



**The Japanese Institute of
Certified Public Accountants**

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November 21, 2013

Mr. James Gunn
Technical Director
International Auditing and Assurance Standards Board
International Federation of Accountants
529 5th Avenue, 6th Floor
New York, NY 10017 USA

Dear Mr. Gunn,

Re: JICPA Response to the Exposure Draft, *Reporting on Audited Financial Statements:
Proposed New and Revised International Standards on Auditing (ISAs)*

The Japanese Institute of Certified Public Accountants (“we”, “our” and “JICPA”) is grateful for the opportunity to comment on the IAASB’s Exposure Draft, *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing (ISAs)* (the Proposed ISAs).

We support the IAASB in proceeding with the project to improve the auditor’s report. Due to the globalization of reporting entities’ activities, consistency between auditors’ reports is becoming more critical. Therefore, we welcome the IAASB playing the leading role in this global initiative.

However, in order to achieve the objective of the Proposed ISAs to enhance the information value of the auditor’s report so as to meet the information needs of users, we also believe that a holistic approach to the entire system that maintains the reliability of disclosure is essential. Concurrent with the consideration of improvements in the auditors’ report, it is also necessary to consider the enhancement of other aspects of the financial reporting system. This would include enhancements to the disclosure provided by the entity as well as the role of those charged with governance. The purpose of the changes to auditor reporting should not be to compensate for deficiencies in financial statements or financial reporting frameworks. Rather, it should be to enhance the reliability of financial reporting through the audit process including use of the audit report. In this respect, we appreciate that the IAASB is seeking to collaborate with relevant organizations, such as accounting standard setters as well as regulators, we encourage the IAASB to continue on this path.

Major Points

Our major points are as follows:

Our Comments to the Questions in the Explanatory Memorandum

Key Audit Matters

- ***The Purpose of Communication:*** Proposed ISA 701 does not clearly explain the purpose of communication of key audit matters. Paragraph 2 of proposed ISA 701 should clearly state that the purpose of providing additional information through communication of key audit matters is, to provide increased transparency about an audit and ultimately, enhance the degree of confidence of intended users in an audit as well as the audited financial statements. (Question 1. (1))
- ***The Necessity of International Discussion:*** International discussion regarding the environment necessary for its implementation, including the issue of auditor liability and the relationship with the relevant ethical requirements of confidentiality is necessary. We also encourage the IAASB to disseminate the purpose of, as well as the environment necessary for this change to the world. (Question 1. (2))
- ***The Effects on the audit:*** In order to avoid the impression that the auditor is providing piecemeal opinions on individual matters, inclusion of the audit procedures and results of the audit procedures in the Key Audit Matters section should not be allowed. (Questions 3 and 4. (1))
- ***The Introductory Language of the Key Audit Matters Section:*** The introductory language of the Key Audit Matters section should be expanded, so as to assist the stakeholders' understanding of the purpose and natures of the communication of key audit matters. (Questions 3 and 4. (2))
- ***The Location of the Key Audit Matters Section:*** We propose that the Key Audit Matters section be included in an Appendix to the auditor's report, so as to clearly show the relationship between the auditor's opinion and the key audit matters, i.e. the auditor forms an opinion on the basis of the audit evidence obtained through the performance of procedures relevant to key audit matters. In addition, an Appendix makes it easier to include sufficient explanatory language which we have proposed. (Questions 3 and 4. (3))
- ***Significant Deficiency in Internal Control:*** In order to avoid the difficulty arising from the auditor providing sensitive and original information about the entity and the potential conflicts with other disclosure mechanisms that may exist in an individual jurisdiction, the phrase "including as a result of the identification of a significant deficiency in internal control" in paragraph 8(c) of proposed ISA 701 should be deleted. (Questions 3 and 4. (4))
- ***Adverse Opinion:*** Communication of key audit matters should not be required when the auditor expresses an adverse opinion or disclaims an opinion, (Other Significant Comments Relating to Key Audit Matters. (2))

Going Concern/Independence

- We do not agree with following proposals. The impediments far outweigh the values:
 - ***The description regarding Going Concern*** (Question 9)
 - ***The Disclosures of the Source(s) of Relevant Ethical Requirements*** (Question 11)

Other Significant Comments

- ***The Effective Date:*** The effective date should be postponed from the proposed date, to ensure all stakeholders have sufficient time for implementation.((1))
- ***Auditor's Responsibilities with Respect to Other Information:*** The direction of the project to revise ISA 720 should be reconsidered. Considering the nature of the responses that the IAASB received on Proposed ISA 720 (Revised), which was issued in November, 2012, we believe re-exposure is indispensable.((2))

Our detailed comments to the questions in the Explanatory Memorandum and other significant comments are set out in Appendix I, along with comments on specific paragraphs of the Proposed ISAs in Appendix II.

Sincerely yours,

Sayaka Sumida
Executive Board Member - Auditing Standards
The Japanese Institute of Certified Public Accountants

Comments to the Questions in the Explanatory Memorandum and Other Significant Comments

Comments to the Questions in the Explanatory Memorandum

Key Audit Matters

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| 1. Do users of the audited financial statements believe that the introduction of a new section in the auditor's report describing the matters the auditor determined to be of most significance in the audit will enhance the usefulness of the auditor's report? If not, why? |
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We believe the usefulness of the auditor's report would be enhanced, only when all participants in the financial reporting supply chain are acting in achieving the goal of introduction of key audit matters. We have following comments relevant to this topic:

(1) The purpose of communicating key audit matters

Paragraph 2 of proposed ISA 701 states that communicating key audit matters provides additional information to users of the financial statements to assist them in understanding those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. However, "those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period" is the definition of key audit matters itself, and therefore, paragraph 2 does not explain the purpose of providing additional information by communicating key audit matters. In addition, the linkage of the communication of key audit matters to the purpose of an audit (i.e. "to enhance the degree of confidence of intended users in the financial statements" (paragraph 3 of ISA 200)) is not clear.

We believe that the purpose of providing additional information about an audit by communicating key audit matters should be, to provide increased transparency about an audit and ultimately, enhance the degree of confidence of intended users in an audit and the audited financial statements. This should be clearly stated in the standard. The communication of key audit matters will have cost and time implications for the both preparers and auditors. It is necessary that relevant stakeholders, including preparers of financial statements and auditors, acknowledge that communication of key audit matters would provide benefit that outweighs the additional cost. Therefore, we believe that clarification of the meaning of communication of key audit matters in the context of the purpose of the audit is especially important for preparers and auditors, so that they can recognize the value of the communication, and take the initiative needed to provide more valuable information to users.

We recognize that there are other potential benefits: to assist users of the financial statements in understanding the entity and areas of significant management judgment in the audited financial statements (paragraph 2 of proposed ISA 701), and further improvement of the quality of the financial reporting (paragraph 8 of Explanatory Memorandum). However, we believe that these are secondary benefits. If they are provided as the purpose of communication of key audit matters, it could result in confusion as to the distinction between the respective responsibilities of auditors and management and/or those charged with governance for disclosing information about the entity. It could also result in confusion as to the relationship between the auditor's opinion and key audit matters.

Therefore, we propose a change to paragraph 2 of proposed ISA 701 as follows:

“Communicating key audit matters, provides additional information to users of the financial statements to assist them in understanding those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period. This communication provides increased transparency about an audit and ultimately, enhances the degree of confidence of intended users in an audit as well as the audited financial statements. Communicating key audit matters may also assist users of the financial statements in understanding the entity and areas of significant management judgment in the audited financial statements, as such matters are areas of focus in performing the audit.”

(2) The necessity of the international discussion regarding the environment necessary for its implementation

To accomplish a successful implementation in communicating key audit matters, we believe it is important that all stakeholders understand the natures¹ as well as the purpose² of key audit matters. If communication of key audit matters results in unintended consequences to the entity, such as its reputation, there is a risk that communication will become boilerplate. In addition, if, after the issuance of the auditor’s report, the auditor is criticized for not disclosing a specific matter as a key audit matter, even though the auditor adequately addressed such matter in accordance with auditing standards, there is a risk that the auditor would in a preventive manner increase the number of key audit matters disclosed in the auditor’s report, and thus the purpose of the communication of key audit matters would not be achieved in an efficient manner. In regards to these issues, we believe that the stakeholders’ behavioral response as well as the inspectors’ approach would have a significant effect.

In addition, we believe that it is necessary to clarify the relationship between the requirements in the auditing standards regarding the communication of key audit matters, and the ethical requirements regarding confidentiality. If the auditor determines additional information that the auditor may provide is critical to the auditor’s description of the key audit matter, but management requests the auditor not to disclose the information in the auditor’s report, and those charged with governance do not take appropriate action, the auditor would encounter practical difficulties. This is especially true when it is reasoned that disclosing such information in the auditor’s report is inappropriate because the auditor has a responsibility to maintain the confidentiality of the information based on ethical requirements.³

We understand that ultimately, these are the issues that each jurisdiction would resolve in the context of its legal environment. However, consistency between auditors’ reports is becoming more critical. In order to ensure global consistency in the basic approach to an auditor’s responsibility relating to the communication of key audit matters, including other environmental factors necessary for implementation, these issues should be discussed at the international level.

In addition, we encourage the IAASB to disseminate the purpose of, as well as the environment necessary, for this change to all participants in financial reporting supply chain to the world. Communication of key audit matters will bring fundamental change in current audit practice. We believe that successful implementation is not achievable merely by changing the auditing standards.

¹ See our comment on *Questions 3 and 4. (2). The Introductory Language of Key Audit Matters.*

² See our comment on *Question 1. (1). The purpose of communicating key audit matters*

³ For our relevant comment on paragraph A35 of proposed ISA 701, see *Other Significant Comments relating to Key Audit Matters. (1).*

2. Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide an appropriate framework to guide the auditor’s judgment in determining the key audit matters? If not, why? Do respondents believe the application of proposed ISA 701 will result in reasonably consistent auditor judgments about what matters are determined to be the key audit matters? If not, why?

We believe that the proposed requirements and related application material in proposed ISA 701 provide an appropriate framework to guide the auditor’s judgment in determining the key audit matters.⁴ The concept of key audit matters is fundamentally new. Therefore, as stated in the Explanatory Memorandum, we believe that a post-implementation review is important. Using this process, the IAASB would monitor whether the application of proposed ISA 701 results in reasonably consistent auditor judgments and to meet the information needs of users. If as a result of the process, it is found to be necessary, the IAASB should take appropriate action, including revisions to the standard.

3. Do respondents believe the proposed requirements and related application material in proposed ISA 701 provide sufficient direction to enable the auditor to appropriately consider what should be included in the descriptions of individual key audit matters to be communicated in the auditor’s report? If not, why?
4. Which of the illustrative examples of key audit matters, or features of them, did respondents find most useful or informative, and why? Which examples, or features of them, were seen as less useful or lacking in informational value, and why? Respondents are invited to provide any additional feedback on the usefulness of the individual examples of key audit matters, including areas for improvement.

We have following comments regarding the proposed requirements, related application materials and illustrative examples of key audit matters.

(1) The effects on the audit

We believe that it is not appropriate to include a discussion of the audit procedures and results of the procedures in the description of a key audit matter. In order for the communication of key audit matters to have value to users, we agree it is necessary for the auditor to explain as to why the auditor considered the matter to be one of most significance in the audit. As in the case of the 3rd example (“Acquisition of XYZ Business”), the auditor can explain it precisely and clearly, without describing the audit procedures and results of the procedures. However, inclusion of a discussion of the procedures and the results of the procedures has following drawbacks:

- It is difficult to avoid the impression that the auditor expresses an opinion on that individual matter, even if the introductory language of the Key Audit Matters section explains otherwise.
- As explained in paragraph A39 of proposed ISA 701, it is difficult to summarize the procedures performed in succinct way, particularly in complex, judgmental areas of the audit. It is possible that the users may misunderstand the nature of the audit procedures performed on the key audit matters.
- If the auditor is allowed to include the audit procedures and the results of the procedures in the description of key audit matters, it creates a situation where only some descriptions

⁴ Regarding our comment on paragraph 8(c) (significant deficiency in internal control), in relation to the description of the Key Audit Matters section, see *Questions 3 and 4. (4) Significant Deficiency in Internal Control*.

include the procedures and results of the procedures, and as a result users may misinterpret that there are unresolved issues on the key audit matter where the procedures and results of the procedures are not included in the description of the key audit matter.

In order to avoid these unintended consequences, we believe that inclusion of the audit procedures and results of the procedures should not be allowed.

(2) The introductory language of the Key Audit Matters section

We propose a change to the introductory language of the Key Audit Matters section as follows:

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period.

Key Audit Matters are a relative concept, and are selected and described in the auditor's report tailored to the specific facts and circumstances that existed during the current period's audit. Accordingly, key audit matters may vary from one year to the next and also vary from one audit engagement to another, in terms of the number and selection of topics addressed and the nature in which they are described.

Key audit matters are selected from the matters communicated with [those charged with governance], but are not intended to represent all matters that were discussed with them.

Our audit procedures relating to these matters were designed in the context of our audit of the consolidated financial statements as a whole, and we do not express an opinion or conclusion on these individual matters. Our opinion on the consolidated financial statements is not modified with respect to any of the key audit matters described below, and we do not express an opinion on these individual matters.

Communicating key audit matters in the auditor's report is not a substitute for the auditor expressing a modified opinion, and accordingly, these matters do not alter our opinion on the consolidated financial statements in any way.

We recognize that some have suggested that expansion of the introductory language is not appropriate, since it gives the impression that the auditor is unduly defensive. However, since the key audit matters is a fundamentally new concept, we believe that it is critical that introductory language of the Key Audit Matters section includes descriptions that are sufficient to enable all participants in the financial reporting supply chain to understand this new concept.

We believe that "of the current period" in the first sentence is necessary in all cases, rather than only when the financial statements include comparative financial information. As stated in paragraph A9, whether a matter is a key audit matter is determined based on the relative significance in the current period's audit, whether or not it was a key audit matter in the prior period's audit. We believe this is one of the most important features of key audit matters and therefore, it should be explained in the introductory language.

In addition, we believe that the fact that key audit matters are a relative concept in the current period's audit is one of the important nature that should be clearly explained in proposed ISA 701. Regarding our suggestion, see our comment on paragraph A9 of proposed ISA 701 in Appendix II.

(3) Location of the Key Audit Matters section

We propose that the Key Audit Matters section be included in the Appendix to the auditor's report for following reasons:

- If the Key Audit Matters section is placed directly below the Opinion section, the relationship between the key audit matters and the auditor's opinion is not clear. It is difficult to avoid the impression that the auditor expresses an opinion on each individual key audit matter or is expressing a qualified opinion.
- An Appendix allows for the Key Audit Matters section to be more noticeable and readable to users, as opposed to being included in the auditor's report itself.
- Use of an Appendix makes it more convenient to include sufficient explanatory language which we have proposed above.

(4) Significant Deficiency in Internal Control

We agree that the identification of a significant deficiency may require significant modification of the auditor's planned approach to the audit. However, we do not agree with paragraph 8(c) of proposed ISA 701, which includes a reference to a significant deficiency in internal control.

First, the existence of a significant deficiency in internal control is sensitive information to disclose for the entity. Absent a requirement for the entity to disclose such information, we anticipate considerable difficulty for the auditor in disclosing it as a key audit matter in the auditor's report.

Second, it is not clear from proposed ISA 701 how to reconcile this requirement with the disclosure requirements for deficiencies that may already exist in individual jurisdictions. For example, in Japan, we have an internal control reporting system which requires management to assess and report on the entity's internal control over financial reporting, and for the external auditor of the financial statements to audit such assessment (internal control audit). In the internal control reporting system, a "material weakness" is defined as a deficiency in internal control that exists at the year-end, and should be disclosed publicly in light of its severity. If, in accordance with proposed ISA 701, the auditor communicates a significant deficiency as a key audit matter and the deficiency is not required to be publicly disclosed in accordance with the requirements of the internal control reporting system, the requirements of the financial statement audit effectively deny the purpose of the internal control reporting system. For example, the internal control reporting system requires management to assess internal control over financial reporting as of year-end, rather than throughout the period, this provides an incentive for management to remedy identified deficiencies during the year. However, in accordance with paragraph 8 (c) of proposed ISA 701, if the auditor significantly modified its planned audit approach as a result of the identification of a significant deficiency in internal control, the auditor may need to disclose such deficiency as a key audit matter, even if such deficiency has been remedied before year-end and, accordingly, the disclosure of such deficiency is not required by the internal control reporting system.

Therefore, we believe the phrase "including as a result of the identification of a significant deficiency in internal control" in paragraph 8(c) of proposed the ISA 701 should be deleted. We also believe it is necessary to clarify the relationship between a significant deficiency that is determined to be a key audit matter in accordance with proposed ISA 701, and a deficiency that is required to be disclosed by another mechanism which may exist in an individual jurisdiction.

(5) Background Information regarding the Illustrative Example of Key Audit Matters

We propose that the IAASB develop and provide supposed related disclosures in the financial statements with each illustrative example of the Key Audit Matters section. We believe it is not appropriate for the auditor to provide original information through communication of key audit matters. However, we also recognize that repetition of the disclosures in the financial statements cannot enhance the usefulness of the auditor's report, and all information that is not exactly the same as the disclosures in the financial statements may be viewed as original information of the entity. Therefore, it is important to give the auditor and other relevant stakeholders guidance on the level of description that can reasonably be expected, by showing the relationship between the individual key audit matter and the related disclosure in the financial statements.

5. Do respondents agree with the approach the IAASB has taken in relation to key audit matters for entities for which the auditor is not required to provide such communication – that is, key audit matters may be communicated on a voluntary basis but, if so, proposed ISA 701 must be followed and the auditor must signal this intent in the audit engagement letter? If not, why? Are there other practical considerations that may affect the auditor's ability to decide to communicate key audit matters when not otherwise required to do so that should be acknowledged by the IAASB in the proposed standards?

We agree with the IAASB's approach that key audit matters may be communicated on a voluntary basis but, if so, proposed ISA 701 must be followed.

However, we believe that clarification is necessary for the provisions regarding the terms of audit engagements in proposed conforming amendments to ISA 210. If the auditor is not required to communicate key audit matters, but intends to do so, paragraph 10 of the proposed conforming amendments to ISA 210 requires the auditor to include a statement that the auditor intends to communicate key audit matters in the agreed terms of the audit engagement. However, paragraph A23a seems to suggest that, if the auditor agrees to the terms of the audit engagement which includes such a statement, which allows the auditor discretion as to whether to communicate key audit matters, there is no need to change the terms of the audit engagement, even if the auditor subsequently determines they will not communicate key audit matters. For the audit in which the communication of key audit matters is not required, the auditor should agree with management and those charged with governance as to whether to communicate key audit matters on voluntary basis, and such agreement should in all cases be included in the terms of the audit engagement.

6. Do respondents believe it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate?
- (a) If so, do respondents agree with the proposed requirements addressing such circumstances?
- (b) If not, do respondents believe that auditors would be required to always communicate at least one key audit matter, or are there other actions that could be taken to ensure users of the financial statements are aware of the auditor's responsibilities under proposed ISA 701 and the determination, in the auditor's professional judgment, that there are no key audit matters to communicate?

We agree that it is appropriate for proposed ISA 701 to allow for the possibility that the auditor may determine that there are no key audit matters to communicate. We also agree with the proposed requirements addressing such circumstances.

7. Do respondents agree that, when comparative financial information is presented, the auditor's communication of key audit matters should be limited to the audit of the most recent financial period in light of the practical challenges explained in paragraph 65? If not, how do respondents suggest these issues could be effectively addressed?

We agree with the proposal.

8. Do respondents agree with the IAASB's decision to retain the concepts of Emphasis of Matter paragraphs and Other Matter paragraphs, even when the auditor is required to communicate key audit matters, and how such concepts have been differentiated in the Proposed ISAs? If not, why?

We agree with the proposal.

Other Significant Comments Relating to Key Audit Matters

(1) Paragraph A35 on proposed ISA 701

Section 140.7(c)(iv) of the IESBA Code of Ethics stipulates that, "professional accountants are or may be required to disclose confidential information or such disclosure may be appropriate, where there is a professional duty or right to disclose, and when not prohibited by law", and "to comply with technical standards and ethics requirements", is one of circumstances "where there is a professional duty or right to disclose". However, paragraph A35 of proposed ISA 701 seems to suggest that there may be circumstances where the communication of key audit matters is in conflict with the auditor's responsibility to maintain information confidentiality, even if the auditing standards establish the requirement to communicate key audit matters, and thus the auditor needs to demonstrate to management that there is no conflict. We propose to delete the phrases that refer to "ethical standards" and "auditor confidentiality" as follows, or to add an explanation to clarify its meaning:

"A35. In addition, law, or regulation or ~~ethical standards~~ may restrict the auditor's ability to communicate key audit matters because of investigations, ~~auditor confidentiality~~ or data protection requirements. The ISAs do not override law or regulation that governs an audit of financial statements ~~or relevant ethical requirements~~, but potential conflicts between the auditor's legal ~~and ethical~~ obligations and obligations to communicate in accordance with this ISA may be complex. In such cases, the auditor may consider discussing the situation with those charged with governance and may consider obtaining legal advice."

(2) Adverse Opinion

We believe that requiring communication of key audit matters when the auditor expresses an adverse opinion is not necessary. When the auditor expresses an adverse opinion, the information that is useful to the investors is that information that assists them in understanding why the auditor expressed an adverse opinion. This information would be included in the Basis of Adverse Opinion section. In addition, we understand that the Proposed Auditing Standard: *The auditor's report on an audit of financial statements when the auditor expresses an unqualified opinion*, which was published by the U.S. PCAOB on August 2013, does not require communication of critical audit matters when the auditor expresses an adverse opinion or disclaims an opinion.⁵ Proposed ISA 701 should similarly not require communication of key audit matters when the auditor expresses adverse opinion or disclaims an opinion.

⁵ PCAOB Release No. 2013-005 Appendix 5 – Additional Discussion Related to the Proposed Auditor Reporting Standard, Page A5-55

(3) The applicability of ISA 701

Paragraph 4 of proposed ISA 701 states that ISA 701 applies to the audits of complete sets of general purpose financial statements of listed entities. However, in some jurisdictions, the listed entity is required to prepare more than one type of general purpose financial statements. For example, listed entities in Japan are required to prepare two types of financial statements: the financial statements required by the Financial Securities Acts and financial statements required by Company laws. These are both general purpose financial statements and prepared in accordance with the financial reporting frameworks designed to meet the common financial information needs of a wide range of users. However, for the financial statements required by Company law, due to the early reporting deadline requirement, we anticipate difficulty in communicating key audit matters in the auditor's report. Financial reporting systems vary between jurisdictions.

Therefore, where the listed entities are required to prepare more than one type of general purpose financial statements, such jurisdiction should be allowed to determine, in light of their circumstances, to which type of financial statements ISA 701 applies. We believe this should be clarified in Application and Other Explanatory Material.

Going Concern

9. Do respondents agree with the statements included in the illustrative auditor's reports relating to:
- (a) The appropriateness of management's use of the going concern basis of accounting in the preparation of the entity's financial statements?
 - (b) Whether the auditor has identified a material uncertainty that may cast significant doubt on the entity's ability to concern, including when such an uncertainty has been identified (see the Appendix of proposed ISA 570 (Revised))?
- In this regard, the IAASB is particularly interested in views as to whether such reporting, and the potential implications thereof, will be misunderstood or misinterpreted by users of the financial statements.

We disagree with the statements included in the illustrative auditor's reports related to going concern. The benefit of the IAASB's proposal is in making explicit in the auditor's report the work effort for an auditor required by ISA 570. In addition, the proposal would expand the expectation gap, rather than enhancing the transparency of the audit work performed for the following reasons:

- Usually, there is no specific disclosure regarding going concern in the notes to the financial statements, except for cases when a material uncertainty is identified. This is also the case for financial statements prepared in accordance with IFRSs. Therefore, the proposal may give the impression that the auditor should provide original information about the entity that goes beyond the opinion on the financial statements. In addition, users may misunderstand that the auditor is providing a piecemeal opinion on the going concern issue, in addition to the auditor's opinion.
- There are no definitions that are widely understood on terms such as "material uncertainty", "significant doubt" and "the going concern basis of accounting".

The issue of going concern has drawn heightened attention, particularly in light of the global financial crisis. However, we believe that the proposal does not provide value that exceeds the impediments. As stated in the Explanatory Memorandum, a more holistic approach is particularly important on the issue of going concern. Just changing the contents of the auditor's report without changing the entity's disclosure requirements will not meet the needs of the users, and will only expand the expectation gap. Therefore, we do not agree with the proposal.

10. What are respondents' views as to whether an explicit statement that neither management nor the auditor can guarantee the entity's ability to continue as a going concern should be required in the auditor's report whether or not a material uncertainty has been identified?

As we stated in our comment on question 9, we do not agree with the proposal regarding going concern. However, if the IAASB does proceed with this proposal, we believe that this statement should be included in the auditor's report in all cases, whether or not the auditor identifies material uncertainties. Neither management nor the auditor can guarantee the entity's ability to continue as a going concern, and this limitation applies whether or not the auditor identifies material uncertainties.

However, the proposed statement included in the illustrative auditor's report is not suitable when the auditor identifies material uncertainties. Therefore, we propose a change to the statement and inclusion in the explanatory language of the Going Concern section as follows:

Going Concern

This section includes our statements based on our audit. However, because not all future events or conditions can be predicted, neither management nor the auditor can guarantee the Company's ability to continue as a going concern.

.....

Compliance with Independence and Other Relevant Ethical Requirements

11. What are respondents' views as to the benefits and practical implications of the proposed requirement to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report?

We do not agree with the proposal to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report.

Obviously, compliance with the relevant ethical requirements, including those pertaining to independence, is mandatory for auditors. However, it is not clear to us whether the disclosure of the source(s) of independence and other relevant ethical requirements provides information value to the users. In addition, member bodies of IFAC shall not apply less stringent standards than those stated in the IESBA Code of Ethics for Professional Accountants (the IESBA Code). Therefore, many jurisdictions apply the standards that are more restrictive than the IESBA code, which ensures the consistency of the ethical requirements globally. We believe investors have not requested information from the auditors on the source(s) of independence and other relevant ethical requirements that the auditor applies and in a group audit situation the component auditors apply.

In a group audit situation, the component auditor usually complies with the ethical requirements in the component auditor's jurisdiction, in addition to the IESBA Code. If the group auditor's report includes disclosure as to the sources of independence and other ethical requirements applied by the component auditors, such disclosure may result in a misunderstanding by the users. However, it is not clear as to how to apply the relevant Requirement and Application and Other Explanatory Material in proposed ISA 700 in a group audit situation.

Therefore, we do not agree with the proposal to disclose the source(s) of independence and other relevant ethical requirements in the auditor's report. If the IAASB proceeds with this proposal, we believe that, at a minimum, proposed ISA 700 should clearly explain that the description of the source(s) of independence and other relevant ethical requirements with which the component auditors comply is not required. We also have a concern with the location of the

proposed statements in the illustrative auditor’s report. The proposed statements are included in the Basis for Opinion section, which is directly below the Opinion section. However, we do not believe that the proposed statements have such a significant value to justify this prominence in the auditors’ report. We believe that the statements on independence should be located in the Auditor’s Responsibilities for the Audit of the Financial Statements section, rather than in the Basis for Opinion section.

Disclosure of the Name of the Engagement Partner

12. What are respondents’ views as to the proposal to require disclosure of the name of the engagement partner for audits of financial statements of listed entities and include a “harm’s way exemption”? What difficulties, if any, may arise at the national level as a result of this requirement?

In Japan, it is a requirement to disclose the name of the engagement partner in the auditor’s report. We have not identified any specific impediments.

Other Improvements to Proposed ISA 700 (Revised)

13. What are respondents’ views as to the appropriateness of the changes to ISA 700 described in paragraph 102 and how the proposed requirements have been articulated?

● Paragraph 37(b) (iii) and (iv) of proposed ISA 700 (Revised)

We believe that paragraph 38(b) (iii) should not be changed from paragraph 31(c) of the current ISA 700. Paragraph 37(c) of the current ISA 700 requires the auditor to state that an audit includes evaluating (i) the appropriateness of the accounting policies used, (ii) the reasonableness of accounting estimates made by management, as well as (iii) the overall presentation of the financial statements in the Auditor’s Responsibility section. However, paragraph 37(b) (iii) of proposed ISA 700 (Revised) only refers to (i) the appropriateness of the accounting policies used, and (ii) the reasonableness of accounting estimates and related disclosures made by management. We understand that this is because paragraph 37(b) (iv) of proposed ISA 700 (Revised) now requires the auditor to refer to the requirement for evaluation of fair presentation, when the financial statements are prepared in accordance with a fair presentation framework. As a result, in the case in which the auditor’s report of the financial statements is in accordance with a compliance framework (Appendix, Illustration 4 of proposed ISA 700 (Revised)), the auditor’s report does not refer to the auditor’s responsibility to evaluate the presentation of the financial statements. We are concerned that this may cause a misunderstanding that the auditor is not required to evaluate the presentation of the financial statements that is prepared in accordance with a compliance framework. We propose following revision:

“37. The auditor’s report shall further:

(b) Describe an audit by stating that the auditor’s responsibilities are:..

(iii) To evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosure made by management, as well as the overall presentation of the financial statements.”

14. What are respondents' views on the proposal not to mandate the ordering of sections of the auditor's report in any way, even when law, regulation or national auditing standards do not require a specific order? Do respondents believe the level of prescription within proposed ISA 700 (Revised) (both within the requirements in paragraphs 20–45 and the circumstances addressed in paragraphs 46–48 of the proposed ISA) reflects an appropriate balance between consistency in auditor reporting globally when reference is made to the ISAs in the auditor's report, and the need for flexibility to accommodate national reporting circumstances?

We agree with the proposal. We believe that global consistency in auditors' reports is important. However, flexibility is necessary so that national auditing standard setters can adjust the order in light of each jurisdiction's circumstances.

Other Significant Comments

(1) Effective Date

We have a concern about the proposed effective date. The Proposed ISAs will result in significant change to current practice. Audit firms need sufficient time for implementation, including establishing quality control procedures, especially with regard to the requirements for communication of key audit matters. In addition, we believe that a sufficient preparation period is critical not only for the auditors, but also for all other participants in financial reporting supply chain. Given the significance and pervasiveness of the changes, we believe that a period of 12 to 15 months after the issuance of the final standard, which is the preparation period that the IAASB typically uses, is too short. We urge the IAASB to postpone the effective date from the proposed date in the Explanatory Memorandum, so as to ensure all stakeholders have sufficient preparation time.

(2) Auditor's Responsibilities with Respect to Other Information

We have a significant concern about the direction of the project to revise ISA 720. We submitted our comment letter on the Proposed ISA 720 (Revised), published in November, 2012. In our letter, we expressed our concerns about several aspects of the Proposed ISA. It is our understanding that there are other respondents who have also submitted their letters describing their concerns. In addition, when comparing the IAASB's proposal and the Proposed Auditing Standard regarding the auditor's responsibility relating to other information that U.S. PCAOB published in August⁶, we believe that there is a significant difference between both approaches, especially with regard to the concept of material inconsistency and the auditor's work effort. If the content of the Other Information section that is included in the auditor's report of a specific entity is substantially different depending on the auditing standards with which the auditor complies, this will lead to serious confusion not only for auditors, but also for users.

We believe that the IAASB should carefully consider the comments received on Proposed ISA 720 as well as the PCAOB's recently issued Proposed Auditing Standard, and reconsider the direction of its project. In addition, considering the nature of the responses received on Proposed ISA 720, we believe re-exposure is indispensable.

We understand that the auditor reporting on other information will be considered in the project to revise ISA 720, and the Proposed ISAs does not ask the comment on this issue. However, we have provided this statement so as to clearly express our concern.

⁶ PCAOB Release No. 2013-005, Proposed Auditing Standard "The Auditor's Responsibilities Regarding Other Information in Certain Documents Containing Audited Financial Statements and the Related Auditor's Report"

Other Comments on the Proposed ISAs

Proposed ISA 700 (Revised)

- Paragraph 49

Paragraph 49 states that the supplementary information is considered to be an integral part of the financial statements, due to either its nature or how it is presented. However, this means that the financial information included as an Appendix to the financial statements (i.e. the 2nd bullet of paragraph A60 of proposed ISA 700 (Revised)) is considered to be an integral part of the financial statements, and cannot be classified as supplementary information that is not covered by the auditor’s opinion. Therefore, we propose following revision:

“49. If supplementary information that is not required by the applicable financial reporting framework is presented with the audited financial statements, the auditor shall evaluate whether, in the auditor’s professional judgment, supplementary information is nevertheless an integral part of the financial statements due to ~~either~~ its nature ~~and/or~~ how it is presented. Where it is an integral part of the financial statements, the supplementary information shall be covered by the auditor’s opinion.”

- Illustrative example of the auditor’s report, the Opinion section

For readability, we propose a change to the Opinion section of the illustrative example of the auditor’s report as described below. We understand that the intent of the proposed order is to give prominence in the auditor’s opinion. However, we believe that our proposal below sufficiently achieves this intent, when reading the auditors’ report in its entirety.

Opinion

We have audited the financial statements of the Company, which comprise the statement of financial position as at December 31, 20X1, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, (or give a true and fair view of) the financial position of ABC Company (the Company) as at December 31, 20X1, and (of) its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Proposed ISA 701

- Paragraph A9, the last sentence

In order to explain the unique concept of “relative significance in the current period audit” of key audit matters, we propose the following revision:

“A9.... Finally, key audit matters are a relative concept that are selected in the auditor’s report tailored to the specific facts and circumstances that existed during the audit of the consolidated financial statements for the current period. Therefore, it may be the case that, while a matter communicated as a key audit matter in the prior period continues to affect the financial statements of the current period, other matters arising during the current period audit may be considered to be relatively more significant and the prior period key audit matter may not, in the auditor’s judgment, be considered to be among those of most significance in the current period’s audit.”

- Paragraph A25

The first sentence, which starts with “the objective of communicating key audit matters”, may create unnecessary confusion with the “Objective” of proposed ISA 701 (i.e. paragraph 8 of proposed ISA 701). We propose following revision:

“A25. The ~~purpose objective~~ purpose of communicating key audit matters in the auditor’s report is to provide additional information about an audit in the context of the auditor having formed an opinion on the financial statements as a whole. Communicating key audit matters in the auditor’s report is not intended to:

- (a) Express an opinion on individual matters; or
- (b) Be a substitute for the auditor expressing a qualified opinion or an adverse opinion when required by the circumstances of a specific audit engagement (see proposed ISA 705 (Revised)).”

- Paragraph A37

We believe “inappropriately” in the first sentence should be deleted, since it is obvious that the auditor should not provide original information inappropriately. Also, “and providing such information is not prohibited by law or regulation” in the first sentence should be deleted, since it makes the sentence more complicated by using a double negative. The ISAs do not override law or regulation that governs an audit of financial statements. Emphasizing this point in this sentence is not necessary. We also propose the revision in the second sentence for clarification as follows:

“A37. It is appropriate for the auditor to seek to avoid the description of key audit matters ~~inappropriately~~ providing original information about the entity that is the responsibility of the entity’s management and those charged with governance unless, in the auditor’s judgment, the additional information that the auditor may provide is critical to the auditor’s description of the key audit matter ~~and providing such information is not prohibited by law or regulation~~. If, in the auditor’s judgment, providing original information about the entity is critical~~In such circumstances,~~ the auditor may encourage management or those charged with governance to make relevant disclosures in the financial statements that include such other information, so that reference can be made to those disclosures within the description of the key audit matters in the auditor’s report, rather than the auditor providing original information.”

Proposed ISA 260 (Revised)

- Appendix 2, Related Matters

We believe that the phrase “significant non-routine transaction, including transactions that are unusual, due either to size or nature, or are not in the ordinary course of business” should be changed to “significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual”. We believe that the proposed additional bullets are drafted based on paragraph A48 of ISA 240, and therefore, these bullets should be consistent with the relevant requirement, (i.e. paragraph 32(c) of ISA 240). In addition, paragraph A9, A15 and A18 of proposed ISA 701 use the phrase “significant unusual transaction”, rather than “significant non-routine transaction”.

Proposed ISA 570 (Revised)

- The description of “Going Concern Basis of Accounting” of illustration 1 to 3 in Appendix
There is overlap between the first sentence and the last sentence. We propose to delete first sentence as follows:

“Going Concern Basis of Accounting

~~The material uncertainty identified above does not indicate that the going concern basis of accounting is inappropriate.~~ The Company’s financial statements have been prepared using the going concern basis of accounting. The use of the going concern basis of accounting is appropriate unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so. As part of our audit of the financial statements, we have concluded that management’s use of the going concern basis of accounting in the preparation of the Company’s financial statements is appropriate.”