

29th October 2013

Sent by Email

Mr. Simon Riley
Director, Standard Setting Department
Hong Kong Institute of Certified Public Accountants
37/F., Wu Chung House
213 Queen's Road East
Hong Kong

Dear Sirs,

Re: Comment on IFAC's International Auditing and Assurance Standards Board (IAASB) Exposure Draft

The Hong Kong Society of Financial Analysts welcomes the opportunity to comment on the IAASB's Exposure Draft to enhance auditor reporting globally.

As users of audited financial statements, we state our comments to the specific questions (Questions: 1, 2, 3, 5, 6, 8, 10) as set out in the Exposure Draft as follows:

Key Audit Matters

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?

Historically, audit reports have been relied upon as the default source of information about the Company's financial position. The usage of audit reports has increased dramatically, both in terms of number of users and nature of information sought. Hence, we believe that the introduction of a new section in the auditor's report describing the matters the auditor determined to be of most significant in the audit will absolutely enhance the usefulness of the auditor's report. There currently is not enough transparency in the two paragraphs found in the current format of the auditor reports. However, such information has the potential to have market impact or may negatively affect business outcomes. As an audit firm may be open to litigation in the case that an inappropriate opinion is issued and relied upon, it has significant incentive not to do so unless it is comfortable with the opinion that is being issued. As such, if management and a firm's opinions on the content of the audit report differ significantly, it is more common to see an auditor resign from the engagement to avoid exposure to litigation. If auditors do disclose key audit matters and there is a negative market event as a result of the disclosure, it will be useful to know if auditors would be held liable for this. To encourage disclosure from auditors, it may be necessary to provide clear guidelines on materiality and to include other areas such as commentary/opinions from management.

The inclusion of “significant matters” in the report will likely:

- 1) provide a broader spectrum of users with relevant information based on which they may form their own conclusions or undertake further analysis;
 - 2) enforce further transparency on the part of the Company; and
 - 3) engender an additional degree of rigor, analysis and transparency to the work done by auditors since material issues considered will now be under the public eye.
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?

Yes. The proposed requirements and related application material in proposed ISA 701 should provide an appropriate framework to guide the auditor’s judgment. Over a period of time, auditor judgment can be expected to be consistent as the framework is publicly applied across time, across clients/industries and also across firms.

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 description of individual key audit matters to be communicated in the auditor’s report? If not, why?

Yes. We agree that the proposed requirements and application material provide sufficient direction and in any event, these materials should be supplemental to the existing process whereby the auditors consider key areas while planning the audit. The significant difference going forward would only be the selection and communication of key matters for which the current guidance appears to be adequate.

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?

No, voluntary basis would most likely not work. Firstly, from a risk management point of view, it can be expected that an auditor will avoid commenting on key matters where unless specifically required, since matters of significant concern would in any case result in modification/qualification of the report. By making it voluntary, it is no longer a standard. Secondly, it raises some issues of asymmetric information - an auditor that opts to not issue any opinions in key audit matters would draw scrutiny to the company and vice versa.

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?
- If so, do respondents agree with the proposed requirements addressing such circumstances?
 - If not, do respondents believe the 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?

It is conceivable that there might be instances where the auditor finds no key matters to be communicated. However, in these cases, a statement to that effect is onerous enough and adequate.

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?

Yes, there is some overlap but they ultimately improve transparency if used together. Emphasis of matter highlights significant findings (such as going concern).

Going Concern

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?

It is doubtful that management would be interested in providing an explicit statement. Frankly speaking, there is limited benefit to be gained from making such a statement as most users should understand this.

HK SFA appreciates the opportunity to comment on IAASB's Exposure Draft which proposes changes to audit reports, including the provision of more information on how audits are performed. We trust you find our comments constructive and useful.

Your Sincerely,
For and on behalf of
The Board of The Hong Kong Society of Financial Analysts

Jimmy Jim, CFA / Ashley Khoo, CFA
Advocacy Chairs