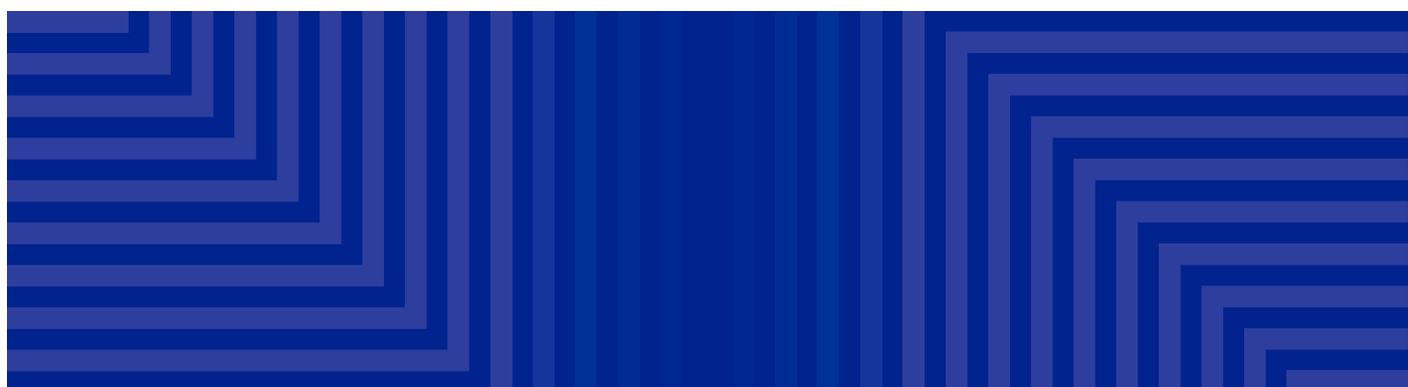


# AFRC Quarterly Report

11 October 2023



## Highlights

- We continued to drive improvements in audit quality through the publication of the 2023 Annual Investigation and Compliance Report, Audit Focus and organising briefing sessions.
- We published the first disciplinary decision to ensure the market understands how our regulatory principles are applied.
- We collected information about the practice units by launching an Inspection Questionnaire.
- We reinforced regulatory collaboration through participation in an international workshop and meeting with our counterparts and professional bodies.

- We welcomed the reappointment and appointment of NEDs and Honorary Advisers.

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

## **Driving improvements in audit quality**

### **2023 Annual Investigation and Compliance Report**

On 4 September 2023, AFRC issued the [2023 Annual Investigation and Compliance Report](#) (the Report) covering the reporting period from 1 April 2022 to 31 March 2023.

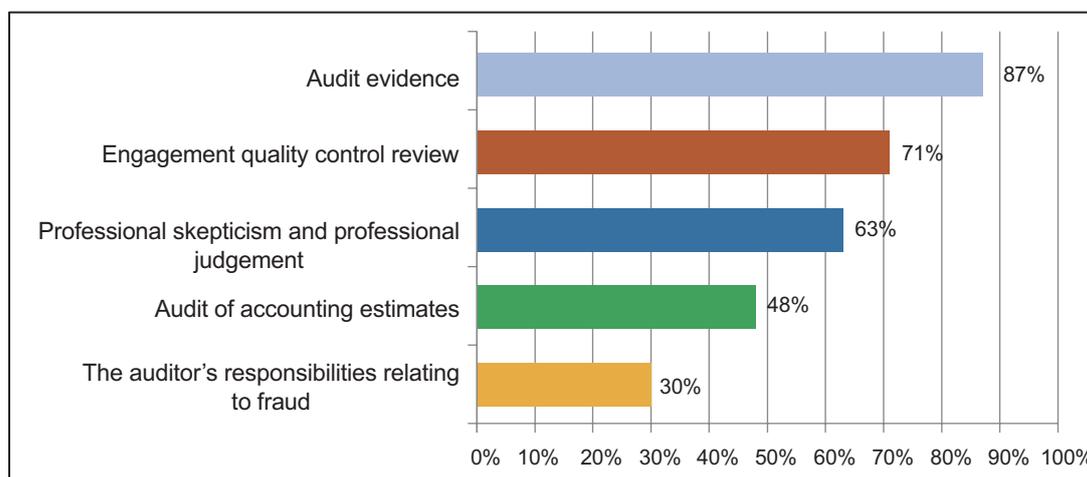
The Report highlights the more common examples of practice irregularities, non-compliance in listed entities' financial reporting, and misconduct of listed entities' auditors (PIE auditors) and other CPAs (professional persons) that were identified during the reporting period.

It shows that the total number of complaints received with pursuable allegations increased by 83%, and the number of investigations initiated increased by 88%. These significant increases reflect heightened public awareness of the AFRC's complaint process and whistleblowing channels, and the community's confidence in the AFRC's ability to perform its role as the sole regulator of the accounting profession.

#### **Potential and actual misconduct by PIE auditors**

The areas of potential and actual misconduct of PIE auditors are similar to those of the last financial year, with an increase in investigations into auditors' potential failure to respond adequately to fraud risks relating to the financial statements of listed entities.

The top 5 areas of misconduct PIE auditors are set out in the chart below:



### **Potential and actual non-compliance in listed entities' financial reporting**

The top 5 areas of financial reporting non-compliance are:

- (i) impairment assessment and fair value measurement (34%);
- (ii) recognition and measurement of financial instruments (25%);
- (iii) fraudulent financial reporting or misappropriation of assets (20%);
- (iv) going concern assessment and reporting (16%); and
- (v) revenue recognition (15%).

### **Potential and actual misconduct of professional persons**

Our investigative work on professional persons shows that the top 4 areas of misconduct are:

- (i) maintaining integrity and proper professional conduct (59%);

- (ii) complying with the auditing and assurance standards (42%);
- (iii) exercising professional competence and due care (17%); and
- (iv) maintaining independence and complying with other ethical requirements (17%).

The AFRC expects the auditors to carry out their audits in strict compliance with relevant auditing standards and reminds auditors, those charged with governance and management, of their responsibilities relating to fraud. Preparers of financial statements and auditors are urged to keep abreast of the financial reporting and auditing standards, be alert to potential misstatements due to errors and fraud and allocate sufficient time and resources to planning.



Dr Kelvin Wong, Chairman (middle), Mr Marek Grabowski, CEO (right), and Ms Florence Wong, Head of Investigation and Compliance (left) present the Report at the press briefing on 4 September 2023.

## First discipline case published

On 29 August 2023, we published our [first disciplinary decision](#), where we reprimanded a corporate practice, an engagement partner and an engagement quality control reviewer for their serious breaches of professional standards, imposed pecuniary penalties totaling HK\$700,000, and cancelled the practising certificate of the engagement partner for 12 months.

This case involved the audit of the consolidated financial statements of a Hong Kong listed company for the financial year ended 31 December 2016, and concerned the accounting for goodwill arising from the Company's acquisition of a subsidiary in late 2016, which was fully impaired in the 2017 financial statements.

Our decision highlights the importance for an auditor to perform robust and rigorous assessment and obtain sufficient appropriate evidence on the identified key audit matters, which if not properly assessed, would give rise to a risk that investors would be misled as to the financial position of the listed company.

Our decision states clearly our rationale for the sanctions imposed, which ensures that the market understands how our regulatory principles are applied in order to uphold audit quality. We considered the breaches of professional standards in this case were serious, which stemmed from the auditor's failure to exercise professional skepticism, a necessary attitude which should be adopted throughout an audit engagement. The past disciplinary records of the corporate practice and engagement partner were also aggravating factors which warranted the sanctions imposed, and to send a strong deterrent message to the regulatees to prevent the repetition of similar failings.

As the audit was completed prior to 1 October 2019, the misconduct in this case was assessed under the old regime pursuant to section 37CA of the Accounting and Financial Reporting Council Ordinance (Cap. 588), which carries a maximum pecuniary penalty of HK\$500,000 for each misconduct. If a similar case were to arise under the new regime in respect of PIE engagements on or after 1 October 2019, the pecuniary penalty to be imposed will be assessed under a different scale where the upper limit for each misconduct is HK\$10 million or three times the profit gained or loss avoided (whichever is higher).

### **Briefing Session on the 2022 Annual Inspection Report**

More than 40 Quality Control System Responsible Persons (**QCSRPs**) from registered PIE auditors attended the briefing session on the 2022 Annual Inspection Report hosted by the AFRC on 22 September 2023. At the briefing, Ms Janey Lai, Head of Inspection presented to the participants the common deficiencies identified in our first three-year inspection cycle and our expectations of auditors in upholding the quality of audits. She also highlighted the deficiencies identified from our review of the root cause analysis and remediation plan submitted by the PIE auditors. Details of the presentation slides can be found [here](#).

Ms Lai urged the participants to disseminate and communicate the following key messages to their firms' professional accountants:

- QCSRPs are responsible for ensuring the Registered PIE Auditor has established and maintained a quality control system in relation to PIE engagements carried by the auditors, and has established policies and procedures for monitoring quality control system under the AFRC Ordinance;
- QCSRPs are ultimately responsible and accountable for the firm's audit quality;
- Firm leadership's commitment to audit quality is of utmost importance; and

- Firms should make sustained efforts to uphold audit quality, which should be their top priority.

The AFRC would continue to closely monitor the risks associated with audit quality in the profession and increase our frequency of inspection of practice units which showed no substantial improvement in their unsatisfactory audit quality ratings.

### **Audit focus – Effective Planning: The Key to High-Quality Audits**

On 31 July 2023, we issued [Audit Focus](#) to urge all auditors to commence their audit planning process well in advance of the financial year-end and heighten their professional skepticism in certain key areas when developing an audit plan.

The key areas that require special consideration in audit planning include:

- Volatile economic environments and market conditions, e.g., continuously rising interest rates and inflation;
- Significant changes in business operations, e.g., acquisitions or disposals of business or assets;
- Significant non-routine transactions or unusual trends;
- Group audits; and
- Updates to audit plans

The Audit Focus also sets out our expectations of the auditors, management and audit committees during the audit planning process, failing which they will be held accountable.

## Inspection Questionnaire

On 4 September 2023, we launched Part 1 of the Inspection Questionnaire (IQ) through an online survey platform to collect information about the practice units. Such information included but not limited to:

- Types of audit and assurance services provided by the practice units and the related service fees and number of clients;
- Cross-border and overseas audit arrangements; and
- Types of services specified in the Guidelines on Anti-Money Laundering and Counter-Terrorist Financing for Professional Accountants provided by the practice units

Approximately 90% of the practice units submitted the IQ by the due date of 22 September 2023.

The information collected provides valuable input to our risk-based regulatory approach. It not only assists us in identifying practice units of higher risks or compliance concerns but also facilitates our determination of inspection priority and frequency of various practice units.

Based on the results of Part 1 of the IQ, PIE auditors and selected practice units other than PIE Auditors are required to complete Part 2 of the IQ which will be launched in due course. Part 2 of the IQ will consist of more in-depth questions. We strongly encourage the practice units to refer to the [step-by-step user manual](#) and the [briefing video](#) provided to complete Part 2 of the IQ.

## Regulatory collaboration

### New MoU signed with HKMA

On 17 August 2023, the AFRC signed a new [Memorandum of Understanding](#) (MoU) with the Hong Kong Monetary Authority (HKMA), superseding the one signed on 19 November 2007.

Under the new MoU, the HKMA and the AFRC agree to strengthen collaboration through case referrals, mutual assistance, capacity building and exchange of information. The enhanced cooperation facilitates the AFRC's regulatory efforts in upholding the quality of financial reporting, auditing and the accounting profession's work in relation to the banking sector, which is vital to the HKMA in assessing the financial resilience of banks and ensuring their safety and soundness. The new MoU also assists both parties in carrying out their respective statutory functions more effectively and efficiently with a view to fostering Hong Kong's status as an international financial centre.



Mr Arthur Yuen, Deputy Chief Executive of the HKMA (second left) and Mr Marek Grabowski, CEO of the AFRC (second right) sign a new MoU on 17 August in the presence of Mr Eddie Yue, Chief Executive of the HKMA (left) and Dr Kelvin Wong, Chairman of the AFRC (right).

## **AFRC delegates present at the ASEAN Audit Regulators Group (AARG) and Financial Statements Surveillance Group (FSSG) workshop**

At the invitation of the Accounting and Corporate Regulatory Authority (ACRA), the AFRC's delegation participated in the 2023 combined AARG and FSSG workshop held in Singapore on 26 September 2023.

The workshop provided a platform for regulators of the accounting profession in the ASEAN region to exchange updates on regulatory developments and other initiatives aimed at enhancing audit quality and the value of audit.

At the workshop, Ms Janey Lai, Head of Inspection of the AFRC was invited to present on the common inspection findings in Hong Kong, while Ms Hester Leung, Head of Discipline was invited to present on the importance of the AFRC as the independent regulator in Hong Kong to spearhead behavioural change in the profession.

The AFRC also built connections with the representatives from ACRA Singapore, Pusat Pembinaan Profesi Keuangan of Indonesia, Audit Oversight Board of Malaysia, Securities and Exchange Commission (SEC) of the Philippines, SEC of Thailand, and the Accounting and Auditing Regulator of Cambodia.



The AFRC delegates participate in the AARG-FSSG workshop.



Ms Janey Lai, Head of Inspection presents at the workshop on common inspection findings.



Ms Hester Leung, Head of Discipline presents on the importance of AFRC in spearheading behavioural change of the accounting profession.

## Visit by the Accounting Regulatory Department of the PRC's Ministry of Finance

On 14 July 2023, Mr Shu Huihao, Head of the Accounting Regulatory Department (ARD) and representatives from the ARD and the Supervision and Evaluation Bureau (SEB) of the PRC's Ministry of Finance (MoF) paid a visit to the AFRC. Dr Kelvin Wong, Chairman and Ms Mary Leung, Head of Policy, Registration and Oversight warmly welcomed the delegates. A meeting was held to discuss recent initiatives in talent building, promoting the growth of the accounting industry, and strengthening financial and accounting supervision. We also explored avenues for enhancing collaboration between the AFRC and the MoF, including the formation of a working group dedicated to strengthening this collaboration.



AFRC warmly welcomes Mr Shu Huihao, Head of the Accounting Regulatory Department (middle) of the PRC's Ministry of Finance.

## Meeting with the International Federation of Accountants

On 14 July 2023, we also hosted Ms Asmâa Resmouki, President of the International Federation of Accountants (IFAC). Following our introduction of the AFRC and an overview of the accounting and regulatory landscape of Hong Kong, Ms Resmouki shared with us the three objectives of IFAC: (i) assisting accounting professional bodies in developing a future-ready profession; (ii) supporting the development and adoption of high-quality standards; and (iii) acting as a global voice of the accounting profession. She also expressed IFAC's intention of fostering closer collaboration with the AFRC.



Ms Asmâa Resmouki, President of the International Federation of Accountants (2nd from right) shares her views on the development of the accounting profession.

## Meeting with Chartered Accountants Australia and New Zealand

On 21 July 2023, we met with the visiting delegation of Chartered Accountants Australia and New Zealand (CA ANZ), led by its President Mr Murray Harrington. The delegates introduced to us their recommendations resulting from the recent Professional Conduct Framework Review, which included a range of procedural and efficiency improvements. They also shared their insights on the profession's readiness to implement sustainability disclosures.



CA ANZ President Mr Murray Harrington (middle) and delegates visit the AFRC.

## Briefing sessions with the Securities and Futures Commission and the Hong Kong Stock Exchange

We conducted two briefing sessions for the Securities and Futures Commission (SFC) and the Hong Kong Stock Exchange (HKEX) on 1 August 2023 and 13 September 2023 respectively to share with them our concern about auditor appointments and the setting of audit fees in Hong Kong.

Approximately 200 staff members from both regulators attended the two sessions whereby we shared the recent inspection results, raised red flags on issues surrounding late changes of auditors and shared our concern about bad audits driving out good ones. We also outlined the opportunities for seamless collaboration among the three regulators on improving audit quality.

During the sessions, we engaged the audience by polling and discussion. The responses to the polling questions indicated an overall consent on the need to continue raising awareness of the role of regulators in improving the quality of financial reporting and audits.

The participants in the SFC session discussed the attractiveness of the auditing profession to young people, the importance of technology, and the understanding of the value of audit among listed companies. The participants in the HKEX session asked about future initiatives concerning audit fees and late auditor resignations.



Ms Mary Leung, Head of Policy, Registration and Oversight (right) and Ms Tracy Chan, Director of Policy, Registration and Oversight (left) present at the briefing session for SFC.



AFRC conducts two briefing sessions for SFC and HKEC to share our concerns about auditor appointments and the setting of audit fees in Hong Kong.

## AFRC Housewarming Cocktail Reception

To officially celebrate the moving-in of the AFRC to the new office at Two Taikoo Place, we hosted a Housewarming Cocktail Reception on 15 September 2023. We were honoured to have the presence of Mr Christopher Hui, GBS, JP, Secretary for Financial Services and the Treasury as the Guest of Honour to perform the auspicious pig-cutting and lion dance eye-dotting ceremonies with Dr Kelvin Wong, SBS, JP, Chairman of the AFRC. Guests who attended the Housewarming enjoyed the cocktail and the lion dance performance to the fullest extent.

After the ceremonies, Mr Christopher Hui, Ms Salina Yan, JP, Permanent Secretary for Financial Services and the Treasury and Mr Joseph Chan, JP, Under-Secretary for Financial Services and the Treasury toured the office accompanied by the AFRC Board Members and Management.



Mr Christopher Hui, GBS, JP Secretary for Financial Services and the Treasury (4<sup>th</sup> from right) and Dr Kelvin Wong, SBS, JP (3<sup>rd</sup> from right) perform the auspicious pig-cutting ceremony accompanied by Ms Salina Yan, JP, Permanent Secretary for Financial Services and the Treasury (2<sup>nd</sup> from right), Mr Joseph Chan, JP, Under-Secretary for Financial Services and the Treasury (4<sup>th</sup> from left) and AFRC Board Members.



Mr Christopher Hui (left) and Dr Kelvin Wong (middle) dot the eyes of the lions.

## **Reappointment and appointment of NEDs and Honorary Advisers**

### **Reappointment and appointment of Non-Executive Directors and an Executive Director to act as the CEO**

On 29 September 2023, the Government announced the reappointment of Dr Kelvin Wong as Chairman and nine Non-Executive Directors (NEDs), and the appointment of two new NEDs for a term of two years from 1 October 2023 to 30 September 2025.

The reappointed NEDs are Mr Roger T Best, Mr Eugene Fung Ting-sek, SC, Mr Stephen Hung Wan-shun, Ms Miranda Kwok Pui-fong, Mr Stephen Lee Hoi-yin, Ms Rosita Lee Pui-shan, Mr Francis Siu Wai-keung, Dr Peter Wan Kam-to and Mr Edward Yuen Siu-bun. The newly appointed NEDs are Dr James C Lin and Mr Andrew Fung Hau-chung.

The Government also appointed Ms Janey Lai Chui-pik, Head of Inspection of the AFRC, as an Executive Director to act as the Chief Executive Officer (CEO) after the retirement of Mr Marek Grabowski on October 11, 2023.

Click [here](#) for profiles of NEDs and ED.

### **Appointment and reappointment of Honorary Advisers**

Over the years, the AFRC has been benefiting from the diverse experiences and collective wisdom of the Honorary Advisers who are appointed to provide advice to the AFRC at the committee level.

The AFRC has appointed Mr Hui Leung-wah, Herbert as an Honorary Adviser for a term of two years from 1 September 2023 to 31 August 2025. Mr Hui is the Finance Director and a member of the executive directorate of MTR Corporation Limited. He has abundant experience in financial reporting at major listed companies. A chartered Financial Analyst, he has extensive corporate finance and investment banking experience.

The AFRC has also reappointed the following Honorary Advisers for a term of two years from 1 October 2023 to 30 September 2025:

- (i) Dr Eva Chan
- (ii) Ms Ashley Khoo
- (iii) Mr Francis Mok
- (iv) Professor Zabihollah Rezaee
- (v) Mr Richard Tsang
- (vi) Ms Nancy Tse
- (vii) Mr Stephen Wong
- (viii) Mr Jackson Woo
- (ix) Professor Wayne Yu
- (x) Ms Ivy Cheung
- (xi) Ms Janet Li
- (xii) Mr William Mak

## Retirement of CEO Mr Marek Grabowski

Mr Marek Grabowski, CEO of the AFRC, retired on 11 October 2023 upon the expiry of his three-year term. To bid farewell to him, the AFRC hosted a farewell party on 29 September 2023.

On behalf of the Board, Dr Kelvin Wong, Chairman of the AFRC, expressed heartfelt gratitude to Mr Grabowski for his service and devotion during the past three years in which he oversaw the transformation of AFRC into Hong Kong's independent regulator of the accounting profession.

The AFRC wishes Mr Grabowski every success in his future endeavours.



CEO Mr Marek Grabowski (left) receives a souvenir from Chairman Dr Kelvin Wong (right).

## Contacts



**If you have any enquiries or comments, please feel free to contact us.**

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