

# 5

## Governance

Governance

> **Corporate Governance**

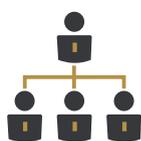
Compliance

Risk Management

Information Management

Governance Data

# Hitachi Sustainability Report 2021

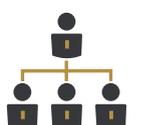


## Corporate Governance GRI 103-2

### Why

— Why it matters —

Hitachi views the expansion of long-term and overall shareholder returns as an important management objective. Hitachi, Ltd. and Hitachi Group companies maintain good relationships with a wide range of stakeholders, and we recognize that these relationships make up an important part of our overall corporate value. Accordingly, we are striving to establish a system that will facilitate the maintenance of these relationships and improve our corporate value primarily through the implementation of measures focused on promoting constructive dialogue.



### Corporate Governance

### What

— What we are doing —

- Implementing all of the principles of the Corporate Governance Code
- Conducting board meetings in a way that sustainably enhances corporate value and shareholders' common interests
- Approving and dismissing the CEO and formulating a succession plan
- Determining appropriate compensation for directors and executive officers
- Implementing internal controls over financial reporting
- Enhancing collaboration through tripartite audits
- Building a more effective and efficient auditing system

### How

— How we are doing it —

Policy and promotion structure	Hitachi, Ltd. adopted its current committee system in 2003 and has established an Audit Committee, Compensation Committee, and Nominating Committee. Independent directors chair these committees and comprise the majority of the members. The company has also created a system that enables sufficient exercise of supervisory functions by separating the execution and supervision of business management.
<b>Achievements in Fiscal 2020</b>	
Ensuring legality, soundness, and transparency of Hitachi's business	Analyzed and evaluated the effectiveness of the Board of Directors
Reviewing executive compensation systems	To achieve carbon neutrality at Hitachi business sites (factories and offices) by fiscal 2030, Hitachi, Ltd. reviewed a system of evaluation taking environmental performance into consideration in executive officers' short-term incentive compensation and decided to introduce it in fiscal 2021. <hr/> A restricted stock compensation unit system was introduced as compensation for non-Japanese executive officers and corporate officers in fiscal 2020, and the scope of was expanded to executives at some Group companies In fiscal 2021.

## 5

## Governance

Governance

&gt; Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

## Corporate Governance

GRI 405-1

Hitachi views the expansion of long-term and overall shareholder returns as an important management objective. Hitachi, Ltd. and Hitachi Group companies maintain good relationships with a wide range of stakeholders, and we recognize that these relationships make up an important portion of our overall corporate value. Accordingly, Hitachi are striving to establish a system that will facilitate the maintenance of these relationships and improve our corporate value primarily through the implementation of measures focused on promoting constructive dialogue. To advance these efforts effectively, we are working to improve our corporate governance by ensuring thorough separation between the oversight and execution of management, establishing a swift business execution system, and striving to achieve highly transparent management.

## History of Hitachi's Corporate Governance Reform

Structure Activities

- |   |   |
|---|---|
| <p><b>1999</b> ● Introduction of Objective Perspective Management Advisory Committees<br/>▶ Practical advice from experts in Japan and overseas</p> <p><b>2003</b> ● Demarcation of Management Oversight and Execution<br/>Shifted to a company with committees (currently a company with nominating committee, etc.)<br/>▶ To increase management speed and improve management transparency</p> <p><b>2006</b> ● Enforcement of Revised Companies Act</p> <p><b>2010</b> ● Enhancement of Interactions with Capital Markets<br/>Hitachi IR Day (briefing on business strategy by division) was launched<br/>▶ Clarification of commitment of top management of the business units to the capital markets</p> <p><b>2012</b> ● Acceleration of Global Management<br/>Independent directors including foreign directors were increased<br/>Independent directors comprised the majority of directors</p> | <p><b>2012</b> ● Development of Guidelines for Strengthening Governance<br/>Development of Corporate Governance Guidelines</p> <p><b>2014</b> ● Development of Stewardship Code</p> <p><b>2015</b> ● Start of Application of Corporate Governance Code</p> <p><b>2016</b> ● Enhancement of Dissemination of Information about Medium- to Long-term Sustainable Growth<br/>Publication of an integrated report</p> <p><b>2019</b> ● Acceleration of the Social Innovation Business across 5 Growth Fields<br/>Executive vice presidents were placed in 5 sectors<br/>ESG briefing session held<br/>▶ An independent director (chair of the Audit Committee) and the CEO shared their remarks</p> |
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## Implementing All the Principles of the Corporate Governance Code

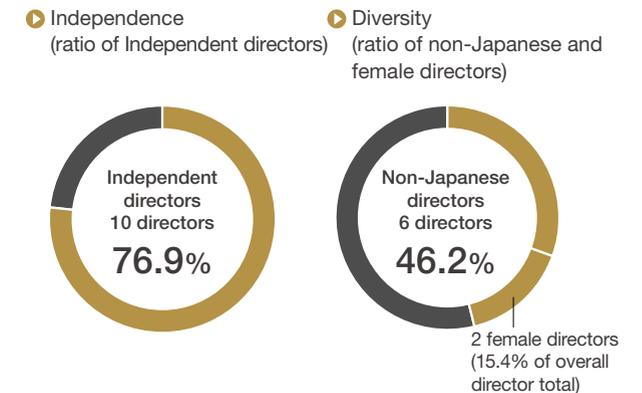
Policy Activities

GRI 102-22

We are implementing all the principles of the Corporate Governance Code.

## Director Composition

Structure



## Directors with Abundant Experience

The Board of Directors applies their abundant experience and knowledge related to the management of global companies, legal affairs, accounting, capital markets, government agencies, and the field of digital technology to facilitate discussions informed by a wide variety of perspectives.

In June 2021, Helmuth Ludwig joined the Audit Committee and Joe Harlan joined the Compensation Committee, enabling even more diverse discussions

# 5

## Governance

Governance

> Corporate Governance

Compliance

Risk Management

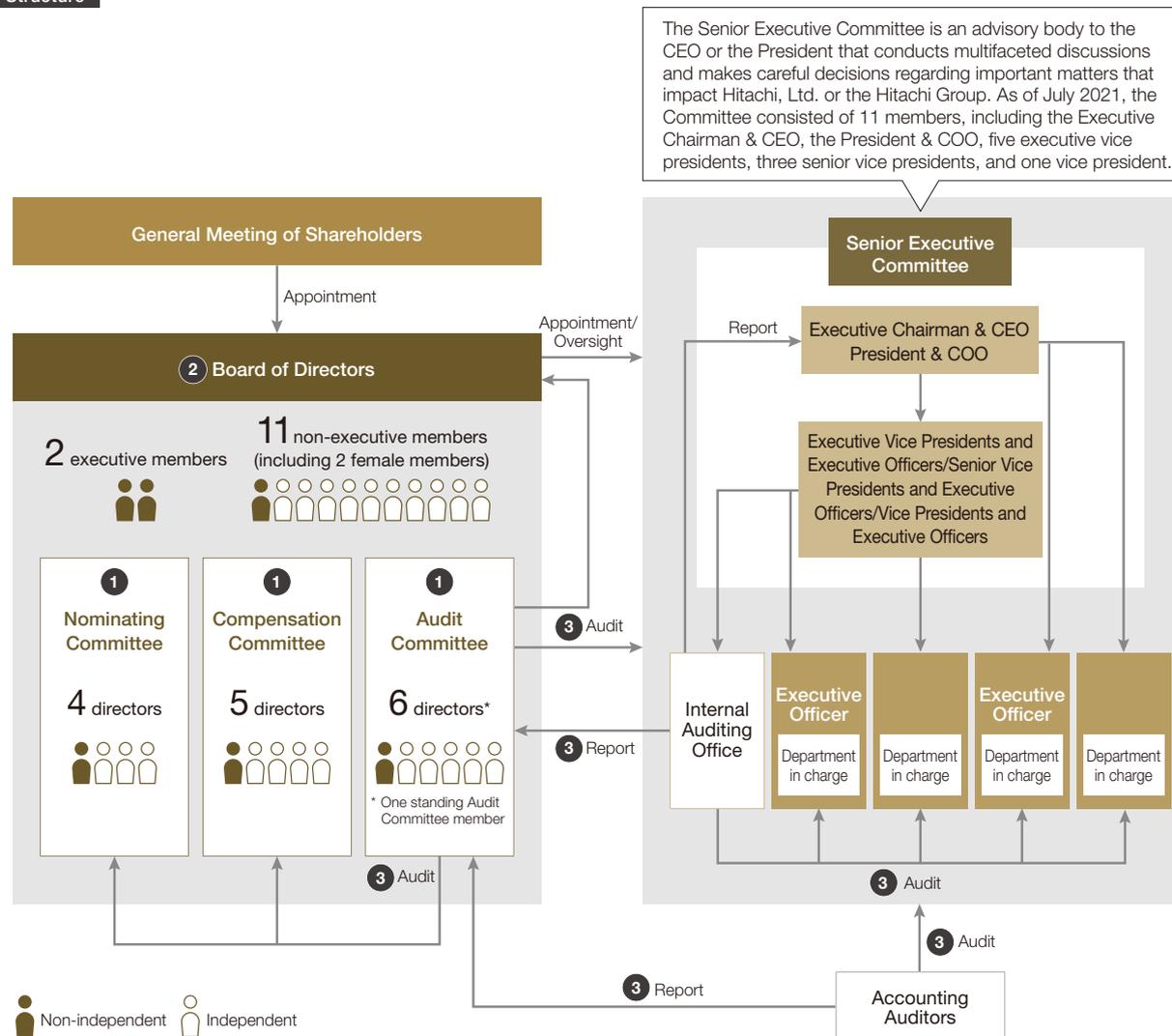
Information Management

Governance Data

### Hitachi's Corporate Governance Framework and Its Features

GRI 102-18/102-22/102-23/102-24

**Structure**



The Senior Executive Committee is an advisory body to the CEO or the President that conducts multifaceted discussions and makes careful decisions regarding important matters that impact Hitachi, Ltd. or the Hitachi Group. As of July 2021, the Committee consisted of 11 members, including the Executive Chairman & CEO, the President & COO, five executive vice presidents, three senior vice presidents, and one vice president.

**POINT 1** Transparency in Management

We became a company with committees (currently a company with a nominating committee, etc.) in 2003. We have established the Nominating Committee, the Compensation Committee, and the Audit Committee, which are mostly made up of, and are chaired by, independent directors. The system we have in place to ensure transparency in management separates the oversight and execution of management, facilitates the full exercise of supervisory functions, and enables discussions and reports to be conducted appropriately within these three committees.

**POINT 2** Independence of the Board of Directors

We increased our number of independent directors, including non-Japanese directors, in 2012. Our Board of Directors, which is chaired by an independent director, has 13 members, including 10 independent directors, two directors who are also serving as executive officers, and one director who is not serving as an executive officer. In addition, we have established a system that facilitates the full exercise of supervisory functions by maintaining separation between the oversight and execution of management.

**POINT 3** Enhanced Collaboration through Tripartite Audits

Hitachi's Audit Committee and internal audit section collaborate with third-party accounting auditors to strengthen its "Tripartite Auditing," which aims to increase the effectiveness of internal controls.

## 5

## Governance

Governance

&gt; Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

Hitachi  
Sustainability  
Report  
2021

## Administrative Performance of the Board of Directors

## Structure Activities

The Board of Directors approves basic management policy for the Hitachi Group and supervises the execution of the duties of executive officers and directors in order to sustainably enhance corporate value and the shareholders' common interests. The basic management policy includes the Mid-term Management Plan and annual budget compilation. The Board of Directors focuses on strategic issues related to the basic management policy, as well as other items to be resolved that are provided in laws, regulations, the Articles of Incorporation, and the Board of Directors Regulations.

Within the Board of Directors, there are three statutory committees—the Nominating Committee, the Audit Committee, and the Compensation Committee—with independent directors accounting for the majority of members of each committee. The Board of Directors meetings were held on nine days during fiscal 2020, and the attendance rate of directors at these meetings was 100%. The attendance rates for each independent director were as shown in the table below. To assist with the duties of the Board of Directors and each committee, staff who are not subject to orders and instructions from executive officers are assigned.

## Attendance at the Board of Directors meetings held in fiscal 2020

Name	Attendance/Number of days on which the meetings were held*			
	Board of Directors	Nominating Committee	Audit Committee	Compensation Committee
Katsumi Ihara	100%	—	100%	100%
Ravi Venkatesan	100%	—	—	—
Cynthia Carroll	100%	100%	—	—
Joe Harlan	100%	—	—	—
George Buckley	100%	—	—	—
Louise Pentland	100%	—	—	—
Harufumi Mochizuki	◎100%	◎100%	100%	◎100%
Takatoshi Yamamoto	100%	—	100%	100%
Hiroaki Yoshihara	100%	100%	◎100%	—
Helmuth Ludwig	100%	—	—	—

\* Number of days during term of office on which the Board of Directors meetings were held: 9; Mr. Venkatesan and Mr. Ludwig: 6

Number of days during term of office on which Nominating Committee meetings were held: 8

Number of days during term of office on which Audit Committee meetings were held: 17

Number of days during term of office on which Compensation Committee meetings were held: 4

◎Indicates role as a board or committee chairperson

## Description of the three committees' activities

## Activities

## Nominating Committee

The Nominating Committee has the authority to determine proposals submitted to the general meeting of shareholders for the election and dismissal of directors. The Nominating Committee consists of four directors, three of whom are independent directors.

It determines director candidates and holds preliminary hearings concerning the appointment and dismissal of executive officers, including the CEO.

In fiscal 2020, the Nominating Committee held meetings on eight days.

## Primary Activities

In addition to deciding upon the contents of the proposal made concerning director appointments at the Annual General Meeting of Shareholders, the Nominating Committee set an upper limit on the total term of office for independent directors and reviewed and confirmed the executive officer system implemented in fiscal 2021. In addition, it promoted committee-related activities including discussions and individual interviews aimed at developing candidates for future management and leadership positions.

## Audit Committee

The Audit Committee has the authority to audit the execution of duties of directors and executive officers and to decide on proposals submitted to the general meeting of shareholders for the election and dismissal of accounting auditors. The Audit Committee currently consists of six directors, including five independent directors and one standing Audit Committee member.

Hiroaki Yoshihara, the chairman of the Audit Committee, has been involved in accounting and other business practices at the KPMG Group for many years and possesses a considerable breadth of knowledge concerning finance and accounting.

In fiscal 2020, the Audit Committee held meetings on 17 days.

## Primary Activities

The Audit Committee conducted activities that were focused on its priority matters for consideration, which included the strengthening of collaboration and the facilitation of information sharing under a "Tripartite Audit" (audit by the Audit Committee, internal audit and audit by accounting auditors), and auditing of the establishment and operation of internal control systems from the perspective of risk management and validity of execution of duties. In addition, a standing committee member worked to obtain information as needed in a timely and accurate manner, mainly by collaborating with the Internal Auditing Office, among other departments, and attending important internal meetings such as the Senior Executive Committee, and facilitated information sharing with other committee members.

## Compensation Committee

The Compensation Committee has the authority to determine remuneration policies for directors and executive officers and remuneration for individuals (including amounts of remuneration) based on them. Currently composed of five directors, including four independent directors, the committee strives to ensure objectivity, transparency, and fairness in the remuneration determination process.

In addition, the Compensation Committee verifies and reviews details of the process used for determining remuneration for individuals, including assessments concerning basic remuneration amounts, evaluations of progress made toward individual targets, and performance appraisals that are tied to short-term incentive compensation.

In fiscal 2020, the Compensation Committee held meetings on four days.

## Primary Activities

The Compensation Committee determined remuneration amounts for individual directors and executive officers in accordance with established policies while verifying and reviewing the processes and results of appraisals for performance and individual targets tied to short-term incentive compensation for executive officers. In addition, the committee reviewed the executive compensation system while giving due consideration to compensation granted to managers at global companies and the goal of sharing value with shareholders, and decided upon policies covering remuneration for directors and executive officers in fiscal 2021.

## 5

## Governance

Governance

&gt; Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

## Analysis and Evaluation of the Effectiveness of the Board of Directors

## Activities

GRI 102-28

The Company evaluates the effectiveness of its Board of Directors each year in a continuous effort to maintain and improve its functions.

## ▶ Fiscal 2020 Evaluation Process

	Points of evaluation
1. Questionnaire-based self-assessment by each director (February–March 2021)	<ul style="list-style-type: none"> <li>● Composition: Diversity on the Board, the number and proportion of Inside and Outside Directors, etc.</li> <li>● Visibility of responsibilities and roles of the Board</li> <li>● Meeting operation: Meeting frequency, deliberation time, agenda setting, quality of deliberation, Chairman's role, etc.</li> <li>● Contribution: Contribution to strategy building and change of company culture, contribution to have constructive discussions, utilization of Director's knowledge and experience, discussions based on taking the Digital Transformation, etc.</li> <li>● Understanding of the Company: Hitachi Group Identity, risk factors, potential challenges and opportunities.</li> <li>● Three committees: Composition, responsibilities and roles, coordination with the Board, etc.</li> <li>● Supporting system for the Board: Provision of necessary information such as the Board materials, etc.</li> </ul>
2. Discussions among independent directors (March 2021)	<ul style="list-style-type: none"> <li>● Independent directors had a meeting and discussed the Board effectiveness there.</li> </ul>
3. Discussions at the Board meeting (May 2021)	<ul style="list-style-type: none"> <li>● The Board analyzed and evaluated its effectiveness as a whole and confirmed the policy on approaches to further enhance the Board's effectiveness based on the results of the preceding process, considering comparison to the evaluation results for fiscal 2018 and measures taken for improving its effectiveness in fiscal 2020.</li> </ul>

## ▶ Evaluation Results and Future Initiatives

	Evaluation Results
Overall evaluation in fiscal 2020	<ul style="list-style-type: none"> <li>● The Board assessed that the Board members are diverse and make use of their knowledge and expertise to speak out, having vigorous discussions especially on matters related to business strategies such as the mid-term management plan toward mid/long-term growth of corporate value. The Board, therefore, concluded that the effectiveness of the Board as a whole is maintained.</li> </ul>
	Future initiatives
Further enhancement of corporate governance	<ul style="list-style-type: none"> <li>● Examine the discussion process for strategy discussions based on a mid to long term perspective and establish a time and forum for deepening discussions.</li> <li>● Business strategy reports and discussions at Board meetings will continue to be implemented on a Sector by Sector basis, and discussions will focus on strategy, such as a risk matrix based on factors such as the standing of the Company, the status of competitors, technology, talent, finance and Lumada strategy.</li> <li>● Risk management, ESG and Investor relations will be submitted as agenda items as important matters for improving long term corporate value.</li> <li>● The Board will attempt to strengthen a relationship with the Nominating Committee and further contribute to succession planning of CEO (e.g. enhancement of Nominating Committee's reports to the Board, one-on-one meeting with CEO successor candidates and next generation leader candidates).</li> </ul>
Enhancement of supporting system for the Board and improve practical issues in operations	<ul style="list-style-type: none"> <li>● Post COVID-19, restarting to provide Independent Directors with information on opportunities of visiting sites and events of Hitachi Group.</li> <li>● Further improve structure and contents of materials for the Board meeting and operation of provision of materials well in advance of the Board meeting.</li> </ul>

# 5

## Governance

Governance

> Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

# Hitachi Sustainability Report 2021

### CEO Appointment, Dismissal, and Succession Plan

Structure

GRI 102-24

Hitachi's Board of Directors decides upon the appointment and dismissal of executive officers, including the CEO, with the goal of constructing an optimal business execution system for management. Decisions regarding the appointment or dismissal of executive officers are based on proposals from the Nominating Committee. As stipulated in our Corporate Governance Guidelines, our basic policy concerning the CEO requires that individuals serving in the position of CEO have extensive experience and achievements in the field of company management. They must also be considered optimally suited for conducting management aimed at achieving Hitachi's goals of continuously raising its corporate value and further serving the common interests of its shareholders. Decisions regarding the appointment or dismissal of the CEO shall be made based on prior deliberations and proposals by the Nominating Committee.

Regarding our CEO Succession Plan, as the speed of change in the management environment accelerates, we are striving to build a system that enables us to appropriately and promptly secure and develop (both internally and globally) necessary management personnel who will provide leadership that will allow us to realize our growth strategies. Accordingly, we are also concentrating on providing training for selected employees while targeting the early development of candidates for future management positions. Moreover, we are developing next-generation leaders capable of acting authoritatively and resolutely by establishing forums where participants can discuss what is necessary for Hitachi's

future growth and make recommendations to management.

In addition, we have identified a group of about 50 employees from around the Hitachi Group with next-generation development potential. People in this "Future 50" group are selected on merit, regardless of age, gender, or nationality. They are given challenges to help expand their horizons and build their perspectives through tough assignments including different types of work and internal and external training opportunities. The Future 50 group members receive one-on-one mentoring opportunities with independent directors to benefit directly from their extensive business experience and global perspectives. Our aim is to change mindsets so that we can develop people for important positions in the future.

### Director and Executive Officer Compensation

GRI 102-35/102-36

Basic Policy

- Compensation shall be such that it enables the Company to attract necessary personnel to achieve an improvement in corporate value through global business growth.
- Compensation shall be commensurate with the roles and responsibilities of each Director and Executive Officer.
- Compensation for Directors shall be such that it enables them to exercise the functions of supervision of management effectively.
- Compensation for Executive Officers shall be such that it enables them to contribute to sustained improvement in corporate value through the execution of business and employs an appropriate balance between short-term performance and medium- and long-term performance.
- The level of compensation shall be determined considering compensation levels at other companies as well as economic and market trends.
- The Compensation Committee utilizes external experts to gain expert advice and an objective viewpoint, if necessary, for considering the details and amounts of compensation.

### Compensation Structure

#### (1) Directors

Compensation for Directors is basic remuneration as fixed pay. The amount of basic remuneration is decided by adjusting a basic amount to reflect full-time or part-time status, committee membership and position, and travel from place of residence, etc. A Director concurrently serving as an Executive Officer is not paid compensation as a Director.

#### (2) Executive Officers

Compensation for Executive Officers consists of basic remuneration as fixed pay and short-term incentive compensation and medium- and long-term incentive compensation as variable pay.

The basic amount of basic remuneration, short-term incentive compensation and medium- and long-term incentive compensation is set based on the ratio of 1:1:1 as the standard, taking into account the composition of executive compensation for major global companies, in order to improve corporate value through the growth of global businesses. The higher position Executive Officer hold, the higher proportion of variable pay is set to the total annual compensation.

As part of efforts to achieve carbon neutrality at Hitachi business sites (factories and offices) by fiscal 2030, in fiscal 2021, an evaluation system that considers environmental value was introduced into short-term incentive compensation for executive officers. Specifically, targets are set for environmental strategies and solutions to environmental issues based on the divisions and operations handled by each executive officer, and performance is evaluated according to the degree of target achievement.

If it is found that an executive officer has been engaged in misconduct during his/her term of office, compensation for Executive Officers that has been already paid shall be returned to the Company (clawback provision).

[Annual Security Report \(the 152nd Business term\), P101 Compensation to Directors and Executive Officers](#)



# 5

## Governance

Governance

> Corporate Governance

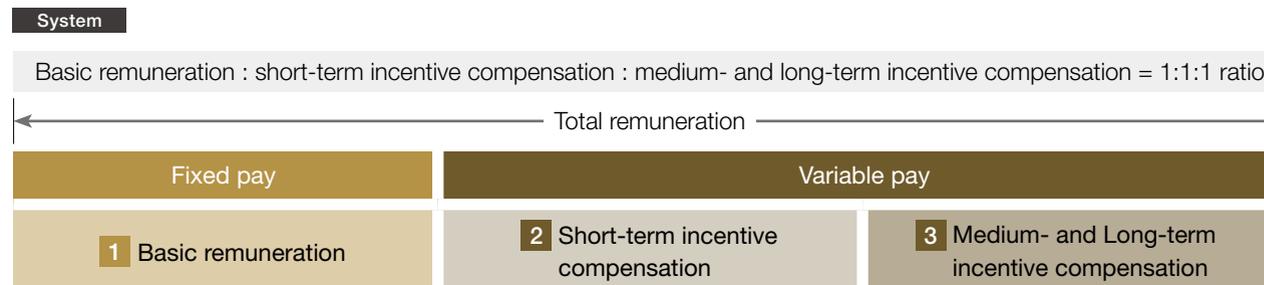
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Risk Management

Information Management

Governance Data

### Compensation to Executive Officers (Fiscal 2021)



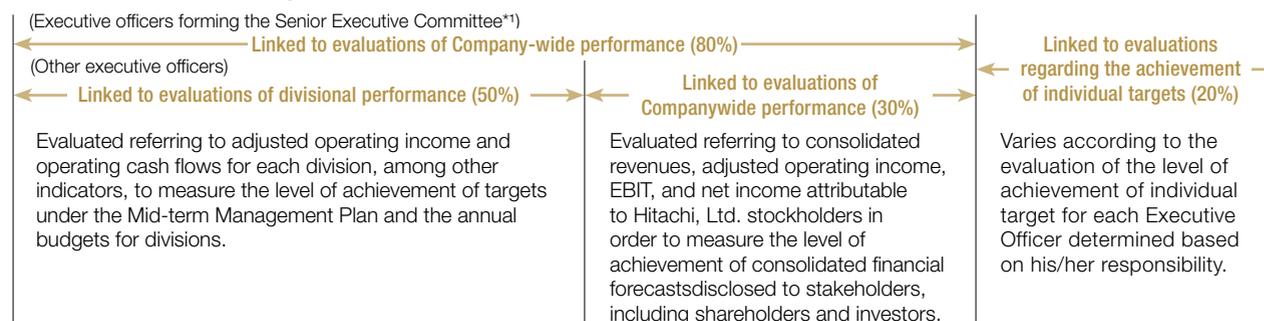
GRI 102-35/102-36

#### 1 Basic remuneration

Set according to the relevant position by adjusting that amount to reflect financial results and individual performance.

#### 2 Short-term incentive compensation

The amount of short-term incentive compensation is decided within the range of 0 to 200% of a basic amount set according to the relevant position by adjusting that amount to reflect financial results and individual performance.



\*1 The rates used for "other executive officers" apply when "executive officers forming the Senior Executive Committee" are in charge of sector or business units.

#### 3 Medium- and Long-term incentive compensation

Shares of restricted stock were introduced in fiscal 2019 as compensation for Japanese executive officers and corporate officers (the executive positions next to Executive Officers) to propel management from a medium- and long-term perspective and to provide incentives to bring about a sustainable increase in enterprise value by further promoting senior management's shared values with shareholders through the holding of shares during their term of office. In fiscal 2020, a restricted stock compensation unit system\*1 was introduced as compensation for non-Japanese executive officers and corporate officers. In fiscal 2021, the scope of the restricted stock compensation unit system was expanded to executives at some Group companies.

#### The shares of restricted stock

- The restriction on transfer shall be lifted if executive officers resign from all of the positions of the Company's executive officer, director, and corporate officer.
- With regard to one-half of the granted shares of restricted stock, the number of shares whose transfer restriction is lifted shall be determined after ex-post evaluation. In the ex-post evaluation, the total shareholder return (TSR) of Hitachi stock over the three years from the beginning of the fiscal year when the medium- and long-term incentive compensation is granted is compared with growth rate of TOPIX over the same period.

TSR/TOPIX growth rate	Shares for which the transfer restrictions are lifted
120% or more	Transfer restrictions are lifted for all granted shares.
Between 80% or more but less than 120%	Transfer restrictions are lifted for part of granted shares*2.
Less than 80%	No granted shares have transfer restrictions lifted.

\*1 A system in which restricted stock compensation units are granted to the eligible persons, and over three years from the start of the business year in which the restricted stock compensation units were granted, one-third of the number of restricted stock compensation units granted is paid in each fiscal year that passes, as Hitachi stock or cash.

\*2 Number of shares whose transfer restrictions are lifted = Number of granted shares × {(TSR/TOPIX Growth Rate Ratio × 1.25) - 0.5} Shares whose transfer restrictions are not lifted shall be acquired by Hitachi without consideration.

# 5

## Governance

Governance

> Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

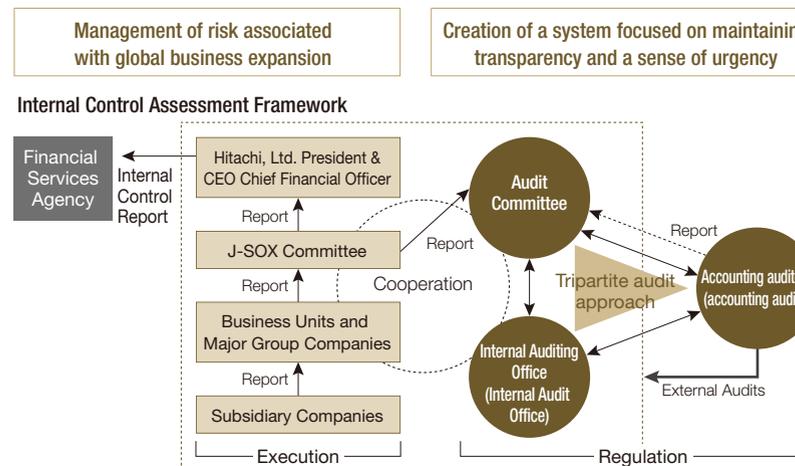
# Hitachi Sustainability Report 2021

### Internal Control over Financial Reporting

#### Structure

To ensure the reliability of its consolidated financial reporting, the Hitachi Group is establishing and implementing relevant internal controls. We evaluate their effectiveness by adhering to standards for the evaluation of internal controls related to financial reporting that are generally accepted as fair and reasonable.

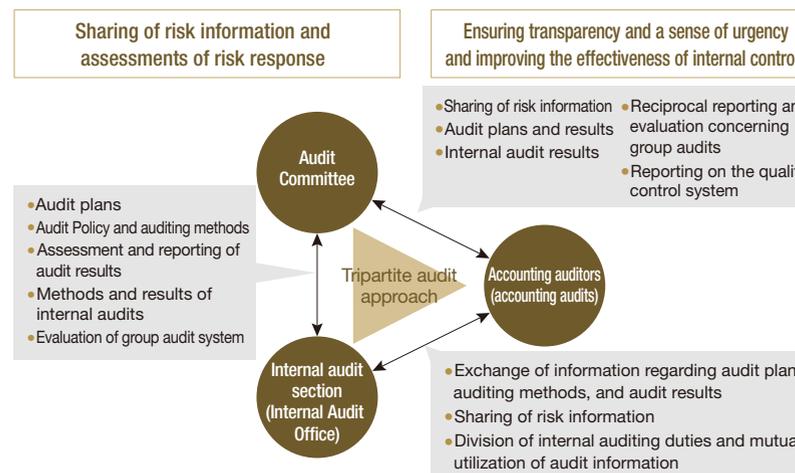
Furthermore, we have established the J-SOX Committee with the goal of raising the effectiveness of these internal controls. This committee evaluates internal control effectiveness and establishes frameworks designed to improve and strengthen them.



### Enhanced Collaboration through Tripartite Audits

#### Structure

In pursuit of sustainable growth in corporate value, Hitachi's Audit Committee and internal audit section collaborate with third-party accounting auditors to strengthen its "Tripartite Auditing," which aims to increase the effectiveness of internal controls. Our Audit Committee takes the lead in this regard, as the three parties communicate closely to share risk information and assessments concerning risk response while securing transparency and ensuring appropriate checks and balances.



### Building a More Effective and Efficient Auditing System

#### Structure

GRI 102-11/102-19

Our Audit Committee formulates audit plans in accordance with its risk-based approaches and conducts audits for each consolidated business unit. Audit Committee members meet directly with business unit heads before the internal audit section's audits are carried out. Then, these members inform the internal audit section about concerns and issues related to the implementation of business strategies aimed at achieving sustainable growth that require attention. At that time, the committee also verifies matters that carry high levels of risk in terms of quality, measuring these risks through employee awareness surveys and thorough implementation of business strategies.

Hitachi's internal audit section performs regular internal audits at each business site and location. This section reports directly to the President and is independent from organizations that are subject to its audits. The internal audit section also formulates audit plans based on past audit records and the most recent business circumstances. In addition, this section performs audits upon receiving direction from the Audit Committee, ensuring their effectiveness. The internal audit section at Hitachi is responsible for confirming the legality and appropriateness of all business operations, including those related to accounting, production management, sales, purchasing, IT systems, compliance, and human resources. Furthermore, acting on behalf of our management team, the internal audit section confirms whether the employees are well versed in the ideas and policies of our management, and their operations are being carried out based on these ideas and policies and if business strategies are being implemented in a way that will efficiently lead to sustainable growth.

To further raise audit effectiveness, we implemented a

## 5

## Governance

Governance

&gt; Corporate Governance

Compliance

Risk Management

Information Management

Governance Data

“chief auditor system” in each of our five sectors (IT, Energy, Industry, Mobility, Smart Life) in April 2019. Through this action, we built an internal control system spearheaded by chief auditors and enhanced collaboration with the executive vice presidents who manage each sector and with the Audit Committee.

Although these chief auditors do not act as legal agents under the Companies Act, they still assume responsibility for governance in each sector. Statutory auditors, which function as legal agents at Hitachi subsidiaries under the Companies Act, also report to these chief auditors and work to improve the effectiveness of Hitachi’s internal control systems.

When conducting business audits, we use IT systems to expeditiously search for reference information contained within materials submitted prior to audit in an attempt to improve efficiency. We are currently enhancing a system that will allow our internal audit section to share information with professional accounting auditors using a data lake. When reading audit reports submitted to the President by the internal audit section, the President must be able to quickly understand the issues identified by these reports and make prompt judgments concerning whether immediate action is required. In the future, our internal audit section will continue to maintain its transparency and independence while working to improve audit efficiency as one member of our Tripartite Audit system.

Our accounting auditors perform audits that focus on the accuracy and reliability of our financial statements. First, they adopt a risk-based approach in response to the Group’s overall financial status. Applying this approach, they then determine the scope and methods of the audit, formulate an audit plan, and share opinions with the Audit Committee. Next, based on the audit plan, they perform audits on each of the five sectors and the business units that comprise them, enabling effective and efficient understanding of data related to Hitachi’s finance department and each of its business segments. If, during the auditing process, our

accounting auditors discover a degree of risk that could impact future financial statements significantly or issues that, even if monetarily small, could have a large qualitative effect, they share related information regarding these risks and issues and the progress on a response from the related divisions with the Audit Committee and internal audit section. They also work to improve and raise the effectiveness of audits by submitting “management letters” containing points of concern and improvement suggestions through the finance department. Recently, they have also been working to raise the efficiency of checks on the accuracy of numerical figures by using some IT systems to investigate all cases rather than performing test-checking through sampling.