

## Appendix 1

### Example of an Audit Engagement Letter

*The following is an example of an audit engagement letter for an audit of general purpose financial statements of a company which is incorporated in Hong Kong under the Companies Ordinance but do not take advantage of the reporting exemption in the Companies Ordinance. This letter is not authoritative but is intended only to be a guide that may be used in conjunction with the considerations outlined in this HKSA. It will need to be varied according to individual requirements and circumstances, for example to the special reporting requirements of regulated entities. It may be appropriate to seek legal advice that any proposed letter is suitable.*

To the directors of [ABC Company Limited]:

#### Objective of services

~~1.1~~ 4.4-You have requested that we audit the (consolidated)\* financial statements of ABC Company Limited ("the Company") (and its subsidiaries)\*. We are pleased to confirm our acceptance and our understanding of this audit engagement by means of this letter.

~~1.2 Our audit will be conducted with the~~ The objectives of our audit are to obtain reasonable assurance about whether the (consolidated)\* financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our expressing an opinion on the (consolidated)\* financial statements. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Hong Kong Standards on Auditing ("HKSA") will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these (consolidated)\* financial statements.

#### Responsibilities of directors

- 2.1 Our audit will be conducted on the basis that you acknowledge and understand that you have responsibility:
- a. To prepare (consolidated)\* financial statements which give a true and fair view of the financial position of the Company (and its subsidiaries)\* as at the end of the financial year and of [its][their] financial performance for the financial year in accordance with [insert applicable financial reporting framework] [Hong Kong Financial Reporting Standards][Hong Kong Financial Reporting Standard for Private Entities] and the Companies Ordinance ("CO");
  - b. (To ensure the subsidiary, if any, of the Company keeps accounting records that are sufficient for the Company to prepare (consolidated)\* financial statements that comply with a. above.)\*
  - c. To take all reasonable steps to ensure the Company keeps sufficient accounting records which show and explain the transactions of the Company (and its subsidiaries)\*, disclose with reasonable accuracy, at any time, the financial position and financial performance of the Company (and its subsidiaries)\*;
  - d. To ensure that the (consolidated)\* financial statements comply with section 383 (Notes to Financial Statements to Contain Information on Directors' Emoluments etc) of the CO which must contain in the notes to the financial statements, the information prescribed by the Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G);

- e. For such internal control as you determine is necessary to enable the preparation of (consolidated)\* financial statements that are free from material misstatement, whether due to fraud or error;
  - f. To provide us with<sup>1</sup>:
    - (i) Access to all information of which you are aware that is relevant to the preparation of the (consolidated)\* financial statements such as Company's accounting records and all other relevant records and documentation, including minutes of all management and shareholders' meetings and other matters;
    - (ii) Additional information that we may request from you for the purpose of the audit; and
    - (iii) Unrestricted access to persons related to the Company (and its subsidiaries)\* from whom we determine it necessary to obtain audit evidence;
  - g. To provide us with (i) any proposed written resolution and (ii) any other document relating to the resolution that is required to be sent to a member of the Company, on or before the circulation of written resolution to a member of the Company; and
  - h. To notify us any passed written resolution within 15 days after resolution is passed.
- 2.2 You are also responsible for the preparation and approval of the directors' report in accordance with the CO [as well as the other information included in the annual report]<sup>#</sup>.

### Responsibilities of the auditor

- 3.1 We have a statutory responsibility to prepare a report to the members to state whether in our opinion the (consolidated)\* financial statements give a true and fair view of the financial position and financial performance of the Company (and its subsidiaries)\* for the financial year and whether they have been properly prepared in compliance with the CO. We shall also state our opinion in the auditor's report if we are of the opinion that:
- a. adequate accounting records have not been kept by the Company (and its subsidiaries)\*; or
  - b. the (consolidated)\* financial statements are not in agreement with the accounting records in any material respect; and

We shall also state the fact in the auditor's report if we have failed to obtain all the information or explanations that, to the best of our knowledge and belief, are necessary and material for the purpose of the audit.

In addition, where the (consolidated)\* financial statements do not contain information on directors' emoluments, etc under section 383(1) of the CO, the CO requires us to include in our report, as far as we are reasonably able to do so, a statement giving the particulars that are required to be, but have not been, contained in the (consolidated)\* financial statements.

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<sup>1</sup> See paragraph A23 for examples of other matters relating to management's responsibilities that may be included.

- 3.2 We have a professional responsibility to report if the (consolidated)\* financial statements do not comply in any material respect with *[insert applicable financial reporting framework] [Hong Kong Financial Reporting Standards][Hong Kong Financial Reporting Standard for Private Entities]*, unless in our opinion the noncompliance is justified in the circumstances. In determining whether or not the departure is justified, we consider:
- whether the departure is required in order for the (consolidated)\* financial statements to give a true and fair view; and
  - whether adequate disclosure has been made concerning the departure.
- 3.3 We are required to read the information in the directors' report for the financial year to identify and report inconsistencies with the (consolidated)\* financial statements. As required by the CO, if we are of the opinion that the information in the directors' report for a financial year is not consistent with the (consolidated)\* financial statements for the financial year, we shall state that opinion in our auditor's report; and we may bring that opinion to the members' attention at a general meeting. However, we are not required to audit or review the director's report and accordingly we will not express an opinion or review conclusion or any assurance on it.
- 3.4 We are required to read the other information included in the annual report. This responsibility applies regardless of whether the other information is made available to us prior to, or after, the date of the auditor's report. We will consider whether the other information is materially inconsistent with the (consolidated)\* financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is an uncorrected material misstatement of this other information, we are required to include that fact in the auditor's report. Our opinion on the (consolidated)\* financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon. If we conclude that a material misstatement exists in other information obtained after the date of the auditor's report and the other information is not corrected after communicating with those charged with governance, we will take appropriate actions considering our legal rights and obligations.] #

## Scope of audit

- 4.1 Our audit will be conducted in accordance with ~~Hong Kong Standards on Auditing ("HKSA")~~ issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements. As part of an audit in accordance with HKSAs, we exercise professional judgment and maintain professional skepticism throughout and plan and perform the audit to obtain reasonable assurance about whether the (consolidated)\* financial statements are free from material misstatement. An audit involves We also:
- ~~performing procedures to obtain audit evidence about the amounts and disclosures in the (consolidated)\* financial statements. The procedures selected depend on the auditor's judgment, including the assessment of~~ identify and assess the risks of material misstatement of the (consolidated)\* financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
  - Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of

expressing an opinion on the effectiveness of the entity's internal control.<sup>2</sup> However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the (consolidated)\* financial statements that we have identified during the audit. Any such report may not be provided to third parties without our prior written consent. Such consent will be granted only on the basis that such reports are not prepared with the interests of anyone other than the Company in mind and that we accept no duty or responsibility to any other party as concerns the reports.

- c. ~~An audit also includes evaluating~~Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by you, ~~as well as~~
- d. ~~Conclude on the appropriateness of your use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.~~
- e. ~~evaluating~~ Evaluate the overall presentation, structure and content of the (consolidated)\* financial statements, including the disclosures, and whether the (consolidated)\* financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

4.2 Because of the inherent limitations of an audit, together with the inherent limitations of internal control, there is an unavoidable risk that some material misstatements may not be detected, even though the audit is properly planned and performed in accordance with HKSA's.

~~4.3 In making our risk assessments, we consider internal control relevant to the entity's preparation of the (consolidated)\* financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. However, we will communicate to you in writing concerning any significant deficiencies in internal control relevant to the audit of the (consolidated)\* financial statements that we have identified during the audit. Any such report may not be provided to third parties without our prior written consent. Such consent will be granted only on the basis that such reports are not prepared with the interests of anyone other than the Company in mind and that we accept no duty or responsibility to any other party as concerns the reports.~~

(4.43) In connection with the audit of the consolidated financial statements, we draw your attention to section 412 of the CO which gives the rights to the auditor of the holding company to require a person that is a related entity of the company to provide any information or explanation that the auditor reasonably requires for the performance of the duties as auditor of the holding company. As defined in section 412 of the CO, a related entity includes an auditor of a subsidiary undertaking.

4.54 In order to express an opinion on the consolidated financial statements which include the financial information of subsidiaries, joint arrangements or associates of which we are not the auditor, it will be necessary for us to communicate directly with the other auditor(s) concerned to satisfy ourselves that:

<sup>2</sup> This sentence would be modified, as appropriate, in circumstances when the auditor also has responsibility to issue an opinion on the effectiveness of internal control in conjunction with the audit of the financial statements

- a. so far as is practicable, there is uniformity within the Company and its subsidiaries in the application of accounting policies;
  - b. the consolidated financial statements contain the information required by the CO, applicable accounting standards and any other legislation or non-statutory requirements affecting the presentation of financial statements; and
  - c. all material aspects of the consolidated financial statements have been subjected to an audit, the nature and extent of which is adequate and reasonable, in our view, for the purpose of forming an opinion on the consolidated financial statements.)\*
- 4.6-5 As part of our audit procedures, we will request you to provide written confirmation concerning representations which we have received from you during the course of the audit in connection with the audit. In connection with representations and the supply of information to us generally, we draw your attention to section 412 of the CO which sets out the rights of the auditor in relation to obtaining information from a person that is a related entity as defined in this section of the CO. You are also referred to section 413 of the CO which sets out the offences relating to section 412 of the CO.
- 4.7-6 In order to assist us with the audit of your (consolidated)\* financial statements, we shall request sight of all documents or statements, including the chairman's statement, operating and financial review and the directors' report, which are due to be issued with the (consolidated)\* financial statements. We are also entitled to attend all general meetings of the Company and to receive notice of all such meetings.
- 4.8-7 The responsibility for safeguarding the assets of the Company (and its subsidiaries)\* and for the prevention and detection of fraud, error and non-compliance with law or regulations rests with you. However, we shall endeavour to plan our audit so that we have a reasonable expectation of detecting material misstatements in the (consolidated)\* financial statements or books of account (including those resulting from fraud, error or non-compliance with law or regulations), but our audit should not be relied upon to disclose all such material misstatements or frauds, errors or instances of non-compliance as may exist.
- 4.9-8 (Where appropriate - Note) We shall not be treated as having notice, for the purposes of our audit responsibilities, of information provided to members of our firm other than those engaged on the audit (for example information provided in connection with accounting, taxation and other services).
- 4.10-9 Once we have issued our report we have no further direct responsibility in relation to the (consolidated)\* financial statements for that period. However, you agree that you will inform us of any material event occurring between the date of our report and that of the Annual General Meeting which may affect the (consolidated)\* financial statements.

## Reporting

- 5.1 *[Insert appropriate reference to the expected form and content of the auditor's report including, if applicable, the reporting on other information in accordance with HKSA 720 (Revised).]*
- 5.2 The form and content of our report may need to be amended in the light of our audit findings.

## (Other services

6. You have requested that we provide other services in respect of ..... The terms under which we provide these other services are dealt with in a separate letter.)\*

## Fees

7. Our fees are computed on the basis of the time spent on your affairs by our partners and our staff and on the levels of skill and responsibility involved plus out-of-pocket expenses. Unless otherwise agreed, our fees will be billed at appropriate intervals during the course of the audit and will be due on presentation.

## Agreement of terms

- 8.1 Once it has been agreed, this letter will remain effective, from one audit appointment to another, until it is replaced. Please sign and return the enclosed copy of this letter to indicate your acknowledgement of, and agreement with, the arrangements for our audit of the (consolidated)\* financial statements including our respective responsibilities.
- (8.2 Since the terms of our engagement as auditors of the subsidiaries listed in the attached appendix are the same, we will not send separate letters to the board of directors of each subsidiary. We would therefore be grateful if you would forward copies of this letter to the boards of directors of each such subsidiary and confirm that these boards have also agreed and confirmed their acceptance of this letter.)\*

Yours faithfully,

ABC & Co.

Certified Public Accountants (Practising) [or Certified Public Accountants]

Date

We agree to the terms of this letter.

(Signed)

.....

Director, for and on behalf of the board of

Date

\* Delete where not applicable.

## Note

*When accounting, taxation or other services are undertaken on behalf of an audit client, information may be provided to members of the audit firm other than those engaged on the audit. In such cases, it may be appropriate for the audit engagement letter to include this or a similar paragraph to indicate that the auditor is not to be treated as having notice, for the purposes of the auditor's responsibilities, of such information, to make it clear that a company would not be absolved from informing the auditor directly of a material matter.*

<sup>#</sup> applicable where the company prepares an annual report which contain other information in addition to the directors' report.