



*Our Precision, Your Advantage*

## **KYB Group Report 2019**

(April 1, 2018 - March 31, 2019)



# To Our Stakeholders

I am pleased to present you with KYB Group Report 2019.

Until now we have published an Annual Report and an Environmental and Social Activity Report to keep you informed about our business and CSR activities, respectively. This year, we have issued KYB Group Report 2019, our first integrated report, featuring enhancements including details on our new management structure and non-financial information. We hope that this report will be a starting point not just in terms of content, but for deeper dialogue with our stakeholders.

We have positioned FY2019 as the first year of KYB's recovery. The entire KYB Group will conduct various measures as it returns to the basis of *monozukuri*.

## The First Year of KYB's Recovery

**We will drastically reform our corporate culture as we rebuild the KYB Group, by returning to the basis of *monozukuri*, Japanese manufacturing expertise, and steadily implementing measures to prevent the recurrence of improper acts.**

### Regaining Trust

In FY2018, we announced nonconforming acts by KYB Corporation and one of its subsidiaries associated with building-use seismic isolation/mitigation oil dampers, as well as improper claims related to working hour billing for defense equipment. I would like to offer my deepest apologies for the trouble and concern we have caused our stakeholders.

We are addressing nonconforming acts associated with seismic isolation/mitigation oil dampers by seriously embracing the guidance and recommendations of the external investigative committee, implementing measures to prevent recurrence, and posting quarterly progress reports on our website. With respect to these acts, eliminating concerns among related parties as quickly as possible is a top management priority. In addition, the improper claims related to working hour billing for defense equipment are currently under investigation. We will promptly report the details as soon as they have been clarified.

We revised our Corporate Spirit\* on October 1, 2019 as one measure to prevent recurrence of improper acts. Our Corporate Spirit is based on the spirit of creative development inherited from founder Shiro Kayaba. The revised Corporate Spirit remains true to this spirit, but we have added "We shall follow all rules and face all issues honestly." This expresses our intention to comply and face the facts, given that the guidance of the external investigative committee pointed out a lack of compliance awareness and a corporate culture that did not face up to inconvenient facts. It also expresses our determination

to preclude improper acts in the future. In addition, fostering compliance awareness among all employees is a top priority because it is crucial for supporting quality management, which has always been one of our core management tenets.

\* For details, please see page 4.

## Our Future Approach

FY2019 is the final year of the FY2017-2019 Medium-Term Management Plan. During FY2017 and FY2018, we largely completed preparations for launching high-value added automotive products and consolidating the production lines for our construction machinery products to increase efficiency. However, there are still issues that require attention. We have been slow to restructure unprofitable businesses, and we have experienced construction machinery production delays because our manufacturing capacity has not kept pace with growth in demand.

We are now working to bring our seismic isolation/mitigation oil dampers into conformance with required standards as quickly as possible, and in view of issues in the past two years, we are restructuring our organization, including closing unprofitable businesses and locations, in order to sharpen our focus on our core operations. We are also preparing for the next medium-term management plan that will begin in FY2020 by developing competitive new products and innovative *monozukuri*.

The KYB Group will continue to devote itself to the challenging task of implementing reforms while fundamentally reviewing conventional approaches to its businesses with the goal of creating a fair and honest corporate group that has high ethical standards and places the highest value on compliance.

We will transition to an operating structure that ensures stable earnings while appropriately fulfilling our corporate social responsibilities. We are determined to regain trust in the KYB brand, so that it can continue to contribute to an affluent, vibrant society through the power of *monozukuri*.

We look forward to your continued support as we take on the challenges ahead.



**Masao Ono**

Representative Director,  
President Executive Officer



# Nonconforming Acts in the Inspection Process for Seismic Isolation/Mitigation Oil Dampers and Other Matters

## Outline of Improper Acts

- 1. Falsified Coefficients:** In the inspection process, measurement results for damping force were deliberately increased or decreased by multiplying them by designated coefficients to keep them within an intended range.
- 2. Origin Adjusting:** In the inspection process, measurement results for damping force were deliberately changed to keep them within a desired range by using a Balance ON function (a program that moves the median damping force on extension and compression in the direction of the origin) and an Amplifier function (to adjust the zero point of the load on the inspection machine) of the personal computers installed in inspection machines.
- 3. Use of Materials That Did Not Conform with Specifications Certified by Minister:** Materials were used that did not comply with specifications certified by the Minister for seismic isolation oil damper components, including the pistons, packing and paints.
- 4. Falsified Device Coefficient of Stiffness:** Figures for device stiffness (the ability to resist deformation when force is applied) were deliberately increased to desired values when customers agreed that device stiffness values exceeded prescribed values.
- 5. Screw Problems:** Galling prevents screws used to attach the piston and piston rod from tightening fully. As a result, the seismic isolation oil dampers were shipped with a gap between the piston and piston rod.

## Causes of Improper Acts

Contents	Cause	Comments
Corporate culture	Lack of compliance awareness	Inspectors at KYB Corporation and Kayaba System Machinery Co., Ltd. (KSM) who acted improperly, the supervisors who were aware of their improper acts but did not correct them, people in other departments, and certain managers and executives, lacked the fundamental compliance awareness that is an essential part of <i>monozukuri</i> .
	Corporate culture that did not face up to inconvenient facts	Certain managers and executives in the oil damper business at KYB Corporation and KSM were in positions where they should have stopped improper acts and rectified the situation in the first place. Instead, they perpetuated a corporate culture in the oil damper business of failing to face inconvenient facts by directing or giving their tacit approval for improper acts.
Business operation system	Factory management focused on simply filling orders received	In their factory operations, KYB Corporation and KSM accepted orders that exceeded their technical capabilities and production capacity for multiple reasons including a lax view of product performance requirements for sustaining the oil damper business and their focus on sales targets and delivery dates.
	Incomplete information-sharing systems	The systems for sharing information among KSM frontline operations and senior management, and between KYB Corporation and KSM, were deficient. Moreover, the Group's whistleblowing system was ineffective.
	Important business operations dominated by entrenched personnel	Certain entrenched management and frontline personnel dominated important operations in the oil damper business of KYB Corporation and KSM.
	Problems related to commercialization	The oil damper business relied heavily on specialized technicians before mass production began, and a system that would allow other managers to carefully and conservatively verify factors including oil damper technology, performance, quality inspection and production capacity was not fully in place. This situation was not remedied even after mass production began, so management was not able to properly monitor the business on a continuous basis as it expanded, or to implement appropriate improvements as they should have.
Quality inspection system	Deficient inspections	Manufacturing departments with a strong incentive to falsify inspection data had conducted performance inspection of themselves, which made it difficult to adopt cross checks, and therefore effective checks and balances were lacking in manufacturing departments.
	Lack of mechanisms to prevent improper acts involving inspection machines	Inspection equipment lacked systems to prevent improper acts, such as automatically recording raw data that would expose subsequent falsification of that data. Inspection machine administration was also inadequate, as it allowed inspection machine software itself to be improperly modified.
Internal audit system	Deficient internal audit system (deficient quality audits)	Quality audits by KYB Corporation or KSM were insubstantial and ineffective because they were conducted perfunctorily using a checklist of predetermined questions prepared in advance. In addition, companies were selected for audits on the basis of quality and percentage of process defects, but not on the basis of investigating improper acts.
	Deficient internal audit system (deficient audits of similar quality misconduct)	There were deficiencies in the internal audit system of KSM and our system for internal audits of KYB Group companies. Therefore, internal audits did not function properly. For example, internal audits conducted for improper acts similar to quality misconduct lacked rigor.

**On its website, KYB periodically posts reports\* of its progress in preventing the recurrence of improper acts and measures to identify and address such acts.**

\*First report posted in July 2019. Second report posted in October 2019.

<https://www.kyb.co.jp/english/company/progress/index.html>

The KYB Group released the report by an external investigative committee and published the results of the Group's internal investigation of the causes of improper acts and measures to prevent their recurrence. Please refer to these reports for details.

- Report by the external investigative committee on nonconforming acts in the inspection process for seismic isolation/mitigation oil dampers manufactured by KYB Corporation and its subsidiary for buildings  
[https://www.kyb.co.jp/company/progress/progress\\_20190213\\_02.pdf](https://www.kyb.co.jp/company/progress/progress_20190213_02.pdf) (Japanese only)
- Investigation into the causes of nonconforming acts in the inspection process for seismic/mitigation oil dampers manufactured by KYB Corporation and its subsidiary for buildings, and measures to prevent their recurrence  
[https://www.kyb.co.jp/company/progress/progress\\_20190213\\_01.pdf](https://www.kyb.co.jp/company/progress/progress_20190213_01.pdf) (Japanese only)

## Outline of Measures to Prevent Recurrence

Foster strict compliance awareness and reform the corporate culture	Establish compliance management	<ul style="list-style-type: none"> <li>• Establish compliance awareness at KYB Corporation and KSM</li> <li>• Foster compliance awareness throughout the Group</li> <li>• Revise the Corporate Guiding Principles and other guidelines</li> <li>• Emphasize the importance of compliance regularly</li> <li>• Implement personnel evaluations and related measures</li> </ul>
	Change the mindset of all officers and employees	<ul style="list-style-type: none"> <li>• Conduct education and training to raise awareness of social responsibility</li> <li>• Conduct education that incorporates numerous case studies and best practices from other companies</li> <li>• Conduct education on laws and regulations specific to businesses and products</li> <li>• Make education regarding quality mandatory</li> </ul>
Evaluate business feasibility, and revise business operations, information-sharing systems and other matters	Establish a balanced business operation system	<ul style="list-style-type: none"> <li>• Ensure appropriate business management at KSM</li> <li>• Review how decisions to accept orders are made at KSM</li> <li>• Develop business systems</li> <li>• Revise use of mass-production evaluation procedures for individual and small-batch products</li> </ul>
	Ensure personnel are rotated	<ul style="list-style-type: none"> <li>• Nurture successors by sharing expertise/know-how in the Company through effective job rotation and by increasing the transparency of operations</li> </ul>
	Collect information and establish a feedback system	<ul style="list-style-type: none"> <li>• Ensure thorough documentation of meetings, reports and instructions at KSM</li> <li>• Ensure that internal regulations are applied in the event of an emergency</li> <li>• Review the internal whistleblowing system to improve its effectiveness</li> <li>• Clarify the actions to be taken when quality misconduct is detected</li> <li>• Create a mechanism for extracting information</li> </ul>
Improve inspection systems and methods	Implement inspection systems	<ul style="list-style-type: none"> <li>• Strengthen the independence of quality assurance</li> <li>• Improve methods for onsite oil damper inspections with the customer present</li> <li>• Review inspection manual</li> </ul>
	Implement preventive measures against fraudulent operation of inspection machines	<ul style="list-style-type: none"> <li>• Tighten internal procedures for changing the software of oil damper inspection machines</li> <li>• Regularly monitor the software of oil damper inspection machines</li> <li>• Automatically record inspection results without human involvement</li> <li>• Automate inspection processes</li> <li>• Tighten controls on access to oil damper inspection machines</li> <li>• Ensure traceability of performance test data</li> </ul>
Strengthen internal audit and control systems	Enhance internal quality inspection system	<ul style="list-style-type: none"> <li>• Perform audits that consider quality misconduct</li> <li>• Perform audits that effectively verify inspection data</li> <li>• Institute audits by KYB Corporation</li> <li>• Leverage the support of external experts</li> </ul>
	Tighten the subsidiary management system	<ul style="list-style-type: none"> <li>• Strengthen systems for sharing information and collaborating among Group companies</li> <li>• Review management systems for Group companies</li> <li>• Analyze and monitor Group companies' business risks</li> <li>• Reorganize Group companies</li> </ul>

# Corporate Spirit

Imbued with the spirit of creative development of founder Shiro Kayaba, the KYB Group will dedicate its collective strengths toward being a highly ethical, fair and honest corporate group in order to regain trust in its brand through *monozukuri* (Japanese manufacturing expertise) that delights people and consistently contributes to a prosperous society.

## Corporate Spirit (What KYB Aims to Be)

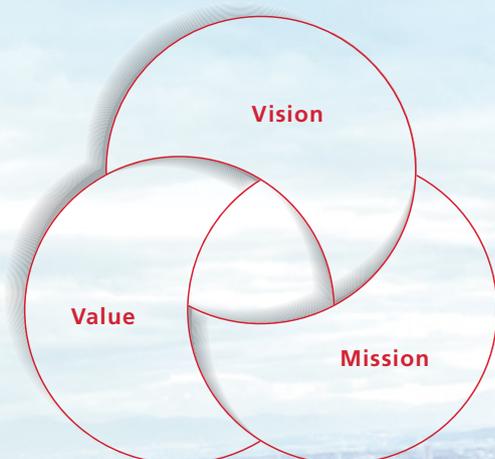
**By serving technologies and products that make people's lives safe and comfortable, KYB group dedicates to the society.**

1. We shall follow all rules and face all issues with honesty.
2. We shall build a corporate culture full of vitality, and hold high goals.
3. We shall value sincerity, cherish nature and care for the environment.
4. We shall constantly pursue creativity to contribute to the prosperity of customers, shareholders, suppliers and society.

### Vision

What the KYB Brand Can Do for the World  
***Monozukuri* That Delights People**

KYB aims to support the development of society through the joy of *monozukuri*, and to make people happier as a result.



### Mission

The Mission of the KYB Brand  
***Monozukuri* Taken One Step Further**

KYB draws on technical expertise acquired over many years to continue delivering value to clients and markets. Using our unique capabilities, we take *monozukuri* one step further to provide clients with new value and greater satisfaction.

### Value

The KYB Brand Delivers Value  
**Technology for Comfortable Living**

Sensory value: Comfortable living and the joy of *monozukuri*

Functional value: Reliable quality

The value KYB promises end users is greater comfort from creative technology and honesty in product development.

The value KYB promises clients is the reliable quality that comes from thinking of end users as clients.

The value KYB promises employees is the joy of *monozukuri* that comes from knowing they are changing the world.



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### Editorial Policy

From FY2019, the KYB Group issues this integrated report to communicate its management policies, business strategies and CSR activities to shareholders, investors and all other stakeholders. We hope to create new opportunities for dialogue by covering business performance, management strategies and other financial information, as well as the environment, society, governance (ESG) and other non-financial information in order to inform readers about our efforts to increase corporate value over the medium to long term. For a better reading experience, we will continue to improve the report based on stakeholder feedback. We welcome your suggestions.

### Reporting Period

FY2018 (April 1, 2018 to March 31, 2019)

(Includes efforts that are outside the above reporting period)

### Scope

The report covers KYB Corporation and subsidiaries and affiliates in Japan and around the world. Environmental data is for KYB Corporation (Sagami Plant, Kumagaya Plant, Gifu North Plant, Gifu South Plant and Gifu East Plant) unless otherwise annotated.

### Date of Issue

December 2019 (We plan to issue our next report in August 2020.)

### Forward-Looking Statements

This report includes plans and forecasts as of the issue date, and estimates based on our business plans and management policies. Forward-looking statements are based on information available at the time of report preparation, and actual results may differ depending on changes in relevant conditions.