



16 May 2016

Our Ref.: C/AASC

International Auditing and Assurance Standards Board
529 Fifth Avenue, 6th Floor,
New York
NY 10017
USA

Dear Sirs,

IAASB Invitation to Comment, *Enhancing Audit Quality in the Public Interest: A Focus on Professional Skepticism, Quality Control and Group Audits*

The Hong Kong Institute of Certified Public Accountants (HKICPA) is the only statutory licensing body of accountants in Hong Kong responsible for the professional training, development and regulation of the accountancy profession. The HKICPA sets auditing and assurance standards, ethical standards and financial reporting standards in Hong Kong. We welcome the opportunity to provide our comments on the captioned IAASB Invitation to Comment (ITC).

We support the IAASB's continuing efforts to enhance audit quality. The focus on professional scepticism (PS), quality control (QC) and group audits (GA) is considered appropriate.

We appreciate the IAASB's commitment in revising the standards such that they stay relevant in the face of continually changing circumstances. We encourage the IAASB to further develop guidance to cover key issues encountered by practitioners, in particular, application guidance on quality control and group audits. Our responses to the specific questions in the ITC are included in the attachment.

We trust that our comments are of assistance to the IAASB in deciding the next steps. If you require any clarification on our comments, please do not hesitate to contact our Selene Ho, Associate Director at selene@hkiipa.org.hk.

Yours faithfully,

Chris Joy
Executive Director

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**HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS'
COMMENTS ON THE IAASB'S INVITATION TO COMMENT
ENHANCING AUDIT QUALITY IN THE PUBLIC INTEREST: A FOCUS ON
PROFESSIONALSKEPTICISM, QUALITY CONTROL AND GROUP AUDITS**

Comments on Professional Skepticism (PS)

PS1. Is your interpretation of the concept of professional skepticism consistent with how it is defined and referred to in the ISAs? If not, how could the concept be better described?

We believe that PS is an attribute that is developed through experience and nurturing within a strong professional and ethical environment. We support IAASB's plan to emphasize the importance of professional scepticism in revising specific standards.

With financial reporting requiring significant management judgments in critical areas such as impairment assessment relating to key items in the statement of financial position, including intangible assets with infinite lives and goodwill, valuations and going concern issues, it is important that auditors are able and be prepared to challenge assumptions made and judgments reached in the preparation of a company's financial statements. PS does not mean that the auditor should mistrust all information and representations provided by management and to take this approach would create a very difficult working relationship.

However, a belief in the honesty and integrity of management does not relieve the auditor of the need to maintain PS or allow the auditor to be satisfied with less than persuasive audit evidence.

PS2. What do you believe are the drivers for, and impediments to, the appropriate application of professional skepticism? What role should we take to enhance those drivers and address those impediments? How should we prioritize the areas discussed in paragraph 37?

Investors, regulators and other stakeholders expect auditors to be "critical challengers". We believe some of the drivers for the application of PS include knowledge, training and performance evaluation. Audit experience together with knowledge would enable auditors to facilitate the exercise of PS and profession judgement.

In addition, appropriate training at the professional level is also important for enhancing the skills towards PS, in particular for junior auditors. It would be beneficial and important for auditors to receive feedback from team reviewers upon completion of engagement.

A key impediment to the application of PS is the work demand and time pressure to complete the engagement on a timely basis. This may cause auditors to apply

a lower level of PS than expected and this would affect the audit quality of the audit.

As highlighted in paragraph 32 of the ITC, environmental and contextual factors can also affect the application of PS including local norms and culture in which an auditor operates. An example cited being auditors in certain jurisdictions may be less comfortable challenging management when auditing areas in the financial statements that are highly judgemental or subjective.

When considering the proposed revisions to enhance PS, we encourage the IAASB to consider the cultural perspective in regard to the application of PS.

To provide additional guidance on the application of PS, we are of the view that the IAASB should:

- compile drivers and areas for improvement after consultation with regulators, the IASB and the profession
- ensure concept of PS is consistently described across professional standards and consideration of how ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statement* can be enhanced to embrace PS.
- issue guidance on the concept of PS
- develop implementation programme/training material

Whilst there is a general understanding of the concept of PS as defined in the ISAs, the IAASB should consider developing practical guidance on what PS is and how it should be documented, together with IAESB and IESBA. This will help to put into context IAASB's intended interpretation of PS.

Comments on Quality Control (QC)

QC1. Views around the use of a Quality Management Approach (QMA)

Given that the ISQC 1 has been in place for many years and practitioners are familiar with the requirements. The IAASB would need to consider the implications to small and medium sized practitioners (SMPs) when introducing a new concept. SMPs would require training support and implementation guidance. It may be more effective to revise ISQC 1.

QC2. Engagement partner roles and responsibilities

We believe that strengthening ISA 220 to clarify what is meant by performance, direction and supervision and review by the engagement partner would be useful in improving audit quality.

Building into ISA 220 a more proactive, scalable and robust approach to the identification of risks to audit quality at the engagement level, and development of specific responses to address those risks would also be helpful to practitioners, in particular, the small and medium sized practitioners (SMPs).

QC3. Others involved in the audit

We support proposals to provide additional guidance on engagement partner's role in reviewing the work of other auditors as well as clarifying the allocation of work between engagement partner and team.

We do not support the proposals to revisit the requirements to make reference to the report of another auditor. Given that the group auditor is responsible for the group audit opinion, making reference to the report of another auditor may confuse readers and give rise to the need for further explanation if the opinions are not consistent. The principles of the involvement of others should be covered by ISA 600.

QC6. Role of Engagement Quality Control Reviews and Responsibilities of EQC Reviewers (EQCR)

In the IESBA Code of Ethics for Professional Accountants (COE), "public interest entity" (PIE) is defined as:

- (a) A listed entity; and
- (b) An entity (i) by regulation or legislation as a public interest entity; or (ii) for which the audit is required by regulation or legislation to be conducted in compliance with the same independence requirements that apply to the audit of listed entities. Such regulation may be promulgated by any relevant regulator, including an audit regulator.

Currently, there is no definition of "public interest entities" in the ISAs. It would be useful to align the definition in the standards. Additional guidance should be developed to clarify IAASB's intentions. If IAASB were to adopt the definition in the COE, in effect, for Hong Kong, it would still only cover listed entities as currently, there is no local legislation or regulation imposing such requirement as set out in (b).

QC9. HR and engagement partner competency

We support the IAASB's proposals to undertake a more detailed review of the relationship between IES 8(Revised) and the quality control standards to determine whether greater attention can be given in the quality control standards to the requirements in IES 8 (Revised).

QC10. Transparency reporting

Currently, there is no such requirement for transparency reporting in Hong Kong.

QC13. What are the specific SMPs and public sector considerations?

When revising ISQC 1 and ISA 220, the proposed revisions should be made scalable for SMPs. In Hong Kong, there is a statutory requirement to perform an audit of financial statements for all companies incorporated in Hong Kong. SMPs in Hong Kong predominately audit small owner-managed entities.

Comments on Group Audits (GA)

In general, we support the proposals to provide further guidance for group auditors to drive earlier identification of potential issues, in particular for complex group structures.

ISA 600 currently does not include guidance on dealing with auditors of associate entities. We believe that the development of such guidance and its inclusion in future standards would be useful to practitioners. However, for the reasons given above, we do not agree with the proposal to make reference to another auditor in the auditor's report.

In certain jurisdictions, the access to component auditors and work papers may be limited by local laws. In these circumstances, increased requirements for the direction, supervision and performance of work done by component auditors would give rise to compliance concerns for group auditors.

In May 2015, the Ministry of Finance in the People's Republic of China has issued the Provisional regulations on CPA Practices carrying out audit services relating to the listing of Mainland enterprises outside Mainland ("Provisional regulations"). The Provisional Regulations are effective from 1 July 2015.

The Provisional regulations have implications for CPA practices established in foreign jurisdictions, Hong Kong, Macau and Taiwan. In the context of the Provisional regulations, audit services relating to the listing of Mainland enterprises outside Mainland mean audit services relating to the direct or indirect issue and listing (including intended listing) outside Mainland of the shares, bonds or other securities of Mainland enterprises and the subsequent audits of their annual financial statements.

Amongst other requirements, a key requirement is for CPA practices from foreign jurisdictions, Hong Kong, Macau and Taiwan to enter into a business cooperation agreement with a Mainland CPA practice when such CPA practices are appointed to conduct audit services of Mainland enterprises. The Provisional regulations also specify that the audit working papers prepared as a result of the work performed in the Mainland should be kept in the Mainland by the Mainland CPA practice.

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