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News Release
(translation)

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Notice of material deficiencies subject to disclosure in internal controls systems related to financial reporting

Fukoku Co., Ltd. (“Company” hereinafter) submitted the Internal Controls Report for the fiscal year ended March 31, 2025 to the Kanto Local Finance Bureau on June 23, 2025, pursuant to Article 24-4-4, Paragraph 1 of the Financial Instruments and Exchange Act of Japan, in which it identified material deficiencies subject to disclosure and noted that the Company’s internal controls systems related to financial reporting were ineffective, as outlined below.

Details

1. Details of material deficiency subject to disclosure

In response to suspicions of embezzlement at consolidated subsidiary Shanghai Fukoku Rubber & Plastics Industry Co., Ltd. (“Shanghai Fukoku” hereinafter) by a Shanghai Fukoku employee in charge of administering receipts and disbursements (“subject employee” hereinafter), as identified in internal investigations undertaken in response to the recognition of marked discrepancies between budgeted vs. actual figures in an analysis of monthly financial data at Shanghai Fukoku, on November 29, 2024, the Company established an investigation committee consisting of neutral and impartial outside experts independent of the Company (“Special Investigation Committee” hereinafter). This Special Investigation Committee was tasked to investigate the facts of the matter and to look for comparable cases; to analyze the factors leading to the incident; and to propose preventive measures to prevent the recurrence of such incidents.

The Company received a report on the investigation by the Special Investigation Committee on February 14, 2025. The report stated that, starting several fiscal years before, an employee at Shanghai Fukoku had engaged in improper withdrawals of cash and deposits and recorded fraudulent expenses paid to hide these actions. Specifically, the subject employee had, on repeated occasions, abused assigned responsibilities involving the administration of receipts and disbursements, preparing, in each case, falsified ledgers to make improper withdrawals of company funds for personal use appear legitimate.

Due to its location, Shanghai Fukoku faces chronic difficulties in securing employees. The proximate causes of this case are recognized to be the following: the inadequacy of internal controls on accounting processes, including the fact that the subject employee's position made it possible independently to withdraw funds from deposit accounts using checks; a state of affairs in which a single individual had, for a long time, been tasked with receipts and disbursements and with their recording; the long tenure of personnel assignments in positions such as finance manager and vice president; and insufficient awareness of the nature of improprieties on the part of the subject employee. The background factors identified include perfunctory implementations of Shanghai Fukoku's governance structure, and the Company's organizational culture that failed to approach internal controls with sufficient seriousness; structural laxity in managing subsidiaries; inadequate evaluations of the risk of improprieties; and inadequate internal audit procedures.

The deficiencies recognized to have resulted from the above causes have been determined to be material deficiencies subject to disclosure, since they significantly affect the integrity of financial reporting. The details of the material deficiencies subject to disclosure are provided below.

- (1) Material deficiencies subject to disclosure in Shanghai Fukoku's companywide internal controls
 - Perfunctory implementation of governance, centered on the board of directors
 - Shortcomings in management and internal controls related to human resource assignments
 - Inadequacies in checks related to the evaluation and control of the risk of improprieties
 - Inadequacies in everyday business process inspections and monitoring
 - Deficiencies in independent evaluations of internal audits related to the risk of improprieties and business processes
- (2) Material deficiencies subject to disclosure in Shanghai Fukoku's settlement of accounts and financial reporting processes including payment processes
 - Inadequate risk evaluations and recognition in accounting rules and related procedures
 - Inadequate risk evaluations and recognition in human resource assignments and the division of responsibilities of Finance Department
- (3) Material deficiencies subject to disclosure in internal controls of the Company overall
 - Inadequate promulgation of policies on internal controls and systems development within the Group
 - Inadequate consideration of the adequacy of human resource assignments from the perspectives of administration and internal control functions
 - Inadequate evaluation of the risk of improprieties at subsidiaries
 - Inadequacies in procedures for monitoring and internal audits of subsidiaries

2. Why these matters could not be resolved by the end of the business year

These matters could not be resolved by the end of the business year due to the inability to secure the time needed to implement improvements within the timeframe from the discovery of the facts to the end of the business year.

3. Addressing the material deficiencies subject to disclosure

Recognizing the importance of internal controls related to financial reporting, the Company will swiftly develop and implement appropriate internal controls by promoting the following preventive measures based on the Special Investigation Committee's report:

(Preventive measures)

(1) Reorganizing the Shanghai Fukoku administration system

- (i) Establishing internal controls in accounting processes
- (ii) Implementing personnel-related risk management
- (iii) Providing training and education on the risk of improprieties and the importance of internal controls
- (iv) Enhancing governance structures under Chinese corporate law

(2) Providing support for and monitoring the formulation and implementation of preventive measures at Shanghai Fukoku

The Company's administrative sections and Internal Audit Office will provide on-site support and monitoring at quarterly intervals.

(3) Strengthening governance structures Groupwide

- (i) Detailed risk evaluations for each subsidiary
- (ii) Checks and balances established based on on-site inspections of the status of internal controls
- (iii) Enhancements and advances in financial data analysis by Finance Department and Business Strategy Office
- (iv) Support by related sections for establishing internal controls
- (v) Incorporating risk evaluations into subsidiary personnel management
- (vi) Enhancing training and education for management human resources dispatched from the Company to overseas facilities
- (vii) Utilization of intermediate management coordination organizations (area headquarters, etc.)

4. Impact on consolidated and nonconsolidated financial statements

All revisions made necessary by the above material deficiencies subject to disclosure have been reflected in consolidated and nonconsolidated financial statements.

5. Audit opinion expressed in audit report on consolidated and nonconsolidated financial statements

Unqualified opinion