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L/M to (5) in G9/8/5(04) Pt.3

15 June 2005

Clerk to Panel on Financial Affairs, Legislative Council
(Attn: Ms. Connie Szeto)
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms. Szeto,

**LegCo Panel on Financial Affairs
Follow-up to Meeting on 6 May 2005**

**Consultation Conclusions on Legislative Proposals
to Establish the Financial Reporting Council**

I refer to your letter of 12 May 2005. Having consulted the Hong Kong Institute of Certified Public Accountants (HKICPA) and the Department of Justice (D of J), we set out our responses in the ensuing paragraphs.

The “Investigatory” Role of the Financial Reporting Council (FRC)

2. We note that a Member was concerned that the referral of cases to the HKICPA and law enforcement agencies might result in “duplication of investigatory efforts” and “wastage of resources”. Suggestions had been made for the Administration to explore whether to -

- (a) empower the FRC to undertake “prosecution” after investigation; or
- (b) put in place a mechanism for the HKICPA or the law enforcement agencies to identify the suspected irregularities, including stating any possible offences of an auditor, for the FRC to undertake investigation.

3. In response, we would like to make reference to the **existing** modus operandi under which the HKICPA deals with a complaint. At present, under the Professional Accountants Ordinance (PAO, Cap. 50), there is generally a “two-stage” approach in dealing with a complaint against HKICPA’s members, registered firms and corporate practices. Where the Council of the HKICPA reasonably suspects or believes that an irregularity has occurred, the Council of the HKICPA may constitute an Investigation Committee (constituted by drawing members from the Investigation Panels) to investigate the complaint¹. Subsequent to the completion of the investigation, the Council of the HKICPA will consider the Investigation Committee’s findings and may refer the case to a Disciplinary Committee (constituted by drawing members from the Disciplinary Panels) to take disciplinary actions².

4. Upon the establishment of the FRC, the FRC will investigate auditors’ irregularities involving listed entities, whereas the HKICPA will continue to deal with other cases including those in the non-listed sector. In this light, the FRC will take the place of the HKICPA’s Investigation Committees in respect of the investigation of auditors’ irregularities concerning listed entities. After the completion of the FRC’s investigation, the FRC may refer the case to the Council of the HKICPA which may constitute a Disciplinary Committee to take disciplinary actions. The proposed arrangement reflects the majority view in the public consultation conducted by the Administration in late 2003, namely that the FRC’s role should be investigatory only and disciplinary proceedings should continue to be vested with the relevant professional bodies such as the HKICPA.

¹ Section 42C(2)(a) of the PAO.

² Section 34(1) of the PAO.

5. We do not consider that there will be practical difficulties in relation to the referral of cases from the FRC to the HKICPA. At present, the Disciplinary Committees of the HKICPA also rely on the findings of the Institute's Investigation Committees, each of which comprises a majority of lay persons, to consider whether a complaint is proven. Furthermore, with a view to enabling a smooth interface between the FRC and the HKICPA (or law enforcement agencies), the FRC Bill will contain provisions to -

- (a) empower the FRC to provide assistance to the HKICPA and other bodies and enter into memoranda of understanding to settle the detailed arrangement therefor. Such assistance may include disclosing the evidence obtained during the investigation to the HKICPA for the preparation of the proceedings and giving evidence during such proceedings; and
- (b) enable a copy of the FRC's investigation report to be admissible in any proceedings before a court or magistrate or the Market Misconduct Tribunal, or any investigation and disciplinary proceedings of the HKICPA under the PAO, as evidence of the facts stated in the report.

Second Public Consultation

6. We would also like to reply that, during the public consultation earlier this year, a respondent had requested that his name should not be disclosed, and that his views have been covered in the summary of submissions attached to the Administration's paper for the Panel meeting on 6 May 2005.

Yours sincerely,

(Alan Lo)
for Secretary for Financial Services and the Treasury

c.c.

Hong Kong Institute of Certified Public Accountants

(Attn: Mr. Edward Chow, President)

(Attn: Ms. Winnie Cheung, Chief Executive and Registrar)

Department of Justice

(Attn: Ms. Beverly Yan, Civil Division)

(Attn: Mr. Lawrence Peng, Law Drafting Division)

(Attn: Miss Selina Lau, Law Drafting Division)

Registrar of Companies

(Attn: Mr. Gordon Jones)