

立法會
Legislative Council

LC Paper No. CB(1)1160/17-18
(These minutes have been seen
by the Administration)

Ref : CB1/BC/4/17/2

Bills Committee on Financial Reporting Council (Amendment) Bill 2018

**Minutes of the third meeting on
Tuesday, 10 April 2018, at 10:45 am
in Conference Room 2A of the Legislative Council Complex**

Members present : Hon WONG Ting-kwong, GBS, JP (Chairman)
Hon Kenneth LEUNG (Deputy Chairman)
Hon CHAN Kin-por, GBS, JP
Hon WU Chi-wai, MH
Hon Dennis KWOK Wing-hang
Hon Christopher CHEUNG Wah-fung, SBS, JP
Hon CHAN Chun-ying
Hon CHEUNG Kwok-kwan, JP
Hon Kenneth LAU Ip-keung, BBS, MH, JP

Members absent : Hon James TO Kun-sun
Hon Starry LEE Wai-king, SBS, JP
Hon Mrs Regina IP LAU Suk-yee, GBS, JP
Hon Charles Peter MOK, JP
Dr Hon Junius HO Kwan-yiu, JP

Public officers attending : Ms NG Ching-ching, Winnie, JP
Deputy Secretary for Financial Services and the
Treasury (Financial Services)³

Mr AU Ka-shing, Billy
Principal Assistant Secretary for Financial Services and
the Treasury (Financial Services)⁴

Mr CHAN Fong-ming
Assistant Secretary for Financial Services and the
Treasury (Financial Services)(4)1

Ms CHAN Ka-man, Carmen
Senior Government Counsel
Department of Justice

Ms CHEUNG Mee-bo, Mabel
Senior Assistant Law Draftsman (LP)
Department of Justice

Attendance by invitation : Mr Paul F WINKELMANN
Chief Executive Officer
Financial Reporting Council

Ms Florence WONG
Senior Director (Investigation & Compliance)
Financial Reporting Council

Clerk in attendance : Ms Connie SZETO
Chief Council Secretary (1)4

Staff in attendance : Miss Evelyn LEE
Assistant Legal Adviser 10

Mr Hugo CHIU
Senior Council Secretary (1)4

Ms Sharon CHAN
Legislative Assistant (1)4

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I Meeting with the Administration

Matters arising from the previous meeting

(LC Paper No. CB(1)771/17-18(01) — List of follow-up actions arising from the discussion at the meeting on 20 March 2018

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- LC Paper No. CB(1)771/17-18(02) — Administration's response to issues raised at the meeting on 20 March 2018
- LC Paper No. CB(1)783/17-18(01) — Letter dated 19 March 2018 from the Legal Service Division to the Administration
- LC Paper No. CB(1)783/17-18(02) — Administration's response to the letter dated 19 March 2018 from the Legal Service Division)

Other relevant papers

- (LC Paper No. CB(3)287/17-18 — The Bill
- File Ref: ACCT/2/1/2C — Legislative Council Brief
- LC Paper No. LS25/17-18 — Legal Service Division Report
- LC Paper No. CB(1)591/17-18(01) — Marked-up copy of the Financial Reporting Council (Amendment) Bill 2018 prepared by the Legal Service Division (Restricted to members only)
- LC Paper No. CB(1)590/17-18(01) — Background brief prepared by the Legislative Council Secretariat)

Discussion

The Bills Committee deliberated (Index of proceedings attached at **Appendix**).

II Any other business

Date of next meeting

2. The Chairman informed that the next meeting was scheduled for 8 May 2018, at 2:30 pm. In order to allow sufficient time for the Legal Advisor to the Bills Committee to study the Administration's response to issues relating to the

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Bill, and for the Administration to respond to any further issues raised by her, members agreed that the meeting on 8 May 2018 should be deferred if necessary.

(Post meeting note: The Chairman decided that the fourth meeting on 8 May be rescheduled for 5 June 2018, at 10:45 am, and the fifth meeting be held on 10 July 2018, at 10:45 am. Members were informed of the meeting arrangements vide LC Paper No. CB(1)858/17-18 issued on 24 April 2018)

3. There being no other business, the meeting ended at 11:38 am.

Council Business Division 1
Legislative Council Secretariat
21 June 2018

**Proceedings of the third meeting of
the Bills Committee on Financial Reporting Council (Amendment) Bill 2018
on Tuesday, 10 April 2018, at 10:45 am
in Conference Room 2A of the Legislative Council Complex**

Time Marker	Speaker	Subject(s)	Action Required
Agenda item I — Meeting with the Administration			
000429 – 001135	Chairman Administration	Briefing by the Administration on its response to issues raised at the meeting on 20 March 2018 [LC Paper No. CB(1)771/17-18(02)]	
001136 – 001905	Chairman Deputy Chairman Administration The Financial Reporting Council ("FRC")	<p>Deputy Chairman's enquiries as follows:</p> <p>(a) whether auditors of public interest entities ("PIE auditors") would be subject to the disciplinary sanctions of the Financial Reporting Council ("FRC") under the proposed new regulatory regime if they had done certain acts because their professional interpretation of certain accounting standards were different from that of FRC;</p> <p>(b) whether the guidelines to be issued by FRC on how it would exercise the power to impose pecuniary penalty ("the Guidelines") would include the consideration that the amount of the pecuniary penalty would not cause financial jeopardy on the auditor or responsible person concerned; and</p> <p>(c) whether the Guidelines would include examples illustrating how FRC would consider the various factors in determining the level of pecuniary penalty to be imposed.</p> <p>FRC responded as follows:</p> <p>(a) PIE auditors would not be subject to disciplinary sanctions if they merely disagreed with FRC on the interpretation of accounting standards. The majority of misconduct cases of auditors referred by</p>	

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		<p>FRC to the Hong Kong Institute of Certified Public Accountants for follow-up at present involved the lack of work and/or depth of the audit procedures by the auditors concerned;</p> <p>(b) the Guidelines would elaborate on how FRC would apply the various principles it had to adhere to in determining the level of pecuniary penalty including that the amount of pecuniary penalty would not put the auditor or responsible person concerned in financial jeopardy;</p> <p>(c) FRC was currently studying an independent report released in the United Kingdom, which advocated more uses of non-financial penalties; and</p> <p>(d) the Guidelines would set out examples of aggravating and mitigating factors to be taken into account by FRC.</p>	
001906 – 002440	Chairman Mr Christopher CHEUNG Administration	<p>Mr CHEUNG's views and enquiries as follows:</p> <p>(a) the proposed levies on securities transactions for funding the post-reform FRC was unfair to investors;</p> <p>(b) the Administration should bear part of the expenditure of the post-reform FRC, and consider providing a seed money of around \$500 million to subsidize the operation of FRC; and</p> <p>(c) FRC should put in place a levy review mechanism for adjusting (i) the rates/amounts of the levies; and (ii) the ratio of contributions from securities transactions, PIEs and PIE auditors when FRC's reserves reached a level equivalent to 36 months of its operating expenses.</p> <p>The Administration responded as follows:</p> <p>(a) it noted some members' views that the Government should be one of the funding sources of FRC under the proposed new</p>	

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		<p>regulatory regime. It would carefully consider the view before finalizing FRC's funding mechanism; and</p> <p>(b) the Financial Reporting Council (Amendment) Bill 2018 ("the Bill") had included provisions for FRC to review the rates/amounts of the levies and consult the Financial Secretary with a view to recommending to the Chief Executive-in-Council for reducing the levies when FRC's reserves (after deducting depreciation and all provisions) were more than twice of its operating expenses for the financial year and FRC had no outstanding debt.</p>	
002441 – 004215	Chairman Deputy Chairman Administration FRC	<p>Deputy Chairman's enquiries as follows:</p> <p>(a) how FRC could conduct inspections and investigations on recognized PIE auditors, and whether recognized PIE auditors in the Mainland ("recognized Mainland PIE auditors") and other jurisdictions ("recognized overseas PIE auditors") would be subject to different arrangements;</p> <p>(b) whether FRC had concluded any regulatory cooperation agreements with major overseas regulators; and</p> <p>(c) whether there would be transitional arrangements for overseas auditors who had been undertaking PIE engagements to migrate to the new regulatory regime.</p> <p>The Administration replied as follows:</p> <p>(a) under the proposed new regulatory regime, FRC's inspection and investigation powers over local PIE auditors would be equally applicable to overseas PIE auditors;</p> <p>(b) the recognition procedures for overseas PIE auditors and Mainland PIE auditors were different. If an overseas corporation or collective investment scheme ("CIS") listed in Hong Kong</p>	

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		<p>intended to engage an overseas auditor for undertaking its PIE engagements, it had to, as the case might be, seek prior approval of the Hong Kong Exchanges and Clearing Limited ("HKEX") or the Securities and Futures Commission ("SFC"). If the requisite approval was obtained, the corporation/CIS might apply to FRC to recognize the overseas auditor concerned. The eligibility criteria for a recognized overseas PIE auditor would be largely modeled on the prevailing requirements of HKEX and SFC. Besides, there must be a regulatory cooperation agreement between FRC and the corresponding overseas regulator before FRC might recognize the overseas auditor concerned;</p> <p>(c) as for auditors in the Mainland, Hong Kong and the Mainland had entered into a reciprocal arrangement ("the Reciprocal Arrangement") in 2009 to enable Mainland-incorporated companies listed or seeking to be listed in Hong Kong to engage any one of the specified Mainland audit firms which had been assessed as meeting specific conditions for auditing financial statements using Mainland auditing standards ("specified Mainland audit firms"). There were currently 11 specified Mainland audit firms and the Bill would enable FRC to recognize such firms as recognized Mainland PIE auditors;</p> <p>(d) when conducting inspection and investigation on a recognized overseas PIE auditor, FRC might seek the assistance of the relevant overseas regulator in accordance with the regulatory cooperation agreement as necessary. Similarly, FRC might seek the assistance of the Mainland regulators in accordance with the relevant mechanism under the Reciprocal Arrangement if FRC conducted inspection and investigation on a recognized Mainland PIE auditor;</p>	

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		<p>(e) FRC would start concluding regulatory cooperation agreements with other overseas regulators upon enactment of the Bill. As only less than 4% of listed corporations or CISs in Hong Kong had been engaging overseas PIE auditors, it was envisaged that FRC would only need to conclude regulatory cooperation agreements with a small number of jurisdictions; and</p> <p>(f) under the proposed new section 90 of the Financial Reporting Council Ordinance (Cap. 588), an overseas auditor might notify FRC of its intention to continue with a PIE engagement which it had undertaken but not yet completed before commencement of the Bill. The overseas auditor concerned would then be taken to be a recognized PIE auditor during the transitional period. The auditor concerned might also file an application to FRC for recognition as a PIE auditor under the new regime during the transitional period.</p> <p>Deputy Chairman's views that FRC should expedite its work in concluding regulatory cooperation agreements with overseas regulators as soon as possible after passage of the Bill so that FRC could recognize these overseas auditors in time. The Chairman concurred with the view.</p> <p>FRC responded as follows:</p> <p>(a) FRC was mindful of the need to expedite its work in concluding regulatory cooperation agreements with overseas regulators, and was also holding discussion with the Ministry of Finance in relation to recognized Mainland PIE auditors;</p> <p>(b) FRC would start concluding regulatory cooperation agreements with overseas regulators upon passage of the Bill. It was envisaged that cross-border regulation of the auditing profession could be further</p>	

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		<p>streamlined if Hong Kong could meet the European Commission regulatory equivalence requirements in future; and</p> <p>(c) FRC anticipated that some 35 overseas audit firms would apply for becoming recognized PIE auditors. The demand for recognized PIE auditors might rise with an expected increase in the number of overseas companies applying for listing in Hong Kong.</p>	
004216 – 004513	Chairman Administration	<p>The Chairman enquired about the mechanism for amending the list of specified Mainland audit firms.</p> <p>The Administration explained that:</p> <p>(a) if an overseas auditor (other than the 11 specified Mainland audit firms) intended to undertake PIE engagements for a corporation/CIS listed in Hong Kong, the corporation/CIS concerned had to apply to FRC to recognize the auditor as a recognized PIE auditor. The 11 specified Mainland audit firms designated under the Reciprocal Arrangement were not required to submit application to FRC for recognition as PIE auditors. The Bill allowed FRC to recognize these PIE auditors as long as they met the specific conditions stipulated in the Bill; and</p> <p>(b) proposed changes to the list of specified Mainland audit firms would necessitate discussion with the Mainland regulators in accordance with the relevant mechanism in the Reciprocal Arrangement.</p>	
004514 – 005138	Chairman Deputy Chairman Administration	<p>Deputy Chairman's enquiries as follows:</p> <p>(a) how FRC could impose disciplinary sanctions (including pecuniary penalty) against recognized PIE auditors;</p> <p>(b) whether the Administration would require recognized PIE auditors to take out professional indemnity insurance in Hong Kong, and whether other major</p>	

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		<p>jurisdictions had imposed similar requirement on PIE auditors; and</p> <p>(c) whether the 11 specified Mainland audit firms could continue to undertake PIE engagement for corporations and CISs listed in Hong Kong if FRC had imposed severe disciplinary sanctions on them.</p> <p>The Administration responded that:</p> <p>(a) under the proposed new regulatory regime, FRC's disciplinary powers over local PIE auditors would be equally applicable to overseas PIE auditors;</p> <p>(b) the 11 specified Mainland audit firms, upon recognition by FRC as recognized PIE auditors, could undertake PIE engagements for any Mainland corporations listed in Hong Kong using Mainland auditing standards. If FRC identified any misconduct in relation to the PIE engagements undertaken by the 11 specified Mainland audit firms, FRC could order the auditor concerned to stop undertaking PIE engagements for the relevant corporation. FRC would also inform the relevant Mainland regulators of its findings, so that the regulators could decide whether they should take further actions against the auditor concerned including removing it from the list of specified Mainland audit firms; and</p> <p>(c) an overseas auditor (other than the 11 specified Mainland audit firms) could not undertake PIE engagements for corporations/CISs listed in Hong Kong at will. A corporation/CIS listed in Hong Kong had to apply to FRC for recognizing an overseas auditor as a recognized PIE auditor first before the auditor could undertake PIE engagements for that corporation/CIS. If the PIE auditor's recognition was suspended/revoked by FRC, it could no longer undertake PIE engagements for the corporation/CIS concerned.</p>	

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005139 – 005650	Chairman Assistant Legal Adviser 10 ("ALA10") Deputy Chairman	<p>The Chairman said that the Legal Adviser to the Bills Committee ("ALA10") had issued a letter on 19 March 2018 to the Administration on certain legal and drafting issues relating to the Bill, and the Administration had provided its response on 9 April 2018 (i.e. a day before the meeting was held). [LC Paper Nos. CB(1)771/17-18(03) and CB(1)783/17-18(01)]. Both documents were tabled at the meeting.</p> <p>Members agreed that in order to allow sufficient time for ALA10 to study the Administration's responses and for the Administration to respond to any further issues raised by ALA10, consideration should be given to re-scheduling the meeting to be held on 8 May 2018 if necessary. Members also agreed that the Bills Committee would commence clause-by-clause examination of the Bill after it had considered the issues raised by ALA10 and the Administration's responses.</p>	
Agenda item II — Any other business			
005651 – 005715	Chairman	Date of next meeting	