

**Bills Committee on  
Financial Reporting Council Bill**

**Tenth meeting on 10 February 2006**

**List of follow-up actions to be taken by the Administration**

Organizational structure of the Audit Investigation Board (AIB) and a Financial Reporting Review Committee (FRRC)

1. The Administration undertakes to propose a Committee Stage amendment (CSA) to expressly provide that the quorum for any meeting of the AIB is to be two members, or half of its members, whichever is the greater (paragraph 6 of LC Paper No. CB(1)866/05-06(04)).
2. The Administration undertakes to propose a CSA to expressly provide that the quorum for any meeting of a FRRC is to be half of its members (paragraph 6 of LC Paper No. CB(1)866/05-06(02)).
3. The Administration undertakes to propose a CSA to the effect that if a member of the Financial Reporting Council (FRC), the AIB, or a FRRC has disclosed an interest in the matter being investigated or enquired, the member will not be counted for the purpose of forming a quorum at the relevant meeting of the FRC, the AIB, or a FRRC (paragraph 7 of LC Paper No. CB(1)866/05-06(04)).
4. In connection with item 4 of the list of follow-up actions for the meeting on 12 January 2006 (LC Paper No. CB(1)866/05-06(01)), the Administration agrees to review whether the drafting of the relevant provisions in the Bill may give rise to any doubts concerning the position that a change in the membership of a FRRC during an enquiry will neither itself constitute a breach of the principles of natural justice nor affect the Committee's legal status and the legality of evidence collected by it. The Administration will revert to the Bills Committee during the clause-by-clause examination of the Bill (paragraph 4 of LC Paper No. CB(1)866/05-06(02)).
5. According to the Administration, in the unlikely situation that where most or all of the members of the AIB or a FRRC cannot or should not continue to serve, for example, due to death or conflict of interest in the matter being investigated or enquired, the AIB or FRRC would not be able to continue to operate as it cannot meet the quorum requirement for meetings. In such circumstances, provisions in the Interpretation and General

Clauses Ordinance (Cap.1) may be invoked to deal with issues relating to vacancy in the membership and dissolution of the AIB or FRRC. In this connection, the Administration is requested to consider and respond to the views and suggestions of members of the Bills Committee, as follows:

- (a) It may not be appropriate to rely on the general principles provided in Cap. 1 to deal with matters relating to the operation of the AIB or a FRRC; and
- (b) The Administration is requested to re-consider the need of setting out clearly in the Bill how matters relating to vacancy in the membership and dissolution of the AIB or a FRRC should be dealt with.

#### Enquiry powers of the AIB and a FRRC

6. Members note that the Administration has consulted the Hong Kong Institute of Certified Public Accountants (HKICPA), and the latter is of the view that, as a matter of principle, it will be preferable for the FRC to utilize the proposed powers conferred upon it under clauses 31, 32 and 45 to enforce an information-gathering requirement imposed on a certified public accountant than to look to the Institute to do so under the Professional Accountants Ordinance (PAO) (Cap. 50). While the PAO provides that a failure or neglect of a certified public accountant to comply with a requirement of an Investigation Committee of the HKICPA is disciplinable under the PAO, the HKICPA considers that the PAO is not generally intended to enforce the powers of statutory bodies other than the HKICPA. The HKICPA therefore considers that it is not necessary to add an express provision in the PAO to the effect that a certified public accountant failing to comply with a requirement imposed by the AIB or a FRRC should be concurrently disciplinable (paragraph 11 of LC Paper No. CB(1)866/05-06(02)). However, the HKICPA also points out that, in serious cases, disciplinary action may be invoked under section 34(1)(a)(x) of the PAO as a catch-all provision for conduct which would be reasonably regarded as bringing discredit upon the Institute or the accountancy profession (footnote 11 of LC Paper No. CB(1)866/05-06(02)). In this connection, the Administration is requested to invite the HKICPA to re-consider its position having regard to views expressed by members of the Bills Committee, as follows:

- (a) Given that the HKICPA may initiate disciplinary proceedings against a certified public accountant who has failed to comply with a requirement of its Investigation Committee under section 34(1)(a)(vii) of the PAO, and that it is the Administration's policy intent that the AIB be set up to take over the investigation functions of the HKICPA in respect of suspected irregularities of

the accountancy profession in relation to the audit of accounts for listed entities, it is justified to provide explicitly in the PAO that a certified public accountant failing to comply with a requirement of the AIB or a FRRC should be subject to disciplinary proceedings of the HKICPA;

- (b) In connection with item (a) above, it should also be noted that failure to comply with an information-gathering requirement imposed by the AIB without reasonable excuse is a criminal offence under clause 31. This forms a justifiable ground for the HKICPA to initiate disciplinary proceedings against the certified public accountant concerned; and
  - (c) Section 34(1)(a)(x) of the PAO is concerned with serious misconduct and may only be invoked for conduct which could be reasonably regarded as bringing discredit upon the HKICPA or the accountancy profession. It appears that the provision may not be readily invoked for every matter relating to accountants' non-compliance with information-gathering requirements of the AIB or a FRRC.
7. In connection with item 6 above, the Administration is requested to consider members' view that administrative arrangements should be put in place for the FRC to inform the HKICPA of non-compliance of accountants with the information-gathering requirement of the AIB or a FRRC so as to facilitate the Institute to initiate appropriate disciplinary actions.

#### Clauses 49 and 50 – Revision of financial reports

8. Having noted the Administration's response to members' concerns on clauses 49 and 50 (paragraphs 12 and 13 of LC Paper No. CB(1)866/05-06(02)), some members raise further questions. In this connection, the Administration is requested to consider and respond to members' views and suggestions, as follows:
- (a) Given that the FRC is tasked to enquire into financial non-compliances of listed entities and does not have sanctioning power, it seems not justified to empower the FRC to request listed entities to revise their defective financial reports;
  - (b) The request for a listed entity to revise its financial report may imply that there is a relevant non-compliance in relation to the entity and the reporting accountant concerned has failed to prepare the reports in accordance with the relevant financial standards. It is doubtful as to whether the FRC should make a positive assertion

that there is a relevant non-compliance in relation to a listed entity without giving the parties concerned an opportunity to respond to the FRC's findings. Such an assertion is against the principles of law and principles of natural justice;

- (c) The question of whether there is a relevant non-compliance in relation to a listed entity and the reporting accountant concerned should be determined by the court or the relevant disciplinary body;
- (d) In connection with items (a) to (c) above, the Administration should review the drafting of clauses 49 and 50 with reference to sections 245A and 245B of the United Kingdom (UK) Companies Act 1985 on which the two clauses are modelled. In particular, the Administration is requested to consider some members' suggestions that consideration should be given to revise the drafting of clause 49(1) to the effect that:
  - (i) the positive assertion "there is a relevant non-compliance ..." in clause 49(1) be replaced by the formulation used in section 245A(1) of the UK Companies Act 1985, i.e. "there is, or may be, a question whether...."; and
  - (ii) the FRC is required to issue a notice to the listed entity concerned indicating the respects in which it appears to the FRC that a question of a relevant non-compliance arises or may arise (section 245A(1) of the UK Companies Act 1985) and specifying a period for the listed entity and the persons concerned to give an explanation (section 245A(2) of the UK Companies Act 1985).

#### Clause 51 - Preservation of secrecy

9. Members note the Administration's policy intent that the Official Receiver (OR) will only use the disclosure gateway under clause 51(3)(b)(ix) to obtain information for performing his statutory duties as OR other than in the capacity of a liquidator/provisional liquidator under the Companies Ordinance (CO) (Cap. 32), while the OR will use the disclosure gateway under clause 51(3)(c) to obtain information for performing his statutory duties as OR in the capacity of a liquidator/provisional liquidator (paragraph 3 of LC Paper No. CB(1)866/05-06(04)). In this connection, the Administration is requested to provide proposals for improving the relevant provisions to clearly reflect the policy intent for the Bills Committee's consideration as soon as practicable.

10. Having noted the Administration's response to members' concern on clause 51 (paragraph 4 of LC Paper No. CB(1)866/05-06(04)) and considered the protection of informers provision under section 30A of the Prevention of Bribery Ordinance (PBO) (Cap. 201) and similar provisions in other ordinances (LC Paper No. LS27/05-06), the Administration is requested to respond to members' views and suggestions, as follows:
  - (a) The purpose of clause 51 is to preserve the secrecy of information obtained by the FRC in the course of performing its functions rather than to protect the identity of the persons who lodge complaints to the FRC; and
  - (b) Given the need to safeguard the interests of informers of the FRC, the Administration should make reference to section 30A of the PBO and relevant provisions in other ordinances to provide in the Bill separate provisions on "Protection of informers".

#### Clause 52 – Avoidance of conflict of interests

11. Clause 52(3) provides that a person has an interest in a matter if the matter relates to a listed entity in which he has an interest, or relates to his past or present employers, clients, associates, or another person whom he knows is or was a client of his, past or present, employers or associates. In this connection, the Administration is requested to clarify whether clause 52(3) would apply to a matter which relates to a person's past employer, which is an entity merged with other entities and no longer exists by itself.
12. Clause 52(5) provides that after a member of the FRC, the AIB or a FRRC has disclosed the nature of any interest in any matter, unless the FRC otherwise determines, he shall not be present during any deliberation of the FRC, the AIB, or a FRRC, or take part in any decision, with respect to the matter. Clause 52(6) further provides that the member shall not be present during any deliberation of the FRC, the AIB, or a FRRC for the purpose of making the determination under clause 52(5), or take part in the making of the determination by the FRC. In this connection, the Administration is requested to respond to members' views and suggestions, as follows:
  - (a) It is not fair and justified to require the FRC to determine whether a person who has disclosed interest in a matter should present during the deliberation of or take part in the decision with respect to the matter, given that it is the person concerned, not the FRC, who has the knowledge about the nature of the interest and conflicts involved. It is suggested that:

- (i) the wording “unless the Council otherwise determines” in clause 52(5) be deleted;
  - (ii) clause 52(6) be deleted; and
  - (iii) clause 52(5)(b) be amended to the effect that the member who has disclosed interest in a matter shall not take part in any meetings of the FRC, the AIB or a FRRC, with respect to the matter.
- (b) While the title of clause 52 is “Avoidance of conflict of interests (避免利益衝突)”, subclauses (2) and (5) require a person to disclose the nature of the interest (披露該利害關係的性質). The Administration should examine whether there is any inconsistency between the title of clause 52 and the requirement under the two subclauses; and if there is, to review the drafting of clause 52 for making improvement;
- (c) Consideration should be given to set out clearly the kinds of interest that required to be disclosed and the circumstances under which such disclosures should be made; and
- (d) Consideration should be given to include provisions in the Bill to prevent a member who has disclosed interest in a matter from accessing information (e.g. papers, minutes of meetings) available to the FRC, the AIB or a FRRC concerning the matter.