Assessment of risks of engagements involving public interest entities

"The assessment of risks is a matter of professional judgment, rather than a matter capable of precise measurement." (HKSA 200)

Transactions associated with complex accounting issues are not uncommon in listed entities. Those accounting issues may involve consideration of, *inter alia*, accounting estimates and fair value measurement which are examples of challenging aspects of auditing. Listed entity audit engagements are generally considered as "higher risk."

Engagements on regulated industries will also require specific skills and resources. Examples include solicitors' accounts, compliance reports of entities regulated under the Securities and Futures Ordinance, authorized institutions under the Banking Ordinance, insurance brokers and insurers.

To manage audit or engagement risks at the outset, identifying risks by carrying out procedures for client and engagement acceptance is an essential step.

HKSQC 1 requires practice units to establish policies and procedures for the acceptance and continuance of client relationships and specific engagements. The standard emphasizes that such policies and procedures should be designed to provide the practice units with reasonable assurance that they will only undertake or continue relationships and engagements where the practice units have the capabilities, time and resources to perform the engagements and comply with relevant ethical requirements.

Section 210 *Professional Appointment* of the *Code of Ethics for Professional Accountants* states that the fundamental principle of professional competence and due care imposes an obligation on CPAs in public practice to provide only those services that they are competent to perform. If the engagement team does not possess, or cannot acquire, the competencies necessary to properly carry out the engagement, it is an example of a self-interest threat to professional competence and due care.

Disciplinary case

Below is extracted from the Reasons for Decision of a disciplinary case handed down by a Disciplinary Committee of the Institute in 2012:

"The... audit deficiencies identified in the complaint not only demonstrate mere slips or misjudgment but a serious incompetence on the part of the respondent. The respondent acknowledged his incompetence but attributed it to the more demanding nature of the audit of listed companies. He also admitted that he lacked the required manpower to cope with the audit of listed companies. Yet the respondent was prepared to take up audit for listed companies when he himself was incompetent to handle the work and he was not assisted by any competent staff..."

The CPA concerned had his practising certificate cancelled and he was not issued with a practising certificate for two calendar years.

Extracts of Reasons and Orders of past disciplinary cases issued by Disciplinary Committees are available at the Institute's website at *www.hkicpa.org.hk*.

HKSQC 1 contains related guidance when a practice unit considers whether it has the competence, capabilities and resources to undertake a new engagement. Section 210 *Professional Appointment* also contains examples of safeguards that can be applied by CPAs in practice to eliminate threats to professional competence and due care or reduce the threats to an acceptable level.

It is reiterated that members should carry out procedures for the acceptance and continuance of engagements to ensure that they have involved the right people with the right skill sets to complete the engagements within the required time limit.

Institute resources

- Section 210 *Professional Appointment* of the *Code of Ethics for Professional Accountants* (Volume I of Members' Handbook)
- HKSQC 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* (Volume III of Members' Handbook)
- Standards on auditing, standards on assurance engagements, practice notes, etc. can be found in Volume III of Members' Handbook.

This article is contributed by the Institute's Compliance Department