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**Bills Committee on
Professional Accountants (Amendment) Bill 2004**

Background Brief

Purpose

This paper sets out some background information on the Professional Accountants (Amendment) Bill 2004 (the Bill), and provides a summary of the views expressed by Members when the legislative proposals under the Bill were deliberated at meetings of the Panel on Financial Affairs (FA Panel).

Background

2. The accounting and auditing profession in Hong Kong is subject to a self-regulatory regime in which the Hong Kong Society of Accountants (HKSA) plays a pivotal role. The Professional Accountants Ordinance (Cap. 50) (the Ordinance) establishes the HKSA and sets out its objects (section 7 of the Ordinance), powers and functions. HKSA's objects include registration; regulation of practices; education and maintaining the integrity of the profession. In pursuing these objectives, HKSA sets admission and continuing registration criteria for its members; sets accounting and auditing standards, including ethical standards; oversees the quality of auditing practices and monitors compliance with standards; conducts investigations and exercises disciplinary powers where warranted.

3. The landscape within which professional accountants operate has undergone dramatic changes in recent years. Confidence in the profession has been brought into sharp focus after the corporate scandals in the United States. In December 2002, the Secretary for Financial Services and the Treasury met with representatives of the accounting profession to discuss ways to improve the existing regime set out in the Ordinance. In response to the Administration's request to enhance the element of oversight in the present regulatory regime, HKSA put forward in late January 2003 a series of proposals to open up its governance structure and to improve the present regulatory processes enshrined in the law. The major proposals include -

- (a) increasing the lay members and Government appointed officials in the HKSA Council (i.e. its governing body);
- (b) expanding the membership of an Investigation Committee instigated by the HKSA Council from three to five, and altering the composition of the Investigation Committee, with the majority of members (including the chairman) being lay persons;
- (c) altering the composition of the 5-member Disciplinary Committee instigated by the HKSA Council, with the majority of members (including the chairman) being lay persons; and
- (d) as a variation of (b) above, establishing an Independent Investigation Board (IIB) to deal with alleged accounting, auditing and/or ethics irregularities related to the audit of companies listed on the Stock Exchange of Hong Kong.

4. The Administration considers that HKSA's proposals are a move in the right direction. The proposals in (a) to (c) above are the key steps in enhancing the oversight of HKSA's key functions and thus the oversight over the accounting profession. Since the proposal to establish an IIB warrants more detailed examination and is the subject of a separate consultation exercise undertaken by the Administration¹, HKSA considers it desirable to implement the proposals set out in (a) to (c) above as the first step. With the written consent of the Chief Executive in compliance with Rule 51(4) of the Rules of Procedures of the Legislative Council, the Bill was presented by Dr Hon Eric LI to the Legislative Council on 24 March 2004.

Objectives of the Bill

5. The Bill seeks to amend the Ordinance to -
- (a) change the name of HKSA to the "Hong Kong Institute of Certified Public Accountants" (the Institute);
 - (b) expand the membership of the Council of the Institute (the Council) by increasing the number of lay members and the number of elected members;

¹ The Administration issued a consultation paper on the proposal to establish an IIB in September 2003 and reported on the outcome of the consultation at the meeting of the Financial Affairs Panel held on 2 April 2004.

- (c) reform the investigation and disciplinary mechanism under the Ordinance, including the expansion of the membership of an Investigation Committee appointed by the Council from three to five, with the majority of members (including the chairman) being lay persons, and altering the composition of a Disciplinary Committee appointed by the Council, with the majority of members (including the chairman) being lay persons;
- (d) broaden the powers of the Council and the Investigation Committee and the sanctions available to the Disciplinary Committee;
- (e) provide immunity to members of the Council and its delegates, the Registrar and officers and employees of the Institute exercising statutory powers in good faith;
- (f) make miscellaneous technical amendments; and
- (g) make consequential amendments to the Professional Accountants By-laws (Cap. 50 sub. leg. A) and to other Ordinances and subsidiary legislation.

Discussions at the Panel on Financial Affairs

6. The FA Panel discussed the policy issues relating to the proposals in the Bill at its meetings on 13 June 2003 and 3 May 2004. Moreover, at its meeting on 2 April 2004, the Panel was briefed by the Administration on the progress of the initiatives to enhance the regulation of the accountancy profession and preparers of financial statements. Members noted that the proposals in the Bill form part of these initiatives.

7. Concern was raised by a member that the proposal of increasing the number of lay members to the Council would signify a departure from the general principle of self-regulation of professional bodies and might have an impact on the governance structure of other professional bodies, such as the Law Society of Hong Kong and the Hong Kong Medical Association. The Administration advised that under the existing Professional Accountants Ordinance, the Chief Executive (CE) might appoint to HKSA's Council two members who were academics from universities or other education institutions which provided courses of instruction in accountancy, but CE had not exercised this power of appointment in the past. To open up the Council, it was proposed under the Bill that CE might appoint four non-accountant members to the Council. The Administration recognized that given the significant impact of the work of the accounting profession on the financial services market and the general public as a whole, there was a need to enhance the public oversight of the profession and the transparency of HKSA's Council. The proposal of increasing the number of lay members of HKSA's Council would serve these purposes and hence was supported by the

Administration. The Administration also indicated that its intention was to make full use of the appointment mechanism to appoint four lay members to the Council.

8. Some members considered that the proposal of reforming HKSA's Investigation Committee and Disciplinary Committee was related to the proposal of establishing an IIB, and hence it might be more appropriate for the Administration to take forward these proposals in a single legislative exercise by way of a Government Bill. Dr Hon Eric LI clarified that the proposal of reforming the investigation and disciplinary mechanisms under the Ordinance was the first step taken by HKSA to open up its self-regulatory structure. The proposal to establish an IIB would be the subject of a separate government Bill, if that was so decided by the Administration. As more time was needed to work out the details of the IIB proposal, it was advisable as the first step to implement the proposals relating to the self-regulatory regime of the accounting profession, i.e. the proposals in the current Member's Bill. Dr Hon Eric LI stressed that there was no conflict between the proposals in the Bill and the IIB proposal.

9. Noting that the majority of the Council members would still be professional accountants, a member was concerned how the proposal under the Bill could meet public aspiration for enhancing public oversight of the accountancy profession. Dr Hon Eric LI explained that apart from increasing the number of lay members in the Council, there were also proposals in the Bill to reform the composition of HKSA's Investigation Committee and Disciplinary Committee and to broaden their powers. Lay members would form the majority of both committees. These changes would enhance public oversight over the conduct and work of professional accountants.

10. On the proposed arrangements to ensure continuity of the work of the HKSA Council, representatives of HKSA advised that upon enactment of the Bill, the immediate past president would be appointed to serve a term of one year, and the appointment periods of the lay members could be staggered to provide for continuity.

11. Members noted that HKSA had consulted its members on the proposals under the Bill and these were supported by a great majority of its members. Members appreciated the need to enhance the effectiveness and transparency of the regulatory regime of the accountancy profession to inspire confidence of the investing public and considered it more prudent for the Legislative Council to form a bills committee to examine the relevant policy and technical issues in detail.