South China Morning Post

9/14/2022

By: Enoch Yiu

[PwC Hong Kong, KPMG China are first firms to host US regulator for audit inspections of mainland firms, sources say]

- ***PwC and KPMG have already prepared the records to be made available on US-listed, China-based companies, sources say***
- ***Inspectors of the US-based Public Company Accounting Oversight Board (PCAOB) have not yet arrived in the city but are expected soon***

PwC Hong Kong and KPMG China are the first accounting firms that will help a US regulator carry out inspections of the audit work of US-listed mainland companies, part of a historic process that aims to head off mass delisting of Chinese companies from US exchanges.

The two firms have received notice that the Public Company Accounting Oversight Board (PCAOB) picked them for inspections of several of their audit clients, two sources familiar with the situation told the South China Morning Post.
Inspectors from PCAOB have not yet arrived in the city but are expected soon. They will serve the required three-day hotel quarantine before they begin work at the Hong Kong offices of the accounting firms, the sources added.

The two firms have already prepared the paper and electronic audit materials to be made available. All the records would have already been archived according to PCAOB standards, while auditors stand ready to be interviewed by the inspectors upon request, the sources said.

The two other Big Four accounting firms, Deloitte and EY, have not yet received notice from the PCAOB, but expect to be inspected as well, according to another two sources.

The Big Four accounting firms audit more than 130 of the 168 US-listed mainland firms, representing more than 78 per cent of the total, according to data from the PCAOB.

The PCAOB, PwC, KPMG, Deloitte and EY did not provide comments in response to a Post inquiry.

China's Securities Regulatory Commission and the PCAOB signed an agreement last month to pave the way for Beijing to allow overseas inspectors to review the audit records of Chinese companies, addressing the PCAOB's complaint about being unable to check audit quality.

Some 168 Chinese firms listed in the US, with a combined market value of US$1.5 trillion as of June, were audited by 15 Hong Kong and mainland accounting firms registered with the PCAOB, according to the audit regulator.

These companies face delisting from US exchanges under the Holding Foreign Companies Accountable Act if they do not allow the PCAOB to review their audit records for three consecutive years.

HutchMed, the pharmaceutical unit of tycoon Li Ka-shing's flagship CK Hutchison Holdings, and tech giant Alibaba Group Holding are among the 168 companies that could be affected. Alibaba owns the Post.

Hong Kong's regulator, the Financial Reporting Council, will provide all necessary help and facilitation for PCAOB inspectors as far as it is able to, Christopher Hui Ching-yu, Secretary for Financial Services and the Treasury, said in an earlier interview with the Post.

The several accounting sources, however, said that the PCAOB did not request much help from the FRC, as the US regulator decided on its inspection targets and logistics itself.

The Chinese regulator will allow auditors to bring records to Hong Kong for PCAOB inspection after redacting sensitive details such as addresses, names of factories and personal information, the sources said.

"While we do not have any specific knowledge of which audits the PCAOB will inspect, generally the PCAOB will seek to look at a representative sample of an auditor's work, with a focus on companies that may present a greater level of audit risk or that are of greatest importance to prospective investors," said Drew Bernstein, co-chairman of Marcum Asia CPAs LLP, a New York-headquartered accounting firm focused on Asia companies seeking access to US capital markets.

It will be a “race against the clock” to complete enough work to allow the PCAOB to certify to the US Congress that China is in compliance with the Holding Foreign Companies Accountable Act by year’s end, Bernstein said.

If the initial round of audit inspections in Hong Kong is carried out successfully, it should encourage more mainland firms to seek listings in the US, he added.

“I believe we will see a sizeable backlog of Chinese companies coming to market in 2023,” he said.