FOR IMMEDIATE RELEASE

Notice Regarding the Receipt and Publication of the Special Investigation Committee's Investigation Report

Tokyo, July 25, 2019 - Hitachi Capital Corporation (TSE:8586, President & CEO: Seiji Kawabe, "the Company") has established a Special Investigation Committee and proceeded with conducting investigations concerning possible inappropriate factoring deals of Hitachi Capital Factoring (China), Co., Ltd., a subsidiary of the Company, to ascertain the whole picture and the root cause of the matter as stated in the "Notice Regarding Establishment of the Special Investigation Committee", on June 17, 2019.
The Company hereby announces that today it received the Investigation Report ("the Report") from the Special Investigation Committee.
Accordingly, we have attached the "Investigation Report (Disclosure version)," which is the Report containing partial redactions (including applying codifications) in the interests of factors such as privacy, protection of confidential information, and possible future legal procedures.
The Company will continue its efforts to recover damages and resolve matters with respect to this issue.

- Description -

1. Investigation Results of the Special Investigation Committee
   Please refer to the attached "Investigation Report (Disclosure version)."

2. Measures to prevent recurrence
   Based on the investigation results described in the Report and the recommendations by the Special Investigation Committee, the Company will drastically review its large-scale factoring businesses and other similar businesses in order to ensure that the Company retains good and operating receivables, and also the Company will further strive to take thoroughgoing measures to prevent recurrence, such as strengthening risk management.
   The recommendations received from the Special Investigation Committee regarding measures to prevent recurrence are set forth in the attached "Investigation Report (Disclosure version)."

3. Actions taken against officers etc.
   The Company will announce actions taken against officers of the Company in relation to this matter as soon as a decision is made.

4. Impact on Consolidated Financial Statements
   The impact on the consolidated financial statements for the year ended March 31, 2019 confirmed by the Special Investigation Committee's investigation is set forth in the attached "Investigation Report (Disclosure version)." Based on the Report, the Company has decided to record a provision of allowance of approximately 20.6 billion yen in the year ended March 31, 2019.

5. Shareholder returns
   The Company is considering issuing special dividends, and will make an announcement as soon as it is confirmed.

The Company expresses its sincerest apologies to its shareholders, investors and all other stakeholders for any concern or inconvenience caused.

# # #

To Hitachi Capital Corporation

July 25, 2019

Investigation Report
(Disclosure version[1])

Special Investigation Committee

Koichiro Hiraiwa, Chairman

Takuei Maruyama, Member

Kaku Hirao, Member

This report summarizes the results of the investigation and analysis conducted as appropriately as possible under the provided time and conditions. The conclusions in this report may change if new facts are identified in the investigation by the Japanese and Chinese investigation authorities. It should also be noted that this report does not predict or guarantee the decisions of the court, investigation authority and other relevant authorities in Japan and China.

[1] In this disclosure version, information such as name of individual and company, date, and amount is presented as encoded or not disclosed from the viewpoint of privacy protection, confidentiality obligation, and prevention of loss arising from leakage of confidential information. In addition, in light of the fact that recovery of damages and other measures are to be taken to resolve incidents in the future, revisions have been made from the original text as necessary.

Chapter 1 Overview of investigation

Section 1 Background of investigation

On March 29, 2019, it was reported at the board of directors meeting of Hitachi Capital Corporation ("**HC**") that Hitachi Capital Factoring (China) Co., Ltd. ("**HCF**"), a subsidiary of HC (percent ownership of voting rights: 100%), is suspected of being involved in fictitious transactions by its suppliers.

HC established an internal investigation committee ("**Internal Investigation Committee**") on April 22, 2019, to confirm receivables held by HCF. It found that there were doubts about existence of receivables with respect to four cases: A, B, C and D (collectively, "**four cases**")[2]. The cause of such doubts is alleged fraud or fraudulent activities by a third party (the possibility of fraud or fraudulent activities by a third party, revealed by the investigation conducted by the Internal Investigation Committee ("**Initial Investigation**"), is collectively referred to as "**Fraud**"). Further, it was confirmed during the course of the Initial Investigation that some of the four cases had been introduced to HCF by Hitachi Capital Leasing (China) Co., Ltd. ("**HCL**"), a subsidiary of HC (percent ownership of voting rights: 90%).

Responding to these facts, and based on a recommendation from the Audit Committee to conduct more objective and reliable investigation, HC established a special investigation committee ("**Committee**") on June 17, 2019. HC requested that the Committee investigate the existence of receivables of HCF and HCL, as well as the involvement of officers and employees of HCF and HCL with the Fraud in order to understand the impact of the Fraud on the financial results of HC[3] ("**Investigation**").

Section 2 Purpose of the Investigation

The purpose of the Investigation is to investigate and consider the following matters to the extent necessary to understand the impact on the financial results of HC.

- Existence of receivables of HCF and HCL
- Involvement of officers and employees of HCF and HCL with the Fraud

Given the results of the investigation for the above, the Committee also considered and analyzed the causes and background of the Fraud, and the necessary measures to help

---

[2] For an overview of the four cases, see Chapter 3, Section 1, 1.

[3] The recovery of damages and resolution in relation to the four cases is being undertaken concurrently with the Initial Investigation and the Investigation. It is expected that these efforts will also continue after the Investigation.

prevent HC from the recurrence of such a fraud.

Section 3 Details and methods of investigation

1 Organization of the Investigation

The Committee consists of the following members:

Chairman	Koichiro Hiraiwa (Independent outside director of HC)
Member	Takuei Maruyama (Partner of PwC Business Assurance LLC, CPA)
Member	Kaku Hirao (Partner of Nishimura & Asahi, Lawyer)

Takuei Maruyama and Kaku Hirao have no interests in HCF, HCL and HC.

Additionally, the Committee appointed Mamoru Honda, CPA, and Mihoko Nasu, CPA, and other 47 members from PwC Business Assurance LLC (including member firms of PwC global network), and Takashi Nomura, Lawyer, Yusuke Suzuki, Lawyer and other six members of Nishimura & Asahi, as assistants of the investigation.

In order to assist with HC's financial closing of their fiscal year ended March 2019 within the limited investigation period, the Committee established an investigation administrative office ("**Investigation Administrative Office**") within HC, which includes members of the Internal Investigation Committee, to help conduct the investigation.

As a result, the Committee did not wholly rely on the "Third-party Committee Guidelines for Corporate Scandals" as defined by the Japan Federation of Bar Associations. It established a system to conduct an objective and reliable investigation through the development of investigation procedures and reporting that is based on the principles of the Guidelines.

2 Period of the Investigation

The Committee conducted the investigation and held a committee meeting six times during the period between June 17, 2019 and July 23, 2019.

3 Methods of the Investigation

(1) Takeover of the Initial Investigation

When commencing the Investigation, the Committee was briefed on the procedures conducted in the Initial Investigation and the status of the investigation from the Internal Investigation Committee, and obtained the documentation collected.

The documents the Committee received from the Initial Investigation included:

- Investigation report prepared by the Internal Investigation Committee
- Master factoring agreement with respect to the four cases, and various supporting documents, including the debtor consent form[4] for transfer of individual receivables
- Refactoring agreement with respect to the B and D cases
- Law firm's legal opinion regarding the existence of receivables
- Minutes of interviews with relevant people
- Results and supporting details from the verification of the existence of receivables other than the four cases

The Committee also considered the methodology and results of the Initial Investigation relating to:

- E-mail review
- Interviews of officers and employees of HCF and HCL
- Inspection of relevant documents (credit application form, sales agreement, Fapiao(発票), receipt, confirmation evidence of People's Bank of China ("**PBOC**"), notice of transfer of trade receivables)
- Questionnaire surveys to HCF employees
- Background checks of creditors and debtors
- Confirmation of registration of factoring agreement with PBOC

(2) Verification of existence of receivables of HCF

In addition to (1) above, the Committee undertook the following steps in the investigation to verify the existence of receivables related to the four cases, where there were doubts about the existence of receivables in the Initial Investigation:

- Interviews and inspection of relevant rules and forms to understand the operations and internal controls related to the conclusion of the factoring agreement of HCF
- Inspection of master factoring agreement with respect to the four cases and various supporting documents, including notice of transfer of trade receivables for transfer of individual receivable
- Inspection of refactoring agreement

4 In HCF, the documents are referred as "notice of transfer of trade receivables" or "Confirmation of transfer of trade receivables."

Also, in particular, the Committee performed the following procedures on the other factoring transactions where it was concluded that there were no doubts on the existence of receivables. This was performed in order to evaluate the appropriateness of the methods and results of the investigation:

- Reviewed the Initial Investigation's results of inspection of relevant documents, including credit application form, sales agreement, Fapiao(発票), confirmation evidence of PBOC, and notice of transfer of trade receivables for certain factoring transactions
- Review of the Initial Investigation's results of confirmation of balances
- Review of the Initial Investigation's results of creditor and debtor visits

(3) Verification of existence of receivables of HCL

i Receivables investigated

The Committee selected certain receivables, which it acknowledged as at a relatively high risk, from those of HCL as at the end of March 2019[5], and verified their existence.
The 32 receivables verified are listed as below:

(in million JPY)[6]

No.	Agreement No.	Nature of agreement	Responsible department	Receivable balance (At the end of March 2019)
1	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
2	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
3	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed

5 HCL's lease receivables include not only lease receivables arising from ordinary lease transactions but also receivables arising from leaseback transactions, transfer of lease receivables and transfer of leased assets. For an overview of each transaction, refer to Chapter 2, Section 1 and Section 2.

6 Unless otherwise stated, amounts in this report have been translated into Japanese yen at the rate of 1 yuan = 16.33 JPY.

No.	Agreement No.	Nature of agreement	Responsible department	Receivable balance (At the end of March 2019)
4	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
5	Not disclosed	Leaseback	Not disclosed	Not disclosed
6	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
7	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
8	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
9	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
10	Not disclosed	Leaseback	Not disclosed	Not disclosed
11	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
12	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
13	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
14	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
15	Not disclosed	Leaseback	Not disclosed	Not disclosed
16	Not disclosed	Transfer of leased assets	Not disclosed	Not disclosed
17	Not disclosed	Transfer of leased assets	Not disclosed	Not disclosed

No.	Agreement No.	Nature of agreement	Responsible department	Receivable balance (At the end of March 2019)
18	Not disclosed	Transfer of leased assets	Not disclosed	Not disclosed
19	Not disclosed	Transfer of leased assets	Not disclosed	Not disclosed
20	Not disclosed	Leaseback	Not disclosed	Not disclosed
21	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
22	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
23	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
24	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
25	Not disclosed	Leaseback	Not disclosed	Not disclosed
26	Not disclosed	Transfer of leased assets	Not disclosed	Not disclosed
27	Not disclosed	Leaseback	Not disclosed	Not disclosed
28	Not disclosed	Leaseback	Not disclosed	Not disclosed
29	Not disclosed	Leaseback	Not disclosed	Not disclosed
30	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
31	Not disclosed	Transfer of lease receivables	Not disclosed	Not disclosed
32	Not disclosed	Transfer of lease	Not disclosed	Not disclosed

No.	Agreement No.	Nature of agreement	Responsible department	Receivable balance (At the end of March 2019)
		receivables		
			Total	55,624

To support the verification, the Committee visited a leasing company, a transferor of the receivable, in the case of lease receivables transfer agreement (with recourse), and a lessee in the lease agreement (user) in the case of leased asset transfer agreement (without recourse) and leaseback agreement. Also, the Committee inspected various supporting documents related to transactions, and obtained confirmations of receivables.

ii Management of receivables

In order to understand HCL's internal controls over lease receivables management, the Committee obtained an understanding of operation by inspecting HCL's rules, interviewing responsible persons, and inspecting relevant supporting documents.

(4) Gathering related documents

In addition to the documents described in (1) to (3) above, the Committee also gathered, inspected and considered the company regulations/manuals of HCF, HCL and HC, accounting records and documents related to receivables, as well as other relevant documentation and evidence as listed below:

Operations at HCF

Credit underwriting operating rules
(HCF) Flow of credit risk management
Factoring guidelines
Operating rules for Account receivable and debt collection
Operating rules for Credit monitoring
Internal application items (Certificate authorization authority, Administrative procedure approval authority, Signing authority)
Operating rules for Payment via bank transfer

Operation manual
Operation flow

Operations at HCL

Accounting Manual of Hitachi Capital Leasing (China) Co., Ltd.
Credit underwriting manual
Credit risk management rules of Hitachi Capital Leasing (China) Co., Ltd.
Credit underwriting guidelines
Credit underwriting guidelines for public sector
Operating rules for Credit lines
Notice regarding decision authority for amendment of contract terms and procedure for such applications
Procedure manual for Change in debt ownership (Confirmation agreement of debt assignment)
Internal application items (Certificate authorization authority, Administrative procedure approval authority, Signing authority)

Subsidiary management at HC

Group Companies Management Policy
Global audit rules
Internal audit rules
Internal audit operating rules
Credit Risk Policy
Credit Risk Management Regulations
Operating rules for Credit Underwriting at Group companies located overseas
Operating rules for Big ticket application procedure

(5) Interview

The Committee interviewed 17 relevant individuals at HCF, HCL and HC between June 26, 2019 and July 8, 2019. Those interviewed are listed in the table below.
The Committee mainly selected management of HCF and HCL as interviewees in order to confirm whether there was the possibility that HCF and HCL were systematically involved in the Fraud. In order to confirm the operations and system of risk management at HCF, HCL

and HC, the Committee interviewed managers/accounting personnel[7] of the departments involved in the most important parts of the factoring and lease operations. Where an intended interviewee had already retired, the Committee selected an individual who was considered to have an equivalent operational knowledge. In order to prevent interfering with the ongoing legal proceedings, interviews with HCF and HCL employees were only conducted where strictly necessary to fulfil the purpose of the Investigation, based on the advice of lawyers specializing in Chinese law. For the same reason, no questionnaire surveys for officers and employees of HCF and HCL was conducted and no hotline was established.

<Interviewee>

Interviewee	Department/Position[8]	Date of interview[9]
Person a	Law Firm A General Counsel of HCF	June 26
Person b	Managerial position at HC (Former managerial position at HCF)	June 26 July 5
Person c	Managerial position at Company B (Former managerial position at HCF)	June 27 July 5
Person d	Managerial position at HCF	June 27 July 2
Person e	Managerial position at HCF	June 28 July 2
Person f	Managerial position at HCF	July 2
Person g	Non-managerial position at HCF	July 2
Person h	Managerial position at HCL and managerial position at HCF	July 1
Person i	Managerial position at HCL	July 1
Person j	Managerial position at HCL	July 1
Person k	Managerial position at HCL	July 1

7 Managerial positions in the companies.

8 Department and position for personnel assignment at the time of interview. For those who have left or returned to the position, the brackets indicate their department and position at the time when they belonged to HCF or HCL.

9 All interviews were held in 2019.

Interviewee	Department/Position[8]	Date of interview[9]
Person l	Managerial position at HCL	July 1
Person m	Managerial position at HCL and managerial position at HCF	July 1
Person n	Managerial position at HC (Former managerial position at HCL and managerial position at HCF)	July 2
Person o	Managerial position at HC, managerial position at HCL and managerial position at HCF	July 1
Person p	Managerial position at HC	July 5
Person q	Managerial position at HC	July 8

(6) Digital forensic investigation

i Preservation and receipt of devices and electronic data to be investigated

Between June 19 and June 24, 2019, the Committee preserved electronic data in company personal computers ("**PC**") and smartphones ("**Smartphones**") used by relevant HCF and HCL employees. With respect to a mail server data, the Committee received and preserved electronic data extracted by individuals responsible for information systems at the third party used by HCF and HCL to manage its mail servers at the time of the Initial Investigation.
Data received and preserved is summarized in the table below:
<Individuals whose data was preserved>

	Company (Note 1)	Name	PC	Mail server	Smartphones
1	HCF	Person c	○	○	○
2	HCF	Person e	○	○	○
3	HCF	Person b	-	○	-
4	HCF	Person r	○ (Note 2)	-	○
5	HCF	Person f	○	○	○ (3 smartphones)
6	HCF	Person s	○	○	○ (2 smartphones)

7	HCF	Person g	〇	〇	〇 (2 smartphones)
8	HCF	Person t	〇	〇	〇 (2 smartphones)
9	HCL	Person i	〇	〇	-
10	HCL	Person l	〇	〇	-
11	HCL	Person m	〇	〇	-
12	HCL	Person j	〇	〇	-
13	HCL	Person u	〇	〇	-
14	HCL	Person v	〇	〇	〇
15	HCL	Person w	〇	〇	〇
16	HCL	Person x	〇	〇	〇
17	HCL	Person y	〇 (Note 2)	-	-
18	HCL	Person z	〇	〇	〇
19	HCL	Person aa	〇	〇	〇
20	HCL	Person ab	〇	〇	〇
	HCL/HCF	Other	42 persons	41 persons	8 smartphones
		Total	61 persons	59 persons	26 smartphones

(Note 1) For those who left or returned to the company, the company shown is where they were based during their employment.

(Note 2) Person r and Person y had already left the company. Data was preserved from the company computer they used during their employment.

ii Process and review[10] of data in the PC and mail server

Deleted data was restored to the extent possible in order to preserve it. From the list of individuals whose data was preserved/received, the Committee selected the following persons noted in No.1 to No. 20 above as a reviewee. Similar to the selection of interviewees (described in (5) above), the Committee primarily selected for review HCF and HCL management and managers/accounting personnel from departments involved in the most

10 Includes work to classify the relevance to the investigation objectives.

important parts of the factoring and lease operation flows. It also included individuals involved in deals, credit examination, contracting and collections related to the four cases. Data for the selected individuals, including MS Word, Excel and PowerPoint files, and PDF files, was uploaded to “Relativity” (an investigation review platform) after database conversion processing. Data preserved from the mail server was directly processed for database conversion to upload.

The total number of electronic documents from the PCs and mail server uploaded into Relativity was 298,281. Of these, 35,091 were extracted using keywords to be read and reviewed.The electronic documents were also searched and reviewed based on other information.

iii Treatment of the Smartphones data

From the list of individuals whose data was preserved/received, the Committee selected No. 5, 6, 7, 8, 14, 15, 16, 18, 19, and 20 in the list as a reviewee. As with the selection of interviewees as described in (5) above, the Committee mainly selected management of HCF and HCL and manager/accounting personnel of the departments involved in the most important part of the factoring and lease operation flows as a reviewee, and also included persons involved in deals, credit examination, contracting and collection for the four cases. The Committee mainly extracted text messages from Smartphones for review. Text messages were reviewed without being uploaded to the investigation review platform.

(7) Investigation on the existence of similar cases

As the Fraud occurred in HCF’s factoring transactions, all factoring receivables of HCF with balance as at the end of April 2019 was verified for existence in the Initial Investigation. As described in (1) and (2) above, the Committee took over the results of the Initial Investigation and verified existence of the factoring receivables of HCF.

The Committee considered the possibility that other similar cases existed in HCL lease receivables and verified the existence as described in (3) above.

As described in Chapter 2, lease receivables of subsidiaries engaged in leasing business, including HCL, include receivables arising from leasing, leaseback and transfer of lease receivables. Among these, the transfer of lease receivables is similar to factoring transactions in that receivables are purchased. It is, however, different from the credit status of HCF’s factoring transactions where the Fraud occurred. Existence of the lease receivables is confirmed through the verification of existence of the leased property. Also, the original creditor is a leasing company that has transactions in the past, and transactions are conducted after considering the credit of the original creditor based on the past transactions. Leasing subsidiaries other than HCL were, therefore, excluded from the scope of the investigation when considering the existence of similar cases.

Further, the background of the Fraud included the fact that HCF had large factoring transactions with new customers, which placed an emphasis on the creditworthiness of the debtors. Overseas subsidiaries that are engaged in factoring transactions outside of China were excluded from the scope of the investigation (for similar cases) because the size of their factoring business and their overall business models/environment was significantly different from that of HCF. The management of HCF and HCL also did not concurrently serve as officers of other overseas subsidiaries.

Chapter 2 Basic information of the investigation

Section 1 Overview of businesses of HCF and HCL

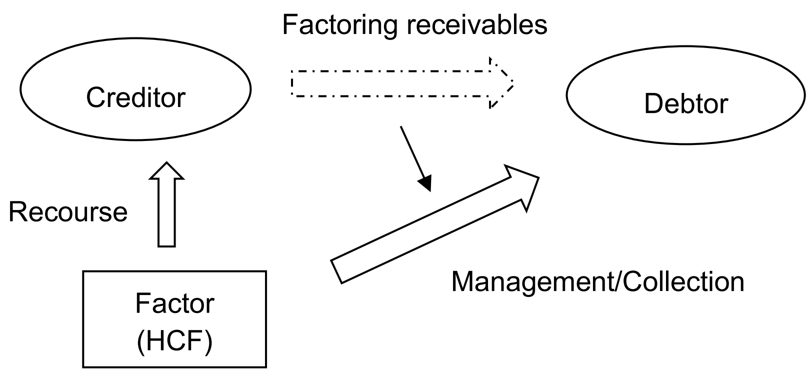
1 Overview of business of HCF

(1) Details of business

HCF specializes in factoring business.

Factoring refers to a financial service in which a creditor transfers the amount due from a debtor for sales (hereinafter "**factoring receivables**") to a third party, and the third party manages the receivables acquired and collects payment on the receivables from the debtor. The third party is generally referred to as a factor and HCF operates as a factor.

[Relationship diagram: Factoring]



The main business risks in factoring are: (1) the risk of not being able to collect payment on the transferred receivables due to the debtor's lack of ability to pay its debt (credit risk of the debtor), and (2) the risk that factoring receivables do not exist due to the absence of sales contract between a creditor and debtor (risk of the existence of factoring receivables).

In a factoring agreement, a factor and a creditor may agree that "if a debtor falls into default after a creditor transfers factoring receivables to a factor, the creditor is responsible for paying the amount due to the factor on behalf of the debtor". A factor makes a claim for reimbursement to a creditor based on the agreement, which is generally referred to as recourse.

If a factor can obtain a "consent without objection" from a debtor in connection with transfer of receivables, the factor directly collects payment on the receivables from the debtor (the

flow of cash: debtor⇒factor). In contrast, if a factor cannot obtain a “consent without objection" from a debtor in connection with transfer of receivables, or the factor does not obtain a “consent without objection,” the factor collects payment on the receivables from the debtor through a creditor (the flow of cash: debtor⇒creditor⇒factor). In the case of (1), the credit risk of the debtor is emphasized, and in the case of (2), the credit risk of the creditor is emphasized. Generally, HCF obtains a “consent without objection” from debtors in connection with transfer of receivables, and HCF has more (1) than (2) in its transactions[11].
A factor may transfer all or part of the receivables transferred in a factoring transaction to another factoring operator (“**refactoring**”).

(2) Establishment of HCF and business development

Originally, in China, factoring business is permitted only for financial institutions such as banks. In order to promote financing of small- and medium-sized companies that did not have the sufficient creditworthiness to borrow from banks, the Chinese government give authorized the factoring business by financing companies other than financial institutions such as banks, only in a special financial district with tax and employment incentives in Shanghai. Following this, HCF was established in August 2013 for the purpose of developing a new business model in Hitachi Capital Group.
At the beginning, HCF developed factoring business with suppliers of each of Hitachi Group companies as its main customers; however, the business for Hitachi Group was sluggish. As such, HCF adopted a policy of providing factoring services for accounts receivables from certain Chinese outstanding companies from around 2016, and then gradually expanded the factoring business for receivables from more outstanding companies.

2 Overview of business of HCL

HCL specializes in businesses related to leasing, leaseback, transfer of lease receivables and leased assets.

(1) Lease

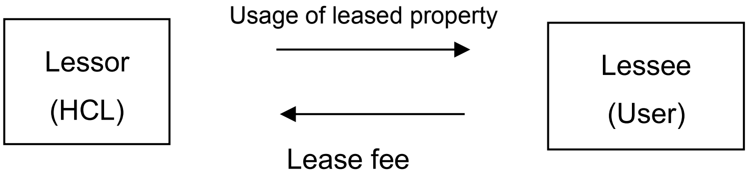
A lease is a transaction in which a lessor who owns a certain property gives a lessee of the property the right to use it for profit over a certain period, and the lessee pays lease fee as a

---

11 Although factoring agreement of HCF also carries a recourse to creditors, the credit quality of creditors was only preliminarily identified, and their recoverability was determined mainly on the basis of the credit quality of debtors.

consideration.
The main business risk in lease is the risk of not being able to collect lease payment due to the lessee’s lack of financial ability to pay its debt (lessee's credit risk).

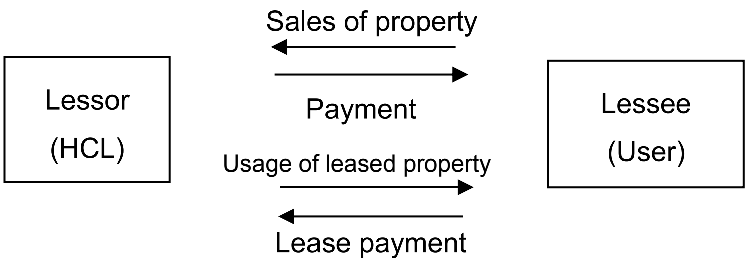
[Relationship diagram: Lease]



(2) Leaseback

A leaseback is a transaction in which after an owner of a certain property sells the property to a leasing company, the owner enters into lease agreement (lease contract) for the property with the leasing company (buyer) and continues to use the property.
In leaseback transactions, there are cases (1) where a property that was originally owned by a lessee is sold to a lessor, and (2) where a lessee purchases a new property from a supplier and sells it to a lessor in entering into leaseback agreement.
The main business risks in leaseback transactions are: (1) the risk of not being able to collect lease fee due to the lessee’s lack of financial ability to pay its debt (lessee's credit risk) and (2) the risk that a leased property does not exist or the leased property is not transferred to a lessee from a supplier (risk of the existence of properties).

[Relationship diagram: Leaseback]

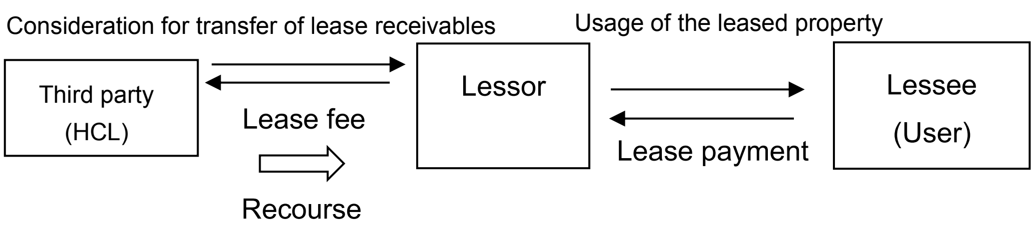


(3) Transfer of lease receivables

A transfer of lease receivables is a transaction in which a lessor transfers its right to claim lease payment to a lessee (“**lease receivables**” and along with factoring receivables, referred to as “**Receivables**”) to a third party, and the third party manages the lease

receivables transferred and collects lease payment from the lessee.
A third party may have the right to claim lease payment (recourse) to a lessor, a transferor of lease receivables, on behalf of a lessee if the lessee falls into default.
The main business risks in transfer of lease receivables are: (1) the risk of not being able to collect on the lease receivables transferred due to the lessee's lack of ability to pay its debt (credit risk of the lessee), and (2) the risk that lease receivables do not exist due to the absence of lease agreement between a lessor and lessee (risk the existence of lease receivables)[12].
In addition, with recourse, the third party (HCL) bears the credit risk of the lessor instead of the credit risk of the lessee.

[Relationship diagram: Transfer of lease receivables]



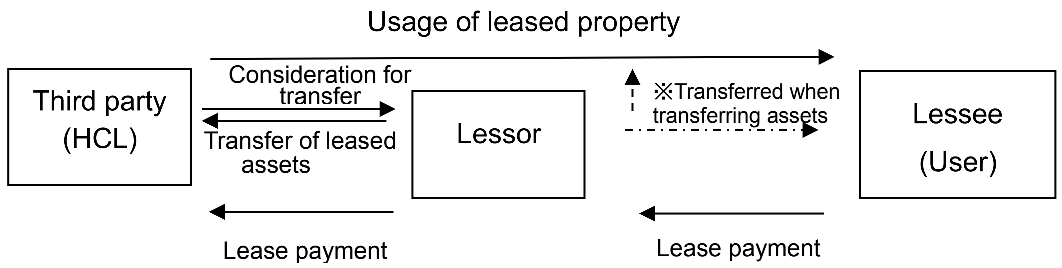
(4) Transfer of leased assets

A transfer of leased assets is a transaction in which a lessor transfers a property, which is leased to a lessee based on lease agreement, to a third party in addition to lease receivables, and the third party is assigned a position as a lessor, manages leased assets and collects lease payment directly from the lessee or indirectly through the lessor.
Depending on the terms of leased assets transfer agreement between a third party and a lessor, the third party may not have recourse to the lessor. In the case of HCL's leased assets transfer, the third party is not assigned the right to claim lease payment to the lessor on behalf of a lessee (recourse) when the lessee falls into default. As such, HCL carefully selects a lessor, a transferor of leased assets, in transferring leased assets and also examines the creditworthiness of the lessee.
The main business risks in transfer of leased assets are: (1) the risk of not being able to collect on the lease receivables transferred due to the lessee's lack of ability to pay its debt

12 In addition, there may be risks that the lease receivables have not been transferred to a third party, or that perfection requirements have not been provided, or that the lease receivables are subordinated to a third party. However, in most cases, such risks are converged on the credit risk of the lessor through a recourse, a detailed description is not presented here.

(credit risk of the debtor), and (2) the risk that lease agreement between a lessor and lessee or property to the agreement does not exist, or right or property to the lease agreement is not transferred to the third party (risk of the existence of lease agreement or leased property).

[Relationship diagram: Transfer of leased assets]



Section 2 Overview of HCF and HCL operations

The operations of HCF and HCL are summarized in the table below:

1 HCF factoring operation flow

Operation category	Responsible department	Summary
Deals (Marketing)	Market Promotion Section Sales departments at HCL	・Market Promotion Section is responsible for sales to Hitachi Group and Japanese companies. Sales departments at HCL are responsible for sales to other Chinese companies. ・ Gather basic information (capital relationships, company structure, other information on the Internet) of creditors and debtors. ・Gather credit related documents (master agreement between creditors and debtors, business operating permit, financial statements for the last three years) from creditors and debtors and submit them to Marketing & Strategy Section.

<table>
<tr><th>Operation category</th><th>Responsible department</th><th>Summary</th></tr>
<tr><td>Credit examination</td><td>Marketing & Strategy Section
Japan headquarters
HCF Board of directors</td><td>・Approve or disapprove credit and determine the amount of credit based on the supporting documents.
・Depending on the amount of credit, the approval of General Manager of Business planning department, the President, Japan headquarters and the board of directors is required.
・If HCL provides guarantees to HCF[13], approval through HCL's examination process is required.</td></tr>
<tr><td rowspan="2">Execution of agreement</td><td>Operating Section</td><td>・Draft agreement.</td></tr>
<tr><td>Market Promotion Section
Sales department of HCL
Marketing & Strategy Section</td><td>・Gather documents (order form, Fapiao(発票), shipment list, inspection form, consent form for transfer of receivables) that are necessary to execute transfer of receivables and submit them to Operating Section.</td></tr>
<tr><td>Transfer of receivables</td><td>Operating Section</td><td>・Confirm credit limit granted to debtors.</td></tr>
<tr><td>Payment</td><td>Finance and administration section</td><td>・Remit payment to creditors.</td></tr>
<tr><td rowspan="2">Collection</td><td>Finance and administration division</td><td>・Confirm status of collection from debtors.</td></tr>
<tr><td>Operating Section</td><td>・If collection on the receivables is overdue, take appropriate measures to collect payment.</td></tr>
</table>

2 HCL lease and leaseback

13 HCL was supposed to provide guarantees to HCF for the transactions that HCL referred to HCF and for the joint projects of HCL and HCF.

Operation category	Responsible department	Overview
Deals (Marketing)	Sales departments (including Strategic Business Development Division)	・Strategy Business Development Division is responsible for sales to Hitachi Group, Japanese companies and new business. Sales departments are responsible for sales to other Chinese companies. ・Gather basic information (capital relationships, company structure, other information on the Internet) of lessees. ・Submit the information to the Big ticket evaluation committee, announce background of deals, company profile, significance of the approach, yield, and obtain approval for the approach through agreement by the Chairman of the board of directors, the President, General Manager of Business Department and Credit Control Department. ・Gather credit related documents (business operating permit, financial statements for the last three years, documents related to lease properties) from lessees and submit them to Credit Control Department.
Credit examination	Credit Planning Section Japan headquarters HCL Board of directors	・Approve or disapprove credit and determine the amount of credit based on the credit related documents. If the amount is less than ○ RMB, only confirmation and approval of the head of Sales department is required. ・Depending on the amount of credit, the approval of the General Manager of Credit Control department, the President, the Chairman of the board of directors, Japan headquarters and the HCL board of directors is required.
Execution of agreement	Business Support Section	・Draft agreement.

	Legal department	・Confirm the contents of the agreement.
Inspection	Asset Management Section	・Visit the site and inspect lease properties. ・In the case of leaseback, obtain a list of properties from a lessee and inspect the properties based on the list. ・Draft a report summarizing inspection results and submit it to Business Support Section.
Payment	Credit Planning Section	・After confirming that credit conditions are met, sign authorization memo and submit it to Business Support Section.
	Business Support Section	・After confirming that all required documents (authorization memo, inspection report) are prepared, provide payment instructions to Treasury Section.
	Treasury Section	・Remit payment to lessees or suppliers.
Collection	Asset Management Section	・Confirm status of cash collection from debtors. ・If collection on the receivables is overdue, take appropriate measures to collect payment.

3 HCL transfer of lease receivable

Operation category	Responsible department	Overview
Deals (Marketing)	Sales departments (including Strategic Business Development Division)	・Strategy business development department is responsible for sales to Hitachi Group, Japanese companies and new business. Sales departments are responsible for sales to other Chinese companies. ・Gather basic information (company registration information, information on the Internet) of lessors and lessees. ・Submit the information to the Big ticket evaluation committee, announce background of deals, company profile, significance of the approach, yield, and obtain approval for the approach through agreement of the Chairman

Operation category	Responsible department	Overview
		of the board of directors, the President, General Manager of Business department and Credit Control Department. ・ Gather credit related documents (lease agreement between lessors and lessees, business operating permit, financial statements for the last three years) from lessors and lessees and submit them to Credit Planning Section.
Credit examination	Credit Planning Section, Japan headquarters HCL Board of directors	・Approve or disapprove credit and determine the amount of credit based on the credit related documents. If the amount is less than 〇 RMB, only confirmation and approval of the head of Sales department are required. ・ Depending on the amount of credit, the approval of General Manager of Credit Control, the President, the Chairman of the board of directors, Japan headquarters and the HCL board of directors is required.
Execution of agreement	Business Support Section	・Draft agreement.
	Legal department	・Confirm the contents of the agreement.
Payment	Credit Planning Section,	・After confirming that credit conditions are met, sign authorization memo and submit it to Business Support Section.
	Business Support Section	・ After confirming that all required documents (authorization memo) are prepared, provide instructions for payment to Treasury Section.
	Treasury Section	・Remit payment to lessors.
Collection	Asset Management Section	・Confirm status of cash collection from lessors. ・If collection on the receivables is overdue, take appropriate measures to collect payment

Operation category	Responsible department	Overview
		mainly from lessors.

4 HCL transfer of leased assets

Operation category	Responsible department	Overview
Deals (Marketing)	Sales departments (including Strategic Business Development Division)	・Strategy business development department is responsible for sales to Hitachi Group, Japanese companies and new business. Sales departments are responsible for sales to other Chinese companies. ・Gather basic information (company registration information, information on the Internet) of lessors and lessees. ・ Submit the information to the Big ticket evaluation committee, announce background of deals, company profile, significance of the approach, yield, and obtain approval for the approach through agreement by the Chairman of the board of directors, the President, General Manager of the Sales department and Credit Control Department. ・ Gather credit related documents (lease agreement between lessors and lessees, business operating permit, financial statements for the last three years) from lessors and lessees and submit them to Credit Planning Section.
Credit examination	Credit management division Japan headquarters	・Approve or disapprove credit and determine the amount of credit based on the credit related documents. If the amount is less than ○ RMB, only confirmation and approval of the

Operation category	Responsible department	Overview
	HCL Board of directors	head of Sales department are required. ・ Depending on the amount of credit, the approval of the General Manager of Credit Control, the President, the Chairman of the board of directors, Japan headquarters and the HCL board of directors is required.
Execution of agreement	Business Support Section	・Draft agreement.
	Legal department	・Confirm the contents of the agreement.
Payment	Credit Planning Section	・After confirming that credit conditions are met, sign authorization memo and submit it to Business Support Section.
	Business Support Section	・ After confirming that all required documents (authorization memo) are prepared, provide instructions for payment to Treasury Section.
	Treasury Section	・Remit payment to lessors.
Collection	Asset Management Section	・Confirm the status of cash collection of lease payment paid by lessees through lessors. ・If collection on the receivables is overdue, take appropriate measures to collect payment mainly from lessees.

Section 3 Overview of internal controls related to factoring of HCF

The overview of internal controls related to factoring agreement of HCF is as described below:

<table>
<tr><th>Operation category</th><th>Name of control</th><th>Description of internal control</th><th>Responsible department</th><th>Frequency</th></tr>
<tr><td rowspan="2">Credit examination</td><td>Credit application</td><td>Fill out credit application form based on the credit related documents obtained and submit it for approval. Documents required for credit application form are as follows (documents provided by customers require a company seal):
・Copy of customer-sealed business permit, tax registration certificate, organization code certificate (the company that completed “unification of three certificates" submits updated business permit only)
・Copy of legal representative's ID card or passport
・Copy of the financial statements for the last three years or credit report
・Summary sheet for request for transaction
・Result of S&P (excluding public and finance)</td><td>Market Promotion Section Marketing & Strategy Section</td><td>As needed</td></tr>
<tr><td>Credit approval</td><td>The credit application is approved based on the following authorities:
・○ RMB or less:
HCF Sales department/Planning department→HCF General Manager of Business Planning Department→HCF President approval
・○ RMB or less (debtor is limited to Hitachi Group):
HCF Sales Department/Planning Department→HCF General Manager of Business Planning Department→HCF President approval
・Less than ○ RMB:
HCF Sales Department →HCF Business Planning Department→HCF President→HC headquarters approval
・○ RMB or more:
HCF Sales Department →HCF Business Planning Department→HCF President→HCF</td><td>Marketing & Strategy Section</td><td>As needed</td></tr>
</table>

Operation category	Name of control	Description of internal control	Responsible department	Frequency
		Chairman of the board of directors→HC headquarters approval ・Over 〇% of HCF's net assets (previously, 〇 RMB)： HCF Sales Department →HCF Business Planning Department→HCF President→HCF Chairman of the board of directors→HC headquarters approval→HCF board of directors resolution		
Execution of agreement	Approval of transfer of trade receivables	A customer scans "Request for transfer of trade receivables" and documents related to relevant transactions and issues (sends) them to HCF. Operating Section receives and examines these documents as follows: ・Order form ・Fapiao(発票) (if available, verifies through VAT invoice online verification system at State Taxation Administration of The People's Republic of China for authenticity of the Fapiao(発票)) ・Shipment list and inspection form ・Checklist ・VAT Invoice records and general certificate of qualification for tax payment (first time only) Even in case where some of the documents are not available, at least Fapiao(発票) or inspection form should be obtained.	Operating Section	As needed
	Confirmation of transfer of trade receivables by debtors	After review of related documents is completed, Operating Section prepares "notice of transfer of trade receivables", and Marketing & Strategy Section and departments responsible for sales visit the debtors and request them to place their seal on the notice.	Operating Section Marketing & Strategy Section	As needed

Operation category	Name of control	Description of internal control	Responsible department	Frequency
	PBOC registration	Operating Section confirms the registration status of the creditors in the PBOC system, confirms that there is no duplicate transfer, and registers the transfer. Then print out registration confirmation and place the seal of "No problem found on PBOC registration “.	Operating Section	As needed
Execution of transfer of receivables	Payment request	Operating Section fills out “Payment Request” and submits it to Finance & Administration Section along with the following documents: ・Confirmation of transfer of trade receivables ・PBOC registration ・Factoring agreement	Operating Section	As needed
Collection	Authority for payment remittance	A user of online banking is not allowed to have authorities for both “payment request” and “payment approval”.	Finance & Administration Section	As needed
	Payment processing	Finance & Administration Section checks the status of payment receipt online banking, and when payment is received, accounts receivable is credited based on the actual payment receipt. Operating Section confirms whether it is “payment by creditor," “payment by debtor" or “indirect payment” in line with terms of the agreement, and if there are any differences, it is reported at the monthly management meeting.	Finance & Administration Section Operating Section	Daily

Chapter 3 Result and Findings of the Investigation

Section 1 Result and Findings related to HCF - Structure of the Fraud

1 Overview of the four cases

As described in Chapter 1 Section 1, the Initial Investigation identified doubts about the existence of receivables in the four cases regarding factoring transactions conducted by HCF, and revealed that HCF may have suffered damages from the fraud in the Case A, Case C and Case D. The overview of four cases are as follows.

(1) Case A

Case A involved a factoring agreement for receivables (an agreement with a recourse between the two parties; a notice is made to a debtor when there is a change in a creditor for debtor's consent) executed in 2018. Under this agreement, the creditor is Company C and the debtor is Company D.
The Case A was a transaction referred from other company to HCL and then referred to HCF. Company D was a new customer for HCF. When entering into a factoring agreement, HCF reviewed supporting documents including the agreement deemed to be exchanged between Company C and Company D and determined that underlying receivables existed. The person in charge at HCF visited Company D and received a notice of transfer of trade receivables from a person introduced him/herself as the Company's responsible person and obtained an acknowledgement letter for payments affixed with the Company D's stamp and signed with this individual.

Subsequently, however, HCF arranged an appointment via another route and held a meeting with another individual. During this meeting it was revealed that the individual who attended the meeting (the individual who introduced him/herself as a responsible person at Company D) was not a responsible person (a false identify) and supporting documents submitted were suspected to be forged, indicating that there is possibility of lack substance of the transaction.

(2) Case B

Case B involved a factoring agreement for receivables (an agreement with a recourse between the two parties; a notice is made to a debtor when there is a change in a creditor for debtor's consent) executed in 2018. Under this agreement, the creditor is Company E and Company F, and the debtor is Company G.

HCF acquired this deal which was referred by other company, in which the debtor is Company G. The Company G was a new customer for HCF. When entering into the factoring agreement, HCL examined supporting documents including the agreement between Company E, Company F and Company G, and determined that underlying receivables existed.
Subsequently, HCF contacted an individual who introduced him/herself as the responsible person through various meetings and phone calls. It is suspected, however, that this person was not the responsible person. Following to that HCF visited Company G and it obtained a confirmation of receivables from Company G. Given this background, it is suspected that a fraudulent act was committed in Case B.

(3) Case C

Case C is a factoring agreement (an agreement with a recourse between the two parties; and a notice made to a debtor when there is a change in a creditor for debtor's consent), which was executed between 2018 and 2019. Under this agreement, the creditor was Company H and the debtors were Company I and Company J.
Case C was acquired by the sales person at HCL referred from other company. Company H was a new customer for HCF. When entering into a factoring agreement, HCF examined supporting documents, including the agreement between Company H, Company I and Company J, and determined that underlying receivables existed.
Since the existence of receivables was in doubt for Case A as described in (1) above, the person in charge at HCF held a meeting with an individual who introduced him/herself as the responsible person at Company I and checked his/her business and employee ID cards. Following the meeting, HCF tried to contact Company I several times through Company H. These requests were not, however, responded to. Therefore the person in charge at HCF visited Company I directly. During this visit, it was revealed that the person who introduced him/herself as the responsible person at Company I was not a true responsible person, and supporting documents obtained from Company H were suspected forgeries. In response, the person in charge at HCF visited Company J. As a result, it was identified that supporting documents related to Company J obtained by HCF were also suspected forgeries.

(4) Case D

Case D involves a factoring agreement for trade receivables (an agreement with a recourse between the two parties; and a notice is made to a debtor when there is a change in a creditor for debtor's consent), which was executed between 2017 and 2019. Under this agreement, the creditor was Company K and the debtor was Company L.

Case D was a transaction referred by the sales person at HCL. Company L was a new customer for HCF. When entering into a factoring agreement, HCF examined supporting documents, including the agreement between Company K and Company L, and determined that underlying receivables existed.

Subsequently, HCF identified that supporting documents were suspected forgeries. The person in charge at HCF held a meeting with the responsible personnel at Company L. Their conclusion was that these documents were likely forged.

2 Existence of receivables

As described in Chapter 1 Section 3 3(1), the Committee's assessment of procedures performed in the Initial Investigation did not specifically identify any unreasonable items in their results, concluding that it is highly probable that underlying receivables do not exist in Case A, Case C and Case D.

With respect to Case B, the Committee did not specifically identify any unreasonable items in the results of the Initial Investigation, concluding that the existence of underlying receivables is doubtful.

In addition, the Committee noted no other specific unreasonable items in the results of the Initial Investigation, concluding that recourse receivables against the original creditors exist because (1) these cases were a factoring agreement related to trade receivables with a recourse between the two parties, and a notice is made to a debtor when there is a change in a creditor to obtain debtor's consent, and (2) the Internal Investigation Committee obtained a legal opinion stating that "these factoring agreements were likely to be deemed to be valid provided that there was no breach of the mandatory requirements set out in applicable laws and administrative laws and regulations or there was no other cause for invalidating the agreement, even if trade receivables does not substantially exist."

In respect of other receivables, the Internal Investigation Committee inspected documents, such as credit application forms, sales agreements, Fapiao (発票), registration in the system of the People's Bank of China, and notices of transfer of trade receivable for some of the cases. For all factoring transactions outstanding as of April 2019, one or more of the following procedures were performed: (1) balance confirmation by mailing to creditors, (2) balance confirmation by mailing to debtors, (3) balance confirmation by visiting creditors, and/or (4) balance confirmation by visiting debtors. As a result, the Internal Investigation Committee verified that the existence of other receivables. The Committee inspected documents obtained by the Internal Investigation Committee (including documents obtained by the Investigation Office during the investigation period), summary of balance confirmation procedures and visit records. As a result, no unreasonable items were specifically noted in the procedures performed by the Internal Investigation Committee.

3 Internal controls over the factoring business

In evaluating the design effectiveness of internal controls factoring business in place at HCF at the time of executing the service for the four cases, inquiries were made with related individuals and relevant documentation was inspected, such as rules and operational manuals. No specific issues were identified from these procedures.
The operating effectiveness of internal controls over the factoring business described in Chapter 2, Section 3 was also conducted through inquiry and inspection of supporting documents. No specific issues were identified in relation to the operating effectiveness of internal controls.
Given that the current internal controls failed to prevent the Fraud, it is recommended that they are further enhanced to strengthen their design to help prevent a reoccurrence. Recommendations are described in Chapter 5.

Section 2 Possibility of Involvement of HCF officers and employees in the Fraud

There are four divisions in HCF: the Marketing & Strategy Section, Market Promotion Section, Operating IT Section and Finance & Administration Section. As described in Chapter 2 Section 2, the Marketing & Strategy Section、Market Promotion Section and Operating IT Section, excluding the Finance & Administration Section, are the main divisions responsible for the factoring related operations at HCF: the Finance & Administration Section is not engaged in activities from the initiation to the execution of the transfer of receivables. If the involvement in the Fraud of management and responsible individuals in these divisions is doubtful, there would be a heightened suspicion that the Fraud had been committed at the organization level.
In light of this, the Internal Investigation Committee undertook procedures to investigate whether HCF officers and employees were involved in the Fraud, including interviews with HCF officers and employees, digital forensic procedures, a questionnaire survey and collection of relevant documentation. No evidence indicating the involvement of HCF officers and employees in the Fraud was identified.
Interviews on behalf of the Internal Investigation Committee were conducted by people who did not have any interest or involvement in the four cases to help prevent the results of the

interviews being biased. Independent external professionals were used to support the digital forensic investigation to maintain independence and objectivity. Based on these procedures, the results of the Internal Investigation Committee were considered to be sufficiently reliable.
As described in Chapter 1 Section 3 3(5), the Committee conducted interviews with Person n, Person c, Person e, Person b, Person d, Person f, Person h and Person g who were officers and employees of HCF. All those interviewed person denied any involvement in the Fraud and commented that they did not suspect any officers or employees of being involved in the Fraud. To corroborate this, the Committee collected related documents and conducted digital forensic procedures described in Chapter 1 Section 3 3(4) (6). No evidence indicating the involvement of HCF officers and employees was identified.
As described in Chapter 2 Section 2, under HCF's procedures, permission to execute a factoring transaction is determined during the credit examination phase and when the receivables are transferred Fraud is, therefore, possible if individuals in the Marketing & Strategy and Operating Sections responsible for these activities could be misled into believing that the underlying transaction existed between the creditor and debtor, without anyone in HCF being intentionally involved in the Fraud. The method used to perpetrate the Fraud is very sophisticated and, combined with the causes described in Chapter 4, it is highly probable that those involved in the Marketing & Strategy and Operating Sections were misled into believe that underlying transactions existed, rather than being knowingly involved in the Fraud.
The Committee's has not conducted interviews, or targeted the questionnaire and hotline, across all employees in order to avoid disruption to ongoing legal proceedings. The Committee believes, however, that evidence indicating the involvement of HCF officers and employees is unlikely to be identified even if such interviews and investigation procedures targeting all employees were to be performed. This is on the basis that no evidence indicating the involvement of HCF officers and employees in the Fraud was identified through the interviews or digital forensic investigation conducted by the Internal Investigation Committee and the Committee.
Based on the above, the Committee considers it is not unreasonable to conclude that no HCF's officers and employees were involved in the Fraud.

Section 3 Possibility of Involvement of HCL officers and employees in the Fraud

As described in Chapter 1 Section 1 (2), HCF had initially developed its factoring business by targeting suppliers of the Hitachi Group as customers. The Market Promotion Section, which is the only sales unit established in HCF, was responsible for sales activities primarily targeting the Hitachi Group and other Japanese companies. There was, therefore, no sales unit/salesforce at HCF targeting Chinese companies. HCF acquires deals related to Chinese company customers through referrals from HCL's sales units or other peer companies. The four cases related to the Fraud were also acquired through referrals from sales personnel at HCL or other companies.

In addition, as noted in Chapter 2, Section 2 1, HCL's processes for referring new transactions to HCF, required a guarantee to be presented to HCF, which was subject to HCL's credit examination process (depending on the amount of the guarantee). In the four cases, HCL provided guarantees to HCF after conducting the credit examination process. Under this practice, those who had approval authority might have been involved in the Fraud. Based on this assumption, the Committee conducted interviews with Person n, Person i, Person l and Person m who all had authority to approve guarantees provided to HCF. All interviewees denied their involvement in the Fraud and commented that no personnel with approval authority in the examination process was suspected of being involved in the Fraud. A digital forensic investigation was also conducted in order to Person i, Person l and Person m. No evidence that rebuts the statements of these interviewees was identified through the investigation. As such, the Committee has not identified any facts indicating that individuals with approval authority in the examination process had been involved in the Fraud, and has not identified any situation that might indicate that such facts exist.

Even if the HCF sales personnel who referred the four cases to HCF were involved in the Fraud, this would not necessarily indicate company-wide organizational involvement as HCL management and key responsible were not suspected to be involved in the Fraud to the extent that those involved in the Fraud were limited to sales persons.

Section 4 Controls in place at HC to manage business activities of HCF and HCL

HC's standards on authority to grant credits requires that HCF and HCL obtain approval from HC for transactions that meet the following criteria: For HCF, transactions with non-Hitachi Group companies that exceed RMB ○; and for HCL, transactions granting credits to hospitals that exceed RMB ○ and other transactions that exceed RMB ○. For transactions that require approval from HC, HCF and HCL prepare a credit application form for large transactions, which will be submitted to HC. The application form includes the background for originating a transaction, the profile of persons involved in the transaction, the overall scheme of the transaction, and information about financial position of the persons involved. HC reviews the application form and undertakes the prescribed approval process depending on the relevant transaction amount. Authority to approve transactions is given to the Asset Management Department, responsible officers or President & CEO, according to the amount of transactions. Transactions of JPY ○ or more requires approval of President

& CEO. For transactions that require approval of the President & CEO, credit risk is also examined by the Credit Risk Examination Committee.
The examination by HC is conducted in accordance with the Credit Risk Policy and Credit Risk Management Regulations. These policies and rules do not set out specific requirements, such as documents to be referenced in the credit risk examination, and instead specify a basic policy for the credit risk examination. Furthermore, these policies and rules primarily focus on how to examine the "credit risk" of parties to the transaction. HC's credit examination focuses on elements such as the credit information of the parties to the transaction and a risk analysis of the transaction scheme, assuming that the existence of receivables is verified. HC is not, therefore, required to examine supporting documents that prove the existence of receivables, which is a key issue for this investigation. HC's examination process, for example, does not include a procedure to obtain all original supporting documents used to prove the existence of underlying receivables of the factoring agreement, such as orders, Fapiao (発票) and acceptance, to determine whether HCF verified the existence. The Committee believes, however, that HC's examination process was sufficient as HC confirmed with HCF and HCL on a periodic basis that they had verified the existence of receivables, based on supporting documents or a legal opinion. Also, it is not practicable for HC to examine all supporting documents used by each company.

As previously mentioned, HC undertook certain examination procedures for each transaction executed by HCF and HCL. The Committee recommends, however, that HC becomes more engaged in HCF and HCL's activities, such determining examination information when transactions are initiated, developing operational manuals that set out necessary documents, and establishing a review system at HCF and HCL. This would be focused on helping ensure procedures at both subsidiaries help to prevent similar cases of Fraud.

Section 5 Existence of a similar case at HCL

As noted above, in verifying the existence of 32 receivables listed in Chapter 1, Section3 3(3) a, the Committee conducted site visits to the lease companies for lease receivable transfer contracts (with a recourse provision) and to lessees of lease contracts for leased asset transfer contracts (with a non-recourse provision) and leaseback contracts, and inspected various supporting documents related to transactions and obtain receivable balance confirmations.
Specifically, the Committee conducted the following verification procedures taking into account that the factors including the fact that the Fraud had been committed at HCF.

- Conducted background check procedures for the lease companies and lessees to verify that persons suspected of having a special conflict of interest with HCL were not registered as officers in advance.
- Conducted site visits to the lease companies and lessees with employees that were not involved in the transactions under Investigation.
- Conducted the identify verification process during the site visits by verifying the name, the department and position of persons in charge at the lease companies and lessees against the identification card, business card and other supporting documents, and confirming the name, department and other information of other employees of the lease companies and lessees.
- Obtained balance confirmations directly during the site visits, and verified that the lease companies and lessees were aware of the lease receivables and the receivable balances identified by HCL were accurate.
- Verified that lease receivable transfer contracts, leased asset transfer contracts and leaseback contracts entered into with HCL maintained by the lease companies and lessees were same as those contracts maintained by HCL. Also inspected supporting documents related to transactions to verify the reliability of responses to the balance confirmations.
- Examined documents showing inspection of leased assets by the lease companies at the time of entering into a lease contract as necessary to verify the existence of underlying lease receivables for the lease receivable transfer contracts.

The Committee has not obtained all necessary supporting documents related to transactions through site visits as some lease companies or lessees declined to provide supporting documents to HCL. In such cases, the Committee performed other procedures using related supporting documents maintained by HCL.

As a result of the procedures above, the Committee did not identify any evidence indicating the occurrence of a case similar to the Fraud.

Section 6 Impacts

The Committee aggregated the impact amount of impacts based on the findings detailed up to Chapter 3 Section 5 and accounting treatment determined by HC. The factual findings include the following:

- No unreasonableness was specifically noted for the result of the Initial Investigation concluding that it is highly probable that underlying receivables do not exist for Case A, Case C and Case D.
- No unreasonable item specifically was noted for the result of the Initial Investigation

concluding that the existence of underlying receivables is doubted for Case B.

- No unreasonable item was specifically noted for the result of Initial Investigation concluding that recourse receivables of original creditors exist.
- In evaluating the design effectiveness of internal controls over the factoring business in place at the time of executing the agreements for the four cases, conducted interviews with the related personnel and inspected documents including related rules and operational manuals. As a result, no issue was noted.
- With regard to the four cases, evaluated the operating effectiveness of internal controls over the four cases described in Chapter 2 Section 3 by conducting inquiries and inspecting related documents. As a result, no specific issue was noted in the operating effectiveness of controls for each case.
- As a result of interviews and digital forensic investigations, no specific evidence indicating that HCF's officers and employees, HCL's management and personnel responsible for key operations had been involved in the Fraud was identified.
- No specific evidence indicating the occurrence of a similar case at HCL was identified.

In the aggregation, the collection status of receivables up to July 5, 2019 is considered. Tax effects and foreign currency translation adjustments recognized in the consolidation are not considered.

Based on the above, the following table shows the results of aggregating the impact on profit before income taxes for the year ended March 31, 2019 (the fourth quarter).

Case	Amount	Unit
Case A	Not disclosed	in thousand RMB
Case B	Not disclosed	in thousand RMB
Case C	Not disclosed	in thousand RMB
Case D	Not disclosed	in thousand RMB
Total	(1,265,476)	in thousand RMB
Foreign exchange rate		16.33 (JPY/RMB)
Impact on profit before income taxes for the year ended March 31, 2019 (the 4Q)	(20,665)	in million JPY

Chapter 4 Causes of failure to prevent the Fraud

As described in Chapter 3 Section 1, 3, the Committee has not identified any issue in the design and operating effectiveness of internal controls over the factoring business in place

at HCF at the time of executing agreements for the four cases. However, given that the Fraud had occurred, these controls may be further enhanced.
The following sections analyze causes that could not prevent or minimize damages by the Fraud for the four cases. Chapter 5 provides recommendations to further enhance actions for the prevention of recurrence based on the identified causes.

Section 1 Risks associated with the factoring business in China had not been sufficiently identified

As described in Chapter 2 Section 1, 1(2), initially, HCF had been developing its factoring business by targeting suppliers of Hitachi Group companies as its main customers. Under this business model, however, it was difficult for HCF to win a sufficient amount of deals and HCF had been struggling to gain income. As a solution to this, HCF had adopted a model to provide a factoring service for trade receivables related to debtors that were leading companies with original Chinese capital. Since then, HCF had gradually expanded its factoring business that employed a scheme in which debtors were such leading companies. The business model of the factoring business generally seeks to gain income by assuming credit risk of debtors from creditors, and hence, the level of income gained will increase in proportion to the level of risks assumed. Therefore, HCF was in a situation where risks of HCF had increased as it expands its factoring business that employed such a scheme.
Creditors may gain benefits from the factoring as they can raise funds through the scheme. On the other hand, debtors cannot gain any benefits from factoring, but rather incur burdens because they need to address factors' visits, or change payees. Therefore, factors may be in a position difficult to make requests to debtors. In particular, where factors do not have a business relationship with debtors, it is difficult for factors to directly contact with debtors, and factors need to arrange a visit to debtors or a meeting with a person in charge through creditors. Therefore, if a creditor has malicious intent, there may be a case where the creditor disguises his/her acquaintance as a true person in charge and coordinates a meeting with this person. In fact, in Case A and Case C, as a result of setting meetings with debtors through creditors, creditors disguised their collaborator as a true person in charge and set up a meeting.
In providing a factoring service, HCF needs to collect financial statements and documents such as historical transaction records necessary for credit examination and documents necessary to verify the existence and authenticity of transactions such as acceptance vouchers and receipt confirmations. In particular, where factors do not have a business relationship with debtors, it is hard for factors to obtain these documents from debtors, and factors need to obtain such documents through creditors. If a creditor has malicious intent,

there may be a case where the creditor provides forged documents as if it had obtained from the debtor. In fact, in Case A, Case C and Case D, it is suspected that the documents collected from debtors through creditors had been forged.

As indicated from the situations above, there is a risk that a meeting is set up with a disguised person in charge or a risk that forged documents are provided because, under factoring practice, factors are difficult to make requests to debtors when initiating a new factoring transaction for receivables related to a debtor with no particular business relationship.

In the Fraud, risks that HCF's management and employees had not anticipated had materialized, as implied in the comments made by some HCF's management and employees stating that "we have never thought that the person in charge at the debtor may be a disguised person (because we had visited and held meetings with them several times)," or "we completely relied on the creditors and had never thought that documents might had been forged."

In light of the situation above, the reason for HCF to fail to sufficiently identify risks associated with the factoring business which had materialized in the Fraud is considered to be as follows: As noted above, HCF's main customers were suppliers of Hitachi group companies, and debtors of transactions were entities of the same Hitachi Group. Therefore, HCF was capable of directly contacting with debtors as a factor, and hence risks that disguised meetings might be set up or forged documents might be provided through creditors had not materialized.

In addition to this reason, in the first place, HCF had not sufficiently identified risks associated with the factoring business in China and had no sufficient accumulated know-how to address these risks because the four cases were executed shortly after the Chinese government deregulated the factoring business. In fact, damages from similar fraudulent acts had been detected in transactions executed by other factoring service providers in China.

Before launching its factoring business, HCF had prepared related documents and vouchers, such as agreements for the factoring business, in consultation with the Law Firm A which was engaged in developing regulations on the factoring business in the Shanghai Special Administrative Region. After launching its factoring business, HCF hired the Law Firm A as its corporate legal counsel and consulted any legal issues on individual deals. No particular issue was raised by the Law Firm A in these HCF's activities at the time of executing the four cases.

Given the above, while unexpected risk that meetings with persons in charge at the debtors were disguised had materialized in the four cases, the Committee considers that it was difficult for persons in charge at HCF to identify such risk before executing the transaction.

However, the Committee noted the following issues as a consequence of failing to sufficiently identify risks associated with the factoring business in China: The persons in charge at HCF had not necessarily confirmed the employee ID card or other identification card or obtained their copy because the location of meetings with the debtors were within the buildings or facilities of the debtors. Furthermore, HCF completely trusted the person who attended the meeting to be a true person in charge and had not necessarily conducted a process to confirm whether the said person at the meeting was a true person in charge at the debtor by, for example, making an inquiry to the debtor through a third party, instead of through the creditor.

For the four cases, there was a risk that forged documents might be submitted. However, the person in charge at HCF had failed to identify such risk, and to verify the authenticity of collected documents, including the verification of the authenticity of official and other seals affixed on the documents.

Section 2 There was room for enhancing the operational risk management framework

The debtors in the four cases were regarded as leading companies in their respective industries, with a substantial amount of assets.

In consideration of the creditworthiness of the debtors, in the four cases, large-scale transactions were executed from the first time.

However, as the creditors in the four cases were new customers with no historical business relationship with HCF, and unexpected fraud risk described in Section 1 above might have materialized. Therefore, HCF should have taken more prudent approach for the due diligence process for creditors, instead of focusing on the examination of creditworthiness, because unexpected fraud risk may materialize. Specifically, HCF should take measures by taking into account that operational risk[14], such as fraudulent acts with malicious intent, may materialize. Such measures may include limiting the amount of transactions executed at the inception of a service and gradually increasing this limit by assessing the status of transactions and payments. If such measures were taken, damages caused by the Fraud and other similar cases could have been reduced.

Section 3 The risk management system and related policies and procedures had not been designed to ensure that malicious fraudulent acts were prevented.

HCF has established internal rules and manuals for its factoring business, such as “(HCF)

[14] While the term “operational risk” is generally considered to include risk resulting from internal processes, people and systems or from external events, in this context, it refers to the risk related to losses that are difficult to predict, such as losses arising from acts attempting to commit fraudulent acts by a third party with a malicious intent, such as fraud or embezzlement.

Flow of Credit Risk Management," "Factoring Guidelines," "Operational Manuals Ver2.0,"[15] and "Operational Flows (Japanese) 20180913."

While these internal rules and manuals set out rules about the procedures to verify the identity of debtors and the authenticity of contracts that mitigate these risks to a certain extent, no procedure or know-how sufficient to prevent third parties from committing fraudulent acts with clear malicious intent, such as in the four cases were prescribed.

Documents to be obtained in executing the factoring service are determined based on various factors, such as the risk management policy adopted by the company, the details of the deal or transaction, and the nature of creditors and debtors and level of their cooperation in the deal and transaction. Therefore, it is impracticable to require, or unrealistic, to determine them uniformly.

Given that third parties may commit fraudulent acts with malicious intent, a potential measure would be to specify requirements related to documents to be obtained in internal rules (for example, mandate the process to obtain Fapiao (発票)) after consultation with HCF and HCL's management and HC.

[15] This manual initially set out that Fapiao (発票) should be obtained in executing a factoring transaction. However, this rule was eliminated as a result of the revision made around June 2017. This manual was developed by an employee of HCF to describe the credit examination procedures in place at HCF for in the purpose of training of new employees, and did not stipulate formal and ideal credit examination procedures to be conducted. Under HCF' actual credit examination procedures conducted when the manual was revised, the process to obtain Fapiao (発票) was not necessarily required. Therefore the revision of this manual was made to reflect such change in the practice and this revision to eliminate the process for obtaining Fapiao (発票) is not considered to be a cause for allowing the Fraud to be committed.

Chapter 5 Measures to enhance controls to prevent recurrence

Section 1 Fully implementing measures to ensure that HCF contacts true persons in charge at debtors

Due to the nature of the factoring, factors may be in a position difficult to make requests to debtors, and it may be difficult to contact directly with debtors and to arrange visits and interviews. This is particularly the case for debtors with no historical relationship.

Even in such a case, however, it is recommended to first attempt to contact a debtor through the Hitachi Group or its peer company, instead of through a creditor. Furthermore, even if an initial visit or interview is arranged through a creditor, it is advisable to ensure arranging second and subsequent visits and interviews through directly contacting the debtor.

When visiting and interviewing debtors, it is recommended to implement the procedure to examine the employee card or other identify card of a person in charge or an interviewee and obtain copies of them as much as possible. After the visit or the meeting, the interviewer should also conduct procedures to verify whether the interviewee is a true person in charge at the debtor by confirming with a peer company or directly confirming with the debtor through a third party.

In the Case A, as a result of conducting an interview with the person in charge at Company D arranged through a person other than the creditor, it was revealed that the person who had represented him/herself as a person in charge was not a true person in charge. To address such a risk, it is advisable to take the measures above for all transactions at an earlier stage.

Section 2 Ensuring to implement a process to verify the authenticity of obtained documents

As the Case A, Case C and Case D indicate, documents obtained from creditors and debtors are not necessarily authentic, and there is a risk that forged documents may be provided. Therefore, it is necessary for persons responsible for examining documents to thoroughly verify whether obtained documents are authentic, taking into account a risk that documents may be forged.

Specifically, if documents related to a debtor are obtained through a creditor, it is necessary to examine the authenticity of the documents by directly inquiring the debtor at a later date. In fact, for the Case A, Case C and Case D, as a result of confirming the authenticity of the documents with debtors, it was revealed that the documents had been forged. Therefore, it is necessary to conduct such process at an earlier stage.

In China, there is no system equivalent to the seal certification system in Japan or similar system for official seals. However, it is desirable to verify the authenticity of official seals by, for example, obtaining documents affixed with the official seal of debtors from peer companies and comparing the official seal with that affixed on the documents.

Section 3 Implementing measures for HCF's employees to gain an understanding about risks associated with the factoring business

As described in Chapter 4, Section 1, the Committee noted instances where some HCF employees had failed to fully recognize the risk that the person who represented him/herself as a person in charge at a debtor was not a true person in charge, or the risk that forged documents may be submitted in the factoring business in China. The lack of such risk awareness is, in part, due to a situation where know-how of the factoring business in China had not been accumulated and shared across the sector at a sufficient level because the factoring business in China had been deregulated relatively recently.
Therefore, it is recommended to collect risk information on fraud cases relating to the factoring business in China in cooperation with peer companies, and share methods used in these fraud cases with the persons in charge at HCF to strengthen their skill to identify risks. Furthermore, it would be useful to appoint local staff familiar with risks inherent in the financial business in China as Manager or Vice Manager of the Marketing & Strategy Section, Operating Section or other departments, who will be responsible for analyzing risks of the factoring business in China, and to assign the roles of providing guidance to and supervising persons in charge at HCF to these local staff.

Section 4 Enhancing the operational risk management framework

For a new customer, a fraud risk may materialize, albite rarely, such as doubts about the existence and authenticity of transactions, at the inception of a factoring transaction. Therefore, to ensure that risks are appropriately managed for the entire scheme of the transaction, it is necessary to enhance the operational risk management framework by taking into account that fraudulent acts by third parties with malicious intent, such as fraud and embezzlement, may be committed. Specifically, HCF needs to take measures to reduce losses incurred from the materialization of operational risk by requiring the following procedures: Conduct due diligence for creditors at the inception of a factoring transaction with a new customer and set a limit on the amount of the initial transaction, and gradually increase the limit based on the results of monitoring elements such as whether repayments are made by due dates and the frequency of requests for changing payment conditions and by comprehensively assessing risks associated with creditors and debtors.

Section 5 Developing internal rules and manuals, and establishing a system whereby HC can involve in the development of internal rules and manuals to the extent necessary.

As described in Chapter 4, Section 3 above, HCF's internal rules and manuals set out rules for verifying the identity of debtors and the authenticity of contracts. However, these rules and manuals do not include measures or know-how sufficient to detect third parties with clear malicious intent from committing fraud. As a result, procedures to verify the identity of debtors and the authenticity of contracts may not had been sufficiently implemented. It is therefore recommended to review the current verification procedures in light of the measures recommended in 1 and 2 above and specify the verification procedures in internal rules and manuals in a specific and clear manner to ensure that the verification of identity of debtors and the authenticity of contracts are sufficiently conducted to detect any fraud committed by a third party with clear malicious intention.

Moreover, as Fapiao (発票) is centrally managed by the Value Added Tax (増値税) Management System of tax authorities, the authenticity of Fapiao (発票) obtained can be verified by accessing this system. As such, Fapiao (発票) is considered to be an important supporting document to verify the existence of a transaction relative to other supporting documents such as a shipping list and acceptance note. In designing HCF's risk management, there may be options to either adopt an approach to mandate the process to obtain Fapiao (発票) or an approach to allow using other supporting documents when Fapiao (発票) cannot be obtained due to an unavoidable reason. Given the importance of Fapiao (発票) as a supporting document, HC should be involved in determining a policy and developing internal rules and/or manuals, regardless of which option is adopted.

However, at HCF, HC was not involved in establishing rules on Fapiao (発票). Therefore, it is recommended to establish a system that ensures the involvement of HC. Specific measures would be to clarify authorities of approving internal rules and manuals and disseminate these authorities within HCF so that HC can be engaged in developing significant internal rules where necessary.