



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

11 October 2012

Our Ref.: C/AASC

International Auditing and Assurance Standards Board  
529 Fifth Avenue, 6th Floor  
New York, 10017  
USA

Dear Sirs,

**IAASB's Invitation to Comment: Improving the Auditor's Report**

The Hong Kong Institute of Certified Public Accountants is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. The HKICPA sets auditing and assurance standards, ethical standards and financial reporting standards in Hong Kong.

We welcome the opportunity to provide you with our comments on the IAASB's Invitation to Comment (ITC). We support the IAASB's continuing efforts to clarify the role of auditors and stakeholders expectations and welcome this ITC.

In principle, we are supportive of the proposed improvements to the auditor's report to provide more information to stakeholders to meet their needs. However, we have concerns as to the extent of information provided under Auditor Commentary. We do not believe that the Auditor Commentary would address the "information gap" without giving rise to implications for auditor liability. We are also of the firm view that audit quality is paramount and that any proposed changes to the form of auditor reporting should only be implemented if they do not have a negative effect on audit quality.

In proposing changes to the auditor's report, we believe it is important for the IAASB to promote an understanding of the objective of performing an audit of financial statements and who are the intended users of auditors' reports. The answers to these questions are the building blocks to the contents of an auditor's report. We are concerned that some of the changes proposed in the ITC would extend the auditor's reporting responsibility in addition to reporting on whether the financial statements give a true and fair view.

To provide further clarity to auditor and management responsibilities, there is a need for education of all parties. Education of users should also cover the auditors' responsibilities relating to fraud under existing professional standards, and that the current audit model is not designed to provide comfort on the financial health of a company but rather it results in an auditor's opinion as to whether the financial statements prepared by management show a true and fair view in accordance with a relevant financial reporting framework.

Responses to the specific questions in the ITC are included in the attachment.



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We trust that our comments are of assistance to you. If you require any clarification on our comments, please contact me at [simonriley@hkicpa.org.hk](mailto:simonriley@hkicpa.org.hk).

Yours faithfully,

Simon Riley  
Director, Standard Setting

SR/al

Encl.



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## ATTACHMENT

### HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS' COMMENTS ON THE IAASB'S INVITATION TO COMMENT: IMPROVING THE AUDITOR'S REPORT

#### Overall Considerations

##### Question 1:

**Overall, do you believe the IAASB's suggested improvements sufficiently enhance the relevance and informational value of the auditor's report, in view of possible impediments (including costs)? Why or why not?**

We support the IAASB's efforts to enhance the relevance and informational value of the auditor's report. However, we have concerns on the proposals for the auditor to report on management's use of the going concern assumption and the extent of information provided under auditor commentary. Please refer to our responses to questions in the relevant sections below.

##### Question 2:

**Are there other alternatives to improve the auditor's report, or auditor reporting more broadly, that should be further considered by the IAASB, either alone or in coordination with others? Please explain your answer.**

We believe further clarification from users is needed for an effective resolution of what information should be included in the auditor's report. We believe that it may not be appropriate for auditors to provide information directly to users on methods and judgments made in valuing assets and liabilities; key business and operational risks; and quality and effectiveness of the governance structure and risk management. We consider that management is in a better position to convey such information to users.

In the respect of narrowing the information gap and to improve the communicative value of auditor reporting, we would encourage the IAASB to explore the following suggested approaches:

- Internal control over financial reporting

It is our observation that a significant number of jurisdictions already have their own respective requirements on companies' reporting on internal control over financial reporting. We believe this is an important area and consideration should be given to introducing comparable reporting requirements across all jurisdictions. Development and implementation of standardized guidance and practice on reporting on internal control over financial reporting should, in theory, help to lower the information gap. Any proposed assurance engagement arising from this approach should be treated as a separate engagement.



- Going concern
  - (i) The Sharman Panel of Inquiry, established at the invitation of the UK Financial Reporting Council, considered going concern and liquidity Risks in their report 'Going Concern and Liquidity Risks: Lessons for Companies and Auditors'. Their June 2012 report can be accessed at: <http://www.frc.org.uk/getattachment/591a5e2a-35d7-4470-a46c-30c0d8ca2a14/Sharman-Inquiry-Final-Report.aspx> .

It was not apparent in the IAASB's ITC whether the IAASB has worked with this Panel. If not, we would encourage the IAASB to work with this Panel as they have raised similar issues on the way forward, particularly on auditors reporting of going concern and liquidity risks. It should be noted that the Sharman Panel believes that there would be considerable benefit in the UK FRC engaging in discussion with other national and international accounting and auditing standard setters about what constitutes "going concern".

- (ii) The IASB's IAS 1 Presentation of Financial Statements, paragraphs 25 and 26 specifically addresses going concern in the context of external financial reporting. The question we believe the IAASB should address is whether the IAASB proposals and the Sharman Inquiry report would work with reference to IAS 1. We would therefore encourage the IAASB to work with the IASB to ensure that any new proposals to ISA 700 are consistent with the requirements of IAS 1. If they are considered not to be consistent with IAS 1, such that IAS 1 needs to be enhanced, we would encourage the IAASB to work with the IASB to ensure that amendments to IAS 1 are put through such that the IAASB proposals would work as intended.

**Which classes of users are, in the view of respondents, most affected by these issues?**

We believe that users of financial statements of listed companies and public interest entities are most affected by the above issues.

**Are there any classes of users that respondents believe are unaffected by these issues?**

We believe that this will ultimately depend on whether changes are brought in for all audits or only for audits of specific entities. Please refer to our response to Question 3 below.



## **Auditor Commentary**

### **Question 3:**

**Do you believe the concept of Auditor Commentary is an appropriate response to the call for auditors to provide more information to users through the auditor's report? Why or why not? (See paragraphs 35–64.)**

We have concerns on the extent of information about the entity or the quality of its financial reporting provided under Auditor Commentary. While it is true that the auditor may have "insights" and "perceptions" about the entity or the quality of its financial reporting or any other aspects of the entity as a result of the work performed during the course of the audit, such "insights" or "perceptions" could only be deemed as by-products of the audit process. Audit procedures are designed and performed solely for the purpose of expressing an audit opinion on the financial statements taken as a whole, rather than providing "insights" or "perceptions" about matters other than the financial statements taken as a whole.

However, we believe that consideration may be given to increase transparency in respect of the matters which would have been communicated to those charged with governance as required by ISA 260, Communication with Those Charged with Governance. There is some value for auditors pointing out important footnotes dealing with matters of significant judgment or highly unusual or material items; a roadmap to the important matters, if those matters have already been disclosed and explained by management or by those charged with governance.

We also believe that there should be an objective basis on which auditors can determine which matters should be reported, and to whom, and accordingly we would encourage the IAASB to consider developing guidance in this respect.

### **Question 4:**

**Do you agree that the matters to be addressed in Auditor Commentary should be left to the judgment of the auditor, with guidance in the standards to inform the auditor's judgment? Why or why not? If not, what do you believe should be done to further facilitate the auditor's decision-making process in selecting the matters to include in Auditor Commentary? (See paragraphs 43–50.)**

Please refer to our response to Question 3 above. We believe the matters should be left to the judgment of the auditor with guidance included in the standards to assist the auditor in forming their judgment. The Auditor Commentary should not be providing new information which is not disclosed in the financial statements itself but that the matters proposed to be included in the Auditor Commentary should have been discussed with the audit committee.

We are of the view that it is important to educate users that the proposed audit model is not designed to provide comfort on the financial health of a company but results in an opinion on the truth and fairness of a set of financial statements.



**Question 5:**

**Do the illustrative examples of Auditor Commentary have the informational or decision-making value users seek? Why or why not? If not, what aspects are not valuable, or what is missing? Specifically, what are your views about including a description of audit procedures and related results in Auditor Commentary? (See paragraphs 58–61.)**

Please also refer our response to Questions 3 and 4.

We are not supportive of including a description of audit procedures and related results in Auditor Commentary. We believe it would be difficult to summarize the auditor's procedures and related results in a clear manner and language understandable to users of financial statements. The key result of the audit procedures is in the overall opinion given. The ISAs are principles-based and the audit procedures for a specific account item may differ as between audits. The proposal would confuse users if they try to compare otherwise similar entities. The opinion on the financial statements is based on an evaluation of the conclusions drawn from the audit evidence obtained. Users will not get a full picture if only certain procedures and related results are included in Auditor Commentary.

**Question 6:**

**What are the implications for the financial reporting process of including Auditor Commentary in the auditor's report, including implications for the roles of management and those charged with governance (TCWG), the timing of financial statements, and costs? (See paragraphs 38 and 62–64.)**

We are of the view that the auditor's report should not contain new information regarding the financial information of an entity. The management is directly responsible for communicating such information to the users. If Auditor Commentary is included in the auditor's report, it would increase the involvement of management, TCWG and audit committee in the audit process.

**Question 7:**

**Do you agree that providing Auditor Commentary for certain audits (e.g., audits of public interest entities (PIEs)), and leaving its inclusion to the discretion of the auditor for other audits is appropriate? Why or why not? If not, what other criteria might be used for determining the audits for which Auditor Commentary should be provided? (See paragraphs 51–56.)**

We believe the proposed Audit Commentary should be restricted to audits of PIEs. Investors or other users of private companies' financial statements typically have access to additional information from the entity and therefore changes to audit of private companies' financial statements may result in costs that exceed the derived benefits.



## Going Concern/ Other Information

### Question 8:

**What are your views on the value and impediments of the suggested auditor statements related to going concern, which address the appropriateness of management's use of the going concern assumption and whether material uncertainties have been identified? Do you believe these statements provide useful information and are appropriate? Why or why not? (See paragraphs 24–34.)**

Management is responsible for assessing whether the company should prepare its financial statements on a going concern basis. The going concern basis of preparation is one of the many aspects that needs to be considered when the auditor carries out an audit of financial statements. A separate section in the audit report may give undue emphasis on the auditor's responsibility and work done on whether the reporting entity is considered to be a going concern when the auditor's report is issued. The financial statements do not currently include any statement from the management in respect of their assertion on whether the company continues to be a going concern.

We are of the view that if auditors are required to make statements on the appropriateness of management's use of the going concern assumption and whether material uncertainties have been identified, there should be corresponding statements by management in the financial statements. Auditors could then state whether or not they agree. An alternative way to satisfy the information needs of stakeholders and financial analysts might be to include further information in the financial statements which, being subject to audit procedures and covered by the opinion contained in the auditor's report, should provide users with a sufficient level of assurance on the information.

In addition, such explicit statements by auditors are likely to be misinterpreted by users. A professional accountant will know that the statements are just simply stating what an unmodified auditor's report already implies. We are concerned, however, that an "average" user of financial statements might likely read far more into a bold statement from the auditors that "there are no material uncertainties" than the statement actual conveys based on IFRS/IAASB literature. It may well be misinterpreted as a guarantee of future solvency and confirmation of lack of business risk that goes far beyond the technical meaning.

Given the current interest in going concern by The Sharman Panel of Inquiry and IASB, we would suggest that the IAASB form a joint working group between these parties to further consider the issues involved.



**Question 9:**

**What are your views on the value and impediments of including additional information in the auditor's report about the auditor's judgments and processes to support the auditor's statement that no material uncertainties have been identified? (See paragraphs 30–31.)**

Given that the ISAs are principles-based and audit processes may vary as between audits, we believe it would be difficult for users to gain a sound understanding of the appropriateness of audit processes from statements in the auditor's report. It may cause more confusion and further widen the "expectations" and "information" gaps.

**Question 10:**

**What are your views on the value and impediments of the suggested auditor statement in relation to other information? (See paragraphs 65–71.)**

We are supportive of the proposed auditor statement in relation to other information under ISA 720 "The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements".

We are assuming that the revision to ISA 720 would not extend the auditor's responsibilities from the current position. In case further explanations are needed from auditors to explain what specific procedures have been performed on other information, we believe those explanations should be included in a stand-alone document and should not be included as part of the audit report.

**Clarifications and Transparency**

**Question 11:**

**Do you believe the enhanced descriptions of the responsibilities of management, TCWG, and the auditor in the illustrative auditor's report are helpful to users' understanding of the nature and scope of an audit? Why or why not? Do you have suggestions for other improvements to the description of the auditor's responsibilities? (See paragraphs 81–86.)**

Generally, we believe the enhanced descriptions of the responsibilities of management and auditor are helpful to users' understanding. However, the language used in the first bullet and last bullet may raise more questions by users. We are not sure if users would understand the concept of "material misstatement risk resulting from fraud" being higher than "material misstatement risk resulting from error".

In the last bullet, there is a statement stating that any significant deficiencies in internal control that are identified during the audit were communicated to those charged with governance. Users may be interested to have further information in this area which is currently not available in the financial statements.



We would request the IAASB to clarify whether the enhanced descriptions are intended to align with the auditor commentary. If there are significant audit findings or significant deficiencies in internal control, there may be a need to consider these for inclusion under auditor commentary. However, if further information is to be included in the auditor's report, this may create a gap between the auditor's contractual/statutory responsibility on an entity's internal control and the users' expectation of the auditor's responsibilities in this regard.

**Question 12:**

**What are your views on the value and impediments of disclosing the name of the engagement partner? (See paragraphs 72–73.)**

In general, we are supportive of disclosing the name of the engagement partner, as currently required under the ISAs and ISQC 1, i.e. the engagement partner being responsible for the conduct and performance of the audit.

We would note, however, that in Hong Kong, the auditor's report is normally signed in the name of the firm because the firm as a whole assumes responsibility for the audit. For a corporate practice, the auditor's report is signed by a director of the practice, who must be a professional accountant holding a current practising certificate. The auditor's report states the name of the corporate practice and the location of its office and is signed in the name of the corporate practice. The auditor's report also identifies the director responsible for the performance of the audit engagement contemplated by such report, and states his/her full name as appearing in his/her practising certificate and the practising certificate number.

**Question 13:**

**What are your views on the value and impediments of the suggested disclosure regarding the involvement of other auditors? Do you believe that such a disclosure should be included in all relevant circumstances, or left to the auditor's judgment as part of Auditor Commentary? (See paragraphs 77–80.)**

We are of the view that it is not necessary to disclose information regarding the involvement of other auditors given that the auditor of the group financial statements is responsible for direction, supervision and performance of the group audit engagement in ISA 600 unless required by law or regulation.

**Question 14:**

**What are your views on explicitly allowing the standardized material describing the auditor's responsibilities to be relocated to a website of the appropriate authority, or to an appendix to the auditor's report? (See paragraphs 83–84.)**

We do not support any proposed relocation of the information on auditor's responsibilities to a website as the auditor's report would no longer contain such information we consider vital to users having a clear understanding of the auditor's responsibilities.



## Form and Structure

### Question 15:

**What are your views on whether the IAASB's suggested structure of the illustrative report, including placement of the auditor's opinion and the Auditor Commentary section towards the beginning of the report, gives appropriate emphasis to matters of most importance to users? (See paragraphs 17–20.)**

We are supportive of the proposal to relocate matters considered important by users to the beginning of the report.

### Question 16:

**What are your views regarding the need for global consistency in auditors' reports when ISAs, or national auditing standards that incorporate or are otherwise based on ISAs, are used? (See paragraphs 21–23 and 87–90.)**

We are supportive of the need for global consistency in auditors' reports as ISAs are being adopted as national auditing standards.

### Question 17:

**What are your views as to whether the IAASB should mandate the ordering of items in a manner similar to that shown in the illustrative report, unless law or regulation require otherwise? Would this provide sufficient flexibility to accommodate national reporting requirements or practices? (See paragraph 17 and Appendix 4.)**

We agree that IAASB should mandate the ordering of items in the auditors' report, unless law or regulation require otherwise. We believe the approach provides sufficient flexibility to accommodate national reporting requirements or practices.

### Question 18:

**In your view, are the IAASB's suggested improvements appropriate for entities of all sizes and in both the public and private sectors? What considerations specific to audits of small- and medium-sized entities (SMEs) and public sector entities should the IAASB further take into account in approaching its standard-setting proposals? (See paragraphs 91–95.)**

We believe the proposed Audit Commentary should be restricted to audits of PIEs. The other improvements are appropriate for entities of all sizes.

~ END ~