

New auditing standards – firms should get ready for the change



HKICPA Technical Director (Ethics & Assurance) Stephen Chan explains the progress of converging Hong Kong Auditing Standards with International Auditing Standards and the new structure of Hong Kong Auditing Standards, and urges firms to make an early start to tackle the change

- Are you aware that a complete set of new auditing standards will be coming into force soon?
- Are you aware of the implementation date?

Progress on international convergence and new structure of auditing standards

Over the last couple of years, in pursuing the International Standards Convergence Policy set by the Institute Council, the Institute's Auditing and Assurance Standards Committee (AASC) has been extremely busy in converging the Institute's auditing standards with the International Auditing and Assurance Standards Board's (IAASB) International Auditing Standards (International Auditing Standards).

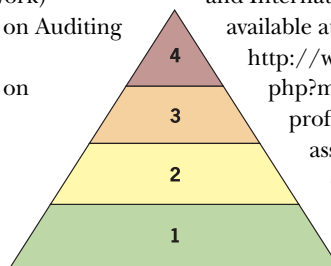
This means that the Institute's extant Statements of Auditing Standards (SAS) and Standards on Assurance Engagements (SAE) will be phased out and replaced by a complete set of new Hong Kong Standards on Quality Control, Auditing, Assurance and Related Services modelled

on International Auditing Standards. The new structure of Hong Kong Auditing Standards as illustrated in the chart on page 66 will comprise:

- Preface to Hong Kong Standards on Quality Control, Auditing, Assurance and Related Services (Auditing Preface)
- Hong Kong Standards on Quality Control (HKSQC)
- Hong Kong Framework for Assurance Engagements (Framework)
- Hong Kong Standards on Auditing (HKSA)
- Hong Kong Standards on Review Engagements (HKSRE)
- Hong Kong Standards on Assurance Engagements (HKSAE)

- Hong Kong Standards on Related Services (HKSRS)
- Hong Kong Standards on Investment Circular Reporting Engagements (HKSIR) (local standards with no international equivalent).

The 'construction' of the new structure of Hong Kong Auditing Standards involves four 'building blocks' as explained below. A comparison table between Hong Kong Auditing Standards and International Auditing Standards is available at the HKICPA website at <http://www.hkicpa.org.hk/index.php?mainLocation=/professionaltechnical/assurance/dueprocess/dueprocess.php>



Building Block 1 – October 2004 Exposure Draft of proposed Auditing Preface

This is the foundation of the new structure of Hong Kong Auditing Standards as it sets out the Council's objectives and due process in respect of setting Hong Kong Auditing Standards and explains the scope, authority and timing of application of these Standards. It also sets out the relationship between Hong Kong Auditing Standards and International Auditing Standards and the authority of Practice Notes, Auditing Guidelines and Auditing and Assurance Bulletins issued by the Institute.

The Exposure Draft is available at <http://www.hkicpa.org.hk/professionaltechnical/assurance/exposedraft/preface.pdf> and its comment deadline is 31 December 2004. The plan is to finalise the Preface for publication in Q1 of 2005.

Building Block 2 – October and November 2004 release of 12 final Hong Kong Auditing Standards

The components of this building block are 12 final Hong Kong Auditing Standards, which were released in October and November 2004 (Members' Handbook Updates 7 & 8 <http://www.hkicpa.org.hk/ebook/main.php>).

- HKSQC 1, 'Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements' (Systems of quality control in compliance with HKSQC 1 are required to be established by firms by 15 June 2005)

- HKSA 220, 'Quality Control for Audits of Historical Financial Information' (Effective for audits of financial statements for periods beginning on or after 15 June 2005 to tie in with the effective date of HKSQC 1)
 - Hong Kong Framework for Assurance Engagements (Effective October 2004)
 - HKSA 200, 'Objective and General Principles Governing an Audit of Financial Statements'
 - HKSA 240, 'The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements'
 - HKSA 300, 'Planning an Audit of Financial Statements'
 - HKSA 315, 'Understanding of the Entity and Its Environment and Assessing the Risks of Material Misstatement'
 - HKSA 330, 'The Auditor's Procedures in Response to Assessed Risks'
 - HKSA 500, 'Audit Evidence'
- HKSA 200, 240, 300, 315, 330 and 500 are effective for audits of financial statements for periods beginning on or after 15 December 2004.
- HKSAE 3000, 'Assurance Engagements other than Audits or Reviews of Historical Financial Information' (Effective for assurance engagements where the assurance report is dated on or after 1 January 2005)
 - HKSRS 4400, 'Engagements to Perform Agreed-Upon Procedures Regarding Financial Information' (Effective November 2004)
 - HKSRS 4410, 'Engagements to Compile Financial Statements' (Effective November 2004)

Building Block 3 – November 2004 Exposure Draft of 21 Proposed Hong Kong Auditing Standards

The components of this building block are 21 proposed Standards including:

- HKSA 210 'Terms of Audit Engagements'
- HKSA 250 'Consideration of Laws and Regulations in an Audit of Financial Statements'
- HKSA 260 'Communications of Audit Matters with Those Charged with Governance'
- HKSA 320 'Audit Materiality'
- HKSA 402 'Audit Considerations Relating to Entities Using Service Organizations'
- HKSA 501 'Audit Evidence – Additional Considerations for Specific Items'
- HKSA 505 'External Confirmations'
- HKSA 510 'Initial Engagements – Opening Balances'
- HKSA 520 'Analytical Procedures'
- HKSA 530 'Audit Sampling and Other Means of Testing'
- HKSA 540 'Audit of Accounting Estimates'
- HKSA 545 'Auditing Fair Value Measurements and Disclosures'
- HKSA 550 'Related Parties'
- HKSA 560 'Subsequent Events'
- HKSA 570 'Going Concern'
- HKSA 580 'Management Representations'
- HKSA 610 'Considering the Work of Internal Auditing'
- HKSA 620 'Using the Work of an Expert'
- HKSA 710 'Comparatives'
- HKSA 720 'Other Information in Documents Containing Audited Financial Statements'
- HKSRE 2400 'Engagements to Review Financial Statements'

It is proposed that if adopted, the 20 proposed HKSA will take effect for audits of financial statements for periods beginning on or after 15 December 2004. The proposed HKSRE 2400 will be effective upon publication.

The Exposure Draft is available at <http://www.hkicpa.org.hk/professionalttechnical/assurance/exposedraft/21standards.pdf> and its comment deadline is 28 February 2005. The plan is to finalise these 21 Standards for publication in Q2 of 2005.

Building Block 4 – Under construction

The components of this building block which is still under construction are five International Auditing Standards that remain to be adopted in Hong Kong. The first four are currently under revision by the IAASB. When the revision is completed they will be adopted by the AASC. The fifth has been issued as an Exposure Draft of proposed SAS 730 and will be finalised as part of the HKSIR series.

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| a. ISA 230 'Documentation' | d. ISA 800 'The Auditor's Report on Special Purpose Audit Engagements' |
| b. ISA 600 'Using the Work of Another Auditor' | e. ISAE 3400 (Previously ISA 810), 'The Examination of Prospective Financial Information' |
| c. ISA 700 'The Auditor's Report on Financial Statements' | |

Impact on auditors

This represents a perfect opportunity for firms to take a close look at their existing policies and procedures to see if there are inefficiencies that can be eliminated.

Many Hong Kong Auditing Standards are similar to the existing SAS and SAE, and little change will be required. But some Hong Kong Auditing Standards are different, and the audit risk, fraud consideration and quality control Standards which are crucial to the audit approach will require some fundamental changes – more consideration of internal controls for example.

Except for HKSA 220, all the final and proposed HKSA will be effective for ALL audits for periods beginning on or after 15 December 2004 while all the SAS (except for SAS 240) continue to be applicable for audits for periods beginning before 15 December 2004. For many firms this effectively means the HKSA will be first applicable for December 2005 year-end audits. However, if any of the clients have interim audits or short accounting periods, they will be affected by these new HKSA before then.

Furthermore firms should now start to make a critical assessment of their existing quality control policies and procedures and audit documentation to make sure that they are sufficient to comply with the systems of quality controls required under HKSQC 1 and HKSA 220.

Training

I have hosted a series of Technical Evening Update (TUE) seminars on the new Hong Kong Auditing Standards and over the course of the next year, I will be holding new and re-run sessions. The TUE Programme is available at <http://www.hkicpa.org.hk//index.php?mainLocation=/professionaltechnical/TUE/menu.php>.

The Annual Auditing Update Conference 2005 is tentatively scheduled to be held in March 2005 and I am sure that these new Hong Kong Auditing Standards will be the main focus.

All firms should start to look at their training schedules, their audit software, audit manuals and audit documentation.

