



The Japanese Institute of Certified Public Accountants

**Overview of the Quality Control Review 2017**

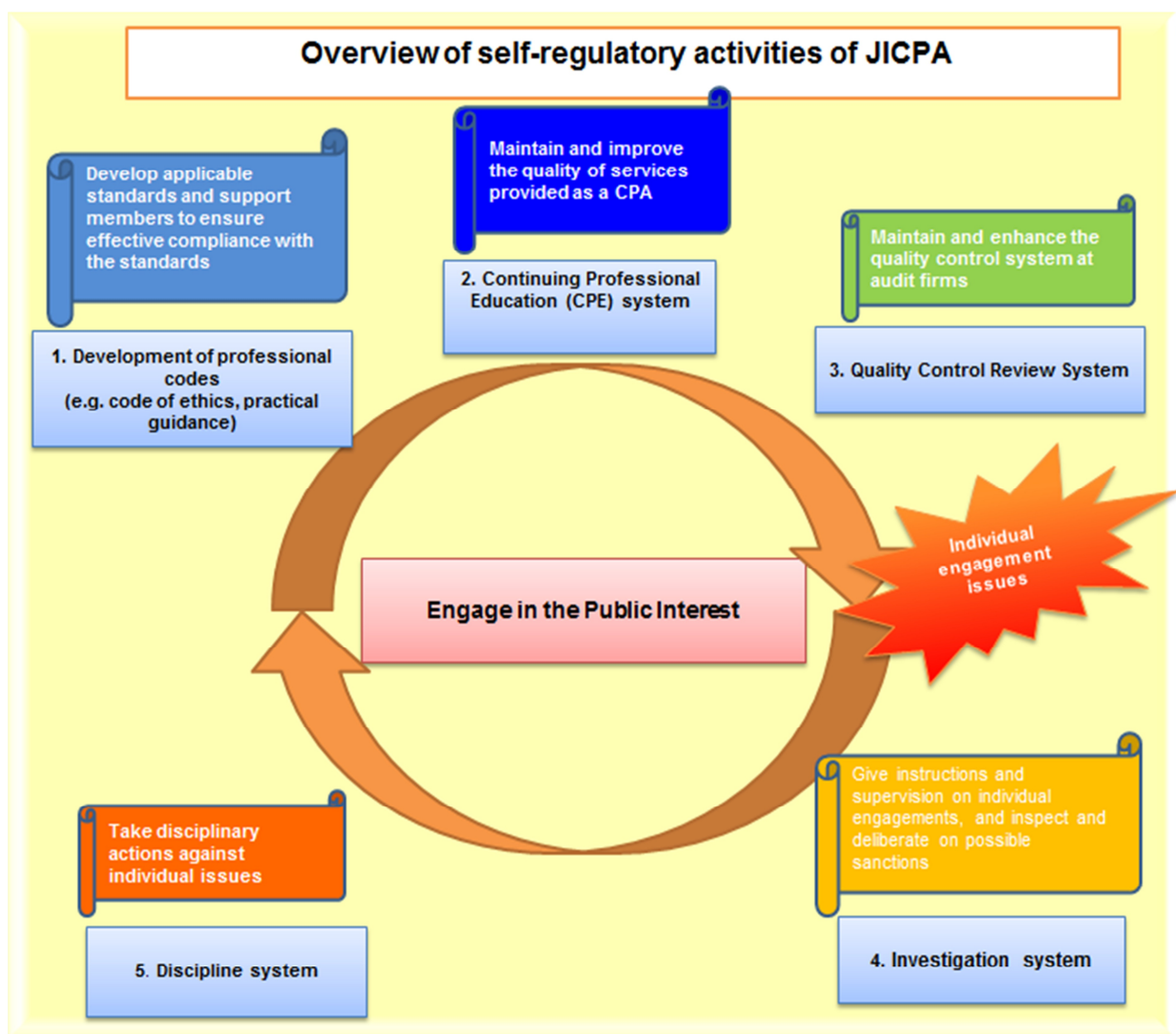
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## Role of JICPA as a self-regulatory organization

### ***JICPA's self-regulatory activities and Quality Control Review System***

The Japanese Institute of Certified Public Accountants (or “JICPA”) is a self-regulatory organization, aiming to maintain high quality of services provided by members in a consistent manner by instructing, supervising and communicating with its members. The following diagram summarizes the self-regulatory activities conducted by JICPA in order to maintain and improve the quality of auditing, accounting and other related fields of professional services and enhance social confidence in those services. Among others, the “Quality Control Review System” is considered as one of the most significant self-regulatory activities of JICPA.



# Quality Control Review System

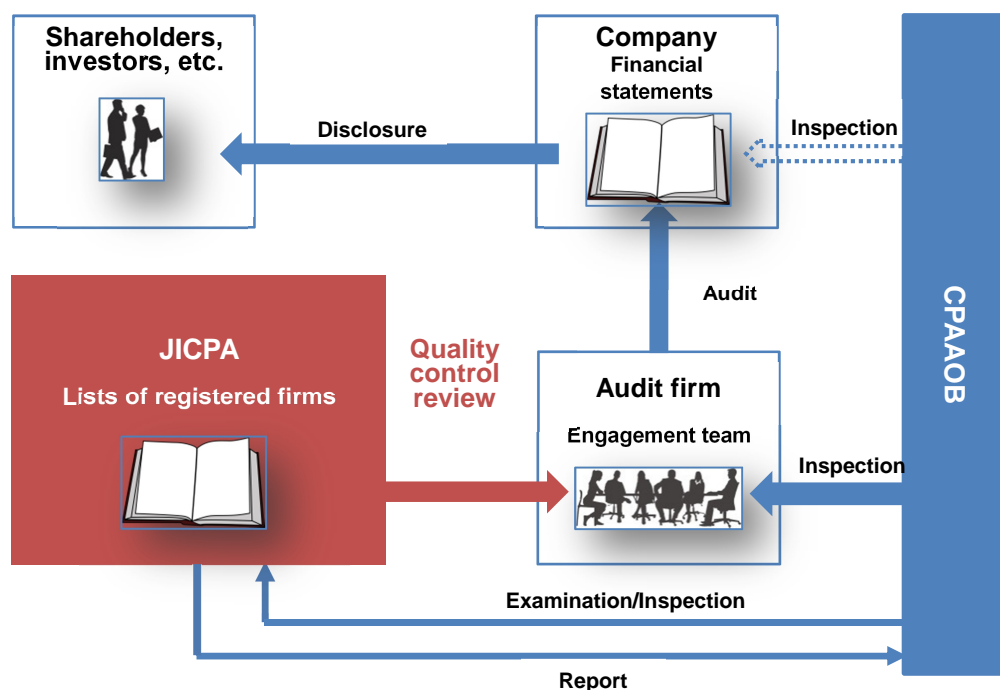
## Overview of the Quality Control Review System

Given the nature of public interest in audit engagements, JICPA has implemented a system for quality control reviews (the “Quality Control Review System”) for audit engagements conducted by audit firms and CPAs (collectively as “audit firms”), which is a self-regulatory activity of JICPA under the Certified Public Accountants Act (the “CPA Act”), for the purpose of maintaining and improving an appropriate quality level of audit engagements and ensuring social confidence in auditing.

Furthermore, JICPA has introduced the “Registration System for Listed Company Audit Firms,” which requires all audit firms engaged in audits of listed companies with wide public influence to register with the system for the purpose of enhancing the quality control of registered audit firms and ensuring trust in capital markets in relation to financial statement audits. Lists of registered firms are published on JICPA's website.

Under the CPA Act, JICPA is required to report the status of quality control reviews to the Certified Public Accountants and Auditing Oversight Board (“CPA AOB”) of the Financial Services Agency, which is responsible for monitoring the quality control reviews conducted by JICPA.

The following chart illustrates the structure of Quality Control Review System, involving JICPA and other parties.



## **Audit quality control**

In audit engagements, engagement teams consisting of engagement partners and staff (collectively as “personnel”) audit whether companies are appropriately preparing their financial statements. Audit firms are responsible for ensuring the quality of the entire audit engagements performed by their engagement teams in a reasonable manner. Further, audit firms are required to design and implement policies and procedures for quality control as well as a monitoring system to check compliance with the policies and procedures in order to promote an internal culture recognizing that quality is essential in performing audit engagements. “Quality control” refers to the activities taken by audit firms to ensure audit quality whereas a “system of quality control” refers to the related policies and procedures implemented by audit firms, which include but are not limited to the following:



## Quality control review

“Quality control reviews” are reviews conducted by JICPA, which is responsible for assessing the quality control status of audits performed by audit firms, reporting the results to audit firms and providing recommendations for improvement as necessary. The following procedures are carried out under JICPA's quality control reviews.



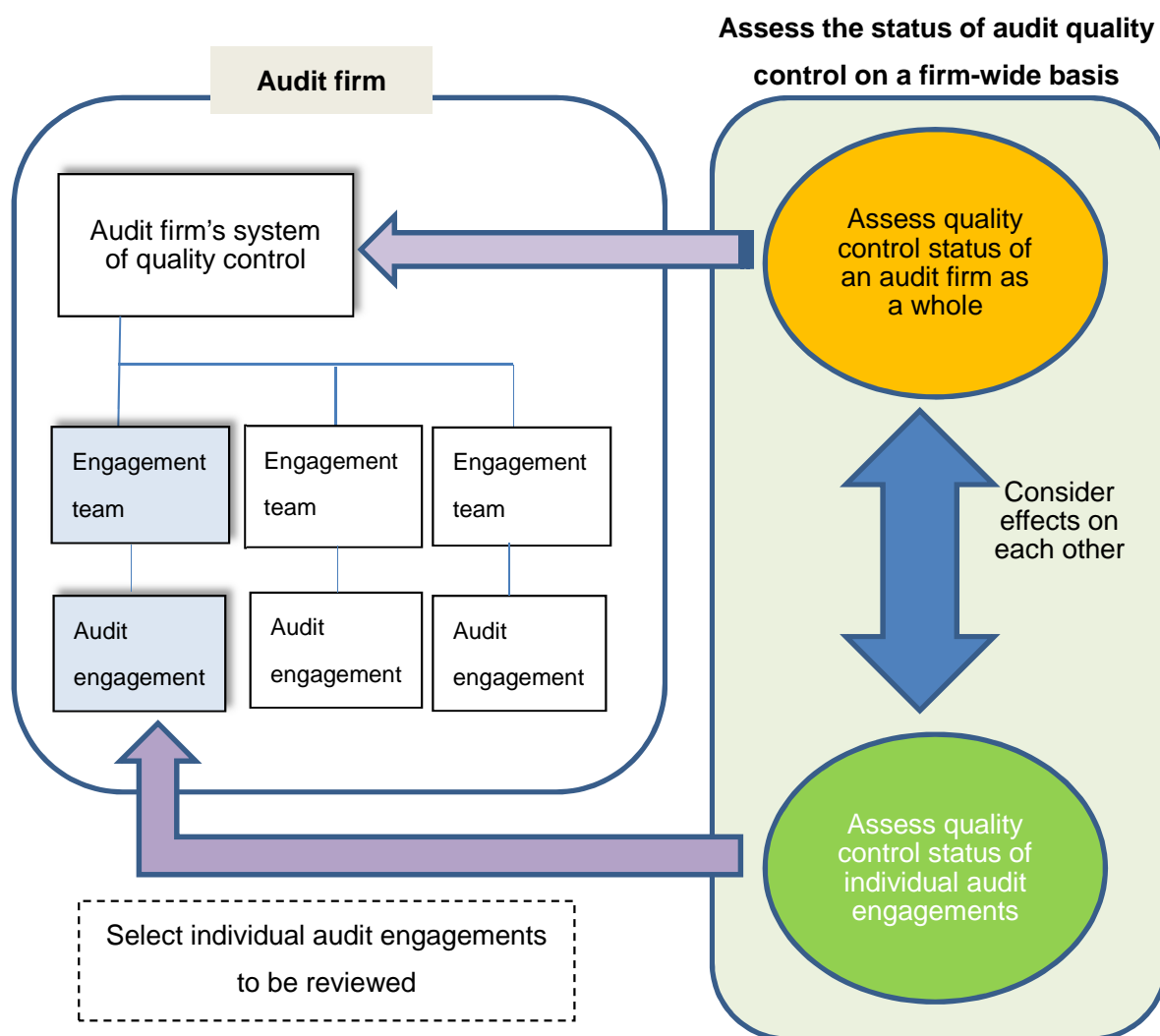
Quality control reviews consist of “Ordinary quality control review” and “Extraordinary quality control review.”

Type of review	Purpose of the review	Audit firms subject to the review	Frequency of the review	
<b>Ordinary quality control review</b>	To assess the status of audit quality control on a firm-wide basis	Audit firms auditing Public Interest Entities defined under the CPA Act as well as large-sized Shinkin Banks (credit associations) and other financial institutions.	Regularly	Once every three years (Once every two years for large audit firms) [Regular review]
			Flexibly	If determined that a regular review should be supplemented subsequently [Additional review]
<b>Extra-ordinary quality control review</b>	1. To assess the status of audit quality control for a specific engagement 2. To assess the status of audit quality control for a specific area of the firm	Any audit firm that provides audit engagements.	Extraordinarily	In the event of possible deterioration of social confidence in audit

## Ordinary quality control review

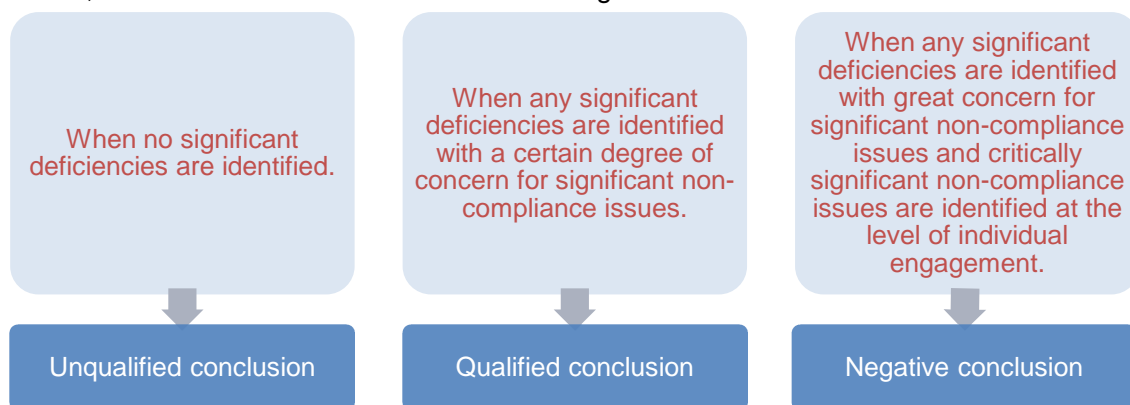
The purpose of ordinary quality control reviews is to assess the status of audit quality control on a firm-wide basis. Major procedures under ordinary quality control reviews are as follows:

- Assess quality control status of an audit firm as a whole  
Review whether the system of audit quality control is appropriately designed and implemented on a firm-wide basis to support individual audit engagements.
- Assess quality control status of individual audit engagements  
Review whether the firm-wide system of audit quality control is appropriately applied to individual audit engagements. Audit engagements should be carefully selected for review purpose so that they reflect the quality control status of the audit firm as a whole, by considering the level of risks in each engagement as well as situations of the audit firm. When any significant findings or a large number of findings are identified in a quality control review, the effect on quality control on a firm-wide basis should also be assessed.



## Results of ordinary quality control reviews

Depending on the level of design and implementation of the quality control system of an audit firm under an ordinary quality control review, JICPA issues a “Quality control review report” to the audit firm, which contains either one of the following conclusions:



When reasonable bases could not be obtained to form an opinion for a quality control review report under certain circumstances, such as when part or all of major review procedures could not be conducted by JICPA, no conclusion is expressed in the report.

## ***Follow-up review***

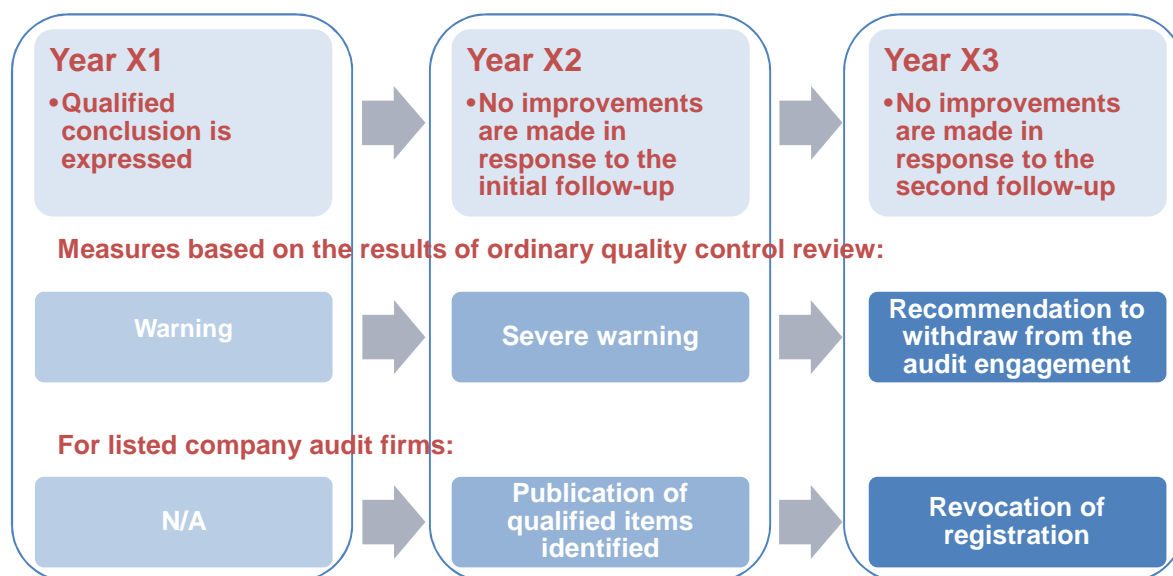
When recommendations for improvement are provided to an audit firm by JICPA as a result of an ordinary quality control review, a “follow-up review” is conducted in the following year to assess the status of improvement measures implemented by the firm. There are two types of results under follow-up reviews: “Improvement measures sufficiently completed;” and “Improvement measures insufficiently conducted.” When the “Improvement measures insufficiently conducted” notice is received from JICPA, the firm will be subject to another follow-up review in the next year.

## ***Measures taken as a result of ordinary quality control reviews***

Depending on the results of an ordinary quality control review and improvements carried out subsequently, the following measures are taken against audit firms urging them to improve the identified deficiencies: “Warning;” “Severe warning;” or “Recommendation for the audit firm to withdraw from the audit engagement.” In addition, listed company audit firms are subject to the following measures in accordance with the Registration System for Listed Company Audit Firms: “Publication of a summary of qualified items identified during the quality control review;” or “Revocation of registration from the list of registered firms.” For example, if an audit firm receives a “qualified conclusion” as a result of an ordinary quality control review in Year X1, and when no appropriate measures are taken for improvement in response to recommendations from JICPA in Year X2 and thereafter, then the audit firm will be subject to more severe measures, such as



“Severe warning” and “Recommendation for the audit firm to withdraw from the audit engagement.” Furthermore, if the firm is a listed company audit firm, it will have to comply with one of the following measures: “Publication of a summary of qualified items identified during the quality control review;” or “Revocation of registration from the list of registered firms.”



## ***Results of quality control reviews***

### ***Number of ordinary/follow-up reviews***

Ordinary quality control reviews and follow-up reviews are conducted as follows:

	2012	2013	2014	2015	2016
Number of audit firms reviewed under ordinary quality control reviews	95	93	89	83	101
Number of audit firms reviewed under initial follow-up reviews	71	72	70	61	52
Number of audit firms reviewed under second follow-up reviews	1	1	6	6	3
Total (A)	167	166	165	150	156
Number of audit firms subject to ordinary quality control reviews (B)	238	234	215	210	209
Percentage of firms reviewed for quality control (A/B)	70%	71%	77%	71%	75%

### ***Results of ordinary quality control reviews***

The following chart represents historical results of ordinary quality control reviews.

There are cases where the total number of audit firms by type of results and the number of audit firms reviewed under ordinary quality control reviews do not agree to each other. This occurs when there is a time lag between the year the ordinary quality control review is conducted and the year the quality control review report is issued.

	2012	2013	2014	2015	2016
Unqualified conclusion	80	85	76	63	83
Qualified conclusion	15	8	9	20	17
Negative conclusion	-	-	-	-	1
No conclusion is expressed	-	-	1	-	-
Total	95	93	86	83	101

### ***Results of initial follow-up reviews***

The following chart represents historical results of initial follow-up reviews.

There are cases where the total number of audit firms by type of results and the number of audit firms reviewed under follow-up reviews do not agree to each other. This occurs when there is a time lag between the year the follow-up review is conducted and the year the follow-up review report is issued.

	2012	2013	2014	2015	2016
Improvement measures sufficiently completed	68	60	61	56	47
Improvement measures insufficiently conducted	3	12	9	4	6
Total	71	72	70	60	53

### ***Results of second follow-up reviews***

The following chart represents historical results of second follow-up reviews.

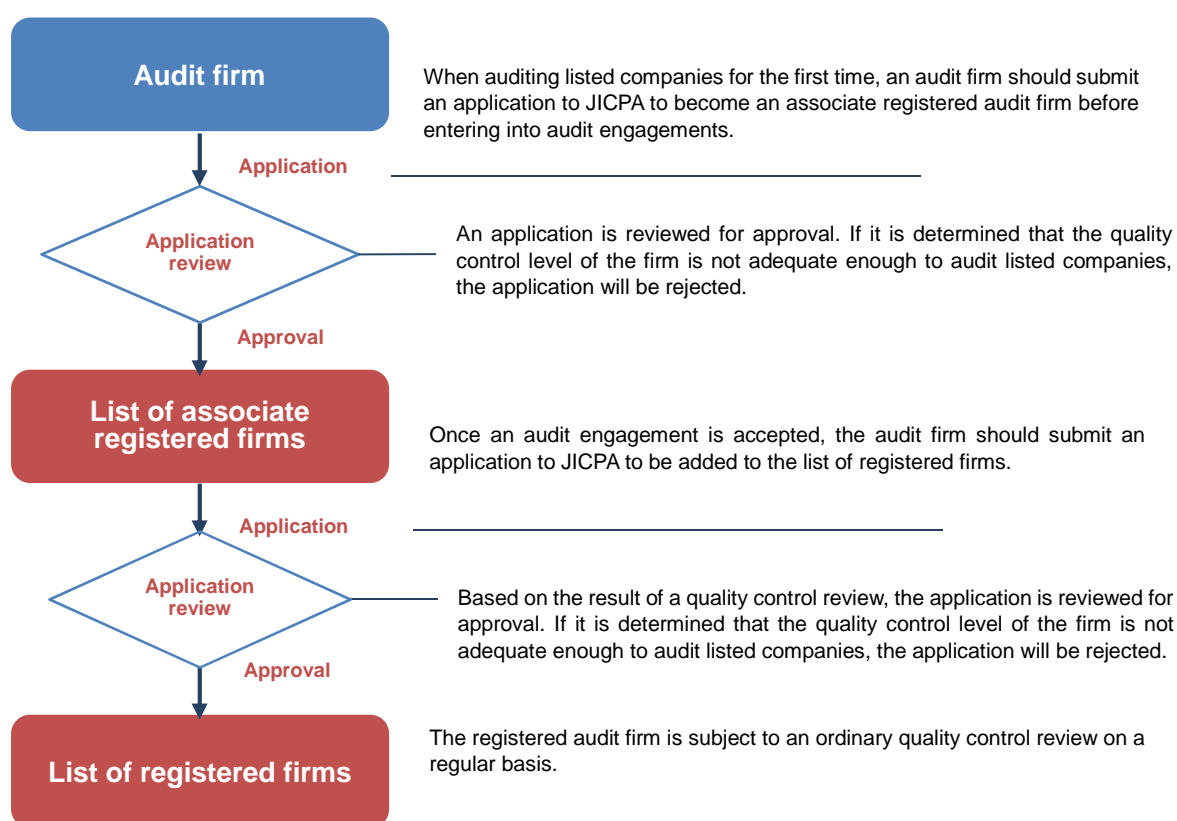
	2012	2013	2014	2015	2016
Improvement measures sufficiently completed	1	1	6	6	2
Improvement measures insufficiently conducted	-	-	-	-	1
Total	1	1	6	6	3

# Registration System for Listed Company Audit Firms

## Overview of the Registration System for Listed Company Audit Firms

JICPA has introduced the “Registration System for Listed Company Audit Firms,” which requires all audit firms engaged in audits of listed companies with wide public influence to register with the system for the purpose of enhancing the quality control of registered audit firms and ensuring trust in capital markets in relation to financial statement audits.

The registration process is summarized as follows:



JICPA posts the list of registered firms on its website, which is made available to the public.

<http://tms.jicpa.or.jp/offios/pub/>

### ***Number of registered audit firms***

As of May 18, 2017, the number of registered audit firms totaled 142, consisting of 131 listed company audit firms registered on the list of registered firms and 11 audit firms on the list of associate registered firms.



