AFRC Accounting and Financial Reporting Council 會計及財務匯報局

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Audit Focus for 2024 year-end audits

Inspection

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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, and promotes the healthy development of the accounting profession.

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

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Introduction

Navigating the uncertainties: Economic shifts and their impacts

Amid various economic and geopolitical events, both the global and domestic economic environments remain volatile in 2024. While uncertainties may create opportunities for certain businesses, they can also lead to heightened business risks and challenges for others.

Uncertain economic conditions have also **elevated risks in financial reporting and auditing**. As a result, auditors must exercise heightened professional scepticism when identifying and assessing the risks of material misstatement in the financial statements, and in planning and performing audit procedures in response to these risks.

Auditors play a pivotal role in fostering trust and confidence in financial information, particularly during periods of economic uncertainty. As we enter the final quarter of 2024, auditors should have prepared audit plans for the 2024 December year-end audits. Considering the impacts of the prevailing economic conditions on this December year-end audits, we highlight **key areas to which auditors should pay particular attention** when reassessing the risks and their responses for these audits.

Turning missteps into lessons

Recent corporate failures have profoundly impacted the economy and weakened public confidence in audited financial statements. Sanctions for audit failures have also reached record highs. This document also provides **key reminders to auditors for the lessons learned**, which help them avoid repeating mistakes.

Collaboration fosters achievement

It is important to recognise that a quality audit does not rest solely on the auditor. **Management and audit committees of listed entities also play an equally important role in ensuring the quality and timeliness of financial reporting.**

"Well begun is half done." Proper audit planning lays the foundation for an effective and efficient quality audit. A clear plan enhances transparency in the audit process and facilitates the early identification and resolution of significant accounting and auditing issues. Auditors, management and audit committees should reference the **key audit milestones** in Annex 1, which serve as critical checkpoints that guide the planning and execution of an audit, ensuring that all necessary actions are taken in a timely manner to achieve a quality audit.

Table of contents

		Page
Section 1	**Areas that require special consideration**	
I.	Audit implications of the current economic environment	2 – 5
II.	Thorough understanding of the entity’s business and its environment	6
Section 2	**Other key reminders to auditors**	
I.	Auditor independence	7
II.	Timely, proactive and sufficient involvement of engagement partner and engagement quality reviewer	8
III.	Set and reinforce an ethical culture	9
IV.	Compliance with all applicable laws and regulations	10
V.	Revised auditing standard for audits of group financial statements	10
VI.	Audit documentation – Evidence of your work	11
VII.	Change in auditor of a listed issuer	12
Section 3	**Our recommendations and expectations**	
I.	Auditors	13
II.	Management	14
III.	Audit committees	14
Annex 1	**Key audit milestones**	
Annex 2	**Start the dialogue – Key questions for audit committees to ask their auditors**	

*Instances of QR codes in this Audit Focus refer to our prior publications or other information. Readers are encouraged to **click** or **scan the QR codes** for additional information.*

Section 1
Areas that require special consideration

I. Audit implications of the current economic environment

Challenging economic conditions create an environment where companies may experience extended financial pressures, increasing their **susceptibility to management bias or fraud**. These conditions have significant audit implications, particularly concerning the entity's ability to continue as a **going concern**, **asset valuation, fair value measurement**, **which auditors should carefully consider when planning their audits.**

Sluggish property market

Despite the removal of all demand-side management measures for residential properties in February 2024, Hong Kong's residential property price index declined by 12.7% in Q2 2024 compared to the same quarter in 2023. Concurrently, the office property price index fell by 18.6%.[1]

Stable yet challenging credit access

According to a recent survey by the Hong Kong Monetary Authority (**HKMA**), the credit condition for small and medium-sized enterprises (**SMEs**) remained stable in Q2 2024. However, it is noteworthy that a notable portion—27% of surveyed SMEs—perceived a "more difficult" credit approval stance in Hong Kong for the quarter.[3]

Volatile stock market

Enhanced mutual access between the Mainland and Hong Kong capital markets rallied the Hang Seng Index (**HSI**) to a near 10-month high in May 2024. However, delays in US rate cuts and concerns over Mainland's economic recovery led to a retreat in the HSI by late June.[5] Nevertheless, the HSI rebounded, reaching an 18-month high following the announcement of the Mainland's latest fiscal measures in late September. Looking ahead, ongoing fiscal and geopolitical events are expected to contribute to continued volatility in the stock market.

Retail headwinds

While the value of total retail sales in Hong Kong improved year-on-year in 2023, the provisional total retail sales value for the first seven months of 2024 declined by 7.3% compared to the same period in 2023.[2] Headwinds in the retail sector are expected to persist in the near term.

Interest rate uncertainty

The Federal Reserve reduced the federal funds rate by 0.5% in Q3 2024 and indicated further rate cuts could happen this year and in 2025.[4] Meanwhile, China's central bank also cut short-term rates by 0.2% along with other stimulus measures in September. Although further cuts are anticipated, the timing and extent remain uncertain.

Growth of virtual assets

Asia's first batch of six virtual assets (**VAs**) spot exchange-traded funds listed in Hong Kong has traded smoothly, achieving a total market capitalisation of HK$2.4 billion as of mid-August 2024. In addition, the Securities and Futures Commission (**SFC**) received 17 applications for virtual asset trading platform licences during Q2 2024.[6] The growth of VA-related activities is expected to continue, which may have a transformative impact in the world of finance.

Risks	Our expectations
Manipulation of financial performance	✓ Perform a robust fraud risk assessment by identifying fraud risk factors that might incentivise management to manipulate financial performance. ✓ Obtain a thorough understanding of the entity and its environment, including information technology (**IT**) systems and relevant internal controls. Focus on how the current economic landscape and associated challenges affect the entity's business operations and business models. ✓ Heighten professional scepticism for any indicators of possible management bias or potential fraud. Critically challenge the reliability and relevance of information and representation provided by management. ✓ Critically challenge the business rationale for significant unusual transactions and evaluate the associated risk of fraud. ✓ Maintain controls over the send-and-receive confirmation processes. Evaluate the reliability of responses, particularly for confirmations received electronically or when signs indicate that they may not have originated from the intended confirming parties.
Swings in property valuation	✓ Critically evaluate management's selection of comparable transactions concerning the subject property. Challenge management on any adjustments, or lack thereof, for factors such as location, size, property condition, and date of transaction. ✓ Evaluate all available audit evidence, including both corroborative and contradictory evidence. Avoid cherry-picking comparable transactions that only support the current valuation and neglect more pertinent transactions. ✓ Do not discharge the auditor's responsibilities to the auditor's experts concerning asset valuation. ✓ Sufficiently consider indirect exposures to the financial statements, for example, implications to valuation of assets with pledge properties.

Risks	Our expectations
Estimation uncertainty in measuring fair value of financial instruments	✓ For financial instruments that used to have quoted prices in active markets, consider the need for a valuation adjustment if there is a significant decrease in the volume or level of activity for those instruments. ✓ For financial instruments with inputs other than the unadjusted quoted price, consider the implications of volatility to the fair value and the fair value hierarchy.
Anticipated challenges in credit access	✓ Assess the appropriateness of the entity's going concern assumption and evaluate whether a possible tightening of credit or increase in financing costs may severely impact the financial conditions. ✓ Critically evaluate the availability of credit access – past precedents do not guarantee future outcomes.
Uncertain interest rate trajectory	✓ Assess the reasonableness of cash flow projections where the anticipated interest rate is a significant input to the calculation, taking into account the implications for foreign exchange rates. ✓ Consider multiple scenarios of cash flows. ✓ Critically evaluate whether a previously recognised asset impairment loss (other than goodwill) should be reversed. Such a reversal should be made if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment assessment in accordance with HKAS 36 *Impairment of Assets*. ✓ An impairment loss recognised for goodwill shall not be reversed in a subsequent period. ✓ Interest rate changes do not tell the whole story about asset valuation. Auditors should exercise sufficient professional scepticism in determining how sensitive an asset's recoverable amount is to failing rates, especially in today's challenging market environment. ✓ Exercise scepticism when evaluating the impact of interest rate reductions on market sentiment. Pay particular attention to instances where management may show excessive optimism in their cash flow projections, attributing it to the rate cuts.

Risks	Our expectations
Deteriorating business performance	✓ Critically assess the assumptions used in the valuation of inventories and impairment of assets (incl. right-of-use-assets, property, plant, and equipment, intangible assets and goodwill), and ensure that they are reasonable and supportable. ✓ Challenge the reliability and relevance of the information used and key inputs adopted by management. ✓ Evaluate the entity's going concern assumption taking into account all possible external and internal factors, including the profitability, cash flows projections etc. ✓ Evaluate whether the credit risk on accounts receivables or other financial assets with direct/ indirect exposures to businesses experiencing deteriorating performance have increased significantly since initial recognition.
Challenges in auditing VAs	✓ Ensure sufficiency and appropriateness of resources in undertaking engagements associated with VAs as they are likely to require specialised skill and knowledge. ✓ Obtain sufficient understanding of the entity and its environment, including the entity's internal controls over the activities associated with VAs. ✓ Identify and assess the risk of material misstatements due to fraud, including an evaluation of the business purpose of these activities an indication of fraudulent activities. ✓ Critically evaluate and document the terms and conditions of VAs-related arrangements, for example, custodial arrangement as these terms and conditions can have a substantial impact to the rights and obligations or other audit assertions. ✓ Thoroughly plan the audit work to be performed over the ownership of the VAs, as it is likely that substantive procedures alone cannot provide sufficient and appropriate audit evidence given the unique nature of VAs.

II. Thorough understanding of the entity's business and its environment

Risks come from not knowing what you're doing. Without a thorough understanding of the entity's business and its environment, the auditor will not be able to adequately identify and assess the risks of material misstatement in the financial statements.

With the use of IT and technologies more extensive than ever, the business landscape is changing rapidly. This change necessitates auditors develop a thorough understanding of the entity and its environment as required by HKAS 315 (Revised 2019) *Identifying and Assessing the Risks of Material Misstatement* to identify and assess the risks of material misstatement.

In particular, auditors should carefully consider the following:

- Changes in consumer habits and market sentiment
- Reshaping of business model
- Advancement and extensive use of IT in business processes

While the nature, timing, and extent of audit procedures may vary depending on the size and complexity of the entity, we expect auditors to, at a minimum, performing the following:

✓ **Communicate early** with management to understand how the entity's business and IT environment have adjusted to ongoing changes.

✓ Conduct **on-site visits** and meet with non-financial personnel to gain a comprehensive understanding of the client's business and business models.

✓ **Refrain from mechanically adopting last year's audit approach**. Auditor should carefully consider current year's specific circumstances and changes in the entity's business when designing audit approach and procedures.

✓ Ensure that the engagement partner and engagement quality reviewer (**EQR**) are **actively involved throughout the risk assessment process**. This is crucial for designing appropriate audit procedures to address identified risks.

✓ Continuously update the engagement team's understanding of the entity and its environment, regularly re-evaluate the assessed risks, and, if necessary, revisit and revise the audit plan during the audit – **Risk assessment does not stop at the audit planning**.

Section 2
Other key reminders to auditors

I. Auditor independence

Auditor independence forms the cornerstone of reliable financial reporting. It is a foundation that ensures auditors perform their duties objectively and with integrity, which is essential for upholding public confidence in the audit profession.

Ensuring auditor independence is not a check-the-box exercise. It is a fundamental pillar underpinning the audit process' integrity, quality, and credibility. It requires auditors to have a compliance mindset at all times. Audit firms must remain vigilant to any threats to independence regarding their relationships with audit clients and implement policies and procedures to identify and address such threats. They should pay particular attention to:

✓ **Non-assurance services**: Firms should identify, evaluate, and address any threats to independence that might arise from providing non-assurance services to an audit client. They should specifically consider whether (i) the non-assurance service is prohibited under the Code of Ethics, and (ii) they would assume management responsibilities while providing such services. As such, the engagement partner should fully understand the scope of the prospective non-assurance services and be satisfied with their provision. In any event, auditors should refrain from preparing financial statements for their listed entity audit clients to maintain independence.

✓ **Long association of personnel with an audit client:** Prolonged relationships between auditors and clients can create excessive familiarity and diminish professional scepticism, leading to an overreliance on management's representations. Firms should implement appropriate policies and procedures to monitor and manage these relationships, including partner rotation and cooling-off periods. Additionally, firm leadership should set the right tone at the top, encouraging the engagement team to challenge management without fear of jeopardising client relationships.

✓ **Procurement and purchases from audit clients** [7] **:** Such transactions are often overlooked as they are perceived as routine, low-risk business activities. However, due to their size and nature, they can create self-interest threats. Firms should have proper policies and procedures for identifying and evaluating these transactions, especially those made by audit team members or their immediate family.

✓ **Audit fee**: Auditors are paid by their clients, which could lead to threats to independence. Therefore, it is crucial for firms to carefully assess the level and payment terms of their audit fees. Specifically, firms should not charge directly or indirectly a contingent fee for an audit engagement. This includes situations where payment of a considerable portion of the audit fee is dependent on the issuance of the auditor's report or the resumption of trading of a suspended stock.

II. Timely, proactive, and sufficient involvement of engagement partner and engagement quality reviewer

All Hands on Deck. An audit without sufficient and appropriate involvement of engagement partner and EQR is like a ship without a rudder—directionless and unstable.

Engagement partner and EQR should be sufficiently **involved in the early stages** of an audit to identify key accounting and auditing issues. Their roles are essential for providing direction and supervision, especially regarding significant risks and areas involving significant judgment. Their sufficient level of involvement allows the engagement team sufficient time to identify and address critical matters early, alleviating resource pressure during the audit peak season. Moreover, it is crucial for firms to continually assess and adjust partners' workloads, ensuring they are maintained at a level that allows for sufficient involvement.

Engagement partner should closely supervise the engagement team throughout the audit and provide timely direction. The engagement partner is expected to **conduct on-site reviews** of audit working papers and examine critical supporting documents obtained by the engagement team members. This ensures that the planned procedures are properly executed, and reliable and relevant audit evidence is obtained to support the conclusions reached.

In addition, engagement partner and EQR must elevate their professional scepticism in light of the ever-evolving economic landscape. They should **consistently step back** and **reassess** whether the **risk assessment** remains appropriate and if the planned audit procedures continue to sufficiently address the identified risks.

Below are the key areas where we expect the EQR to be involved in the audit, though they are not exhaustive:

Planning

☐ Independence assessment

☐ Risk assessment

☐ Identification of key auditing & accounting issues

☐ Determination of materiality

☐ Audit scope

☐ Audit plan for significant risks and areas involving significant judgement

☐ Key milestones dates and review timetable

☐ Audit plan to the audit committee

Interim procedures

☐ Re-evaluate assessed risks and update audit plan

☐ Discuss significant matters, including key audit matters

☐ Updates on audit work to address significant risks and areas involving significant judgement

☐ Evaluate if appropriate consultation has taken place

☐ Timetable for review of working papers and reporting

Final procedures

☐ Re-evaluate assessed risks and update audit plan

☐ Audit work to address significant risks and matters, incl. key audit matters

☐ Evaluation of audit results, incl. control deficiencies, contradictory/ disconfirming evidence and misstatements

☐ Report to the Audit Committee

☐ Management representation letter

☐ Auditor's report and financial statements

III. Set and reinforce an ethical culture

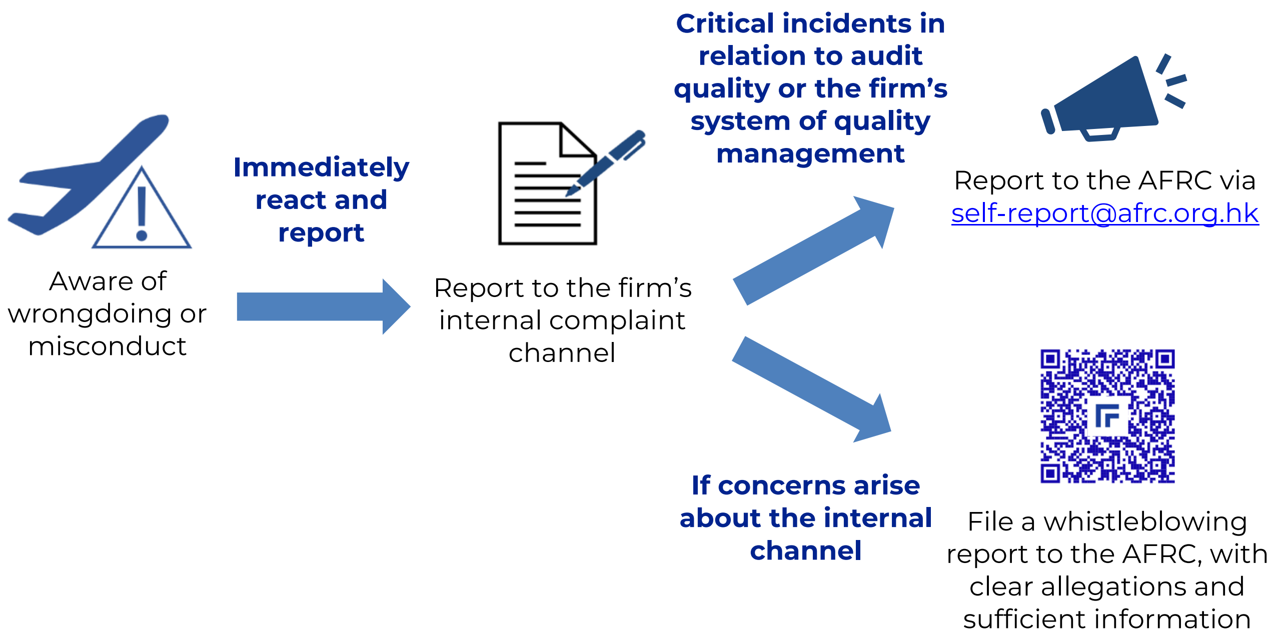
Auditors must be straightforward and honest in all professional and business relationship.

Audit firms should set and reinforce the **right tone at the top**[8] that promotes a culture of ethical behaviour, integrity, and a commitment to audit quality. Firm leadership should communicate the behaviours expected from all individuals within the firm and ensure that the tone at the engagement level aligns with the tone set at the top.

Additionally, audit firms should have appropriate policies and procedures for monitoring compliance with relevant ethical requirements. This includes having effective policies and procedures for dealing with complaints and allegations against individuals, including leadership, who do not act or behave according to the expected standards of behaviour.

Report any unethical behaviour

Firms should cultivate a culture where all staff feel empowered to **speak up** and put in place non-retaliation policies to protect whistleblowers. Anyone who witness or becomes aware of wrongdoing or misconduct has a responsibility to report it. Examples of such misconduct include deceptive activities like misrepresenting that audit procedures were completed without performing them or making unauthorised alterations to assembled audit files.



IV. Compliance with all applicable laws and regulations

Compliance with laws and regulations is a legal obligation and a fundamental pillar of a responsible and sustainable practice.

Audit firms should thoroughly understand and strictly comply with the applicable laws and regulations of the jurisdictions where they practise or provide audit services. These include those in Mainland China, particularly all requirements under the "Interim Provisions on Accounting Firms' Provision of Auditing Services for Overseas Listing of Enterprises in Mainland China" promulgated by the Ministry of Finance (**Interim Provisions**), which governs the provision of audit services by Hong Kong audit firms for Mainland enterprises listed in Hong Kong.

Generally, the Interim Provisions apply to audits of Hong Kong-listed entities with their principal place of business in Mainland China. The exemption applies only under very limited circumstances. Audit firms should seek advice from their legal counsel when in doubt.

V. Revised auditing standard for audits of group financial statements

HKSA 600 (Revised) *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)* introduces significant changes to the audit of groups for periods commencing on or after 15 December 2023.

The revised standard strengthens the auditor's responsibilities in relation to:

- ✓ Professional scepticism
- ✓ Scoping and risk assessment
- ✓ Two-way communication between the group and component auditors
- ✓ Clarification on the application of materiality and aggregation risk in group audits
- ✓ Documentation related to the review of component auditors' work

These changes will likely require more time and effort from the group engagement team and group engagement partner, particularly due to the enhanced responsibilities for directing, supervising and reviewing the work of component auditors. Firms should ensure that their audit methodologies are updated to reflect these changes, and that the group and component auditors fully understand the revised requirements.

VI. Audit documentation — Evidence of your work

Audit documentation is the primary means by which auditors evidence their compliance with auditing standards. It provides transparency into the auditor's work and decision-making process, creating an auditable trail that enables both internal and external reviewers to assess the quality of work supporting the auditor's conclusions.

Audit firms should have appropriate policies, procedures, and controls to ensure the completeness and **integrity of audit documentation**[9].

Audit documentation is a written record of the work performed, the evidence obtained, and the conclusions reached by the auditor. It also facilitates the planning, performance, and supervision of the audit. It is the basis for which the quality of audit work is assessed because it provides the reviewer with written documentation of the evidence supporting the auditor's conclusions.

As such, audit documentation should be prepared in sufficient detail to provide a clear understanding of its purpose, the work performed by the auditor, and the conclusions reached. Specifically, the audit documentation should include:

- ✓ The purpose of the test
- ✓ The nature, timing and extent of the test
- ✓ The source documents examined
- ✓ The relevant information from the source documents examined
- ✓ The results of the audit procedures performed
- ✓ Any inconsistencies identified and the audit procedures performed to address them
- ✓ The significant professional judgements applied
- ✓ The conclusion and its basis
- ✓ The individuals who performed and reviewed the work, along with the dates of completion and review

It is essential that audit documentation sufficiently demonstrates the exercise of professional scepticism, particularly in areas involving significant judgement or higher audit risks.

VII.Change in auditor of a listed issuer

Public interest entity (**PIE**) auditors have an unquestionable responsibility to consider the public interest first before deciding to resign from or accept an auditor appointment by a listed entity.

As year-end approaches, audit firms should have largely completed their audit planning and resource allocation for their clients and engagements with December year-end. Changing auditors at this stage is concerning due to the potential risk of opinion shopping by listed entities, which could undermine the public interest.

The **expectations for outgoing and incoming auditors**[10] have been repeatedly communicated in previous publications. Nevertheless, we highlight again our critical expectations to:

Outgoing auditors

- ✓ Exhaust all available means to address unresolved matters with management and the audit committees before resigning.
- ✓ Detail in the letter of resignation the specific circumstances, including any significant matters or audit issues, resolved or unresolved, that led to their resignation.

Incoming auditors

- ✓ Critically assess the firm's competence and capabilities regarding manpower, time and available resources.
- ✓ Evaluate the integrity of the potential client, exercising heightened professional scepticism concerning the reasons behind the outgoing auditor's resignation and the management's representation of unresolved audit matters.
- ✓ Appropriately plan and perform necessary audit procedures to obtain sufficient appropriate audit evidence regarding the opening balances in accordance with HKSA 510 *Initial Audit Engagements – Opening Balances*. Request and obtain the predecessor auditor's working paper for review.

The AFRC will continue to closely monitor changes in auditors by listed entities, especially late-stage changes, and will not hesitate to take appropriate follow-up actions to ensure the quality of audits is upheld and the public interest is protected.

Section 3
Our recommendations and expectations

I. Auditors

The demand for accurate and reliable financial statements has never been more critical in an ever-evolving economic landscape. Auditors serve as gatekeepers, instilling investor confidence and upholding public trust in the capital market through the delivery of quality audits.

To ensure consistent execution of quality audits, the leadership of all firms, regardless of their size, must set the right tone at the top and adopt a more **assertive and proactive approach** in responding to all critical areas highlighted in this Audit Focus.

☐ **Heighten professional scepticism** for any indicators of possible management bias or potential fraud

☐ Do **not overly rely on** management's representations

☐ Challenge the **reliability** and **relevance of information** used by management

☐ Obtain and evaluate **multiple sources of evidence** to form independent conclusions

☐ **Document** your scepticism, (including any inconsistencies identified and your procedures to address them)

☐ Set and reinforce an **ethical** and **compliance culture**

☐ **Prioritise professionalism** over commercial considerations

☐ Commit to **continuous quality improvement**

☐ Critically **evaluate internal resources** (including manpower, expertise and time) and **client's integrity** before client engagement acceptance and continuance

☐ Thoroughly **understand** the **client's business** and its **environment** (including IT systems and internal controls)

☐ Evaluate the **impact of current economic conditions** on risk assessments and audit procedures

☐ Ensure **early** and **sufficient involvement** of **engagement partners** and **EQRs** in supervising the risk assessment process

☐ **Timely**, **proactive** and **sufficient involvement** by **engagement partners and EQRs** to provide direction and supervision to address potential risk of fraud and significant risks

☐ Critically **evaluate** the audit evidence obtained, including **contradictory** or **disconfirming evidence**

☐ **Closely monitor** and **evaluate the work** of **auditor's experts** and **component auditors**.

☐ **Identify knowledge and skill gaps** among staff and **upskill** them to the required level of competence

☐ Ensure the engagement teams possess the **necessary competence** (including relevant industry knowledge and experience) and **capabilities** to perform quality audits

☐ Ensure **audit fee is set at an appropriate level that does not compromise audit quality**.

☐ Set a **communication plan** and hold **regular meetings** with management and audit committee to review audit progress and findings

☐ **Proactively address** and **resolve** any **contentious matters** with management and audit committee in a timely manner

II. Management

A challenging economic environment introduces significant uncertainties for listed entities, making them more susceptible to management bias and fraudulent activities. To safeguard the integrity of financial statements, management must establish a **robust control environment** and implement effective internal control procedures to detect and prevent fraud and errors.

Management should **allocate sufficient resources and assign competent personnel**, including experts, to support the financial reporting process. It is crucial that financial statements are prepared in accordance with applicable financial reporting standards, with management exercising judgements that are **reasonable and well-supported.**

Furthermore, management should **remain open** and **receptive** to challenges from auditors and audit committees. Open dialogues enhance transparency and strengthen the robustness and integrity of the financial reporting process.

III. Audit Committees

Audit committees of listed entities are pivotal in ensuring the quality of financial reporting through **effective oversight of auditors**[11]. As entities navigate the complexities of today's economic environment, the public demands more transparent interactions between audit committees and auditors.

Audit committees should establish a **clear communication timeline** with auditors and maintain constructive, in-depth dialogue throughout the audit process. Timely and robust two-way communication enhances transparency and helps pre-emptively identify and address potential issues before they become too costly or too late to manage.

Audit committees should also hold **private meeting** with auditors **at least once a year** to discuss accounting and audit issues and other observations in the absence of management.

Annex 2 contains a list of questions to guide audit committees during their discussions with auditors. While not exhaustive, these questions aim to facilitate comprehensive and effective conversations between the auditors and the audit committees. Audit committees are encouraged to build upon and tailor these questions to fit their circumstances.

Annex 1

Key Audit Milestones

(Illustrative Timeline for a December year-end PIE audit)

List of suggested procedures are not exhaustive

30 Sep 202X
Establish **Audit Plan**
Planning meetings with **component auditors**

31 Oct 202X
Agree Audit Plan and **Timetable** with **Management** and **Audit Committee**

31 Dec 202X
Complete **Interim Procedures**
Progress meetings with **component auditors**

Progress meetings with **Audit Committee**, incl. **private meeting** with no management presence

At least 1 month before auditor's report date
Evaluate work of **auditor's expert** and **component auditors**

On or before 31 Mar 202X+1
Complete **Final Procedures**
Communicate audit results and hold **private meeting** with **Audit Committee**

Team debrief and **formulate action plan**

On or before 31 May 202X+1
Complete **File Assembly** process

Before AGM
Complete **client and engagement continuance assessment**

Propose and agree **indicative audit scope and fee** for the coming year

Planning | Interim procedures | Final procedures | Before AGM

Auditor

Planning
- ☐ Independence assessment
- ☐ Understand the entity and its environment
- ☐ Risk assessment
- ☐ Develop audit scope and plan
- ☐ Establish audit timetable and key milestones
- ☐ Issue group instructions and hold planning meetings with component auditors

Interim procedures
- ☐ Understand and test entity's internal controls
- ☐ Perform substantive audit procedures on significant risks, non-routine transactions, and other material account balance
- ☐ Hold progress meetings with component auditors
- ☐ Re-evaluate assessed risks and update audit plan as necessary

Final procedures
- ☐ Evaluate work of auditor's expert and component auditors
- ☐ Re-evaluate assessed risks and perform further audit procedures as necessary
- ☐ Evaluate control deficiencies and contradictory/disconfirming evidence
- ☐ Complete remaining audit procedures
- ☐ Evaluate sufficiency and appropriateness of audit evidence

Before AGM
- ☐ Complete client and engagement continuance assessment
- ☐ Hold team debriefing meeting and formulate action plan

Management

Planning
- ☐ Plan and allocate sufficient resources and competent personnel, including management's experts, in preparing the financial statements

Interim and final procedures
- ☐ Use reasonable and well-supported evidence to substantiate judgments and estimates
- ☐ Provide auditor with timely access to all necessary information and personnel
- ☐ Be open and receptive to any challenges raised by auditor and audit committee

Audit Committee

- ☐ Oversee the entity's financial reporting processes and internal controls
- ☐ Provide support to auditor as needed to facilitate the resolution of any contentious matters with management

Planning
- ☐ Review and approve audit plan, incl. any revisions to audit scope and fee
- ☐ Agree on communication timeline
- ☐ Obtain and discuss the AFRC's inspection results and remedial action

Interim procedures
- ☐ Hold progress meetings with auditor, incl. private meeting
- ☐ Understand and evaluate audit progress and audit findings to date

Final procedures
- ☐ Challenge sufficiency and appropriateness of audit evidence obtained by auditor
- ☐ Hold private meeting with auditor

Before AGM
- ☐ Evaluate the suitability of auditor for consideration of reappointment
- ☐ Review and approve indicative audit scope and fee for the coming year

Elevate Audit Quality with Audit Milestones
- ✓ **Promote transparency in audit process**
- ✓ **Facilitate early identification and resolution of accounting and auditing issues**
- ✓ **Enhance audit efficiency**
- ✓ **Alleviate staff workload during peak season**

Represents expected EQR involvement

Annex 2

Start the dialogue - Key questions for audit committees to ask their auditors

Audit Planning

☐ What is the background and team mix of the engagement team? Do they possess the required knowledge and experience to address audit risks relevant to the PIE?

☐ How do the current economic conditions and challenges faced by the listed entity impact the risk assessment and planned audit procedures?

☐ How does your planned scope of work for this year's audit differ from that of the prior year?

☐ Are there any matters that create or might create threats to your independence? How do you address such threats and what safeguards will be used?

☐ Will component auditors be involved in the audit? If yes, what will be the extent of their involvement? How does the firm ensure that the work performed by the component auditor is adequate for the group auditor's purpose?

☐ (For audits related to Mainland enterprises) Did your firm appropriately evaluate the applicability of the "Interim Provisions on Accounting Firms' Provision of Auditing Services for Overseas Listing of Enterprises in Mainland China" to the audit? Have required reporting been filed with the Ministry of Finance?

☐ (If the auditor provides non-assurance services) What are the relevant considerations and safeguards for threats to auditor independence?

☐ (For first-year audit) What is your planned approach to auditing the opening balances?

☐ (For first-year audit) Regarding the unresolved audit matters that were raised by the outgoing auditor, what will be performed to address them?

Audit Reporting

☐ Did your actual scope of work differ materially from your plan? Is there any scope limitation?

☐ How many work hours did the engagement team spend on the engagement? How many hours have the engagement partner and managers spent on the audit, and the percentage of the total audit hours? Is there any significant variance compared to the budget?

☐ What key matters involve significant accounting estimates and management's judgement? What supporting evidence have you obtained to evaluate these significant management's judgement and accounting estimates? How do you assess the relevance and reliability of information produced by the entity for this purpose? Have you encountered any challenges in auditing these estimates or evaluating these assumptions?

☐ Have you ever encountered significant disagreements between you and management regarding accounting, auditing or reporting matters? If yes, have they been resolved, and how?

☐ Are you satisfied that there is no significant doubt regarding the entity's ability to continue as a "going concern"?

☐ How did you ensure that your audit firm and other audit firms of your network have maintained (and addressed the threats of, if applicable) independence throughout the audit?

Private Meeting with the Auditor

- ☐ Concerning the recent AFRC inspection results, findings and observations, what audit quality initiatives have your firm taken to address these matters?
- ☐ Was the engagement partner or the EQR subject to your firm's internal or AFRC inspection in the past three years? If yes, what were the inspection results, and what was the nature of the significant findings? What action has been taken by your firm to address the inspection findings? (If the entity's audit/assurance engagement was subjected to AFRC inspection, please request a copy of the AFRC engagement inspection report.)
- ☐ Do you have any reason to believe that information was withheld from you or that management representations were incorrect?
- ☐ In your view, is there undue pressure on management to meet financial targets, including sales or profitable incentive goals?
- ☐ Has management pressured you on any contentious issues by threatening to seek other auditors?
- ☐ Were there any circumstances in which the management did not promptly provide relevant and reliable information, creating difficulty and challenges to your work?
- ☐ Did you detect any material errors, fraud, illegal acts, significant deficiencies or weaknesses in the internal control system of the listed entity? If yes, how do they affect the audit and how did you respond to them?
- ☐ What is your general assessment of the integrity and competence of the entity's financial, accounting, IT and internal audit staffs? What improvements would you recommend?
- ☐ What percentage does the audit fee for this engagement represent in relation to your firm's total fee? Is this percentage considered material?

[1] Property Market Statistics, Rating and Valuation Department of the HKSAR
[2] Provisional statistics of retail sales for July 2024, Census and Statistics Department of the HKSAR, August 2024
[3] Survey on SMEs Credit Conditions for Second Quarter 2024, HKMA, August 2024
[4] Remarks after the US Fed FOMC Meeting, HKMA, September 2024
[5] Half-year Economic Report 2024, Government of the HKSAR
[6] April – June 2024 Quarterly Report, SFC, August 2024
[7] Safeguarding Auditor Independence: Concerns Surrounding Procurement and Purchases from Audit Clients, AFRC, October 2024
[8] Setting and Reinforcing Tone at the Top to Achieve Quality Audits, AFRC, June 2024
[9] The Importance of Audit Documentation Integrity, AFRC, May 2024
[10] Guidance Notes on Changes of Auditors, AFRC, September 2023
[11] Guidelines for Effective Audit Committees – Selection, Appointment and Reappointment of Auditors, AFRC, December 2021

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