

Press Release

29 July 2025

AFRC presents key findings and insights from its Inspection and Investigation & Compliance Reports to strengthen Transparency, Regulation, and Development

The Accounting and Financial Reporting Council (**AFRC**) today released two reports: the [Annual Inspection Report](#) and the [Annual Investigation and Compliance Report](#) for the year ended 31 March 2025. The profession is making progress in improving audit quality, supported by a clear commitment from firms in enhancing the quality of their audit work. However, recurring audit deficiencies remain, indicating the need for further improvements to ensure consistency and reliability across the profession.

Dr David Sun, Chairman of the AFRC, remarked, “Our inspections and investigations enable the AFRC to proactively identify potential threats to audit quality. We provide timely guidance to help the profession address current challenges and anticipate systemic risks. By ensuring that audit firms maintain high standards of competence and capability, we safeguard the integrity and reputation of our profession and the financial sector, while aligning our practices with international standards of excellence.”

Ms Janey Lai, CEO of the AFRC, emphasised the significance of publishing these findings and insights. She stated, “External audits are crucial for ensuring the accuracy and reliability of financial statements, which protect investors. We aim to strengthen transparency and accountability, ensuring stakeholders have clear and reliable information regarding audit quality when engaging with audit service providers, while fostering a culture of high-quality reporting and auditing.”

Overview of the 2024-25 Inspection Report:

The AFRC 2024-25 Annual Inspection Report shows some improvements in audit quality findings, with fewer PIE audits rated 4 (Significant Improvements required) compared to 2023. The report also flags continued challenges to audit quality, particularly in relation to first-year audits, audit fee pressures, and hasty client and engagement acceptance decisions.

Key Inspection Highlights

- **Improvements observed in Audit Quality ratings (AQR)**
Of the 46 PIE engagements inspected, 35% received AQR 1 or 2 (Good or Limited Improvements Required), an increase from 26% in 2023-24. The

number of PIE engagements inspected that received AQR 4 (Significant Improvements required) decreased from 46% to 28%. The improvement was most notable among Category A and B firms, where proactive leadership and timely remediation were evident.

Enhancing Transparency and Accountability

- The AFRC is increasing transparency by disclosing inspection results of individual Category A and B firms. This initiative aims to provide insights into firm-specific engagement inspection results, improving accountability and strengthening public trust in the audit process.
- **Recognising progress in one Category B Firm**
Category B firms have progressively shown more commitment to learning and improvement. One Category B firm received AQR 2 for both PIE engagements inspected for the first time. The improvement was linked to strong partner involvement and a sound understanding of client risks.

Areas of Concern

- **First-year audits and fee pressure**
The AFRC inspected 16 first-year audits in the 2024-25 fiscal year. Of these, 13 had lower audit fees compared to previous years, and 12 were rated 3 (Improvements required) or 4. Many of these audits were conducted under tight timelines due to late changes in auditor appointments. These practices threaten both the independence of auditors and the quality of audits.
- **Readiness of new PIE auditors entering the PIE market**
Inspection findings for new PIE auditors, especially Category C firms, reveal that a significant percentage of their inspected PIE engagements have received a rating of 4. This is primarily due to insufficient capacity and technical capabilities. As more firms enter the PIE market, the AFRC will be stepping up inspections of the new PIE auditors to address and mitigate potential risks.

“We are pleased to observe that an increasing number of PIE auditors are contributing to more informed governance decisions. Nearly all PIE auditors, subject to our 2024-25 inspections, have promptly shared their specific inspection findings with relevant audit committees,” said Ms Eva Lau, AFRC Head of Inspection.

Overview of the 2024-25 Investigation and Compliance Report:

The AFRC completed a total of 16 investigations, with 11 involving PIE auditors and five pertaining to professional persons. 14 of the completed investigations were referred to its Discipline Department for review of possible disciplinary actions.

Repeated deficiencies have been observed over multiple years in both completed and newly initiated investigations. Key issues include inadequate audit evidence, lack of professional scepticism, and insufficient professional judgement.

- **Impairment assessment of assets**

Some auditors relied solely on management's information when evaluating asset impairment, neglecting to obtain a thorough understanding of the business and assess the risk of management bias. Additionally, they failed to evaluate the work of the auditor's expert or conduct necessary additional procedures to obtain sufficient evidence.

- **Risk assessment procedures**

Certain auditors did not identify key indicators of potential fraud, primarily relying on management representations without exercising adequate professional scepticism. They overlooked contradictory evidence and failed to consider changes in economic conditions and the entity's environment, resulting in audit procedures that inadequately address the risks of material misstatement due to fraud.

- **External confirmations**

Some auditors did not thoroughly investigate exceptions or inconsistencies identified in external confirmations or non-responses to confirmation requests. They neglected to determine whether these indicate potential misstatements or any previously unidentified fraud risks, failing to perform the necessary further procedures.

The AFRC's findings highlight the importance of robust systems of quality management (SQM) within audit firms, noting that strong governance, effective workload monitoring, and timely remediation contribute to improved audit quality. However, recurring deficiencies, including insufficient partner accountability, non-compliance with independence requirements, and inadequate controls over audit documentation, require the immediate attention and action of firms, particularly small- and medium-sized practices.

To address these issues, the AFRC is intensifying its guidance and enforcement efforts, urging audit firms and engagement partners to allocate the necessary expertise and resources to ensure high-quality audits. Firms are encouraged to

proactively enhance their capabilities before accepting new engagements and to take full ownership throughout the audit process.

Additionally, the AFRC has introduced several resources including “AFRC Connect,” “Report Digest” videos and “Checkpoint” publication series to offer practical support for auditors. We also encourage audit committees to prioritise auditor selection based on quality and to ensure that audit fees are commensurate with the complexity of the engagement. These measures are essential to upholding rigorous standards and maintaining the integrity of the profession.

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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.afr.org.hk.

For media enquiries:

Joyce Mak

Manager, Corporate and Public Affairs

Tel: +852 3586 7889

Email: joycemak@afrc.org.hk

Chelsy Chan

Senior Officer, Corporate and Public Affairs

Tel: +852 2236 6066

Email: chelsychan@afrc.org.hk