



香港會計師公會
HONG KONG SOCIETY OF ACCOUNTANTS
(Incorporated by the Professional Accountants Ordinance, Cap. 50)

By e-mail < Edcomments@ifac.org > and by fax (0062 1 212 286 9570)

Our. Ref.: C/AASC

19 November 2003

Technical Director,
International Auditing and Assurance Standards Board,
International Federation of Accountants,
545 Fifth Avenue, 14th Floor,
New York,
New York 10017,
USA.

Dear Sir,

IAASB Exposure Draft on Review of Interim Financial Information Performed by the Auditor of the Entity

The Hong Kong Society of Accountants (HKSA) welcomes the opportunity to provide the IAASB with comments on the captioned IAASB Exposure Draft, which are set out in the attachment.

The HKSA has a policy of converging its Auditing Standards with the IAASB's Standards. The standard setting due process applied in Hong Kong (details of which are available on the HKSA's website) acts to support this policy. The HKSA's Auditing and Assurance Standards Committee (AASC) issued an Invitation to Comment on the captioned IAASB Exposure Draft with a comment period concurrent with that set by the IAASB. Accordingly, the accompanying comments may reflect the views not only of members of the AASC but also of constituents in Hong Kong who provided comments to the HKSA.

We trust that the IAASB will find our comments helpful. If you require any clarifications on our comments, please contact our Deputy Director (Ethics & Assurance), Stephen Chan < schan@hksa.org.hk >, in the first instance.

Yours faithfully,

WINNIE C.W. CHEUNG
SENIOR DIRECTOR

PROFESSIONAL & TECHNICAL DEVELOPMENT

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ATTACHMENT

HONG KONG SOCIETY OF ACCOUNTANTS' COMMENTS ON THE IAASB EXPOSURE DRAFT "REVIEW OF INTERIM FINANCIAL INFORMATION PERFORMED BY THE AUDITOR OF THE ENTITY"

A. Assurance Framework – Issuance of review standards as ISAs or ISAEs

The HKSA believes that the proposed ISA should be issued as an International Standard on Assurance Engagements (ISAE) rather than as an International Standard on Auditing (ISA) for the following reasons:

- It may cause confusion among users of the review reports due to the fact that standards that apply to the review of interim financial information, the scope of which is substantially less than the scope of an audit, are dealt with in an ISA.
- The objective of a review of interim financial information differs significantly from that of an audit conducted in accordance with ISAs:
 - A review of interim financial information does not provide a basis for expressing an opinion whether the financial information gives a true and fair view, or is presented fairly in all material respects, in accordance with an identified financial reporting framework, within the bounds of reasonable assurance;
 - A review consists primarily of applying analytical procedures and making enquiries of persons responsible for financial and accounting matters;
 - A review may bring significant matters affecting the interim financial information to the auditor's attention, but it does not provide assurance that the auditor will become aware of any or all significant matters that might be identified in an audit; and
 - A review does not, ordinarily, contemplate corroboration of the information obtained and does not provide assurance that the auditor will become aware of any or all significant matters that might be identified in an audit.

As the proposed IAASB Assurance Framework will encompass both ISAs and ISAEs, it is becoming increasingly important that there is a clear understanding of which standards will be designated as "ISAs". The HKSA considers that it would be unhelpful for Standards that do not apply to the audit of general purpose financial statements to be included under the umbrella of ISAs. Designation of the proposed Standard on the review of financial information (interim or otherwise) as an ISAE may give a better understanding to users. As the nature of the extant ISA 910 is similar to the proposed ISA, the IAASB should also consider changing it to an ISAE if the IAASB decides to retain it as a standard.

B. Applicability of ISAs

In the extant preamble to the ISAs, it is stated that ISAs are to be applied in the audit of financial statements. ISAs are also to be applied, adapted as necessary, to the audit of other information and to related services.

The HKSA notes that, despite the above statement in the preamble, the proposed ISA covers in summary matters that are covered in specific ISAs. For example, quality control (proposed revised ISA 220) is covered in paragraph 7, going concern (ISA 570) is covered in paragraphs 27 and 28, management representations (ISA 580) are covered in paragraphs 33 and 34, accompanying information (ISA 720) is covered in paragraph 35 and documentation (ISA 230) is covered in paragraph 54.

Clearly the work expected of an auditor in a review of interim financial information is not expected to equal that for an audit and accordingly guidance relating to obtaining sufficient audit evidence will be significantly different for the review. For example, guidance relating to going concern considerations is expected to be different for a review of interim financial information. However, once the auditor becomes aware of events or conditions that cast significant doubts on the entity's ability to continue as a going concern, the work expected in an audit should be applied during a review of interim financial information. We consider that the proposed ISA should include all the guidance in paragraphs 26 to 29 of ISA 570.

The standard expected of auditors in areas concerning the performance of the auditors' work rather than the extent of the work should remain the same for any assurance engagements. Thus guidance for review of interim financial information should mirror those set for audit engagements in respect of matters such as quality control (proposed revised ISA 220), documentation (ISA 230), communication with those charged with governance (ISA 260), materiality (ISA 320), using the work of another auditor (ISA 600) and using the work of an expert (ISA 620). We consider that the guidance provided in the proposed ISA relating to quality control, documentation and communication with those charged with governance is insufficient and note that no guidance is provided in respect of materiality, using the work of another auditor and using the work of an expert. We recommend that IAASB reviews each ISA and establishes those that have general application to an assurance engagement. The relevant guidance from these standards should be reflected in full in the proposed ISA. This can be achieved by a combination of including much of the text from the other ISAs in the proposed ISA or by cross referencing back to the other ISAs.

For areas of guidance covered by other ISAs, the IAASB should ensure that guidance in the proposed ISA on how to react when the results of the auditors' enquiries identify exceptions or anomalies that call into question the reliability of the financial statements is appropriate for a review of interim financial information.

C. Responses to specific questions asked in the Request for Comments

1. Proposed ISA and the extant ISA 910 – Scope of the Proposed ISA

The HKSA questions as to whether there is really a need to have 2 Standards covering a similar subject. It may be desirable that there is only one Standard addressing reviews of financial information and that the scope of the proposed Standard is widened to include all reviews of financial information. Additional guidance can be included to address specific issues in respect of reviews performed by a practitioner who is not the entity’s auditor, obviating the need to retain ISA 910.

The HKSA considers that the additional guidance required for the practitioner who is not the entity’s auditor should be similar to that for an auditor who has recently been appointed auditor of the entity as mentioned in the proposed ISA (paragraphs 4, 17 and 18) in which case the practitioner is required to obtain an understanding of the entity and its environment, including its internal control, before performing a review of interim financial information.

2. Conclusion expressed in the written report

The HKSA considers that it would be preferable for there to be only one form of conclusion; using the wording proposed for reviews of condensed interim financial information. This will avoid the risk of users of the review report believing that different levels of assurance are being conveyed when the work performed in both instances are actually the same.

D. Comments on other significant aspects of the proposed ISA

1. Paragraph 2

(i) In relation to criteria “the entity is required or permitted under legislation, regulation, or equivalent authority to issue such interim financial information”, the HKSA questions the need to have this criteria included in the proposed ISA as it is unlikely that legislation, regulation, or equivalent authorities would explicitly prohibit the issuance of interim financial information. In addition, while interim reviews are required under company or securities law or listing requirements in many jurisdictions, there are also many jurisdictions where there is no such legal or regulatory requirement for them. Financial reporting frameworks do not restrict the application of their guidance (for example, IAS 34 “Interim Financial Reporting” applies “if a company is required or elects to publish an interim financial reporting”). Thus, entities may, and do, prepare interim financial information under those frameworks whether or not required by legislation or regulation.

(ii) In relation to the criteria “the audited annual financial statements of the entity are required to be filed with a regulatory authority, or equivalent, and are publicly available”, the HKSA considers that the key principle is that the audited annual financial statements are publicly available. This is important because it ensures that users of the interim report have appropriate context for that information. How the annual financial statements are made publicly available is not particularly relevant and tends to confuse the key principle. Therefore, the HKSA suggests shortening the criteria to “The audited annual financial statements are publicly available”.

2. Paragraph 6

This paragraph requires the auditor to comply with the requirements of Parts A and B of the IFAC *Code of Ethics for Professional Accountants*. The HKSA suggests that the wording of this paragraph be aligned with that in the proposed International Standards on Quality Control (ISQC) 1 “*Quality Control for audit, assurance and related services practices*”. It refers to relevant ethical requirements in the bold lettered principle and explains in the accompanying guidance that the relevant ethical requirements ordinarily comprise Parts A and B of the IFAC Code together with applicable national requirements where these are more restrictive.

3. Paragraph 10

The description of the objective of an engagement to review interim financial information would be enhanced if it explained that a review consists primarily of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters *and does not, ordinarily, contemplate corroboration of the information obtained*. While this is described in paragraph 12 in the description of the matters ordinarily covered in the communication regarding the terms of the engagement, the HKSA believes that this phrase helps to demonstrate the restricted scope of the review engagement and would enhance the discussion of the limits of a review in paragraph 10.

4. Paragraph 12

In the last bullet, the HKSA believes that the option that management simply “indicate” where the auditor’s report can be obtained should be deleted. Given the limited nature of the auditor’s work and the fact that users may be more familiar with the auditor’s involvement with the audited annual financial statements, it is important that the auditor’s report accompanies the interim financial information whenever management states that the interim financial information has been reviewed by an independent public accountant. The risk of users being confused about the auditor’s association with the interim financial information or misinterpreting the nature of the auditor’s limited review is too high.

However, the last bullet only applies to those jurisdictions that a review of the interim financial information of the entity be performed by its auditor and with legislative requirement to publish such interim review report. In other jurisdictions, there may be no legislative requirement to publish the auditor’s interim review report. For example, as mentioned in paragraph 3 of the proposed ISA, in some jurisdictions, there may be no requirement for review to be performed by auditor, but only those charged with governance request its auditor to perform a review of the interim financial information and report to them directly. In these circumstances, the review report is a private report to directors and should not be published. The last bullet of this paragraph does not apply. In such circumstances, it is more important for the auditor to obtain management’s agreement that the review report, or reference to the auditor, will not be included in any such document without auditor’s prior written permission or consent.

In addition to cover the point that the scope of review is substantially less than the scope of audit, the HKSA recommends to include the fact that the review engagement cannot be relied upon to disclose errors, illegal acts or other irregularities, for

example, fraud or defalcations that may exist. This point is similar to the sixth bullet of paragraph 12 of ISA 910.

Also the HKSA recommends the IAASB to include an example of an engagement letter in the Appendix similar to that of ISA 910.

5. Paragraph 17

If an auditor has recently been appointed as auditor of the entity, the scope of review should be no different from that of ISA 910 since the auditor has no audit-based knowledge of the entity. Obtaining further understanding of the entity and its environment alone may not provide adequate audit-based knowledge for the review conclusion. In such situation, the auditor needs to understand other matters relevant to the financial statements as described in ISA 910, e.g. knowledge of the entity's production and distribution methods, product lines, operating locations and related parties. Before drawing the review conclusion, the incoming auditor is also required to obtain sufficient appropriate evidence that opening balances have been appropriately brought forward and that the accounting policies used for the comparatives are consistent with those of the current period.

6. Paragraph 18

It states that the incoming auditor ordinarily reviews the predecessor auditor's documentation for the preceding annual audit and interim review. However, in some jurisdictions, there may not be any legal or professional obligation for the predecessor auditor to make any of his working papers available for review by the incoming auditor. The existing and proposed IFAC Code of Ethics also does not have such requirement. The HKSA recommends that such practice should not be considered as "common practice" in the ISA. The HKSA therefore suggests to delete the word "ordinarily" and to revise the relevant sentence as "The incoming auditor may review the predecessor auditor's documentation...."

7. Paragraph 21

The HKSA believes that it would be useful to add to the list of inquiries of management whether there has been any litigation or claims that could have a material effect on the interim financial information. This would be consistent with the inquiries regarding actual or possible noncompliance with laws and regulations, and would set the stage for the discussion in paragraph 24 regarding corroboration of such inquiries.

In the inquiry regarding significant transactions, the HKSA also suggests that it might be useful to inquire about those occurring not only in the last several days of the interim period, but also those in the first several days of the next interim period.

8. Paragraph 25

This paragraph suggests that the auditor "considers inquiring of management as to the process by which the financial information has been prepared..." The HKSA suggests deleting "considers", as the HKSA believes the auditor should obtain that understanding.

9. Paragraphs 30-32

The context for the auditor's determination of materiality for the interim financial information is not clearly explained in these paragraphs. It is not clear, for example, what is intended in paragraph 31 when it refers to the materiality judgments made in conjunction with the current and prior year's annual audit. The HKSA questions whether the proposed ISA is suggesting that materiality in the context of the interim financial information is considered to be that determined for the annual financial statements. If this is the case, this would not be consistent with, for example, IAS 34, which specifically states that materiality should be assessed in relation to the interim period financial data (IAS 34, paragraph 23). As drafted paragraph 31 may confuse more than clarifying and either needs expansion or should be deleted.

10. Paragraph 34

The HKSA recommends the IAASB to consider the following additional points in the letter of representations:

- (a) acknowledgement by management of its responsibility for the consistency of accounting policies; and
- (b) acknowledgement by management of its responsibility for the completeness of the financial records and of the minutes (and summaries of meetings for which minutes have not been prepared) that were made available to the auditor for the purpose of the review.

11. Paragraph 44(g)

In relation to the review conclusion, as explained above the HKSA believes that it should be the wording proposed for reviews of condensed interim financial information. However, the HKSA believes that the reference should be to the standard that specifies the required condensed interim financial information rather than to the financial reporting framework broadly. For example, in the case of the IFRSs, the HKSA considers the reference should be to IAS 34 "Interim Financial Reporting" rather than to IFRSs broadly. This is because, by definition, the interim financial information will not include all of the required disclosures that would be expected for a complete set of IFRS financial statements. Thus, the more specific reference is the most useful to readers as it reinforces that the interim financial information is not a complete set of financial statements. This position is consistent with IAPS 1014, which aims to restrict references to compliance with IFRS to those financial statements that comply fully with them.

12. Paragraph 44(i)

The HKSA recommends that this paragraph be expanded to include the essential procedures on how the auditor should date the review report as provided in paragraph 28 of the extant ISA 910.

13. Paragraph 49

This paragraph requires the auditor to modify the review report by adding an emphasis of matter paragraph to highlight a material matter regarding a going concern problem. While such guidance is appropriate when the entity has adequately disclosed the going concern problem, consistent with the approach adopted in ISA 570 “*Going Concern*”, if the financial information does not adequately disclose a going concern problem that exists, the auditor should express a qualified or adverse opinion, as appropriate. It could be argued that such a modification would be required by paragraph 46. But a link between the guidance in paragraphs 50 and 46 would be useful to ensure that this is clear. For a better understanding of the requirements, the HKSA recommends that the IAASB may:

- a) include headings like “Matters that do affect the auditor’s opinion” and “Matters that do not affect the auditor’s opinion” before paragraphs 46 and 48 respectively;
- b) include situations for disclaimer and adverse conclusion, similar to paragraphs 27(b) and (c) of ISA 910; and
- c) include examples of each type of modified reports in the Appendix.

14. Appendix 3

The HKSA recommends that the scope paragraph of the review report should make reference to specific auditing standard (i.e. this proposed ISA), instead of a general reference to “standards issued by the International Auditing and Assurance Standards Board” for a better understanding of the scope of engagement.

15. Other

Since IAS 34 “Interim Financial Reporting” requires that comparatives are given in the interim financial report, the HKSA recommends that the IAASB may include more guidelines on the implication to review report under different circumstances. For example,

- a) interim comparatives were not reviewed; and
- b) if the prior period review report on the interim comparatives or the audit report on the preceding annual financial statements was modified.