

2024-25 Annual Inspection Report

July 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.

Highlights of 2024-25 Inspections

Category A firms¹

All 5
firms inspected

These firms audit
1,455
listed entities

87%
listed entities
by market capitalisation²

Category B firms¹

A total of 21 firms audit
939 listed entities or 3% of listed entities by
market capitalisation²

7
firms inspected

These firms audit
425 **2%**
listed entities listed entities
by market
capitalisation²

Category C firms¹

A total of 25 firms audit
73 listed entities or 0.1% of listed entities by
market capitalisation²

9
firms inspected

These firms audit
16 **0.1%**
listed entities listed entities
by market
capitalisation²

Engagements inspected

PIE Auditors

Non-PIE Auditors

51³

18

28

PIE engagements non-PIE engagements non-PIE engagements

51

firms inspected

with respect to **compliance with
AML/CTF requirements**

¹ Annex 1 provides details on the categorisation of PIE auditors.

² The figures represent percentages of the total market capitalisation of all equity securities as at 31 December 2023. As at that date, overseas auditors recognised under the AFRCO audit approximately 10% of listed entities by market capitalisation.

³ Five PIE engagements were selected for follow-up inspections and were not rated.

Introduction

High quality audits are crucial to maintaining public trust and confidence in financial reporting

Accurate and reliable financial reporting is fundamental for maintaining public trust and confidence in businesses and capital markets. Public interest entities (**PIE**) auditors must uphold the highest standards of professional ethics, rigorously follow auditing standards, and consistently exercise judgement and scepticism in fulfilling their responsibilities.

In these uncertain times, external audits are more important than ever, as investors and the broader public increasingly demand more timely, reliable, and transparent financial information to make informed decisions. As such, an external audit is not a compliance formality and should never be viewed as such.

While the inspection results showed some improvements, there remains a need for further progress, and firms should continue their efforts to improve

A commitment to continuous improvement is critical for achieving high quality audits, and each step forward will bolster public confidence in financial reporting and the audit profession. We observed some improvements in the inspection results, as the percentage of PIE engagements receiving an audit quality rating (**AQR**) of 4 (Significant Improvements required) decreased from 46% last year to 28% this year.

Further, a Category B firm that was subjected to our re-inspections received, for the first time, an AQR 2 (Limited Improvements required) for both PIE engagements inspected. This proves that firms of all sizes can deliver high quality audits when they commit whole-heartedly and turn that commitment into concrete action, especially by acting promptly on our inspection findings and observations. While progress was evident this year, recurring issues remain prevalent, and we urge all PIE auditors to keep striving for improvements.

Introduction

Core principles of auditing – objectivity, integrity and professional scepticism – remain the only constant amidst persistent changes

Auditors continue to navigate a complex and ever-changing business and economic environment. They need to embrace change, particularly digital transformation, to enhance efficiency and deliver more effective risk-based audits. While technology is reshaping the profession, the core principles of auditing – objectivity, integrity, and professional scepticism – remain unchanged. In this context, it is essential for auditors to critically assess their competence and capabilities before accepting or continuing a client or an engagement.

Recently, our concerns about underpricing, or lowballing, have increased. This trend appears to be driven in part by the current economic uncertainties, which have led many industries and listed entities to demand fee reductions. Moreover, we have also observed a more troubling pattern of changes of auditors, where some incoming auditors have offered significant fee discounts or accepted delayed payments to gain market share. We are concerned that these practices pose serious threats to auditor independence and compromise audit quality, as firms may not allocate sufficient resources to these engagements, thus undermining the value and trust that external audits are meant to provide.

Section 2 of this report provides further details of our observations on this issue, along with our expectations of auditors, audit committees, and management to address this troubling trend.

The AFRC is committed to safeguarding audit quality and will continue to intensify monitoring of firms that appear to be engaging in such practices. At the same time, we will strengthen our engagement with all relevant stakeholders, especially audit committees, to ensure that they recognise the pivotal role they play in the financial reporting ecosystem, in promoting and enhancing audit quality, and in reinforcing the importance of good governance.

Client acceptance and continuance are critical, and arguably the most critical, procedures in an audit, and they require the immediate attention of firm leadership.

Introduction

We are undertaking various initiatives to support the long-term development of the profession

Balancing regulation and development of the accounting profession is pivotal to achieving the AFRC's mission. Over the past year, we have expanded our resources to support the development of the accounting profession, particularly small and medium-sized practices (**SMP**).

Notable initiatives include the launch of the new publication series "Checkpoint" and the introduction of the new video series "AFRC Connect" and "Report Digest". These resources are designed to provide auditors with clear, accessible information to support their professional development and enhance audit performance. All of these materials are publicly available on the AFRC website or via the QR code provided in this report.

In parallel, we have provided – and will continue to provide – more guidance to firms on their remediation processes, which are essential for driving sustained improvements in audit quality.

Looking ahead

The world today is full of uncertainties, and many businesses are adjusting their strategies to mitigate risks while seizing opportunities. Auditors should remain vigilant about these uncertainties, critically assessing how they may affect their clients' businesses and operations, as well as the implications for their audits. To navigate these challenges, firms should continue to strengthen their systems of quality management (**SQM**). A robust, risk-focused SQM not only supports the delivery of high quality audits but also enables firms to respond effectively to emerging challenges.

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Section 1

Overview

I. Purpose of the AFRC inspections

The AFRC is committed to maintaining rigorous standards in financial reporting and auditing to ensure market stability and efficiency, ultimately contributing to the overall health of the economy. Inspection is one of our key regulatory tools for accomplishing this mission. Through inspections, the AFRC can assess audit firms' compliance with professional standards, laws and regulations, and drive improvements to ensure the accuracy and reliability of audited financial statements.

Our inspections are subject to appropriate oversight by the Inspection Committee and the Process Review Panel of the AFRC, which ensures that our inspections are carried out in compliance with internal procedures, maintaining fairness and consistency, and that our inspectors are exercising their regulatory powers appropriately.

II. Purpose of this report

This report summarises the work of the AFRC Inspection Department for the year ended 31 March 2025 (**2024 Inspections**), highlighting key findings, observations and insights from our inspections of:

- SQM of 33 firms, including both PIE and non-PIE auditors (**Section 3**);
- 97 audit engagements (including 51 PIE audit engagements) and corresponding assurance engagements, where applicable (**Section 4**); and
- 51 firms' compliance with AML/CTF requirements (**Section 5**).

By offering auditors insights into leading practices and providing audit committees and financial statement preparers with information on audit quality matters, we aim to motivate and drive auditors to improve their audits, with the active support of key stakeholders in the financial reporting ecosystem.

III. Our approach

What do we do

To effectively and efficiently exercise our inspection powers, we adopt a risk-based approach and apply the principle of proportionality when selecting firms and audit engagements for inspection. This approach enables us to remain agile and responsive to a changing environment, effectively utilising our resources to identify and address risks to audit quality. Further details of our inspection roles and duties are provided below.

Tri-faceted inspection model



How do we select firms and engagements for inspections

General inspections

Our general inspections typically include a review of a firm's SQM, a sample of its audit and assurance engagements, and an assessment of its compliance with AML/CTF requirements.

Risk-based selection

We employ a data-driven and risk-based approach in our firm and engagement selections. We identify and assess market, firm, and engagement-specific risks based on relevant information gathered from our ongoing market monitoring activities, intelligence sharing from other regulators, and information submitted periodically by firms. We consider, among others, the following risk factors in our selection processes:

- Market risks
 - Industries significantly affected by current economic conditions
 - Emerging industries or businesses, such as those related to virtual assets
- Firm-specific risks
 - Firms servicing a significant number of public interest entities
 - Firms without improvement in inspection results
 - New entrants into the PIE audit market
- Engagement-specific risks
 - Frequent or late changes of auditors
 - Disagreements over audit fees
 - The incoming auditor accepted a substantial reduction in the audit fee
 - Areas that present persistent audit challenges

Random selection

To enhance the robustness of our inspections, we also randomly select a small number of firms and engagements for inspection each year.

Specific scope inspections

From time to time, we may conduct a specific scope inspection of an auditor, usually a PIE auditor, in addition to our general inspections.

A specific scope inspection is initiated when a firm is assessed as being at a significantly higher risk of not delivering quality audits, such as a firm that has grown rapidly within a relatively short period, has accepted many PIE audit clients in the late stage of the reporting cycle, or has not taken the necessary remedial actions to address our inspection findings. This proactive and risk-based approach enables us to promptly address emerging risks in the audit market and mitigate the negative consequences they may pose to the audit and capital markets.

We may perform an in-depth inspection on a PIE engagement(s), a comprehensive review of a selected aspect(s) of a firm's SQM, an on-site review of a firm's remediation plan, or a combination of those during our specific scope inspection.

What action do we take after an inspection

Inspection

All firms subject to our inspections are required to submit remediation plans, with specific implementation timelines to address identified deficiencies.

We will consider the inspection results of a firm and the quality of its remediation plan in determining whether we should:

- increase its inspection frequency;
- accelerate its next inspection; and/or
- expand the scope of review in the next inspection.

If the quality of the remediation plan submitted by a firm does not meet our expectations, we will take follow-up action by requiring the firm to take specific remedial action, failing which may lead to regulatory consequences, including but not limited to further inspection or disciplinary action.

Investigation and discipline

Where matters, including but not limited to the following, are identified during our inspection, they will be referred to the Investigation and Compliance Department (**INC**), which may initiate an investigation:

- non-compliance with our statutory requirements;
- breach of CoE's requirements; or
- quality of an audit falling significantly below standard.

We will prioritise our disciplinary action against those who do not comply with our statutory requirements regarding inspections and remediations, as these are essential for the AFRC to discharge its statutory duties and drive firms to uphold audit quality.

PIE auditor registration

The AFRC considers all relevant information in its possession, including past inspection results, when handling registration and renewal applications for registered PIE auditors. This applies to adding the name of a person to a PIE auditor's list of registered responsible persons, including engagement partners, engagement quality reviewers (**EQR**) and quality control system responsible persons (**QCSR**P).

Applications will take longer to process when we have concerns about an individual's or a firm's capabilities and competencies in servicing listed entity audit clients.

Where we have significant concerns about the quality of audit work of a PIE auditor, we may impose conditions (restrictive or non-restrictive) or amend existing conditions, if any, when it renews its registration.

What we do beyond inspections to drive improvement

We have been communicating with firm leadership and publishing resources via multiple channels to foster a quality-driven culture across firms, driving continuous improvement in the accounting and auditing ecosystem. Below is a summary of publications and alerts issued by us in 2024 and the first half of 2025, as well as our engagements with firm leaders.

Meetings



Briefing sessions and one-on-one meetings

We held two sharing sessions to brief firm leaders and QCSRP about the key findings and insights from our 2023 inspections.

We met with firm leaders in person to **reinforce the importance of a quality-driven culture** and remind them of their duties to deliver high quality audits.

Publications



Audit Focus – provides **key reminders** to auditors for year-end audits

Our 2024 Audit Focus provided critical reminders on effectively identifying and responding to the elevated risks in financial reporting and auditing created by the current uncertain economic conditions.



Inspection Insights – highlights **key observations and insights from inspections**

Our 2024 Inspection Insights highlighted the importance of tone at the top for ensuring effective root cause analysis (**RCA**) and remediation.



Checkpoint – provides **practical guidance** to auditors on specific audit matters

In January and March 2025, we issued two Checkpoints relating to IT audits and auditors' reporting on licensed corporations (**LC**), respectively.

Video series



AFRC Connect – promotes **audit quality** and advances **professional excellence within the profession**

In January 2025, we launched our debut episode on risk assessment. In April 2025, we launched another episode on IT audits.



AFRC Report Digest – presents **key takeaways** from our publications

In February 2025, we distilled our essential takeaways from the 2024 Audit Focus and communicated them via our AFRC Report Digest.

Communication Channels



Outreach activities
AFRC website
Social media



Publications



Videos



IV. Inspection results

(a) PIE auditors

We selected five Category A firms, seven Category B firms, and nine Category C firms for our 2024 Inspections, and they are:

Table 1. List of PIE auditors inspected in 2024

Category A Firms (5 firms)	Category B Firms (7 firms)	Category C Firms (9 firms)
<ul style="list-style-type: none"> • BDO Limited (BDO) • Deloitte Touche Tohmatsu (Deloitte) • Ernst & Young (EY) • KPMG • PricewaterhouseCoopers (PwC) 	<ul style="list-style-type: none"> • D & PARTNERS CPA LIMITED • HLB Hodgson Impey Cheng Limited (HLB) • MOORE CPA LIMITED • Prism Hong Kong Limited¹ • RSM Hong Kong • SHINEWING (HK) CPA Limited • ZHONGHUI ANDA CPA Limited 	<ul style="list-style-type: none"> • Conpak CPA Limited² • Global Link CPA Limited¹ • Infinity CPA Limited • JH CPA Alliance Limited • Jon Gepsom CPA Limited² • Kenswick CPA Limited • LIF & Wong CPA Limited • Suya WWC CPA Limited³ • Zenith CPA Limited

¹ Only subject to engagement inspections

² Engagement inspections in progress as at 31 March 2025

³ Only subject to SQM inspection and ACMI

We completed inspecting 51 (2023: 56) PIE engagements in 2024, including five (2023: two) that were selected for follow-up inspections. The table below presents the PIE engagement inspection results for 2023 and 2024, excluding:

- two in 2023 and five in 2024 that were subject to follow-up inspections as they were not rated; and
- PIE engagement inspection results of three Category C firms because they were either undergoing a SQM inspection and an ACMI, or had ongoing engagement inspections as at 31 March 2025.

Table 2. Number of completed PIE engagement inspections by category of firms and their AQR

Category	2024 Inspections					2023 Inspections				
	Total number of firms inspected	Number of PIE engagements inspected				Total number of firms inspected	Number of PIE engagements inspected			
		Total	AQR of 1 or 2	AQR of 3	AQR of 4		Total	AQR of 1 or 2	AQR of 3	AQR of 4
Category A ¹	5	24	14	9	1	6	31	14	12	5
Category B ¹	7	16	2	7	7	8	17	0	1	16
Category C	6	6	0	1	5	6	6	0	2	4
Total	18	46	16	17	13	20	54	14	15	25

¹ HLB was categorised as a Category B firm in the 2024 inspections and a Category A firm in 2023. For comparative purposes, if HLB were a Category A firm in 2024, our inspections of 28 PIE engagements completed by Category A firms would reveal that 50% received an AQR of 1 or 2 (2023: 45%, 14 of 31 PIE engagements completed by Category A firms).

The Category A and B firms listed below received an AQR of 4 (Significant Improvements required) for at least one of their PIE engagements inspected in our 2024 inspections.

- BDO
- Prism Hong Kong Limited
- RSM Hong Kong
- SHINEWING (HK) CPA Limited
- ZHONGHUI ANDA CPA Limited

Annex 2 presents the results of the 2023 and 2024 PIE engagement inspections for individual Category A and B firms. As Category C firms each audited only a very small number of PIE engagements annually, collectively representing just 0.1% of listed entities by market capitalisation as at 31 December 2023, their inspection results are not disclosed on an individual basis to safeguard the anonymity of the PIE in this report.

Each PIE engagement subject to our inspection is rated based on the number and severity of its inspection findings. We use AQR to describe our overall assessment of the quality of a PIE audit completed by a firm. There are four categories of AQR and they are:

- 1 – Good
- 2 – Limited Improvements required
- 3 – Improvements required
- 4 – Significant Improvements required

1 represents the highest score and 4 the lowest score.

In interpreting the inspection results, it is important to recognise that our ratings do not necessarily indicate that the financial statements are material misstated.

Read Section 1.III of our 2023 Annual Inspection Report for further details of AQR and its importance.

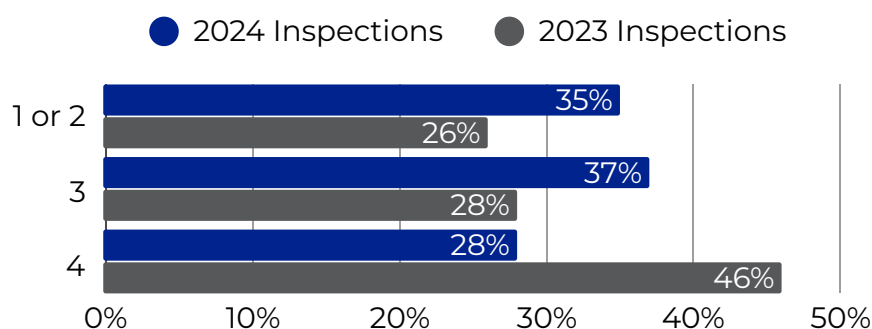


Caveat – how to use AQR for different categories of firms

Category A firms are inspected annually, while Category B and C firms are inspected at least once every three years. The inspection results for Category A firms are firm-specific and comparable over time. Since different Category B and C firms are inspected each year, the results for these categories may not be comparable across years.

Given the relatively small number of engagements inspected for each firm in a given year, the AQR presented above are not necessarily indicative of the audit quality across their entire portfolio.

The bar chart below presents the percentage of PIE engagements inspected in 2023 and 2024 by their AQR category.



Larger firms are contributing to the improvements in the 2024 inspection results

- The year-on-year percentage of inspected engagements requiring significant improvements (AQR of 4) decreased from 46% in 2023 to 28% in 2024.
- This improvement is observed in larger firms, particularly those in Category A and B firms that we have previously inspected.
- The inspection results of Category C firms were significantly below standard, especially among those inspected for the first time in 2024.

All 5

Category A firms
(audit 1,455 listed
entities or 87% of
listed entities by
market
capitalisation)

- Our inspections of 24 PIE engagements revealed that 14, or 58%, received an AQR of 1 or 2, largely consistent with the previous year (2023: 14 of 26 PIE engagements completed by Category A firms, excluding HLB, or 54%).
- Only one engagement received an AQR of 4 in 2024, compared to five in 2023. This significant reduction suggests that these firms are on the right track in improving audit quality.

- Our 2024 inspection results revealed mixed results for the Category B firms.
- While four firms demonstrated meaningful improvement in their inspection results compared to their previous performance, with a decrease in the number of engagements rated 4, three others did not show the required improvement.
- It is encouraging to see that one of the Category B firms showed a significant improvement by receiving an AQR 2 for both PIE engagements inspected. This improvement is primarily attributed to the partners' sufficient and timely involvement throughout the entire audits, as well as their thorough understanding of their clients' businesses and operations, which enables the engagement teams to properly identify audit risks and design corresponding audit responses.

7 of 21

Category B firms
(audit 425 listed
entities or 2% of
listed entities
by market
capitalisation)

6 of 25

Category C firms
(audit 7 listed
entities or 0.1%
of listed entities
by market
capitalisation)

- All six PIE engagements inspected were rated 3 or 4, of which five, or 83%, of the inspected engagements were rated 4. All these firms must take robust action to improve their audit quality.
- In 2024, five firms were subjected to first-time inspections, and their inspection results were all below a satisfactory level.
- More audit firms are entering the PIE audit market, with existing Category C firms increasing their market share. In view of this, the AFRC will be allocating more resources to inspecting Category C firms to address the specific risks associated with this category of firms.

Targeting firms with higher quality risks through specific scope inspections



Our market monitoring activities have identified firms with potential audit quality issues, such as those taking on engagements that do not appear to be proportionate to their size, resources, and expertise, or significantly increasing the number of PIE audits without a commensurate increase in resources. To address these concerns, we have conducted and will continue to undertake more targeted inspections.

In 2024, we identified one Category B firm and one Category C firm for specific scope inspections. We inspected one PIE engagement for each firm, and both engagements received an AQR of 4 (Significant Improvements required). We required both firms to take urgent and immediate remedial actions to address our findings and improve the quality of their work. We will closely monitor whether these firms implement the necessary remedial actions and will continuously assess their audit quality through more frequent inspections. In the meantime, these cases have been referred to our INC for additional evaluation and action.

Holding firms accountable for their remediations to drive improvement



Remediation is a key driver for audit quality improvement. All firms subject to our inspection are required to conduct RCA and formulate remediation plans within a specified time frame to address the findings of our inspection. This is essential for us to determine the appropriate follow-up action under the AFRCO.

Failure to effectively remediate significant findings raises serious concerns about a firm's leadership commitment to audit quality and the effectiveness of its SQM. Please read our Inspection Insights – Root Cause Analysis and Remediation: A Call to Action for Quality Improvement for details on the important role of firm leadership in this process and how they can contribute.



Fostering ongoing and enhanced communication around audit quality

All PIE auditors are allowed to share a copy of the PIE engagement inspection report with the audit committee to which the report pertains, without requiring our prior approval. This enables PIE auditors to share the report with the audit committees promptly.

We are observing more PIE auditors responding to our guidance and promptly communicate their engagement inspection results and findings with the audit committees. As at 30 June 2025, we are pleased to note that nearly all PIE auditors who received their 2024 inspection reports have already shared their engagement inspection results and findings with the respective audit committees.

This enhanced communication represents a significant step in firms' commitments to upholding audit quality through transparency and accountability. With this transparency, audit committees are provided with more relevant information to oversee the audit process, including auditor selection and reappointment, ensuring that high standards are maintained.

We will continue to monitor the situation to ensure that this positive and necessary trend continues.

(b) Non-PIE auditors (other than PIE auditors)

We inspected 14 non-PIE auditors in 2024, compared to 13 in 2023. We inspected their SQM, a sample of their audit and assurance engagements, as well as their compliance with the AML/CTF requirements.

To benefit the wider community of non-PIE auditors, we launched a new series of publications and videos to help them raise their audit quality.

Unlike PIE engagements, we do not assign AQR to non-PIE engagements. Yet, our inspections continued to show a high number of significant findings, with the table below showing areas where we have identified the highest number of deficiencies.

Inspections of non-PIE audit engagements	
Common findings	What have gone wrong
Ineffective risk assessment .	The inability to identify risks specific to audit clients could result in missing key areas where material misstatements are likely.
Insufficient or no testing on the reliability (i.e., accuracy and completeness) of the information provided by clients .	Undue reliance on management representation or information left inaccurate or incomplete data undetected.
Insufficient or no procedures to ensure that the test samples were representative of the total population .	Biased or incomplete audit evidence, undermining the validity of audit conclusion.

We continued to identify recurring inspection findings in several key areas that we reviewed most frequently, including revenue recognition, expected credit losses (**ECL**) on receivables, and journal entry testing. Auditors should refer to Section 4 of our 2023 Annual Inspection Report for specific details, including details of the procedural deficiencies, their root causes, and how they can be addressed.



2023 Annual
Inspection
Report



Our SQM inspections have identified the following common findings, which may apply to all firms.

Inspections of SQM	
Common findings	What have gone wrong
Non-compliance with independence requirements Lack of or insufficient policies and procedures to identify, evaluate and address the threats to auditors' independence arising from a long association with clients and the provision of non-assurance services.	At the engagement level, familiarity, self-review or self-interest threats undermined objectivity and result in an inappropriate audit opinion.
Insufficient intellectual resources and training Insufficient guidance to support the consistent delivery of quality audits. Specifically, firms lack a defined audit sampling approach to test the reliability of information provided by audit clients.	Inconsistent procedures, inappropriate judgement, insufficient evidence increased the risk of audit deficiencies.
Insufficient controls over the integrity of audit documentation Lack of or insufficient policies or procedures to ensure the integrity of archived audit documentation and control retrieval or access to archived files.	Insufficient controls over the retention and retrieval of archived audit files increased the risk of data loss and improper modification to the archived audit documentation.

Our newly launched short video series, “**AFRC Connect**”, offers practical insights and technical reminders on specific topics drawing on observations from our inspectors. SMP may find them particularly useful in helping their professionals acquire the necessary knowledge to uphold audit quality.



How Important is Audit Risk Assessment?



Understand and Evaluate IT Risks and Controls



Stay tuned for our next AFRC Connect videos.

V. Key drivers for improvements in audit quality

Several larger PIE auditors identified the following key drivers that contributed to their improvements in audit quality, offering valuable insights for others seeking to make improvements.



Instil a quality culture and encourage right behaviours:

These firms recognised the importance of fostering an environment that prioritises quality and integrity. This involves (a) cascading the right tone from firm leaders to audit personnel to encourage the right behaviours, and (b) devoting sufficient resources to improve audit quality, including taking timely and robust remedial actions in response to inspection findings.

Strengthen monitoring: These firms have enhanced their monitoring procedures and processes for ensuring consistent delivery of quality audits, which include (a) enhancing quality review procedures performed during the audit and before its completion, (b) establishing audit milestones which indicate the expected involvement of engagement partner and EQR in different phases of an audit, and (c) using technology to monitor the completion of each audit milestone.

Prioritise talent management and development:

These firms continued to develop the professional competence and capabilities of their audit personnel, including both technical knowledge and soft skills, thereby fostering team continuity and facilitating effective sharing of knowledge and experience.

Act on regulators' expectations:

These firms demonstrated positive changes in compliance attitudes, aligning with the requirements of professional standards. They were receptive to feedback from regulators and maintained a cooperative and constructive relationship with them.

Section 2

Change of Auditor

I. Overview

In both 2023 and 2024, more than 10% of Hong Kong-listed entities changed their auditors, with some entities even changing their auditors more than once. Notably, approximately one-third of these changes involved switching auditors from a larger firm to a smaller firm, i.e., from a Category A firm to a Category B or C firm or from a Category B firm to a Category C firm. In other words, the financial statements of these listed entities were subject to first-year audits by incoming auditors that are generally smaller in size than their predecessors.

As listed entities commonly change auditors due to an inability to reach an agreement over audit fees and/or unresolved issues identified by the outgoing auditor, this creates significant challenges to the work of the incoming auditors.

In general, incoming auditors spend more time and effort on first-year audits, as they start from the beginning. For instance, incoming auditors need to gain knowledge of and understand their new clients' businesses and operations, including the accounting policies they have adopted, to perform a first-time risk assessment. Additionally, they may also need to address any unresolved issues identified by the outgoing auditors and perform procedures that are not typically required for recurring audits, such as inventory rollback, to conclude that the opening balances do not contain misstatements that materially affect the current period's financial statements. These factors increase the complexity of first-year audits, highlighting the need for additional time and effort, as well as the involvement of more experienced audit personnel.

Given the additional time and effort required for first-year audits, the remuneration of the incoming auditor should be comparable to, or even exceed, that of the outgoing auditor. Yet there is a concerning trend of incoming auditors being paid considerably less than their predecessors. This situation raises questions on whether the audited entities may have engaged in opinion shopping, switching to auditors who may not be as diligent but are willing to provide a favorable view on their financial statements.

II. Our approach

To address these concerns, the AFRC has been taking various measures, including increasing our engagement with audit committees and listed companies to reinforce the importance of good governance and increasing our collaboration with the Securities and Futures Commission (**SFC**) and The Stock Exchange of Hong Kong Limited (**SEHK**) on intelligence sharing for follow-up action. The figure below illustrates additional measures we are taking:



III. Our observations

Insufficient resources compromise audit quality. Our inspections revealed that initial audits, particularly those associated with significant reductions in audit fees or late auditor changes, generally received a poor AQR.

Number of PIE engagements inspected				
	Total	AQR		
		1 or 2	3	4
First-year audit engagements	16	2	4	10
Key reasons* for auditor changes				
Disagreements over audit fees	13	1	4	8
Audit issues, internal resources or corporate governance considerations	3	1	0	2

* Based on the reasons disclosed in the announcements made by the listed entities

Fee squeeze may compromise audit quality

Out of the 16 first-year audits inspected, 13 received lower audit fees compared to their predecessors. 12 of these 13 audits were rated 3 or 4, indicating improvements or significant improvements were required.

The fee reduction accepted by the incoming auditors for these 13 engagements ranged from 3% to as high as 47%.

It is disappointing to note that some of these auditors did not even estimate the resources required before submitting their fee proposals to the companies.

Audit quality can easily be compromised when auditors face resource constraints. Unreasonably low audit fees often lead to insufficient time, resources, and expertise being allocated to the audits.

We have encountered instances where the incoming auditors did not perform critical audit procedures in their first-year audits, such as resolving issues reported by the outgoing auditors and testing opening balances.

Lowballing raises serious concerns about the independence of auditors and the quality of audits. Firms may aim to cross-sell non-audit services and/or spend less effort or cut corners in audit engagements.

When the audit committee receives a fee proposal with significant audit fee discounts, they should carefully evaluate the proposed scope of audit services, the qualifications and experience of the audit firm, the resources to be allocated, and the basis used to determine the fees.



Significant audit fee discounts can lead to compromised audit quality and expose directors to regulatory, legal, and reputational risks if material financial statements go undetected.

Time pressure created by the late auditor change may compromise audit quality

Out of the 16 first-year audits inspected, eight listed entities changed their auditor late, i.e., changes occurred one month before or even after the financial year-end date. As a result of the late changes, compressed audit timelines may lead to poor audit planning and quality – none of these eight inspected engagements received satisfactory inspection results with six of them receiving an AQR of 4.

Firms must, therefore, implement robust procedures to ensure that sufficient time and resources are secured before taking on new engagements. They must complete all necessary audit procedures before issuing audit opinions. They should not commit to an unrealistic audit timetable based solely on management requests to meet the reporting deadline.

The AFRC will intensify its monitoring of the audit market and will increase inspections of firms that are currently engaging in, or have previously engaged in, any of these unhealthy practices. If such practices are found to have caused a significant deterioration in audit quality, we will take prompt enforcement action against the firms involved.



Call for collective efforts in upholding audit quality and building trust

Following the AFRC's concerted efforts to address boilerplate or generic disclosures about the reasons for the change of auditor, we see improvements in the quality of these disclosures in recent years.

Stakeholders, such as investors and banks, now receive clearer and more transparent information regarding the reasons why directors propose a change of auditor, as well as whether these changes are associated with unresolved matters, suspicious transactions, or potential corporate governance issues, which are essential for them to make their decisions.

Every step forward counts. All stakeholders in the financial reporting ecosystem play a critical role in ensuring and upholding the quality of audits. It is essential for the audit committee to recognise the value of an external audit and to carefully select and appoint an external auditor based on the auditor's competence and capabilities to deliver a high quality audit. Audit fees should not be the sole or overriding factor in determining an auditor's appointment. Therefore, we urge the following stakeholders to:



Auditors

Establish a strong tone at the top that prioritises audit quality over short-term gains, recognising that this commitment is essential for fostering credibility and trust in financial reporting and the accounting profession.



Management

- Have open and transparent communication with the auditor throughout the audit process.
- Provide the auditor with complete and accurate financial and non-financial information required for the audit.



Audit committees

- Oversee auditor changes, ensuring an objective, fair and transparent selection process.
- Understand how the auditor's SQM can support the consistent delivery of quality audits.
- Ensure effective two-way communication with the external auditor.
- Ensure that the auditor is reasonably remunerated for their work.



For more details, read our market alerts and guidance.



Guidelines for Effective Audit Committees Selection, Appointment and Reappointment of Auditors (December 2021)

Open letter regarding late auditor resignations (October 2022)



Follow-up open letter on auditor changes (January 2023)

Guidance Notes on Change of Auditors (September 2023)



Section 3

Inspections of Systems of Quality Management

I. Our approach

We continued to adopt a risk-focused, cyclical approach in our 2024 inspections of all the Category A firms' SQM with a focus on governance and leadership, resources, and monitoring and remediation process. We followed the same approach we used in 2023 in this year's inspections of other auditors' SQM, details of which are outlined in Section 2.I of our 2023 Annual Inspection Report.

II. Our observations

Leading practices

In 2024, our inspections observed some leading practices, mostly from the Category A firms. We encourage all firms to learn and adopt these leading practices for their continuous improvement of audit quality.

Governance and leadership



Foster a strong tone at the top that focuses on integrity, independence and quality

- Leadership roles are taken up by individuals responsible for ethics and risk management.
- Assign an independent and dedicated team to investigate potential integrity issues or whistleblower complaints.



Accountability for audit quality

- Audit quality is a key factor in evaluating and compensating audit partners, and it is a determining factor for admission to partnership.
- Create an environment where high quality audits are recognised and valued.



Open and effective communication

- Build a culture where staff can speak up about their concerns and any observed misconduct without fear of retaliation.
- Establish clear and accessible policies and procedures, including having multiple channels for reporting any observed misconduct, such as hotlines, online portals, or designated personnel.
- Mandate annual completion of ethics and integrity-related training with real-life examples provided.



Transparency with stakeholders

- Publish annual transparency reports.
- Report critical incidents regarding audit quality or the firm's SQM to the AFRC promptly.

Resources



Partner workload monitoring

- Monitor partner workload by using metrics, such as the partner's supervising hours, chargeable hours, and number of engagements, and set predefined thresholds to identify partners who may be overloaded.
- Workload monitoring encompasses all work commitments of an audit partner, e.g., management duties and time spent serving the community.



Continuing professional development (CPD)

- Use the AFRC's publications as part of their training materials.
- Monitor partners' and qualified staff's compliance with CPD requirements. For registered PIE auditors, ensure that all responsible persons complete at least five verifiable hours of CPD activities related to PIE engagements annually.



Technological tools

- Use data analytics tools for risk assessment procedures and journal entry testing.
- Use audit workflow software to uphold the integrity of audit documentation.
- Use technology to track milestones in an audit, including the assembly of final audit files.



Sufficient partner involvement is the cornerstone of audit quality

The workload of an audit partner directly impacts the amount of time he or she can dedicate to each audit, which ultimately affects the quality of an audit. The 2024 inspections revealed that some audit engagement partners manage relatively large client portfolios, raising concerns about their abilities to devote sufficient attention to each engagement and ensure the quality of the audits. Firm leadership should ensure that their partners' workload monitoring is effective in identifying partners who have heavy workloads.

Monitoring and remediation process



Effective monitoring

- Maintain strict oversight of objectivity at all levels, including the partner level.
- Conduct pre-issuance reviews to ensure that accounting and auditing issues are satisfactorily resolved before the audit report is issued.



Read our Inspection Insights – Root Cause Analysis and Remediation: A Call to Action for Quality Improvement for leading practices on the remediation process.



Objective monitoring free from pressure and blind spots

Firm leadership should ensure that the **objectivity** of individuals performing monitoring activities (**Monitoring Reviewers**) is not compromised by:

- **Self-review threat:** Assigning individuals to monitor SQM responses in which they were involved in the design, implementation, or operation.
- **Inadequate authority or competence:** Assigning individuals who lack the appropriate qualifications, experience, or authority to effectively perform the review.

Findings identified from the SQM inspections of Category B and C firms

We observed that many Category B and C firms have established their SQM based on the quality management manuals developed by the Hong Kong Institute of Certified Public Accountants (**HKICPA**) or service providers. Firms need to customise these resource tools for their specific circumstances to ensure compliance with HKSQM 1 *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements*.

Our 2024 inspections indicated that Category B and C firms may need to urgently review and enhance their policies and procedures to mitigate the following threats to auditors' independence:

- Fee dependency on a single or a few PIE audit clients (especially for Category C firms newly entering the PIE market);
- Non-compliance with the rotation and cooling-off period for audit partners and/or EQR; and
- Client-to-auditor employment offers.

The table below summarises examples of SQM findings identified from our 2024 inspections of some Category B and C firms, as they did not:

Risk assessment process	Governance and leadership	Relevant ethical requirements	Acceptance and continuance
<p>Address specific quality risks</p> <p>Identify information indicating the need for changes in quality objectives, quality risks and responses</p>	<p>Establish a quality-oriented recognition and accountability framework for ultimate/operational responsible individuals</p> <p>Demonstrate a commitment to quality through leadership's actions and behaviours</p>	<p>Effectively monitor independence compliance for partners and staff</p> <p>Effectively identify and address independence threats from the provision of non-audit services</p> <p>Provide ethics training to partners and staff</p>	<p>Conduct client and engagement continuance assessment before the reappointment is sought</p> <p>Accept clients and engagements with a robust evaluation of the firm's sufficiency of resources</p>
Engagement performance	Information and communication	Resources	Monitoring and remediation process
<p>Evaluate the objectivity and eligibility of EQR</p> <p>Ensure the integrity of archived audit documentation</p> <p>Sufficiently direct and supervise the engagement teams</p>	<p>Communicate with the audit committees how the firm's SQM supports the consistent delivery of quality audits</p> <p>Ensure the accuracy of information submitted to the AFRC</p>	<p>Effectively monitor partners and staff workload</p> <p>Establish a quality-oriented recognition and accountability framework for partners and staff</p> <p>Evaluate the competencies of service providers, including the component auditors not within the firm's network, external IT service providers, auditors' experts and EQR</p>	<p>Sufficiently design the nature, timing or extent of monitoring activities</p> <p>Investigate the root causes of identified deficiencies, and design and implement corresponding remedial actions</p> <p>Evaluate the objectivity of Monitoring Reviewers</p>

Category B and C firms can enhance their SQM by designing and implementing appropriate policies and procedures to address the above findings with reference to the leading practices summarised in the subsection headed "Leading practices" above.

Section 4

Engagement Inspections

I. Our approach

Our engagement inspection evaluates an auditor's compliance with applicable professional standards, laws, and regulations by reviewing selected aspects of an audit.

Our inspections evaluate the quality of the audit work in the selected focus areas. It is important to note that our inspections do not cover every aspect of the audit engagements. Therefore, our findings do not necessarily indicate misstatements in the financial statements. Rather, they highlight findings regarding the quality of the audits performed in the areas inspected.

Audit areas that we reviewed most frequently include revenue recognition, impairment of non-current assets, and receivables, which are typically material to the financial statements or identified as key audit areas by auditors. Additionally, we reviewed how auditors tested journal entries and other adjustments to address possible material misstatements due to fraud or management override of controls for every engagement we inspected.

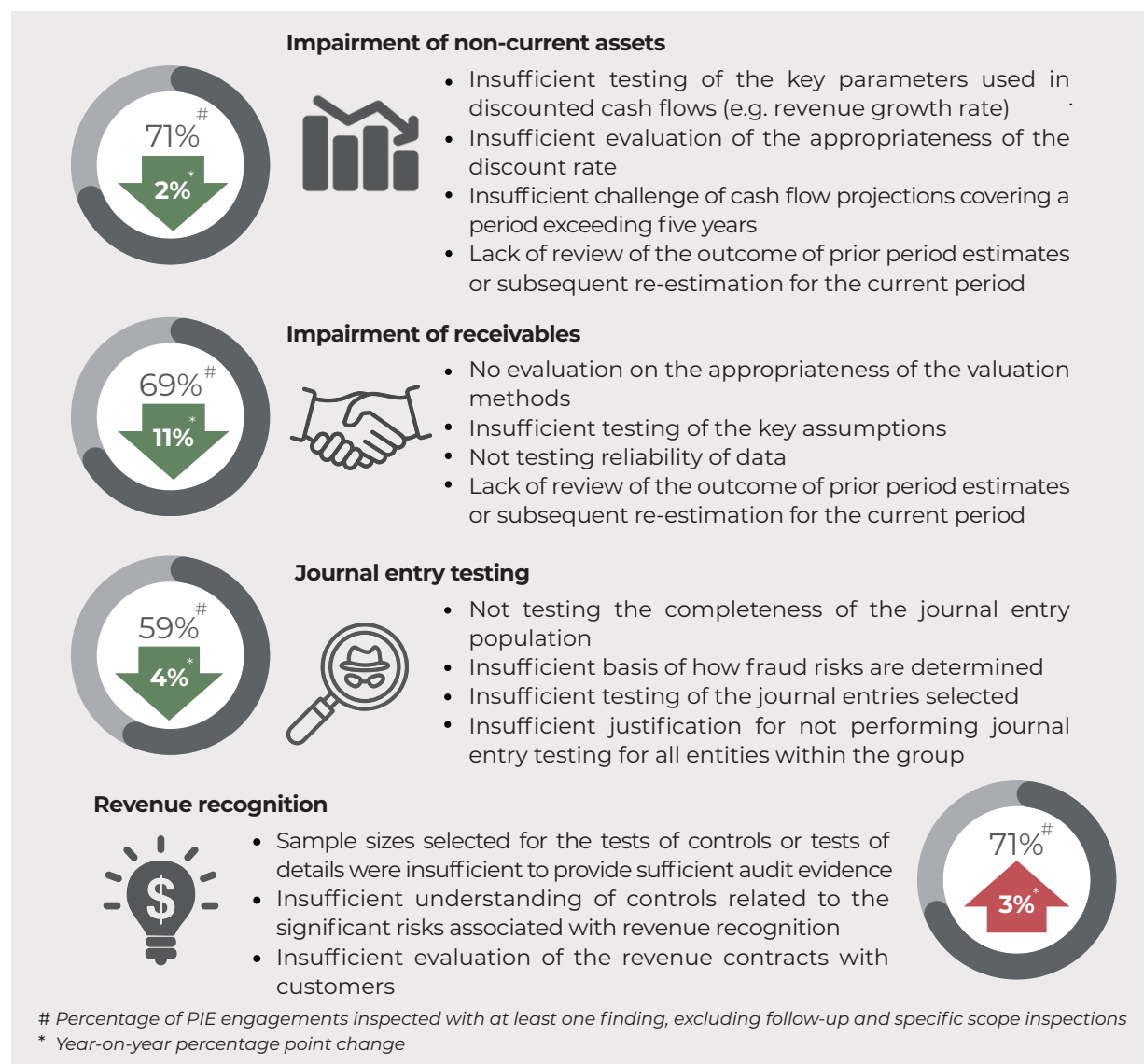
II. Our observations

Areas of focus in our 2024 inspections

We inspected 51 PIE engagements and 46 non-PIE engagements in 2024. Except for those discussed further on pages 25 to 27, the nature of this year's findings was largely consistent with those identified in our 2023 inspections.

While we observed some improvements this year in three of the four most frequently reviewed areas, the level of deficiencies remains high. As these areas involve accounting estimates and significant management judgement, auditors should enhance their application of professional scepticism to achieve more substantive improvements.

Below presents a summary of the key findings identified for each of the four most frequently reviewed areas, the level of deficiencies and the year-on-year improvement or deterioration.



Auditors should read Section 3 of our 2023 Annual Inspection Report for details of these common findings, and take robust action to prevent their recurrence.



2023 Annual
Inspection Report



Inspection findings specific to audit and assurance engagements for authorised institutions

The ongoing uncertainties in the macroeconomic environment, coupled with fluctuations in interest rates and geopolitical tensions, have created challenges for various industries, including the banking sector. As a result, bank audits are becoming increasingly complex, especially when auditors assess the appropriateness of allowances for expected credit losses on loans and fair values of financial instruments.

Considering the crucial role that banks play in maintaining financial stability in Hong Kong and the significant public interest they represent, we will place a greater emphasis on bank audits in our future inspections. The table below highlights key findings from our 2024 inspections of two unlisted bank audits.

Audit engagements		Assurance engagements
Control tests	Substantive tests	Compliance tests
Insufficient understanding of the client's key business processes for an effective risk assessment	Insufficient testing of key accounting estimates in ECL models	Insufficient understanding of the completion instructions and relevant regulatory requirements, which impacted the effectiveness of certain compliance testing procedures
Inappropriate design and execution of control tests	Insufficient testing over the application of staging criteria	Insufficient work over the compilation of banking returns
Insufficient evaluation of the adequacy of the work of auditor's experts		
Insufficient testing of the reliability of client-produced information before using the information as audit evidence.		

Inspection findings specific to audit and assurance engagements for LC

We inspected 18 (2023: 22) audit and related assurance engagements of LC completed by both PIE and non-PIE auditors in 2024. Our inspections highlighted the importance of assigning engagement team members with the appropriate industry knowledge and experience to deliver quality audits for LC.

The most common audit deficiencies were related to insufficient testing of brokerage income and insufficient evaluation of the appropriateness of ECL on receivables. In assurance engagements, we identified significant findings in auditors' work in assessing LCs' compliance with the Securities and Futures (Client Money) Rules and the Securities and Futures (Client Securities) Rules. Auditors should read our Checkpoint – Reminders for auditors' reporting on licensed corporations for further details.



Areas that require special attention

Our 2024 inspections also focused on areas perceived to be more challenging for auditors in respect of their 2023 year-end audits, which included:

Use of information technology (IT)

Companies are utilising more sophisticated IT systems in their daily operations. Many companies are undergoing digital transformation, such as implementing enterprise resource planning systems or using online platforms, to enhance their operations and remain competitive. Our inspection placed a greater focus on audits that heavily rely on the clients' IT systems in daily operations and preparation of financial statements. Our key inspection findings include:



Insufficient understanding of the IT environment:

Information systems supporting the business processes related to the preparation of the financial statements

Information flow between information systems

Cybersecurity environment and associated risks



Insufficient audit procedures in evaluating the effectiveness of general IT controls (GITC) and IT application controls (ITAC):

Not testing the completeness of the GITC testing population

Insufficient coverage of ITAC scenarios to support the effectiveness conclusion

No assessment was performed to determine the applicability of the evidence obtained after year-end to support the effectiveness of controls during the reporting period



Insufficient evaluation of deficiencies identified in the testing of GITC and ITAC:

Severity and impact of the identified deficiencies

Identification and testing of compensating controls

Consideration of other audit procedures in mitigating the underlying risks of the identified deficiencies

Whether deficiencies are considered significant individually or in aggregate with other deficiencies

Read our Checkpoint – Obtaining an Understanding of the Audit Clients' IT Environments and watch our AFRC Connect – Understand and Evaluate IT Risks and Controls for further details on these findings and practical guidance on how auditors can obtain a proper understanding of their clients' IT environments and appropriately assess the risks associated with their clients' uses of IT in financial reporting.



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



AFRC Connect –
Understand and
Evaluate
IT Risks and
Controls



Investment property valuations

Amid a volatile economic environment, the valuations for investment properties, including those in the Chinese Mainland and Hong Kong, fluctuated significantly. The downward pressure on property prices most notably affected listed entities with large investment property portfolios. With a reduced volume of property transactions, management may find it challenging to obtain sufficient data and to base assumptions on comparable transactions. Auditors may in turn encounter substantial difficulties in evaluating the appropriateness of property valuations. Our key inspection findings include:



Insufficient evaluation of the appropriateness of key assumptions, e.g., market rents, capitalisation rates, and adjustments made by valuers



Insufficient evaluation of the appropriateness of key data, e.g., tenancy details and comparable transactions, used in the valuations

Bank borrowings and covenants

Persistent high interest rates along with other factors could negatively impact a listed entity's financial position and performance, particularly for those with high gearing ratios. This may lead to breaches of bank covenants, which could trigger immediate repayment of outstanding bank borrowings and/or cross-default, or cause banks to impose stricter conditions for future borrowings, all of which would adversely affect an entity's ability to continue as a going concern.

Our inspections identified the following key findings in the audits of bank borrowings and clients' compliance with bank covenants.



Insufficient assessment of an entity's compliance with bank covenants and the implications of non-compliance on going concern



Lack of audit procedures to ascertain the proper classification of current and non-current liabilities



Insufficient assessment of the reliability of bank confirmation responses

Fraud risks associated with significant loans, advances and prepayments

There were instances where loans, advances or prepayments were used to inappropriately channel a listed company's funds to third parties. Red flags include funds provided to related or unknown parties with little or no commercial rationale, as well as amounts written off in full shortly after such loans, advances, or prepayments were made. To address this common regulatory concern, we collaborated with the SFC and issued a joint statement in July 2023, setting out the expected standards of conduct and procedures that auditors should follow regarding such arrangements. Auditors should also take note of the following inspection findings identified during the 2024 inspections.



Insufficient exercise of professional scepticism in the identification of fraud risks



Not evaluating the design and implementation effectiveness of controls over loans approval and collection



Not evaluating the business rationale and commercial substance



Not evaluating the recoverability of loans, advances and/or prepayments

Businesses involved in holding or trading virtual assets (VA)

We noted a growing trend among entities engaging in VA-related activities, including cryptocurrency trading and provision of trading services to customers. However, auditors face unique challenges in auditing VA due to several factors, including difficulties in verifying the ownership and existence of VA, complexities in valuation, heightened risks of fraud, and the lack of specific accounting standards for VA. Furthermore, the evolving regulatory landscape and the need of specialised industry expertise in blockchain technology pose additional hurdles in effectively assessing risks and designing and performing appropriate audit responses. Our 2024 inspections have identified several significant findings in this area:



Insufficient understanding of the business model, control activities and the risks associated with the VA



Lack of evaluation of the design and implementation effectiveness of internal controls in relation to processing VA-transactions and custody of clients' VA



Insufficient testing of the ownership of VA-wallets, the occurrence of hash transactions, and the valuation of VA

How to create and maintain a culture of professional scepticism

Auditors must maintain **professional scepticism** throughout the entire audit process, from risk assessment to conclusion. A sceptical mindset strengthens the auditor's ability to design appropriate procedures, question the validity of evidence, avoid over-reliance on management representations and identify material misstatements.

We observed some firms supporting their engagement teams to sufficiently exercise professional scepticism by adopting the following practices:



Exercise professional scepticism – ask questions and challenge the status quo

Use of data analytics

These firms develop and utilise data analytical tools to identify transactions that may suggest potential fraudulent activities. Furthermore, data analytics is used to streamline and automate repetitive processes, such as data extraction and cleansing, during risk assessment and journal entry testing. This enables audit teams to concentrate on high-risk areas that require their professional judgement.



Incorporating elements of unpredictability in audit procedures

These firms require audit teams to incorporate elements of unpredictability in the audit procedures that management may not be able to anticipate. These unpredictable elements increase the likelihood of identifying fraudulent activities or management override of controls. Audit teams can enhance unpredictability by varying the nature, timing, or extent of their procedures.



Timely engagement partner and EQR reviews

These firms require the engagement partner and EQR to provide timely guidance and supervision throughout the audits by completing audit milestone programmes. The engagement partner and/or EQR are also required to randomly reperform some of the tests of details performed by the engagement team. This strengthens the accountability and integrity of audit work and also allows the engagement partners to closely guide and coach their teams.



Pre-issuance quality reviews

These firms establish policies and procedures that require an independent quality review to be performed by someone not on the engagement team, usually an experienced specialist in professional standards. This review, occurs during the audit and before its completion, provides timely oversight and objective viewpoints on whether key aspects of an audit comply with professional standards and the firm's requirements.



Section 5

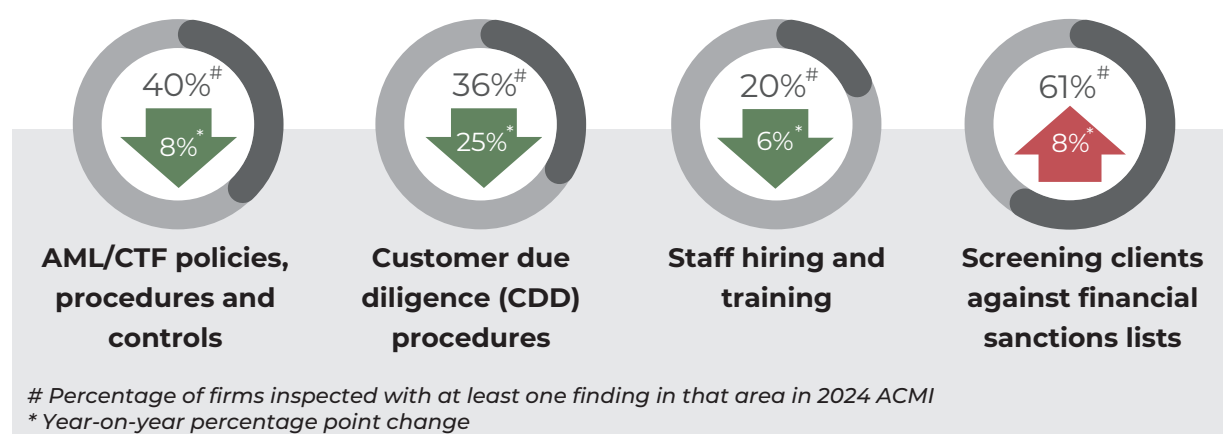
Anti-money Laundering and Counter-terrorist Financing Compliance Monitoring Inspections

I. Our approach

We continued to adopt a risk-based approach in our 2024 AML/CTF compliance monitoring inspections (**ACMI**), focusing our resources on inspecting firms which serve clients exhibiting specific money laundering/terrorist financing (**ML/TF**) risk.

II. Our observations

Common findings



Overall inspection results

We inspected 51 firms regarding their compliance with AML/CTF requirements in our 2024 inspections. We continued to identify various findings regarding firms' compliance with the Guidelines on AML and CTF for professional accountants as set out in Chapter F of the CoE issued by the HKICPA (**AML Guidelines**). Yet, it is encouraging to see a decrease in the number of findings in certain aspects, as shown in the figure above.

More robust CDD procedures drove improvements

We observed significant improvements in how firms conduct the CDD procedures. In the 2024 inspections, we observed that firms demonstrated better policies and clearer procedures for determining when to apply the three different levels of CDD (standard, simplified, and enhanced).

Key challenge – insufficient understanding of AML/CTF obligations

Despite these improvements, staff at SMP generally showed insufficient understanding of their obligations under Cap. 615 (the Anti-Money Laundering and Counter-Terrorist Financing Ordinance) and the related requirements in the AML Guidelines. Firms should provide appropriate guidance and adequate training to ensure staff are aware of and comply with their legal obligations.

This knowledge gap might have caused a significant number of firms to fail to meet key requirements of Section 650 concerning targeted financial sanctions – specifically, by not conducting name checks of their clients and beneficial owners against the latest sanction lists maintained by the UN Security Council and its Sanctions Committees, either at the establishment of client relationships or on an ongoing basis.

Findings that can be addressed easily

Identification and verification of a natural person

During our 2024 inspections, we continued to observe deficiencies in firms' identification and verification of beneficial owners and persons purporting to act on behalf of clients (**PPTA**). Specifically, firms did not identify and verify these individuals using documents from reliable sources.

The lack of government-issued or reliable identity documents undermines the integrity of the customer verification process and exposes firms to significant compliance risks. Firms should therefore strengthen their procedures to ensure that all beneficial owners and PPTA are properly identified and verified, using reliable sources such as government-issued identity documents.

Record keeping

Firms must ensure that their CDD records are retained on microfilm or stored in a computer database, as required by Section 660 of the AML Guidelines.



Speak up about suspicious transactions

In 2024, the Joint Financial Intelligence Unit (**JFIU**) received only 11 suspicious transaction reports from the accounting professionals, the fewest among all sectors* for the past two consecutive years. Firms are reminded that they are obliged to make a timely report to the JFIU when they have grounds for knowledge or suspicion of ML/TF.

It is worth noting that a suspicion can be formed without knowing all the detailed elements that comprise a particular indictable offence, or whether those elements have occurred, or without knowing the details of any plan for an act of terrorism.

Firms and all their staff should be aware that failure to report a suspicious transaction where a person has the requisite knowledge or suspicion is a criminal offence which carries a penalty of imprisonment and fines.

Given its importance, firms are urged to review and enhance their policies and procedures for identifying and reporting suspicious transactions.

* Excluding the VA service providers who started to subject to the AML/CTF requirements in 2023

Section 6

Priorities for 2025-26 Inspections

This section provides auditors with information about the types of engagements that we will prioritise for 2025-26 inspections and the key areas of focus of our SQM and engagement inspections.

Systems of quality management



- Firms' governance and culture. Specifically, on how firms foster the culture of fulfilling the fundamental principle of professional behaviour to comply with the CoE
- Client acceptance and continuance processes. Specifically, on how firms assess their technical ability and capability to take on new engagements
- Partner workload monitoring
- Audit approach for group audits
- Indicators used by firms to assess and monitor audit quality

Engagement selections



- First-year PIE engagements
- PIE engagements for which the current economic uncertainties significantly impact the clients' businesses
- Cross-border PIE engagements
- PIE engagements completed by a PIE auditor without prior industry experience
- Engagements carry significant public interest

Areas of focus



- Areas where recurring inspection findings are identified
- Areas highlighted in our Audit Focus that require auditors' special attention
- Auditors' consideration of the client's IT risks and control, and data security
- Compliance with Hong Kong Standard on Auditing 600 (Revised) *Special Considerations*
– *Audits of Group Financial Statements*
(Including the Work of Component Auditors)

Annex 1

Categorisation of PIE Auditors

Registered PIE auditors are categorised into three groups (A, B and C) based on the number of listed entities they audit annually. Category A firms complete more than 100 such audits, Category B firms complete between 10 and 100, and Category C firms complete at least one but fewer than 10.

Category A firms, which audit almost 90% of listed entities by market capitalisation, are inspected annually. Category B and C firms, which audit less than 5% of listed entities by market capitalisation, are inspected at least once every three years.

The selection of PIE engagements for inspection is determined by the total number of PIE engagements that a PIE auditor has as at 31 December, immediately preceding the start of our inspection year on 1 April. For Category A firms, the selection ranges from three to seven; for Category B firms, it ranges from two to four; and for Category C auditors, only one is selected.

In our 2024 inspections, HLB was recategorised as a Category B firm (2023: Category A). As a result, past data for Category A firms' inspection results, which previously included HLB and covered six firms, are not strictly comparable with this year's results and should be interpreted with caution. Despite the recategorisation, HLB was inspected in 2024, and our inspection frequency is based on a range of risk factors, including firms' past inspection results.

Annex 2

Inspection Results by Individual Category A and B Firms

The tables below present the Category A and B firms we inspected in 2023 and 2024, along with the scope and results of those inspections.

Given the relatively small number of engagements we inspected for each firm each year, the AQR shown below are not necessarily indicative of the audit quality across their whole portfolio. Further details about the AQR and its interpretation are outlined on page 8 of this report.

Table 3. Number of PIE engagements inspected by Category A firms and their AQR (excluded follow-up inspections)

Category A firms	Total number of listed entities (by auditor appointments) as at 31 December 2023	2024 Inspections				2023 Inspections			
		Number of PIE engagements inspected				Number of PIE engagements inspected			
		Total	AQR of 1 or 2	AQR of 3	AQR of 4	Total	AQR of 1 or 2	AQR of 3	AQR of 4
BDO	181	6	2	3	1	6	2	3	1
Deloitte	250	5	2	3	0	4	2	0	2
EY	382	4	4	0	0	4	3	1	0
HLB ¹	84	Disclosed in Table 4 ¹				5	0	4	1
KPMG	238	4	2	2	0	5	2	2	1
PwC	404	5	4	1	0	7	5	2	0
Total	1,539	24	14	9	1	31	14	12	5

¹ HLB was categorised as a Category B firm in the 2024 inspections and a Category A firm in the 2023 inspections.

Table 4. Number of PIE engagements inspected by Category B firms and their AQR (excluded follow-up inspections)

Category B firms	Total number of listed entities (by auditor appointments) as at the specified date*	2024 Inspections				2023 Inspections			
		Number of PIE engagements inspected				Number of PIE engagements inspected			
		Total	AQR of 1 or 2	AQR of 3	AQR of 4	Total	AQR of 1 or 2	AQR of 3	AQR of 4
CCTH CPA Limited	31	N/A	N/A	N/A	N/A	2	0	0	2
Crowe (HK) CPA Limited	57	N/A	N/A	N/A	N/A	2	0	1	1
D & PARTNERS CPA LIMITED	15	2	0	2	0	N/A	N/A	N/A	N/A
Elite Partners CPA Limited [^]	67	N/A	N/A	N/A	N/A	2	0	0	2
Forvis Mazars CPA Limited (formerly named as Mazars CPA Limited)	69	N/A	N/A	N/A	N/A	3	0	0	3
Grant Thornton Hong Kong Limited	61	N/A	N/A	N/A	N/A	2	0	0	2
HLB	84 (31 December 2022: 102)	4	0	4	0	5	0	4	1
McMillan Woods (Hong Kong) CPA Limited [^]	44	N/A	N/A	N/A	N/A	2	0	0	2
MOORE CPA LIMITED	64	2	2	0	0	N/A	N/A	N/A	N/A
Prism Hong Kong Limited (formerly named as Prism Hong Kong and Shanghai Limited) [^]	44 (31 December 2022: 20)	1	0	0	1	2	0	0	2
Rongcheng (Hong Kong) CPA Limited (formerly named as CL Partners CPA Limited)	13	N/A	N/A	N/A	N/A	2	0	0	2
RSM Hong Kong	57	2	0	0	2	N/A	N/A	N/A	N/A
SHINEWING (HK) CPA Limited	67	2	0	1	1	N/A	N/A	N/A	N/A
ZHONGHUI ANDA CPA Limited	94	3	0	0	3	N/A	N/A	N/A	N/A

* For the 2024 inspections, the figures represent the total number of listed entities (based on auditor appointments) as at 31 December 2023. For the 2023 inspections, the figures represent the total number of listed entities (based on auditor appointments) as at 31 December 2022.

[^] Subject to our specific scope inspections.

By disclosing the inspection results for individual Category A and B firms that have been inspected, we aim to:

- Inform stakeholders, especially audit committees, about which PIE auditors have been inspected. This will enable them to engage with these auditors regarding their inspection results and commitments to improving audit quality.
- Increase the transparency of our regulatory process.
- Hold firms accountable for the quality of their work.
- Motivate audit firms to raise their standards of quality and address any identified issues during inspections.

Annex 3

Glossary

This glossary provides definitions of the acronyms, abbreviations, and key terms used in this report:

ACMI	AML/CTF compliance monitoring inspections
AFRCO	Accounting and Financial Reporting Council Ordinance
AML	Anti-money laundering
AML Guidelines	Guidelines on AML and CTF for professional accountants as set out in Chapter F of the CoE issued by the HKICPA
AQR	Audit quality rating
CDD	Customer due diligence
CoE	Code of Ethics for Professional Accountants
CPD	Continuing professional development
CTF	Counter-terrorist financing
ECL	Expected credit losses
EQR	Engagement quality reviewers
GITC	General IT controls
HKICPA	Hong Kong Institute of Certified Public Accountants
INC	Investigation and Compliance Department
IT	Information technology
ITAC	IT application controls
JFIU	Joint Financial Intelligence Unit
LC	Licensed corporations
ML	Money laundering
Monitoring Reviewers	Individuals performing monitoring activities
PIE	Public interest entities
PPTA	Persons purporting to act on behalf of clients
QCSR	Quality control system responsible persons
RCA	Root cause analysis
SEHK	The Stock Exchange of Hong Kong Limited
SFC	Securities and Futures Commission
SMP	Small and medium-sized practices
SQM	System(s) of quality management
TF	Terrorist financing
VA	Virtual assets

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