

AFRC Quarterly Report

19 April 2023



Highlights

- We published the results of a study on recent trends in audit fees for Hong Kong listed entities and of a survey on the implementation of our Guidelines on Effective Audit Committees – Selection, Appointment and Reappointment of Auditors.
- We presented our budget for financial year 2023-24 to Members of the Legislative Council Panel on Financial Affairs on 17 March 2023.
- To help auditors prepare well for our upcoming inspections, we published our first Audit Focus publication.
- We held a celebratory event for practising certificate holders who have held their certificates for 50 years.

- We have highlighted the importance to auditors of having good anti-corruption practices.

All the details can be found as you turn the pages of this quarterly report.

Survey Report on implementation of our Guidelines for Effective Committees – Selection, Appointment and Reappointment of Auditors and Audit Fee Report

In promoting the quality of financial reporting and auditing and supporting the development of the accounting profession, the AFRC published two reports on [implementation of our Guidelines for the appointment of listed entity auditors in Hong Kong](#) and [recent trends in listed entity audit fees](#) in March 2023. In the reports, we called for auditors, audit committees, listed companies and institutional investors to develop a stronger focus on the appointment of auditors and the setting of audit fees, both of which are crucial in upholding the quality of financial reporting and audit in listed companies.

Survey Report

The Survey Report presents the results of AFRC's online survey, which highlights the practical realities facing auditors and audit committees in relation to auditor appointments and audit fee setting. Key findings include:

- (i) In terms of the implementation of the Guidelines, the picture is mixed. On the one hand, implementation of the Guidelines has been slow, however, on a more positive note, 97% of audit committee respondents agreed that they play a pivotal role in overseeing audit quality.
- (ii) Despite AFRC's efforts in promoting the importance of audit quality during auditor selection, listed companies still ranked proposed audit fees as one of the top three factors.
- (iii) Audit teams experienced frequent pressure to reduce fees and to issue a clean audit opinion.
- (iv) In three out of the four disclosure areas, more than half of the auditor respondents believed that disclosures by listed companies were not satisfactory.

Audit Fee Report

The Audit Fee Report provides an analysis of the audit fees paid by listed companies and analysed what effects, if any, COVID-19 and the ensuing economic downturn have had on the market. Key findings include:

- (i) Total audit fees in Hong Kong in 2021 were HK\$13.1 billion, representing a compound annual growth rate (CAGR) of 6.0% from 2010.
- (ii) On a per engagement basis, average and median audit fees were HK\$5.4 million and HK\$2.1 million respectively in 2021. When adjusted for inflation, average and median fees show a decline of 20% and 10% respectively since 2010.
- (iii) Even though the level of audit fees typically reflects the complexity in the underlying business, growth of average audit fees (9%) in Hong Kong between 2010 and 2021 significantly lags behind the growth experienced by listed companies (Average total assets: 91%; Average revenue: 67%).
- (iv) For local Category A PIE auditors, their market share has been in decline since peaking in 2019. This is most marked when measured by number of engagements.
- (v) There is a strong association between a change in auditors and a subsequent reduction in audit fees. Out of the 249 and 285 listed companies that changed auditors in 2020 and 2021, 80.7% and 69.5% experienced a fee reduction.

By raising awareness on a complicated issue, by providing guidance to the profession, and by calling for relevant stakeholders to act appropriately, we aim to raise the quality of financial reporting, with the ultimate goal of maintaining public trust and confidence in Hong Kong's capital markets.



Dr Kelvin Wong, Chairman (middle), Mr Marek Grabowski, CEO (right) and Ms Mary Leung, Head of Policy, Registration and Oversight (left) present to media The Survey Report and The Audit Fee Report.

Celebrating a major milestone for the accounting profession – 50th anniversary of the accounting profession

This year marks the 50th anniversary of the issuance of practising certificates to accounting professionals in Hong Kong. 26 certified public accountants have held their practising certificates for 50 years. It is a major milestone for them, for us, and for the wider profession. On 2 March 2023, the AFRC, as the issuer of practising certificates, hosted a celebratory reception to commemorate their Golden Jubilee.

At the reception, Dr Kelvin Wong, Chairman of the AFRC, Ms Mary Leung, Head of Policy, Registration and Oversight (PRO) and Ms Tracy Wong, Deputy Head of PRO extended a warm welcome to the 10 participants. They shared their observations and insights about the current accounting profession, as well as their inspiring career stories as accountants and practitioners. Their success serves as a powerful motivation for aspiring accounting professionals.

Dr Wong presented to each participant their practising certificates, as a special souvenir, to commemorate this major milestone.



AFRC hosts a reception to celebrate the 50th anniversary of the issuance of practising certificates to accounting professionals in Hong Kong.

Front row (from left to right):

Mr Li Kong Shing, Dr Lam Hoi Ham, Dr Li Kwok Po, David, Dr Kelvin Wong, Chairman of AFRC, Mr Cheng Kwok Wai, David, Mr Luk Shu Kuen

Back row (from left to right):

Ms Mary Leung, Head of Policy, Registration and Oversight, AFRC, Mr Ip Yin Wah, Mr Tam Kwan Ping, Ignatius, Mr Lo Kai Ming, Charles, Mr Yeung Lai Woo, Noohu, Ms Tracy Wong, Deputy Head of Policy, Registration and Oversight, AFRC

AFRC's Briefing at LegCo Panel on Financial Affairs on 2023-24 budget

On 17 March 2023, the AFRC briefed Members of the LegCo Panel on Financial Affairs on its [budget](#) for 2023-24.

At the briefing, Dr Kelvin Wong, Chairman of the AFRC highlighted to Members the latest developments, work progress and accomplishments of the AFRC. These included:

- (i) Organised 50 stakeholder engagement activities in the Consultation for the further reform, participated by 6,000 accounting and auditing professionals.
- (ii) Conducted 55 PIE engagement inspections, 6 non-PIE engagement inspections and 26 firm-wide quality control inspections.
- (iii) Conducted policy research that contributes to the enhancement of audit quality and corporate governance.

Mr Marek Grabowski, CEO of the AFRC, presented the budget and explained that in 2023-24, the AFRC would moderately increase the headcounts from the existing 115 to 145 to deal with the continuing progressive implementation of the non-PIE related functions and an increasing investigation workload in the PIE-related functions.

In response to a question on the salary increment of 3.7%, which was comparatively lower than other regulators, Dr Wong stressed that while the increment was not enough, the AFRC can effectively discharge its duties as the staff of the AFRC have a strong sense of mission in protecting the public interest. He also explained that due to the limited manpower in the Human Resources team, it would be more efficient to engage a recruitment agency to hire the additional 15 senior headcounts. However, it would not be a recurring practice.

Dr Wong stressed that the AFRC would continue to play its pivotal role in protecting the public interest and safeguarding Hong Kong's status as a competitive international financial centre.

- [Chairman's Speech at LegCo Panel on Financial Affairs on 2023-24 budget](#)
- [CEO's Speech at LegCo Panel on Financial Affairs on 2023-24 budget](#)

How to prepare for the next inspection?

With the expanded inspection powers being vested with the AFRC, the Inspection Department adopted the principle of proportionality and a risk-based approach to cover practice units (other than listed entity auditors) in its inspection programme.

For the 2023 inspection, the Department will not only assess the quality of a selection of audit and assurance engagements conducted by the practice units based on the applicable professional standards and legal and regulatory requirements, but also will evaluate the effectiveness of the practice units' systems of quality management. The Inspection Department will also commence its inspections of the practice units' compliance with the anti-money laundering and counterterrorist financing requirements.

To help auditors prepare well for our upcoming inspections, the Inspection Department issued our first year-end audit reminders in the form of our "[Audit Focus](#)" publication prior to the busy audit season in December 2022. During February 2023, the Inspection Department organized a webinar for listed entity auditors. The seminar enabled us to reiterate the importance of those key audit issues and areas that listed entity auditors should pay particular attention to.

As the busy audit season soon comes to an end and ahead of our expanded inspection this year, practice units and their auditors are suggested to:

- (i) Continue to pay particular attention to key areas of the audits as stated in the Audit Focus;
- (ii) Assess the sufficiency and appropriateness of the procedures performed in a compliance reporting engagement (i) in accordance with *Hong Kong Standard on Assurance Engagements 3000 (Revised) Assurance Engagements Other than Audits or Reviews of Historical Financial Information*, and (ii) with reference to *Practice Note 820 (Revised) The Audit of Licensed Corporations and Associated Entities of Intermediaries*, before forming a conclusion in the compliance report;
- (iii) Ensure that the assembly of final audit files is completed in a timely manner and that the final audit files contain all relevant working papers that support the audit opinion;
- (iv) Maintain sufficient documentation of the system of quality management and perform periodic monitoring procedures to ensure the system of quality management is in place to comply with the new and revised quality management standards that became effective on 15 December 2022; and
- (v) Keep abreast of the amendments that are relevant to a practice unit in the Anti-Money Laundering and Counter-Terrorist Financing (Amendment) Bill 2022, which will be effective in June 2023, and ensure compliance with the upcoming revised Guidelines on Anti-Money Laundering and Counter-Terrorist Financing for Professional Accountants in the Code of Ethics for Professional Accountants.

Our [policy statements](#) and [outlines of our inspection processes](#) for all practice units (including compliance with the anti-money laundering and counterterrorist financing requirements) are made available on the AFRC website. The Inspection Department will continue to conduct effective inspections to shape the behaviour that promotes a self-imposed improvement culture within practice units and to uphold audit quality across the profession.

The importance of anti-corruption practices to auditors

Some people may think that the exchange of gifts and hospitality is a widely-accepted and harmless way of fostering business relationships. They may not be aware that these and other inducements offered or accepted by an auditor could affect the auditor's integrity and objectivity and undermine the public's trust in his work. In some circumstances, this may even lead to a violation of the Prevention of Bribery Ordinance (POBO) as well as the Code of Ethics for Professional Accountants (Code of Ethics). The consequences can be serious.

Requirements under the POBO and Code of Ethics

Under the POBO, auditors are prohibited from soliciting or accepting any advantage (e.g. gift, loan, fee, commission, employment, service, favour) without the permission of their employer. The offeror of the advantage is also guilty of an offence.

Even if permission has been granted by the employer, auditors are prohibited under the Code of Ethics from offering/accepting, or encouraging others to offer/accept, any inducement that a reasonable and informed third party would be likely to conclude is made, with the intent of improperly influencing the behaviour of the recipient or another individual. Inducements can range from minor acts of hospitality among business colleagues to acts that result in non-compliance with laws and regulations.

What audit firms should do

Since corrupt practices undermine objectivity and audit quality, each audit firm should set out its policy and rules governing anti-corruption practices, such as acceptance and offering of gifts and hospitality, in a Code of Conduct. Such a policy should cover the key provisions in the Sample Code of Conduct for the Private Sector published by the Independent Commission Against Corruption, which can be found in the Code of Ethics.

In our inspections, we noted that some audit firms had not put in place any such policies. We urge audit firms to do so as soon as possible to address the relevant requirements under the POBO and Code of Ethics. AFRC will continue to look out for this issue in our future inspections.

Contacts

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