

## Press Release

11 July 2023

### **AFRC 2022 Annual Inspection Report provides transparency about audit quality and holds firms accountable for their performance**

The Accounting and Financial Reporting Council (**AFRC**) today issues the [2022 Annual Inspection Report](#) on its inspections of public interest entity (**PIE**) auditors and non-PIE auditors completed from 1 April 2022 to 31 March 2023.

#### **Overall audit quality rating - improved but not enough**

In 2022, the AFRC inspected 55 PIE engagements, representing a nearly 50% increase when compared to 2020, in response to the unsatisfactory inspection results from previous years. For the first time, 6 non-PIE engagements were inspected under the power given to the AFRC in the Further Reform.

Introducing the 2022 Annual Inspection Report, Ms Janey Lai, Head of Inspection, said, “The average audit quality rating for all PIE engagements inspected improved to 2.8 in 2022 from 3.1 in 2020, but it was not enough. We saw a progressive improvement in audit quality, mainly in Category A (**Cat A**) firms. However, the inspection results of most of the Category B and C (**Cat B and C**) firms were disappointing. In other words, there is still huge room for improvement.

The recurrence of deficiencies indicated that some firms have not learnt or have not learnt enough from our previous inspection findings. This is a loud and clear message that those firms without substantial improvement in audit quality rating during the 2020-22 Cycle, should immediately sharpen its focus on improving audit quality and protecting public interest. Their attitude in compromising audit quality either by impaired objectivity or by cutting corners is unacceptable. This could have a severe impact to the public’s confidence in the quality of financial reporting of Hong Kong as an International Financial Centre.”

#### **System of quality control – good practices in some Cat A firms, but unsatisfactory results in most Cat B and C firms**

In respect of the Systems of Quality Control (**SQC**), we noticed good practices adopted by some Cat A firms during the inspection. We encourage other firms to learn these good practices in the system quality of management development.

There were a total of 14 Cat B and C firms inspected in 2022, we identified they had deficiencies in different elements of the SQC. In particular, the number of firms found to have deficiencies in acceptance and continuance of client relationships jumped significantly from 33% in 2020 to 71% in 2022, which required immediate attention.

Ms Lai continued, “It is unacceptable to find such high rates of deficiencies in the Cat B and C firms in our third year of the 2020-22 Cycle. These firms did not take benefits from our previous publications to enhance their SQC. To protect the public interest, the firmwide quality controls over client and engagement acceptance procedures will be under our focus. We will keep monitoring the current situation and taking further steps, particularly on firms with a tendency to accept higher-risk and more complex engagements which are disproportionate to their experiences and resources.”

We urge auditors to take robust actions and firms’ leadership such as firms’ Chairmen, Managing Partners and engagement quality reviewers (**EQR**) to set the right tone in order to improve the effectiveness of quality management system and the quality of their audit work.

At the same time, we also urge directors of the listed entities and their audit committees to take advantage of our comments on audit firms when assessing the competence and capabilities of their auditors. It is their primary responsibility to ensure the quality of financial reporting and audits and therefore should maintain regular communications with the auditors on the key audit risks and resolve any issues identified during the audit.

During our inspections, we saw uncooperative behaviours of some firms which slowed down the entire inspection process. These uncooperative behaviours included not providing or delay in providing relevant documents, providing incomplete or inaccurate information to our inspectors. We emphasise the importance of cooperating with our inspectors as our inspections serve the purpose of improving their audit quality and benefit all parties, including the accounting profession and the public.

Dr Kelvin Wong, Chairman of the AFRC concluded, “It is of utmost importance for firms to foster a culture of upholding audit quality. However, the AFRC noted a great degree of variance in the existence of such culture among firms, which we believe, is one of the root causes for the repeated deficiencies. While the AFRC cannot regulate firms’ culture, we would like to urge the leaderships of the firms including Chairmen, Managing Partners and EQR to build and strengthen such a culture so as to assure public expectation of their professionalism and reliability.”

End



Dr Kelvin Wong, Chairman (right) and Ms Janey Lai, Head of Inspection (left) of the AFRC present to media the 2022 Annual Inspection Report.

### **About the Accounting and Financial Reporting Council**

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

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

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