

[Translation Purpose Only]

March 22, 2018

To whom it may concern:

Company Name: Nippon Yusen Kabushiki Kaisha  
Representative: Tadaaki Naito, President  
(Stock Code: 9101, First Sections of  
the Tokyo Stock Exchange and the  
Nagoya Stock Exchange)  
Inquiries: Ushio Koiso, General Manager of  
Corporate Communication Group  
(TEL. 03-3284-5151)

**Completion of the Filing Quarterly Securities Report and Result of Investigation  
For Illegal Conducts in Chinese Subsidiary**

Nippon Yusen Kabushiki Kaisha (the “Company”) hereby provides this notification that it has completed to file Quarterly Securities Report for the Nine Months Ended December 31, 2017 to the Kanto Local Finance Bureau today, March 22 2018, before the extended filing deadline of March 23, 2018.

We sincerely apologize for any inconvenience caused to the shareholders, investors, and all other stakeholders.

Regarding the investigation led by the investigation committee announced as of February 13 and 14 2018, for a suspected unlawful expenditure or embezzlement by former locally-hired management personnel in NYK Car Carrier (China) Co., Ltd., located in Shanghai, China, which is engaged in finished-car logistics business in China, the Company provides the fact as a result of investigations completed as attached (Summary and disclosure version of the Investigation report). As a result of the investigation, we estimated the corporate income tax and VAT to be additionally assessed and late payment and penalty that may arise in the future from revising the accounting and tax reassessment including for the past years due to Inappropriate Accounting, and concluded that the effect on the consolidated financial results will be minimal. Therefore, it is concluded that no corrections would be required to the Company’s consolidated financial results for the past years and Company’s consolidate financial highlights for nine months ended December 31, 2017. Furthermore, it is estimated that the amount which may be influenced in the future due to the above tax reassessment is approx. RMB 53.4 million (approx. JPY 880 million) and the entire amount of this is scheduled to be reflected in the financial results for the year ending in March 2018. No changes in prospects for Company’s consolidate financial result announced on January 31, 2018.

(Translation Purpose Only)

# Investigation Report

**【Summary and Disclosure Version】**

March 22, 2018

Nippon Yusen Kabushiki Kaisha (NYK Line)

Investigation Committee

March 22, 2018

To: Board of Directors, Nippon Yusen Kabushiki Kaisha (NYK Line)

Nippon Yusen Kabushiki Kaisha (NYK Line)

Investigation Committee

Tadaaki Naito, Committee Chair

Yoshiyuki Yoshida, Committee Member

Yutaka Higurashi, Committee Member

Yuichi Sakata, Committee Member

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## **Part 1. Overview of the Investigations Conducted by the Investigation Committee**

### **1. Overview of this Incident**

This incident is an allegation that A, who was the Chairman and President of the Company's consolidated subsidiary, NYK Car Carrier (China) Co., Ltd. (hereinafter "NCCC") (incorporated on August 7, 2006) that is engaged in finished-car logistics business inside China, in collaboration with some of former executive managers of NCCC (hereinafter, including A, collectively referred to as the "group lead by A"), caused NCCC's trading counterparties to make unjust claims for expenses in a total amount of approx. RMB 50.6 million (the amount estimated by the Investigation Committee (hereinafter, the "Committee"), approx. JPY 830 million) (hereinafter, the "Improper Conducts"). Furthermore, the group lead by A inappropriately accounted these unjust expenditures as losses when filing for NCCC's corporate income tax (which is an equivalent of Japan's corporate tax), excessively declared value-added tax (hereinafter, "VAT") (which is an equivalent to Japan's consumption tax), where these erroneous accounting resulted in inadequate tax filings, and thereby created a possibility of additional tax burden of approx. RMB 53.4 million (the amount estimated by the Committee, approx. JPY 880 million) comprised of additional tax and late payment of corporate income tax and consumption tax, and penalty (hereinafter, "Inappropriate Accounting").

Nippon Yusen Kabushiki Kaisha (hereinafter, "The Company") became aware of the strong suspicion of the Improper Conducts and quickly established the Committee on February 5, 2018 and proceeded with the investigation. In the course of conducting relevant investigation and through consultation with Deloitte Touche Tohmatsu LLC (hereinafter "Tohmatsu"), which is the Company's auditor for the submission of the Quarterly Securities Report for the Nine Months ended December 31, 2017, the Company decided that it is necessary to assess the importance and fairness of the expenses for this year and the past years, and to review the fairness of its accounting including local tax consequences in China. As such, on February 14, 2018, the Company applied with the Kanto Local Finance Bureau for extension of the filing deadline for its Quarterly Securities Report for the Nine Months ended December 31, 2017, which was approved and the deadline was extended to March 23, 2018, and conducted the investigation of the Improper Conduct.

### **2. The effect on the Company's consolidated financial results and accounting**

We estimated the corporate income tax and VAT to be additionally assessed and late payment and penalty that may arise in the future from revising the accounting and tax reassessment including for the past years due to Inappropriate Accounting, and concluded that the effect on the consolidated financial results will be minimal as explained below. Therefore, it is projected that no corrections would be required to the Company's consolidated financial results for the past years and to the Company's consolidated financial highlights for nine months ended December 31, 2017. Furthermore,

it is estimated that the amount which may be influenced in the future due to the above tax reassessment is approx. RMB 53.4 million (approx. JPY 880 million) and the entire amount of this is scheduled to be reflected in the financial results for the year ending in March 2018.

(1) The amount found to be affected by the Improper Conducts

The amount of transactions found to be affected by the Improper Conducts at NCCC was approx. RMB 50.6 million (approx. JPY 830 million) in total, and the counterparties to these transactions and the respective amount of transactions involved are as follows:

Unit: RMB

Counterparties	Fiscal Year	Amount	The amount of transactions found as improper
(1) Trading Counterparties found having unjust payment	2013	11,360,645	6,702,781
	2014	9,431,334	5,564,487
	2015	13,263,031	7,825,188
	2016	12,067,958	8,596,095
	2017	20,757,225	18,716,563
	<b>Total</b>	<b>66,880,193</b>	<b>47,405,114</b>
(2) Trading Counterpart found having unjust payment based on the unreasonable contract	2016	1,800,000	1,800,000
	2017	1,350,000	1,350,000
	<b>Total</b>	<b>3,150,000</b>	<b>3,150,000</b>
<b>(1) + (2) Total</b>	<b>Total</b>	<b>70,030,193</b>	<b>50,555,114</b>

The facts found as Improper Conducts are categorized as follows as explained in “Part 3. 2. Facts which constitute the Improper Conducts”

- Unjust payment towards Trading Counterparties
- Unreasonable agreement with and unjust payment to Trading Counterpart

(2) Details of the Inappropriate Accounting

The amounts that NCCC’s Inappropriate Accounting affected NCCC’s past financial results are as follows. The transactions that became subject to tax reassessment are the following, which will be stated in below “Part 3. 4. Details of the Inappropriate Accounting” and the total amount which

may affected in the future is estimated to be approx. RMB53.4 million (approx. JPY 880 million) of corporate income tax.

- Inappropriate payment to Trading Counterparties and deduction of this as expenses
- Deduction of penalty, etc. as expenses
- Inadequate proof concerning disposal of fixed assets

<Necessary revision of journalizing>

Unit: RMB ( ) indicates credit

Fiscal year	Balance Sheet	Statements of Income	Statements of Income	Statements of Income
	Amount in short of “Income taxes payable”	Incorrectly accounted item “Cost and expenses”	Incorrectly accounted item “Non-operating expenses”	Amount in short of “Total income taxes”
2013	(14,748,141)	(7,839,195)	7,839,195	14,748,141
2014	(9,164,946)	(4,023,274)	4,023,274	9,164,946
2015	(10,421,393)	(7,366,034)	7,366,034	10,421,393
2016	(11,711,135)	(8,573,857)	8,573,857	11,711,135
2017	(7,407,059)	(20,254,087)	20,254,087	7,407,059
<b>Cumulative amount</b>	<b>(53,452,674)</b>	<b>(48,056,447)</b>	<b>48,056,447</b>	<b>53,452,674</b>

### 3. The Committee and its objectives

The Company established the Committee on February 5, 2018. The Committee is comprised of the below members, and some external specialists were also retained in Japan and China for the below objectives to conduct the investigation (hereinafter, the investigation conducted by the Committee shall be referred to as the “Investigation”).

• Composition of the Committee

Chairman	Tadaaki Naito	President, Representative Director and President Corporate Officer
Member	Yoshiyuki Yoshida	Director and Managing Corporate Officer, Chief Compliance Officer
Member	Yutaka Higurashi	Corporate Officer and Deputy Chief Compliance Officer
Member	Yuichi Sakata	Attorney at Abe & Sakata Legal Professional Corporation



• Objectives of the Committee

1. Investigation and analysis of the facts and the cause of the alleged Improper Conducts and investigation of similar incidents

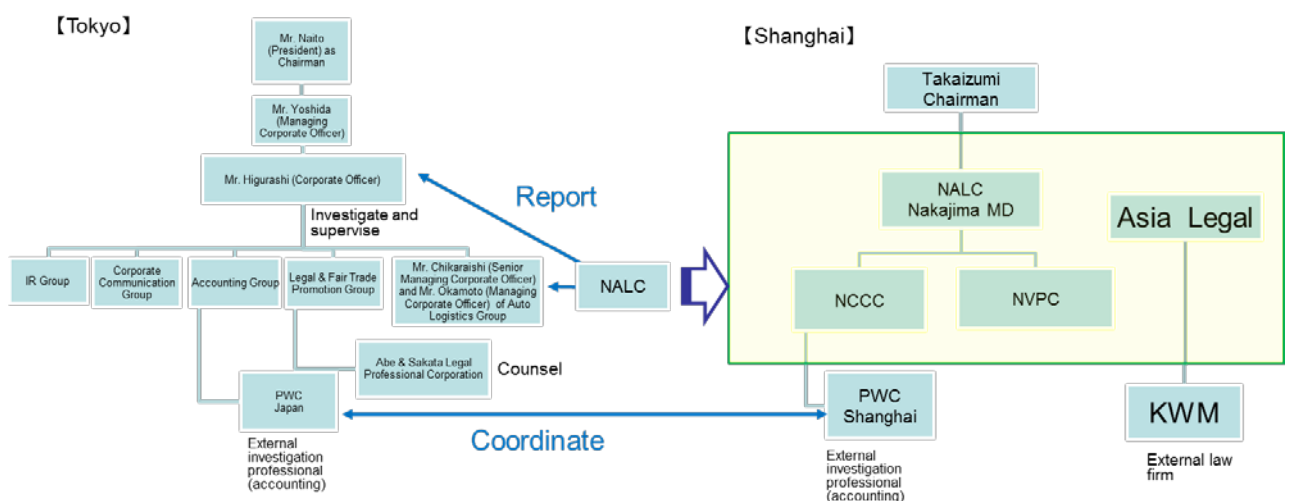
2. Analysis and evaluation of issues concerning internal control and recommendation on measures to prevent recurrence

3. Collect evidence such as tax accusations and criminal accusations towards the parties relating to the Improper Conducts

• The Investigation Team

The investigation team comprised of the Committee and the internal organizations and external specialists relating to the Investigation are as follows. The Company retained PwC, Abe & Sakata Legal Professional Corporation and KWM as external specialists.

The Arrangement of the Committee



PwC: PricewaterhouseCoopers Aarata LLC

PwC Shanghai: PwC Business Consulting (Shanghai) Co., Ltd (Risk Assurance)  
PwC Consultants (Shenzhen) Limited, Shanghai Branch (Tax)  
(PwC and PwC Shanghai may be collectively referred to as “PwC”)

KWM: King & Wood Mallesons (hereinafter, “KWM”)

NALC: NYK Automotive Logistics (China) Co., Ltd. (a wholly-owned subsidiary that is engaged in finished-car logistics business in China that is the parent company of NCCC, hereinafter, “NALC”)

NVPC: NYK Vehicle Processing Service (Shanghai) Co., Ltd. (a subsidiary of NALC, hereinafter, “NVPC”)

#### 4. Period and schedule of the Investigation

The period and schedule of the investigation are as follows:

Schedule	Events
February 5	Establishment of the Committee
February 7 -9	Explain to the Kanto Local Finance Bureau
February 13	Make a timely disclosure with the Tokyo Stock Exchange (1) (Illegal Conducts in Chinese Subsidiary)
February 14	Decision to file with the Kanto Local Finance Bureau the application for extension of the filing deadline for the Quarterly Securities Report for the Nine Months Ended December 31, 2017
February 14	Make a timely disclosure with the Tokyo Stock Exchange (2) (Receive approval from the Kanto Local Finance Bureau on Extension of the Filing Deadline for the Quarterly Securities Report for the Nine Months Ended December 31, 2017)
March 5	Interim report (PwC)
March 13	Final report (PwC)
March 16	Report from Abe & Sakata Legal Professional Corporation on issues concerning internal control
March 22	Submit the investigation report to the Company's Board of Directors
March 22	Scheduled to make a timely disclosure with the Tokyo Stock Exchange (3) (Report on Investigations Concerning the Improper Conducts of the Chinese Subsidiary)
March 22	Scheduled to receive a report on the review of quarterly results (Tohmatsu)
March 22	Scheduled to file Quarterly Securities Report with the Kanto Local Finance Bureau through the EDINET
March 22	Scheduled to make timely disclosure with the Tokyo Stock Exchange (4) to report the submission of the Quarterly Securities Report

#### 5. Background of the Incident (from discovery to establishment of the Committee)

- On May 5, 2017, there was a system trouble in NCCC (it was found that the image of the top page of NCCC's system was replaced with the image of a Company managed by A).
- On June 10, 2017, there was an anonymous whistle-blowing which revealed A's involvement in a Company described above.
- On July 17, 2017, there was a whistle-blowing to NALC's CEO seconded from the Company regarding the possibility of the group led by A misusing the research and development information

of new NCCC's Dealer Delivery System.

- On 25, July, 2017, it was revealed that a Company described above has a system which is almost the same as that of NCCC. There was a suspicion of the group led by A misusing the NCCC's system.
- On August 4, 2017, NCCC's Board of Directors Meeting was held. An explanation regarding an introduction of external audit (with appointment of PwC) was given.
- On August 16, 2017, emails were sent from the locally-hired management personnel to the Company which criticize the fact that the consideration for an external audit was mainly led by the employee seconded from the Company, and on the same day, NALC's CEO seconded from the Company explained and consulted with KWM.
- On November, 2017, there was a sabotage initiated by the group led by A.
- On November 22, 2017, an investigation on tax affairs was requested to PwC Shanghai (hereinafter "Previous Investigation").
- On December 6, 2017, PwC Shanghai Forensic Team initiated the investigation (hereinafter "Previous Investigation").
- On January 19, 2018, consultation with PwC Shanghai and KWM regarding tax accusation and criminal accusation.
- On January 26, 2018, PwC Shanghai reported the progress regarding the possibility of estimated penalty tax or the like.
- On January 29, 2018, the progress report dated January 26 was reported to the Company.
- On February, 2018, a policy on tax accusation and criminal accusation was determined.

## **6. Method and scope of the Investigation**

### **(1) Status of Implementation of the Previous Investigation**

Digital forensic investigation of emails or the like of the group led by A was conducted (preservations of evidence and investigations/analysis of electronic records such as PC data and emails).

### **(2) Investigation regarding Alleged Improper Conducts**

#### **(i) Target Companies of the Investigation**

Three companies to the extent that A might have an influence were identified: (a) NCCC at which many of the persons in the group led by A work, (b) NALC in which A served as the Director and the President, and (c) NVPC, a subsidiary of NALC, in which A served as the Chairman since its establishment until the retirement.

#### **(ii) Method of the Investigation of NCCC**

The Committee decided to conduct digital forensic investigation of the emails of the group

led by A. In addition, the Committee decided to conduct interviews against the relevant officers and employees.

(iii) Method of the Investigation of NALC

As described later, given that NALC has an administrator who conducts a monitoring on purchasing and payments independent from the group led by A, and that no sign of improper conduct was identified in the Previous Investigation, the Committee decided to conduct interviews against the relevant officers and employees.

(iv) Method of the Investigation of NVPC

As described later, given that NVPC has an administrator who conducts a monitoring on purchasing and payments independent from the group led by A, and that no sign of improper conduct was identified in the Previous Investigation, the Committee decided to conduct interviews against the relevant officers and employees.

(v) Investigations on Similar Incidents

The Committee investigated whether or not there were any similar incidents in the companies other than those three companies described above. Please see Part 2 “3. Investigations and Results regarding the Possibility of Similar Events in Other Subsidiaries” for the details and results of the Investigation conducted.

(3) Investigation regarding Issues on the Internal Control

In addition to NCCC at which the Improper Conducts were conducted, the Committee also conducted investigations in relation to the internal control system, management of internal control or the like of the Company, which forms a business group with NALC, the parent company of NCCC. Also, the Committee conducted interviews against the current and former officers and employees who have or had been mainly engaged in the automobile logistics business relevant to the matter.

## 7. Investigation by the Investigation Committee and premises of fact findings

Although certain reasonable findings of facts were obtained through the Investigation by the Committee to accomplish the purpose of the Investigation, given that the Committee conducted the Investigation without cooperation from the group led by A which involved in the Improper Conducts, that there was limited data, and as described in Part 1. “4. Period and schedule of the Investigation”, due to a time constraint, the Investigation conducted by the Committee, including the investigations conducted by external specialists, does not guarantee the completeness of the results of Investigation. In addition, in principle, this Investigation Report and the results of Investigation are intended to be used for the purpose of the Investigation, and the Committee assumes no responsibility against any third party other than the Company.

## **Part 2. Facts Discovered from the Relevant Investigation (No Similar Incident was Found)**

### **1. Results of the Investigation conducted against NALC**

As described below, no issues were found:

- (i) No document or the like was found which suggests that similar improper accounting treatment was conducted by NALC.
- (ii) As a result of interviews against officers who give internal approvals and treasurers, no similar sign of fraud was identified.
- (iii) On February, 2018, legal representatives, shareholders and Directors in respect of NALC's ten major vendors were investigated via the National Companies Credit Information Disclosure System (<http://www.gsxt.gov.cn/corp-query-homepage.html>) and none of them had the same name as those persons in the group led by A.
- (iv) As a result of reviewing the checks and approvals of bank payment transactions in respect of 24 transactions, which are sampled from the transactions conducted from July 2010 to December, 2017, deficiencies were found in two transactions. However, neither of them suggests any risk of fraud.
- (v) As a result of reviewing the access to the system in which bank transfer payments are made, no deficiency was found.

### **2. Results of Investigation conducted against NVPC**

As described below, no issues were detected:

- (i) No document or the like was found which suggests that similar improper accounting treatment was conducted by NVPC.
- (ii) As a result of interviews against officers who give internal approvals and treasurers, no similar sign of fraud was identified.
- (iii) The legal representatives, shareholders, and Directors in respect of the ten major vendors were investigated via the National Companies Credit Information Disclosure System (<http://www.gsxt.gov.cn/corp-query-homepage.html>), and none of them had the same name as those persons in the group led by A and no payment was made against the counterparty who was determined to be inappropriate as a results of the Investigation of NCCC.
- (iv) As a result of internal control testing pertaining to the approvals of payment request system and approvals on banking payment transactions conducted on the six transactions which are sampled from the period during January, 2016 to December, 2017, no deficiency was found.

### **3. Investigation and its results regarding the possibility of similar incidents in other subsidiaries**

As a result of interviews conducted to the officers and employees in NCCC, the Committee

did not identify any additional improper conduct. With regard to the other group companies including NALC/NVPC, based on the results of the questionnaire surveys etc., no situation was identified which suggests a strong doubt of the similar improper conduct.

### **Part 3. Facts Discovered from the Investigation against NCCC and findings thereof**

#### **1. Members of the group led by A**

It is recognized that the Improper Conducts were performed by the group led by A, and All of them had the authority over finance or purchase.

#### **2. Facts which constitute the Improper Conducts**

The following is the facts which were recognized as the Improper Conducts with strong suspicion.

However, the specific details of these conducts will not be disclosed since such disclosure may affect the procedures of criminal accusation in China.

##### **(1) Unjust payment Trading Counterparties**

Approx. RMB 47.4 million (approx. JPY 780 million) was unjustly paid from NCCC in the name of service fees for services which considered having never been provided.

##### **(2) Payment under unjust agreement with Trading Counterpart**

An unnecessary and inappropriate agreement was executed and approx. RMB 3.2 million (approx. JPY 50 million) in total was paid from NCCC

#### **3. Cause of the Improper Conducts and disablement of internal control**

##### **(1) The environment that allowed improper activities**

- (i)** Since NCCC covered on-site operation of logistics, communication was often made only in Chinese and it was difficult for assigned employees to monitor the details.
- (ii)** NCCC did not have a resident monitoring manager independent of the group led by A and was located an hour's drive from NALC, which are considered a factor of insufficient daily

management.

(iii) Although the Company's automobile logistics group periodically reviewed the financial statements since it is a consolidated subsidiary, unjust expenditure was not conspicuous enough to create abnormality in the overall financial statements; therefore, it was difficult to discover such unjust expenditure at this point.

(iv) While A had successively assumed the management of NALC/NCCC, A allocated important posts to the member of the group led by A to create an organization which would be under the control of A.

(2) Disablement of internal control over financial reporting in NCCC (management override)

Since the main business of NCCC was on-site operations of logistics, communication was often made only in Chinese and location was remote, the group led by A occupied the important posts while independent monitoring and management were insufficient. Although internal control over financial reporting was in place, its locally recruited management team did not appropriately operate it. A created an organization which was under the control of A while A had successively assumed the management of NALC/NCCC. Under such circumstances, A who was the general manager of NCCC disabled the internal control.

(3) Defect of internal control over financial reporting in NALC

NALC believes that NALC management needs to check important transactions in terms of value or a business scope with high risk in NCCC's business by additional approval or monitoring functionality. However, since NCCC covers on-site operation of logistics, communication was often made in Chinese and location was remote; hence, there was a circumstance where NALC's close monitoring and management independent of NCCC did not function. Thus, the actual management was performed only by NCCC executives, which resulted in the Incident.

#### **4. Details of the Inappropriate Accounting**

(1) Details of the Inappropriate Accounting and tax reassessment

It is necessary to transfer the misappropriated money from operating expense to non-operating expense and previous expenses included in deductible expense will not be expenses for tax purpose. Further, the money misappropriated by the group led by A is considered extremely difficult to collect.

As the result, the total amount of additional tax of corporate income tax and VAT which are expected to occur in the future resulting from the tax correction, and late payment and penalty are estimated approx. RMB 53.4 million (approx. 880 million). Of the transactions listed in "Part 3. Facts which constitute the Improper Conducts," the transactions subject to the tax correction are the following 3 transactions:

- Unjust payment to Trading Counterparties and the inclusion in deductible expenses

These two transactions plus the following two transactions which are described below in (2) and (3)

- Inclusion of penalties in deductible expenses
- Insufficient evidence of disposal of fixed assets

(2) Inclusion of penalties in deductible expenses

The Chinese tax expert pointed out that NCCC recorded penalties of approx. RMB 43.9 million (approx. JPY 720 million) under deductible expenses from 2013 to 2017 and possibility of disapproving such inclusion in deductible expenses and resulting in additional tax payment. Since the Chinese tax expert determined that they are deemed as an item which is excluded from deductible expenses under Chinese tax laws and the tax authority is highly likely to disapprove such inclusion, the Chinese tax expert made the transaction subject to tax correction. The amount is estimated RMB 27.2 million (approx. JPY 450 million) as the aggregation of additional tax, and late payment and penalty.

Although the investigation into the details of such expenses was conducted as much as possible in spite of the limitation caused by confiscation of accounting related materials by the tax authority, the use was not identified from the descriptions of “Special account,” an accounting expense under which penalties are recorded. By collating data from new and old systems of request for decision and from accounting system data, an expense “Guiding fee” was paid to individuals and such fee was presumed to be used to avoid penalty at any locations. Further, the data of the penalty paid by the company in the past 5 years were extracted from the system data of trucks and the amount which would fall under coordinating fee or the equivalent thereto was calculated (RMB 21.6 million (approx. JPY 350 million)).

According to KWM, if such payment is recognized as bribery to the police or government employees, NCCC will be imposed fines pursuant to Chinese criminal code and since the prescription takes 10 years to expire, there is a risk that such conduct from 2008 may be subject to such punishment. It is assumed that RMB 38.5 (JPY 630 million) had been paid under coordinating fee in total 10 years since 2008, by calculation using average proportion in the “Special account”. Although, in Item 37, Paragraph 14 of the International Accounting Standard (IAS), requirements for recognizing reserves are (a) a company has current (legal or constructive) obligations as a result of past events, (b) it is highly probable for resources having economic benefits to outflow in order to settle such obligations and (c) the amount of such obligations can be estimated in a reliable manner, it is decided not to recognize reserves because a fact cannot be recognized which can prove the existence of legal or constructive obligations. Moreover, since the possibility of being pursued is considered significantly low, it is determined that disclosure as contingent obligations is not necessary as well.



(3) Insufficient evidence of disposal of fixed assets

The Chinese tax expert detected the fact that when NCCC's client's tentative tent for storing finished-car was disposed of in 2016, NCCC did not go through necessary registration for tax purpose. Since it is highly probable that the tax authority disapproves the inclusion because prior notification which is a requirement for inclusion in deductible expenses for tax purpose in China was not given, the Chinese tax expert estimated RMB 1.6 million (approx. JPY 30 million) as the total of additional tax, and late payment and penalty.

(4) Accounting treatment in the Company's consolidated accounting

Although the effect on the consolidated accounting occurs in connection with the effects of corporate income taxes which are expected in the future resulting from accounting correction and tax correction of previous fiscal years due to the Improper Accounting, correction on the Company's consolidated accounting in the previous fiscal years and the summary of the third-quarter consolidated accounting is not expected as such effect is minimal. The total amount of additional tax of corporate income tax and VAT which are expected to occur in the future resulting from the tax correction above, and late payment and penalty are estimated approx. RMB 53.4 million (approx. 880 million). All of this amount will be included in the fiscal year ending March 2018.

#### **Part 4. Status of the Internal Control of the Company, NALC and NCCC**

##### **1. Internal control system of The Company**

(1) Outline of the structure of internal control system

The structure of internal control system has been resolved every year at the Board of Directors meetings since it was initially resolved at the meeting of the Board of Directors of the Company held on May 10, 2006, the fact of which is also disclosed in the business report in the convocation notice (on the Company's web page).

(2) Operation and implementation of internal control system

(i) Internal control committee and major risk control

• At major risk selection meetings of each headquarters, each business headquarters had evaluated the impact of each risk item when it is realized and feasibility (frequency) thereof by dividing respective risk item into four grades totaling sixteen grades (Aa-Dd). However, the Automotive Transportation Headquarters had never reported any fact concerning the Improper Conducts nor any fact suggesting that, nor had any fact concerning the Improper Conducts or any fact suggesting that been reported at the internal control committee meetings.

(ii) Operation related to internal audit

• Internal audit pertaining to NCCC

Internal audit of NCCC was conducted in September 2007, December 2009, March 2013 and March 2015. The audit report submitted after the visiting audit described as follows:

(a) Corporate governance and compliance (“Moderate” risk)

- No provision pertaining to response to government officials and quasi-government officials.
- No annual written pledge pertaining to the disclosure related to conflicts of interest by employees.

(b) Contract management (risk level: “Low”)

- There are some contracts with key vendors in which the Anti-Bribery clause is not inserted.

(c) Sales and accounts receivable

- Nothing particular.

(d) Purchasing, disbursements & accounts payable

- Nothing particular.

(e) Operation (risk level: “Moderate”)

- No inspection record on the keys of commerce cars and other matters.

(f) Accounting & finance (risk level: “High”)

• Claims receivables from insurance companies in the amount of RMB28.7 Million are outstanding.

(g) Human & resources & general affairs (risk level: “Moderate”)

- Meetings upon retirement of employees are not regularly held.

(h) Information technology and contingency management (risk level: “High”)

- Passwords for the company’s key systems have not been frequently changed, etc.

With regard to the written pledge in Paragraph 2 of (a), the internal audit office was informed of acquisition of the written pledge from the executive manager belongs to Group lead by A in August 2015, and the Regional Administration Office (hereinafter “RAO”) was also informed to the effect that such failure had been resolved from NALC Director and General Manager who is an agent for A at the Internal Audit Follow-Up Committee held in August 2016. Internal audit reports have also been submitted in September 2007, December 2009 and March 2013, some of which had several problems but there was no part that was clearly defective or insufficient in the reports themselves.

• Internal Audit pertaining to NALC

Internal audit of NALC was conducted in March 2012, March 2015 and July 2017, respectively. In the internal audit, there was also no part that was clearly defective or insufficient in the reports themselves despite some problems. In addition, a follow-up audit to confirm whether the matters that were deemed necessary to respond to in the previous audit was conducted in May 2013.

(iii) Operation concerning compliance

The Company has established a system in which the control division of the Company may be informed of compliance incidents concerning overseas subsidiaries by email or other means, and the Legal and Fair Trade Promotion Group/Compliance Team receives daily reports on compliance incidents concerning domestic and overseas subsidiaries from the control division. Reports to CCO have been made in an appropriate manner, and factual investigations and corrective measures have been taken and reports have been provided to the compliance committee as necessary.

## **2. Internal control system structured by NALC and NCCC**

### **(1) Internal control system Structured by NALC**

#### **(i) Organization structure and its actual status**

##### **• Board of Directors**

Meetings of the Board of Directors had been held twice every year at first and once every year since 2013. At the meetings of the Board of Directors, management policy and investment plan of the company, election of Directors and Auditors and approval of budgets and settlement of accounts, which belong to shareholders' authorities under the Company Law, were determined in addition to the election of the General Manager, which authority is vested with the Board of Directors. The officers of the Automotive Transportation Headquarters and the head of the Auto Logistics Group attended the meetings as Directors and the head of the same group and his subordinates also attended the meetings as Observers.

#### **(ii) Internal control system structured by NALC**

At NALC, the business division and the accounting division had been separated, and with regard to the business execution by each division, authorization standards had been established and matters to be approved by the General Manager, the President, the Board of Directors and finally by the headquarters had been specified in detail according to the content of services and the amount relevant thereto. A system called "Office Anywhere" (OA System) should be used for decision-making on application, request for approval and approval.

The rules of NALC related to finance and accounting as a system to procure that the business execution by officers conforms to the laws and the articles of incorporation are as follows:

##### **• Management of accounts receivable and accounts payable**

➤ Accounts Receivable Management Policy 应收账款管理制度

➤ Accrual Management Rules 预估管理流程

➤ Accounts Payable Management Policy 应付账款管理制度

##### **• Invoice management**

➤ Invoice Management Rule 发票管理制度

➤ Rule for Invoice Making Out Procedure 业务开票流程制度

➤ Regulation for Limitation of Invalid Freight Invoice 公路运输发票月作废限额的税务规定

• Accounting and tax

- Summary Table of Accounting Items 会计科目汇总表
- Management System for Accounting Statement 会计报表管理制度
- Monthly Financial Closing Procedure 月末账务处理流程
- Management System for Corporation Tax 公司税务管理制度
- Accounting Files Management Rules 会计档案管理制度

• General financial management

- Financial Management System Management Policy 财务管理信息系统管理办法
- Cash Advance Management Rules 暂借款管理细则
- Bill and Financial Seal Management System 票据与财务印章管理制度
- Company Credit Card Management 公司信用卡使用制度

(iii) Conditions of operation of internal control system

It is impossible to deem that the internal control system in (ii) symbolized by the evidence provision was not operated in an appropriate manner.

(2) Internal control system which had been structured by NCCC

(i) Organization structure and its actual condition

• Board of Directors

At NCCC, meetings of the Board of Directors had been held approximately once every year. At the meetings, determination of management plan of the company, election of Directors and Auditors and approval of budgets and settlement of accounts as well as election of the General Manager, which is an authority of the Board of Directors, were resolved in general.

(ii) Internal control system which had been structured by NCCC

• Organization and system of business execution

NCCC improved the authorization standard for business execution by each division by around 2012, and therefore it seems that matters to be resolved by the General Manager, the President and other officers and the Board of Directors seems to have been classified in detail according to the content of services and the amount relevant thereto. A system called Office Anywhere (OA System) was used in making decisions.

• Improvement of various types of provisions

(a) Summary

Since 2012, various types of provisions for proper management of NCCC have been improved on the initiative of A by advocating SOP management (management by Standard Operation Procedure).

(b) Supplier management

- October 2012 Contract Management System (“合同管理制度”)
- October 2012 Purchase Control Procedure (“采购控制程序”)

➤ September 2016 Related Party Management Procedure(“相关方控制程序”)

(c) Management of accounts receivable and accounts payable

➤ April 2012 Standard for Accounts Receivable Management Method

➤ October 2012 Accounts Receivable Management Flow Chart

➤ April 2012 Standard for Accounts Payable Management Method

➤ October 2012 Accounts Payable Management Flow Chart

➤ October 2012 Payment Procedure Flow Chart

(d) Invoice management

➤ April 2012 Standard for Invoice Management Method

(e) General accounting and finance

➤ April 2012 Financial Management System

➤ April 2012 Corporate Accounting System

(f) Other

With regard to the service disciplines for employees, NCCC Employee Code of Conduct and Management Handbook have been prepared and distributed. They include detailed descriptions on so-called code of conduct such as compliance with various rules of the company and employment conditions and employee benefits in addition to limitations on conflicts of interest, and also include so-called whistle-blowing system specifying the contact information and telephone number when a business execution that goes against them is found.

(iii) Operation status of internal control system

Since 2015, NCCC has held meetings once every year to confirm the status of achievement of establishment of the quality management system and the challenges thereof. This suggests that the group lead by A which had controlled the transportation administration division and the general administration division arbitrarily ignored various types of provisions and conducted the Improper Conducts in violation thereof despite this structure.

### **3. Relationship between the Company's Automotive Transportation Headquarters and NALC, and between NALC and NCCC**

(1) Relationship between the Company's Automotive Transportation Headquarters and NALC

At the Company, the Auto Logistics Group supervises the finished-car logistics companies. Specifically, this is (i) to supervise on the matters relating to car-related projects and (ii) to oversee compliance with foreign and local laws applicable to the Auto Logistics Group.

(2) Relationship between NALC and NCCC

(i) NALC subcontracted to NCCC to perform the road transportation agreement of the finished cars consigned from car manufacturers. However, in actual situation, the executive managers of

Group lead by A of NALC's transportation department concurrently serve as executive managers of NCCC's relevant business department and this agreement was substantially subcontracted to and accepted by the same parties.

(ii) It could therefore be viewed that NALC's officers in fact made decisions for NCCC.

#### **4. Problems of internal control inside the Group**

(1) Concerning the internal control system established at NALC/NCC

(i) Organization of NALC/NCCC is substantially integrated with the Automotive Transportation Headquarters

With respect to the relationship respectively between the Automotive Transportation Headquarters and NALC, and between NALC and NCCC, it is fair to substantially view them as one organization that constitutes the Auto Logistics Group. Also with respect to the relationship between NALC and NCCC, NCCC could substantially be viewed to be organizationally integrated with NALC. Therefore, it is interpreted that the Automotive Transportation Headquarters assumes an obligation to establish and operate the internal control system stipulated by the Companies Act with respect to NALC and NCCC as if this system is its own system.

(ii) Regulations prepared by NALC/NCCC

With respect to the regulations prepared by NALC/NCCC to ensure legitimate and efficient execution of business (the regulations to prevent unjust activities of the nature of the Improper Conducts in question), it could be said that those regulations for NALC are appropriate. The regulations for NCCC could be said that they are generally appropriate. Therefore, it cannot be found that the Automotive Transportation Headquarters neglected its obligations to prepare regulations for NALC/NCCC.

(iii) Problems inside NCCC that allowed the Improper Conducts

The group lead by A ignored and breached the regulations concerning purchase and disbursements and it issued an order the Trading Counterpart, etc. for temporary staffing. One of the problems that allowed the Improper Conducts is attributable to allowing only the persons of the group lead by A to dominate the head positions at NCCC's general administration department and transportation department and conducting both operations of purchasing and disbursements. Therefore, the operation of the internal control system was inappropriate in certain respects.

(iv) Causes that allowed the Improper Conducts at the Automotive Transportation Headquarters

It is found that A made decisions and executed NCCC's business without anyone checking and supervising him whatsoever. One of the causes that allowed the Improper Conducts was the shortfall in NALC's organizational structure to enable the Automotive Transportation Headquarters to check and supervise the group lead by A at NCCC.

(v) The shortfall in NALC's organizational structure only exists in relation to NCCC

The failure of the internal control system to operate due to shortfall in the organizational structure of NALC existed only in relation to NCCC, and this problem does not exist in relation to NALC itself or other logistics companies managed and administered by NALC.

(2) Concerning the Company's internal control system

(i) The Company's internal control regulations

The Company's internal control regulations (internal audit rule and internal audit manual (for Japan and overseas)) are appropriate.

(ii) Internal audit towards NALC/NCCC

Internal audit on NALC was conducted in March 2012, March 2015, and in July 2017. Internal audit on NCCC was conducted in September 2007, December 2009, March 2013, and in March 2015. The internal audit division and RAO's auditors who actually conducted the audit did not discover the Improper Conducts through these audits. It was heard that an auditor discovered in the audit conducted on NCCC in March 2015 that an employee has not submitted a written covenant concerning disclosure relating to conflicts of interest. The auditor indicated this fact to NCCC and the auditor later received a report from NCCC attached with a copy of that covenant and heard that the situation was corrected. From these circumstances, it cannot be said that there was a shortcoming in internal audit.

(3) Concerning the Company's compliance system

The contents of the Company's compliance regulations are in accordance with the provisions of the laws and the contents therein stipulate on necessary matters and are reasonable, and they could be evaluated to be appropriate. It cannot be said that there was a shortfall in the operation of compliance system also in connection with the implementing of the Company's compliance regulations.

## **Part 5. Measures for Recurrence Prevention (Corrective Measures)**

### **1. Fair and severe internal punishment and pursuit of liability**

The biggest cause of the occurrence of this incident is lack of compliance awareness of the group led by A. In order for the Group to prevent recurrence by developing compliance awareness and by instilling discipline, it is most important to clearly indicate the Group's intention of disallowing injustice.

### **2. Development of compliance awareness**

Lack of compliance awareness of the group led by A which was involved in the Improper

Conducts is also considered as one of the causes of this case. As the countermeasures against such primary cause, it is necessary to improve management of subsidiaries. In addition, as the measure for developing employees' compliance awareness, it is necessary to conduct training within NCCC in order to again instill internal rules, etc., concerning compliance at the work site. Furthermore, in NCCC, it is necessary to ensure that oath regarding conflict-of-interest transactions is obtained every year from all the employees based on the matters pointed out by the internal audit division of NGEA.

In addition, the management of NALC/NCCC considers that it is necessary to have a full understanding of the obligations and responsibilities under Company Law and to thoroughly conduct internal control including management of subsidiaries. In order to reduce the risk of occurrence of similar events in other affiliates, it must be ensured that compliance education is given also to the local managers, personnel in charge of finance and accounting of the overseas affiliates, in particular.

### **3. Reorganization of bodies and organizations, etc., in NALC/NCCC and monitoring by the headquarters**

#### **(1) Restructuring of the organizations of NALC/NCCC**

In the body of NALC back when the Improper Conducts occurred, there was an external President who was the representative, some Directors (more than one of whom were external Directors who were managers or officers in charge in the headquarters of the company from which they were dispatched). While the rest of the Directors were full-time directors, they were subordinates of A (the division head) in the executive division. Meetings of the Board of Directors were only held once a year or so. A was the President of NCCC. While Auditors of NCCC are Directors of NALC, they were A's subordinates in NCCC's executive department. Directors or the Board of Directors assume the obligation to oversee and supervise the execution of accounting operations under Company Law. Although the Directors or the Board of Directors of NALC assumed the obligation to oversee and supervise the execution of NCCC's business in terms of internal control of the Company, it is considered that they did not fulfill such duties. Although it cannot be said that it is not reasonable in terms of management to delegate the management and operation of NCCC to the locally hired officers and employees, it is considered that the Directors and the General Manager of NALC and the Auditor of NCCC who oversee and supervise NCCC's management should shift to a system where such oversight and supervision practically becomes possible. It is also considered that meetings of the Board of Directors should be held at least every three months, in which the condition of oversight and supervision NCCC should be reported and discussed.

#### **(2) Reorganization and securing of key personnel in NCCC**

In order to eliminate concentration of power, to strengthen mutual control functions, and to aim for the strengthening of payment management, reorganization should be considered. Efforts for



strengthening of a system toward early restructuring should be made, which should include dispatching of the management and officers of NCCC from the headquarters or NALC or recruiting them from outside entities.

(3) Consideration of the process of appointment of local manager

A established an organization under his control by assigning the group led by A to important posts while he held various managerial positions in NALC/NCCC. This is considered to be one of the causes of the improper conducts by the group led by A. Therefore, NCCC should establish fair processes such as a system where its management is appointed after going through formal meetings which should involve NALC as a parent company.

(4) Periodical transfer of personnel in charge of purchase and accounts

Since the Improper Conducts became possible due to the fact that both of these operations were controlled by the group led by A, it is considered that periodical transfer of the personnel engaged in these operations is necessary. It is likely that such transfer would have had a deterrent effect on the occurrence of improper acts such as this incident and led to early discovery.

(5) Pursuit of the effectiveness of the supervision and monitoring by the headquarters

The above-mentioned reorganization should be conducted under the responsibility and supervision of the control division of the headquarters. Depending on the situation, the headquarters should lead or assist the same, urge NALC/NCCC to promptly implement the restructuring and reorganization of the bodies and other countermeasures, and thereafter also periodically monitor the operation of the same at the Board of Directors, etc., of NALC/NCCC.

**4. Improvement of operating process and review of internal rules in NALC/NCCC**

In NCCC, it is considered that the operational risk in the selection of vendors, such as registration with the vendor master, is high. Thus, upon giving approval to the registration with the vendor master, operational methods independent of NCCC should be introduced. For example, the manager who conducts monitoring should give approval or control the registration.

In addition, together with the strengthening of the system in NCCC, the cooperation between NALC and NCCC should be strengthened by incorporating control through additional approval given by the management of NALC and the performance of monitoring functions. Furthermore, in the internal audit by the internal audit division of NGEA, it is necessary to ensure that new contract templates concerning prevention of bribery are used in the contracts with major vendors, and to reexamine whether the internal rules concerning operational process are appropriately maintained and operated in NCCC, as well as reexamine whether the actual situation of the work site deviates from

the internal rules. In addition, efforts such as training and education should be made so that internal rules are instilled at the work site and are complied with appropriately.

## **5. Intensification of operation of internal control system of the Group**

- (1) Clarification of supervisory responsibility of the control division and the responsibilities of the management division

The understanding that the control division is responsible for the management and control of subsidiaries including those overseas should be ensured, and a system which aims to improve the maintenance and operation of the internal control system should be established for the subsidiaries which the control division actively controls.

In addition, the management division should cooperate in the direct supervision by the control division and give consideration to a system which particularly detects information concerning the incidents of fraud, and such effect should be expressly indicated in the rules, etc.

- (2) Efforts for new internal audit activities (management audit and fraud audit)

After specifying the subject of the audit, consideration should be given to the commitment to audits which are focused on issues such as the appropriateness of the governance in management, and the existence of improper conducts.

- (3) Strengthening of audit

In order to improve the effectiveness of the internal audit by the Group, in addition to each company further improving its internal whistle-blowing system and discussing more effective methods of internal audit, the Group should also consider use of external accounting auditors after analyzing and selecting overseas group companies which potentially raise concern, while having an option to introduce external audit.

- (4) Strengthening of the measures for the issues that may occur

Together with the ensuring of reporting obligations by the control divisions of group companies, the current situation of the information sharing and cooperation within the Company including the management division should be reviewed, and the responsibility and authority of the control division and the management division which deals with unjust acts, etc., should be organized and clarified. In addition, it must be ensured that appropriate measures are promptly discussed and the operation of such measures should be monitored after evaluating the effects on the Group by seeking opinions from company auditors, accounting auditors and other external specialists depending on the situation.

(5) Strengthening of governance by the managing company of each area abroad

From the viewpoint of strengthening the governance of group companies, improvement of governance should be promoted in accordance with the conditions of each country and business by establishing the position of Regional Governance Officer who belongs to the management promotion group of the headquarters group which is a management division.

END