



22 September 2005

**By e-mail < [EDComments@ifac.org](mailto:EDComments@ifac.org) > and by fax (0062 1 212 286 9570)**

Our Ref.: C/AASC

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

Dear Sir,

**[IAASB Exposure Draft on ISA 260 \(Revised\)](#)  
**[“The Auditor’s Communication with Those Charged with Governance”](#)****

The Hong Kong Institute of Certified Public Accountants welcomes the opportunity to provide you with our comments on the captioned IAASB Exposure Draft.

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We set out in the attachment our comments on the proposed revised ISA 260 for your consideration.

We trust that our comments are of assistance to you. If you require any clarifications on our comments, please contact the undersigned at [schan@hkcipa.org.hk](mailto:schan@hkcipa.org.hk).

Yours faithfully,

Stephen Chan  
Executive Director

SSLC/PM/jc  
Encl.



**HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS' COMMENTS ON  
THE IAASB EXPOSURE DRAFT ON ISA 260 (REVISED)  
"THE AUDITOR'S COMMUNICATION WITH THOSE CHARGED WITH  
GOVERNANCE"**

We are supportive of the proposed revision to ISA 260 and believe it is both important and helpful to practitioners. However, we have the following key and other specific comments which we request that they be considered carefully by the IAASB before finalizing the revised ISA.

**KEY COMMENTS**

**1. The requirement to communicate corrected material misstatements**

Paragraph 33(a) (bold) states unless all those charged with governance are involved in managing the entity, the auditor should also communicate material, corrected misstatements that were brought to the attention of management as a result of audit procedures. Furthermore paragraph 41 (non bold) states that communication of corrected misstatements identified as a result of audit procedures is important in assisting those charged with governance to fulfill their responsibility to oversee the financial reporting and disclosure process.

**Frequently management is preparing the financial statements at the same time as the auditors are performing the audit procedures and there is ongoing dialogue between management and the auditor. In such circumstances, it may be difficult to discern what constitutes an "error" as the matter may be resolved before it is reflected in the accounts. It may also be difficult to determine whether a particular error has been identified by management or by the auditor. We question the benefit in debating those points with management for the purpose of reporting to those charged with governance. We believe that an example of whether errors should be reported would be those which are indicative of a weakness in internal control. The auditor is already required to communicate such weaknesses to those charged with governance in ISA 315. Paragraph 120 (bold) of ISA 315 requires the auditor to make those charged with governance or management aware, as soon as practicable, and at an appropriate level of responsibility, of material weaknesses in the design or implementation of internal control which have come to the auditor's attention.**

**2. Use of the terms "significant", "serious", and "major"**

The term "significant" is used in paragraph 25 but no guidance is provided of what items should be considered significant. Paragraph 47 gives examples of matters that are "serious" and relevant to the responsibilities of those charged with governance, and the term is used in paragraphs 22, 25 and 46. Paragraph 42 introduces the term "major" issues.

**We would suggest that the above terms be considered carefully again and whether it is necessary to use the different terms. For consistency and to avoid confusion, it may be appropriate to only use one appropriate term.**



### **3. Scope of the Communications**

- (a) Paragraph 43(b) (bold) states that the auditor should communicate to those charged with governance, matters that have been agreed with those charged with governance or management to be communicated.

**We believe that this is extending the scope of the communications. The focus of ISAs should be on the auditor’s responsibilities in the audit of financial statements and the actions that are necessary to support a high quality audit. We do not believe that the ISA should have requirements that extend beyond that scope. Accordingly, we do not support paragraph 43(b) as drafted.**

**As drafted, the auditor could be held not to have conducted the audit in accordance with the ISAs for failure to fulfil responsibilities that have been separately agreed with management or those charged with governance but which extend beyond those necessary to support a quality audit.**

**We believe that the focus of the ISAs should be on the auditor’s responsibilities in the audit of financial statements and actions necessary to support a high quality audit.**

- (b) Paragraph 46 (bold) states that the auditor should communicate to those charged with governance other matters of which the auditor is aware that, in the auditor’s professional judgment, are serious and relevant to the responsibilities of those charged with governance.

**We are, similarly, concerned about this requirement regarding reporting on matters which in the auditor’s professional judgment are “serious and relevant to the responsibilities of those charged with governance”. We are concerned that the boundaries around the auditor’s responsibilities in this section are not defined sufficiently clearly to be effective in practice. For example, paragraph 47 refers to matters which arise from the financial statements or “Otherwise come to the attention of the auditor”. As ISA 315 “Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement” already requires the auditor to consider other information relevant to the audit, it is unclear what additional information might otherwise come to the attention of the auditor that is not already contemplated elsewhere in the ISAs, and are concerned how the requirement might be interpreted by others with the benefit of hindsight.**

**Furthermore, this section also introduces a new benchmark of matters that are “serious” and gives the example of “Serious deficient” governance structure and processes but the criteria by which auditors are expected to make such judgments are not defined and, in the absence of such criteria, we question how auditors will know how to effectively meet these requirements in practice.**



#### **4. Smaller Entities**

Paragraph 20 (non bold) states where all of those charged with governance are involved in managing the entity e.g. a small business where a single owner manages the entity and no one else has a governance role, if matters required by the ISA are communicated to person(s) with management responsibilities, and those person(s) also have governance responsibilities, the matters need not be communicated again to those same person(s) in their governance role. Paragraph 21 provides further guidance for smaller entities.

**We welcome the guidance in paragraphs 20 and 21 for smaller entities but consider that the proposed Standard could go further in addressing the needs of the auditors of smaller entities. It would be helpful for an overarching paragraph in the proposed Standard to deal with particular issues affecting smaller entities. For example, with regard to the auditor’s responsibilities as required in paragraphs 23 to 26, it would be useful to clarify in the ISA that these might be communicated through the engagement letter.**

#### **OTHER SPECIFIC COMMENTS ON PARAGRAPHS**

##### **1. Paragraphs 44 and 56 on matters of communication**

Paragraph 44 (non bold) states that other ISAs require communication with those charged with governance of matters such as:

- Material weaknesses in the design or implementation of internal control that could have a material effect on the financial statements that have come to the auditor’s attention (ISA 315, paragraph 120)
- Fraud the auditor has identified that involves management; employees who have significant roles in internal control; or others where the fraud results in a material misstatement in the financial statements (ISA 240 “The Auditor’s Responsibility to Consider Fraud in an Audit of Financial Statements”, paragraph 95)
- Non compliance with laws and regulations that comes to the auditor’s attention (ISA 250 “Consideration of Laws and Regulations”, paragraph 32)
- Events or conditions that may cast significant doubt on the entity’s ability to continue as a going concern (ISA 570 “Going Concern”)
- Circumstances that lead to expected modifications to the opinion in the auditor’s report (Proposed ISA 705 “Modifications to the Opinion in the Independent Auditor’s Report”, paragraph 36)

Paragraph 56 (bold) states that the auditor should issue a written communication to those charged with governance regarding significant matters arising from the conduct of, and findings from the audit.

**We are uncertain as to whether the “significant matters” referred to in paragraph 56 are the same as those defined in paragraph 44 and would recommend that further clarification be provided in this regard.**

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