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Mitsubishi Electric Announces Results of Internal Investigation Regarding Overcharged Expenses and Countermeasures

Tokyo, December 21, 2012 – [Mitsubishi Electric Corporation](#) (TOKYO: 6503) today issued a report on the results of its internal investigation and resulting countermeasures regarding the overcharging of expenses by its Electronic Systems Group to Japan's Ministry of Defense (MOD), the Cabinet Satellite Intelligence Center (CSICE), the Japan Aerospace Exploration Agency (JAXA), the National Institute of Information and Communications Technology (NICT) and the Ministry of Internal Affairs and Communications (MIC).

All Mitsubishi Electric Group executive officers and employees are committed to working together to prevent any recurrence and to restore public trust.

Mitsubishi Electric separately announced today that it expects to record a reserve to refund overcharged expenses for contracts with MOD, CSICE, JAXA and NICT. The company has also revised its financial results forecast for the current fiscal year ending March 2013.

Links to related announcements today:

- [*Mitsubishi Electric to Record Reserve for Refund Payments Resulting from Overcharged Expenses on Certain Contracts with Four Public Entities*](#)
- [*Mitsubishi Electric Announces Revised Consolidated Earnings Forecast for Fiscal 2013 \(April 1, 2012-March 31, 2013\)*](#)

Background

On January 17, Mitsubishi Electric received inquiries from MOD, CSICE and JAXA regarding costs accrued by the company's Kamakura Works. An internal investigation revealed that in certain projects expenses had been overcharged by shifting work records between different orders. On January 27, Mitsubishi Electric notified MOD, CSICE and JAXA of its findings and subsequently launched a detailed investigation. The company also investigated the possible existence of similar cases involving contracts with other customers or those signed by affiliated companies.

Further investigation revealed that Mitsubishi Electric also had overcharged expenses to NICT and MIC, and that four of the company’s affiliated companies had overcharged expenses to MOD. The findings were reported to each customer and a detailed investigation was launched.

Timeline

January 17	Received inquiries from MOD, CSICE and JAXA regarding costs accrued by the Kamakura Works. Launched an internal investigation.
January 27	Reported to MOD, CSICE and JAXA that certain projects had overcharged expenses by shifting work records between different orders.
February 3	Reported to NICT that work records had been shifted between different contracts.
February 24	Mitsubishi Precision Co., Ltd., Mitsubishi Electric TOKKI Systems Corporation and Mitsubishi Space Software Co., Ltd., all subsidiaries of Mitsubishi Electric, as well as Taiyo Musen Co., Ltd., an equity-method affiliate, each informed MOD that they had overcharged expenses by shifting work records between different orders.
March 2	Reported to MIC that Mitsubishi Electric had overcharged expenses for contracts regarding consigned research and development conducted on behalf of MIC. Paid refunds to the national treasury on July 4.

Outline of internal investigation

To ensure neutrality, the investigation members comprised mainly employees in the company’s Corporate Legal & Compliance Division and lawyers. The team investigated sections involved in defense and space businesses, namely, the Electronic Systems Group, the Kamakura Works and the Communication Systems Center, in addition to corporate divisions of Mitsubishi Electric. Each of the four affiliated companies also formed investigation teams, which included lawyers, to conduct self investigations.

The investigation covered a wide range of contracts, including not only cost audit contracts but also general fixed contracts. Cost audit contracts require a decrease in the contract amount or a reimbursement of excess profit if the initial cost does not reach the amount assigned in the original contract, while general fixed contracts determine the sum at the time of the contract.

During the investigation, contract- and labor-related documents, emails and other materials were inspected and executive officers and employees were interviewed.

Investigation results

How work records were shifted

It became clear that in certain projects work records had been shifted and recorded inappropriately, including those in both general fixed contracts and cost audit contracts. Details regarding when or how the inappropriate recording of work began could not be identified, but the company confirmed that such activities had been taking place since at least the 1970s in its defense business and since the beginning of the 1990s in its space business.

There also were cases in which design outsourcing and other expenses were charged to orders separate from those to which they were actually supposed to be charged.

Work records were shifted in the following manner:

- Based on the contract fee, target costs were decided for materials, processing, design and other expenses.
- Based on the target costs, the division coordinating a certain order, or contract, assigned target work to sections.
- Each section manager assigned target work to section members.
- When the actual work of the section members did not match the target work amount, work records were amended, or shifted, to match the target by recording the work in a different order, or by not recording it. In some workplaces, the work records typed in by section members were found to have been amended and shifted by section managers.
- Work amounts recorded according to these instructions were then used when processing the charges, resulting in overcharging. Records of actual work do not exist.

Involvement of high-level personnel

Section managers who were required to adhere to target work amounts mainly carried out the work shifting. Division managers and other higher-level managers in factories were not found to be proactively involved in matters such as instructing the shifting of work records. These higher-level managers were, however, generally aware that work records were being shifted based on their experience as section managers, although there may have been slight differences in the level of awareness from person to person. With an awareness of work shifting, managers drafted their factory business plans.

Motives and background

To sustain the defense and space businesses, the Kamakura Works and the Communication Systems Center adopted a management style that focused on maintaining overall profit for the business as a whole. Factories reduced loss amounts and prevented contract fee reductions, or reimbursements, by assigning target work that had been calculated according to target costs. Work records were shifted from unprofitable to profitable

orders to prevent actual work from exceeding targets.

If actual work exceeded a target, any unrecorded work could lower the direct work rate (ratio of work hours to recorded work), which was used as an index for determining staff size. Section managers, therefore, shifted work records to maintain direct work rates and thereby prevent staff reductions, with the aim of maintaining the workforce levels required to sustain the overall business.

Previous investigations by customers

To prevent work shifting from being detected in previous investigations by customers, the Kamakura Works and the Communication Systems Center prepared question and answer sheets, chose which materials they would or would not provide, removed posters and notices in factories and hid terminals used to shift work.

In 2004, when the Kamakura Works was instructed by JAXA to conduct a self investigation regarding the possibility of overcharges due to work shifting, the factory responded that it had been unable to find evidence of any work shifting.

Inappropriate recording of work by four affiliates

Mitsubishi Precision Co., Ltd., Mitsubishi Electric TOKKI Systems Corporation and Mitsubishi Space Software Co., Ltd., all subsidiaries of Mitsubishi Electric, and Taiyo Musen Co., Ltd., an equity-method affiliate, each reported that they also had shifted work inappropriately. The motives and backgrounds were the same as those of Mitsubishi Electric—reducing losses, preventing reimbursements and maintaining staff levels. Meanwhile, among businesses transferred from Mitsubishi Electric to affiliates, there were cases in which the practice was implemented to maintain work levels transferred from Mitsubishi Electric.

Cause analysis

Based on the investigation report, the causes of the problem have been determined as follows.

1. Issues in the Electronics Systems Group

a. Habitual management of target workloads

Due to the practice of shifting work to match target workloads and thereby maintain overall profitability, work shifting continued for years and gradually became a habitual on-site practice without any clear instructions from higher-level managers.

b. Weak perception of need to correct work practices and habits

Professionalism and specialization are heavily valued in the defense and space businesses, so these businesses tended not to exchange human resources with other groups. Consequently, perceptions and work habits became uniform, which resulted in a weak perception of the need to proactively correct practices and habits as required. Employees also lacked sufficient knowledge of cost audit contracts and cost calculations, and thus lacked understanding that work shifting would lead to overcharging.

2. Systemic issues with company-wide compliance

a. Ineffective control over business groups

Corporate divisions had little involvement with the compliance activities of business groups and therefore lacked the ability to identify improper practices.

b. Weak audits and checks regarding compliance

It was difficult for outsiders to identify improper practices through internal audits and other checks because only post-shifted work data were recorded and archived. Given the sensitive nature and environment of the defense and space businesses, important factors that required confirmation were not sufficiently incorporated into internal audits.

In addition, due to the habitual practice of work shifting, as well as a lack of awareness among employees, the company's internal whistle-blowing system was not utilized.

Countermeasures

Based on the cause analysis, Mitsubishi Electric implemented and is promoting the following countermeasures with regard to the Electronics Systems Group and the company-wide compliance system.

1. Countermeasures for the Electronics Systems Group

Issue	Countermeasures
Habitual management of target workloads	<p>- Replacement of managers The group president, group vice president and planning and administration manager were replaced and new ones were assigned from different divisions on March 1, 2012. At the conclusion of this matter, the company will reassign the managers who were involved in the improper practices.</p> <p>- Revision of business practices The practice of managing profit on a business-wide basis has been changed. Profit is now managed by individual or product-based contracts. Also, factories now record actual work accurately in the following manner:</p> <ul style="list-style-type: none">a. Work hours are properly calculated and audited.b. A system has been established to soundly maintain data and information systems.c. Other expenses also are managed appropriately. <p>For orders in which profit margins are tight, appropriately calculated costs are utilized to maximize cost reductions and productivity, thereby strengthening product competitiveness and improving profitability.</p>
Weak perception of need to correct work practices and habits	<p>- Education regarding contract systems and cost-calculation rules To help employees better understand if they are in violation of a contract, the company will provide education, including through the use of actual cases, about contract basics and cost calculation rules used in the defense and space businesses. Employees' level of understanding will also be checked.</p>

2. Measures regarding company-wide compliance system

Issue	Countermeasures
<p>Ineffective control over business groups</p>	<p>- Ensuring that Mitsubishi Electric’s compliance policy is clear and familiar to employees</p> <p>A message from the president was emailed to all employees to alert them of the problem. The message also was run in the company’s internal magazine.</p> <p>Mitsubishi Electric will further enhance compliance training among different employee rank levels.</p> <p>- Strengthened company-wide compliance system</p> <p>The Legal Division was renamed the Corporate Legal & Compliance Division on October 1 to clarify its responsibility of promoting company-wide compliance. The division has also increased its workforce to extend compliance awareness throughout the company. Mitsubishi Electric also established compliance divisions under the president of each business group, and now implements compliance as an inseparable part of its business.</p> <p>- Training future management</p> <p>Managers and others involved with administration, accounting, procurement and other functions are being trained to ensure a diverse workforce with wide-ranging values and knowledge of matters, including compliance. This initiative includes rotating personnel among business groups to give them experience in a wide range of businesses inside and outside Japan.</p>
<p>Weak audits and checks regarding compliance</p>	<p>- Strengthening the system of audits and checks with regard to compliance</p> <p>The company will make employees thoroughly aware of the internal whistle-blowing system, called the Ethics and Legal Compliance Hotline. The system itself is being improved to make it more effective. In addition, to identify misconduct or improper practices at an early stage through audits, the company will select topics from internal and external cases of misconduct and then audit high-risk divisions in light of these topics.</p>

Disciplinary actions

1. Punishments in the Electronics Systems Group

The group president of the Electronics Systems Group at the time of the case's revelation was replaced as of March 2012. Former group presidents of this group who are currently advisers will be discharged.

Other persons involved in improper conduct will be strictly punished according to company rules.

2. Penalties to Mitsubishi Electric's Executive Officers

Considering the severity of this matter, the company will cut the pay of the president and CEO by six months and the pay of other executive officers by one month.

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About Mitsubishi Electric Corporation

With over 90 years of experience in providing reliable, high-quality products, Mitsubishi Electric Corporation (TOKYO: 6503) is a recognized world leader in the manufacture, marketing and sales of electrical and electronic equipment used in information processing and communications, space development and satellite communications, consumer electronics, industrial technology, energy, transportation and building equipment. Embracing the spirit of its corporate statement, Changes for the Better, and its environmental statement, Eco Changes, Mitsubishi Electric endeavors to be a global, leading green company, enriching society with technology. The company recorded consolidated group sales of 3,639.4 billion yen (US\$ 44.4 billion*) in the fiscal year ended March 31, 2012. For more information visit <http://www.MitsubishiElectric.com>

*At an exchange rate of 82 yen to the US dollar, the rate given by the Tokyo Foreign Exchange Market on March 31, 2012