

Audit Focus for 2025 year-end audits

Inspection

3 October 2025



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, the AFRC leads the accounting profession by upholding professional standards, safeguarding the public interest, and promoting the profession's healthy development.

For more information about the statutory functions of the AFRC, please visit www.afrc.org.hk.

Introduction

Navigate the dynamic risk environment of 2025

The challenging economic conditions of 2025, coupled with new and increasingly complex business models, present significant challenges for both companies and their auditors.

Ongoing geopolitical and economic uncertainties continue to affect business operations, with fluctuating interest rates and shifting consumer sentiment further exacerbating challenges related to profitability, liquidity, and an entity's ability to continue as a going concern. Meanwhile, the rapid technology advancements, such as the adoption of artificial intelligence (**AI**), are fundamentally transforming business processes and introducing new risks to operational reliability, data security, and cybersecurity. These factors are not only testing business resilience but also increasing the risk of material misstatements — whether due to error or fraud.

The imperative of audit quality and heightened professional scepticism

High-quality audits are a cornerstone of market integrity. The role of an auditor extends beyond simply ensuring compliance; they are critical for building investor trust and ensuring that financial statements provide an accurate and reliable reflection of a company's performance and position. This responsibility becomes even more important during uncertain times, when capital markets rely heavily on credible information.

A typical audit approach is insufficient in today's rapidly evolving risk landscape. Auditors must combine strong technical competence with heightened professional scepticism to identify and assess the risk of material misstatement in financial statements, and to plan and perform audit procedures in response to these risks. Additionally, auditors must ensure that sufficient documentation is maintained to clearly demonstrate the work performed, particularly in areas involving the exercise of professional judgement.

Purpose of this publication

This publication offers an overview of the macroeconomic and market landscape in 2025. It highlights key focus areas for 2025 year-end audits and firm-level considerations to ensure the delivery of high-quality audits amidst a complex and evolving landscape.

However, it is important to note that this publication is not intended to serve as a comprehensive guide for auditors preparing for their 2025 year-end audits. Auditors should exercise professional judgement and consider the specific facts and circumstances of their audit clients when determining the appropriate audit approach and responses.

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Section 1

Audit implications of the current macroeconomic and market landscape

Challenging market and economic conditions create an environment where companies may experience extended financial pressure, increasing their susceptibility to management bias or fraud. Auditors should carefully consider current market and economic conditions and incorporate them into the risk assessment and audit planning process.

This section highlights key developments within the current macroeconomic and market landscape. It provides insights into areas where auditors should exercise heightened professional scepticism and adapt their audit strategies accordingly. Specific focus areas, indicated by 🎯, will be discussed in detail in Section 2.



Geopolitical uncertainty

Ongoing geopolitical tensions and tariff-driven uncertainties introduce complexities for businesses, which may affect their operations, profitability, liquidity, as well as financial reporting.



Matters to consider:

- **Inventory valuation:** Assess whether write-downs of inventories are necessary due to rising selling costs and/or weakened customer demand.
- **Revenue recognition:** Evaluate whether and how tariffs may affect contracts with customers, e.g., transaction price, and measurement of progress toward satisfaction of a performance obligation under a cost-to-cost input method.
- **Onerous contracts:** Ensure adequate provisions are made for onerous contracts where the unavoidable costs of fulfilling the contract exceed the expected economic benefits.
- **Subsequent events:** Evaluate the occurrence of subsequent events that may require adjustments to, and/or disclosures in, the financial statements.
- **Impairment of non-current assets** 🎯
- **Going concern assessment** 🎯

Liquidity pressures

External factors, such as geopolitical and economic uncertainties and weak market sentiment, may result in liquidity challenges and financial distress for some entities. These pressures may be further intensified by tightening credit availability.



Matters to consider:

- **Classification of liabilities:** Duly review loan agreements, repayment records, and correspondence with lenders to identify any potential breaches of covenants or cross-default. Evaluate liability classification as at the financial year-end date.
- **Going concern assessment** 🎯





Persistent headwinds in the retail and real estate sectors, with signs of slow recovery

Hong Kong's retail industry has faced persistent challenges due to sluggish domestic consumption, driven by northbound travel and a shift toward online shopping platforms. The provisional total retail sales value for the first seven months of 2025 declined by 2.6% compared to the same period in 2024¹.

Hong Kong's property market has continued to experience a downward trend over the past seven months in 2025, with the office and retail sectors adjusting to changing demand and pricing dynamics. The provisional price indices for private offices and retail in July 2025 have decreased by 9.1% and 7.3%, respectively, compared to December 2024².

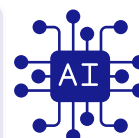


Matters to consider:

- **Property valuation:** Evaluate management's selection of comparable transactions. Challenge management on any adjustments made, or the lack of adjustments, such as the absence of adjustments to reflect the date of transactions in a softening property market.
- **Expected credit losses:** Evaluate whether the credit risks related to accounts receivable or other financial assets, particularly those with direct or indirect exposure to the retail and real estate sectors, have significantly increased since initial recognition.
- **Inventory valuation:** Evaluate whether current market conditions have affected product demand, indicating potential risks of obsolescence or the need for inventory markdowns.
- **Impairment of non-current assets** 
- **Going concern assessment** 

Advancements in technologies

To promote the development of the local AI ecosystem, the Hong Kong SAR Government has allocated HK\$3 billion for the launch of a three-year AI Subsidy Scheme to support local universities, research institutes, enterprises and more in leveraging the computing power of Cyberport's AI Supercomputing Centre³.



Matters to consider:

- **Thorough understanding:** Obtain a thorough understanding of the audit clients' IT environment, with a particular focus on the adoption of technologies, such as AI, in their business processes and financial reporting.
- **IT risks assessment:** Assess the audit clients' IT risks arising from the adoption of technologies, and evaluate the effectiveness of the measures and controls they have implemented to address them.
- **Competence and capabilities of auditors:** Consider the risks arising from the adoption of technologies and determine whether specialised skills or expertise are needed to assess and address them.

¹ [Provisional statistics of retail sales for July 2025](#), Census and Statistics Department of the HKSAR, September 2025

² [Property Market Statistics](#), Rating and Valuation Department of the HKSAR, September 2025




³ [Artificial Intelligence Subsidy Scheme](#), Digital Policy Office of the HKSAR


Section 2

Engagement-specific focus areas


I. Risk assessment


A robust risk assessment is the cornerstone of an effective and efficient audit. Nevertheless, some auditors approach this process as a mere checkbox exercise, failing to understand their audit clients’ businesses and operating environment thoroughly. Such a superficial approach can lead to misplaced audit focus and result in material misstatements going undetected.


Key reminders	
	Stay relevant: The risk assessment should reflect the specific circumstances of an entity, including any changes in its business and operating environment. It should also consider the impact of emerging technologies, such as AI, on the business process and transaction flows.
	Reflect the risk assessment results in audit planning: The engagement partner should take an active role in designing the appropriate audit approach to ensure the nature, timing, and extent of audit procedures are appropriately designed to address the assessed risks, rather than defaulting to prior-year audit approaches. The engagement quality reviewer (EQR) should perform an objective evaluation of the engagement team’s identification and planned responses to assessed risks, particularly significant risks.
	Risk assessment does not stop at audit planning: While risk assessment decisions are generally made during audit planning, the process should be dynamic and iterative. Auditors should regularly re-evaluate the assessed risks to ensure they appropriately reflect the evolving business landscape and the entity’s adaptations to these developments.

**Turning scepticism into action with the ICC approach**

The **Inquiry, Challenge, and Corroboration (ICC)** approach provides auditors with a structured framework to apply professional scepticism effectively. Below are some illustrative, **non-exhaustive** examples of its application in practice.

**Inquire management**

**Challenge management**

**Corroborate**

- How did the current economic landscape and associated challenges affect an entity's business operations and financial performance?
- Have there been any changes to the entity's business model or operations since the last audit, particularly in relation to technology adoption?
- What specific sources or discussions can be pursued to enhance the understanding of these developments?






- Why did the financial performance of your company differ significantly from your peers?
- Why did the new business not bring any new risks to your company's financials, governance, and internal controls?

- Identify and assess how industry, regulatory, and other external factors relevant to the audit client may have given rise to specific risks of material misstatement.
- Evaluate whether the engagement team had appropriately identified, assessed, and responded to the IT risks.

II. Impairment of non-current assets

Asset impairment assessment may involve significant management judgement and estimates that can be subject to a high degree of subjectivity and complexity. Challenging market and economic conditions, combined with ongoing geopolitical uncertainties, further heighten the difficulty of auditing these accounting estimates. Auditors must exercise heightened professional scepticism and obtain sufficient corroborative audit evidence to support the appropriateness of key assumptions underlying the asset impairment assessments.

Key reminders

	Understand management's estimation process: Understand how prevailing market and economic conditions impact the entity's business performance and cash flow projections. Perform a retrospective review to assess the effectiveness of management's estimation process.
	Evaluate inputs and data used: Verify the reliability of historical data and the carrying amount of the cash-generating unit (CGU). Challenge the relevance and reliability of information and key inputs adopted by management.
	Critical challenge of optimism: Corroborate management's representation with appropriate supporting evidence, such as industry forecasts and the entity's historical financial performance. Consider and address contradictory or inconsistent evidence obtained.
	Compare like with like: Ensure that the cash flows used to determine the recoverable amount are consistent with the assets included in the carrying amount of the CGU. Specifically consider corporate assets, working capital, income taxes, and liabilities.
	Take ownership of the auditor's expert work: Evaluate the relevance and reasonableness of the significant assumptions and methods, and the relevance, completeness, and accuracy of significant source data used by the expert. Address any caveats, findings, or observations reported by the expert.



Inquiry, Challenge, and Corroboration



- How were uncertainties arising from changes in the business environment incorporated into the discounted cash flow model?
- What evidence supported the optimistic projection of revenue growth, despite low demand?
- Were multiple cash flow scenarios considered to address the significant uncertainties related to future events or the timing of cash flows?



- What specific evidence supported the appropriateness of your assumptions, which appeared to be inconsistent with your company's historical performance and the current market trends?
- Why was the weighted average cost of capital from another company used directly as your company's discount rate without any adjustments?



- Compare historical data and carrying amount of the CGU with the audited financial information.
- Corroborate significant assumptions against external data (e.g., industry and economic forecasts) and internal data (e.g., historical performance and committed sales orders).
- Consider events occurring after the end of the reporting period that may indicate a need to adjust key assumptions and inputs.

III. Going concern assessment

Current economic headwinds and soft market sentiment in the retail and real estate sectors are placing entities at risk of financial distress and liquidity challenges. Auditors act as gatekeepers in assessing the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements and in evaluating the adequacy of related disclosures. This provides users of financial statements with the transparency needed to make informed decisions about the entity's going concern.

Key reminders



Extend the assessment beyond the 12-month horizon: Critically assess whether events or conditions, such as a material debt repayment in 12 to 18 months, require extending the going concern assessment beyond 12 months from the date of the financial statements.



Consider the impact of external factors: Remain alert to changes in the macroeconomic environment, such as tariffs and interest rate movement, that could adversely affect the entity's operations, liquidity, or ability to repay and refinance debts.



Assess compliance with loan covenants and credit availability: Critically evaluate how the current economic environment and the entity's financial condition impact its credit availability, keep in mind that past precedents do not guarantee future outcomes.



Evaluate management's plans: Challenge the feasibility, timing, and outcomes of proposed plans (e.g., disposal of assets or cost reductions). Obtain evidence to assess management's intent and ability to implement these plans.



Complete and accurate disclosures: Evaluate the adequacy of financial statement disclosures regarding events or conditions that may cast significant doubt about an entity's ability to continue as a going concern, as well as management's plan to address them and whether any material uncertainties exist. Assess the need for the inclusion of an emphasis of matter paragraph in the auditor's report or the issuance of a modified opinion.



Inquiry, Challenge, and Corroboration

Inquire management



- What evidence supported your intent and ability of the forecast asset realisations, particularly regarding the timing and amounts involved?
- How did you forecast the expected patterns of cash receipts and payments on a monthly basis?

Challenge management



- Why was the assessment of going concern limited to a period of 12 months, even though a material borrowing matures in 15 months?
- What evidence demonstrated your entity's ability to renew or secure additional financing following a credit rating downgrade and deteriorating financial conditions, and what supported the progress made in discussions with lenders?

Corroborate








- Perform an independent search for comparable market transactions to assess the reasonableness of the forecasted asset realisation values and timelines.
- Review the correspondence between the entity and its lenders regarding the facility negotiations. Assess any evidence indicating the bank's reluctance to lend to the entity.

IV. Addressing fraud risks




The increasing complexity of business operations and pressures to meet financial targets have created greater opportunities and pressures for fraudulent activities and requires auditors to adjust their approach to effectively identify and respond to fraud risks. Auditors must exercise heightened professional scepticism and design and perform audit procedures that are responsive to potential fraud risks.

Key reminders

	Scepticism is not optional: Heighten professional scepticism for any indicators of possible management bias or potential fraud. This includes critically evaluating evidence that contradicts management's responses to inquiries, unusual transactions, previously unidentified related parties, and arrangements with contractual terms that deviate from the entity's or normal industry practices. Consider the risk of fraud using the fraud triangle.
	Challenge the business rationale: Critically challenge the business rationale (or lack thereof) for significant non-routine transactions. Corroborate management's representation with evidence from independent third parties and evaluate the associated risk of fraud. Immediately report any suspicious transactions to the Joint Financial Intelligence Unit ⁴ .
	Maintain control over the send-and-receive confirmation processes: Evaluate the reliability of responses, particularly those received electronically or where there are indications that the response may not have come from the originally intended confirming party.
	Response to possible management bias: Evaluate management's identification and determination of comparable transactions or companies used in the valuations or impairment assessment. Critically challenge the exclusion of any transactions or companies that appear to be more pertinent.
	Assign the right staff: Assign experienced engagement team members to complex and high-risk areas. Ensure close and appropriate supervision and thorough review of the work performed in these areas.



Inquiry, Challenge, and Corroboration

 <p>Inquire management</p>	<ul style="list-style-type: none"> • How had ongoing business challenges and soft market sentiment affected management's ability to meet financial targets and influence their compensation? • How were comparable transactions and companies identified, and how was it determined that they are comparable?
 <p>Challenge management</p>	<ul style="list-style-type: none"> • What was the business or commercial rationale for the significant non-routine transaction, and what was the relationship between the entity and the counterparty? • What was the rationale for excluding a more recent transaction that appeared to qualify as a comparable from management's analysis?
 <p>Corroborate</p>	<ul style="list-style-type: none"> • Avoid over-reliance on management's representations. Obtain and evaluate multiple sources of evidence to form independent conclusions. • Consider all available audit evidence, including both corroborative and contradictory. Document the exercise of professional scepticism, particularly the audit procedures performed to address any inconsistent or contradictory information.

⁴ [How to identify a Suspicion?](#) Joint Financial Intelligence Unit

V. Group audit

The group auditor's overall objective is to ensure sufficient appropriate audit evidence is obtained by the group and component auditors to support the group audit opinion. As such, the group auditor's responsibility in directing and supervising component auditors and reviewing their work is imperative to the overall quality of a group audit.

Key reminders



Timely and proactive involvement: Clearly communicate the scope of work and expectations to component auditors in a timely manner. Be sufficiently and appropriately involved in directing, supervising, and reviewing the component auditors' work through ongoing interactions, as evidenced by minutes/notes from discussions with component auditors.



Evidence your review: Maintain sufficient documentation to demonstrate your evaluation of the sufficiency and appropriateness of audit evidence obtained by the component auditor to address significant matters arising from the group audit. Simply creating a boilerplate review memorandum with generic concluding statements is not enough.



Audit work on consolidated financial statements: Evaluate whether the financial information identified in the component auditor's communication is the same as the financial information incorporated in the group financial statements.



Don't overlook consolidation adjustments: Consolidation adjustments represent a high-risk area that may conceal errors or manipulations. Their audit requires experienced staff with a thorough understanding of group operations.



Inquiry, Challenge, and Corroboration



- (To component auditors) What were the key local economic, regulatory, and external factors that influenced the component and its environment? How did these factors impact your risk assessment of the component's financial information?
- (To management) How did you ensure that all subsidiaries had been scoped in for consolidation, and the accuracy and completeness of the consolidation adjustments?



- (To component auditors) What specific evidence supported your conclusion regarding the appropriateness of the significant assumptions used by the component management in making accounting estimates? What alternative scenarios did you consider?
- (To management) What adjustments were made to the component's financial information before being incorporated into the group financial statements, and what evidence supported these adjustments?







- Corroborate the sufficiency of the component auditor's work through ongoing interactions and a review of their audit working papers. Ensure that the group engagement audit files contain sufficient documentation, including but not limited to the nature, timing, and extent of audit procedures performed by the component auditors, conclusions reached, and how the group auditor evaluated or challenged any significant professional judgement made in arriving at those conclusions.

VI. First-year audit




First-year audits are inherently challenging as auditors must start from the ground up. They need to understand the client's business, operations, and accounting policies to perform a robust first-time risk assessment. Additionally, they may need to address unresolved matters from outgoing auditors and perform procedures, such as testing the opening balances, that are not typically required for recurring audits. These factors highlight the need for additional time, resources, and the extensive involvement of experienced team members to ensure audit quality.

Key reminders

	<p>Critically assess your competence and capabilities: Ensure you have the appropriate competence, sufficient time, and available resources (including component auditors) commensurate with the size, structure, and complexity of the prospective clients before accepting the appointment.</p>
	<p>Address unresolved audit matters: Obtain a thorough understanding of the matters by reviewing correspondence between the outgoing auditor and the entity, corroborating management's responses through inquiries with the outgoing auditor, and requesting access to their working papers. Design and perform audit procedures that address the specific facts and circumstances of these matters.</p>
	<p>Test the opening balances: Appropriately plan and perform the necessary audit procedures to obtain sufficient appropriate audit evidence regarding opening balances. This should not be limited to sending confirmation requests on material assets and liabilities, but should also include, for example, evaluating areas of significant judgement.</p>
	<p>Early and open dialogue with the audit committee: Engage with the audit committee early to discuss the nature and significance of any unresolved audit matters identified by the outgoing auditor, as well as any concerns they may have regarding the current year's audit.</p>



Inquiry, Challenge, and Corroboration

<p>Inquire management</p> 	<ul style="list-style-type: none"> • What was the nature and significance of the unresolved audit matters identified by the outgoing auditor? What specific challenges or limitations were encountered by the outgoing auditor in resolving them? • Were there any changes in accounting policies or methodologies for making accounting estimates compared to the prior year, and what were the reasons for those changes?
<p>Challenge management</p> 	<ul style="list-style-type: none"> • What factors led to the adoption or change in accounting policies that deviated from industry practices or differed from prior periods, and how was compliance with applicable accounting standards ensured? • What evidence supported your representation that adjustments made in prior years should be carried forward to the current year?
<p>Corroborate</p> 	<ul style="list-style-type: none"> • Obtain a comprehensive understanding of the entity's business and operations by engaging directly with the audit committee and personnel outside the finance function. • Evaluate the relevance and appropriateness of the 'brought-forward' adjustments and obtain corroborative evidence to support them. Simply indicating that they were 'brought-forward' is not sufficient.

Section 3

Firm-specific key considerations

I. Set the right tone at the top

Establishing the right tone at the top is fundamental for fostering a culture of integrity and delivering high-quality audits. When leaders of the audit firm set audit quality as their highest priority and demonstrate their commitment to achieving it, it profoundly influences the behaviour and work ethics of staff.

The diagram below outlines our six key expectations of the audit firm's leadership and the corresponding actions to be taken.



II. Build competence in the evolving audit profession

In today's rapidly evolving economic and technological landscape, developing and sustaining the necessary competence among audit team members is essential for safeguarding audit quality. Advancements in technology and the increasing complexity of business operations are reshaping how audits are conducted, which in turn requires auditors to adapt and expand their expertise.

To keep pace with these changes, **continuing professional development** plays a critical role in equipping audit professionals with the skills, knowledge, and judgement needed to deliver high-quality audits. Below, we outline four key areas for audit firms to focus on:



The audit profession thrives on human interaction

Quality audits are grounded in **person-to-person development**, where technical expertise, judgement, and professional scepticism are refined through **guidance** and **shared experience**.

Senior members of the engagement team should dedicate a **substantial proportion of their time** to **on-site reviews**, providing direct guidance, facilitating skills transfer, and fostering collaborative learning to ensure the development of both technical expertise and interpersonal skills.



Technical excellence is the foundation

Technical excellence underpins the integrity and quality of audits. Audit firms should **proactively identify** and **address knowledge and skill gaps** through targeted training and development programmes. These programmes should include not only technical skills but also **soft skills**, such as critical thinking and the exercise of professional judgement. **Reinforcing fundamental concepts** and **skills** is equally essential to upholding professional excellence.



Elevating auditors with growth and development

Audit firms should prioritise **ongoing professional development** to ensure their teams remain equipped to address evolving business complexities and regulatory requirements.

They should incorporate **insights from the AFRC's inspections and publications** into training programmes to avoid common audit deficiencies and improve audit quality.



Technology enhances, people lead

While technology and data analytics play an increasingly important role in today's audits, they are tools designed to support the audit process—not to replace the professional judgement and expertise of auditors.

Audit firms should ensure that auditors receive **appropriate training** and are provided with **adequate guidance** in utilising advanced technological tools effectively. This includes developing and enhancing the ability to **evaluate the reliability and accuracy** of the outputs produced by such tools and ensuring the **appropriate usage** within the audit.


III. Closely monitor audit partners' workload and their involvement in audits

Managing audit partners' workloads is crucial to ensuring they can allocate the necessary time, attention, and expertise to each engagement. The recovery of the IPO markets has driven increased demand for audits, further straining partners' already substantial workloads and potentially diverting their focus from recurring audits. Audit firms should establish **robust systems** to continuously **assess and adjust partners' workloads**, ensuring they have the capacity for sufficient involvement in each engagement.

In addition, the **timely, proactive, and sufficient involvement** of the engagement partner and EQR in an engagement is of paramount importance to uphold audit quality. As the year-end approaches, we outline critical reminders for the engagement partners and EQRs to fulfil their responsibilities.



Timely, proactive, and sufficient involvement

The engagement partner and the EQR must ensure their involvement is both timely and sufficient at each **key audit milestone** . They should be **involved early** to identify and assess risks and ensure the planned audit procedures are **relevant and responsive** in addressing the identified risks.



Leadership in direction, supervision, and review

The engagement partner should provide active direction, supervision, and timely guidance. This includes **conducting on-site reviews** of audit working papers to ensure that audit procedures are appropriately executed as planned, and to identify and address any critical matters.

The engagement partner should also **examine critical audit evidence** obtained by the engagement team members to ensure its appropriateness and relevance in supporting the conclusions reached.



Evidence of engagement quality review

The EQR is responsible for ensuring **sufficient documentation** of the **engagement quality review**. The documentation should include, but is not limited to, the identification of the engagement documentation reviewed, minutes/notes of discussions with the engagement team, the challenges raised by the EQR regarding the significant judgements made by the engagement team, and how those challenges were addressed.



Key audit milestones

Annex 1 of the 2024 Audit Focus, published in October 2024, outlines the key audit milestones that serve as critical checkpoints for planning and executing an audit. Auditors are encouraged to refer to the publication for additional guidance.

[2024 Audit Focus](#)



Annex

Additional guidance and resources

The AFRC is dedicated to fostering a culture of continuous improvement within the accounting profession. To support this, we publish a range of communications, including reports, guidelines, and videos. Auditors are encouraged to draw upon these resources to advance their professional excellence and uphold audit quality.



2024-25 Annual Inspection Report

The annual inspection report presents key findings and insights from our 2024 inspections.



Checkpoint - Obtaining an Understanding of the Audit Clients' IT Environments

The checkpoint provides practical guidance to auditors relating to IT audits.



AFRC Connect Video Series

The video series provides practical insights and essential technical reminders in an engaging format.

[How important is Audit Risk Assessment?](#)



[Understand and Evaluate IT Risks and Controls](#)



[Revealing the Hidden Truths of Management Fraud: The Vital Role of Journal Entry Testing](#)



Setting and Reinforcing Tone at the Top to Achieve Quality Audits

This article emphasises the importance of an audit firm's leadership in setting and reinforcing the tone at the top. It also outlines our expectations of the leadership of audit firms, audit committees, and company management in promoting and maintaining the right tone at the top.

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