



5 October 2012

Prof. Arnold Schilder
Chairman
International Auditing and Assurance Standards Board
529 Fifth Avenue
New York, NY 10017
USA

Dear Prof. Schilder:

**re: Comments in response to Invitation to Comment on
“Improving the Auditor’s Report”**

The Corporate Accounting Committee (CAC) of the Securities Analysts Association of Japan (SAAJ) is pleased to comment on the Invitation to Comment (ITC) on “Improving the Auditor’s Report” (hereafter just “ITC”) put out by the International Auditing and Assurance Standards Board (IAASB). The SAAJ is a not-for-profit organization providing investment education and examination programs for securities analysts. Its certified members number 25,000. The CAC is a standing committee of the SAAJ composed of 14 members, most of whom are users including equity and credit analysts, and portfolio managers, while a few others are academicians and public accountants. The CAC writes comment letters to global accounting standard setters, including the International Accounting Standards Board (IASB) and Accounting Standards Board of Japan (ASBJ), and exchanges opinions with organizations including the IASB, the ASBJ, and Financial Services Agency.

General Comments

The CAC highly regards the ITC which proposes substantial improvements to auditors’ reports on financial statements. While the current auditor’s report only provides a dichotomic view of modified or unmodified opinion, the ITC proposes both qualitative and quantitative improvements which would make individual audits provide guidance for a true understanding of an entity through financial statements. In the past, we witnessed several instances when modified opinions were suddenly given to entities regarded as healthy, some of which subsequently went bankrupt in the next period. On these occasions, stock prices collapsed in a minute, depriving most investors of opportunities to sell the stocks

concerned at reasonable prices. If an auditor's report is given in the format and substance proposed in the ITC, a prudent investor would notice possible future changes in financial statements in advance and be able to liquidate his/her position before any substantial fall in stock price. It is possible that a negative view of an entity being expressed in the proposed way might trigger a fall in the stock price. However, compared to a collapse of a stock price associated with sudden bankruptcy as mentioned above, such a fall would be limited in terms of price and longer in terms of timeframe. Such moderate price adjustments would contribute to enhancing the efficient pricing of financial instruments in capital markets.

It can be argued that preparing an auditor's report as proposed in the ITC is a costly endeavor and induces higher audit fees. However, the ITC does not require disclosure of any facts that are not found in current financial statements, just that the auditor express his/her views obtained through the current auditing process. Therefore, additional costs are limited even including possible necessary dialog with management, and audit fees will not increase materially. On the other hand, the proposed auditor's opinion is beneficial in that it would contribute to promoting capital market efficiency as discussed above. Such benefits will far outweigh the costs. Following are our answers to specific questions.

1. Overall, do you believe the IAASB's suggested improvements sufficiently enhance the relevance and informational value of the auditor's report, in view of possible impediments (including costs)? Why or why not?

The CAC believes that the IAASB's suggested improvements will substantially enhance the relevance and informational value of the auditor's report by transforming what has hitherto been a mere inspection report of past financial data into a forward looking report valuable for thinking about the future of an entity. As mentioned in "General Comments" above, the benefits will far outweigh possible impediments (including costs).

3. Do you believe the concept of Auditor Commentary is an appropriate response to the call for auditors to provide more information to users through the auditor's report? Why or why not?

Important matters identified and explained by an auditor in Auditor Commentary will be precious roadmap information for financial statement users in reading statements. The CAC regards Auditor Commentary as a channel for the auditor to convey matters he/she

feels important to a wide range of financial information users.

4. Do you agree that the matters to be addressed in Auditor Commentary should be left to the judgment of the auditor, with guidance in the standards to inform the auditor's judgment? Why or why not? If not, what do you believe should be done to further facilitate the auditor's decision-making process in selecting the matters to include in Auditor Commentary?

What financial statement users want to find in Auditor Commentary are the impressions/feelings that the auditor concerned has obtained during the audit process. As these are highly subjective and qualitative, the CAC agrees that matters to be addressed in Audit Commentary should be left to the judgment of the auditor.

On the other hand, many corporate bankruptcies are actually triggered by cash flow problems. Emphasis should naturally be put on cash flow statements in auditors' selection of matters to be discussed in Audit Commentary.

5. Do the illustrative examples of Auditor Commentary have the informational or decision-making value users seek? Why or why not? If not, what aspects are not valuable, or what is missing? Specifically, what are your views about including a description of audit procedures and related results in Auditor Commentary?

The illustrative examples are valuable as visualization of the proposals in the ITC. Specifically, examples of goodwill and financial instrument valuation will be precious input for corporate valuation. Auditor's comment on material inconsistency under Other Information also has significant informational value as a bridge between audited and non-audited information.

On the other hand, the CAC thinks that description of audit procedures should be kept to a minimum because in most cases it will be a boilerplate. The CAC believes it sufficient to put standard procedures on the auditor's website while specific description be added in the Auditor Commentary when non-standard audit has been conducted.

8. What are your views on the value and impediments of the suggested auditor statements related to going concern, which address the appropriateness of management's use of the going concern assumption and whether material uncertainties have been identified? Do

you believe these statements provide useful information and are appropriate? Why or why not?

The CAC regards the proposal to require an auditor to state the appropriateness of management's use of going concern and whether material uncertainties have been identified appropriate in terms of balance between value and impediments. The CAC thinks use of the going concern assumption is within the realm of management responsibility and an auditor stepping into that territory would be expansion of audit practices and be too costly.

9. What are your views on the value and impediments of including additional information in the auditor's report about the auditor's judgments and processes to support the auditor's statement that no material uncertainties have been identified?

In situations, as described in paragraph 30, where the auditor may have determined that no material uncertainties exist, but certain events or conditions nevertheless have been identified that may cast significant doubt on the entity's ability to continue as a going concern, the CAC believes such events or conditions should be explained in Auditor Commentary. Paragraph 31 expresses concern that such explanation may disclose entity specific information that has not been disclosed by management. However, if such information is about events or conditions that may cast significant doubt on the entity's viability and such information can be inferred from financial statements, such information should be disclosed by management in the first place. To make such disclosure possible, accounting standards or disclosure requirements may need to be revised in some jurisdictions.

10. What are your views on the value and impediments of the suggested auditor statement in relation to other information?

So far, audited financial statements and non-audited other information including MD&A and OFR etc. are perceived by financial statement users as divided and qualitatively different sets of information. The CAC welcomes the proposed auditor statement of other information as a bridge which connects two sets of information to enhance the decision usefulness of financial reports. The CAC regards the analysis of value

and impediments in ITC as appropriate.

15. What are your views on whether the IAASB's suggested structure of the illustrative report, including placement of the auditor's opinion and the Auditor Commentary section towards the beginning of the report, gives appropriate emphasis to matters of most importance to users?

The proposals in the ITC will significantly improve auditors' reports. The CAC agrees to place the auditor's opinion at the beginning of the report as a symbol of such improvement. The CAC thinks the proposed illustrative report is appropriate.

If you have any questions or need further elaboration, please do not hesitate to contact Sei-Ichi Kaneko, Executive Vice President, SAAJ (s-kaneko@saa.or.jp).

Sincerely yours,



Keiko Kitamura

Chair

Corporate Accounting Committee