

STATEMENT 3.0

AUDITING STANDARDS AND GUIDELINES

EXPLANATORY FOREWORD

Introduction

1. This Explanatory Foreword explains the scope and authority of Auditing Standards and Auditing Guidelines approved by the Council of the Hong Kong Society of Accountants (HKSA). It should be read in conjunction with the Auditing Standards and Guidelines to which it forms a collective preface. (The ethical standards relevant to the work of an auditor are described in ethical statements published by the HKSA.)

Definitions

2. An "audit" is the independent examination of, and expression of an opinion on, the financial statements of an entity. (When reading Auditing Standards and Guidelines, the term "entity" should be read as embracing any body corporate or other organisation, whether profit oriented or not.)
3. Unless the relevant Auditing Standard or Auditing Guideline indicates to the contrary, the term "audit" applies:
 - a. where there is a statutory requirement for the auditor to express an opinion in terms of whether the financial statements give a true and fair view (for example, audits under the Companies Ordinance);
 - b. where there is a statutory requirement for the auditor to express an opinion in terms other than whether the financial statements give a true and fair view (for example, audits of statutory corporations); and
 - c. where the terms and scope of the engagement are agreed between the auditor and his client (for example, the audit of a sole trader or partnership) or where they are specified in a legal document (for example, a trust deed).
4. Where the term "the auditor" is used, reference is to the individual, the firm or the organisation carrying out the audit of the entity. Where appropriate the term includes the auditor's staff acting within

delegated authority, and references to the masculine include the feminine.

5. "Financial statements" comprise all those statements and other financial information which are identified as being within the scope of the audit. These will normally include balance sheets, profit and loss accounts (or other forms of income and expenditure statements) and statements of changes in financial position together with relevant notes.
6. The responsibility for the preparation of financial statements and the presentation of the information included therein rests with the management of the entity (in the case of a company, the directors). The auditor's responsibility is to report on the financial statements as presented by management.

Scope and authority of Auditing Standards

7. Auditing Standards are those Statements of Auditing Standards which have been approved for issue by the Council of the HKSA.
8. Auditing Standards prescribe the basic principles and practices which members of the HKSA are expected to follow in the conduct of an audit. Auditing Standards apply whenever an audit is carried out by them.
9. Members of the HKSA who assume responsibility as auditors are expected to observe Auditing Standards. Apparent failures by members to observe Auditing Standards may be enquired into by the appropriate committees established by the Council of the HKSA, and disciplinary action may result.
10. It would be impracticable to establish a code of rules sufficiently elaborate to cater for all situations and circumstances which an auditor might encounter. Such a code could not provide for innovations in business and financial practice and might hinder necessary development and experiment in auditing practice. In the observance of Auditing Standards, therefore, the auditor must exercise his judgement in determining both the auditing procedures necessary in the circumstances to afford a reasonable basis for his opinion and the wording of his report.
11. Explanatory notes may be added to the text of Auditing Standards. These explanatory notes have the same scope and authority as Auditing Guidelines (see paragraphs 13 and 14 below).

Scope and authority of Auditing Guidelines

12. Auditing Guidelines are those guidelines which have been approved for issue by the Council of the HKSA.
13. Auditing Guidelines are intended to assist the auditor by giving guidance on:
 - a. procedures by which Auditing Standards may be applied;
 - b. the application of Auditing Standards to specific items appearing in the financial statements of entities;
 - c. the application of Auditing Standards to particular sectors, industries and service organisations;
 - d. specific types of reporting engagement other than audits as defined in paragraph 2; and
 - e. other matters relating to the proper performance of audit work.
14. Auditing Guidelines are intended to be persuasive. They are not prescriptive and there may be occasions when the auditor considers it appropriate to depart from the guidance given. However, they should normally be followed, and the auditor should be prepared to explain departures if called upon to do so.

Auditing Standards and Guidelines and the law

15. Members are advised that a court of law may, when considering the adequacy of the work of an auditor, take into account any pronouncements or publications which it thinks may be indicative of good practice. Auditing Standards and Guidelines are likely to be so regarded.

International auditing pronouncements

16. International Auditing Guidelines are issued by the International Federation of Accountants. The HKSA have agreed to incorporate the principles on which International Auditing Guidelines are based into their own Auditing Standards and Guidelines when and to the extent practicable. International Auditing Guidelines are authoritative in Hong Kong only to the extent that they have been so incorporated.

Application of Auditing Standards overseas

17. Where the financial statements of an entity, wherever incorporated are audited by a Hong Kong auditor (as represented by signing the audit report in the style "Certified Public Accountant, Hong Kong") the audit of the entity should conform to Auditing Standards, unless paragraph 19 applies in which case specific reference to the auditing standards adopted must be made in the audit report.
18. Where the financial statements of an overseas entity are to be incorporated into Hong Kong financial statements, the audit of the overseas entity should conform to Auditing Standards in so far as this is necessary to ensure that the audit of the Hong Kong financial statements as a whole is in accordance with Auditing Standards.
19. Where a member of the HKSA is carrying out an audit overseas for purposes other than Hong Kong reporting, Auditing Standards may not be appropriate. The auditor should therefore observe any generally accepted local standards or practice when carrying out the audit.

Technical Bulletins

20. Technical Bulletins may be issued by the Auditing Standards Committee. They are informative publications on subjects of topical interest and are intended to assist auditors in the discharge of their duties or to stimulate debate on important auditing issues. They do not require the approval of the Council of the HKSA and they do not have the same authority as either Auditing Standards or Auditing Guidelines.

APPENDIX

Glossary of terms

The following terms in this Explanatory Foreword, in the Auditing Standards and in the Auditing Guidelines are used with the following meanings:

1. *Audit* — The independent examination of, and expression of opinion on, the financial statements of an entity by an appointed auditor in pursuance of that appointment and in compliance with any relevant statutory obligation.
2. *Joint audit* — Where two or more auditors are responsible for an audit engagement and jointly produce an audit report to the client.
3. *The auditor(s)* — The individual or firm carrying out the audit of the entity and the partners of such individual or in such firm. Where appropriate the term includes audit staff acting within delegated authority.
4. *Audit staff* — Those members of the auditor's staff, who take a direct part in an audit engagement.
5. *The entity* — Any body corporate or other organisation on whose financial statements the auditor is reporting.
6. *Financial statements* — Balance sheets and profit and loss accounts (or other forms of income statements) together with such additional statements and notes as are identified as being within the scope of the audit opinion.
7. *Reporting partner* — The partner in a firm responsible for the conduct of the audit.
8. *Internal control system* — The whole system of controls, financial and otherwise, established by the management in order to carry on the business of the entity in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of the records. The individual components of an internal control system are known as "controls" or "internal controls".

9. *Compliance and substantive tests* — Audit tests classified according to their primary purpose. Both purposes are sometimes achieved concurrently.
 - a. *Compliance tests* — Those tests which seek to provide audit evidence that internal control procedures are being applied as prescribed.
 - b. *Substantive tests* — Those tests of transactions and balances, and other procedures such as analytical review, which seek to provide audit evidence as to the completeness, accuracy and validity of the information contained in the accounting records or in the financial statements.
10. *Auditing Standards* — Those Statements of Auditing Standards which are approved for issue by the Council of the Hong Kong Society of Accountants and which are effective for the period covered by the financial statements on which the auditor is reporting.