

9 March 2018

Clerk to Bills Committee on Financial Reporting Council (Amendment) Bill 2018  
Legislative Council Secretariat  
Legislative Council Complex  
1 Legislative Council Road  
Central  
Hong Kong

Dear Sir

## **Financial Reporting Council (Amendment) Bill 2018 (the "Bill")**

We are pleased to have this opportunity to provide our comments on the Bill.

We would like to start by making clear that Deloitte welcomes audit regulatory reform in Hong Kong. The move from self-regulation to independent auditor oversight, including the participation of the Financial Reporting Council (the "FRC") in the International Forum of Independent Audit Regulators ("IFIAR"), is the right thing for Hong Kong. We look forward to working with the FRC in a spirit of constructive engagement to continually enhance audit quality in the interests of the Hong Kong capital market and, therefore, in the Hong Kong public interest.

We have the following specific comments:

- We believe that inspection is the proper instrument for raising the standards of audit quality. We also believe that, in normal circumstances, the inspection process should proceed without the need for recourse to disciplinary action. Adverse inspection findings should be dealt with through articulated remediation plans, the effective implementation of which can be assessed by the FRC through follow up visits or otherwise.
- We do not agree with the provision of criminal offences against a person who fails to comply with the requirements in relation to FRC inspections (referred to Section 21F of Part 2 of the Bill). We understand this is modelled on the existing provisions in the FRC Ordinance concerning failure to comply with requirements in relation to an investigation. An inspection occurs as part of a regular programme, the purpose of which is to test whether the inspected firm is complying with applicable professional standards. An investigation, in contrast, is a "one-off" occurrence triggered by there being evidential grounds for concern about potential audit failure

or auditor misconduct. In an investigation, therefore, the case for non-compliance being a criminal offence is a reasonable one. Given the quite different nature of inspection, however, making non-compliance a criminal offence seems to be disproportionate. Instead, in our view, any person who fails to comply with an FRC inspection request should be dealt with under FRC's regulatory system and disciplinary procedures.

- As regards the description of a public interest entity ("PIE") engagement (referred to Part 1 of Schedule 1A of the Bill), it would make sense for that description to be widened to include all engagements for PIEs so that all PIE engagements can be regulated by the FRC.
- The Bill allows "practitioners" to be members of the FRC Council. In order to ensure that the FRC Council is, and is perceived to be, fully independent of the profession, we would support the FRC Council being comprised wholly of "non-practitioners". It would, however, remain as important as ever that the FRC Council ensures that its members have sufficient relevant and up-to-date professional knowledge and expertise to enable it to exercise its oversight and decision-making responsibilities effectively.
- The Bill constitutes enabling legislation and the FRC will need to issue written implementation guidelines to make the work of the FRC operational (and operationally effective). The publication of such implementation guidelines would provide transparency as to the processes which the FRC is obliged to follow.

We look forward to meeting with the Bills Committee on 20 March 2018.

Yours faithfully

*Deloitte Touche Tohmatsu*