



Auditing and Assurance Standards Committee
Meeting Summary – July 2006

The Auditing and Assurance Standards Committee (Committee) met on 20 July 2006.

Members present at the meeting were: Richard George (Deputy Chairman as Acting Chairman), Keith Pogson (Deputy Chairman), Colin Chau, William Crowe, Lucia Li (Represented by Li Kwok-tso), Ng Shiu Hong, Michael Sim, Kelvin Wong, Wilfred Wong, Thomas Wong and Desmond Yuen (Represented by Mabel Cheung).

Secretariat staff present at the meeting were: Patricia McBride, Steve Ong, Elaine Chan and Elsa Ho.

The following agenda items were discussed:

1. IAASB Proposed Guide for National Setters that adopt International Standards
2. Proposed HKSA 700 “The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements” and HKSA 701 “Modifications to The Independent Auditor’s Report”
3. Draft Submission on IAASB Exposure Draft of Proposed ISA 600 (Revised and Redrafted) on the Audit of Group Financial Statements
4. Comments received on the application of PN 730 “Guidance for Auditors Regarding Preliminary Announcements of Annual Results”
5. Accountants’ Report Project – Progress Report

1. IAASB Proposed Guide for National Setters that adopt International Standards

The Committee noted that the IAASB had issued a proposed guide for National Setters that adopt International Standards. It was noted that the following modifications to an International Standard should be communicated to the IAASB:

- Additions to an International Standard of “other requirements or guidance” that are not inconsistent with the current requirements or guidance on the International Standard
- Deletions from, or other amendments to an International Standard on requirements or guidance, the application of which law or regulation does not permit, or which require amendment to be consistent with law or regulation.

[Post meeting note: The proposed guide was issued by the IAASB as a final guide on 28 July 2006.]

2. Proposed HKSA 700 “The Independent Auditor’s Report on a Complete Set of General Purpose Financial Statements” and HKSA 701 “Modifications to The Independent Auditor’s Report”

The Committee considered and discussed at length the revised proposed HKSA 700 and HKSA 701 and recommended certain local guidance to be reflected as footnotes. Certain improvement changes were also made to the draft example audit reports developed locally to be reflected in the appendices to the proposed Standards.

It was agreed that the recommended changes would be updated by the secretariat and thereafter circulated to the members of the Committee for their further consideration by the end of August. It was noted that the plan is to have final drafts of the proposed HKSA 700 and HKSA 701 endorsed by the Committee at its meeting in September and that Council’s approval be obtained shortly thereafter in order that the final Standards are issued in early October.

It was also agreed that once the proposed HKSA 700 and HKSA 701 are finalized, which will have seven local example audit reports, other example audit reports and a Chinese version example audit report can be developed.

[Post meeting note: The proposed HKSA 700 and HKSA 701 were submitted to Council for approval by circulation on 4 October 2006.]

3. Draft Submission on IAASB Exposure Draft of Proposed ISA 600 (Revised and Redrafted) on the Audit of Group Financial Statements

The Committee noted that the consultation period of the Institute's Invitation to Comment ended on 7 July and comments were received from a member firm.

The Committee considered the Institute's draft submission to the IAASB prepared by the secretariat based on the key point of the submission received and suggested certain editorial changes. The secretariat was requested to revise the draft submission incorporating the Committee's comments.

[Post meeting note: The revised Institute's submission was endorsed by the Committee by circulation and approved by Council at its July meeting for submission to the IAASB.]

4. Comments received on the application of PN 730 "Guidance for Auditors Regarding Preliminary Announcements of Annual Results"

The Committee considered the comments received from two committee members and noted the following:

- Listed issuers were generally confused as to when they could or could not use the term "audited" in preliminary announcements
- Listed issuers would generally prefer not to hold two board meetings to approve the following matters:
 - the preliminary announcement (usually based on draft financial statements where audit is substantially completed but where audit report has not been signed); and
 - the final audited financial statements.

It was noted that the practice in Hong Kong would normally be to hold only one board meeting to approve both the above matters (preliminary announcement and the financial statements for the year (draft/audited)). As a result of this, some confusion has arisen among listed issuers as to whether the draft financial statements could be classified as "audited" after the board meeting approving the preliminary announcement. The position taken by the Committee was that a preliminary announcement of the results should not be classified as "audited" until the audit report is signed. The Committee was of the view that the Exchange might need to provide more information/education to listed issuers in this regard.

5. Accountants' Report Project – Progress Report

The Acting Chairman gave a brief summary of the status of the project and took the Committee through an issues paper that summarized the key proposals in the professional pronouncements developed under the project which have not yet been finalized and the major issues relating to those proposals, including:

- Independence requirement of reporting accountants;
- Requirement for sponsors to be party to the engagement letter;
- The respective roles and responsibilities of directors and reporting accountants under the proposed new reporting framework;
- The new format of the accountants' report;
- Reporting accountants' opinion on historical financial information;
- Reporting on statement of adjustments;
- Reference to previous audit qualifications and previous auditors in the accountants' report;
- Reporting accountants' opinion on cash flow forecasts and projections; and
- Reporting accountants' opinion on schedule of indebtedness.

The Acting Chairman also went through the proposed consequential changes to the Listing Rules in order to put in place the new proposals.

The Committee discussed the opinion to be given by reporting accountants on historical financial information and the interaction with the proposed Accounting Guideline (AG) 6 "Preparation of Historical Financial Information for Inclusion in Investment Circulars". It was noted that the proposed AG 6 specifically permits the financial statements of entities that have been under common control but have not yet formed a legal group throughout the track record period to be presented on a combined basis provided that the group reorganization is completed before the date of the approval of the consolidated financial statements by the directors. It was also noted that under the proposals, reporting accountants' would report in "true and fair" terms for the purposes of the investment circular in accordance with a basis of preparation to be set out in the notes to the historical financial information.

The Committee considered whether it would be necessary to provide guidance on circumstances where directors of listing applicants are not able to sign the engagement letter prior to the start of the reporting accountants' engagement since the directors have not yet been appointed at that time. It was considered that the issue would better be dealt with between the reporting accountants, the listing applicant and its legal advisor rather than through a professional pronouncement issued by the Institute.

Subject to any further comments that might be raised by members before the end of July 2006, the Committee endorsed the submission of the following proposed professional pronouncements, together with the proposed AG 6 that was earlier endorsed by the Financial Reporting Standards Committee, to the Stock Exchange and the Securities and Futures Commission for consideration of consequential changes to the Listing Rules:

- a. HKSIR 100 "Investment Circulars and Reporting Accountants";
- b. HKSIR 200 "Accountants' Report on Historical Financial Information in Investment Circulars"; and
- c. PN 2000 "Other Letters Issued in Relation to Investment Circulars".

[Post meeting note: Subsequent to the meeting, the secretariat received some further comments on HKSIR 100, HKSIR 200 and AG 6 from a member. A meeting and a conference call were held on 15 August 2006 and 23 August 2006 respectively to discuss the comments.]

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