Attachment 1
(Provisional translation)

Eleven Misunderstandings about the Internal Control Report System

1. Is the Internal Control Report System identical to the one originally introduced by the Sarbanes-Oxley (SOX) Act in the United States?

Misunderstanding	The Japanese system is identical to the one that was originally introduced by the Sarbanes-Oxley (SOX) Act in the United States.
⇧	
Truth	The Japanese internal control report system was designed, taking account of criticism against the one originally introduced by the SOX Act in the United States.

(Examples)

○ Top-down/Risk-based approach
A management should design and assess internal controls to the extent necessary so as to mitigate the risks that would result in material misstatements of financial reporting (elaborated in narrowing down the scope of assessment).

○ Simplified classification for deficiencies of internal controls
Deficiencies in internal controls are classified into two categories consist of "material weaknesses" and other "deficiencies." In the United States, control deficiencies are classified into three categories.

* Further measures were taken to minimize burdens (Please see following pages).

2. Is additional documentation always necessary?

Misunderstanding	Additional documentation, such as the preparation of flow charts, is necessary solely for the purpose of the internal control report system.
⇧	
Truth	Relevant records that has already been prepared and used may be utilized.

(Examples)

○ Recording of internal controls
Preparation of flow charts and narrative documents explaining the operation are not necessarily required. Relevant records that companies prepare and use may be utilized, as supplemented as necessary.

○ Retention of records
All records are not necessarily required to be documented in a paper form, but may be recorded in an appropriate scope and format (e.g. digital media).

3. Do all business operations require internal controls?

Misunderstanding	A management is required to design and assess internal controls, regardless of the size of business operations (processes).
⇧	
Truth	The company-level internal control is the most important. Accordingly, based on the assessment of company-level internal controls, managements may narrow down the scope for assessment of business operations (processes), considering the risks of material misstatements in financial reporting.

(Examples)

○ Narrowing down the scope of business operations to be assessed

A management may narrow down the scope of business operations for assessment to three major accounts (sales, account receivables, inventories) at the business locations that generate up to two-thirds of revenues, as supplemented necessary.

○ Excluding insignificant business operations

A management may exclude insignificant business operations among those to be assessed.

(It is decided on a case-by-case basis; for example, business operations that make up less than 5% of the total from materiality.)

4. Do even small and medium-sized companies need internal controls as required for large companies?

Misunderstanding	Although small and medium-sized companies in the United States are given specific consideration, the same level of internal control system as adopted by large-sized companies is required in Japan.
Truth	Internal control report system is mandatory for listed companies only. Small and medium-sized listed companies are allowed to design a simplified system taking account of their respective situations, such as business size and characteristics.

(Examples)

- ○ Alternative controls in place for segregation of duties
  When human resource is not sufficient, appropriate monitoring by management or persons in other divisions may be sufficient.

- ○ Use of experts from outside the company
  The work of experts outside the company may be utilized a part of the monitoring.

5. Is a company subject to punishments, if any deficiencies are found?

Misunderstanding	If any deficiencies are reported as part of internal control assessment, a company is subject to punishments such as delisting from securities exchanges.
⇧	
Truth	The mere existence of deficiencies (material weaknesses) in internal controls may not constitute the cause of delisting from securities exchanges or other punishment due to violations of the Financial Instruments and Exchange Act.

(Examples)

○ "Material weakness" per se is not be a cause for delisting from securities exchanges (Please refer to "Comprehensive Improvement Program for Listing System 2007"published by Tokyo Stock Exchange, Inc.).

○ The mere existence of "material weakness" in internal controls neither constitutes a cause for violation of the Financial Instruments and Exchange Act nor a cause for punishment under the Act. (If internal control report is materially misstated, it constitutes a cause for punishment. [Financial Instruments and Exchange Act, Article 197- 2])

6. Does a management always need to comply with suggestions from its auditors or consultants?

Misunderstanding	A management always needs to comply with suggestions from its auditors or consultants in designing and assessing internal controls.
⇧	
Truth	A management, who is most familiar with risks of the company, should determine internal controls.

(Examples)

○ The extent of suggestions from an auditor
An auditor’s suggestions need to be made to the extent appropriate with a condition that a company or management actively conducts or judges the work associated with establishment of an internal control system.

○ A manual or system developed by an auditor or a consultant
A management does not need to use a manual (e.g. internal control tools) or a system developed by an audit firm or a consultant.

7. Will auditing costs be doubled?

Misunderstanding	Auditing costs will be doubled, since audits of internal controls will be conducted in addition to those of financial statements.
⇧	
Truth	An auditor of financial statements is responsible for audit of internal controls in an integrated manner so as to enhance efficiency and effectiveness.

(Examples)

○ Integrated audit planning
An auditor draws up plans for audits of financial statements as well as those of internal controls in an integrated manner.

○ Use of audit evidences
Audit evidences obtained through internal control audits and those obtained through audits of financial statements may be utilized in respective audits.

8. Is an unlisted company also required to design internal controls, when entering into transactions with listed companies?

Misunderstanding: Even an unlisted company is required to design and assess internal controls when it has entered into transactions with a listed company.

⇧

Truth: An unlisted company is not required to design and assess internal controls, solely because it has entered into transactions with a listed company.

(Examples)

- ○ A trade counterpart (excluding the service organization)
  A trade counterpart of an unlisted company such as a supplier or a customer of a listed company is not required to design and assess internal controls (previous practices, including preparation of invoice and bill is sufficient as before).

- ○ A service organization of listed companies
  A service organization is not subject to assessment, if it is not engaged in significant business operations (processes).

9. Is the absence of a project team a problem?

Misunderstanding

If a company does not designate a project team or a person in charge of the internal control report system, it constitutes a deficiency (material weakness).

Truth

A company may utilize an existing division for the internal control report system. A project team or a person with full-time involvements is not necessarily required.

(Examples)

- ○ Utilization of an existing division
  A company may utilize an existing division such as its Accounting Department or Internal Audit Department.

- ○ Use of experts from outside the company
  A company may employ experts outside the company as a part of the assessment of internal controls.

10. Does a company need to finish the whole preparation by the effective date?

Misunderstanding	A company cannot meet the deadline, since the internal control report system comes into effect from April 2008.
⇧	
Truth	Since an internal control is a process, what is important is to remedy deficiencies each time once they are identified.

(Examples)

○ The deadline for submitting a report
Even a company with its fiscal year ending March may submit an internal control report as of the end of March 2009, by the end of June 2009.

○ Response to deficiencies (material weaknesses)
Internal controls are effective if deficiencies are remedied by the end of the fiscal year.
Even if deficiencies are not remedied, a company may describe a measure taken for remediation or a planned step for remediation after the year-end in the report.

11. Does a company need to postpone modifications to an IT system scheduled around the end of a fiscal year?

Misunderstanding	For conducting the assessment of internal controls, a company needs to postpone the modifications of an IT system or re-organization of group structures such as a merger that are scheduled around the end of the fiscal year.
⇧	
Truth	Internal controls may be effective even when a company executes the modification of an IT system or re-organization as scheduled.

(Examples)

○ Even if a management may not be able to perform sufficient assessment procedures to a part of process within a specified period, it is possible that a management may scope out the process and assess whole internal controls, certifying that it is due to “unavoidable circumstances.”

○ In this case, an auditor may express an “unqualified opinion.”