



MEMBERS' HANDBOOK

Update No. 238

(Issued 29 May 2020)

VOLUME I

Document Reference and Title

[Contents of Volume I](#)

Instructions

Discard the existing pages i and ii and replace with the revised pages i and ii.

Explanations

Revised contents page

PROFESSIONAL ETHICS

[Code of Ethics for Professional Accountants, Chapter A Part 4B, Independence for Assurance Engagements Other Than Audit and Review Engagements](#)

Insert after Code of Ethics for Professional Accountants (Revised 2018).

Note 1

VOLUME III

Document Reference and Title

[Contents of Volume III](#)

Instructions

Discard the existing pages i and iii and replace with the revised pages i and iii.

Explanations

Revised contents page

HONG KONG STANDARDS ON INVESTMENT CIRCULAR REPORTING ENGAGEMENTS

[HKSIR 500, Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness](#)

Discard HKSIR 500 revised in September 2019 and replace with the attached HKSIR 500 revised in May 2020.

Note 2

Note:

1. Amendments as a result of revisions to Part 4B of the *International Code of Ethics for Professional Accountants (Including Independence Standards)* to reflect terms and concepts used in ISAE 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*.

Chapter A, Part 4B of the *Code of Ethics for Professional Accountants* (the “Code”) comprises the independence standards for assurance engagements other than audit and review engagements. The main amendments are:

- changes in key terminology, including a revised definition of the term “assurance client”;
- amendments to certain independence requirements in light of the revised assurance client definition;
- greater clarity as to the parties to an assurance engagement and their roles and responsibilities, and the related independence requirements that apply; and
- a clearer distinction between the types of assurance engagement covered in Chapter A, Parts 4A (addressing independence for audit and review engagements) and 4B of the Code.

These amendments for assurance engagements with respect to underlying subject matter covering periods will be effective for periods beginning on or after 15 June 2021; otherwise, it will be effective as of 15 June 2021. Early adoption will be permitted. In order for readers to easily identify all the changes, marked-ups to Part 4B, Chapter A of the Code are included in the pronouncement.

2. HKSIR 500 is revised to conform to the latest regulatory and financial reporting requirements. The main revisions are:
 - aligning definitions with those in HKSIR 200 *Accountants’ Reports on Historical Financial Information in Investment Circulars*;
 - amending references to the latest Listing Rules;
 - amending the guidance on procedures on indebtedness statement in paragraph 51;
 - in the example letter on a working capital statement in Appendix 2, providing suggested modification to opinion when confirmations are not returned but alternative evidence has been sought; and
 - in the example letter on a statement of indebtedness in Appendix 3, redrafting the sample procedures for lease liabilities.

Revisions to HKSIR 500 are effective on 1 June 2020. In order for readers to easily identify all the changes, a marked-up version is posted at:

https://www.hkicpa.org.hk/-/media/Document/SSD/update/changes_update238.pdf



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Code of Ethics for Professional Accountants
Chapter A Part 4B

Independence for Assurance Engagements Other Than Audit and Review Engagements



Hong Kong Institute of
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香港會計師公會

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The revisions to Part 4B of Chapter A of the Code of Ethics for Professional Accountants (Code of Ethics) is based on *Revisions to Part 4B of the Code to Reflect Terms and Concepts Used in International Standard on Assurance Engagements 3000 (Revised)* of the International Ethics Standards Board for Accountants (IESBA), published by the International Federation of Accountants (IFAC) in January 2020 and is used with permission of IFAC.

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PART 4B – INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

SECTION 900

APPLYING THE CONCEPTUAL FRAMEWORK TO INDEPENDENCE FOR ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS

Introduction

General

900.1 This Part applies to assurance engagements other than audit engagements and review engagements ~~(referred to as “assurance engagements” in this Part)~~. Examples of such engagements include:

- Assurance on an entity’s key performance indicators.
- Assurance on an entity’s compliance with law or regulation.
- Assurance on performance criteria, such as value for money, achieved by a public sector body.
- Assurance on the effectiveness of an entity’s system of internal control.
- Assurance on an entity’s greenhouse gas statement.
- An audit of specific elements, accounts or items of a financial statement.
- ~~Performance assurance on a company’s key performance indicators.~~

900.2 In this Part, the term “professional accountant” refers to individual professional accountants in public practice and their firms.

900.3 HKSQC 1 requires a firm to establish policies and procedures designed to provide it with reasonable assurance that the firm, its personnel and, where applicable, others subject to independence requirements maintain independence where required by relevant ethics standards. In addition, HKSAEs and HKSAAs establish responsibilities for engagement partners and engagement teams at the level of the engagement. The allocation of responsibilities within a firm will depend on its size, structure and organization. Many of the provisions of Part 4B do not prescribe the specific responsibility of individuals within the firm for actions related to independence, instead referring to “firm” for ease of reference. Firms assign responsibility for a particular action to an individual or a group of individuals (such as an assurance team) in accordance with HKSQC 1. ~~In addition~~ Additionally, an individual professional accountant remains responsible for compliance with any provisions that apply to that accountant’s activities, interests or relationships.

900.4 Independence is linked to the principles of objectivity and integrity. It comprises:

- (a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

- (b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm’s or an assurance team member’s integrity, objectivity or professional skepticism has been compromised.

In this Part, references to an individual or firm being “independent” mean that the individual or firm has complied with the provisions of this Part.

900.5 When performing assurance engagements, the Code requires firms to comply with the fundamental principles and be independent. This Part sets out specific requirements and application material on how to apply the conceptual framework to maintain independence when performing assurance engagements other than audit or review ~~such~~ engagements. The conceptual framework set out in Section 120 applies to independence as it does to the fundamental principles set out in Section 110.

900.6 This Part describes:

- (a) Facts and circumstances, including professional activities, interests and relationships, that create or might create threats to independence;
- (b) Potential actions, including safeguards, that might be appropriate to address any such threats; and
- (c) Some situations where the threats cannot be eliminated or there can be no safeguards to reduce the threats to an acceptable level.

Description of ~~Other~~ Assurance Engagements

900.7 ~~Assurance engagements are designed to enhance intended users’ degree of confidence about the outcome of the evaluation or measurement of a subject matter against criteria. In an assurance engagement, the firm aims to obtain sufficient appropriate evidence in order to~~ expresses a conclusion designed to enhance the degree of confidence of the intended users (other than the responsible party) about the subject matter information. HKSAE 3000 (Revised) describes the elements and objectives of an assurance engagement conducted under that Standard, and the Assurance Framework provides a general description of assurance engagements. An assurance engagement might either be an attestation engagement or a direct engagement. ~~outcome of the evaluation or measurement of a subject matter against criteria. The Assurance Framework describes the elements and objectives of an assurance engagement and identifies engagements to which HKSAEs apply. For a description of the elements and objectives of an assurance engagement, refer to the Assurance Framework.~~

900.8 In this Part, the term ‘assurance engagement’ refers to assurance engagements other than audit engagements and review engagements. ~~The outcome of the evaluation or measurement of a subject matter is the information that results from applying the criteria to the subject matter. The term “subject matter information” is used to mean the outcome of the evaluation or measurement of a subject matter. For example, the Assurance Framework states that an assertion about the effectiveness of internal control (subject matter information) results from applying a framework for evaluating the effectiveness of internal control, such as COSO or CoCo (criteria), to internal control, a process (subject matter).~~

900.9 ~~Assurance engagements might be assertion-based or direct reporting. In either case, they involve three separate parties: a firm, a responsible party and intended users.~~

~~900.10 In an assertion-based assurance engagement, the evaluation or measurement of the subject matter is performed by the responsible party. The subject matter information is in the form of an assertion by the responsible party that is made available to the intended users.~~

~~900.11 In a direct reporting assurance engagement, the firm:~~

- ~~(a) Directly performs the evaluation or measurement of the subject matter; or~~
- ~~(b) Obtains a representation from the responsible party that has performed the evaluation or measurement that is not available to the intended users. The subject matter information is provided to the intended users in the assurance report.~~

Reports that Include a Restriction on Use and Distribution

~~900.429~~ An assurance report might include a restriction on use and distribution. If it does and the conditions set out in Section 990 are met, then the independence requirements in this Part may be modified as provided in Section 990.

Audit and Review Engagements

~~900.4310~~ Independence standards for audit and review engagements are set out in Part 4A – *Independence for Audit and Review Engagements*. If a firm performs both an assurance engagement and an audit or review engagement for the same client, the requirements in Part 4A continue to apply to the firm, a network firm and the audit or review team members.

Requirements and Application Material

General

~~R900.4411~~ A firm performing an assurance engagement shall be independent of the assurance client.

~~900.11 A1~~ For the purposes of this Part, the assurance client in an assurance engagement is the responsible party and also, in an attestation engagement, the party taking responsibility for the subject matter information (who might be the same as the responsible party).

~~900.11 A2~~ The roles of the parties involved in an assurance engagement might differ and affect the application of the independence provisions in this Part. In the majority of attestation engagements, the responsible party and the party taking responsibility for the subject matter information are the same. This includes those circumstances where the responsible party involves another party to measure or evaluate the underlying subject matter against the criteria (the measurer or evaluator) where the responsible party takes responsibility for the subject matter information as well as the underlying subject matter. However, the responsible party or the engaging party might appoint another party to prepare the subject matter information on the basis that this party is to take responsibility for the subject matter information. In this circumstance, the responsible party and the party responsible for the subject matter information are both assurance clients for the purposes of this Part.

~~900.11 A3~~ In addition to the responsible party and, in an attestation engagement, the party taking responsibility for the subject matter information, there might be other parties in relation to the engagement. For example, there might be a separate engaging party or a party who is a measurer or evaluator other than the party

taking responsibility for the subject matter information. In these circumstances, applying the conceptual framework requires the professional accountant to identify and evaluate threats to the fundamental principles created by any interests or relationships with such parties, including whether any conflicts of interest might exist as described in Section 310.

R900.4512 A firm shall apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence in relation to an assurance engagement.

Multiple Responsible Parties and Parties Taking Responsibility for the Subject Matter Information

900.13 A1 In some assurance engagements, whether an attestation engagement or direct engagement, there might be several responsible parties or, in an attestation engagement, several parties taking responsibility for the subject matter information. In determining whether it is necessary to apply the provisions in this Part to each individual responsible party or each individual party taking responsibility for the subject matter information in such engagements, the firm may take into account certain matters. These matters include whether an interest or relationship between the firm, or an assurance team member, and a particular responsible party or party taking responsibility for the subject matter information would create a threat to independence that is not trivial and inconsequential in the context of the subject matter information. This determination will take into account factors such as:

(a) The materiality of the underlying subject matter or subject matter information for which the particular party is responsible in the context of the overall assurance engagement.

(b) The degree of public interest associated with the assurance engagement.

If the firm determines that the threat created by any such interest or relationship with a particular party would be trivial and inconsequential, it might not be necessary to apply all of the provisions of this section to that party.

Network firms~~Firms~~

R900.4614 When a firm knows or has reason to believe that interests and relationships of a network firm create a threat to the firm's independence, the firm shall evaluate and address any such threat.

900.46-14 A1 Network firms are discussed in paragraphs 400.50 A1 to 400.54 A1.

Related Entities

R900.4715 When the assurance team knows or has reason to believe that a relationship or circumstance involving a related entity of the assurance client is relevant to the evaluation of the firm's independence from the client, the assurance team shall include that related entity when identifying, evaluating and addressing threats to independence.

Types of Assurance Engagements

Assertion-based Assurance Engagements

~~R900.18~~—When performing an assertion-based assurance engagement:

- ~~(a)~~—The assurance team members and the firm shall be independent of the assurance client (the party responsible for the subject matter information, and which might be responsible for the subject matter) as set out in this Part. The independence requirements set out in this Part prohibit certain relationships between assurance team members and (i) directors or officers, and (ii) individuals at the client in a position to exert significant influence over the subject matter information;
- ~~(b)~~—The firm shall apply the conceptual framework set out in Section 120 to relationships with individuals at the client in a position to exert significant influence over the subject matter of the engagement; and
- ~~(c)~~—The firm shall evaluate and address any threats that the firm has reason to believe are created by network firm interests and relationships.

~~R900.19~~—When performing an assertion-based assurance engagement where the responsible party is responsible for the subject matter information but not the subject matter:

- ~~(a)~~—The assurance team members and the firm shall be independent of the party responsible for the subject matter information (the assurance client); and
- ~~(b)~~—The firm shall evaluate and address any threats the firm has reason to believe are created by interests and relationships between an assurance team member, the firm, a network firm and the party responsible for the subject matter.

~~900.19 A1~~—In the majority of assertion-based assurance engagements, the responsible party is responsible for both the subject matter information and the subject matter. However, in some engagements, the responsible party might not be responsible for the subject matter. An example might be when a firm is engaged to perform an assurance engagement regarding a report that an environmental consultant has prepared about a company's sustainability practices for distribution to intended users. In this case, the environmental consultant is the responsible party for the subject matter information but the company is responsible for the subject matter (the sustainability practices).

Direct Reporting Assurance Engagements

~~R900.20~~—When performing a direct reporting assurance engagement:

- ~~(a)~~—The assurance team members and the firm shall be independent of the assurance client (the party responsible for the subject matter); and
- ~~(b)~~—The firm shall evaluate and address any threats to independence the firm has reason to believe are created by network firm interests and relationships.

Multiple Responsible Parties

~~900.21 A1~~—In some assurance engagements, whether assertion-based or direct reporting, there might be several responsible parties. In determining whether it is necessary to apply the provisions in this Part to each responsible party in such engagements, the firm may take into account certain matters. These matters include whether an interest or relationship between the firm, or an assurance team member, and a particular responsible party would create a threat to

~~independence that is not trivial and inconsequential in the context of the subject matter information. This determination will take into account factors such as:~~

- ~~(a) The materiality of the subject matter information (or of the subject matter) for which the particular responsible party is responsible.~~
- ~~(b) The degree of public interest associated with the engagement.~~

~~If the firm determines that the threat created by any such interest or relationship with a particular responsible party would be trivial and inconsequential, it might not be necessary to apply all of the provisions of this section to that responsible party.~~

[Paragraphs 900.22-16 to 900.29 are intentionally left blank]

Period During which Independence is Required

R900.30 Independence, as required by this Part, shall be maintained during both:

- (a)** The engagement period; and
- (b)** The period covered by the subject matter information.

900.30 A1 The engagement period starts when the assurance team begins to perform assurance services with respect to the particular engagement. The engagement period ends when the assurance report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has ended or the issuance of the final assurance report.

R900.31 If an entity becomes an assurance client during or after the period covered by the subject matter information on which the firm will express a conclusion, the firm shall determine whether any threats to independence are created by:

- (a)** Financial or business relationships with the assurance client during or after the period covered by the subject matter information but before accepting the assurance engagement; or
- (b)** Previous services provided to the assurance client.

R900.32 Threats to independence are created if a non-assurance service was provided to the assurance client during, or after the period covered by the subject matter information, but before the assurance team begins to perform assurance services, and the service would not be permitted during the engagement period. In such circumstances, the firm shall evaluate and address any threat to independence created by the service. If the threats are not at an acceptable level, the firm shall only accept the assurance engagement if the threats are reduced to an acceptable level.

900.32 A1 Examples of actions that might be safeguards to address such threats include:

- Using professionals who are not assurance team members to perform the service.
- Having an appropriate reviewer review the assurance and non-assurance work as appropriate.

R900.33 If a non-assurance service that would not be permitted during the engagement period has not been completed and it is not practical to complete or end the service before the commencement of professional services in connection with the assurance engagement, the firm shall only accept the assurance engagement if:

- (a) The firm is satisfied that:
 - (i) The non-assurance service will be completed within a short period of time; or
 - (ii) The client has arrangements in place to transition the service to another provider within a short period of time;
- (b) The firm applies safeguards when necessary during the service period; and
- (c) The firm discusses the matter with those charged with governance.

[Paragraphs 900.34 to 900.39 are intentionally left blank]

General Documentation of Independence for Assurance Engagements ~~Other than Audit and Review Engagements~~

R900.40 A firm shall document conclusions regarding compliance with this Part, and the substance of any relevant discussions that support those conclusions. In particular:

- (a) When safeguards are applied to address a threat, the firm shall document the nature of the threat and the safeguards in place or applied; and
- (b) When a threat required significant analysis and the firm concluded that the threat was already at an acceptable level, the firm shall document the nature of the threat and the rationale for the conclusion.

900.40 A1 Documentation provides evidence of the firm's judgments in forming conclusions regarding compliance with this Part. However, a lack of documentation does not determine whether a firm considered a particular matter or whether the firm is independent.

[Paragraphs 900.41 to 900.49 are intentionally left blank]

Breach of an Independence Provision for Assurance Engagements ~~Other than Audit and Review Engagements~~

When a Firm Identifies a Breach

R900.50 If a firm concludes that a breach of a requirement in this Part has occurred, the firm shall:

- (a) End, suspend or eliminate the interest or relationship that created the breach;
- (b) Evaluate the significance of the breach and its impact on the firm's objectivity and ability to issue an assurance report; and
- (c) Determine whether action can be taken that satisfactorily addresses the consequences of the breach.

In making this determination, the firm shall exercise professional judgment and take into account whether a reasonable and informed third party would be likely to

conclude that the firm's objectivity would be compromised, and therefore, the firm would be unable to issue an assurance report.

R900.51 If the firm determines that action cannot be taken to address the consequences of the breach satisfactorily, the firm shall, as soon as possible, inform the party that engaged the firm or those charged with governance, as appropriate. The firm shall also take the steps necessary to end the assurance engagement in compliance with any applicable legal or regulatory requirements relevant to ending the assurance engagement.

R900.52 If the firm determines that action can be taken to address the consequences of the breach satisfactorily, the firm shall discuss the breach and the action it has taken or proposes to take with the party that engaged the firm or those charged with governance, as appropriate. The firm shall discuss the breach and the proposed action on a timely basis, taking into account the circumstances of the engagement and the breach.

R900.53 If the party that engaged the firm does not, or those charged with governance do not concur that the action proposed by the firm in accordance with paragraph R900.50(c) satisfactorily addresses the consequences of the breach, the firm shall take the steps necessary to end the assurance engagement in compliance with any applicable legal or regulatory requirements relevant to ending the assurance engagement

Documentation

R900.54 In complying with the requirements in paragraphs R900.50 to R900.53, the firm shall document:

- (a) The breach;
- (b) The actions taken;
- (c) The key decisions made; and
- (d) All the matters discussed with the party that engaged the firm or those charged with governance.

R900.55 If the firm continues with the assurance engagement, it shall document:

- (a) The conclusion that, in the firm's professional judgment, objectivity has not been compromised; and
- (b) The rationale for why the action taken satisfactorily addressed the consequences of the breach so that the firm could issue an assurance report.

SECTION 905

FEES

Introduction

- 905.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 905.2 The nature and level of fees or other types of remuneration might create a self-interest or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

Fees—Relative Size

- 905.3 A1 When the total fees generated from an assurance client by the firm expressing the conclusion in an assurance engagement represent a large proportion of the total fees of that firm, the dependence on that client and concern about losing the client create a self-interest or intimidation threat.
- 905.3 A2 Factors that are relevant in evaluating the level of such threats include:
- The operating structure of the firm.
 - Whether the firm is well established or new.
 - The significance of the client qualitatively and/or quantitatively to the firm.
- 905.3 A3 An example of an action that might be a safeguard to address such a self-interest or intimidation threat is increasing the client base in the firm to reduce dependence on the assurance client.
- 905.3 A4 A self-interest or intimidation threat is also created when the fees generated by the firm from an assurance client represent a large proportion of the revenue from an individual partner's clients.
- 905.3 A5 Examples of actions that might be safeguards to address such a self-interest or intimidation threat include:
- Increasing the client base of the partner to reduce dependence on the assurance client.
 - Having an appropriate reviewer who was not an assurance team member review the work.

Fees—Overdue

- 905.4 A1 A self-interest threat might be created if a significant part of fees is not paid before the assurance report, if any, for the following period is issued. It is generally expected that the firm will require payment of such fees before any such report is issued. The requirements and application material set out in Section 911 with respect to loans and guarantees might also apply to situations where such unpaid fees exist.

905.4 A2 Examples of actions that might be safeguards to address such a self-interest threat include:

- Obtaining partial payment of overdue fees.
- Having an appropriate reviewer who did not take part in the assurance engagement review the work performed.

R905.5 When a significant part of fees due from an assurance client remains unpaid for a long time, the firm shall determine:

- (a) Whether the overdue fees might be equivalent to a loan to the client; and
- (b) Whether it is appropriate for the firm to be re-appointed or continue the assurance engagement.

Contingent Fees

905.6 A1 Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed. A contingent fee charged through an intermediary is an example of an indirect contingent fee. In this section, a fee is not regarded as being contingent if established by a court or other public authority.

R905.7 A firm shall not charge directly or indirectly a contingent fee for an assurance engagement.

R905.8 A firm shall not charge directly or indirectly a contingent fee for a non-assurance service provided to an assurance client if the outcome of the non-assurance service, and therefore, the amount of the fee, is dependent on a future or contemporary judgment related to a matter that is material to the subject matter information of the assurance engagement.

905.9 A1 Paragraphs R905.7 and R905.8 preclude a firm from entering into certain contingent fee arrangements with an assurance client. Even if a contingent fee arrangement is not precluded when providing a non-assurance service to an assurance client, a self-interest threat might still be created.

905.9 A2 Factors that are relevant in evaluating the level of such a threat include:

- The range of possible fee amounts.
- Whether an appropriate authority determines the outcome on which the contingent fee depends.
- Disclosure to intended users of the work performed by the firm and the basis of remuneration.
- The nature of the service.
- The effect of the event or transaction on the subject matter information.

905.9 A3 Examples of actions that might be safeguards to address such a self-interest threat include:

- Having an appropriate reviewer who was not involved in performing the non-assurance service review the relevant assurance work.
- Obtaining an advance written agreement with the client on the basis of remuneration.

SECTION 906

GIFTS AND HOSPITALITY

Introduction

- 906.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 906.2 Accepting gifts and hospitality from an assurance client might create a self-interest, familiarity or intimidation threat. This section sets out a specific requirement and application material relevant to applying the conceptual framework in such circumstances.

Requirement and Application Material

- R906.3** A firm or an assurance team member shall not accept gifts and hospitality from an assurance client, unless the value is trivial and inconsequential.
- 906.3 A1 Where a firm or assurance team member is offering or accepting an inducement to or from an assurance client, the requirements and application material set out in Section 340 apply and non-compliance with these requirements might create threats to independence.
- 906.3 A2 The requirements set out in Section 340 relating to offering or accepting inducements do not allow a firm or assurance team member to accept gifts and hospitality where the intent is to improperly influence behavior even if the value is trivial and inconsequential.

SECTION 907

ACTUAL OR THREATENED LITIGATION

Introduction

- 907.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 907.2 When litigation with an assurance client occurs, or appears likely, self-interest and intimidation threats are created. This section sets out specific application material relevant to applying the conceptual framework in such circumstances.

Application Material

General

- 907.3 A1 The relationship between client management and assurance team members must be characterized by complete candor and full disclosure regarding all aspects of a client's operations. Adversarial positions might result from actual or threatened litigation between an assurance client and the firm or an assurance team member. Such adversarial positions might affect management's willingness to make complete disclosures and create self-interest and intimidation threats.
- 907.3 A2 Factors that are relevant in evaluating the level of such threats include:
- The materiality of the litigation.
 - Whether the litigation relates to a prior assurance engagement.
- 907.3 A3 If the litigation involves an assurance team member, an example of an action that might eliminate such self-interest and intimidation threats is removing that individual from the assurance team.
- 907.3 A4 An example of an action that might be a safeguard to address such self-interest and intimidation threats is having an appropriate reviewer review the work performed.

SECTION 910

FINANCIAL INTERESTS

Introduction

- 910.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 910.2 Holding a financial interest in an assurance client might create a self-interest threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 910.3 A1 A financial interest might be held directly or indirectly through an intermediary such as a collective investment vehicle, an estate or a trust. When a beneficial owner has control over the intermediary or ability to influence its investment decisions, the Code defines that financial interest to be direct. Conversely, when a beneficial owner has no control over the intermediary or ability to influence its investment decisions, the Code defines that financial interest to be indirect.
- 910.3 A2 This section contains references to the “materiality” of a financial interest. In determining whether such an interest is material to an individual, the combined net worth of the individual and the individual’s immediate family members may be taken into account.
- 910.3 A3 Factors that are relevant in evaluating the level of a self-interest threat created by holding a financial interest in an assurance client include:
- The role of the individual holding the financial interest.
 - Whether the financial interest is direct or indirect.
 - The materiality of the financial interest.

Financial Interests Held by the Firm, Assurance Team Members and Immediate Family

- R910.4** A direct financial interest or a material indirect financial interest in the assurance client shall not be held by:
- (a) The firm; or
 - (b) An assurance team member or any of that individual’s immediate family.

Financial Interests in an Entity Controlling an Assurance Client

- R910.5** When an entity has a controlling interest in the assurance client and the client is material to the entity, neither the firm, nor an assurance team member, nor any of that individual’s immediate family shall hold a direct or material indirect financial interest in that entity.

Financial Interests Held as Trustee

R910.6 Paragraph R910.4 shall also apply to a financial interest in an assurance client held in a trust for which the firm or individual acts as trustee unless:

- (a) None of the following is a beneficiary of the trust: the trustee, the assurance team member or any of that individual's immediate family, or the firm;
- (b) The interest in the assurance client held by the trust is not material to the trust;
- (c) The trust is not able to exercise significant influence over the assurance client; and
- (d) None of the following can significantly influence any investment decision involving a financial interest in the assurance client: the trustee, the assurance team member or any of that individual's immediate family, or the firm.

Financial Interests Received Unintentionally

R910.7 If a firm, an assurance team member, or any of that individual's immediate family, receives a direct financial interest or a material indirect financial interest in an assurance client by way of an inheritance, gift, as a result of a merger, or in similar circumstances and the interest would not otherwise be permitted to be held under this section, then:

- (a) If the interest is received by the firm, the financial interest shall be disposed of immediately, or enough of an indirect financial interest shall be disposed of so that the remaining interest is no longer material; or
- (b) If the interest is received by an assurance team member, or by any of that individual's immediate family, the individual who received the financial interest shall immediately dispose of the financial interest, or dispose of enough of an indirect financial interest so that the remaining interest is no longer material.

Financial Interests – Other Circumstances

Close Family

910.8 A1 A self-interest threat might be created if an assurance team member knows that a close family member has a direct financial interest or a material indirect financial interest in the assurance client.

910.8 A2 Factors that are relevant in evaluating the level of such a threat include:

- The nature of the relationship between the assurance team member and the close family member.
- Whether the financial interest is direct or indirect.
- The materiality of the financial interest to the close family member.

910.8 A3 Examples of actions that might eliminate such a self-interest threat include:

- Having the close family member dispose, as soon as practicable, of all of the financial interest or dispose of enough of an indirect financial interest so that the remaining interest is no longer material.

- Removing the individual from the assurance team.

910.8 A4 An example of an action that might be a safeguard to address such a self-interest threat is having an appropriate reviewer review the work of the assurance team member.

Other Individuals

910.8 A5 A self-interest threat might be created if an assurance team member knows that a financial interest is held in the assurance client by individuals such as:

- Partners and professional employees of the firm, apart from those who are specifically not permitted to hold such financial interests by paragraph R910.4, or their immediate family members.
- Individuals with a close personal relationship with an assurance team member.

910.8 A6 An example of an action that might eliminate such a self-interest threat is removing the assurance team member with the personal relationship from the assurance team.

910.8 A7 Examples of actions that might be safeguards to address such a self-interest threat include:

- Excluding the assurance team member from any significant decision-making concerning the assurance engagement.
- Having an appropriate reviewer review the work of the assurance team member.

SECTION 911

LOANS AND GUARANTEES

Introduction

- 911.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 911.2 A loan or a guarantee of a loan with an assurance client might create a self-interest threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 911.3 A1 This section contains references to the “materiality” of a loan or guarantee. In determining whether such a loan or guarantee is material to an individual, the combined net worth of the individual and the individual’s immediate family members may be taken into account.

Loans and Guarantees with an Assurance Client

- R911.4** A firm, an assurance team member, or any of that individual’s immediate family shall not make or guarantee a loan to an assurance client unless the loan or guarantee is immaterial to both:
- (a) The firm or the individual making the loan or guarantee, as applicable; and
 - (b) The client.

Loans and Guarantees with an Assurance Client that is a Bank or Similar Institution

- R911.5** A firm, an assurance team member, or any of that individual’s immediate family shall not accept a loan, or a guarantee of a loan, from an assurance client that is a bank or a similar institution unless the loan or guarantee is made under normal lending procedures, terms and conditions.
- 911.5 A1 Examples of loans include mortgages, bank overdrafts, car loans and credit card balances.
- 911.5 A2 Even if a firm receives a loan from an assurance client that is a bank or similar institution under normal lending procedures, terms and conditions, the loan might create a self-interest threat if it is material to the assurance client or firm receiving the loan.
- 911.5 A3 An example of an action that might be a safeguard to address such a self-interest threat is having the work reviewed by an appropriate reviewer, who is not an assurance team member, from a network firm that is not a beneficiary of the loan.

Deposit or Brokerage Accounts

- R911.6** A firm, an assurance team member, or any of that individual’s immediate family shall not have deposits or a brokerage account with an assurance client that is a bank, broker, or similar institution, unless the deposit or account is held under normal commercial terms.

Loans and Guarantees with an Assurance Client that is not a Bank or Similar Institution

R911.7 A firm or an assurance team member, or any of that individual's immediate family, shall not accept a loan from, or have a borrowing guaranteed by, an assurance client that is not a bank or similar institution, unless the loan or guarantee is immaterial to both:

- (a) The firm, or the individual receiving the loan or guarantee, as applicable; and
- (b) The client.

SECTION 920

BUSINESS RELATIONSHIPS

Introduction

- 920.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 920.2 A close business relationship with an assurance client or its management might create a self-interest or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 920.3 A1 This section contains references to the “materiality” of a financial interest and the “significance” of a business relationship. In determining whether such a financial interest is material to an individual, the combined net worth of the individual and the individual’s immediate family members may be taken into account.
- 920.3 A2 Examples of a close business relationship arising from a commercial relationship or common financial interest include:
- Having a financial interest in a joint venture with either the assurance client or a controlling owner, director or officer or other individual who performs senior managerial activities for that client.
 - Arrangements to combine one or more services or products of the firm with one or more services or products of the client and to market the package with reference to both parties.
 - Distribution or marketing arrangements under which the firm distributes or markets the client’s products or services, or the client distributes or markets the firm’s products or services.

Firm, Assurance Team Member or Immediate Family Business Relationships

- R920.4** A firm or an assurance team member shall not have a close business relationship with an assurance client or its management unless any financial interest is immaterial and the business relationship is insignificant to the client or its management and the firm or the assurance team member, as applicable.
- 920.4 A1 A self-interest or intimidation threat might be created if there is a close business relationship between the assurance client or its management and the immediate family of an assurance team member.

Buying Goods or Services

- 920.5 A1 The purchase of goods and services from an assurance client by a firm, or an assurance team member, or any of that individual’s immediate family does not usually create a threat to independence if the transaction is in the normal course of business and at arm’s length. However, such transactions might be of such a nature and magnitude that they create a self-interest threat.

920.5 A2 Examples of actions that might eliminate such a self-interest threat include:

- Eliminating or reducing the magnitude of the transaction.
- Removing the individual from the assurance team.

SECTION 921

FAMILY AND PERSONAL RELATIONSHIPS

Introduction

- 921.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 921.2 Family or personal relationships with client personnel might create a self-interest, familiarity or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 921.3 A1 A self-interest, familiarity or intimidation threat might be created by family and personal relationships between an assurance team member and a director or officer or, depending on their role, certain employees of the assurance client.
- 921.3 A2 Factors that are relevant in evaluating the level of such threats include:
- The individual's responsibilities on the assurance team.
 - The role of the family member or other individual within the assurance client, and the closeness of the relationship.

Immediate Family of an Assurance Team Member

- 921.4 A1 A self-interest, familiarity or intimidation threat is created when an immediate family member of an assurance team member is an employee in a position to exert significant influence over the underlying subject matter of the assurance engagement.
- 921.4 A2 Factors that are relevant in evaluating the level of such threats include:
- The position held by the immediate family member.
 - The role of the assurance team member.
- 921.4 A3 An example of an action that might eliminate such a self-interest, familiarity or intimidation threat is removing the individual from the assurance team.
- 921.4 A4 An example of an action that might be a safeguard to address such a self-interest, familiarity or intimidation threat is structuring the responsibilities of the assurance team so that the assurance team member does not deal with matters that are within the responsibility of the immediate family member.
- R921.5** An individual shall not participate as an assurance team member when any of that individual's immediate family:
- (a)** Is a director or officer of the assurance client;

- (b) In an attestation engagement, is an employee in a position to exert significant influence over the subject matter information of the assurance engagement; or
- (c) Was in such a position during any period covered by the engagement or the subject matter information.

Close Family of an Assurance Team Member

921.6 A1 A self-interest, familiarity or intimidation threat is created when a close family member of an assurance team member is:

- (a) A director or officer of the assurance client; or
- (b) An employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, a An employee in a position to exert significant influence over the subject matter information of the assurance engagement.

921.6 A2 Factors that are relevant in evaluating the level of such threats include:

- The nature of the relationship between the assurance team member and the close family member.
- The position held by the close family member.
- The role of the assurance team member.

921.6 A3 An example of an action that might eliminate such a self-interest, familiarity or intimidation threat is removing the individual from the assurance team.

921.6 A4 An example of an action that might be a safeguard to address such a self-interest, familiarity or intimidation threat is structuring the responsibilities of the assurance team so that the assurance team member does not deal with matters that are within the responsibility of the close family member.

Other Close Relationships of an Assurance Team Member

R921.7 An assurance team member shall consult in accordance with firm policies and procedures if the assurance team member has a close relationship with an individual who is not an immediate or close family member, but who is:

- (a) A director or officer of the assurance client; or
- (b) An employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, a An employee in a position to exert significant influence over the subject matter information of the assurance engagement.

921.7 A1 Factors that are relevant in evaluating the level of a self-interest, familiarity or intimidation threat created by such relationships include:

- The nature of the relationship between the individual and the assurance team member.
- The position the individual holds with the client.
- The role of the assurance team member.

921.7 A2 An example of an action that might eliminate such a self-interest, familiarity or intimidation threat is removing the individual from the assurance team.

921.7 A3 An example of an action that might be a safeguard to address such a self-interest, familiarity or intimidation threat is structuring the responsibilities of the assurance team so that the assurance team member does not deal with matters that are within the responsibility of the individual with whom the assurance team member has a close relationship.

Relationships of Partners and Employees of the Firm

921.8 A1 A self-interest, familiarity or intimidation threat might be created by a personal or family relationship between:

(a) A partner or employee of the firm who is not an assurance team member; and

(b) Any of the following individuals at the assurance client:

i. A director or officer;

ii. An employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, of the assurance client or an employee in a position to exert significant influence over the subject matter information of the assurance engagement.

921.8 A2 Factors that are relevant in evaluating the level of such threats include:

- The nature of the relationship between the partner or employee of the firm and the director or officer or employee of the client.
- The degree of interaction of the partner or employee of the firm with the assurance team.
- The position of the partner or employee within the firm.
- The role of the individual within the client.

921.8 A3 Examples of actions that might be safeguards to address such self-interest, familiarity or intimidation threats include:

- Structuring the partner's or employee's responsibilities to reduce any potential influence over the assurance engagement.
- Having an appropriate reviewer review the relevant assurance work performed.

SECTION 922

RECENT SERVICE WITH AN ASSURANCE CLIENT

Introduction

- 922.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 922.2 If an assurance team member has recently served as a director or officer or employee of the assurance client, a self-interest, self-review or familiarity threat might be created. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

Service During the Period Covered by the Assurance Report

- R922.3** The assurance team shall not include an individual who, during the period covered by the assurance report:
- (a) Had served as a director or officer of the assurance client; or
 - (b) Was an employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, an employee in a position to exert significant influence over the subject matter information of the assurance engagement.

Service Prior to the Period Covered by the Assurance Report

- 922.4 A1 A self-interest, self-review or familiarity threat might be created if, before the period covered by the assurance report, an assurance team member:
- (a) Had served as a director or officer of the assurance client; or
 - (b) Was an employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, an employee in a position to exert significant influence over the subject matter information of the assurance engagement.

For example, a threat would be created if a decision made or work performed by the individual in the prior period, while employed by the client, is to be evaluated in the current period as part of the current assurance engagement.

- 922.4 A2 Factors that are relevant in evaluating the level of such threats include:

- The position the individual held with the client.
- The length of time since the individual left the client.
- The role of the assurance team member.

- 922.4 A3 An example of an action that might be a safeguard to address such a self-interest, self-review or familiarity threat is having an appropriate reviewer review the work performed by the assurance team member.

SECTION 923

SERVING AS A DIRECTOR OR OFFICER OF AN ASSURANCE CLIENT

Introduction

- 923.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 923.2 Serving as a director or officer of an assurance client creates self-review and self-interest threats. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

Service as Director or Officer

- R923.3** A partner or employee of the firm shall not serve as a director or officer of an assurance client of the firm.

Service as Company Secretary

- R923.4** A partner or employee of the firm shall not serve as Company Secretary for an assurance client of the firm unless:
- (a) This practice is specifically permitted under local law, professional rules or practice;
 - (b) Management makes all decisions; and
 - (c) The duties and activities performed are limited to those of a routine and administrative nature, such as preparing minutes and maintaining statutory returns.
- 923.4 A1 The position of Company Secretary has different implications in different jurisdictions. Duties might range from: administrative duties (such as personnel management and the maintenance of company records and registers) to duties as diverse as ensuring that the company complies with regulations or providing advice on corporate governance matters. Usually this position is seen to imply a close association with the entity. Therefore, a threat is created if a partner or employee of the firm serves as Company Secretary for an assurance client. (More information on providing non-assurance services to an assurance client is set out in Section 950, *Provision of Non-assurance Services to an Assurance Client.*)

SECTION 924

EMPLOYMENT WITH AN ASSURANCE CLIENT

Introduction

- 924.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 924.2 Employment relationships with an assurance client might create a self-interest, familiarity or intimidation threat. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 924.3 A1 A familiarity or intimidation threat might be created if any of the following individuals have been an assurance team member or partner of the firm:
- A director or officer of the assurance client.
 - An employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, An-an employee who is in a position to exert significant influence over the subject matter information of the assurance engagement.

Former Partner or Assurance Team Member Restrictions

- R924.4** If a former partner has joined an assurance client of the firm or a former assurance team member has joined the assurance client as:

- (a) A director or officer; or
- (b) An employee in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, An-an employee in a position to exert significant influence over the subject matter information of the assurance engagement,

the individual shall not continue to participate in the firm's business or professional activities.

- 924.4 A1 Even if one of the individuals described in paragraph R924.4 has joined the assurance client in such a position and does not continue to participate in the firm's business or professional activities, a familiarity or intimidation threat might still be created.

- 924.4 A2 A familiarity or intimidation threat might also be created if a former partner of the firm has joined an entity in one of the positions described in paragraph 924.3 A1 and the entity subsequently becomes an assurance client of the firm.

- 924.4 A3 Factors that are relevant in evaluating the level of such threats include:

- The position the individual has taken at the client.
- Any involvement the individual will have with the assurance team.

- The length of time since the individual was an assurance team member or partner of the firm.
- The former position of the individual within the assurance team or firm. An example is whether the individual was responsible for maintaining regular contact with the client's management or those charged with governance.

924.4 A4 Examples of actions that might be safeguards to address such a familiarity or intimidation threat include:

- Making arrangements such that the individual is not entitled to any benefits or payments from the firm, unless made in accordance with fixed pre-determined arrangements.
- Making arrangements such that any amount owed to the individual is not material to the firm.
- Modifying the plan for the assurance engagement.
- Assigning to the assurance team individuals who have sufficient experience relative to the individual who has joined the client.
- Having an appropriate reviewer review the work of the former assurance team member.

Assurance Team Members Entering Employment Negotiations with a Client

R924.5 A firm shall have policies and procedures that require assurance team members to notify the firm when entering employment negotiations with an assurance client.

924.5 A1 A self-interest threat is created when an assurance team member participates in the assurance engagement while knowing that the assurance team member will, or might, join the client sometime in the future.

924.5 A2 An example of an action that might eliminate such a self-interest threat is removing the individual from the assurance engagement.

924.5 A3 An example of an action that might be a safeguard to address such a self-interest threat is having an appropriate reviewer review any significant judgments made by that assurance team member while on the team.

SECTION 940

LONG ASSOCIATION OF PERSONNEL WITH AN ASSURANCE CLIENT

Introduction

- 940.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 940.2 When an individual is involved in an assurance engagement of a recurring nature over a long period of time, familiarity and self-interest threats might be created. This section sets out requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- 940.3 A1 A familiarity threat might be created as a result of an individual's long association with:
- (a) The assurance client;
 - (b) The assurance client's senior management; or
 - (c) The underlying subject matter or, in an attestation engagement, and-subject matter information of the assurance engagement.
- 940.3 A2 A self-interest threat might be created as a result of an individual's concern about losing a longstanding assurance client or an interest in maintaining a close personal relationship with a member of senior management or those charged with governance. Such a threat might influence the individual's judgment inappropriately.
- 940.3 A3 Factors that are relevant to evaluating the level of such familiarity or self-interest threats include:
- The nature of the assurance engagement.
 - How long the individual has been an assurance team member, the individual's seniority on the team, and the nature of the roles performed, including if such a relationship existed while the individual was at a prior firm.
 - The extent to which the work of the individual is directed, reviewed and supervised by more senior personnel.
 - The extent to which the individual, due to the individual's seniority, has the ability to influence the outcome of the assurance engagement, for example, by making key decisions or directing the work of other engagement team members.
 - The closeness of the individual's personal relationship with the assurance client or, if relevant, senior management.
 - The nature, frequency and extent of interaction between the individual and the assurance client.

- Whether the nature or complexity of the underlying subject matter or subject matter information has changed.
- Whether there have been any recent changes in the individual or individuals at the assurance client who are responsible for the underlying subject matter or, in an attestation engagement, the subject matter information ~~who are the responsible party~~ or, if relevant, senior management.

940.3 A4 The combination of two or more factors might increase or reduce the level of the threats. For example, familiarity threats created over time by the increasingly close relationship between an assurance team member individual and an individual at the assurance client who is in a position to exert significant influence over the underlying subject matter or, in an attestation engagement, the subject matter information, would be reduced by the departure of ~~the that individual from the client who is the responsible party~~.

940.3 A5 An example of an action that might eliminate the familiarity and self-interest threats in relation to a specific engagement would be rotating the individual off the assurance team.

940.3 A6 Examples of actions that might be safeguards to address such familiarity or self-interest threats include:

- Changing the role of the individual on the assurance team or the nature and extent of the tasks the individual performs.
- Having an appropriate reviewer who was not an assurance team member review the work of the individual.
- Performing regular independent internal or external quality reviews of the engagement.

R940.4 If a firm decides that the level of the threats created can only be addressed by rotating the individual off the assurance team, the firm shall determine an appropriate period during which the individual shall not:

- (a) Be a member of the engagement team for the assurance engagement;
- (b) Provide quality control for the assurance engagement; or
- (c) Exert direct influence on the outcome of the assurance engagement.

The period shall be of sufficient duration to allow the familiarity and self-interest threats to be addressed.

SECTION 950

PROVISION OF NON-ASSURANCE SERVICES TO ASSURANCE CLIENTS ~~OTHER THAN AUDIT AND REVIEW ENGAGEMENT CLIENTS~~

Introduction

- 950.1 Firms are required to comply with the fundamental principles, be independent, and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 950.2 Firms might provide a range of non-assurance services to their assurance clients, consistent with their skills and expertise. Providing certain non-assurance services to assurance clients might create threats to compliance with the fundamental principles and threats to independence. This section sets out specific requirements and application material relevant to applying the conceptual framework in such circumstances.

Requirements and Application Material

General

- R950.3** Before a firm accepts an engagement to provide a non-assurance service to an assurance client, the firm shall determine whether providing such a service might create a threat to independence.
- 950.3 A1 The requirements and application material in this section assist firms in analyzing certain types of non-assurance services and the related threats that might be created when a firm accepts or provides non-assurance services to an assurance client.
- 950.3 A2 New business practices, the evolution of financial markets and changes in information technology are among the developments that make it impossible to draw up an all-inclusive list of non-assurance services that might be provided to an assurance client. As a result, the Code does not include an exhaustive listing of all non-assurance services that might be provided to an assurance client.

Evaluating Threats

- 950.4 A1 Factors that are relevant in evaluating the level of threats created by providing a non-assurance service to an assurance client include:
- The nature, scope and purpose of the service.
 - The degree of reliance that will be placed on the outcome of the service as part of the assurance engagement.
 - The legal and regulatory environment in which the service is provided.
 - Whether the outcome of the service will affect the underlying subject matter and, in an attestation engagement, matters reflected in the subject matter or subject matter information of the assurance engagement, and, if so:
 - The extent to which the outcome of the service will have a material or significant effect on the underlying subject matter and, in an attestation engagement, the subject matter information of the assurance engagement.

- The extent of the assurance client's involvement in determining significant matters of judgment.
- The level of expertise of the client's management and employees with respect to the type of service provided.

Materiality in Relation to an Assurance Client's Information

950.4 A2 The concept of materiality in relation to an assurance client's subject matter information is addressed in *Hong Kong Standard on Assurance Engagements (HKSAE) 3000 (Revised), Assurance Engagements other than Audits or Reviews of Historical Financial Information*. The determination of materiality involves the exercise of professional judgment and is impacted by both quantitative and qualitative factors. It is also affected by perceptions of the financial or other information needs of users.

Multiple Non-assurance Services Provided to the Same Assurance Client

950.4 A3 A firm might provide multiple non-assurance services to an assurance client. In these circumstances the combined effect of threats created by providing those services is relevant to the firm's evaluation of threats.

Addressing Threats

950.5 A1 Paragraph 120.10 A2 includes a description of safeguards. In relation to providing non-assurance services to assurance clients, safeguards are actions, individually or in combination, that the firm takes that effectively reduce threats to independence to an acceptable level. In some situations, when a threat is created by providing a service to an assurance client, safeguards might not be available. In such situations, the application of the conceptual framework set out in Section 120 requires the firm to decline or end the non-assurance service or the assurance engagement.

Prohibition on Assuming Management Responsibilities

R950.6 A firm shall not assume a management responsibility related to the underlying subject matter and, in an attestation engagement, the ~~or~~ subject matter information of an assurance engagement provided by the firm. If the firm assumes a management responsibility as part of any other service provided to the assurance client, the firm shall ensure that the responsibility is not related to the underlying subject matter and, in an attestation engagement, the ~~or~~ subject matter information of the assurance engagement provided by the firm.

950.6 A1 Management responsibilities involve controlling, leading and directing an entity, including making decisions regarding the acquisition, deployment and control of human, financial, technological, physical and intangible resources.

950.6 A2 Providing a non-assurance service to an assurance client creates self-review and self-interest threats if the firm assumes a management responsibility when performing the service. In relation to providing a service related to the underlying subject matter and, in an attestation engagement, the ~~or~~ subject matter information of an assurance engagement provided by the firm, assuming a management responsibility also creates a familiarity threat and might create an advocacy threat because the firm becomes too closely aligned with the views and interests of management.

950.6 A3 Determining whether an activity is a management responsibility depends on the circumstances and requires the exercise of professional judgment. Examples of activities that would be considered a management responsibility include:

- Setting policies and strategic direction.
- Hiring or dismissing employees.
- Directing and taking responsibility for the actions of employees in relation to the employees' work for the entity.
- Authorizing transactions.
- Controlling or managing bank accounts or investments.
- Deciding which recommendations of the firm or other third parties to implement.
- Reporting to those charged with governance on behalf of management.
- Taking responsibility for designing, implementing, monitoring and maintaining internal control.

950.6 A4 Providing advice and recommendations to assist the management of an assurance client in discharging its responsibilities is not assuming a management responsibility. (Ref: Paras. R950.6 to 950.6 A3).

R950.7 To avoid assuming a management responsibility when providing non-assurance services to an assurance client that are related to the underlying subject matter and, in an attestation engagement, the ~~or~~ subject matter information of the assurance engagement, the firm shall be satisfied that client management makes all related judgments and decisions that are the proper responsibility of management. This includes ensuring that the client's management:

- (a) Designates an individual who possesses suitable skill, knowledge and experience to be responsible at all times for the client's decisions and to oversee the services. Such an individual, preferably within senior management, would understand:
 - (i) The objectives, nature and results of the services; and
 - (ii) The respective client and firm responsibilities.

However, the individual is not required to possess the expertise to perform or re-perform the services.

- (b) Provides oversight of the services and evaluates the adequacy of the results of the service performed for the client's purpose; and
- (c) Accepts responsibility for the actions, if any, to be taken arising from the results of the services.

Other Considerations Related to Providing Specific Non-Assurance Services

- 950.8 A1 A self-review threat might be created if, in an attestation engagement, the firm is involved in the preparation of subject matter information which ~~is~~ subsequently becomes the subject matter information of an assurance engagement. Examples of non-assurance services that might create such self-review threats when providing services related to the subject matter information of an assurance engagement include:
- (a) Developing and preparing prospective information and subsequently issuing an assurance report ~~providing assurance~~ on this information.

 - (b) Performing a valuation that is related to or forms part of the subject matter information of an assurance engagement.

SECTION 990**REPORTS THAT INCLUDE A RESTRICTION ON USE AND DISTRIBUTION (ASSURANCE ENGAGEMENTS OTHER THAN AUDIT AND REVIEW ENGAGEMENTS)****Introduction**

- 990.1 Firms are required to comply with the fundamental principles, be independent and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats to independence.
- 990.2 This section sets out certain modifications to Part 4B which are permitted in certain circumstances involving assurance engagements where the report includes a restriction on use and distribution. In this section, an engagement to issue a restricted use and distribution assurance report in the circumstances set out in paragraph R990.3 is referred to as an “eligible assurance engagement.”

Requirements and Application Material**General**

- R990.3** When a firm intends to issue a report on an assurance engagement which includes a restriction on use and distribution, the independence requirements set out in Part 4B shall be eligible for the modifications that are permitted by this section, but only if:
- (a) The firm communicates with the intended users of the report regarding the modified independence requirements that are to be applied in providing the service; and
 - (b) The intended users of the report understand the purpose, subject matter information and limitations of the report and explicitly agree to the application of the modifications.
- 990.3 A1 The intended users of the report might obtain an understanding of the purpose, subject matter information, and limitations of the report by participating, either directly, or indirectly through a representative who has authority to act for the intended users, in establishing the nature and scope of the engagement. In either case, this participation helps the firm to communicate with intended users about independence matters, including the circumstances that are relevant to applying the conceptual framework. It also allows the firm to obtain the agreement of the intended users to the modified independence requirements.
- R990.4** Where the intended users are a class of users who are not specifically identifiable by name at the time the engagement terms are established, the firm shall subsequently make such users aware of the modified independence requirements agreed to by their representative.
- 990.4 A1 For example, where the intended users are a class of users such as lenders in a syndicated loan arrangement, the firm might describe the modified independence requirements in an engagement letter to the representative of the lenders. The representative might then make the firm’s engagement letter available to the members of the group of lenders to meet the requirement for the firm to make such users aware of the modified independence requirements agreed to by the representative.

R990.5 When the firm performs an eligible assurance engagement, any modifications to Part 4B shall be limited to those modifications set out in paragraphs R990.7 and R990.8.

R990.6 If the firm also issues an assurance report that does not include a restriction on use and distribution for the same client, the firm shall apply Part 4B to that assurance engagement.

Financial Interests, Loans and Guarantees, Close Business, Family and Personal Relationships

R990.7 When the firm performs an eligible assurance engagement:

- (a) The relevant provisions set out in Sections 910, 911, 920, 921, 922 and 924 need apply only to the members of the engagement team, and their immediate and close family members;
- (b) The firm shall identify, evaluate and address any threats to independence created by interests and relationships, as set out in Sections 910, 911, 920, 921, 922 and 924, between the assurance client and the following assurance team members:
 - (i) Those who provide consultation regarding technical or industry specific issues, transactions or events; and
 - (ii) Those who provide quality control for the engagement, including those who perform the engagement quality control review; and
- (c) The firm shall evaluate and address any threats that the engagement team has reason to believe are created by interests and relationships between the assurance client and others within the firm who can directly influence the outcome of the assurance engagement, as set out in Sections 910, 911, 920, 921, 922 and 924.

990.7 A1 Others within the firm who can directly influence the outcome of the assurance engagement include those who recommend the compensation, or who provide direct supervisory, management or other oversight, of the assurance engagement partner in connection with the performance of the assurance engagement.

R990.8 When the firm performs an eligible assurance engagement, the firm shall not hold a material direct or a material indirect financial interest in the assurance client.

GLOSSARY, INCLUDING LISTS OF ABBREVIATIONS

In the *Code of Ethics for Professional Accountants*, the singular shall be construed as including the plural as well as the reverse, and the terms below have the following meanings assigned to them.

In this Glossary, explanations of defined terms are shown in regular font; italics are used for explanations of described terms which have a specific meaning in certain parts of the Code or for additional explanations of defined terms. References are also provided to terms described in the Code.

Acceptable level A level at which a professional accountant using the reasonable and informed third party test would likely conclude that the accountant complies with the fundamental principles.

Advertising The communication to the public of information as to the services or skills provided by professional accountants in public practice with a view to procuring professional business.

Appropriate reviewer *An appropriate reviewer is a professional with the necessary knowledge, skills, experience and authority to review, in an objective manner, the relevant work performed or service provided. Such an individual might be a professional accountant.*

This term is described in paragraph 300.8 A4.

Assurance client The responsible party and also, in an attestation engagement, the party taking responsibility for the subject matter information (who might be the same as the responsible party). ~~The responsible party that is the person (or persons) who:~~

~~(a) In a direct reporting engagement, is responsible for the subject matter; or~~

~~(b) In an assertion-based engagement, is responsible for the subject matter information and might be responsible for the subject matter.~~

Assurance engagement An engagement in which a professional accountant in public practice aims to obtain sufficient appropriate evidence in order to expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the subject matter information ~~outcome of the evaluation or measurement of a subject matter against criteria.~~

~~(HKSAE 3000 (Revised) For guidance on assurance engagements, see the *Hong Kong Framework for Assurance Engagements* issued by the Institute. The *Hong Kong Framework for Assurance Engagements* describes the elements and objectives of an assurance engagement conducted under that Standard and the Assurance Framework provides a general description of assurance engagements and identifies engagements to which *Hong Kong Standards on Auditing* (HKSAAs), *Hong Kong Standards on Review Engagements* (HKSREs) and *Hong Kong Standards on Assurance Engagements* (HKSAEs) apply.)~~

In Part 4B, the term 'assurance engagement' addresses assurance

engagements other than audit engagements or review engagements.

- Assurance team
- (a) All members of the engagement team for the assurance engagement;
 - (b) All others within a firm who can directly influence the outcome of the assurance engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the assurance engagement partner in connection with the performance of the assurance engagement;
 - (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the assurance engagement; and
 - (iii) Those who provide quality control for the assurance engagement, including those who perform the engagement quality control review for the assurance engagement.

Attestation engagement An assurance engagement in which a party other than the professional accountant in public practice measures or evaluates the underlying subject matter against the criteria.

A party other than the accountant also often presents the resulting subject matter information in a report or statement. In some cases, however, the subject matter information may be presented by the accountant in the assurance report. In an attestation engagement, the accountant's conclusion addresses whether the subject matter information is free from material misstatement.

The accountant's conclusion may be phrased in terms of:

- (i) The underlying subject matter and the applicable criteria;
- (ii) The subject matter information and the applicable criteria; or
- (iii) A statement made by the appropriate party.

Audit *In Part 4A, the term "audit" applies equally to "review."*

Audit client An entity in respect of which a firm conducts an audit engagement. When the client is a listed entity, audit client will always include its related entities. When the audit client is not a listed entity, audit client includes those related entities over which the client has direct or indirect control. (See also paragraph R400.20.)

In Part 4A, the term "audit client" applies equally to "review client."

Audit engagement A reasonable assurance engagement in which a professional accountant in public practice expresses an opinion whether financial statements are prepared, in all material respects (or give a true and fair view or are presented fairly, in all material respects), in accordance with an applicable financial reporting framework, such as an

engagement conducted in accordance with *Hong Kong Standards on Auditing*. This includes a Statutory Audit, which is an audit required by legislation or other regulation.

In Part 4A, the term “audit engagement” applies equally to “review engagement.”

- Audit report *In Part 4A, the term “audit report” applies equally to “review report.”*
- Audit team
- (a) All members of the engagement team for the audit engagement;
 - (b) All others within a firm who can directly influence the outcome of the audit engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the audit engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm’s Senior or Managing Partner (Chief Executive or equivalent);
 - (ii) Those who provide consultation regarding technical or industry-specific issues, transactions or events for the engagement; and
 - (iii) Those who provide quality control for the engagement, including those who perform the engagement quality control review for the engagement; and
 - (c) All those within a network firm who can directly influence the outcome of the audit engagement.

In Part 4A, the term “audit team” applies equally to “review team.”

Close family A parent, child or sibling who is not an immediate family member.

Conceptual framework *This term is described in Section 120.*

Contingent fee A fee calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed by the firm. A fee that is established by a court or other public authority is not a contingent fee.

Cooling-off period *This term is described in paragraph R540.5 for the purposes of paragraphs R540.11 to R540.19.*

Criteria In an assurance engagement, the benchmarks used to measure or evaluate the underlying subject matter. The “applicable criteria” are the criteria used for the particular engagement.

Direct engagement An assurance engagement in which the professional accountant in public practice measures or evaluates the underlying subject

matter against the applicable criteria and the accountant presents the resulting subject matter information as part of, or accompanying, the assurance report. In a direct engagement, the accountant's conclusion addresses the reported outcome of the measurement or evaluation of the underlying subject matter against the criteria.

Direct financial interest	<p>A financial interest:</p> <p>(a) Owned directly by and under the control of an individual or entity (including those managed on a discretionary basis by others); or</p> <p>(b) Beneficially owned through a collective investment vehicle, estate, trust or other intermediary over which the individual or entity has control, or the ability to influence investment decisions.</p>
Director or officer	Those charged with the governance of an entity, or acting in an equivalent capacity, regardless of their title, which might vary from jurisdiction to jurisdiction.
Eligible audit engagement	<i>This term is described in paragraph 800.2 for the purposes of Section 800.</i>
Eligible assurance engagement	<i>This term is described in paragraph 990.2 for the purposes of Section 990.</i>
Engagement partner	The partner or other person in the firm who is responsible for the engagement and its performance, and for the report that is issued on behalf of the firm, and who, where required, has the appropriate authority from a professional, legal or regulatory body.
Engagement period (Audit and Review Engagements)	The engagement period starts when the audit team begins to perform the audit. The engagement period ends when the audit report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has ended or the issuance of the final audit report.
Engagement period (Assurance Engagements Other than Audit and Review Engagements)	The engagement period starts when the assurance team begins to perform assurance services with respect to the particular engagement. The engagement period ends when the assurance report is issued. When the engagement is of a recurring nature, it ends at the later of the notification by either party that the professional relationship has ended or the issuance of the final assurance report.
Engagement quality control review	A process designed to provide an objective evaluation, on or before the report is issued, of the significant judgments the engagement team made and the conclusions it reached in formulating the report.
Engagement team	All partners and staff performing the engagement, and any individuals engaged by the firm or a network firm who perform assurance procedures on the engagement. This excludes external experts

engaged by the firm or by a network firm.

The term “engagement team” also excludes individuals within the client’s internal audit function who provide direct assistance on an audit engagement when the external auditor complies with the requirements of HKSA 610 (Revised 2013), *Using the Work of Internal Auditors*.

Existing accountant A professional accountant in public practice currently holding an audit appointment or carrying out accounting, tax, consulting or similar professional services for a client.

External expert An individual (who is not a partner or a member of the professional staff, including temporary staff, of the firm or a network firm) or organization possessing skills, knowledge and experience in a field other than accounting or auditing, whose work in that field is used to assist the professional accountant in obtaining sufficient appropriate evidence.

Financial interest An interest in an equity or other security, debenture, loan or other debt instrument of an entity, including rights and obligations to acquire such an interest and derivatives directly related to such interest.

Financial statements A structured representation of historical financial information, including related notes, intended to communicate an entity’s economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework. The related notes ordinarily comprise a summary of significant accounting policies and other explanatory information. The term can relate to a complete set of financial statements, but it can also refer to a single financial statement, for example, a balance sheet, or a statement of revenues and expenses, and related explanatory notes.

The term does not refer to specific elements, accounts or items of a financial statement.

Financial statements on which the firm will express an opinion In the case of a single entity, the financial statements of that entity. In the case of consolidated financial statements, also referred to as group financial statements, the consolidated financial statements.

Firm

- (a) A sole practitioner, partnership or corporation of professional accountants;
- (b) An entity that controls such parties, through ownership, management or other means; and
- (c) An entity controlled by such parties, through ownership, management or other means.

Paragraphs 400.4 and 900.3 explain how the word “firm” is used to address the responsibility of professional accountants and firms for compliance with Parts 4A and 4B, respectively.

Fundamental principles *This term is described in paragraph 110.1 A1. Each of the fundamental principles is, in turn, described in the following paragraphs:*

<i>Integrity</i>	<i>R111.1</i>
<i>Objectivity</i>	<i>R112.1</i>
<i>Professional competence and due care</i>	<i>R113.1</i>
<i>Confidentiality</i>	<i>R114.1</i>
<i>Professional behavior</i>	<i>R115.1</i>

Historical financial information Information expressed in financial terms in relation to a particular entity, derived primarily from that entity's accounting system, about economic events occurring in past time periods or about economic conditions or circumstances at points in time in the past.

Immediate family A spouse (or equivalent) or dependent.

Independence Independence comprises:

(a) Independence of mind – the state of mind that permits the expression of a conclusion without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity, and exercise objectivity and professional skepticism.

(b) Independence in appearance – the avoidance of facts and circumstances that are so significant that a reasonable and informed third party would be likely to conclude that a firm's, or an audit or assurance team member's, integrity, objectivity or professional skepticism has been compromised.

As set out in paragraphs 400.5 and 900.4, references to an individual or firm being "independent" mean that the individual or firm has complied with Parts 4A and 4B, as applicable.

Indirect financial interest A financial interest beneficially owned through a collective investment vehicle, estate, trust or other intermediary over which the individual or entity has no control or ability to influence investment decisions.

Inducement An object, situation, or action that is used as a means to influence another individual's behavior, but not necessarily with the intent to improperly influence that individual's behavior.

Inducements can range from minor acts of hospitality between business colleagues (for professional accountants in business), or between professional accountants and existing or prospective clients (for professional accountants in public practice), to acts that result in non-compliance with laws and regulations. An inducement can take many different forms, for example:

- *Gifts.*
- *Hospitality.*

- *Entertainment.*
- *Political or charitable donations.*
- *Appeals to friendship and loyalty.*
- *Employment or other commercial opportunities.*
- *Preferential treatment, rights or privileges.*

Key audit partner	The engagement partner, the individual responsible for the engagement quality control review, and other audit partners, if any, on the engagement team who make key decisions or judgments on significant matters with respect to the audit of the financial statements on which the firm will express an opinion. Depending upon the circumstances and the role of the individuals on the audit, “other audit partners” might include, for example, audit partners responsible for significant subsidiaries or divisions.
Listed entity	An entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.
May	<i>This term is used in the Code to denote permission to take a particular action in certain circumstances, including as an exception to a requirement. It is not used to denote possibility.</i>
Might	<i>This term is used in the Code to denote the possibility of a matter arising, an event occurring or a course of action being taken. The term does not ascribe any particular level of possibility or likelihood when used in conjunction with a threat, as the evaluation of the level of a threat depends on the facts and circumstances of any particular matter, event or course of action.</i>
Network	A larger structure: <ul style="list-style-type: none"> (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.
Network firm	A firm or entity that belongs to a network. <i>For further information, see paragraphs 400.50 A1 to 400.54 A1.</i>
Non-compliance with laws and regulations (Professional Accountants in Business)	<i>Non-compliance with laws and regulations (“non-compliance”) comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:</i> <ul style="list-style-type: none"> (a) <i>The professional accountant’s employing organization;</i>

- (b) *Those charged with governance of the employing organization;*
- (c) *Management of the employing organization; or*
- (d) *Other individuals working for or under the direction of the employing organization.*

This term is described in paragraph 260.5 A1.

Non-compliance with laws and regulations
(Professional Accountants in Public Practice)

Non-compliance with laws and regulations (“non-compliance”) comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:

- (a) *A client;*
- (b) *Those charged with governance of a client;*
- (c) *Management of a client; or*
- (d) *Other individuals working for or under the direction of a client.*

This term is described in paragraph 360.5 A1.

Office

A distinct sub-group, whether organized on geographical or practice lines.

Predecessor accountant

A professional accountant in public practice who most recently held an audit appointment or carried out accounting, tax, consulting or similar professional services for a client, where there is no existing accountant.

Professional accountant

An individual who is a member of an IFAC member body.

In Part 1, the term “professional accountant” refers to individual professional accountants in business and to professional accountants in public practice and their firms.

In Part 2, the term “professional accountant” refers to professional accountants in business.

In Parts 3, 4A and 4B, the term “professional accountant” refers to professional accountants in public practice and their firms.

Professional accountant in business

A professional accountant working in areas such as commerce, industry, service, the public sector, education, the not-for-profit sector, or in regulatory or professional bodies, who might be an employee, contractor, partner, director (executive or non-executive), owner-manager or volunteer.

Professional accountant in public practice

A professional accountant, irrespective of functional classification (for example, audit, tax or consulting) in a firm that provides professional services.

The term “professional accountant in public practice” is also used to refer to a firm of professional accountants in public practice.

Professional activity	An activity requiring accountancy or related skills undertaken by a professional accountant, including accounting, auditing, tax, management consulting, and financial management.
Professional services	Professional activities performed for clients.
Proposed accountant	A professional accountant in public practice who is considering accepting an audit appointment or an engagement to perform accounting, tax, consulting or similar professional services for a prospective client (or in some cases, an existing client).
Public interest entity	<p>(a) A listed entity; or</p> <p>(b) An entity:</p> <p style="padding-left: 20px;">(i) Defined by regulation or legislation as a public interest entity; or</p> <p style="padding-left: 20px;">(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^{1c}. Such regulation might be promulgated by any relevant regulator, including an audit regulator.</p>

Other entities might also be considered to be public interest entities, as set out in paragraph 400.8.

Reasonable and informed third party	<p><i>The reasonable and informed third party test is a consideration by the professional accountant about whether the same conclusions would likely be reached by another party. Such consideration is made from the perspective of a reasonable and informed third party, who weighs all the relevant facts and circumstances that the accountant knows, or could reasonably be expected to know, at the time that the conclusions are made. The reasonable and informed third party does not need to be an accountant, but would possess the relevant knowledge and experience to understand and evaluate the appropriateness of the accountant’s conclusions in an impartial manner.</i></p>
Reasonable and informed third party test	

These terms are described in paragraph R120.5 A4.

Related entity	<p>An entity that has any of the following relationships with the client:</p> <p>(a) An entity that has direct or indirect control over the client if the client is material to such entity;</p> <p>(b) An entity with a direct financial interest in the client if that entity has significant influence over the client and the interest</p>
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^{1c} Currently under the legislation of Hong Kong, there is no definition of public interest entity or requirement for the audit of an entity to be conducted with the same independence requirements applicable to the audit of listed entities. Hence, there is no entity falling within this part of the definition under the legislation of Hong Kong.

in the client is material to such entity;

- (c) An entity over which the client has direct or indirect control;
- (d) An entity in which the client, or an entity related to the client under (c) above, has a direct financial interest that gives it significant influence over such entity and the interest is material to the client and its related entity in (c); and
- (e) An entity which is under common control with the client (a “sister entity”) if the sister entity and the client are both material to the entity that controls both the client and sister entity.

Responsible party In an assurance engagement, the party responsible for the underlying subject matter.

Review client An entity in respect of which a firm conducts a review engagement.

Review engagement An assurance engagement, conducted in accordance with *Hong Kong Standards on Review Engagements* or equivalent, in which a professional accountant in public practice expresses a conclusion on whether, on the basis of the procedures which do not provide all the evidence that would be required in an audit, anything has come to the accountant’s attention that causes the accountant to believe that the financial statements are not prepared, in all material respects, in accordance with an applicable financial reporting framework.

Review team

- (a) All members of the engagement team for the review engagement; and
- (b) All others within a firm who can directly influence the outcome of the review engagement, including:
 - (i) Those who recommend the compensation of, or who provide direct supervisory, management or other oversight of the engagement partner in connection with the performance of the review engagement, including those at all successively senior levels above the engagement partner through to the individual who is the firm’s Senior or Managing Partner (Chief Executive or equivalent);
 - (ii) Those who provide consultation regarding technical or industry specific issues, transactions or events for the engagement; and
 - (iii) Those who provide quality control for the engagement, including those who perform the engagement quality control review for the engagement; and
- (c) All those within a network firm who can directly influence the outcome of the review engagement.

Safeguards *Safeguards are actions, individually or in combination, that the professional accountant takes that effectively reduce threats to*

compliance with the fundamental principles to an acceptable level.

This term is described in paragraph 120.10 A2.

Senior professional accountant in business *Senior professional accountants in business are directors, officers or senior employees able to exert significant influence over, and make decisions regarding, the acquisition, deployment and control of the employing organization’s human, financial, technological, physical and intangible resources.*

This term is described in paragraph 260.11 A1.

Substantial harm *This term is described in paragraphs 260.5 A3 and 360.5 A3.*

Special purpose financial statements Financial statements prepared in accordance with a financial reporting framework designed to meet the financial information needs of specified users.

Subject matter information The outcome of the measurement or evaluation of the underlying subject matter against the criteria, i.e., the information that results from applying the criteria to the underlying subject matter.

Those charged with governance The person(s) or organization(s) (for example, a corporate trustee) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance might include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager.

Threats *This term is described in paragraph 120.6 A3 and includes the following categories:*

- Self interest* 120.6 A3(a)
- Self-review* 120.6 A3(b)
- Advocacy* 120.6 A3(c)
- Familiarity* 120.6 A3(d)
- Intimidation* 120.6 A3(e)

Time-on period *This term is described in paragraph R540.5.*

Underlying subject matter The phenomenon that is measured or evaluated by applying criteria.

LISTS OF ABBREVIATIONS AND STANDARDS REFERRED TO IN THE CODE

LIST OF ABBREVIATIONS

Abbreviation	Explanation
Assurance Framework	Hong Kong Framework for Assurance Engagements
COSO	Committee of Sponsoring Organizations of the Treadway Commission
CoCo	Chartered Professional Accountants of Canada Criteria of Control
HKSAAs	Hong Kong Standards on Auditing
HKSAEs	Hong Kong Standards on Assurance Engagements
HKSQCs	Hong Kong Standards on Quality Control
HKSREs	Hong Kong Standards on Review Engagements
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
POBO	Prevention of Bribery Ordinance (Cap. 201)

LIST OF STANDARDS REFERRED TO IN THE CODE

Standard	Full Title
HKSA 320	Materiality In Planning and Performing an Audit
HKSA 610 (Revised 2013)	Using the Work of Internal Auditors
HKSAE 3000 (Revised)	Assurance Engagements Other than Audits or Reviews of Historical Financial Information
HKSQC 1	Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements
HKSRE 2400 (Revised)	Engagements to Review Historical Financial Statements

EFFECTIVE DATE OF CHAPTER A, REQUIREMENTS AND APPLICATION MATERIAL FOR PROFESSIONAL ACCOUNTANTS

Parts 1 – 3

- Parts 1, 2 and 3 of Chapter A will be effective as of 15 June 2019.

Independence Standards (Parts 4A and 4B)

- Part 4A of Chapter A relating to independence for audit and review engagements will be effective for audits and reviews of financial statements for periods beginning on or after 15 June 2019.
- Part 4B of Chapter A relating to independence for assurance engagements with respect to subject matter covering periods will be effective for periods beginning on or after 15 June 2019; otherwise, it will be effective as of 15 June 2019.
- Part 4B relating to independence for assurance engagements with respect to underlying subject matter covering periods will be effective for periods beginning on or after 15 June 2021; otherwise, it will be effective as of 15 June 2021. Early adoption will be permitted.

Early adoption is permitted.

Long Association Provisions (Section 540)

The effective date of Chapter A of the Code does not override the effective date of the revised Long Association provisions in Sections 290 and 291 as set out in the January 2017 long association [close-off document](#) released by the IESBA, which is as follows:

- (a) Subject to the transitional provision in (c) below, paragraphs 290.148 to 290.168 are effective for audits of financial statements for periods beginning on or after 15 December 2018. Early adoption is permitted.
- (b) For assurance engagements covering periods, paragraphs 291.137 to 291.141 will be effective for periods beginning on or after 15 December 2018; otherwise, they will be effective as of 15 December 2018. Early adoption is permitted.
- (c) Paragraph 290.163 shall have effect only for audits of financial statements for periods beginning prior to 15 December 2023. This will facilitate the transition to the required cooling-off period of five consecutive years for engagement partners in those jurisdictions where the legislative body or regulator (or organization authorized or recognized by such legislative body or regulator) has specified a cooling-off period of less than five consecutive years^{1d}.

^{1d} Currently no other legislative body or regulator in Hong Kong has specified separate cooling-off period for professional accountants in public practice in respect of long association of personnel (including partner rotation) with an audit client.



**MEMBERS' HANDBOOK
CONTENTS OF VOLUME III**

(Updated to May 2020)

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Preface (Amended)	Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance and Related Services Prouncements	07/12
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Effective for reports dated on or after 1 June 2020

*Hong Kong Standard on
Investment Circular Reporting Engagements 500*

Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness



Hong Kong Institute of
Certified Public Accountants
香港會計師公會

**HONG KONG STANDARD ON
INVESTMENT CIRCULAR REPORTING ENGAGEMENTS 500
REPORTING ON PROFIT FORECASTS, STATEMENTS OF SUFFICIENCY OF
WORKING CAPITAL AND STATEMENTS OF INDEBTEDNESS**

(Effective for reports dated on or after 1 June 2020)

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Hong Kong Standard on Investment Circular Reporting Engagements (HKSIR) 500 "Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness" should be read in the context of the "Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements" which sets out the application and authority of HKSIRs.

This HKSIR reflects the Listing Rules/GEM Rules, the Takeovers Code and the Companies (Winding Up and Miscellaneous Provisions) Ordinance that were in effect as at 1 October 2019.

Introduction

1. The purpose of this HKSIR is to establish standards and provide guidance for reporting accountants when providing letters on certain information included in an investment circular, namely, in connection with a profit forecast by the Issuer's directors, a statement by the Issuer's directors on the Issuer's sufficiency of working capital and a statement by the Issuer on the Issuer's indebtedness. This HKSIR is written in the context of new listings of equity securities unless otherwise indicated. The sample letters set out in the appendices should be modified in the case of, for example, an investment circular of a notifiable transaction.

Definitions

2. The definitions used in this HKSIR are:

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| a. | Consent letter: | A letter whereby the reporting accountants consent to the inclusion in an investment circular of references to their name or the inclusion of any of their reports which are to be published therein in accordance with the Listing Rules/GEM Rules and/or the Companies (Winding Up and Miscellaneous Provisions) Ordinance. |
| b. | GEM Rules: | Rules Governing the Listing of Securities on GEM of the Stock Exchange. |
| c. | HKSAE 3000 (Revised): | Hong Kong Standard on Assurance Engagements 3000 (Revised), <i>Assurance Engagements Other Than Audits or Reviews of Historical Financial Information</i> . |
| d. | Investment circular: | A document issued by an entity relating to securities and for the information or investment decision of the holders of the entity's securities or other parties, including without limitation a listing document, a prospectus, a circular to shareholders or similar document. |
| e. | Issuer: | As defined by the Listing Rules/GEM Rules, an issuer is any company or other legal person any of whose securities are the subject of an application for listing or some of whose securities are already listed. |
| f. | Listing Rules: | Rules Governing the Listing of Securities on the Stock Exchange. |
| g. | Prospectus: | A document which has the same meaning as in section 2(1) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance. |

- h. Reporting accountants: Certified public accountants who are engaged to prepare public reports and letters for inclusion in, or private letters in connection with, an investment circular. Where the context requires, this term includes auditors where they are carrying out a role in connection with an investment circular, other than that of reporting as auditors on financial statements.
- i. SFC: Securities and Futures Commission.
- j. Sponsor: Any corporation or authorised financial institution, licensed or registered under applicable laws to advise on corporate finance matters and appointed as a sponsor by a new applicant under the Listing Rules / GEM Rules to assist the new applicant with its initial application for listing.
- k. Stock Exchange: The Stock Exchange of Hong Kong Limited.
- l. Takeovers Code: The Codes on Takeovers and Mergers and Share Buy-backs issued by the SFC.

Relevant Regulations

Profit Forecasts

3. Listing Rules 11.17 and 14.61 and GEM Rules 14.29 and 19.61 define a profit forecast (referred to in this HKSIR as a "Profit Forecast") as any forecast of profits or losses, however worded, and includes any statement which explicitly or implicitly quantifies the anticipated level of future profits or losses, either expressly or by reference to previous profits or losses or any other benchmark or point of reference. This also includes any profit estimate, being an estimate of profits or losses for a financial period which has expired but for which the results have not yet been audited or published. In addition, any valuation of assets (except for property interests (as defined in Listing Rule 5.01(3) and GEM Rule 8.01(3)) or businesses acquired by an Issuer based on discounted cash flows or projections of profits, earnings or cash flows is regarded as a profit forecast.
4. There is no specific regulation or requirement that an investment circular should incorporate a profit forecast¹. Listing Rule 11.17 and GEM Rule 14.29 require that, in the case of a new listing of equity securities, the Issuer must determine in advance whether to include a Profit Forecast in an investment circular. Where a Profit Forecast appears in any investment circular, it must be clear, unambiguous and presented in an explicit manner. The principal assumptions, including commercial assumptions, upon which it is based, must be stated and such profit forecast must be prepared on a basis that is consistent with the accounting policies normally adopted by the Issuer. Listing Rule 11.17 and GEM Rule 14.29 also state that the accounting policies and calculations for the Profit Forecast must be reviewed and reported on by the reporting accountants and their letter must be set out.
5. Following the new sponsor regulations taking effect in October 2013, a draft investment circular relating to a new listing of equity securities (referred to as an "Application Proof") shall include the draft reporting accountants' letter on the Profit Forecast (if any) upon submission to the Stock Exchange. The reporting accountants are required to provide a written confirmation to the applicant, with a copy to the sponsor, the Stock Exchange and the SFC, that no significant modification is expected to be made to the draft letter on the Profit Forecast based on the work done as of the date of the confirmation.

¹ The inclusion of a profit estimate may be required when a listing applicant applies for a waiver from compliance with Listing Rule 4.04(1) or GEM Rules 7.03(1) and 11.10.

6. Rule 10 of the Takeover Code provides that a Profit Forecast must be compiled with due care and consideration by the directors, whose sole responsibility it is. The reporting accountants must report on the Profit Forecast, so far as the accounting policies and calculations are concerned, as to whether it has been properly compiled on the basis of the assumptions made.
7. Listing Rule 11.18 and GEM Rule 14.30 require that a Profit Forecast appearing in an investment circular (other than one supporting a capitalisation issue) should normally cover a period which is coterminous with the Issuer's financial year end. If, exceptionally the profit forecast period ends at a half year-end the Stock Exchange will require an undertaking from the Issuer that the interim report for that half year will be audited. Ordinarily, profit forecast periods not ending on the financial year end or half year-end will not be permitted.
8. Listing Rule 11.19 and GEM Rule 14.31 require that the assumptions upon which any Profit Forecast appearing in a listing document (other than one supporting a capitalisation issue) are based must provide useful information to investors to help them in forming a view as to the reasonableness and reliability of the forecast. Such assumptions should draw the investors' attention to, and where possible quantify, those uncertain factors which could materially disturb the ultimate achievement of the forecast. The assumptions should be specific rather than general, definite rather than vague. All embracing assumptions and those relating to the general accuracy of the estimates made in the Profit Forecast should be avoided. Furthermore it will not normally be acceptable for assumptions to relate to matters which the directors, by virtue of their particular knowledge and experience in the business, are best able to take a view on or are able to exercise control over since such matters should be reflected directly in the Profit Forecast itself.

Statements of Sufficiency of Working Capital

9. Paragraph 36 of Appendix 1A to the Listing Rules and Paragraph 36 of Appendix 1A to the GEM Rules² require an investment circular relating to a new listing of equity securities to include a statement by the directors that in their opinion the working capital available to the group is sufficient for the group's present requirements, that is for at least the next 12 months from the date of publication of the investment circular³, or, if not, how it is proposed to provide the additional working capital thought by the directors to be necessary (referred to in this HKSIR as "Working Capital Statement"). As explained in Note 3 of Appendix 1A to the Listing Rules/GEM Rules², reference to the group is to be construed as including any company which will become a subsidiary of the Issuer by reason of an acquisition which has been agreed or proposed since the date to which the latest audited accounts of the Issuer have been made up.
10. Following the new sponsor regulations taking effect in October 2013, a draft investment circular relating to a new listing of equity securities must include the Working Capital Statement upon submission to the Stock Exchange. An advanced draft of a letter from the listing applicant's sponsor confirming that it is satisfied that the Working Capital Statement in the Application Proof has been made by the directors after due and careful enquiry must be submitted to the Stock Exchange at the same date as the Application Proof. Before a listing document is bulk-printed, the listing applicant's sponsor is required to provide a final confirmation letter on the Working Capital Statement.

² In the case where listing is sought for equity securities of an issuer some part of whose share capital is already listed, reference should be made to Paragraph 30/Note 2 of Appendix 1B to the Listing Rules and the GEM Rules.

³ For listing of a "mineral company" as defined under Chapter 18 of the Listing Rules and Chapter 18A of the GEM Rules and listing of a "biotech company" as defined under Chapter 18A of the Listing Rules, an applicant must demonstrate that it has available sufficient working capital for 125% of its working capital needs (refer to the requirements set out in the relevant Listing Rules/GEM Rules) for the next 12 months from the date of the publication of the investment circular.

11. Where an investment circular relating to a notifiable transaction contains a Working Capital Statement, the Stock Exchange will require a letter from the Issuer's financial advisers or auditors confirming that the directors have made such statement after due and careful enquiry and that the persons or institutions providing finance have confirmed in writing that such facilities exist⁴.
12. Paragraph 12(9) of Appendix 28 to the Listing Rules requires that where an Issuer listed on GEM applies for a transfer of listing to the Main Board, the Stock Exchange will require a written confirmation, together with relevant supporting information⁵, from the Issuer confirming that the working capital available for the group is sufficient for its present requirements. The Issuer's financial advisers or auditors should be satisfied that this confirmation has been given after due and careful enquiry and that persons or institutions providing finance have stated in writing that the relevant financing facilities exist⁶.

Statements of Indebtedness

13. As more fully explained below, amongst other things, Paragraph 32 of Appendix 1A to the Listing Rules and Paragraph 32 of Appendix 1A to the GEM Rules⁷ require an investment circular relating to a new listing of equity securities to include a statement as at the most recent practicable date of the total amount of debt securities, borrowings, indebtedness, mortgages, charges, contingent liabilities and guarantees, of the new applicant on a consolidated or combined basis (referred to in this HKSIR as a "Statement of Indebtedness"). For the purposes of that requirement, the Stock Exchange ordinarily requires that the relevant information should be as at a date that is no more than two calendar months before the issuance of the investment circular relating to a new listing of equity securities.⁸
14. Paragraph 32 of Appendix 1A to the Listing Rules and Paragraph 32 of Appendix 1A to the GEM Rules⁷ require disclosure by the Issuer of details of any loan capital, borrowings, mortgages or charges and indebtedness, contingent liabilities and guarantees, as at the most recent practicable date (ordinarily no more than two calendar months before the issuance of the investment circular relating to a new listing of equity securities⁷), or an appropriate negative statement. The Issuer is required to set out, as at the most recent practicable date (which must be stated), the following on a consolidated or combined basis if material:
 - (a) the total amount of any debt securities of the group issued and outstanding, and authorised or otherwise created but unissued, and term loans, distinguishing between guaranteed, unguaranteed, secured (whether the security is provided by the Issuer or by third parties) and unsecured, or an appropriate negative statement;
 - (b) the total amount of all other borrowings or indebtedness in the nature of borrowings of the group including bank overdrafts and liabilities under acceptances (other than normal trade bills) or acceptance credits or hire purchase commitments, distinguishing between guaranteed, unguaranteed, secured and unsecured borrowings and debt, or an appropriate negative statement;

⁴ Refer to Listing Rules 14.66(12), 14.67A(2)(b)(ii) and 14.69(1)(b) and GEM Rules 19.66(13), 19.67A(2)(b)(ii) and 19.69(1)(b) for situations where a Working Capital Statement is required in an investment circular relating to a notifiable transaction.

⁵ As explained in Note to Paragraph 12(9) of Appendix 28 to the Listing Rules, supporting information for this purpose typically includes cash flow forecast memoranda, profit forecasts and written statements from persons or institutions providing finance.

⁶ This applies to the transitional arrangements for an Eligible Issuer applying for a transfer of its listing from GEM to the Main Board during the transitional period of three years from 15 February 2018 to 14 February 2021 as set out in Chapter 9A of and Appendix 28 to the Listing Rules.

⁷ In the case where listing is sought for equity securities of an issuer some part of whose share capital is already listed, reference should be made to Paragraph 28 of Appendix 1B to the Listing Rules and the GEM Rules.

⁸ For the purpose of the Statement of Indebtedness, the most recent practicable date is normally a date no more than

- Two calendar months before the date of the Application Proof or the final listing document, in the case of a listing of new equity securities (see Guidance Letter 37-12 issued by the Stock Exchange); or
- Eight calendar weeks before the date of the investment circular, in the case of notifiable transactions (see HKEX FAQ Series 7 FAQ No.25).

- (c) all mortgages and charges of the group, or an appropriate negative statement; and
- (d) the total amount of any contingent liabilities or guarantees of the group, or an appropriate negative statement. Intra-group liabilities should normally be disregarded, a statement to that effect being made where necessary. Reference to group is to be construed as including any company which will become a subsidiary of the Issuer by reason of an acquisition which has been agreed or proposed since the date to which the latest audited accounts of the Issuer have been made up.

In addition, the Issuer should set out a commentary on (i) the group's liquidity and financial resources, which may include comments on the level of borrowings at the end of the period under review, the seasonality of borrowing requirements and the maturity profile of borrowings and committed borrowing facilities; and (ii) the capital structure of the group. The Issuer is also expected to disclose information about unutilised banking facilities.

- 15. Following the new sponsor regulations taking effect in October 2013, an Application Proof relating to a new listing of equity securities must also include a Statement of Indebtedness upon submission to the Stock Exchange. The relevant information should be as at a date that is no more than two calendar months before the date of the Application Proof⁸. The Statement of Indebtedness must be updated as necessary in subsequent draft and final investment circulars relating to a new listing of equity securities to satisfy the two calendar months requirement.

Preparation of the Profit Forecast, Working Capital Statement and Indebtedness Statement by the Issuer's Directors

- 16. The directors are solely responsible for the Profit Forecast, Working Capital Statement and the Statement of Indebtedness included in an investment circular.
- 17. Ordinarily, a Profit Forecast and a Working Capital Statement are prepared in conjunction with a memorandum prepared by the Issuer (hereafter referred to as a "board memorandum") which would normally include the preparation of supporting prospective financial information in the form of internally consistent forecast/projected profit or loss, balance sheet information, cash flow forecasts/projections, details of facilities and resources available, or to become available to the group, together with supporting analyses and details of the assumptions on which they are based.
- 18. The requirements of the regulations governing Profit Forecasts and Working Capital Statements are not aligned. A Profit Forecast for the current (or unexpired) accounting period is required to be submitted to the Stock Exchange as part of the board memorandum but the working capital forecast must cover a period of at least 12 months from the date of the investment circular. For example, a Profit Forecast may cover a period for the financial year ending 31 December 20X3 while the working capital forecast may cover a period for the 18 months ending 31 December 20X4. For the purpose of preparation of a board memorandum, the Profit Forecast generally covers a period shorter than that of the working capital forecast. However, the Issuer's directors also should prepare a forecast of the profit or loss for an extended period, in support of the working capital forecast even if the profit forecast for that extended period does not get formally incorporated into the board memorandum.

19. The directors are expected to undertake appropriate procedures in the preparation of the Profit Forecast and working capital forecast supporting the Working Capital Statement, which would normally include:
 - (a) business analysis covering the profit or loss, cash flows of the business and the terms and conditions and commercial considerations associated with banking and other financing arrangements;
 - (b) consideration of the strategy and plans of the business and the related implementation risks together with checks against external evidence and opinion; and
 - (c) assessment of whether there is sufficient margin or headroom to cover a reasonable worst case scenario, i.e. sensitivity analysis, for the purpose of a working capital forecast.
20. The directors should consider the relevant guidance in Listing Rule 11.19 and GEM Rule 14.31 as described in paragraph 8 above when setting assumptions for the Profit Forecast and working capital forecast. The board memorandum setting out such assumptions should be approved by the directors and recorded in the board minutes. The Profit Forecast and working capital forecast should be properly compiled on the basis of these underlying assumptions.
21. The preparation of a Profit Forecast, a Working Capital Statement and a Statement of Indebtedness are interrelated to the extent that consistent analyses should be made covering all three documents. In particular the amounts included in the Statement of Indebtedness and the Profit Forecast should be incorporated into the Working Capital Statement.
22. Ordinarily, a schedule of indebtedness as at the most recent practicable date, containing details of the items listed in paragraph 14(a) to (d) above, should be prepared by the directors in support of the Statement of Indebtedness that is included in the investment circular. Figures in the schedule should in turn agree to amounts disclosed in the investment circular. The investment circular not only includes the Statement of Indebtedness but often may include management discussion and analysis which are further discussed in paragraph 55 below.

Reporting on Profit Forecasts

23. The reporting accountants' responsibility is to express an opinion on the accounting policies and calculations of the Profit Forecast based on their procedures. It is not the reporting accountants' responsibility to report upon the assumptions or to report on the prospects of the Issuer achieving the Profit Forecast. Nevertheless, reporting accountants should not allow any assumption to be published which appears to them to be unrealistic (or one to be omitted which appears to them to be important), without commenting on it in their letter.
24. It is emphasised that Profit Forecasts necessarily depend on subjective judgements. They are, to a greater or lesser extent according to the nature of the business and period the Profit Forecast covers, subject to numerous and substantial inherent uncertainties. In consequence, Profit Forecasts are not capable of being substantiated by reporting accountants in the same way as financial statements which present the results of completed accounting periods. Due to the uncertainties mentioned above, reporting accountants should normally restrict their reporting on Profit Forecasts to those for one year or less from the date to which the last audited financial statements were made up. Only in exceptional circumstances should they report on profit forecasts for a future accounting period which should in any case be limited to the immediately succeeding period and then only if a significant part of the current period has already elapsed.

In practice, it is unusual to provide a forecast for a succeeding period unless:

- (a) at least 10 months of the current period has elapsed; and
- (b) the Issuer's operations lend themselves to reasonably accurate forecasting such as in the case of a regulated utilities company.

25. The reporting accountants should make the reporting period clear when they accept instructions to examine the accounting policies and calculations for Profit Forecasts, and in the wording of their letter they should take care to avoid giving any impression that they are in any way confirming, underwriting, guaranteeing or otherwise accepting responsibility for the ultimate accuracy and realisation of forecasts. Moreover, bearing in mind their special status and authority, reporting accountants should do or say nothing to encourage directors, third parties or the public to place a mistaken degree of reliance on statements as to future profits, the achievement of which must always be subject to uncertainty.
26. Reporting accountants should agree with the directors the following fundamental points before accepting instructions to report:
- (a) the purpose for which the Profit Forecast has been prepared and the reporting accountants' letter is required;
 - (b)
 - (i) that the reporting accountants' instructions and responsibilities for reporting are limited to the requirements under the regulations and do not constitute an audit;
 - (ii) that the directors assume full responsibility for the Profit Forecast under review; and
 - (iii) that the directors will signify their responsibility for formal adoption by the board;
 - (c) that the Profit Forecast is for:
 - (i) an expired accounting period;
 - (ii) the current (or unexpired) accounting period; or
 - (iii) the current and the immediately succeeding accounting period, provided that a sufficiently significant part of the current period has already elapsed;
 - (d) no material restrictions on the scope of the reporting accountants' work (for example, by restricting visits to overseas companies or material factory units) can normally be accepted unless the matter is dealt with in the reporting accountants' letter and in the published documents; and
 - (e) that the time within which the reporting accountants' letter is required is not so severely restricted that, having regard to the Issuer's circumstances and forecasting experience, and notwithstanding their best endeavours, it would be plainly impossible for the reporting accountants to obtain sufficient information to enable them properly to exercise their professional judgement.
27. In the case of a Profit Forecast in an investment circular relating to a new listing of equity securities, the sponsors should report whether or not they have satisfied themselves that the forecast has been stated by the directors after due and careful enquiry. In the case of a Profit Forecast in a document connected with an offer, the Takeover Code requires that any adviser mentioned in the document should also report on the forecast. The responsibilities of such persons are distinct from those of the reporting accountants. From the outset, liaison should be established with such other advisers to ensure that there is no doubt or misunderstanding on either side as to the respective responsibilities or as to the work which will be carried out by each party to enable it to fulfil its reporting function.
28. The reporting accountants should consider materiality when determining the nature, timing and extent of evidence-gathering procedures. Considering materiality requires the reporting accountants to understand and assess what factors might influence the decisions of the intended users. The reporting accountants may also consider factors such as the preciseness of the Profit Forecast being made by the Issuer's directors. The reporting accountants should make reference to HKSAE 3000 (Revised) for further guidance when determining materiality.

29. When reporting on the Profit Forecast, the reporting accountants should plan and perform the work in accordance with this HKSIR and with reference to HKSAE 3000 (Revised). HKSAE 3000 (Revised) requires, among other things, compliance with Chapter A, Parts 1, 3 and 4B, and Chapter C of the HKICPA's *Code of Ethics for Professional Accountants* (the Code) related to assurance engagements, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding.⁹ It also requires the engagement partner to be a member of a firm that applies HKSQC 1,¹⁰ or other professional requirements, or requirements in law or regulation, that are at least as demanding as HKSQC 1. The degree of work required will in part depend on whether forecasts made in the past have proved reliable. The approach to such an assignment typically may include:
- (a) obtaining the board memorandum prepared by the directors;
 - (b) reviewing the Issuer's recent history, with reference to such matters as the general nature of its activities and its main products, markets, customers, suppliers, divisions, locations, management, labour force, trend of results and organisational changes;
 - (c) discussing the plans, strategies and risk analysis with the directors in the context of the preparation of the Profit Forecast, considering documentary support for the plans, strategies and risk analysis of the directors and assessing whether they are consistent with the analysis of the business, and with information generated within the Issuer itself as well as from external sources such as key economic indicators and reliable industry statistics;
 - (d) considering the consistency of underlying assumptions with the business analysis of the directors and assessing the source and reliability of the evidence supporting management's best-estimate assumptions. Sufficient appropriate evidence supporting such assumptions would be obtained from internal and external sources including consideration of the assumptions in the light of historical information and an evaluation of whether they are based on plans that are within the entity's capacity;
 - (e) establishing which accounting policies have been adopted by the Issuer in published financial statements so as to ensure that they are acceptable and have been consistently applied in the preparation of interim accounts and the Profit Forecast;
 - (f) considering the assumptions on which the Profit Forecast has been based in the course of their work to determine that the Profit Forecast is consistent with and has been properly compiled on the basis of the assumptions adopted by the directors;
 - (g) reading the minutes of the board and of other important management meetings which contain key factors that might affect the forecast;
 - (h) checking the arithmetical accuracy of the forecast and the supporting information; and
 - (i) obtaining written representations where necessary from the board of directors regarding the intended use of the Profit Forecast, the completeness of significant management assumptions and management's acceptance of its responsibility for the Profit Forecast.
30. In addition to checking the arithmetical accuracy of the Profit Forecast and that it is properly compiled on the basis of the stated assumptions, the reporting accountants will also need to consider the assumptions. If any assumption appears to be unrealistic, or if any important assumption has not been included in the Profit Forecast, the reporting accountants should consider the need to draw attention to it in their letter or whether to withhold issuing their letter until the matter is addressed to their reasonable satisfaction. The reporting accountants have

⁹ HKSAE 3000 (Revised), paragraphs 3(a), 20 and 34

¹⁰ HKSAE 3000 (Revised), paragraphs 3(b) and 31(a). Hong Kong Standard on Quality Control (HKSQC) 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

no specific responsibilities for and are not required by the regulations or otherwise to report on the assumptions and should not comment on any assumption beyond the reporting accountants' area of expertise. In carrying out the review of a Profit Forecast, the main points which the reporting accountants will wish to consider include the following:

- (a) whether the Profit Forecast under review is based on forecasts regularly prepared for the purpose of management, or whether it has been separately and specifically prepared for the immediate purpose;
- (b) where Profit Forecasts are regularly prepared for management purposes, the degree of accuracy and reliability previously achieved, and the frequency and thoroughness with which estimates are revised;
- (c) whether the Profit Forecast under review represents the management's best estimate of results which they reasonably believe can and will be achieved as distinct from targets which the management have set as desirable;
- (d) whether all significant implications of management's assumptions have been taken into consideration. For example, if sales are assumed to grow beyond the entity's current plant capacity, the Profit Forecast will need to include the necessary investment in the additional plant capacity or the costs of alternative means of meeting the anticipated sales, such as subcontracting production. Reporting accountants would need to be satisfied that they are consistent with the purpose of the Profit Forecast and that there is no reason to believe they are clearly unrealistic;
- (e) the extent to which those areas that are particularly sensitive to variation will have a material effect on the results shown in the Profit Forecast. This will influence the extent to which the reporting accountants will seek appropriate evidence and the reporting accountants' evaluation of the appropriateness and adequacy of disclosure;
- (f) when any elapsed portion of the current period is included in the Profit Forecast, the extent to which procedures need to be applied to the historical information. Procedures will vary depending on the circumstances, for example, how much of the prospective period has elapsed;
- (g) the extent to which Profit Forecast results for expired periods are supported by reliable interim accounts;
- (h) the details of the procedures followed to generate the Profit Forecast and the extent to which it is built up from detailed profit forecasts of activity and cash flow;
- (i) the extent to which profits are derived from activities having a proven and consistent trend and those of a more irregular, volatile or unproven nature;
- (j) how the Profit Forecast takes account of any material unusual items and prior year adjustments, their nature, and how they are presented; and
- (k) whether adequate provision is made for foreseeable losses and contingencies and how the Profit Forecast takes account of factors which may cause it to be subject to a high degree of risk, or which may invalidate the assumptions.

The reporting accountants' letter

31. The reporting accountants' letter will be addressed to the directors and to the sponsors (in the case of a new listing of equity securities) and will normally include statements dealing with the following matters, so far as appropriate:
- (a) specific identification of the Profit Forecast and documents to which the letter refers;
 - (b) the fact that the directors are solely responsible for the Profit Forecast;

- (c) that the firm of which the practitioner is a member applies HKSQC 1, or other professional requirements, or requirements in law or regulation, that are at least as demanding as HKSQC 1;
 - (d) that the practitioner complies with the independence and other ethical requirements of the Code, or other professional requirements, or requirements imposed by law or regulation, that are at least as demanding as Chapter A, Parts 1, 3 and 4B, and Chapter C of the Code related to assurance engagements;
 - (e) the fact that the reporting accountants have reviewed the accounting policies and calculations used in arriving at the Profit Forecast;
 - (f) if, as will frequently be the case, the reporting accountants have not carried out an audit of results for expired periods, a statement to that effect; and
 - (g) whether in the opinion of the reporting accountants the Profit Forecast, so far as the accounting policies and calculations are concerned, has been properly compiled on the bases and assumptions adopted by the directors, as set out in the document, and is presented on a basis consistent with the accounting policies normally adopted by the Issuer.
32. The letter should be qualified if, inter alia, the reporting accountants:
- (a) have reason for material reservation about the accounting policies or calculations for the Profit Forecast;
 - (b) have reason to consider the accounting policies and calculations to be inconsistent with the stated bases or assumptions; or
 - (c) have not obtained all the information they consider necessary (for example, the fact that they were unable to review the forecasts of material subsidiary or associated companies or because of unduly restrictive time limits).
33. If any of the assumptions which are to be published and which fall within the reporting accountants' area of expertise appear to them to be unrealistic, or if any assumption is to be omitted which appears to the reporting accountants to be important, they should include an appropriate comment in their letter.
34. Where the Profit Forecast involves assumptions of a high level of uncertainty, such as the projected change in fair value in respect of an investment property during the forecast period, the reporting accountants should consider whether to include an other matter paragraph concerning such uncertainties in the reporting accountants' letter.
35. An appropriate form of reporting accountants' letter is attached as Appendix 1.
36. As mentioned in paragraph 3 above, any valuation of assets (except for property interests (as defined in Listing Rule 5.01(3) and GEM Rule 8.01(3)) or businesses acquired by an Issuer based on discounted cash flows or projections of profits, earnings or cash flows is regarded as a profit forecast (referred to in this paragraph as a "deemed forecast") as set out in Listing Rules 11.17 and 14.61 and GEM Rules 14.29 and 19.61. The reporting on a deemed forecast is ordinarily outside the scope of this HKSIR as the forecast period covered by a deemed forecast is longer than the maximum acceptable period set out in paragraph 24 above. The reporting accountants should adopt HKSAE 3000 (Revised) to report on the calculations and, where applicable, the accounting policies of a deemed forecast. Nevertheless, the reporting accountants can make reference to the work and procedures on Profit Forecasts set out in this HKSIR when reporting on a deemed forecast except that the preparation of such a forecast may not involve the application of accounting policies (for example, in the case of a deemed forecast relating to a valuation based on discounted cash flows). In addition, the compilation of and the key assumptions supporting the forecast may be set out in the valuation model itself

rather than in a separate board memorandum. The reporting accountants should appropriately modify their work and the reporting on a deemed forecast to take account of these differences.

Consent letter

37. The regulations require that a reporting accountants' letter contained in a document must be accompanied by a statement that the reporting accountants have given in writing, and not withdrawn, their consent to its publication.
38. Most of the documents containing profit forecasts are also prospectuses for Companies (Winding Up and Miscellaneous Provisions) Ordinance purposes, in which case there is a statutory requirement that the consent specifically refers to the statement being included, in the form and context in which it is included, and that the statement that the consent has been given and has not been withdrawn should appear in the prospectus.

Reporting on Statements of Sufficiency of Working Capital

39. When reporting on the Working Capital Statement, the reporting accountants should plan and perform the work in accordance with this HKSIR and with reference to HKSAE 3000 (Revised). The degree of work required will in part depend on whether forecasts made in the past have proved reliable, and on the extent of the surplus of resources over the estimated cash flow requirements. The reporting accountants should follow the guidance as set out in paragraph 28 above in determining materiality when reporting on the Working Capital Statement. The approach to such an assignment typically may include those procedures and considerations applicable to a Profit Forecast as set out in paragraphs 29 and 30 above and the following:
 - (a) comparing the forecast with the group's existing financing facilities and cash resources, or that are to become available to the group;
 - (b) in general, independently obtaining direct confirmation from the appropriate third party of the extent of financing facilities and resources available to the group. The extent of amounts confirmed is discussed in greater detail in paragraph 41 below. Where requested confirmations have not been returned, the reporting accountants should evaluate the reasons (for example, whether there is doubt over the availability of such financing) and should also seek to obtain suitable alternative evidence;
 - (c) considering adjustments for items such as capital expenditure and prepayments which exert no impact on the Profit Forecast but may significantly impact the working capital forecast; and
 - (d) considering management's sensitivity analysis and the extent of any margin or headroom.
40. Whilst the reporting accountants will consider the key assumptions, in doing so they are not giving any separate assurance on the validity of those assumptions, as such consideration is made in the context of issuing their letter on the Working Capital Statement as a whole in the form and context in which it is made. In cases where an assumption appears unreasonable or overly optimistic the working capital forecast may have sufficient headroom or the effects of other more conservative assumptions may counteract the effect of an unreasonable or aggressive assumption, so that, when considered in aggregate, the reporting accountants may nevertheless be able to conclude that the Working Capital Statement is made by the Issuer's directors, in the form and context in which it is made, after due and careful enquiry.
41. The directors should ordinarily set out in the board memorandum the financing facilities and resources available to the Issuer as of a specified date and, where applicable, those expected to be available to the Issuer at future dates during the forecast period. The directors should identify in the board memorandum which financing facilities and resources are required to satisfy their statement regarding the adequacy of working capital. The reporting accountants should seek to confirm the amount of existing financing facilities and resources as of the

specified date to the extent that they are identified by the directors as needed for the forecast working capital to be sufficient. The reporting accountants may consider confirming the remaining financing facilities and resources that exist as of the specified date taking appropriate account of sensitivity analyses prepared by the directors. For example, if an Issuer requires financing facilities of HKD 100 million as part of its working capital forecast and has separately identified such facilities in the board memorandum, but facilities of say HKD 300 million are available as of the specified date, the reporting accountants may determine only to obtain confirmation of the existence of those facilities amounting to HKD 100 million. The reporting accountants may obtain confirmation of the remaining facilities of HKD 200 million, in whole or in part, for the purpose of expressing an opinion on the Working Capital Statement taking into account the sensitivity analyses and the level of headroom available in the working capital forecast. The reporting accountants ordinarily are not in a position to obtain direct confirmation from the appropriate third party in respect of financing facilities and resources that are expected to be available to the Issuers at future dates. The reporting accountants should consider the assumptions as to the availability of such future facilities and resources as part of their procedures as described in paragraph 40 above. The reporting accountants should make clear the extent of financing facilities for which evidence of written confirmation has been obtained.

42. As the Issuer's directors have sole responsibility for their statement regarding the adequacy of working capital, the reporting accountants should satisfy themselves that the directors have considered all the relevant information with due care. The reporting accountants should obtain appropriate and sufficient evidence that the working capital forecast and the related board memorandum have been formally approved by the board, for example by being recorded in the board minutes, or by obtaining a representation letter or other suitable evidence of approval.
43. Where there may be concern or doubts on the sufficiency of working capital (for example, if sufficiency of working capital is dependent on future events such as a minimum net proceeds raised in an initial public offering, or if the availability of sources of finance is contingent on certain conditions being fulfilled), as part of their procedures, the reporting accountants should evaluate whether the Working Capital Statement adequately draws attention to any such matters, before concluding whether the Working Capital Statement, in the form and context in which it is made, has been made after due and careful enquiry.
44. The letter on the Working Capital Statement also needs to report whether the persons or institutions providing finance to the group have confirmed in writing that such financing facilities exist. As noted in paragraphs 39(b) and 41 above, the reporting accountants should normally independently obtain direct confirmations from the appropriate third party of the extent of financing facilities and resources available to the group that are required for working capital purposes, which usually include banks and other lenders providing finance to the group in the form of borrowings and/or committed facilities. Where direct confirmation has not been received and instead the reporting accountants have relied on alternative evidence (for example, having sighted a letter from the Issuer's bankers confirming banking facilities that is addressed to the Issuer), ordinarily the reporting accountants should highlight those facilities which have not been directly confirmed to them and in respect of which they have relied on alternative evidence as well as the nature of such alternative evidence.
45. The reporting accountants' letter should clearly identify the information on which it is based. The letter should be addressed to the Issuer's directors with a copy to the sponsor, the Stock Exchange and the SFC, but it should not be referred to in the investment circular. The form of the letter will usually be that, based on the procedures performed, in the opinion of the reporting accountants, the directors have made their statement on sufficiency of working capital, in the form and context in which it is made, after due and careful enquiry and that the reporting accountants have confirmed that the persons or institutions providing finance to the group have confirmed in writing that such financing facilities exist as of a specified date to the extent that they have been identified as required by the Issuer's directors for the working capital forecast.

46. In respect of the Working Capital Statement included in an Application Proof, the reporting accountants should seek to complete the work insofar as is practicable at the time of the submission of the Application Proof to the Stock Exchange. However, as the board memorandum and the working capital forecast supporting the Working Capital Statement are likely still subject to change, and the facilities and resources expected to be available upon listing may not be fully in place at the time of the submission of the Application Proof, it will generally be inappropriate for the reporting accountants to issue a letter in final form to the Issuer's directors. The reporting accountants should present draft letters and provide verbal updates to the sponsor on the status and work performed in respect of the Working Capital Statement included in the Application Proof to assist the sponsor in providing its draft confirmation as described in paragraph 10 above.
47. In the case of a new listing of equity securities, having regard to the Stock Exchange's requirement that the listing applicant's sponsor provides a final confirmation letter on the Working Capital Statement before a listing document is bulk-printed, the reporting accountants should issue a letter on the Working Capital Statement on the same date as the date of the sponsor's final confirmation letter, which should also be the date of the final working capital forecast board memorandum approved by the directors. In addition, the reporting accountants shall be in a position to issue a second signed letter on the Working Capital Statement upon the issue of the listing document. The second letter of the reporting accountants should be in substantially the same form as the first letter, except that the second letter would be dated the date of the listing document and would refer to the final listing document, which would not have been available at the time of the issue of the first letter. The reporting accountants should obtain appropriate written representations from the directors confirming that no modification to the board memorandum and the working capital forecast supporting the Working Capital Statement is required since the date of approval of the board memorandum.
48. An example letter on a Working Capital Statement upon issue of an investment circular is set out in Example 1 of Appendix 2 to this HKSIR. An example letter on a Working Capital Statement upon the listing applicant's sponsor providing a final confirmation letter on the Working Capital Statement before a listing document is bulk-printed in the case of new listing of equity securities (i.e. the first letter referred to in paragraph 47 above) is set out in Example 2 of Appendix 2 to this HKSIR.

Reporting on Statements of Indebtedness

49. As the date to which the Statement of Indebtedness is prepared is the most recent practicable date, typically audited financial statements for a period ending on such date are unavailable. Accordingly, the reporting accountants will often have less evidence on which to base their letter than they would have if the Statement of Indebtedness were made as at the end of an audited financial period. In these circumstances reporting accountants have to place substantial reliance on management as to the identification of amounts and disclosures in the Statement of Indebtedness.
50. When issuing a letter on a Statement of Indebtedness, the reporting accountants perform a range of agreed upon procedures on the schedule of indebtedness as agreed with the Issuer and agree the amounts disclosed in the Statement of Indebtedness as at the most recent practicable date to the schedule of indebtedness. In such an engagement, the reporting accountants follow the principles in Hong Kong Standard on Related Services 4400 "Engagements to Perform Agreed-upon Procedures Regarding Financial Information" ("HKSR 4400") and the guidance in this HKSIR.
51. The reporting accountants' procedures on the Issuer's indebtedness may include:
- (a) obtaining the schedule of indebtedness prepared by the directors including a complete list of bankers and other lenders of the group;
 - (b) agreeing amounts shown on the Statement of Indebtedness to the relevant amounts in the schedule of indebtedness;
 - (c) agreeing amounts shown on the schedule of indebtedness to the Issuer's records;

- (d) in respect of bank loans and other borrowings and mortgages and charges (other than debt securities), obtaining direct confirmations from banks and other lenders and finance providers regarding the outstanding amounts at the relevant date and whether the amounts are secured and, where the amounts shown on the confirmations are different from the amounts shown in the Issuer's accounting records, tracing the amounts to the reconciliations prepared by management of the Issuer. If such confirmations have not been received, setting out the alternative evidence in support of the amounts;
- (e) in respect of debt securities, obtaining the schedules prepared by management of the Issuer to reconcile the principal amounts of debt securities to the amounts shown in the Issuer's accounting records and checking the principal amounts to underlying agreements (or obtaining direct confirmations from appropriate third parties such as the trustee to confirm the principal amounts where possible);
- (f) in respect of lease liabilities, checking the amounts to calculation schedules prepared by management of the Issuer, the arithmetical accuracy of such calculation schedules and the key parameters used in the calculation to underlying agreements; and
- (g) obtaining written representations from the Issuer's directors regarding the completeness and accuracy of the amounts disclosed in the schedule of indebtedness.

The procedures on the Issuer's indebtedness should be tailored depending on the specific facts and circumstances, subject to discussion and agreement between the reporting accountants and the Issuer.

- 52. The reporting accountants are not required to report on the reconciling items included in the reconciliations prepared by the Issuer in respect of its bank or other indebtedness. However, the reporting accountants should seek explanations from the Issuer's management on large and unusual reconciling items and consider whether anything has come to their attention to indicate that adjustments should be made to the schedule of indebtedness. For example, adjustments may arise on fair value accounting of certain financial instruments. The extent of such enquiries and other procedures will be a matter for the reporting accountants' judgement.
- 53. The identification and quantification of contingent liabilities or guarantees are subject to management's judgment. Reporting accountants can agree to report on contingent liabilities prepared by the directors provided the amounts of such contingent liabilities are subject to the Issuer's internal controls, policies and procedures of which reporting accountants have knowledge.
- 54. The reporting accountants' procedures on the amounts of contingent liabilities or guarantees would typically include:
 - (a) obtaining the schedule of contingent liabilities or guarantees prepared by the directors;
 - (b) agreeing amounts to the Issuer's records;
 - (c) reading board minutes;
 - (d) obtaining direct confirmation from banks regarding the amounts of guarantees provided as at the relevant date or if such confirmation has not been received, setting out the alternative evidence in support of the amount;
 - (e) in respect of litigation obtaining confirmation from Issuer's external legal counsel. However, the reporting accountants should also make clear that they do not comment on matters subject to legal interpretation and nor can they give any assurance on the eventual outcome of any litigation;

REPORTING ON PROFIT FORECASTS, STATEMENTS OF SUFFICIENCY OF WORKING CAPITAL AND STATEMENTS OF INDEBTEDNESS

- (f) comparing items and amounts disclosed in the schedule to items and amounts disclosed in the historical financial information on which the reporting accountants have issued their accountants' report; and
 - (g) obtaining written representations from the Issuer's directors regarding the completeness and accuracy of the information disclosed in the schedule of indebtedness, as well as on other matters where the reporting accountants so require.
55. Reporting accountants would generally not be in a position to comment on management's discussion and analysis of indebtedness or contingent liabilities which primarily involves the exercise of management's judgment. For example, the possibility of obtaining a loan in the future or the outcome of litigation may not be within the reporting accountants' knowledge and expertise.
56. Where the reporting accountants identify any errors or discrepancies, they should discuss these with management. Where they believe it to be necessary, the reporting accountants request management to amend the amounts disclosed in the investment circular. Where management does not make amendments that the reporting accountants believe to be necessary, the reporting accountants consider the need to draw attention to the errors or discrepancies in their letter or whether to withhold issuing their letter until the matters are addressed to their reasonable satisfaction.
57. The reporting accountants issue a letter on the Statement of Indebtedness reporting factual findings in respect of the agreed-upon procedures performed, including appropriate details of errors and exceptions found. The letter should be addressed to the Issuer's directors with a copy to the sponsor, where applicable, but it should not be referred to in the investment circular. A copy of the reporting accountants' letter may also be provided to the Stock Exchange and the SFC upon their request.
58. In respect of the Statement of Indebtedness presented in an Application Proof, the reporting accountants may also be engaged to report on indebtedness information as at a date that is different from and earlier than the date used for the purpose of the final investment circular. The reporting accountants would normally be in a position to issue a letter on the factual findings in respect of the agreed-upon procedures performed regarding the indebtedness position as at the earlier date, even though the Statement of Indebtedness is expected to be updated in the final investment circular, provided that the agreed-upon procedures have been performed and subject to the relevant requirements set forth in HKSRS 4400 and in this HKSIR.
59. An example letter on a Statement of Indebtedness is set out in Appendix 3 to this HKSIR.

Appendix 1

Example letter on a Profit Forecast

The following example letter is provided for illustrative purposes only. It is intended to be used only as a guide to the possible form and content of a letter that reporting accountants may wish to provide, and is not intended to suggest standard wording to be used in any particular set of circumstances.

(letterhead of reporting accountants)

The Board of Directors
XYZ Limited

Sponsor Limited

Date

Dear Sirs,

[XYZ Limited] ("the Company")

Profit [Forecast]/[Estimate] for [Period/Year][Ending/Ended][Date]

We refer to the [forecast]/[estimate] of the [combined]/[consolidated] profit attributable to equity holders of the Company for the [period/year][ending/ended] [date] ("the Profit [Forecast]/[Estimate]") set forth in the section headed [Financial Information] in the prospectus of the Company dated [date] ("the Prospectus").

Directors' Responsibilities

The Profit [Forecast]/[Estimate] has been prepared by the directors of the Company based on the audited [combined]/[consolidated] results of the Company and its subsidiaries (collectively referred to as "the Group") for the [x] months ended [date], the unaudited [combined]/[consolidated] results based on the management accounts of the Group for the [x] months ended [date] and [a forecast]/[an estimate] of the [combined]/[consolidated] results of the Group for the remaining [x] months [ending]/[ended] [date].

The Company's directors are solely responsible for the Profit [Forecast]/[Estimate].

Our Independence and Quality Control

We have complied with the independence and other ethical requirements of the *Code of Ethics for Professional Accountants* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.

The firm applies Hong Kong Standard on Quality Control 1¹ and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

Reporting Accountants' Responsibilities

Our responsibility is to express an opinion on the accounting policies and calculations of the Profit [Forecast]/[Estimate] based on our procedures.

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 500, *Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness* and with reference to Hong Kong Standard on Assurance

Engagements 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* issued by the HKICPA. Those standards require that we plan and perform our work to obtain reasonable assurance as to whether, so far as the accounting policies and calculations are concerned, the Company's directors have properly compiled the Profit [Forecast]/[Estimate] in accordance with the [bases and assumptions][bases] adopted by the directors and as to whether the Profit [Forecast]/[Estimate] is presented on a basis consistent in all material respects with the accounting policies normally adopted by the Group. Our work is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing issued by the HKICPA. Accordingly, we do not express an audit opinion.

Opinion

In our opinion, so far as the accounting policies and calculations are concerned, the Profit [Forecast]/[Estimate] has been properly compiled in accordance with the [bases and assumptions][bases] adopted by the directors as set out in Appendix [x] of the Prospectus and is presented on a basis consistent in all material respects with the accounting policies normally adopted by the Group as set out in our accountants' report dated [date], the text of which is set out in Appendix [x] of the Prospectus.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong

Note

1. *HKSQC 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements.*
2. *If any assumption used in the preparation of the Profit Forecast appears to the reporting accountants to be unrealistic or if any important assumption has been omitted in the forecast, the reporting accountants should include an appropriate comment in the letter. The comment should ordinarily be included in a separate section after the opinion paragraph.*

The reporting accountants may also include an additional paragraph in the separate section after the opinion paragraph to draw users' attention in the case that the Profit Forecast involves assumptions of a high level of uncertainty, such as the projected change in fair value of investment properties during the forecast period. An example paragraph is set out below:

"Other Matter

We draw attention to Section [X] of Appendix [X] headed "Bases and Assumptions" on pages [xx] to [xx] of the Prospectus which sets out the assumptions adopted by the directors of the Company regarding the fair value of the Group's investment properties as at [31 December 20X3]. In preparing the Profit Forecast, the directors of the Company have assumed that there will be an increase in the amount of [x] in the fair value of the Group's investment properties from [date] to [31 December 20X3]. The actual increase or decrease in the fair value of the Group's investment properties is likely to be different from the amount estimated or forecast. Any difference between the actual increase or decrease in the fair value of the Group's investment properties during the period from [date] to [31 December 20X3] when compared to the amount as estimated by the directors of the Company would have the effect of increasing or decreasing the consolidated profit of the Group for the year ending [31 December 20X3] attributable to equity holders of the Company. Our opinion is not qualified in respect of this matter."

Appendix 2

Example letter on a Working Capital Statement

The following example letter is provided for illustrative purposes only. It is intended to be used only as a guide to the possible form and content of a letter that reporting accountants may wish to provide, and is not intended to suggest standard wording to be used in any particular set of circumstances.

Example 1 - upon issue of the investment circular

(letterhead of reporting accountants)

The Board of Directors
XYZ Limited

Date

Dear Sirs,

[XYZ Limited] ("the Company")

Directors' Statement of Sufficiency of Working Capital

We refer to the board memorandum dated [date] which has been prepared by the directors of the Company in connection with their statement relating to the sufficiency of working capital of the Company and its subsidiaries (collectively referred to as "the Group") ("the Statement") contained in section headed [Working Capital Statement] in the investment circular dated [date] ("Investment Circular"). Copies of the board memorandum and extracts of the Investment Circular, for which the directors of the Company are solely responsible, are attached hereto and stamped by us solely for the purpose of identification.

Directors' Responsibilities

The Company's directors are solely responsible for the Statement and the board memorandum, including the working capital forecast therein, in support of the Statement.

Our Independence and Quality Control

We have complied with the independence and other ethical requirements of the *Code of Ethics for Professional Accountants* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.

The firm applies Hong Kong Standard on Quality Control 1¹ and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

Reporting Accountants' Responsibilities

Our responsibility is to express an opinion on the Statement and to report our opinion to you.²

We conducted our engagement in accordance with the terms of our engagement letter dated [date] and Hong Kong Standard on Investment Circular Reporting Engagements 500, *Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness* and with reference to Hong Kong Standard on Assurance Engagements 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* issued by the HKICPA. Those standards require that we plan and perform our work to obtain reasonable assurance as to whether the Company's directors have made the Statement, in the form and context in which it is made, after due and careful enquiry. Our work was limited primarily to making inquiries of the Company's management, considering the analyses and assumptions on which the working capital forecast is based and applying analytical procedures to financial data in the working capital forecast. It is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing issued by the HKICPA. Accordingly, we do not express an audit opinion.

Opinion

On the basis of our procedures, we report that:

- (a) in our opinion, the Statement has been made by the directors of the Company after due and careful enquiry; and
- (b) the persons or institutions providing finance have confirmed in writing the existence of such facilities as of [date] that are shown to be required by the Company's working capital forecast.^{3, 4}

Other Matters

Without qualifying our opinion, we draw your attention to the sensitivity factors set out in paragraph [x] of the board memorandum.

Furthermore, the Statement is based on the Company's forecasts and estimation of future transactions and cash flows and other assumptions about the future. Actual cash flows are likely to be different from those estimated or forecast since anticipated events frequently do not occur as expected and unforeseen events may arise, and their impact on estimates and forecasts may be material.

We make no representation regarding the sufficiency for your purposes of the aforementioned procedures.

Intended Users and Purpose

This letter has been prepared in connection with [the proposed listing of the Company's shares on The Stock Exchange of Hong Kong Limited]⁵. It should not be relied upon by any party for any other purpose and we expressly disclaim any liability or duty to any party in this respect. It should not be disclosed, referred to or quoted in whole or in part without our prior written consent, nor is it to be filed with or referred to in whole or in part in the Investment Circular or any other document, except that references may be made to its existence in (i) contracts among any of the Company, [Name of sponsor(s)] and ourselves and (ii) any communications in relation to the [proposed listing] among any of the Company, [Name of sponsor(s)] and ourselves, and a copy of this letter may be included in the bible of transaction documents memorialising the [proposed listing] prepared for the Company. Nothing in the preceding sentence shall prevent [Name of sponsor(s)] from disclosing this letter to [their][its] professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements [Name of sponsor(s)] [are][is] complying with.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong

cc [Name of sponsor(s)]
The Stock Exchange of Hong Kong Limited
Securities and Futures Commission

Notes

1. *HKSQC 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements.*
2. *Reporting accountants may consider it appropriate to clarify to whom they are responsible here or elsewhere in the report in accordance with their risk management policies and reference to Professional Risk Management Bulletin No. 2 "Auditors' Duty of Care To Third Parties and The Audit Report". Example text is included under "Intended Users and Purpose" of this example letter.*
3. *Where the requested confirmations have not been returned, the reporting accountants should seek to obtain suitable alternative evidence such as checking to the underlying agreements or having sighted a letter from the Issuer's bankers confirming banking facilities that is addressed to the Issuer. The extent of facilities covered by direct confirmations and alternative evidence should be clearly stated in the opinion. In such situation, opinion (b) can be replaced and (c) included, as follows:*
 - (b) *the persons or institutions providing finance have confirmed to us in writing the existence of the facilities in the amount of [amount covered by direct confirmations received] as of [date] that are shown to be required by the Company's working capital forecast; and*
 - (c) *direct confirmations have not been received as of the date of this letter for facilities in the amount of [amount of which direct confirmations have not been received] that are shown to be required by the Company's working capital forecast. We have relied on the [the source document reviewed as alternative procedures, e.g. signed loan agreements] between the [lenders] [facility providers] and the Company as alternative evidence of the existence of these facilities."*
4. *If no facilities are shown to be required, opinion (b) can be modified as "(b) no facilities are shown to be required by the Company's working capital forecast".*
5. *Or state other purpose where appropriate.*

Example 2 - upon the listing applicant's sponsor providing a final confirmation letter on the Working Capital Statement before a listing document is bulk-printed in the case of new listing of equity securities

(letterhead of reporting accountants)

The Board of Directors
XYZ Limited

Date

Dear Sirs,

[XYZ Limited] ("the Company")

Directors' Statement of Sufficiency of Working Capital

We refer to the board memorandum dated [date] which has been prepared by the directors of the Company in connection with their statement relating to the sufficiency of working capital of the Company and its subsidiaries (collectively referred to as "the Group") ("the Statement") contained in section headed [Working Capital Statement] therein. A copy of the board memorandum, for which the directors of the Company are solely responsible, is attached hereto and stamped by us solely for the purpose of identification.

Directors' Responsibilities

The Company's directors are solely responsible for the Statement and the board memorandum, including the working capital forecast therein, in support of the Statement.

Our Independence and Quality Control

We have complied with the independence and other ethical requirements of the *Code of Ethics for Professional Accountants* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behavior.

The firm applies Hong Kong Standard on Quality Control 1¹ and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

Reporting Accountants' Responsibilities

Our responsibility is to express an opinion on the Statement and to report our opinion to you.²

We conducted our engagement in accordance with the terms of our engagement letter dated [date] and Hong Kong Standard on Investment Circular Reporting Engagements 500, *Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness* and with reference to Hong Kong Standard on Assurance Engagements 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* issued by the HKICPA. Those standards require that we plan and perform our work to obtain reasonable assurance as to whether the Company's directors have made the Statement, in the form and context in which it is made, after due and careful enquiry. Our work was limited primarily to making inquiries of the Company's management, considering the analyses and assumptions on which the working capital forecast is based and applying analytical procedures to financial data in the working capital forecast. It is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing issued by the HKICPA. Accordingly, we do not express an audit opinion.

Opinion

On the basis of our procedures, we report that:

- (a) in our opinion, the Statement has been made by the directors of the Company after due and careful enquiry; and
- (b) the persons or institutions providing finance have confirmed in writing the existence of such facilities as of [date] that are shown to be required by the Company's working capital forecast.^{3, 4}

Other Matters

Without qualifying our opinion, we draw your attention to the sensitivity factors set out in paragraph [x] of the board memorandum.

Furthermore, the Statement is based on the Company's forecasts and estimation of future transactions and cash flows and other assumptions about the future. Actual cash flows are likely to be different from those estimated or forecast since anticipated events frequently do not occur as expected and unforeseen events may arise, and their impact on estimates and forecasts may be material.

We make no representation regarding the sufficiency for your purposes of the aforementioned procedures.

Intended Users and Purpose

This letter has been prepared in connection with [the proposed listing of the Company's shares on The Stock Exchange of Hong Kong Limited]⁵. It should not be relied upon by any party for any other purpose and we expressly disclaim any liability or duty to any party in this respect. It should not be disclosed, referred to or quoted in whole or in part without our prior written consent, nor is it to be filed with or referred to in whole or in part in the [prospectus for the proposed listing] or any other document, except that references may be made to its existence in (i) contracts among any of the Company, [Name of sponsor(s)] and ourselves and (ii) any communications in relation to the [proposed listing] among any of the Company, [Name of sponsor(s)] and ourselves, and a copy of this letter may be included in the bible of transaction documents memorialising the [proposed listing] prepared for the Company. Nothing in the preceding sentence shall prevent [Name of sponsor(s)] from disclosing this letter to [their][its] professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements [Name of sponsor(s)] [are][is] complying with.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong

cc Name of sponsor(s)
The Stock Exchange of Hong Kong Limited
Securities and Futures Commission

Notes

1. *HKSQC 1, Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements.*
2. *Reporting accountants may consider it appropriate to clarify to whom they are responsible here or elsewhere in the report in accordance with their risk management policies and reference to Professional Risk Management Bulletin No. 2 "Auditors' Duty of Care To Third Parties and The Audit Report". Example text is included under "Intended Users and Purpose" of this example letter.*
3. *Where the requested confirmations have not been returned, the reporting accountants should seek to obtain suitable alternative evidence such as checking to the underlying agreements.*

REPORTING ON PROFIT FORECASTS, STATEMENTS OF SUFFICIENCY OF WORKING CAPITAL AND STATEMENTS OF INDEBTEDNESS

The extent of facilities covered by direct confirmations and alternative evidence should be clearly stated in the opinion. In such situation, opinion (b) can be replaced and (c) included, as follows:

- (b) the persons or institutions providing finance have confirmed to us in writing the existence of the facilities in the amount of [amount covered by direct confirmations received] as of [date] that are shown to be required by the Company's working capital forecast; and*
 - (c) direct confirmations have not been received as of the date of this letter for facilities in the amount of [amount of which direct confirmations have not been received] that are shown to be required by the Company's working capital forecast. We have relied on the [the source document reviewed as alternative procedures, e.g. signed loan agreements] between the [lenders][facility providers] and the Company as alternative evidence of the existence of these facilities."*
4. *If no facilities are shown to be required, opinion (b) can be modified as "(b) no facilities are shown to be required by the Company's working capital forecast".*
 5. *Or state other purpose where appropriate.*

Appendix 3

Example letter on a Statement of Indebtedness

The following example letter is provided for illustrative purposes only. It is intended to be used only as a guide to the possible form and content of a letter that reporting accountants may wish to provide, and is not intended to suggest standard wording to be used in any particular set of circumstances. The contents of the letter will vary according to the procedures agreed between reporting accountants, the Issuer and sponsors, where appropriate.

(letterhead of reporting accountants)

The Board of Directors
XYZ Limited

Date

Dear Sirs,

Statement of Indebtedness

This letter is written to you pursuant to the terms agreed between us in our engagement letter dated [date]. For the purpose of this letter, we have carried out the procedures agreed with you as set out below with regard to the attached statement of indebtedness and contingent liabilities of [XYZ Limited] ("the Company") and its subsidiaries (collectively referred to as "the Group") as at [most recent practicable date]¹ ("the Statement") prepared by the directors of the Company for inclusion in the investment circular dated [date]² ("Investment Circular"). We carried out our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 500 "Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness" and with reference to Hong Kong Standard on Related Services ("HKSRs") 4400 "Engagements to Perform Agreed-upon Procedures Regarding Financial Information" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

Our work in respect of the Statement has in turn been based on a schedule of indebtedness ("Schedule") prepared by the directors of the Company from the Group's accounting records in support of the Statement.

Both the Statement and Schedule are the sole responsibility of the directors of the Company. Copies of the Statement and Schedule are attached hereto and stamped by us for the purpose of identification only.

1. Bank loans and overdrafts, debt securities and other borrowings, mortgages and charges³
 - a. [We have compared the amounts shown on the Statement with the relevant amounts included in the Schedule and found them to be in agreement [or state the differences, if any].]
 - b. [We have enquired of management whether reconciliations have been prepared where amounts in the Schedule are different to the amounts in the relevant bank statements at the relevant date. Management have confirmed that these reconciliations have been appropriately performed and reviewed⁴.
 - c. [We have requested confirmations from the banks[, the relevant trustee]⁵ and other providers of finance listed on the Schedule confirming the balances with them and the mortgages and charges at that date. We have compared the amounts shown on the confirmations with the relevant amounts included in the Schedule and found the amounts to be in agreement or where the amounts confirmed were different to the amounts in the [Company/Group]'s books and records, we traced them to reconciliations prepared by the [Company/Group] and found them to be in agreement. We have indicated on the Schedule those balances, mortgages and charges which have been directly confirmed to us. [We have not received confirmations in respect of balances which account for [x]%

of the amount included on the Schedule and have noted alternative sources of evidence on the Schedule (*e.g. bank statements where available*).]]

- d. [We have compared the amounts of debt securities shown in the Schedule to copies of agreements made available to us by the [Company/Group] and found the amounts noted to be in agreement];

2. Lease liabilities^{6, 7}

- a. [We have compared the amounts shown on the Statement with the relevant amounts included in the Schedule and found them to be in agreement [*or state the differences, if any*].]
- b. [We have compared the amounts of lease liabilities shown in the Schedule to lease liabilities calculation schedules prepared by management and found them to be in agreement. We have compared the lease periods and the lease payments as adopted in the lease liabilities calculations to relevant copies of lease agreements made available to us by the Group and found them to be in agreement. We have checked the arithmetical accuracy of the lease liabilities calculation schedules and found them to be arithmetically accurate]^{6, 7}

3. Contingent liabilities or guarantees⁶

In relation to contingent liabilities or guarantees we have:

- a. [compared the amounts shown on the Statement with the relevant amounts included in the Schedule and found them to be in agreement [*or state the differences, if any*];]
- b. [read the items on the Schedule which, in the view of the directors of the Company, would at [latest practicable date] be expected to be disclosed pursuant to [Hong Kong Accounting Standard ("HKAS") /International Accounting Standard ("IAS")] 37 "Provisions, Contingent Liabilities and Contingent Assets" in any financial statements of the [Company/Group] were they to be prepared at that date;]
- c. [read the minutes of board meetings and made inquiries of management with responsibility for financial and accounting matters as to whether they are aware of any other contingent liabilities which, in their view would be expected to be disclosed pursuant to [HKAS/IAS] 37 in any published financial statements of the Company were they to be prepared at the [latest practicable date]⁴;]
- d. [requested confirmations from the banks listed on the Schedule confirming the amounts of guarantees at that date. We have compared the amounts shown on the confirmations with the relevant amounts included in the Schedule and found the amounts to be in agreement. We have indicated on the Schedule those amounts which have been directly confirmed to us. [We have not received confirmations in respect of amounts of guarantees which account for [x]% of the amount included on the Schedule and have noted alternative sources of evidence on the Schedule (*e.g. bank letters where available*);]
- e. [noted on the Schedule the sources of evidence in support of the amounts disclosed by the Company.]

We have placed reliance on representations from the directors of the Company as to the completeness of the amounts shown in the Statement and Schedule.

We make no representations regarding questions of legal interpretation or regarding the sufficiency for your purposes of the aforementioned procedures; also, such procedures do not constitute an assurance engagement performed in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the HKICPA, and therefore would not necessarily reveal any material misstatement of the amounts or percentages or ratios listed above. We do not express any assurance on the Statement or Schedule. Further, we

have addressed ourselves solely to the foregoing data in the Investment Circular and we make no representations regarding the adequacy of disclosures or regarding whether any material facts have been omitted.

This letter has been prepared in connection with [the proposed listing of the Company's shares on The Stock Exchange of Hong Kong Limited]⁸. It should not be relied upon by any party for any other purpose and we expressly disclaim any liability or duty to any party in this respect. It should not be disclosed, referred to or quoted in whole or in part without our prior written consent, nor is it to be filed with or referred to in whole or in part in the Investment Circular or any other document, except that references may be made to its existence in (i) contracts among any of the Company, [Name of sponsor(s)] and ourselves and (ii) any communications in relation to the [proposed listing] among any of the Company, [Name of sponsor(s)] and ourselves, and a copy of this letter may be included in the bible of transaction documents memorialising the [proposed listing] prepared for the Company. Nothing in the preceding sentence shall prevent [Name of sponsor(s)] from disclosing this letter to [their][its] professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements [Name of sponsor(s)] [are][is] complying with.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong

[cc [Name of sponsor(s)]]

Notes

1. *Most recent practicable date is a date normally no more than*
 - *two calendar months prior to the date of the Application Proof or the final listing document, in the case of a listing of new equity securities; or*
 - *eight calendar weeks prior to the date of the investment circular, in the case of notifiable transactions.*
2. *In the case that where the reporting accountants are reporting on the information in an Application Proof, "investment circular dated [date]" should be amended as "draft listing document to be submitted to The Stock Exchange of Hong Kong Limited"*
3. *Details of mortgages and charges are also a legal issue, in respect of which the Issuer and sponsor may need to discuss with the Issuer's legal advisors.*
4. *Management's confirmation could be obtained in the form of management representation.*
5. *May be applicable in the case of debentures.*
6. *To be included where applicable.*
7. *These are sample procedures for lease liabilities. Reporting accountants should discuss and agree with the Company on the extent of scope and specific procedures to be performed, in particular when a large quantity of lease contracts is involved.*
8. *Or state other purpose where appropriate.*