Furthermore, the "Standard on Quality Control for Audits" were formulated for audit and attestation services in 2005, but the services requiring development of quality control as part of firm's operation control structure are not limited to audit and attestation services but encompass all of audit firm's operations. Consequently, audit firms need to comply with professional ethics in their services other than audit and attestation services as well.

In association with the "Quality Control Standards for Audits," the International Standard on Quality Management (ISQM) 1 (ISQM1: Quality Management for Firms that Perform Audits or Reviews of

Financial Statements, or Other Assurance or Related Services Engagements), which is an international quality management standard, and other standards were newly established or revised. Accordingly, the Audit Standard Committee of the Business Accounting Council commenced deliberations in February 2021, and a written opinion on the revision of the Quality Control Standards for Audits was compiled at the general meeting of the Council in November 2021. The revised Quality Control Standards for Audits (hereinafter referred to as the "Revised Standards") require individual audit firms to introduce a quality control system based on a risk-based approach, under which they should

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

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

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

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

The Revised Standards are to be applied to audits of financial statements for a business year or an accounting period starting on or after July 1, 2023 (for audit firms other than large-sized audit firms under the Certified Public Accountants Act, for a business year or an accounting period starting on or after July 1, 2024).

Large-sized and mid-tier audit firms are moving forward with responses to the Revised Standards in parallel with responses to ISQM1 and other standards that began to be applied from December 2022. Large-sized audit firms and some mid-tier audit firms are moving forward with responses in

collaboration with global networks. They have completed the development of components of quality control systems based on quality goals and quality risks set by global networks while adding evaluation items according to the Revised Standards' own requirements, and are dry-running toward the application of the Revised Standards.

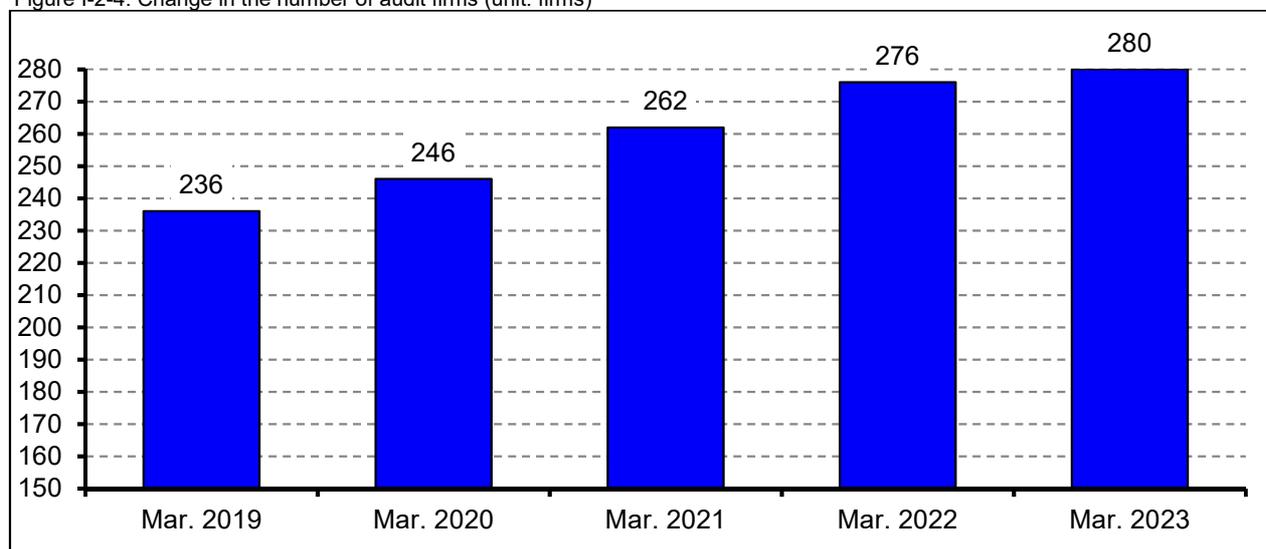
Furthermore, large-sized audit firms are considering measures to ensure that the quality control system they have developed continues to permeate the workplace even after the application of the Revised Standards and does not lose substance. These measures include implementing measures to improve the quality control system based on the root cause analysis conducted in periodic inspections, and having persons in charge of quality control conduct self-assessments of the quality control system and review the risks of the quality control system in a timely manner.

According to the collection of reports from 55 small and medium-sized audit firms in PY2022, approximately 90% of these firms have started consideration of applying the Revised Standards gathering information provided by the JICPA's training programs or publicly available information. On the other hand, approximately 10% of these firms have not started making concrete preparations.

### 3. Number of Audit firms

The number of audit firms has been on an upward trend in recent years. As of March 31, 2023, there were 280 firms, and 9 firms disappeared as a result of dissolution or merger and 13 were established in the period April 2022-March 2023, ending up with a net increase by 4 firms (Figure I-2-4) year on year. See "4. Mergers of Audit Firms" (page 18) for details on mergers from FY2018 onwards.

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



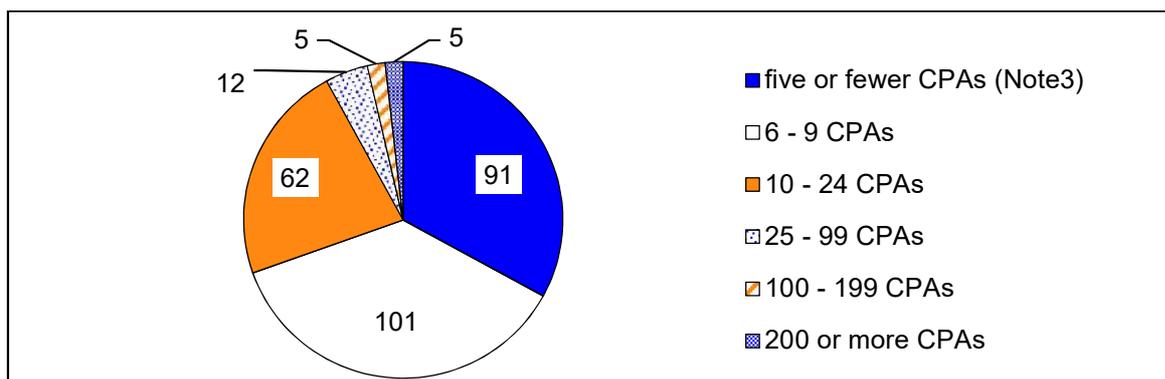
(Note 1) The number of audit firms as of the end of March 2021 is adjusted based on the data obtained after publishing the 2021 Monitoring Report.

(Note 2) The number of limited liability audit firms as of the end of March 2023 was 45.

(Source) Prepared by the CPAAOB based on data (e.g. survey of numbers of members) from the JICPA and reports of individual audit firms. The list of limited liability audit firms is published on the FSA website.

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

Figure I-2-5: Number of audit firms by scale in terms of full-time CPAs (FY2021; unit: firms)



(Note 1) The number of full-time CPAs is the total of partners who are CPAs and full-time staff who are CPAs.

(Note 2) Data on 276 audit firms was collected from operational reports submitted by these firms in FY2021

(Note 3) An audit firm where the number of partners who are CPAs drops to four or fewer should be dissolved, but six months is granted as suspended term as stipulated in the CPA Act.

#### 4. Mergers of Audit Firms

There have been 9 mergers of audit firms since FY2018 (Figure I-2-6). The main reasons for the mergers were to reinforce management infrastructure and to expand business.

Figure I-2-6: Audit firms involved in mergers from FY2017 (March 31, 2022)

FY	Surviving firm	Disappearing firm
2018	Grant Thornton Taiyo LLC	Yusei Audit & Co.
	Toho Audit Corporation	Aoyagi Accounting Office
2019	Sohken Audit Corporation (Sohken Nichiei Audit Corporation)	Nichiei Audit Corporation
2020	Ark LLC	Kinki Daiichi Audit Corporation
	Nishi-Nihon Audit Corporation (Kowa Audit Corporation)	Hibiya Audit Corporation
2021	Yasaka Kaikeisha Audit Corporation	Keihin Audit Corporation
2022	Kyoritsu Audit Corporation (Kyoritsu-Shinmei Audit Corporation)	Shinmei Audit Corporation
	Moore Shisei Audit Corporation (Moore Mirai Audit Corporation)	Kisaragi Audit Corporation
	SKIP Audit Corporation	Godai Audit Corporation

(Note) Names in parentheses show the name of the surviving firm as of March 31, 2023.

(Source) Prepared by the CPAAOB from materials made publicly available by audit firms

Reports collected from mid-tier audit firms (five firms) in PY2022 showed that four of them considered mergers as an option for their future business strategies.

The collection of reports from small and midsize audit firms (involving 42 firms) in the same program year found that roughly 35% of them were either considering mergers in specific terms or were willing to consider mergers if they find a promising merger partner.

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

Audit firms offer not only audit and attestation services but – non-audit services such as assurance services other than audit and attestation services and financial advisory services (support for initial

public offerings, introduction of IFRS, organizational realignment and so forth). Operating revenues over the five years until FY2022 (FY2021 in the case of small and medium-sized audit firms) showed an uptrend all at large-sized, mid-tier and small and medium-sized audit firms.

Revenues from audit and attestation services roughly accounted for 70% of operating revenues at large-sized audit firms, while the ratio was about 95% and 90% respectively at mid-tier and small and medium-sized audit firms (Figure I-2-7). For audit firm groups' operating revenues, see "III. Operation of Audit Firms, A. Operations Management System, 9. Domestic Audit Firm Groups" (page 85).

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

a. Large-sized audit firms

The ratio of audit service and attestation revenues, which has been around 75% for large-sized audit firms as a whole. Seeing the ratio of each large-sized audit firm, the ratio has ranged between 60% and 85% at three of the four firms, but at the remaining firm it has hovered at around 50%. The ratio of audit service and attestation revenues for large-sized audit firms combined slightly decreased compared to the previous fiscal year due to the increase in revenues of non-audit services such as financial advisory service.

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

b. Mid-tier audit firms

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

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

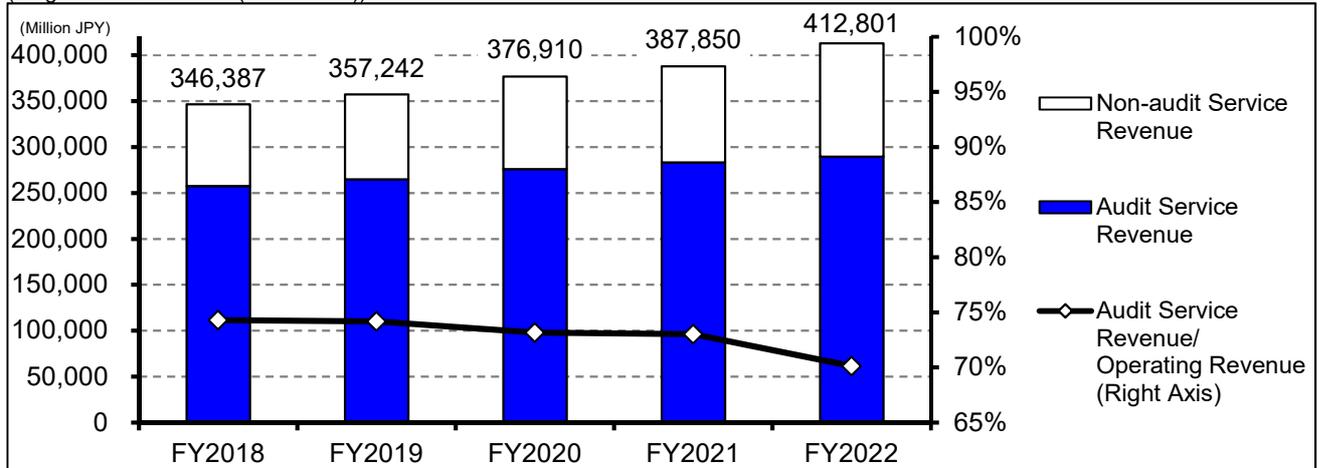
There was a wide variation in revenues between mid-tier audit firms, and the gap may change depending on future developments, such as mergers.

c. Small and medium-sized audit firms

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

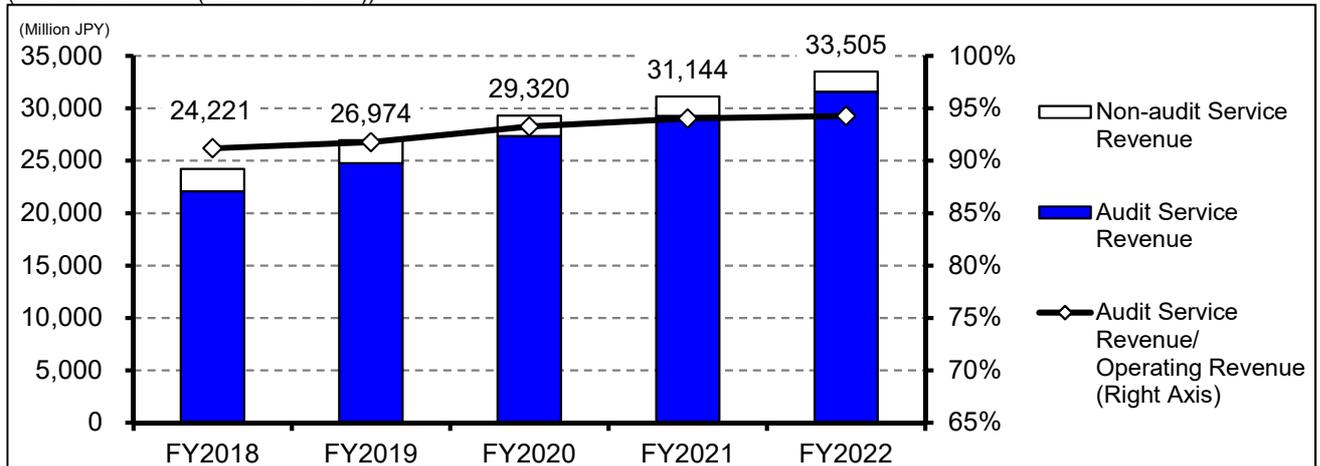
The operating revenues of small and medium-sized audit firms are moderate on the whole, but some of the largest firms in this category are expanding their business through newly concluding audit engagements with companies for which mainly large-sized audit firms had cancelled audit engagements. For changes in accounting auditors, see "III. Operation of Audit Firms, E. Acceptance of New Audit Engagements and Changes of Accounting Auditors" (page 97).

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



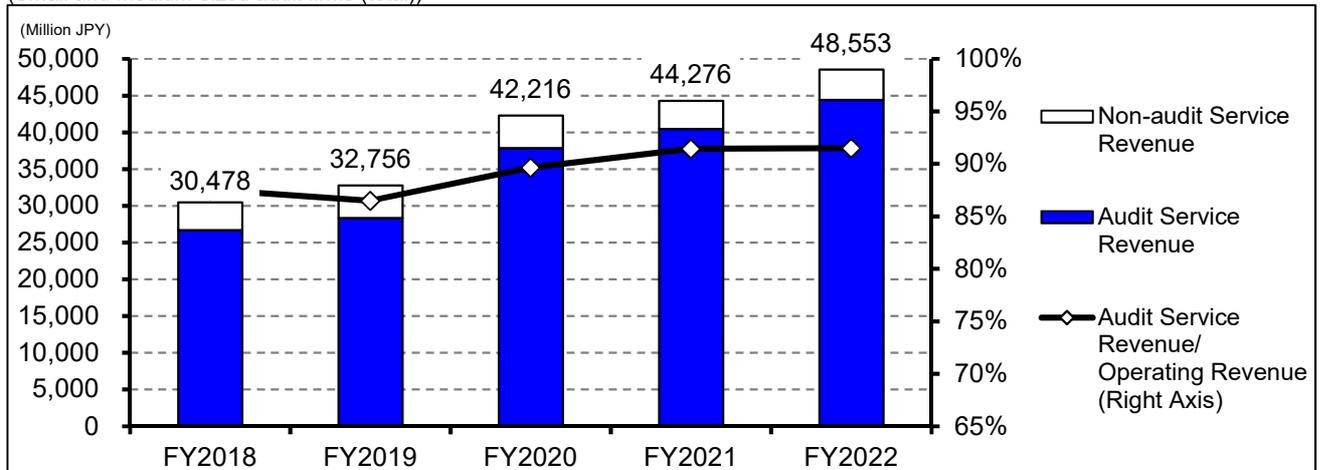
(Note) In FY2017, one audit firm changed its fiscal year-end, so calculations are based on eight-month figures. As a result, FY2017 operating revenues are calculated by extrapolating eight-month operating revenues to one-year periods (by multiplying figures by 12 months/8 months) for the audit firm that changed its fiscal year-end.

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



(Note) In FY2016 one firm changed its fiscal year-end, closed its books after a 15-month fiscal year, and did not submit its report within the program year. As a result, when aggregating the figures, operating revenues of this firm for FY2017 represent 15 months' worth of operating revenues.

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



(Note 1) As fiscal year-end varies widely among small and medium-size audit firms, their results in FY2022 have yet to be tallied. This report therefore covers their results through FY2021 (from April 2021 through March 2022). The number of small and medium-sized audit firms differs each fiscal year. For FY2021, the results of 253 firms were tallied.

(Note 2) Audit and attestation service revenues greatly increased as a whole because of a steep rise at a firm.

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

### C. Audited Companies

Audit and attestation services differ by content and status due to statutory audits mandated by different regulations and audited companies' business scale, etc.

#### 1. Types of Audit and Attestation Services

As previously noted (see "B. Audit Firms" (page 13)), audit and attestation services include statutory audits, which are based on such laws as the FIEA, the Companies Act, the Act on Subsidies for Private Schools, and the Labor Union Act and non-statutory audits whose objectives and content are decided by the parties involved. The types of audit and attestation services provided by audit firms are shown below (Figure I-3-1).

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

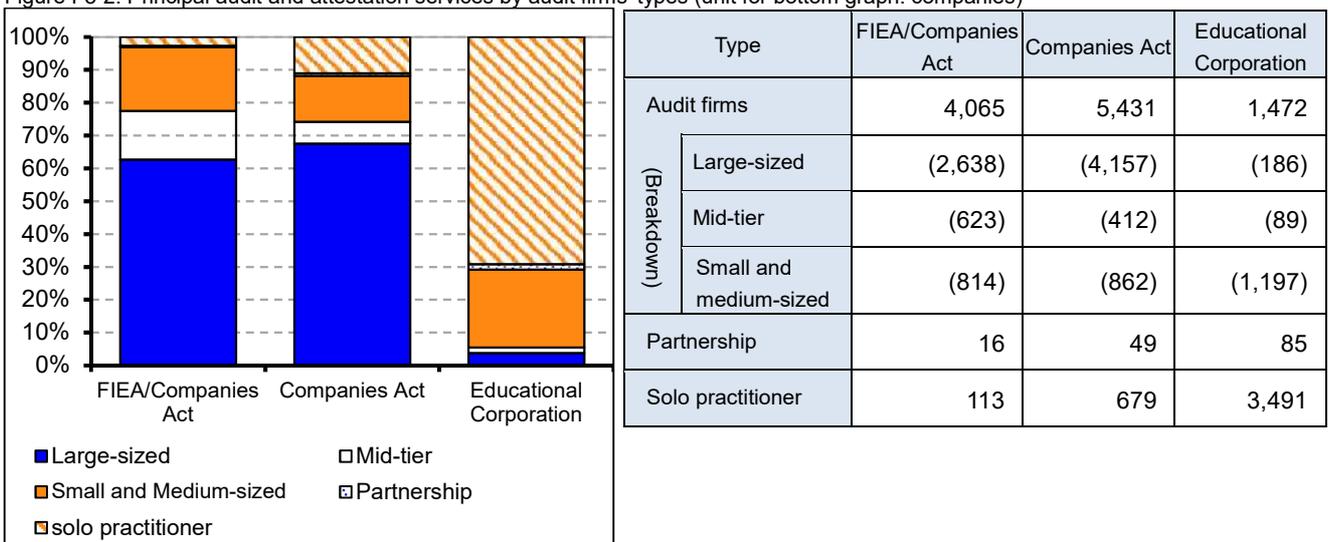
Type	Statutory audits						Non-statutory audits	Total
	FIEA / Companies Act	FIEA	Companies Act	Act on Subsidies for Private Schools	Labor Union Act	Other		
Number of companies	4,091	300	5,430	1,561	414	3,856	5,521	21,713
Percentage	19.3	1.4	25.7	7.4	2.0	18.2	26.0	100.0

(Note 1) The number of audited companies has been aggregated from operational reports submitted by audit firms in FY2021

(Note 2) "FIEA/Companies Act" denotes operations where audit and attestation under both the FIEA and Companies Act are required, while "FIEA" and "Companies Act" denote operations where audit and attestation under the respective act only is required.

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

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



(Note 1) Data was aggregated from audits conducted from the term ended April 2021 to the term ended March 2022. The figures do not match with the figures in Figure I-3-1 because the collection period is different.

(Note 2) The figures in the column "FIEA/Companies Act" include services requiring audit and attestation only under the FIEA, in addition to services requiring audit and attestation under the FIEA and the Companies Act.

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

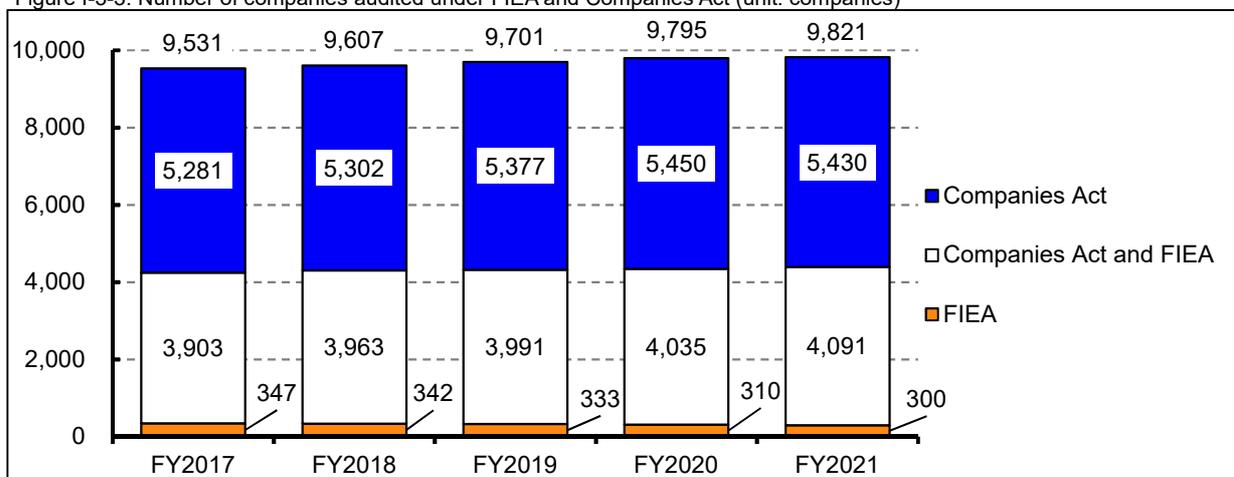
## 2. FIEA and Companies Act Audits

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

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

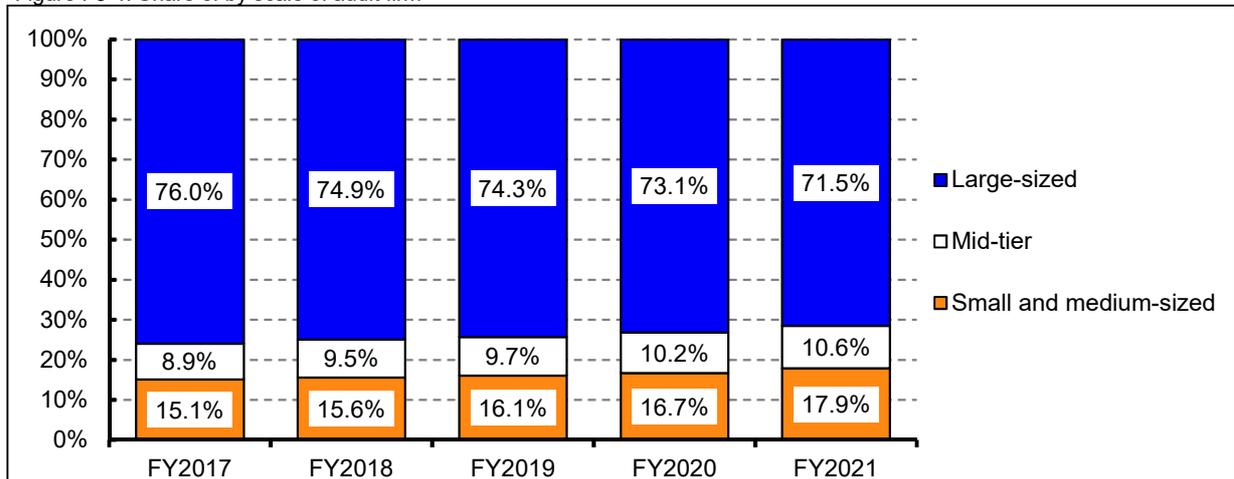
There has been no significant change in the number of companies audited under the FIEA or the Companies Act (Figure I-3-3). With regard to share by scale of audit firm, large-sized audit firms' share has been going down, mid-tier and small and medium-sized audit firms' share have been going up annually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

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



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

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



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

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

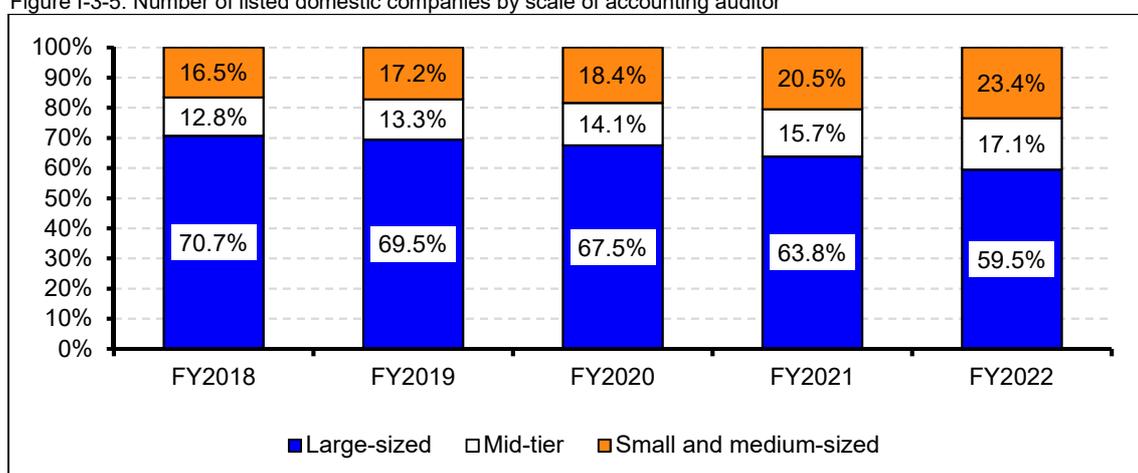
Audits at about 60% of listed domestic companies are conducted by large-sized audit firms, but in terms of market capitalization, large-sized audit firms have about 90% share and this trend has been persisting for many years. This is because listed domestic companies with large market capitalizations conduct operations on a large scale, and their operations are complex as well as

international by nature. As a result, their audits require a large number of audit personnel and various specialist capabilities, which likely makes it difficult for firms other than large-sized audit firms to handle their audits (Figures I-3-5 and I-3-6).

At the end of FY2022, there were 3,897 domestic listed companies, and 2,317 of them were audited by large-sized audit firms, 668 of them were audited by mid-tier audit firms, and 912 were audited by small and medium-sized audit firms. Meanwhile, the market capitalization of domestic listed companies was 751,091.6 billion yen, of which large-sized audit firms handled 676,685.2 billion yen, mid-tier audit firms handled 44,113.1 billion yen, and small and medium-sized audit firms handled 30,293.3 billion yen.

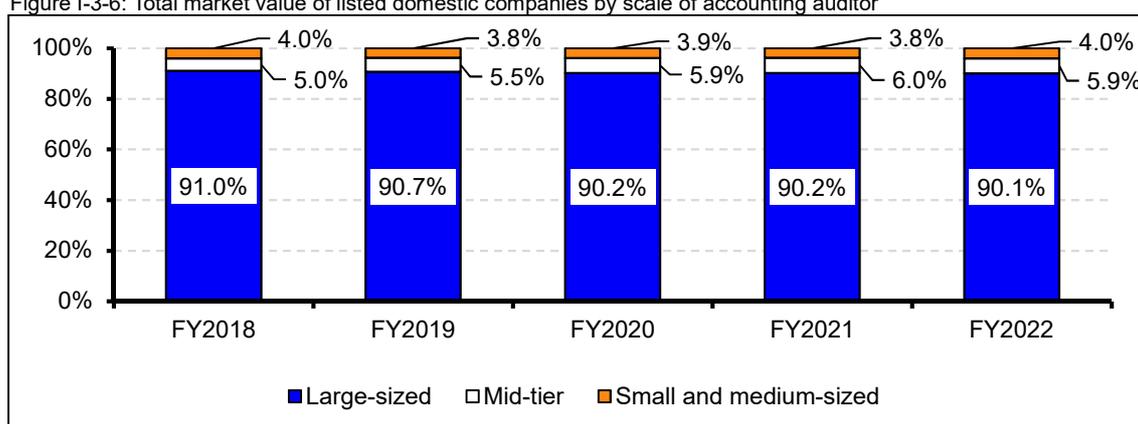
Among the top 20 companies in terms of market capitalization at the end of FY2022 (accounting for about 27% of total market capitalization), 18 companies were audited by large-sized audit firms.

Figure I-3-5: Number of listed domestic companies by scale of accounting auditor



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

Figure I-3-6: Total market value of listed domestic companies by scale of accounting auditor

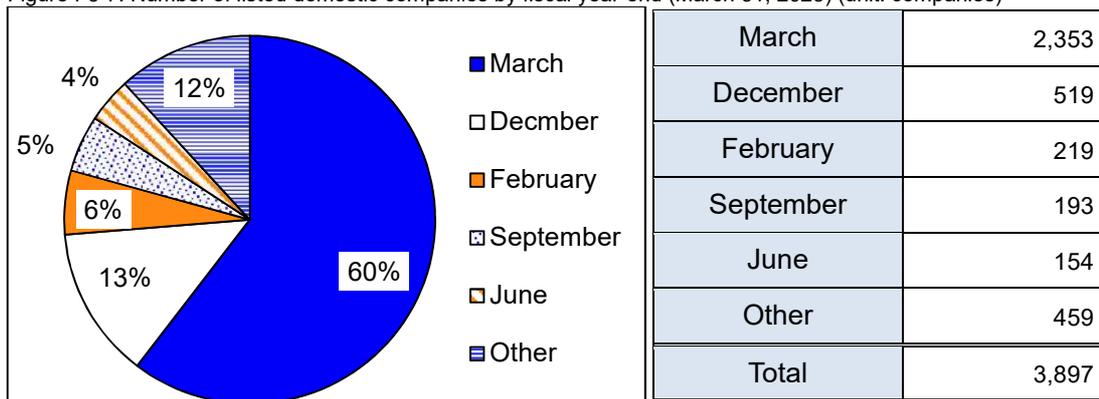


(Source) Prepared by the CPAAOB based on data from Quick and exchanges

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

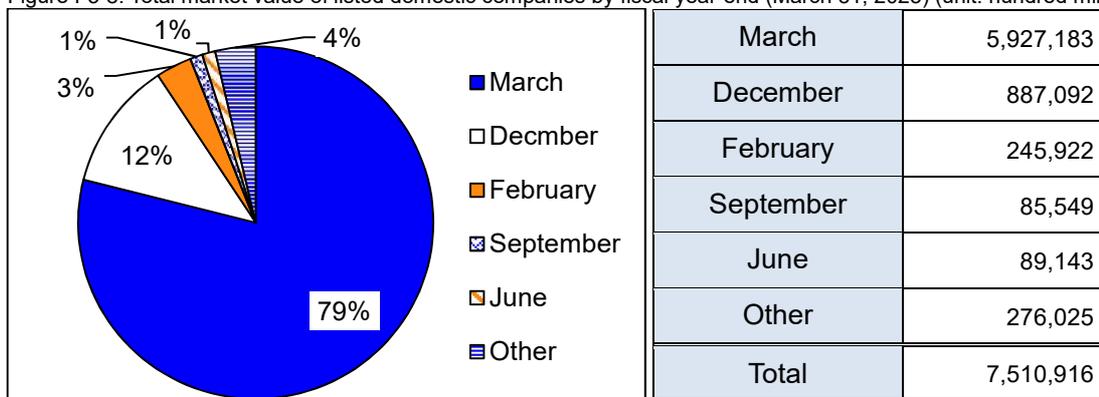
60% of listed domestic companies close their books at the end of March, and that they account for 79% of the total market capitalization. This fact explains why audit operations are heavily concentrated in specific periods (Figures I-3-7 and I-3-8).

Figure I-3-7: Number of listed domestic companies by fiscal year-end (March 31, 2023) (unit: companies)



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

Figure I-3-8: Total market value of listed domestic companies by fiscal year-end (March 31, 2023) (unit: hundred million JPY)



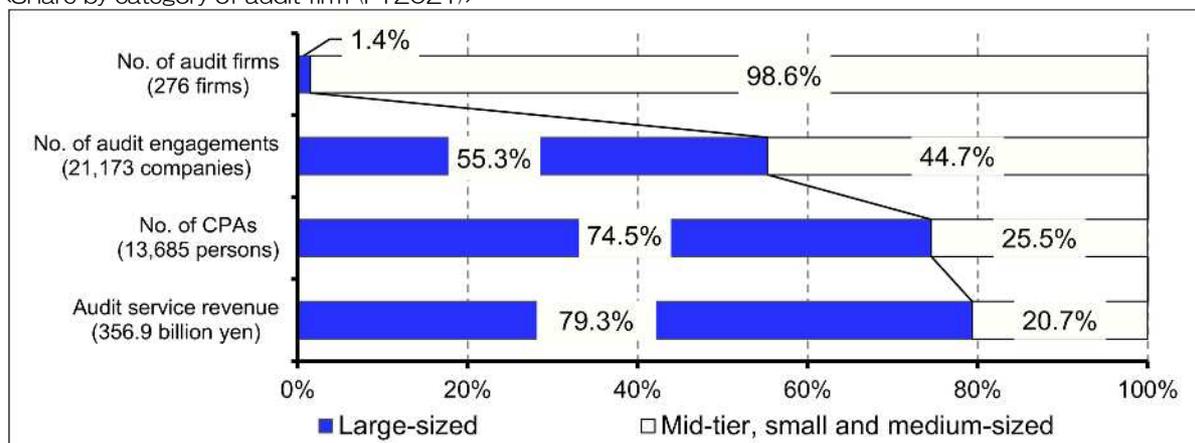
(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

**■ Concentration at Large-sized Audit Firms ■**

Among the 276 audit firms as of the end of FY2021, large-sized audit firms accounted for a large portion of the number of audit and attestation engagements, the number of CPAs and audit and attestation service revenues.

The share of large-sized audit firms in the number of audit and attestation engagements, audit service revenues and other categories has been on the decline in recent years as a result of operations management related to the continuation of their audit service contracts. See “III. Operation of Audit Firms, E. Acceptance of New Audit Engagements and Changes of Accounting Auditors” (page 97).

<Share by category of audit firm (FY2021)>

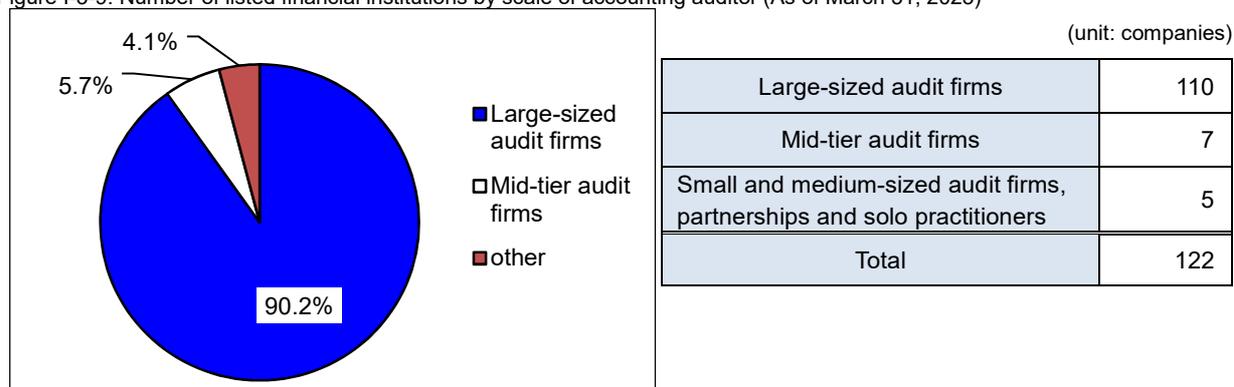


(Note 1) Compiled based on FY2021 JICPA member data and operational reports submitted by audit firms

### 3. Audits of Financial Institutions

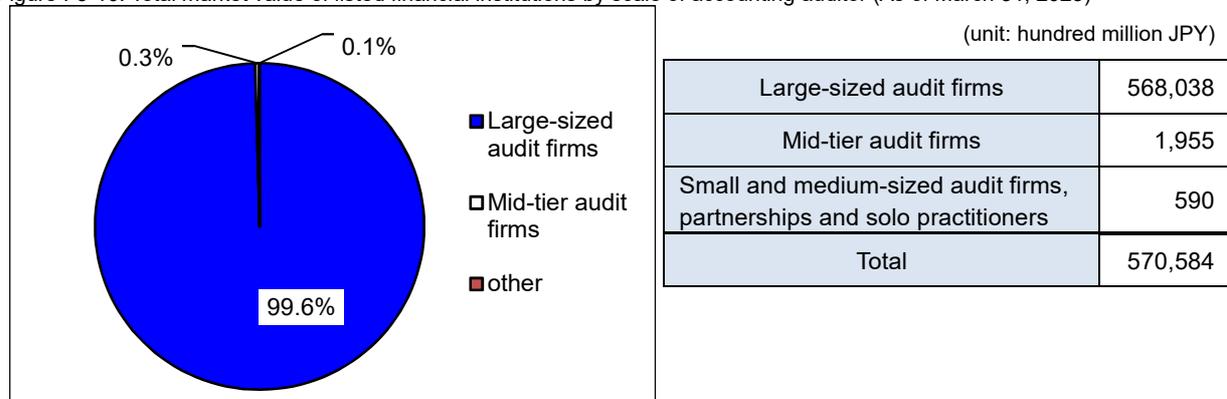
90% of listed financial institutions (122 companies) were audited by large-sized audit firms, and in terms of market capitalization, large-sized audit firms handled 99%. So compared with all domestic listed companies, large-sized audit firms' share presented a further increase (Figures I-3-9 and I-3-10). For information about domestic listed firms as a whole, see 2. FIEA and Companies Act Audits (page 22). Large-sized audit firms are pursuing initiatives to enable them to cope with accounting and audit practices that are designed to the listed financial institutions. These include establishing organizational and audit structures specifically for the financial sector and providing education/training to audit practitioners.

Figure I-3-9: Number of listed financial institutions by scale of accounting auditor (As of March 31, 2023)



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

Figure I-3-10: Total market value of listed financial institutions by scale of accounting auditor (As of March 31, 2023)



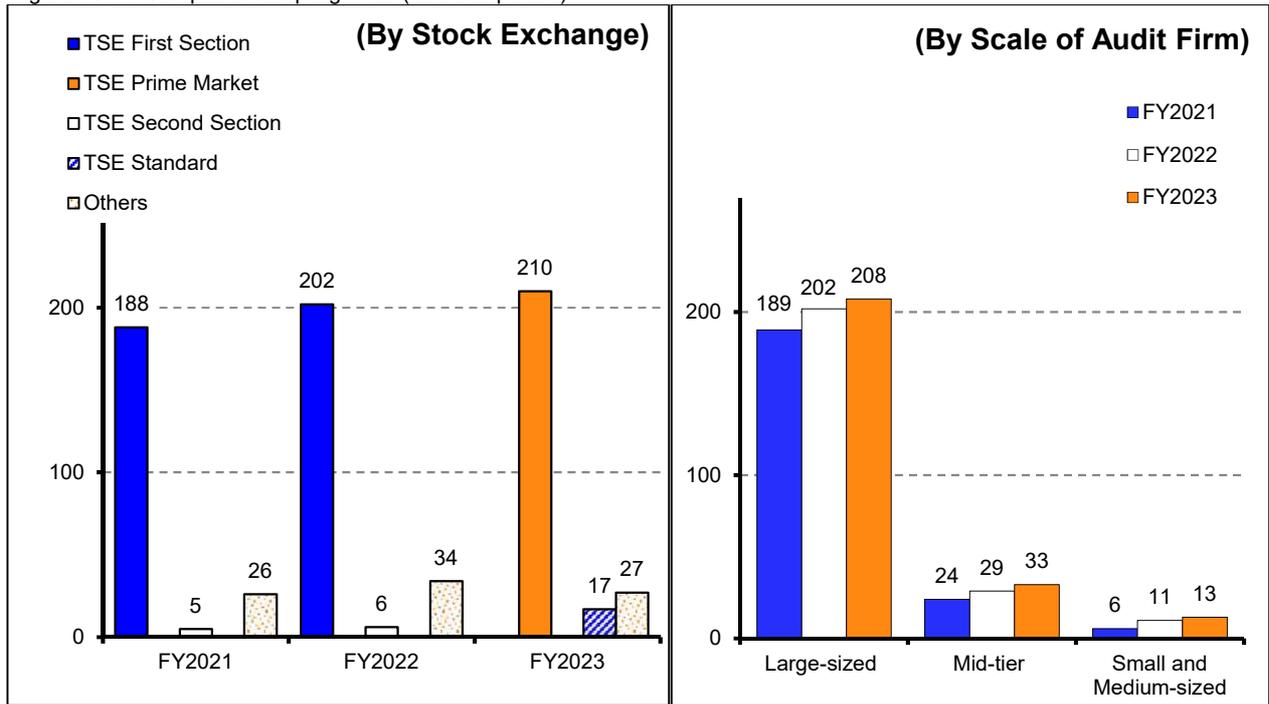
(Source) Prepared by the CPAAOB based on data from QUICK and exchanges

### 4. Companies Adopting IFRS

The following figures show the listing markets for companies that have adopted IFRS and the scale of the accounting auditors for these companies as of the end of March 2023 (Figures I-3-11).

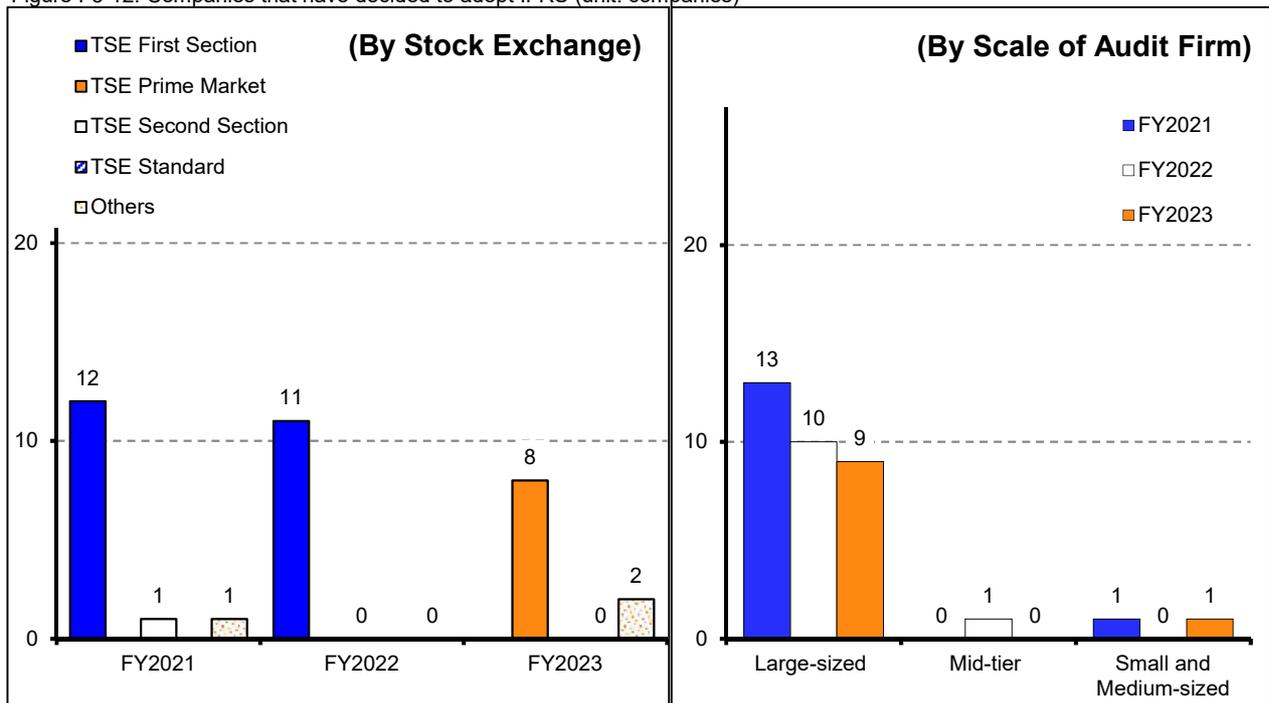
The majority of companies that have adopted IFRS are listed on the Prime Section of the Tokyo Stock Exchange, and many of them operate internationally. Audit contracts are concentrated in large-sized audit firms which collaborate with large global networks. A similar situation is seen with companies that have decided to adopt IFRS (companies in which the business execution organ has decided to adopt IFRS and has publicly disclosed this) (Figure I-3-12).

Figure I-3-11: Companies adopting IFRS (unit: companies)



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

Figure I-3-12: Companies that have decided to adopt IFRS (unit: companies)



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

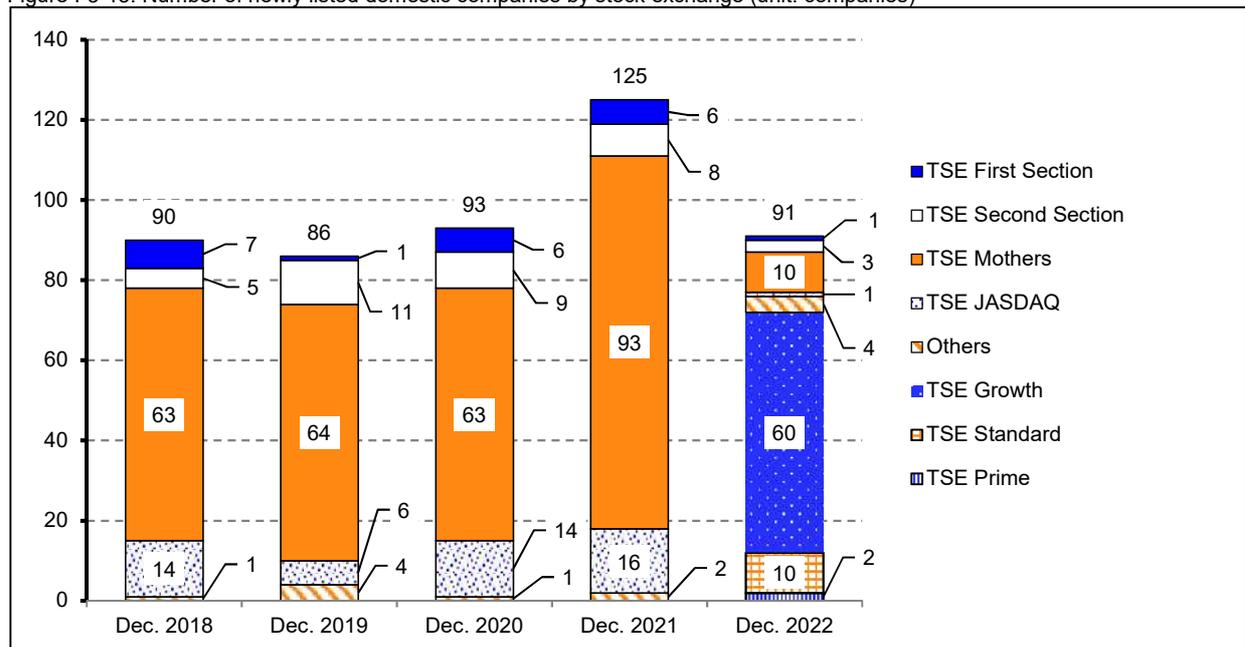
## 5. Audits of Initial Public Offerings

The number of IPOs (excluding listings on the Tokyo Pro Market) for the period from January 2022 to December 2022 (hereinafter referred to as the "year through December 2022") came to 91. Although the number has decreased from the previous year when 125 IPOs occurred due to the favorable domestic stock price, it remains at the same level in recent years. Listings on the Tokyo Stock Exchange's Mothers and Growth market were particularly large in number (Figure I-3-13).

Seeing shares by size of audit firms, large-sized audit firms maintain a large share (Figure I-3-14). However, the shares held by each of the large-sized audit firms have changed, which likely reflects changes in the business operation policies and IPO operations embedded in each firm. For information about the policies, organizational structures, etc. of audit firms regarding the acceptance of IPO audit engagements, see III. Operation of Audit Firms, A. Operations Management System, 4. Organizational Structure for Providing Audit Services (page 67).

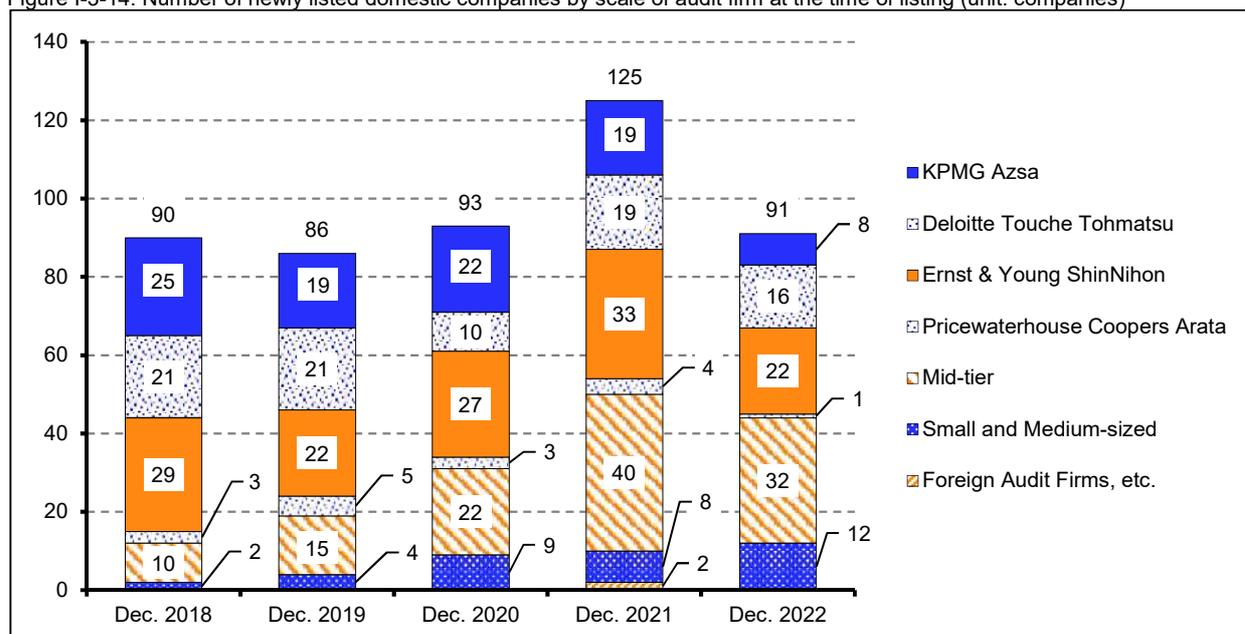
The share of large-sized audit firms was 52% in the year through December 2022. While the share of med-tier and small and medium-sized audit firms showed an uptrend.

Figure I-3-13: Number of newly listed domestic companies by stock exchange (unit: companies)



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

Figure I-3-14: Number of newly listed domestic companies by scale of audit firm at the time of listing (unit: companies)

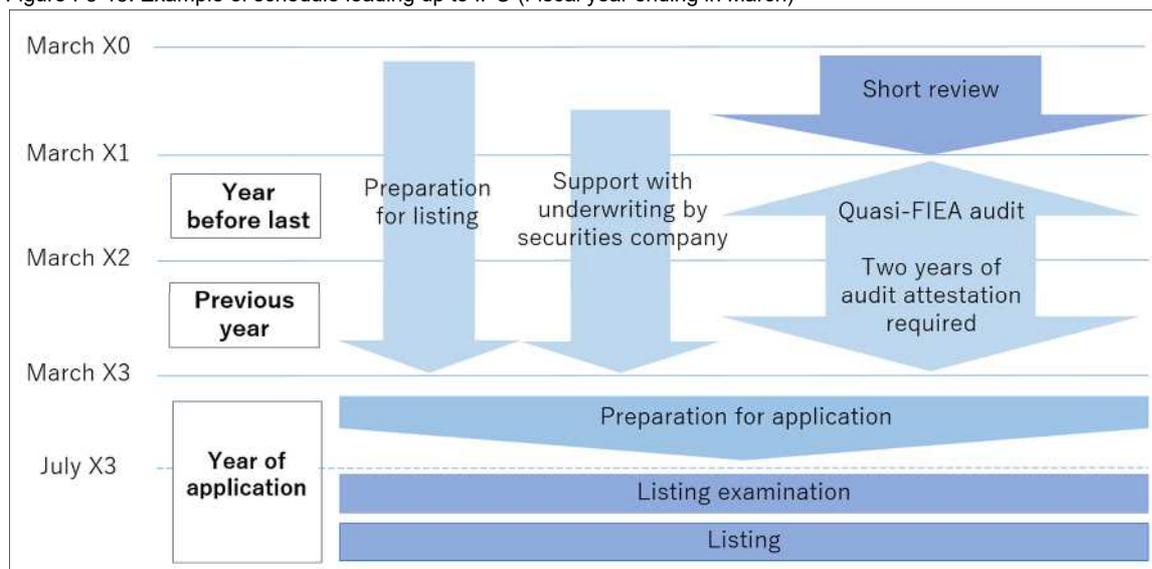


(Source) Prepared by the CPAAOB based on data from exchanges

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

However, IPO audits often entail a relatively high audit risk, such as vulnerable internal control structure of the audited company, and there were cases where improper accounting had already been practiced by the time of IPO. Accordingly, before accepting IPO audit engagements, many audit firms follow their policies requiring more rigorous risk assessments than normal audit engagements.

Figure I-3-15: Example of schedule leading up to IPO (Fiscal year ending in March)



(Source) Prepared by the CPAAOB

### ■ IPO support services ■

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

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