



February 6, 2020

To Whom It May Concern

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**Results of Investigation Report of Special Investigation Committee,  
Impact on the Company's Consolidated Financial Statements, and  
Measures to Prevent Recurrence**

As was announced in our notice dated December 13, 2019 entitled "Notice Concerning the Establishment of Special Investigation Committee", NS Solutions Corporation ("NS Solutions" or the "Company") became aware that it was unable to verify the actual existence of certain of the Company's recorded purchase and resale of goods transactions, after the National Tax Agency pointed out to the Company in mid-November 2019 that such transaction were questionable as to their actual existence. Due to this situation, the Company established a Special Investigation Committee consisting of one member of the Company's outside Audit & Supervisory Board and two independent outside experts with no interest in the Company (total of three members), and the Special Investigation Committee has since been investigating this matter (the "Relevant Transactions").

Today NS Solutions received the "Investigation Report" from the Special Investigation Committee. The Company makes the following announcements regarding its determination of the impact of this matter on its consolidated financial statements, and measures to prevent recurrence.

NS Solutions is taking this incident very seriously and once again expresses its deepest apologies to its shareholders and other stakeholders for causing great concern and inconvenience. The Company remains determined to do everything it can to prevent recurrence in order to restore the public's trust, and ask for your understanding.

## **1. Special Investigation Committee**

### **(1) Members of the Special Investigation Committee**

Chairman: Hidetaka Miyake, Attorney-at-Law, Anderson Mori & Tomotsune  
Member: Toraki Inoue, CPA, Accounting Advisory Co., Ltd.  
Member: Tetsuro Higuchi, CPA, Outside Audit & Supervisory Board Member,  
NS Solutions

### **(2) Purpose of the Investigation**

- To investigate and ascertain facts related to this matter, including the presence or absence of any other similar transactions.
- To verify the degree of financial impact of this matter on the consolidated financial statements of the Company.
- To identify the cause of this matter and to propose measures to prevent recurrence.
- To work on other matters deemed necessary by the Special Investigation Committee.

### **(3) Method of the Investigation**

During the investigation conducted from December 13, 2019 to February 5, 2020, the Special Investigation Committee closely reviewed related documents and materials, interviewed related parties, conducted digital forensic investigation, verified various matters with the Company's business partners, and conducted employee surveys, among other things.

## **2. Results of Investigation of Special Investigation Committee**

### **(1) Outline of the Special Investigation Committee Report**

As a result of the investigation by the Special Investigation Committee, it was found as follows:

“The Relevant Transactions were found to be part of a so-called ‘fictitious circular transaction scheme’, wherein NS Solutions was an intermediary participant in a multiple number of fictitious transactions with particular trading counterparties. Each of these transactions formed part of a series of commercial transactions in which circular transaction chains were repeatedly used, involving a multiple number of companies including NS Solutions as intermediaries without the existence of any end-user.

This fictitious circular transaction scheme was orchestrated by ‘X’, a particular sales representative of ‘A’, a business partner of NS Solutions, and NS Solutions did not participate in the fictitious circular transaction scheme in any systematic or deliberate manner, either as a company or as its Public Sector System Solutions Division. The individual employee of NS Solutions who handled the transactions was not aware that such transactions were fictitious or that they were

part of a circular transaction scheme. It has been found that this individual unknowingly participated in the fictitious circular transaction scheme orchestrated by X.”

### 3. Impact on the Company’s Consolidated Financial Statements

As a result of the investigation regarding the Relevant Transactions, in respect of transactions that were found to have been improperly accounted for between fiscal year 2014 and the first half of fiscal year 2019, the Company will revise the financial statements for these past fiscal years. The following table shows the impact from these revisions on the consolidated financial statements and the financial statements.

Fiscal Year	Number of Transactions	Sales (¥in billions)	COGS (¥in billions)	Profits (¥in billions)
2019	4	13.4	12.5	0.9
2018	4	10.6	9.9	0.6
2017	9	13.3	12.5	0.8
2016	7	4.6	4.3	0.2
2015	1	0.1	0.1	0.0
2014	4	0.6	0.6	0.0
Total	29	42.9	40.2	2.7

(Note 1) The above transactions were conducted between NS Solutions and six business partners.

(Note 2) In addition to the above, there were four unprocessed orders received during FY2019.

The investigation did not disclose any additional fictitious purchase and resale of goods transactions within the NS Solutions Group entities that are consolidated on the financial statements.

### 4. Measures to Prevent Recurrence

The Special Investigation Committee pointed out issues within the Company relating to its risk management system for purchase and resale of goods transactions, business operation processes, monitoring activities, the check and balance function assigned to the general control section, and the risk sensitivity of the sales department. The Company accepts the recommendations of the Special Investigation Committee regarding measures to prevent recurrence, and therefore, the Company’s Board of Directors decided today to implement the following recurrence prevention measures.

- (1) Strengthening risk management
  - Strengthen initiatives to realize self-disciplined and continuous risk management, by improving risk sensitivity
- (2) Review of business operation processes

- Strengthen risk management in purchase and resale of goods transactions
  - Stricter implementation of internal rules regarding transactions with business partners in the same industry
  - Improvement of business processes related to documentation of transaction
- (3) Monitoring and other improvement measures
- Strengthen monitoring of purchase and resale of goods transactions
  - Sophistication of internal audit processes such as fraud investigations
  - Revision of inventory management rules
- (4) Strengthen the check and balance functions within business units, and improve sales representatives' awareness of rules of business operations
- Strengthen the check and balance functions assigned to the control division of each business unit
  - Ensuring that all sales representatives throughout the Company are aware of the business processes that must be followed

NS Solutions has already begun to implement some of the above measures. With respect to the remaining ones, it will formulate the steps to be taken by the end of March 2020 and will implement them as they become ready, to further ensure prevention of recurrence.

## **5. Future Schedule**

### **(1) Corrections of financial statements for past fiscal years**

Along with the revisions to the Company's consolidated financial statements and financial statements for the past fiscal years, the Company will disclose today (February 6, 2020) the corrections to the financial results for the previous fiscal years from the fiscal year ending March 2015 to the second quarter of the fiscal year ending March 2020. In addition, the Company will make revisions to the annual securities reports, quarterly reports and internal control reports on February 14, 2020 for the relevant fiscal years.

### **(2) Announcement of third quarter financial results for the fiscal year ending March 2020**

The financial results for the third quarter of the fiscal year ending March 2020 is being announced today (February 6, 2020). The third quarter securities report for the 40th Fiscal Term (ending March 2020) will be issued on February 14, 2020.

Attached “Results of Investigation by Special Investigation Committee “

In this document, non-disclosure measures (including encoding, etc.) have been implemented for business partners and internal and external personal names.

February 6, 2020

NS Solutions Corporation

## **Results of Investigation by Special Investigation Committee**

NS Solutions (“NS Solutions” or the “Company”) has summarized this case based on the investigation report submitted by the Special Investigation Committee as follows.

### **Chapter 1 Outline of investigation**

#### **1. Background**

In the course of the tax investigation by the National Tax Agency in mid-November 2019, the Agency pointed out that some of the Company’s purchase and resale of goods transactions were circular transactions and were questionable as to their actual existence. In response, the Company established, by a resolution of the Board of Directors passed at a meeting held on December 13, 2019, a Special Investigation Committee (the “Investigation Committee”) consisting of two independent outside experts and one member of the Company's outside Audit & Supervisory Board (timely disclosure information entitled “Notice Concerning the Establishment of Special Investigation Committee” published on the same day).

#### **2. The objective and scope of investigation**

- ① To investigate and ascertain facts related to this matter (including existence of similar transactions)
- ② To verify the degree of financial impact of this matter on the consolidated financial statements of the Company.
- ③ To identify the cause of this matter and to propose countermeasures for preventing recurrence.
- ④ To work on other matters the Investigation Committee deems necessary

In relation to ① above, in consideration of the matters pointed out by the National Tax Agency, the Investigation Committee extracted certain transactions, more specifically, 69 transactions executed by the Public Sector System Solutions Division of the Company (“Public Sector Division”) that were questionable as to their existence, including transactions of a value of 10 million JPY or more which had already been accepted, involving ‘A Co.’, ‘B Co.’, ‘C Co.’, ‘D Co.’, ‘E Co.’ and ‘F Co.’ either as a purchaser or a supplier (these 6 companies are collectively referred to as “Particular Trading Parties”), and investigated these transactions (“Investigation regarding Transactions”) as to their existence.

Transactions that were not subject to the Investigation regarding Transactions were covered by the investigation conducted to examine whether there were any similar cases (“Investigation of Other Transactions”).

### 3. Structure and other details of investigation

#### 1 Composition of the Special Investigation Committee

Chairman	Hidetaka Miyake, Attorney-at-law, Anderson Mori & Tomotsune
Member	Toraki Inoue, CPA, Accounting Advisory Co., Ltd.
Member	Tetsuro Higuchi, CPA, Outside Audit & Supervisory Board Member, NS Solutions

#### 2 Supporting members of investigation

Organization	Outside experts
Accounting Advisory Co., Ltd.	Hiroyuki Ikeuchi, CPA Hidetaka Asami, CPA
Anderson Mori & Tomotsune	Hiroyuki Ito, Attorney-at-law Masahiro Takada, Attorney-at-law Ryohei Sakai, Attorney-at-law

## Chapter 2 Outline of investigation procedure

### 1. Period of investigation

The Investigation Committee was established on December 13, 2019, and conducted investigation and reviews based on the investigation results until February 5, 2020.

### 2. Period covered by the investigation

As figures of financial results for the period ending March 2014 are stated as comparative information in the Annual Securities Report for the period ending March 2015, which was the oldest statutory required disclosure documents of the Company available for public inspection at the time of investigation by the Investigation Committee, the Investigation Committee set the period covered by the Investigation regarding Transactions to the period from April 2013 to October 2019.

As to the Investigation of Other Transactions by which the actual existence of individual transactions would be examined, in order to focus on the transactions that were suspected to be circular transactions during the fiscal year ending March 2020 when this case was in the progressive state and the previous fiscal year ending March 2019, the basic period covered by this investigation was set to the period from April 2018 to October 2019.

### 3. Outline of investigation procedure

In summary, the Investigation Committee carried out the following procedure, and held meetings at which all members of the Investigation Committee were present ten times in total, and examined issues and investigation results.

## **1 Verification and thorough investigation of relevant materials**

Main relevant materials verified and thoroughly investigated by the Investigation Committee are as follows:

- ① Articles of Incorporation and other internal rules and regulations of the Company;
- ② A set of relevant materials prepared and/or collected by the Internal Investigation Committee and Internal Task Force (“Internal TF”) of the Company;
- ③ Organization chart of the Company and Table of Changes to the Management Staff of the Public Sector Division;
- ④ Loss and profit in sales data and manufacturing cost information and other accounting data of the Company;
- ⑤ Materials related to approval and vouchers and other documented evidence of transactions that were questionable as to their existence and related documents;
- ⑥ Minutes of meetings of the Board of Directors, Management Meetings and Board of Auditors of the Company, and internal audit plans and reports from April 2016 to October 2019; and
- ⑦ Audit plans and audit reports for and after the fiscal year ending in March 2017 by KPMG AZSA LLC (“AZSA”).

## **2 Interviews to officers and employees of the Company**

The Investigation Committee conducted face-to-face or TV-conference interviews with officers and employees of the Company (including former officers and employees) and other relevant persons during the period of investigation, and verified facts related to the transactions that were questionable as to their existence (the number of persons interviewed: 21; total number of interviews: 26 times).

## **3 Verification and thorough investigation of email data and other information**

The Investigation Committee verified and took over the digital forensic investigation conducted by the Internal Investigation Committee of the Company, and conducted additional digital forensic investigation by expanding data to be investigated and reviewed (reviewed 40,131 data items).

In addition to the digital forensic investigation which reviewed e-mail data extracted from stored data, the Investigation Committee also carried out verification and thorough investigation of e-mail and materials that were deemed relevant to this case and voluntarily submitted by certain individuals interviewed.

## **4 Third-party investigation of trading parties**

### **(1) Verification of commercial distribution with Particular Trading Parties and other actions taken**

The Company communicated with Particular Trading Parties (multiple companies) which started investigation into a series of transactions which were suspected to be circular transactions at around the same time as the Internal Investigation Committee started its investigation, to jointly verify relevant facts, and examined the materials and information obtained through the communication. At the same time, the Investigation Committee conducted interviews, made questions and inquiries in writing, conducted third-party investigations, and carried out other activities toward Particular Trading Parties, in collaboration with Internal TF.

**(2) Inquiries to trading parties concerning transactions**

The Investigation Committee sent an inquiry letter to verify the status of commercial distribution of certain transactions and actual items transacted to a total of 30 purchasers and suppliers which were deemed necessary, in order to verify the actual existence of transactions, and conducted a third-party investigation to obtain answers to the questions and copies of evidential documents, as part of Investigation regarding Transactions and Investigation of Other Transactions. Replies to the inquiry letter sent out were all collected, and follow-up verification was conducted, as needed.

**(3) Interviews to officers and employees of Particular Trading Parties responsible for sales, and other actions taken**

The Investigation Committee, after obtaining their consent to collaborate in the investigation, interviewed and took other actions in relation to a number of sales representatives of Particular Trading Parties (multiple companies) or their superiors to verify relevant facts.

**5 Questionnaires to employees**

The Investigation Committee sent out questionnaires asking questions such as involvement in fictitious transactions without actual existence and commercial distribution in which provision of goods and services was circulated among several trading parties, and received responses, to and from approximately 570 employees of the Company group companies. In addition, follow-up investigation was conducted, as needed.

**6 Review of issues regarding business operation processes**

The Investigation Committee instructed the Internal TF to examine issues regarding business operation processes of the Company and to consider actions to be taken, and in January 2020, received a report on the result of the examination, which was utilized by the Investigation Committee to analyze causes of the occurrence of this case and to consider recommendations regarding measures to prevent recurrence.

**7 Exchange of information with audit firm**

The Investigation Committee had a total of 6 meetings with the auditing team of AZSA which audited the Company's financial statements for the period covered by the investigation, to share the status of progress of investigation by the Investigation Committee and to exchange other information, in consideration of the possibility that the Company would have to correct financial results for previous fiscal years based on the results of investigation by the Investigation Committee.

In January 2020, the Investigation Committee interviewed the auditing team of AZSA including their partners to verify the status of audit of financial statements for the period covered by the investigation.

**8 Inspection of bankbooks of certain sales representatives**

The Investigation Committee inspected bankbooks of the bank accounts held by the persons who were sales representatives involved in purchase and resale of goods transactions which were suspected to be circular transactions, such as the bank account to which salary was deposited, to verify the status of deposit transactions.



### Chapter 3 Outline of results of Investigation regarding Transactions

#### 1. Outline of facts recognized by the Investigation Committee

As a result of the Investigation regarding Transactions, the transactions investigated were found to be part of a so-called ‘fictitious circular transaction scheme’, wherein NS Solutions was an intermediary participant in a multiple number of fictitious transactions with Particular Trading Parties. Each of these transactions formed part of a series of commercial distribution in which circular transaction chains were repeatedly used, involving a multiple number of companies including NS Solutions as intermediaries without the existence of any end-user.

This fictitious circular transaction scheme was orchestrated by ‘X’, a particular sales representative of ‘A’, and NS Solutions did not participate in the fictitious circular transaction scheme in any systematic or deliberate manner, either as a company or as its Public Sector Division. In addition, the sales representative of NS Solutions was not aware that such transactions were fictitious, without actual existence, or that they were part of a circular transaction scheme. It has been found that this individual unknowingly participated in the fictitious circular transaction scheme orchestrated by X.

#### 2. Fictitious circular transaction scheme recognized by the Investigation regarding Transactions

The Investigation Committee extracted 69 transactions which were questionable as to their existence including transactions involving Particular Trading Parties, and examined each of these transactions as to their actual existence, in particular as to the reasonableness of commercial distribution (existence of end-users, etc.) and involvement of the Company in the transactions (whether or not the Company provided installation, maintenance and other associated services).

In addition, third-party investigation was conducted to investigate Particular Trading Parties and some of the commercial distribution which the Company was not aware of was examined. As a result, the following facts were confirmed: 26 transactions listed in the table below and 4 other transactions, a total of 30 transactions for orders already accepted were all processed by the Public Sector Division as purchase and resale of goods transactions (some of the transactions were fixed term maintenance services), but no goods or services for which these transactions were executed existed; and each transaction formed part of a series of commercial distribution in which circular transaction chains were repeatedly used without actual end users.

(Unit: Million JPY)

Transaction No.	Order date	Sale recording date	Customer (Purchaser) (Party to contract)	Final customer name	Project name	Order amount receivable (exclusive of taxes)	Ordered party (Supplier)	Order amount payable (exclusive of taxes)
1	2014/6	2014/12			A set of information-related hardware and software	619		592
2	2015/6	2015/10			A set of information system devices, etc.	123 (122) <sup>1</sup>		115 (113)
3	2016/5	2016/7			A set of software license	575		545
4	2016/9	2016/9			A set of server software for _____	83		79
5	2016/6	2016/11			A set of document system devices for _____	1,868		1,605
								113

<sup>1</sup>. For this transaction, a portion of sales was not recorded, as a fixed term maintenance service is still continuing.

Transaction No.	Order date	Sale recording date	Customer (Purchaser) (Party to contract)	Final customer name	Project name	Order amount receivable (exclusive of taxes)	Ordered party (Supplier)	Order amount payable (exclusive of taxes)
6	2016/10	2016/12			A set of various software for _____	259		82
7	2016/8	2017/3			A set of BI-related software for _____	825		670
								95
								15
8	2017/3	2017/3			A set of software license for _____	532		505
9	2016/12	2017/3			A set of information network-related software	479		120
								335
10	2016/9	2017/4			A set of database software for _____	319		303
11	2017/4	2017/5			A set of security software license for _____	2,343		80
								2,145
12	2016/11	2017/6			A set of various software for _____	2,445		2,320
13	2016/10	2017/6			A set of operation-related software for _____	875		830
14	2017/9	2017/9			A set of server-related software for _____	298		80
								202
15	2017/9	2017/10			A set of licenses for server OS and others	152		15
								130
16	2018/2	2018/3			A set of server-related devices for _____	274		173
								85
17	2018/2	2018/3			A set of various software	2,345		2,085
								120
18	2017/10	2018/3			A set of various software for _____	4,300		2,856
								1,020
								80
19	2017/10	2018/6			A set of security-related software for _____	3,395		3,095
								96
20	2018/4	2018/9			A set of server and other devices for _____	3,375		1,714
								1,370
								54
21	2018/7	2018/10			A set of information system devices for _____	365		140
								120
								80
22	2018/9	2018/12			A set of products for _____	3,446		3,273
23	2018/11	2019/4			A set of information system devices for _____	4,721		2,817
								1,212
								120
								120
								120

Transaction No.	Order date	Sale recording date	Customer (Purchaser) (Party to contract)	Final customer name	Project name	Order amount receivable (exclusive of taxes)	Ordered party (Supplier)	Order amount payable (exclusive of taxes)
24	2019/2	2019/5			A set of various products	4,525		1,830
								1,547
								681
								70
								80
25	2018/9	2019/5			A set of server devices for _____	4,050		1,898
								1,908
26	2019/4	2019/6			A set of software licenses for _____	191		70
								45
								65
Total					Order amount receivable (Amount of sales record)	42,788 (42,786)	Order amount payable (Amount of cost of sales record)	40,091 (40,090)

In addition to those listed in the above table, there are 4 unprocessed projects which were ordered and accepted in FY2019.

### 3. Inappropriate transactions other than fictitious circular transactions

As a result of the Investigation regarding Transactions, the following transactions could not be recognized as having linked to the fictitious circular transaction scheme and no evidence was found to deny their existence. However, reasonableness of these transactions could not be verified from the documented evidence maintained within the Company, and their specifics and reasonableness could also not be verified by interviews with then-relevant persons.

As there were no sufficient grounds to prove their reasonableness, it is difficult to recognize that these transactions were normal sales transactions of the Company, as in the case of fictitious circular transactions, and thus they were considered to be inappropriate transactions.

(Unit: Million JPY)

Transaction No.	Order date	Sale recording date	Customer (Purchaser) (Party to contract)	Final customer name	Project name	Order amount receivable (exclusive of taxes)	Ordered party (Supplier)	Order amount payable (exclusive of taxes)
1	2014/4	2014/4			A set of refurbishing of additional PCs for information infrastructure system	30		27
2	2014/4	2014/4			Additional goods for information infrastructure system, etc. ③	40		35
3	2014/6	2014/12			A set of WEB-related hardware and software	108		103
				<b>Total</b>	<b>Order amount receivable (Amount of sales record)</b>	<b>179 (179)</b>	<b>Order amount payable (Amount of cost of sales record)</b>	<b>165 (165)</b>

## Chapter 4 Outline of results of Investigation of Other Transactions

### 1. Outline of investigation procedure of Investigation of Other Transactions

#### 1 Investigation of individual transactions

As part of the investigation of individual transactions, the following transactions were investigated to examine whether there were similar cases, more specifically, whether similar fictitious circular transactions without actual existence existed, other than this case.

[Period covered by the investigation]

The investigation was conducted based on the following policy: the initial period of investigation during which analysis and investigation of particular transactions would be conducted was set from April 2018 to October 2019, based on the characteristics of fictitious circular transaction schemes, which is generally that the purpose of the scheme can be achieved by executing a series of transactions continuously without interruption, and if any issue was found as a result of such investigation, then investigation would be expanded for a further period necessary to correct financial statements for previous fiscal years.

However, the period of investigation for transactions carried out by the Public Sector Division that were not covered by the Investigation regarding Transactions was set from April 2013 to October 2019, as is the case in the Investigation regarding Transactions.

[Transactions investigated]

Investigation was conducted for direct shipping (= not through the Company's warehouse) sales transactions which did not involve development, manufacture or other associated work by the consolidated group companies, more specifically, transactions that are ① direct shipping sales of goods; and ② subcontracting of entire development. However, covered transactions were limited to those of 50 million JPY in value per transaction.

The table below shows applicable transactions for each consolidated group company.

	Name	Main operations	Direct shipping sales of goods	Development outsourcing
Parent company (NS Solutions)	NS Solutions Corporation	Business solutions and service solutions	○	○
Consolidated subsidiary	Hokkaido NS Solutions Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	Tohoku NS Solutions Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions Tokyo Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions Chubu Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions Kansai Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions Kyushu Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NSSLC Service Corporation	Operation and maintenance service	-	-

	Name	Main operations	Direct shipping sales of goods	Development outsourcing
Consolidated subsidiary	Network Value Components Ltd.	Sale and maintenance of network and security-related products	○	○
Consolidated subsidiary	NS Financial Management Consulting Inc.	Consultation for financial institutions, etc.	-	○
Consolidated subsidiary	Financial Engineering Group, Inc.	Consultation for financial institutions, etc.	-	○
Consolidated subsidiary	NCI Systems Integration, Inc.	System solutions, etc.	-	○
Consolidated subsidiary	Nittetsu Hitachi Systems Engineering, Inc.	System solutions, sales of computer-related devices, etc.	○	○
Consolidated subsidiary	NS Solutions (Shanghai) Co., Ltd.	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions Asia Pacific Pte. Ltd.	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	Thai NS Solutions Co., Ltd.	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	PT. NSSOL SYSTEMS INDONESIA	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	PT. SAKURA SYSTEM SOLUTIONS	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions USA Corporation	Software development, operation and maintenance of information system	-	○
Consolidated subsidiary	NS Solutions IT Consulting Europe Ltd.	Software development, operation and maintenance of information system	-	○

## 2 Overall investigation

As part of the overall investigation, questionnaire investigation was conducted to sales representatives and employees of the Public Sector Division.

### 2. Outline of findings

Through the Investigation of Other Transactions, no fictitious circular transactions or similar transactions suspected to have been executed by consolidated group companies were detected.

## Chapter 5 Amount of financial impact on the consolidated financial statements

The Investigation Committee's views are as follows.

The current fictitious circular transactions are fictitious transactions that look like direct shipping transactions but are actually fictitious transactions with no substance and which do not involve any movement of products at all. In other words, the purchase price paid to the supplier by the Company thereafter circulates among Particular Trading Parties, and the funds collected by the Company as sales proceeds from different transactions are actually funds of the Company and Particular Trading Parties circulated back into the Company.

Therefore, for accounting purposes, sales, cost of sales, and profit which is the difference between them, as well as accounts receivable, inventory, accounts payable, etc. related to the fictitious circular transactions in question need to be canceled as they lack substance. Sales and cost of sales, balance of accounts receivable, balance of inventory, and balance of accounts payable which need to be canceled for each fiscal year in relation to the transactions that have been recognized as fictitious circular transactions in “Chapter 3, 2. Fictitious circular transactions recognized by the Investigation regarding Transactions” and inappropriate transactions in “Chapter 3, 3. Inappropriate transactions other than fictitious circular transactions” are as follows.

Unit: 1000 JPY (exclusive of taxes, rounded down to the nearest 1,000 JPY)

	Sales	Cost of Sales	Difference (Profit)
FY ending March 2015	643,980	608,776	35,203
FY ending March 2016	154,460	146,338	9,121
FY ending March 2017	4,658,760	4,364,078	294,681
FY ending March 2018	13,390,506	12,562,012	828,494
FY ending March 2019	10,620,727	9,981,350	639,377
FY ending March 2020 Second quarter (Total)	13,497,880	12,595,038	902,842
Total	42,966,314	40,256,594	2,709,720

Unit: 1000 JPY (rounded down to the nearest 1,000 JPY)

	Accounts receivable (inclusive of taxes)	Inventory (Exclusive of taxes)	Accounts payable (inclusive of taxes)
FY ending March 2015	0	149,593	0
FY ending March 2016	0	119,254	0
FY ending March 2017	1,982,880	82,976	923,400
FY ending March 2018	7,473,441	143,598	1,101,600
FY ending March 2019	0	5,461,210	2,062,800
FY ending March 2020 Second quarter (Total)	0	1,080	0

As explained earlier, since the funds paid by the Company appear to have gone to the Particular Trading Parties, for accounting purposes, it is appropriate, based on facts, to recognize the settlement difference between the funds paid and funds collected by the Company as claims and obligations against or to the Particular Trading Parties. Trends in amounts paid and amounts collected by the Company, and difference of funds settled during each fiscal year in relation to the fictitious circular transactions in question and inappropriate transactions listed in “Chapter 3, 3. Inappropriate transactions other than fictitious circular transactions” are as follows. As the difference between funds settled are not claims and obligations arising from normal commercial transactions, this could be recorded as temporary payment, temporary receipt or other appropriate account.

Unit: 1000 JPY (inclusive of taxes, rounded down to the nearest 1,000 JPY)

	Temporary Payment	Temporary Receipt
FY ending March 2015	0	43,351
FY ending March 2016	0	52,531
FY ending March 2017	690,076	0
FY ending March 2018	5,213,700	0
FY ending March 2019	1,872,117	0
FY ending March 2020	0	2,926,627
Second quarter (Total)		

Funds for 4 other transactions for orders already accepted that are listed in Chapter 3, 2. have not been settled, as goods for these transactions had not been delivered or payment deadline had not arrived at the time of discovery of this irregular trading.

## **Chapter 6 Analysis of causes of occurrence of this case**

This case involves continuous fictitious circular transactions orchestrated by ‘X’ of ‘A’ which was discovered through the investigation by the National Tax Agency, and the Company also unknowingly participated in the fictitious circular transaction scheme orchestrated by ‘X’ of ‘A’ with which the Company had been doing business.

Main causes for the Company not being able to detect this case until pointed out by the National Tax Agency through their investigation are as follows.

- It was explained that those projects were for the customers of highly confidential nature;
- These transactions had been with trading parties who had a history of doing business with the Company, and no issues concerning these trading parties had been found at any periodical credit review;
- There had been proper vouchers and other documented evidence required by internal rules and internal systems;
- Gross profit had been maintained to a certain level; and
- Settlement of funds and payments had been paid properly.

Through the analysis of causes of this case based on recognized facts, the Investigation Committee further pointed out certain issues in various areas including: risk management system of the Company for sales of goods transactions; business operation processes to verify actual goods delivered and to prepare invoices and other transaction documents; internal audit and monitoring activities to verify the actual existence of transactions; education and instruction on internal rules concerning Prohibited Commercial Distribution<sup>2</sup> (rules concerning Prohibited Commercial Distribution”); internal check and balance functions within the Public Sector Division; and risk sensitivity.

## **Chapter 7 Recommendations regarding measures to prevent recurrence**

Recommendations presented by the Investigation Committee to the Company as to measures to prevent recurrence are as follows.

### **1. Strengthening risk management**

Improving business operation processes and monitoring activities will be effective as measures to prevent recurrence of fictitious circular transactions. However, as more fundamental preventive measures, it is important for the Company to create a self-disciplined system by which the Company can accurately detect the risk of large scale fraudulent activities and misconduct and take appropriate actions to prevent or detect at an early stage any such incidents by assessing such risk.

### **2. Review of business operation processes**

#### **1 Review of risk management in the sale of goods transactions**

From the perspective of appropriately managing risks associated with the sale of goods transactions, review mechanism of Project Policy Meeting, primarily for projects for which SE (system engineers) are involved, should be reviewed and a system by which a review on the decision on acceptance or refusal of orders for the sale of goods transactions led by the sales

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<sup>2</sup> Translator’s note: “Prohibited Commercial Distribution” refers to commercial distribution wherein NS Solution would be a party to the transaction contract without adding any value, with the goods physically being transferred from the party which sells them to NS Solutions directly to the party who purchases them from NS Solutions.



## Attachment

divisions can be accurately conducted should be established, for the sale of goods transactions that are not commercial distribution of goods.

**2 More stringent operation of rules against prohibited commercial distribution**

Rules against prohibited commercial distribution and their purposes and intent should be informed to, and understood by, all relevant persons through education and training.

**3 Improvement of business operation processes (such as management of seals) related to the preparation of transaction documents**

**3. Monitoring and other improvement measures**

**1 Review of investigation of prohibited commercial distribution**

Standards for identifying sales of goods transactions with high risk of misconduct should be reviewed and effective monitoring activities should be implemented.

**2 Sophistication of internal audits**

To ensure prevention of recurrence, it is worth examining the way to carry out monitoring through internal audits, using more sophisticated procedures.

**3 Revision of inventory management rules**

It is worth considering revising the inventory management rules appropriate to the Company's actual situation.

**4. Strengthen the check and balance functions within business units, and improve sales representatives' awareness of rules of business operations, by the Public Sector Division**

**1 Clarification of functions and roles of control division of business units**

It is worth considering clarifying functions of control division of business units and their expected roles in various situations.

**2 Documentation and clarification of business operation process rules**

Business operation process rules to be complied with by sales representatives should be documented and clarified in a manner that can be easily understood, and common understanding and awareness of these rules should be fostered.

**3 Ensuring that all sales representatives are properly educated and trained.**

END