HKSA 560
Issued June 2005

Effective for audits of financial statements
for periods beginning on or after 15 December 2004*

Hong Kong Standard on Auditing 560

Subsequent Events

* This HKSA 560 is effective for audits of financial statements for periods beginning on or after 15 December 2004. HKSA 560 (Revised) issued in October 2006 is effective for auditor's report dated on or after 31 December 2006 and supersedes this HKSA 560.

Hong Kong Institute of
Certified Public Accountants
香港會計師公會

INTERNATIONAL STANDARD ON AUDITING 560

SUBSEQUENT EVENTS

(Effective for audits of financial statements
for periods beginning on or after 15 December 2004)

CONTENTS

	Paragraphs
Introduction	1-3
Events Occurring Up to the Date of the Auditor's Report	4-7
Facts Discovered After the Date of the Auditor's Report But Before the Financial Statements are Issued	8-12
Facts Discovered After the Financial Statements Have Been Issued	13-18
Offering of Securities to the Public	19
Effective Date	20
Conformity and Compliance with International Standards on Auditing	21-22
Appendix: Additional local guidance on "facts discovered after the financial statements are laid before the shareholders or equivalent"	

Hong Kong Standard on Auditing (HKSA) 560, "Subsequent Events" should be read in the context of the "Preface to Hong Kong Standards on Quality Control, Auditing, Assurance and Related Services" which sets out the application and authority of HKSAs.

Introduction

1. The purpose of this Hong Kong Standard on Auditing (HKSA) is to establish standards and provide guidance on the auditor's responsibility regarding subsequent events. In this HKSA, the term "subsequent events" is used to refer to both events occurring between period end and the date of the auditor's report, and facts discovered after the date of the auditor's report.

2. **The auditor should consider the effect of subsequent events on the financial statements and on the auditor's report.**

3. Hong Kong Accounting Standard 10, "Events after the Balance Sheet Date" deals with the treatment in financial statements of events, both favourable and unfavourable, occurring after period end and identifies two types of events:

   (a) Those that provide evidence of conditions that existed at the balance sheet date (adjusting events after the balance sheet date); and

   (b) Those that are indicative of conditions that arose after the balance sheet date (non-adjusting events after the balance sheet date).

Events Occurring Up to the Date of the Auditor's Report

4. **The auditor should perform audit procedures designed to obtain sufficient appropriate audit evidence that all events up to the date of the auditor's report that may require adjustment of, or disclosure in, the financial statements have been identified.** These procedures are in addition to procedures which may be applied to specific transactions occurring after period end to obtain audit evidence as to account balances as at period end, for example, the testing of inventory cutoff and payments to creditors. The auditor is not, however, expected to conduct a continuing review of all matters to which previously applied audit procedures have provided satisfactory conclusions.

5. The audit procedures to identify events that may require adjustment of, or disclosure in, the financial statements would be performed as near as practicable to the date of the auditor's report. Such audit procedures take into account the auditor's risk assessment and ordinarily include the following:

   - Reviewing procedures management[2] has established to ensure that subsequent events are identified.
   - Reading minutes of the meetings of shareholders, those charged with governance, including established committees such as relevant executive committees and the audit committee, held after period end and inquiring about matters discussed at meetings for which minutes are not yet available.
   - Reading the entity's latest available interim financial statements and, as considered necessary and appropriate, budgets, cash flow forecasts and other related management reports.
   - Inquiring, or extending previous oral or written inquiries, of the entity's legal counsel concerning litigation and claims.
   - Inquiring of management as to whether any subsequent events have occurred which might affect the financial statements. Examples of inquiries of management on specific matters are:
     - ➢ The current status of items that were accounted for on the basis of preliminary or inconclusive data.
     - ➢ Whether new commitments, borrowings or guarantees have been entered into.

1 Not used.

2 Under the Companies Ordinance, the directors are responsible for the preparation of financial statements showing a true and fair view.

- Whether sales or acquisition of assets have occurred or are planned.
- Whether the issue of new shares or debentures or an agreement to merge or liquidate has been made or is planned.
- Whether any assets have been appropriated by government or destroyed, for example, by fire or flood.
- Whether there have been any developments regarding risk areas and contingencies.
- Whether any unusual accounting adjustments have been made or are contemplated.
- Whether any events have occurred or are likely to occur which will bring into question the appropriateness of accounting policies used in the financial statements as would be the case, for example, if such events call into question the validity of the going concern assumption.

6. When a component, such as a division, branch or subsidiary, is audited by another auditor, the auditor would consider the other auditor's procedures regarding events after period end and the need to inform the other auditor of the planned date of the auditor's report.

7. **When the auditor becomes aware of events which materially affect the financial statements, the auditor should consider whether such events are properly accounted for and adequately disclosed in the financial statements.**

Facts Discovered After the Date of the Auditor's Report But Before the Financial Statements are Issued

8. The auditor does not have any responsibility to perform audit procedures or make any inquiry regarding the financial statements after the date of the auditor's report. During the period from the date of the auditor's report to the date the financial statements are issued, the responsibility to inform the auditor of facts which may affect the financial statements rests with management.

9. **When, after the date of the auditor's report but before the financial statements are issued, the auditor becomes aware of a fact which may materially affect the financial statements, the auditor should consider whether the financial statements need amendment, should discuss the matter with management, and should take the action appropriate in the circumstances.**

10. When management amends the financial statements, the auditor would carry out the audit procedures necessary in the circumstances and would provide management with a new report on the amended financial statements. The new auditor's report would be dated not earlier than the date the amended financial statements are signed or approved and, accordingly, the audit procedures referred to in paragraphs 4 and 5 would be extended to the date of the new auditor's report.

11. **When management does not amend the financial statements in circumstances where the auditor believes they need to be amended and the auditor's report has not been released to the entity, the auditor should express a qualified opinion or an adverse opinion.**

12. When the auditor's report has been released to the entity, the auditor would notify those charged with governance not to issue the financial statements and the auditor's report thereon to third parties. If the financial statements are subsequently released, the auditor needs to take action to prevent reliance on the auditor's report. The action taken will depend on the auditor's legal rights and obligations and the recommendations of the auditor's lawyer.

Facts Discovered After the Financial Statements Have Been Issued[3]

13. After the financial statements have been issued, the auditor has no obligation to make any inquiry regarding such financial statements.

14. **When, after the financial statements have been issued, the auditor becomes aware of a fact which existed at the date of the auditor's report and which, if known at that date, may have caused the auditor to modify the auditor's report, the auditor should consider whether the financial statements need revision, should discuss the matter with management, and should take the action appropriate in the circumstances.**

15. When management revises the financial statements, the auditor would carry out the audit procedures necessary in the circumstances, would review the steps taken by management to ensure that anyone in receipt of the previously issued financial statements together with the auditor's report thereon is informed of the situation, and would issue a new report on the revised financial statements.

16. **The new auditor's report should include an emphasis of a matter paragraph referring to a note to the financial statements that more extensively discusses the reason for the revision of the previously issued financial statements and to the earlier report issued by the auditor.** The new auditor's report would be dated not earlier than the date the revised financial statements are approved and, accordingly, the audit procedures referred to in paragraphs 4 and 5 would ordinarily be extended to the date of the new auditor's report. Local regulations of some countries permit the auditor to restrict the audit procedures regarding the revised financial statements to the effects of the subsequent event that necessitated the revision. In such cases, the new auditor's report would contain a statement to that effect.

17. When management does not take the necessary steps to ensure that anyone in receipt of the previously issued financial statements together with the auditor's report thereon is informed of the situation and does not revise the financial statements in circumstances where the auditor believes they need to be revised, the auditor would notify those charged with governance of the entity that action will be taken by the auditor to prevent future reliance on the auditor's report. The action taken will depend on the auditor's legal rights and obligations and the recommendations of the auditor's lawyers.

18. It may not be necessary to revise the financial statements and issue a new auditor's report when issue of the financial statements for the following period is imminent, provided appropriate disclosures are to be made in such statements.

Offering of Securities to the Public

19. **In cases involving the offering of securities to the public, the auditor should consider any legal and related requirements applicable to the auditor in all jurisdictions in which the securities are being offered.** For example, the auditor may be required to carry out additional audit procedures to the date of the final offering document. These procedures would ordinarily include carrying out the audit procedures referred to in paragraphs 4 and 5 up to a date at or near the effective date of the final offering document and reading the offering document to assess whether the other information in the offering document is consistent with the financial information with which the auditor is associated.

Effective Date

20. This HKSA is effective for audits of financial statements for periods beginning on or after 15 December 2004.

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[3] Additional local guidance is provided in the appendix to this HKSA on "facts discovered after the financial statements are laid before the shareholders or equivalent".

Conformity and Compliance with International Standards on Auditing

21. As of June 2005 (date of issue), this HKSA conforms with International Standard on Auditing (ISA) 560 "Subsequent Events". Compliance with the requirements of this HKSA ensures compliance with ISA 560.

22. Additional local explanations are provided in footnotes 2 and 3. Additional local guidance is provided in the Appendix to this HKSA.

Appendix

Additional local guidance on "facts discovered after the financial statements are laid before the shareholders or equivalent"

1. Because of the variety of conditions which might be encountered, some of the procedures set out in paragraphs 2 to 7 below are necessarily set out only in general terms; the specific actions to be taken in a particular case may vary somewhat in the light of the circumstances. The auditors would be well advised to consult with their lawyers when they encounter such circumstances.

2. The auditors' appointment expires at the annual general meeting. If after the annual general meeting, the auditors become aware of information which may materially affect financial statements previously reported on by them which were laid before the shareholders or equivalent at that meeting, they would, as soon as practicable, consider undertaking steps to determine whether the information is reliable. These steps would need to be performed even when the auditors have resigned, retired, not been re-appointed or have been discharged. In this connection, the auditors would discuss the matter with the directors and request cooperation with whatever investigation may be necessary.

3. When such subsequently discovered information is found to be reliable and relates to facts which may materially affect the financial statements, the auditors would take the action set out in paragraphs 4 to 6 below.

   However, the auditors may take the view that such action is not necessary after discussing with the directors and giving consideration to all the circumstances including, amongst other things:

   a. the time elapsed since the financial statements were issued;

   b. the materiality of the facts discovered; and

   c. whether the audited financial statements for a subsequent period report or will report a correction of a fundamental error in respect of the facts discovered.

4. When the auditors have concluded that action would need to be taken to prevent future reliance on the auditors' report, they would advise the directors to make appropriate disclosure of the newly discovered facts and their effect on the financial statements to shareholders or equivalent. When the directors undertake to make appropriate disclosure, the method used and the disclosure made will depend on the circumstances.

   a. If the effect on the financial statements or auditors' report of the subsequently discovered facts can promptly be determined, disclosure would consist of issuing, as soon as practicable, revised financial statements and auditors' report. The reasons for the revision would be described in a note to the financial statements and referred to in the auditors' report.

   b. When the issuance of the audited financial statements for a subsequent period is imminent, so that disclosure is not delayed, appropriate disclosure of the revision could be made in such financial statements instead of reissuing the earlier financial statements pursuant to subparagraph (a).

c. When the effect on the financial statements of subsequently discovered facts cannot be determined without a prolonged investigation, the steps set out in paragraphs 4(a) and (b) above may be delayed. In these circumstances the auditors would advise the directors of the facts discovered and of the possibility that the facts may require the financial statements and/or auditors' report to be re-issued or may need to be disclosed in the financial statements for a subsequent period. The directors would be advised to make appropriate disclosure to the shareholders or equivalent and, where appropriate, the relevant regulatory authorities.

d. In addition to taking the actions as set out in paragraphs 4(a), (b) and (c) above, the auditors would also consider whether notification or disclosure needs to be made to any other party who may be relying on the previously issued auditors' report.

5. If the directors refuse to make the disclosure recommended in paragraph 4 above, the auditors would notify each member of the board of directors of such refusal and that, in the absence of disclosure being made, the auditors may take steps to prevent future reliance upon the auditors' report. The steps which the auditors would consider taking may include:

   a. Notification to the directors that the auditors' report must no longer be associated with the financial statements; and

   b. Notification to shareholders or equivalent that the financial statements and the auditors' report should no longer be relied upon; and/or

   c. Notification to the appropriate regulatory authorities that the financial statements and the auditors' report should no longer be relied upon; and/or

   d. Resignation.

   However, such steps would only be taken after seeking legal advice and after considering the auditors' duty of confidentiality as set out in Statement 1.204A "Confidentiality" and any relevant legislation.

6. The following provides guidance on the content of any disclosure made by the auditors in accordance with paragraph 5:

   a. The disclosure would describe the effect the subsequently discovered facts would have had on the auditors' report if they had been known to the auditors at the date of the auditors' report and had not been reflected in the financial statements. The disclosure would include a description of the nature of the subsequently discovered facts and of their effect on the financial statements.

   b. The disclosure would be as precise and factual as possible and would not go beyond that which is reasonably necessary to accomplish the purpose mentioned in the preceding subparagraph (a). Comments concerning the conduct or motives of any person would be avoided.

7. There may be circumstances in which the auditors are unable satisfactorily to investigate the information discovered, for example because the directors refuse to co-operate or to provide information or explanations. In these circumstances the auditors would for example consider taking the following steps:

   a. Requesting the directors to make an appropriate disclosure as soon as practicable to the shareholders or equivalent and, where appropriate, the appropriate regulatory authorities.

The contents of such disclosure would normally include:

i. the nature of the subsequently discovered information;

ii. where these can be identified, the items in the financial statements which may be materially affected by the information;

iii. the fact that the auditors have been unable satisfactorily to obtain all the information and explanations which they consider necessary for the purposes of investigating the information;

iv. a statement that, as a result of the scope limitation stated in (iii) above, the auditors have been unable to establish the effect of the discovered information on the financial statements. It may also be indicated that there is an uncertainty as to whether further reliance on the previous auditors' report would be appropriate;

v. if known, the reason or reasons why the auditors have been unable satisfactorily to investigate the information.

b. Should the directors fail or refuse to make the appropriate disclosure as set out in (a) above, the auditors would consider notifying the shareholders or equivalent and the appropriate regulatory authorities. The contents of this notification would be as set out in paragraphs (a)(i) - (v) above.

c. Particularly in circumstances where the directors refuse to co-operate in allowing the auditors to investigate the information discovered or refuse to make the disclosure set out in paragraph (a) above, the auditors would also consider resigning.

Such steps would only be taken after seeking legal advice and after considering the auditors' duty of confidentiality as set out in Statement 1.204A "Confidentiality" and any relevant legislation.