

## Press Release

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### **2023 Annual Inspection Report emphasises the pivotal roles of the firm's leadership in upholding audit quality and reinforces the importance of continuous learning as a key driver of improvement**

The AFRC has published the [2023 Annual Inspection Report](#) today. The report covers the findings, observations, and insights from our 2023 inspection. To reflect our risk-based and proportionality approach to inspection, the AFRC inspected:

- 20 (or 44%) PIE auditors, covering 56 PIE engagements and 17 non-PIE engagements
- 13 (or 0.5%) non-PIE auditors, covering 25 non-PIE engagements

The number of firms inspected increased by 27%, and engagements inspected increased by 61% year-on-year. Our first inspection cycle has created a virtuous cycle among PIE auditors, resulting in heightened responsiveness and accelerated learning among the profession, thereby enhancing inspection efficiency.

For the first time following the further reform of the accounting profession, we inspected audit firms' compliance with the legal requirements on Anti-Money Laundering and Counter-Terrorism Financing, which is important for protecting the integrity and stability of Hong Kong as an international financial centre.

#### **Strong commitment from leaders of larger firms to improve audit quality**

Category A firms audited 89% of the PIE audits by market capitalisation. The leadership of most of them has taken proactive steps to improve their firms' systems of quality management and audit practice. The improvements, based on our previous inspection findings, guidance and reminders for auditors in our publications, are a reassuring sign of these firms' commitment to continuous improvement. Positive changes across most of these firms include:

- i. Cultivate a culture prioritising quality
- ii. Ensure accountability for quality
- iii. Enhance a proactive compliance approach
- iv. Effectively manage resources
- v. Continuously improve audit practices
- vi. Strengthen audit documentation integrity
- vii. Closely monitor partner performance and workload

The 2023 engagement inspection results show that 45% of the PIE engagements inspected at the Category A firms required no or limited improvements. We expect to see better results in the future as these firms continue their journey to audit quality improvements.

### **Firm leaders of Category B and C firms must take action to improve audit quality**

The 2023 inspection results of Category B and C firms, which accounted for 3% of the PIE audits by market capitalisation, were mostly below a satisfactory level. In particular, the AFRC has noted the following areas which require immediate attention and action by leaders of these firms:

- i. Firm leadership should prioritise audit quality over commercial considerations and nurture a compliance culture;
- ii. Firm leadership should foster a culture of professional skepticism, where engagement teams are empowered to challenge management's key judgments and estimates; and
- iii. Engagement partners should properly supervise their engagement teams to ensure delivery of quality audits.

Although there is relatively less public interest connected with the audit work of Category B and C firms, we urge their leaders to improve audit quality by proactively making reference to our publications, including this report, and acting on them to achieve holistic improvement.

Ms Eva Lau, Acting Head of Inspection, said, "Auditors of PIE engagements assume a much greater responsibility of upholding audit quality. Therefore, they are subject to more stringent scrutiny by the public, whose interests must be sufficiently protected. We urge firm leadership to communicate the right tone internally while leveraging our inspection findings for their good."

### **Promoting governance and transparency**

Transparency breeds confidence. To provide greater transparency to the public, we published a full list of PIE auditors subject to our inspection for the first time. This enhanced disclosure should:

- i. Enable PIEs and audit committees to make informed decisions about the appointment and re-appointment of auditor by engaging with audit firms regarding their inspection results; and
- ii. Increase PIE auditors' public accountability which should help promote healthy market development when firms strive for continuous improvement.

### **Enhanced approach and closer stakeholder collaboration to drive sustainable quality improvement and market development**

A more proactive and collaborative stance is needed to drive sustainable improvements in audit quality and compliance across the accounting profession. To that end, we will continue to engage with firms and strengthen our collaboration with other key stakeholders, including other regulatory bodies and standard setters. In particular, we will place greater emphasis and effort to ensure audit committees of listed entities will uphold the quality of financial reporting from their dual role as overseers and governing body of PIEs. This collaborative approach will ensure that our inspection remains relevant, responsive, and effective to our dual role of regulation and development.

Ms Janey Lai, CEO of the AFRC, stressed, “In fulfilling our dual role as a defender of law and a promoter of the accounting profession, the AFRC has been dedicating continuing efforts and considerable resources towards fostering a sustainable development of the profession. Our inspection findings demonstrated that firms that have taken guidance from the AFRC benefit from improving their audit quality. Though learning process and behavioural change take time to reflect on audit quality, we are seeing signs of improvement among most Category A firms and are confident that firm leaders of Category B and C firms could deliver high-quality audits through their undeniable responsibility to set the right tone at the top to drive a firm-wide improvement in audit quality.”

Dr Kelvin Wong, Chairman of the AFRC, concluded, “While the AFRC tangoes with the dual mission of effective regulation and market development with the audit profession, it is pivotal for the leaders of the PIE audit firms to establish and ensure an effective governance policy and system in place. The key to success lies on those firm leaders who sit at the top to exhaust their effort and wisdom to foster a firm-wide quality-driven culture. I am confident that good governance and healthy culture will drive home with superior performance”

End

## About the Accounting and Financial Reporting Council

The Accounting and Financial Reporting Council (AFRC) is an independent body established under the Accounting and Financial Reporting Council Ordinance. As an independent regulator, AFRC spearheads and leads the accounting profession to constantly raise the level of quality of professional accountants, and thus protects the public interest and promotes the healthy development of the accounting profession.

For more information about the statutory functions of the AFRC, please visit [www.afrc.org.hk](http://www.afrc.org.hk).

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