



December 18, 2013

To Whom It May Concern:

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Notice Regarding the Improper Supply of Defense Equipment

Sumitomo Heavy Industry, Ltd. (hereinafter referred to as "SHI" or the "Company") regrets to inform that the Company has discovered that its Defense Equipment Division improperly supplied certain machine guns to the Ministry of Defense (MOD). Further, details are provided below.

SHI deeply apologizes for causing significant inconvenience and trouble to the involved parties as a result of this event. The Company plans to develop response measures based on further deliberations with the MOD.

1. History of the Event

On May 22 of this year, the Company completed the annual durability tests for the "12.7mm Heavy Machine Gun" that it manufactures. The following day, the Head of Quality Assurance submitted a report to the Division Manager indicating that the "durability tests for this year have failed and performance standards have also not been met in previous years". After receiving this information, the Company carried out an immediate investigation into the issue and verified that the durability tests for the "12.7mm Heavy Machine Gun" had been improperly handled in the past. The findings were voluntarily reported to the MOD on June 13, and at the same time, the Company established an Investigation Response Committee to further look into the issue.

Subsequently, the Company expanded its investigation from not only the results of the durability tests for the "12.7mm Heavy Machine Gun" but also to other defense equipment supplied to the MOD. Upon completion of this broad investigation, a report was submitted to the MOD on November 22.

2. Improper Handling Issues

(1) Falsification of Test Results

With regard to the durability tests performed on the barrel of the "12.7mm Heavy Machine Gun", the investigation discovered that despite test results indicating that specification standards were not being met since the time the contract was awarded (1984), falsified test results were being submitted to the MOD when the product was delivered. Moreover, with regard to firing speed tests performed on the "Type 74 – 7.62mm Machine Gun" for equipment contracts awarded between 1974 and 2002, the investigation discovered that despite test results indicating that specification standards were not being met, falsified test results were being submitted to the MOD when the product was delivered.

(2) False Reports

With regard to firing speed tests performed on the "12.7mm Heavy Machine Gun" for certain years, the investigation discovered that despite not meeting the required firing speed standards, the inspection was labeled as "passed" and delivery of the product to the MOD was completed.

With regard to the firing speed tests performed on the "Type 74 – 7.62mm Machine Gun" for certain years, the investigation discovered that despite the equipment misfiring (i.e. stopped firing) during the test, the product was delivered to the MOD without the mandatory post adjustment re-firing (i.e. re-testing) of the equipment being conducted. Furthermore, for contracts awarded after 2010, the Company made improvements to ensure that

firing speeds were satisfactory. However, prior approval for this adjustment from the MOD was never sought.

Finally, with regard to certain batches of the "5.56mm Machine Gun – MINIMI" in certain years, the investigation discovered that sampling tests in accordance with the specifications for weapons accuracy testing were never carried out.

(3) Other Issues

In addition to the above, the investigation discovered that despite component damage being detected during the various inspection stages of the manufacturing process (acceptance, in-process, and finished product inspections), a "pass" mark was inappropriately granted, and the product was delivered to the MOD.

3. Safety of Products that Have Already Been Delivered to the MOD

Upon completion of a hazard analysis that evaluates the degree of a specific product's risk, the Company was able to verify the safety of the products that have already been delivered to the MOD. Further, a review of previous claims information indicated that no claims relating to the aforementioned non-conforming products had been received. These results have already been submitted to and accepted by the MOD.

4. Suspension of MOD Orders

(1) Suspension of MOD Orders

From December 18, 2013 to May 17, 2014 (5-Month Period)

(2) Compensatory Damages

With regard to the barrel of the "12.7mm Heavy Machine Gun", the Company received a claim for compensatory damages in the amount of JPY62,474,916 (the debt default amount) from the MOD. Payment for this amount has been made today.

5. Future Response Measures

(1) Measures to be Taken for Delivered Products

SHI will voluntarily repair and test all non-conforming products associated with aforementioned quality issues. Details regarding this process will be finalized after further deliberations with the MOD.

(2) Measures to Prevent Future Recurrences

The Company has formulated and submitted a Future Recurrence Prevention Plan to the MOD that includes measures to clarify the manufacturing processes associated with its defense equipment and increase the scrutiny of test results. In addition, the plan calls for the establishment of an internal system to prevent the delivery of non-conforming products. This plan is already being implemented in phases. Moreover, the Company is re-emphasizing compliance education across its entire employee base.

6. Impact on Financial Results

The impact of this incident on the Company's financial results is expected to be minimal.

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