STATEMENT OF AUDITING STANDARDS 150 SUBSEQUENT EVENTS

(Effective for audits of financial statements for periods beginning before 15 December 2004)[*]

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[*] HKSA 560 "Subsequent Events" is effective for audits of financial statements for periods beginning on or after 15 December 2004.

STATEMENT OF AUDITING STANDARDS 150 SUBSEQUENT EVENTS

*Statements of Auditing Standards (SASs) are to be read in the light of SAS 010 "The scope and authority of auditing pronouncements". In particular, they contain basic principles and essential procedures (auditing standards), indicated by paragraphs in **bold italic type**, with which auditors are required to comply in the conduct of any audit including those of companies applying section 141D of the Companies Ordinance. SASs also include explanatory and other material which is designed to assist auditors in interpreting and applying auditing standards.*

Introduction

1. The purpose of this Statement of Auditing Standards (SAS) is to establish standards and provide guidance on auditors' responsibilities regarding subsequent events. In this SAS, the term "subsequent events" is used to refer to both events occurring between the period end and the date of the auditors' report, and facts discovered after the date of the auditors' report.

2. This SAS is written in the context of the audit of financial statements of limited companies. However, its principles also apply to the audit of financial statements of other entities.

3. ***The auditors should consider the effect of subsequent events on the financial statements and on the auditors' report. (SAS 150.1)***

4. When a component, such as a division, branch, subsidiary, joint venture or associate, is audited by other auditors, the principal auditors would consider the other auditors' procedures regarding subsequent events and the need to inform the other auditors of the planned date of the principal auditors' report.

5. Statement of Standard Accounting Practice 9 (revised) "Events after the balance sheet date" defines events after the balance sheet date as those events, both favourable and unfavourable, that occur between the balance sheet date and the date when the financial statements are authorised for issue.

Events occurring between the period end and the date of the auditors' report ("relevant events")

6. Standards and guidance on dating of auditors' reports are given in SAS 600 "Auditors' reports on financial statements". In accordance with the requirements of SAS 600, the auditors should date the auditors' report as of the completion date of the audit.

7. ***The auditors should perform procedures designed to obtain sufficient appropriate audit evidence that all material relevant events that may require adjustment of, or disclosure in, the financial statements have been identified and properly reflected therein. (SAS 150.2)***

8. These procedures are in addition to routine procedures which may be applied to specific transactions occurring after the period end to obtain audit evidence as to account balances as at the period end, for example, the testing of inventory cut-offs and payments to creditors. The auditors are not, however, expected to conduct a continuing review of all matters to which previously applied procedures have provided satisfactory conclusions.

9. The procedures to identify relevant events that may require adjustment of, or disclosure in, the financial statements would be performed as near as practicable to the date of the auditors' report and ordinarily include the following:

   a. reviewing procedures which management has established to ensure that relevant events are identified;

   b. reading minutes of the meetings of shareholders, the board of directors and audit and executive committees held after the period end and enquiring about matters discussed at meetings for which minutes are not yet available;

c. reviewing the entity's latest available management accounts and, as considered necessary and appropriate, budgets, cash flow forecasts and other related management reports;

d. enquiring, or extending previous oral or written enquiries, of the entity's lawyers concerning litigation and claims; and

e. enquiring of management as to whether any relevant events have occurred which might affect the financial statements.

The extent to which the results of these procedures require reviewing and updating immediately before the date of the auditors' report depends on the length of time which has elapsed between the date when these procedures were initially performed and the date of the auditors' report and the susceptibility of items to change over time.

10. Examples of specific enquiries which may be made of management include:

a. the current status of items that were accounted for on the basis of preliminary or inconclusive data;

b. whether new commitments, borrowings or guarantees have been entered into;

c. whether sales of assets have occurred or are planned;

d. whether the issue of new shares or debentures or an agreement to merge or liquidate has been made or is planned;

e. whether any assets have been appropriated by government or destroyed, for instance, by fire or flood;

f. whether there have been any developments regarding risk areas and contingencies;

g. whether any unusual accounting adjustments have been made or are contemplated; and

h. whether any relevant events have occurred or are likely to occur which will bring into question the appropriateness of accounting policies used in the financial statements as would be the case, for instance, if such events call into question the validity of the going concern assumption.

11. When, before the date of the auditors' report, the auditors become aware of relevant events which materially affect the financial statements, they should consider whether such events are properly accounted for and adequately disclosed in the financial statements. (SAS 150.3)

Facts discovered after the date of the auditors' report but before the financial statements are issued

12. The directors have the responsibility to issue financial statements which give a true and fair view and are not otherwise misleading. They may therefore reasonably be expected to inform the auditors of any facts discovered during the period from the date of the auditors' report to the date the financial statements are issued (for example to shareholders or equivalent), which may affect the financial statements.

13. The auditors do not have any responsibility to perform procedures or make any enquiry regarding the financial statements after the date of the auditors' report.

14. When, after the date of the auditors' report but before the financial statements are issued, the auditors become aware of facts which may materially affect the financial statements, they should consider whether the financial statements need amendment, should discuss the matter with the directors and should consider the implications for the auditors' report, taking the action appropriate in the circumstances. (SAS 150.4)

15. When the directors amend the financial statements, the auditors would carry out the procedures necessary in the circumstances and would provide the directors with a new auditors' report on the amended financial statements. The new auditors' report would be dated not earlier than the date the amended financial statements are approved by the directors and, accordingly, the procedures regarding relevant events would be extended to the date of the new auditors' report.

16. When the directors do not amend the financial statements in circumstances where the auditors believe they need to be amended, the auditors would consider issuing a revised auditors' report. They would also request the directors not to issue the financial statements with the original auditors' report. If the financial statements are subsequently released with the original auditors' report, the auditors would consider taking steps on a timely basis to prevent reliance on the auditors' report. For example, they may consider notifying the appropriate regulatory authorities and making an appropriate statement at the annual general meeting. They would also consider taking legal advice on their position. The action taken will depend on the auditors' legal rights and obligations and the recommendations of the auditors' lawyers.

Facts discovered after the financial statements have been issued but before their laying before the shareholders or equivalent

17. When, after the financial statements have been issued but before they have been laid before the shareholders or equivalent, the auditors become aware of facts which may materially affect the financial statements, they should consider whether the financial statements need revision, should discuss the matter with the directors and should consider the implications for the auditors' report, taking the action appropriate in the circumstances. (SAS 150.5)

18. When the directors revise the financial statements, the appropriate action for the auditors to take includes:

    a. carrying out the audit procedures necessary in the circumstances;

    b. considering, where appropriate, whether any laws or regulations (for example, the Stock Exchange Listing Rules) require the revision to be publicised;

    c. considering whether there is any requirement, in the case of entities in regulated industries, to communicate with the appropriate regulator;

    d. reviewing the steps taken by the directors to ensure that anyone in receipt of the previously issued financial statements together with the auditors' report thereon is informed of the situation; and

    e. issuing a new auditors' report on the revised financial statements.

19. When the auditors issue a new auditors' report, they would include a paragraph in their report referring to the note to the financial statements which more extensively discusses the reason for the revision of the previously issued financial statements, or setting out such reason, and referring to the earlier auditors' report issued by them on the financial statements. The auditors would date the new auditors' report not earlier than the date the revised financial statements are approved by the directors and, accordingly, the procedures regarding relevant events would be extended to the date of the new auditors' report.

20. If the directors do not revise the financial statements which the auditors believe need to be revised, the auditors would consider taking steps on a timely basis to prevent reliance on the auditors' report as suggested in paragraph 16 above.

Facts discovered after the financial statements are laid before the shareholders or equivalent

21. Because of the variety of conditions which might be encountered, some of the procedures set out in paragraphs 22 to 27 below are necessarily set out only in general terms; the specific actions to be taken in a particular case may vary somewhat in the light of the circumstances. The auditors would be well advised to consult with their lawyers when they encounter such circumstances.

22. The auditors' appointment expires at the annual general meeting. If after the annual general meeting, the auditors become aware of information which may materially affect financial statements previously reported on by them which were laid before the shareholders or equivalent at that meeting, they would, as soon as practicable, consider undertaking steps to determine whether the information is reliable. These steps would need to be performed even when the auditors have resigned, retired, not been re-appointed or have been discharged. In this connection, the auditors would discuss the matter with the directors and request cooperation with whatever investigation may be necessary.

23. When such subsequently discovered information is found to be reliable and relates to facts which may materially affect the financial statements, the auditors would take the action set out in paragraphs 24 to 26 below.

    However, the auditors may take the view that such action is not necessary after discussing with the directors and giving consideration to all the circumstances including, amongst other things:

    a. the time elapsed since the financial statements were issued;

    b. the materiality of the facts discovered; and

    c. whether the audited financial statements for a subsequent period report or will report a correction of a fundamental error in respect of the facts discovered.

24. When the auditors have concluded that action would need to be taken to prevent future reliance on the auditors' report, they would advise the directors to make appropriate disclosure of the newly discovered facts and their effect on the financial statements to shareholders or equivalent. When the directors undertake to make appropriate disclosure, the method used and the disclosure made will depend on the circumstances.

    a. If the effect on the financial statements or auditors' report of the subsequently discovered facts can promptly be determined, disclosure would consist of issuing, as soon as practicable, revised financial statements and auditors' report. The reasons for the revision would be described in a note to the financial statements and referred to in the auditors' report (see guidance in paragraph 19 above).

    b. When the issuance of the audited financial statements for a subsequent period is imminent, so that disclosure is not delayed, appropriate disclosure of the revision could be made in such financial statements instead of reissuing the earlier financial statements pursuant to subparagraph (a).

    c. When the effect on the financial statements of subsequently discovered facts cannot be determined without a prolonged investigation, the steps set out in paragraphs 24(a) and (b) above may be delayed. In these circumstances the auditors would advise the directors of the facts discovered and of the possibility that the facts may require the financial statements and/or auditors' report to be re-issued or may need to be disclosed in the financial statements for a subsequent period. The directors would be advised to make appropriate disclosure to the shareholders or equivalent and, where appropriate, the relevant regulatory authorities.

    d. In addition to taking the actions as set out in paragraphs 24(a), (b) and (c) above, the auditors would also consider whether notification or disclosure needs to be made to any other party who may be relying on the previously issued auditors' report.

25. If the directors refuse to make the disclosure recommended in paragraph 24 above, the auditors would notify each member of the board of directors of such refusal and that, in the absence of disclosure being made, the auditors may take steps to prevent future reliance upon the auditors' report. The steps which the auditors would consider taking may include:

    a. Notification to the directors that the auditors' report must no longer be associated with the financial statements; and

    b. Notification to shareholders or equivalent that the financial statements and the auditors' report should no longer be relied upon; and/or

    c. Notification to the appropriate regulatory authorities that the financial statements and the auditors' report should no longer be relied upon; and/or

    d. Resignation.

    However, such steps would only be taken after seeking legal advice and after considering the auditors' duty of confidentiality as set out in Statement 1.204A "Confidentiality" and any relevant legislation.

26. The following provides guidance on the content of any disclosure made by the auditors in accordance with paragraph 25:

a. The disclosure would describe the effect the subsequently discovered facts would have had on the auditors' report if they had been known to the auditors at the date of the auditors' report and had not been reflected in the financial statements. The disclosure would include a description of the nature of the subsequently discovered facts and of their effect on the financial statements.

b. The disclosure would be as precise and factual as possible and would not go beyond that which is reasonably necessary to accomplish the purpose mentioned in the preceding subparagraph (a). Comments concerning the conduct or motives of any person would be avoided.

27. There may be circumstances in which the auditors are unable satisfactorily to investigate the information discovered, for example because the directors refuse to co-operate or to provide information or explanations. In these circumstances the auditors would for example consider taking the following steps:

a. Requesting the directors to make an appropriate disclosure as soon as practicable to the shareholders or equivalent and, where appropriate, the appropriate regulatory authorities.

   The contents of such disclosure would normally include:

   i. the nature of the subsequently discovered information;

   ii. where these can be identified, the items in the financial statements which may be materially affected by the information;

   iii. the fact that the auditors have been unable satisfactorily to obtain all the information and explanations which they consider necessary for the purposes of investigating the information;

   iv. a statement that, as a result of the scope limitation stated in (iii) above, the auditors have been unable to establish the effect of the discovered information on the financial statements. It may also be indicated that there is an uncertainty as to whether further reliance on the previous auditors' report would be appropriate;

   v. if known, the reason or reasons why the auditors have been unable satisfactorily to investigate the information.

b. Should the directors fail or refuse to make the appropriate disclosure as set out in (a) above, the auditors would consider notifying the shareholders or equivalent and the appropriate regulatory authorities. The contents of this notification would be as set out in paragraphs (a)(i) - (v) above.

c. Particularly in circumstances where the directors refuse to co-operate in allowing the auditors to investigate the information discovered or refuse to make the disclosure set out in paragraph (a) above, the auditors would also consider resigning.

Such steps would only be taken after seeking legal advice and after considering the auditors' duty of confidentiality as set out in Statement 1.204A "Confidentiality" and any relevant legislation.

Compliance with International Standards on Auditing

28. Compliance with the auditing standards contained in this SAS ensures compliance in all material respects with the basic principles and essential procedures in International Standard on Auditing (ISA) 560 "Subsequent Events" with the exception of paragraph 16 of ISA 560 which has been restated in this SAS in paragraph 19 as guidance only. Further, the guidance given in ISA 560 which relates to the offering of securities to the public, has not been reflected in this SAS.

Effective date

29. This SAS is effective for audits of financial statements for period beginning before 15 December 2004.