

STATEMENT 3.290
AUDITING GUIDELINE
AUDIT APPROACH TO COMPANIES APPLYING SECTION 141D
OF COMPANIES ORDINANCE

Introduction

1. Paragraph 3 of the Explanatory Foreword to Auditing Standards and Guidelines states that "unless otherwise indicated in the text, Auditing Standards apply whenever an audit is carried out". This Guideline gives guidance on the applicability of auditing standards and guidelines to the audit of companies applying Section 141D of the Companies Ordinance. The guideline has been prepared on the basis of legal advice as to the status of an audit opinion under Section 141D.
2. Section 141D of the Companies Ordinance exempts certain private companies from complying with the full disclosure requirements of the Ordinance. In particular, companies which take advantage of these exemptions do not have to produce financial statements which show a true and fair view of the state of the company's affairs and of its profit or loss for the year. Instead the auditor is required to report on whether the company's balance sheet shows a true and correct view of the state of the company's affairs. A profit and loss account is still required to be included into the financial statements even though the audit report covers only the balance sheet. Details of the exemptions are summarised in Appendix 1 but reference should be made to the Companies Ordinance for the exact requirements.
3. There is no statutory definition of either a "true and fair view" or a "true and correct view" and consequently no clear legal explanation of the difference, if any, between the two. It appears, however, that the two concepts do differ from each other and that the fact that financial statements show a true and correct view does not necessarily mean that they also show a true and fair view. This guideline therefore gives guidance on the extent of audit work necessary to reach an opinion on financial statements prepared under Section 141D.

Applicability of accounting and auditing standards

4. Although the Explanatory Foreword to Accounting Standards does not refer to the applicability of accounting standards to financial statements which show a true and correct view, it is the Society's opinion that the requirements of accounting standards should be

applied to such statements except that, to the extent that the standards prescribe disclosure requirements, these do not override the exemptions granted under Section 141D of the Companies Ordinance. An analysis of the applicability of accounting standards is included in Appendix 2.

5. As discussed in paragraph 1 above, auditing standards apply whenever an audit is carried out, unless otherwise indicated in the text. An analysis of the applicability of auditing standards and guidelines is included in Appendix 3.

Audit procedures

6. The same procedures should be adopted for all audits regardless of the extent to which disclosure must be made in the financial statements. Thus, whilst the audit report is limited to the balance sheet prepared under Section 141D, the auditor should still carry out the appropriate tests on profit and loss account items to ensure that the net results for the year, incorporated in the balance sheet, are true and correct.
7. In addition to carrying out the normal audit procedures required to comply with Auditing Standard 3.101, the auditor should ensure:
 - (a) that the company is entitled to take advantage of the exemptions permitted under Section 141D(3);
 - (b) that the shareholders have entered into a new unanimous agreement for the particular financial year under review; and
 - (c) that the balance sheet contains the information required under the Eleventh Schedule.

The audit report

8. The contents of the audit report are outlined specifically in the section and an example is attached as Appendix 4. The general requirements of Auditing Standard 3.102 and Auditing Guideline 3.310 "The auditor's report on financial statements" should be adopted with such modifications as are appropriate. In particular, auditors are asked to note the following:
 - (a) the audit report should identify those to whom it is addressed;
 - (b) the report should normally be dated with the date on which the financial statements are approved by the directors, or the date of completion of the audit if this is later, and should make clear the fact that it is signed in Hong Kong;

- (c) the auditor should refer expressly in his report to the fact that the financial statements have been audited in accordance with approved Auditing Standards for the reasons discussed in paragraph 6 above;
 - (d) the auditor is required by Section 141D to state explicitly whether or not he has obtained all the information and explanations which he required;
 - (e) the auditor's opinion must refer to whether the balance sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs according to the best of the auditor's information and the explanations given to him, and as shown by the books of the company.
9. Where the auditor is unable to give an affirmative opinion, the principles relating to qualified audit reports, outlined in Auditing Standard 3.102 and Auditing Guideline 3.320 "Forms of qualifications in auditors' reports" should be adopted. Consequently the auditor should refer to all material matters about which he has reservations in a separate paragraph or paragraphs. In particular the amounts involved should be quantified where this is relevant and practicable and the qualification should leave the reader in no doubt as to its meaning and its implications for an understanding of the financial statements.
10. It is possible that many companies which apply Section 141D will have systems of control which are dependent upon the close involvement of the directors. In such cases the auditor should consider whether he needs to qualify his audit report on this basis. If so, the wording proposed in Example 12 "Uncertainty — subject to: acceptance of management assurances (small business)" in Auditing Guideline 3.330 "Audit report examples" may be appropriate.
11. It should be noted that, whilst the statutory audit report makes no reference to compliance with the disclosure provisions of the Companies Ordinance, the auditor still has an obligation under Sections 161 and 161B to give details in his report of directors' remuneration and loans to officers to the extent that the information is not provided in the financial statements.

Appendix 1

EXEMPTIONS

Section 141D(1) exempts certain private companies from complying with the following requirements of the Companies Ordinance:

- S121(2) Books of account to give a true and fair view of the state of the company's affairs and to explain its transactions.
- S123 Balance sheet to give a true and fair view of the state of affairs of the company as at the end of its financial year.
- Profit and loss account of a company to give a true and fair view of the profit or loss of the company for the financial year.
- Balance sheet and profit and loss account to comply with the Tenth Schedule of the Companies Ordinance, so far as applicable.
- S129 Statement in company's financial statements of identities and places of incorporation of companies, other than subsidiaries, whose shares it holds, and particulars of those shares.
- S129A Statement in subsidiary company's financial statements of name and place of incorporation of its ultimate holding company.
- S129D Directors' report to be attached to balance sheet [NB Section 141D(1)(c) does make certain provisions for a limited directors' report.].
- S129E Directors' report to show corresponding amounts for preceding financial year for items included under authority of proviso to Section 141C.
- S141(3) Auditors' report to state whether the financial statements have been prepared in accordance with the provisions of the Companies Ordinance and whether in their opinion the financial statements give a true and fair view.

Appendix 2

APPLICABILITY OF ACCOUNTING STANDARDS

The following table outlines the applicability of individual accounting standards to financial statements prepared under Section 141D.

<i>Accounting Standards</i>	<i>Applicable</i>
2.101 Disclosure of accounting policies:	
Adoption of fundamental concepts	YES
Disclosure of material accounting policies	YES
2.102 Extraordinary items and prior year adjustments:	
Disclosure of extraordinary and exceptional items	YES (Note 1)
Treatment of prior year adjustments	YES (Note 1)
Presentation of profit and loss account	YES (Note 1)
2.103 Stocks and work in progress:	
Valuation of stocks and work in progress	YES
Disclosure in financial statements	YES
2.104 Statements of changes in financial position	NO
2.105 Earnings per share	NO
2.106 Depreciation accounting:	
Calculation of depreciation charge	YES
Treatment of land and buildings	YES
Disclosure in financial statements	YES (Note 2)
2.107 Group accounts	N/A
2.108 Accounting for contingencies	YES
2.109 Accounting for post balance sheet events	YES

<i>Accounting Standards</i>	<i>Applicable</i>
2.110 Accounting for the results of associated companies:	
Treatment in individual company's financial statements	YES
Treatment in consolidated financial statements	N/A
Disclosure of particulars	NO
2.111 Foreign currency translation:	
Treatment in individual company's financial statements	YES
Forward contracts	YES
Treatment in consolidated financial statements	N/A
Disclosure	YES

NOTES

Note 1: applicable only if company's financial statements include a profit and loss account

Note 2: excluding paragraph 20(d)

Appendix 3

**APPLICABILITY OF AUDITING STANDARDS
AND GUIDELINES**

The following table outlines the applicability of individual auditing standards and guidelines to financial statements prepared under Section 141D.

<i>Auditing Standards</i>	<i>Applicable</i>
3.101 Audit approach	YES
3.102 Reporting:	
Form and content of report	YES (Note 1)
Compliance with approved Auditing Standards	YES
True and fair view	NO
Compliance with legislation	YES
Emphasis of matter	YES
Qualified reports	YES
 <i>Auditing Guidelines</i>	
3.210 Planning, controlling, and recording	YES
3.211 Quality control	YES (Note 2)
3.220 Accounting systems	YES
3.230 Audit evidence	YES
3.231 Auditing stocks and work in progress	YES
3.232 Verification of debtor balances: confirmation by direct communication	YES
3.240 Internal controls	YES (Note 3)
3.250 Review of financial statements	YES
3.251 The auditor's considerations in respect of going concern	YES
3.252 Events after the balance sheet date	YES
3.260 Auditing in an EDP environment — general principles	YES

3.261	The effects of an EDP environment on the study and evaluation of the accounting system and related internal controls	YES
3.262	Computer – assisted audit techniques (CAATs)	YES
3.270	Engagement letters	YES
3.280	Group financial statements — reliance on the work of other auditors	YES

Auditing Guidelines

Applicable

3.310	The auditor's report on financial statements:	
	Form of report	YES
	Companies Ordinance requirements	NO (Note 4)
	Statements of standard accounting practice	YES (Note 5)
	Statements of changes in financial position	N/A
	Reports on group financial statements	N/A
3.320	Forms of qualifications in auditors' reports	YES (Note 6)
3.330	Audit report examples	YES (Note 7)

NOTES

- Note 1: Paragraph 4(b), relating to true and fair view, is inapplicable but S141D requirements will need to be met instead.
- Note 2: Guideline does not relate specifically to audits of any financial statements but rather to conduct of audit firm and applies irrespective of type of work carried out.
- Note 3: It is probable that companies which apply Section 141D will be too small to ensure the existence of an adequate internal control system. Substantive testing, as discussed in Auditing Guideline 3.230, is therefore more likely to be appropriate in such cases.
- Note 4: S141D requirements should be applied instead.
- Note 5: Audit reports should refer to departures from SSAPs to the extent that these apply to Section 141D financial statements (see Appendix 2).
- Note 6: Guideline applies to the extent that it refers to form of qualification only (see paragraph 9 of this guideline).
- Note 7: Example 4 refers specifically to private companies applying Section 141D.

Appendix 4

DRAFT REPORT OF THE AUDITORS**Report of the Auditors to the Members of Limited**

We have audited the balance sheet together with the notes thereon in accordance with approved Auditing Standards and have obtained all the information and explanations we have required.

In our opinion, the balance sheet together with the notes thereon is properly drawn up so as to exhibit a true and correct view of the state of affairs of the company at, 19 according to the best of our information and the explanations given to us and as shown by the books of the company.