

Press Release

3 November 2021

FRC issues Annual Investigation and Compliance Report and Interim Inspection Report

Financial Reporting Council (FRC) today issues its Annual Investigation and Compliance Report ([I&C Report](#)), covering the 18-month period from 1 October 2019 to 31 March 2021. It also publishes its Interim Inspection Report ([Inspection Report](#)) in the middle of its first 3-year inspection cycle. Both reports can be accessed on the FRC's official website – www.frc.org.hk.

Mr Marek Grabowski, CEO of the FRC remarked, "The significance of these two reports is that they provide our stakeholders with insights about the most common issues we have identified. By sharing this information with the public, we aim to remind directors, audit committees and management of listed entities in Hong Kong and their auditors to the common areas of accounting non-compliance and auditing irregularities or misconduct. We expect them to take timely action to avoid their recurrence. This should ultimately enhance the quality of financial reporting and audits of listed entities."

Dr Kelvin Wong, Chairman of the FRC remarked, "As the independent auditor regulator of Hong Kong, the FRC is held accountable to the protection of public interest. Our reports not only serve communication and education purposes but also facilitate public oversight of our regulatory performance in respect of inspection and investigation. This is how we garner public trust in our determination in combating financial misconducts, enhancing the reliability of financial information and safeguarding Hong Kong's position as an international financial centre."

Highlights of the Annual Investigation and Compliance Report:

In the 18-months to 31 March 2021, the FRC received 77 reports of matters by informants, of which 67 related to pursuable allegations, and the remaining 10 related to matters outside the remit of the FRC. It also handled 43 investigations and enquiries brought forward from 2019, initiated 25 new cases and completed 7 cases.

Speaking at the press briefing held today, Ms Wincey Lam, Head of Investigation and Compliance said, "Based on our investigations and enquires, we have identified the most common areas of financial reporting non-compliance as areas of financial reporting where management is required to make significant judgements or estimates. These are often required in areas such as fair value measurement and impairment assessment, which are commonly encountered in accounting for business combinations, financial instruments or changes in their terms, exchanges involving non-financial assets and contracts for the provision of goods or services to customers."

We further identified that these are also one of the most common areas where the related work of auditors gives rise to actual or potential auditing irregularities.”

“The most common areas of auditing irregularities that we identify include:

- (i) failing to perform the engagement quality control review adequately (85%);
- (ii) failing to properly conduct the audit to obtain sufficient appropriate audit evidence on which to base their opinion (82%);
- (iii) failing to exercise appropriate professional skepticism and professional judgement (72%); and
- (iv) aspects of the audit addressing aspects of accounting where preparers are required to make significant judgements and estimates (46%).”

Highlights of the Interim Inspection Report:

Introducing the second Interim Inspection Report, Mr Benjamin Rhys, Head of Inspection remarked, “We highly appreciate that firms have been responsive and proactive in making improvements in some of the key areas where we identified deficiencies in audits as reported from our inspections last year. For example, 55%, or 12 of the 22 engagements, completed to date had one or more deficiencies relating to the lack of exercise of professional scepticism in the audit which, while still not acceptable, is an improvement compared with the 81% of engagements inspected in 2020 with deficiencies in this area.”

“Despite the improvements in many areas, one area where there has been a marked increase in the number and significance of deficiencies identified in the auditor’s work is revenue recognition. This is a key area of the audit because of the importance of revenue as an indicator of a company’s performance to shareholders and the investing public. Of the 17 engagements where this was an area of our inspection focus, we found deficiencies in 11 cases (65%, up from 46% in 2020).”

“The Report provides information to auditors on common deficiencies identified from our inspections to date, as well as highlighting characteristics of those engagements to which we awarded the highest quality rating for the first time. Our aim is to enable auditors and audit committees to take action ahead of the next audit cycle.”

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About the Financial Reporting Council

The FRC is the full-fledged independent listed entity auditor regulator for Hong Kong committed to upholding the quality of financial reporting of listed entities of Hong Kong so as to enhance investor protection and strengthen investor confidence in corporate reporting.

For more information about the statutory functions of the FRC, please visit www.frc.org.hk.

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