

## **Practice Review Self-assessment Questionnaire 2020 - Explanatory notes**

The explanations below are intended to provide guidance on the questions in the practice review self-assessment questionnaire.

These explanatory notes are to be read in conjunction with Hong Kong Standard on Quality Control 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* (“HKSQC 1”), and the *Guidelines on Anti-money Laundering and Counter-terrorist Financing for Professional Accountants* (Part F of the Code of Ethics for Professional Accountants (“Code of Ethics”), “AML Guidelines”).

The Quality Assurance Department welcomes your comments and feedback on the questionnaire and these explanatory notes. Please send any comments to [qualityassurance@hkiipa.org.hk](mailto:qualityassurance@hkiipa.org.hk).

### **Explanatory notes**

#### **Part A – General**

##### **Question A2**

A practitioner takes the meaning of (1) the sole proprietor in case of a sole proprietorship, (2) a partner in case of a firm of CPA (practising) and (3) a director in case of a corporate practice.

#### **Part B – Audit and assurance**

##### **Questions B3(a), B11(b) and B11(c)**

Audit staff are both qualified and non-qualified staff of the practice that carry out audit or other assurance work under control and supervision of a practising principal.

##### **Question B3(b)**

International Education Standard (“IES”) 8 *Professional Competence for Engagement Partners Responsible for Audit of Financial Statements* provides a closer link between the competence and capability requirements set out in ISA/HKSA 220 *Quality Control for an Audit of Financial Statements* and ISQC/HKSQC 1. IES 8 also recognizes that learning and development occurs throughout an individual’s career and development and maintenance of competence required for performing the roles of an engagement partner occurs over time. While a premise of IES 8 is that engagement partners have already developed the professional competence to assume that role, IES 8 acknowledges that engagement partners operate in an environment of significant change which is why this particular IES requires engagement partners to develop and maintain professional competence throughout their careers. Further details are set out in the below designated webpage in the Institute’s website:

<https://www.hkiipa.org.hk/en/Standards-and-regulation/Standards/New-and-major-standards/New-and-Major-Standards/IES8-Professional-Competence-for-Engagement-Partners-Responsible-for-Audit-of-Financial-Statements>

#### **Questions B4**

Monitoring is a periodic firm level review of quality control policies and procedures that includes reviews of a sample of completed engagement files of each partner/ director. A monitoring review is expected to be carried out on the firm's system of quality control on an annual basis and on the level of engagements normally over a cycle of no more than three years. This function is different from an Engagement Quality Control Review ("EQCR"), which is a process designed to provide an objective evaluation, before the report is issued, of the significant judgments made and conclusions reached by the engagement team in formulating the audit / other assurance report. Some practices may describe this review as a second partner review.

#### **Question B5**

Relevant ethical requirements refer to the requirements to which the engagement team and engagement quality control reviewer are subject, which ordinarily comprise Chapter A, Parts 1, 3, 4A and 4B, and Chapter C of the *Code of Ethics*.

#### **Question B8**

A network firm is a firm or entity that belong to a network. According to the *Code of Ethics*, a network is a larger structure (a) that is aimed at co-operation; and (b) that is clearly aimed at profit or cost sharing or shares common ownership, control or management, common quality control policies and procedures, common business strategy, the use of a common brand-name, or a significant part of professional resources.

#### **Question B10**

A letter was issued by the Quality Assurance Department on 28 April 2014 to all practising members drawing their attention to the five common deficiencies (the "Top 5 findings"). Practices are again reminded that if a practice is found in a practice review to have made no or little attempt or effort to address any of the Top 5 findings existing within the practice, such behaviour will be taken as amounting to serious professional misconduct. The letter can be found at:

[https://www.hkicpa.org.hk/-/media/HKICPA-Website/HKICPA/section6\\_standards/quality\\_assurance/practice-review/practice-review-findings.pdf?la=en&hash=755E1C9444F09EDDA07FCA4D37921070](https://www.hkicpa.org.hk/-/media/HKICPA-Website/HKICPA/section6_standards/quality_assurance/practice-review/practice-review-findings.pdf?la=en&hash=755E1C9444F09EDDA07FCA4D37921070)

#### **Question B11(d)**

A practising principal is a practising certificate holder who can sign documents in the name of the practice. An authorised signatory is a practising principal.

The practising principal can be a sole practitioner practising in his/her own name, a partner of a partnership practice, or a director of a corporate practice.

#### **Question B11(e)**

##### **Non-Public Interest Entity ("Non-PIE") engagements**

Under section 3(1) of the FRCO, a Public Interest Entity ("PIE") means a listed corporation with listed shares or stocks or a listed collective investment scheme in Hong

Kong.

A non-PIE engagement is an engagement that **falls outside the definition of a PIE engagement** as set out in Part 1 of Schedule 1A of the FRCO. Those PIE engagements include annual audits, specified reports and accountants' reports on a listed or "seeking to be listed" corporation or collective investment scheme. Practices are reminded that non-PIE engagements also **include** (a) statutory audits and compliance reports on non-PIE subsidiaries and non-PIE regulated entities within a listed group; and (b) audits of entities whose debts only are listed in Hong Kong. Other examples of non-PIE engagements are set out in the Explanatory note to Question B11(h) below.

Definition of a PIE in the FRCO is set out below:

- 1) An auditor's report on a PIE's annual financial statements required by the Companies Ordinance (Cap 622), the Listing Rules or any relevant code issued by the Securities and Futures Commission.
- 2) A specified report<sup>1</sup> required to be included in (i) a listing document for the listing of the shares or stocks of a corporation seeking to be listed or a listed corporation, or (ii) a listing document of a collective investment scheme seeking to be listed or a listed collective investment scheme.
- 3) An accountant's report required under the Listing Rules to be included in a circular issued by or on behalf of a PIE for a reverse takeover or a very substantial acquisition.

### **Question B11(g)**

#### **Listed entity**

An entity is listed if its shares, stocks or debts are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body. An engagement requiring an auditor's or accountant's report to be issued on an entity with its shares and stocks listed in Hong Kong falls within the definition of a PIE engagement. However, an engagement requiring an auditor's or accountant's report to be issued on an entity with only its debts listed in Hong Kong falls outside the definition of a PIE engagement (i.e. non-PIE Engagement).

### **Question B11(h)**

Engagements not falling within the definition of PIE Engagements (i.e. non-PIE Engagements) include those requiring an auditor's or accountant's report to be issued in relation to:

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<sup>1</sup> Specified report — (a) in relation to a prospectus issued by or on behalf of a listed corporation, means any report, specified in Part II of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32), that is required under section 38 or 342 of that Ordinance to be set out in the prospectus; (Amended 28 of 2012 ss. 912 & 920) (b) in relation to a listing document (other than a prospectus) issued by or on behalf of a listed entity, means any report on the profits and losses of, the assets and liabilities of, and other financial information on— (i) the entity; or (ii) a business or undertaking to be acquired, or disposed of, by the entity, that is required for inclusion in the listing document issued for the purposes of the relevant code or the Listing Rules.

### A major transaction

Based on the definition set out in rule 14.06 of Chapter 14 EQUITY SECURITIES – NOTIFIABLE TRANSACTIONS of the Listing Rules (“Chapter 14”), a major transaction is a transaction or a series of transactions by a listed issuer where any relevant percentage ratio is 25% or more, but less than 100% for an acquisition or 75% for a disposal.

### A very substantial disposal

Rule 14.06 of Chapter 14 defines a very substantial disposal as a disposal or a series of disposals (aggregated under rules 14.22 and 14.23) of assets (including deemed disposals referred to in rule 14.29) by a listed issuer where any relevant percentage ratio is 75% or more.

### An extreme transaction

Based on the definition set out in rule 14.06C of Chapter 14, an “extreme transaction” is an acquisition or a series of acquisitions of assets by a listed issuer, which individually or together with other transactions or arrangements, may, by reference to the factors set out in Note 1 to rule 14.06B of Chapter 14, have the effect of achieving a listing of the acquisition targets, but where the issuer can demonstrate to the satisfaction of the Hong Kong Stock Exchange that it is not an attempt to circumvent the requirements for new applicants set out in Chapter 8 of the Listing Rules and those factors set out in rule 14.06C of Chapter 14 including (a) the issuer must operate a principal business of substantial size; or (b) the issuer must have been under the control or de facto control of the same person(s) for a long period (normally not less than 36 months) and the transaction will not result in a change in control or de facto control of the issuer.

### **Question B12**

Hong Kong CPA practices carrying out audit services in the Mainland that are not subject to or exempted from the "Provisional regulations on CPA practices carrying out audit services relating to the listing of Mainland enterprises outside Mainland" 《會計師事務所從事中國內地企業境外上市審計業務暫行規定》 ("Provisional Regulations") which took effect from 1 July 2015 shall apply for a temporary license with the Ministry of Finance (“MoF”). Based on the temporary license regulations 《境外會計師事務所在中國內地臨時執行審計業務暫行規定》 clause 10, each practice that has applied and obtained a temporary license is required to file an annual reporting form (境外會計師事務所臨時執業業務報告表) on or before 31 May each year on activities undertaken under temporary license(s) in the preceding year. Information regarding overseas engaging parties (境外委托方) and relevant Mainland entities (境內相關機構) is required to be provided under the second and third columns of that form respectively. A copy of the form can be downloaded by clicking the following link:

[https://www.hkicpa.org.hk/-/media/HKICPA-Website/HKICPA/section6\\_standards/technical\\_resources/pdf-file/appform.pdf](https://www.hkicpa.org.hk/-/media/HKICPA-Website/HKICPA/section6_standards/technical_resources/pdf-file/appform.pdf)

### **Question B13**

Under the Provisional Regulations, Hong Kong CPA practices auditing Mainland enterprises listed in Hong Kong will have to enter into business cooperation arrangements with Mainland CPA practices. Hong Kong CPA practices will be responsible for the scope of arrangements and for making appropriate filing to the MoF at least 7 days before entering into the Mainland to carry out audit services.

## **Part C – AML / CTF compliance**

### **Question C1**

The amended Anti-Money Laundering and Counter-Terrorist Financing (“AML / CTF”) Ordinance (“AMLO”), effective on 1 March 2018, extends the scope of the AMLO to cover designated non-financial businesses and professions, including accountants. The Institute issued *AML Guidelines* as part of the *Code of Ethics and practices*<sup>2</sup> are required to carry out certain AML / CTF policies and procedures when they, by way of business, prepare for or carry out for clients any of the specified transactions as set out in paragraphs 600.2.1 and 600.2.2 of the *AML Guidelines* in Part F of the Code from 1 March 2018. The guidelines can be found here:

[http://www.hkicpa.org.hk/file/media/section5\\_membership/Professional%20Representation/aml/HKICPA\\_AML\\_Enforceable\\_GLs\\_Feb2018\\_20180228.pdf](http://www.hkicpa.org.hk/file/media/section5_membership/Professional%20Representation/aml/HKICPA_AML_Enforceable_GLs_Feb2018_20180228.pdf)

The definition of specified transactions is reproduced below for easy reference:

- (a) buying or selling of real estate;
- (b) managing of client money, securities or other assets;
- (c) management of bank, savings or securities accounts;
- (d) organisation of contributions for the creation, operation or management of corporations;
- (e) creation, operation or management of legal persons or arrangements;
- (f) buying or selling of business entities;
- (g) forming corporations or other legal persons;
- (h) acting as, or arranging for another person to act as, a director or secretary of a corporation, a partner of a partnership, or a similar position in relation to other legal persons;
- (i) providing a registered office, business address, correspondence or administrative address for a corporation, a partnership or any other legal person or arrangement;
- (j) acting as, or arranging for another person to act as, a trustee of an express trust or similar legal arrangement; or
- (k) acting, or arranging for another person to act, as a nominee shareholder for a person other than a corporation whose securities are listed on a recognized stock market.

### **Question C2**

According to Section 600.2 of the *AML Guidelines*, the extent to which a practice should comply with the requirements depends on the nature of transactions / services that a practice carries out or prepares for its clients (see the table below). If a practice carries out or prepares for its clients transactions or services specified in paragraphs 600.2.1 and 600.2.2 of the *AML Guidelines*, all sections are mandatory for the practice to the extent that they are applicable to the part of its business concerning specified service activities.

If a practice does not carry out or prepare for its clients transactions or services specified in paragraphs 600.2.1 and 600.2.2 of the *AML Guidelines*, it is not mandatory for it to

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<sup>2</sup> Practices referred to in the AML guidelines includes (a) practice units under the Professional Accountants Ordinance; (b) trust or company service providers, where the proprietors, partners or directors are members and; (c) members working in practices.

comply with sections other than suspicious transaction reporting and financial sanctions. If this practice chooses to comply with all sections of the AML Guidelines (including applying customer due diligence (“CDD”), ongoing monitoring and record keeping (“RK”) measures on clients regardless of services provided), the practice is considered to have applied “good practices”.

The <i>AML Guidelines</i> apply to practices as follows:	AML / CTF policies, procedures and controls (section 610)	CDD, RK and ongoing monitoring (sections 620, 630, 660)	Suspicious transaction reporting and financial sanctions (sections 640, 650)	Staff hiring and training (section 670)
When providing any service specified in paragraphs 600.2.1 or 600.2.2	<b>Mandatory</b>	<b>Mandatory</b>	<b>Mandatory</b>	<b>Mandatory</b>
When providing services other than those specified in paragraphs 600.2.1 or 600.2.2	<b>Good practice</b>	<b>Good practice</b>	<b>Mandatory</b>	<b>Good practice</b>

#### Question C4

High ML / TF risk situations set out in Section 620.12 of the *AML Guidelines* are:

- A client not physically present for identification purposes
- A politically exposed person
- A client with bearer shares
- A client that is connected with or has transactions or businesses in jurisdictions that do not apply, or insufficiently apply, the Financial Action Task Force recommendations, or otherwise posing higher ML / TF risk

#### Frequent asked questions (“FAQs”) on AML / CTF compliance monitoring

The Institute has issued answers to FAQs regarding AML / CTF compliance monitoring which can be accessed via the following link:

<https://www.hkicpa.org.hk/en/Tools/FAQ/Quality-assurance/Practice-review---AML-Monitoring>