



# **Progress Report** 1 Apr 2019 -31 Mar 2020

Efficient Process, Effective Outcome

May 2020





# Transformation of the FRC

Presented by
Dr Kelvin Wong

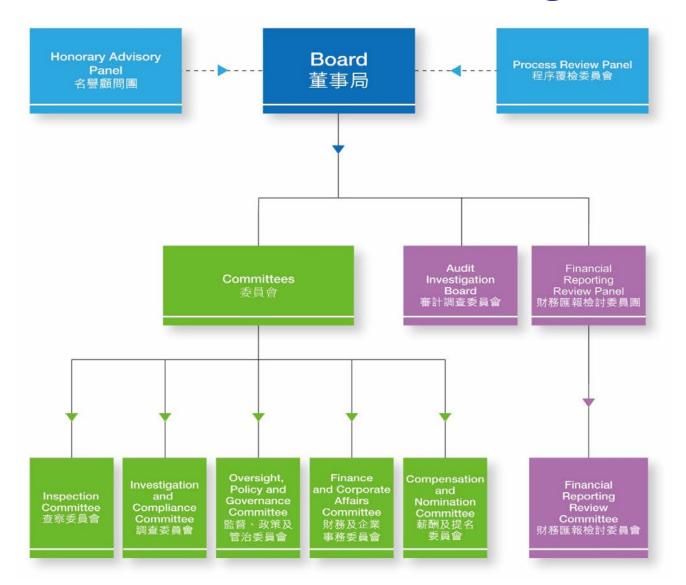
Chairman

# The full-fledged independent oversight body of auditors of listed entities ("PIEs") of Hong Kong

- Inspection
- Investigation and enquiry
- Discipline
- Recognition of overseas auditors
- Oversight of HKICPA's performance on areas in relation to PIE auditors:
  - Registration of local auditors
  - > Setting of standards on professional ethics, auditing and assurance
  - > Setting of continuing professional development requirements



# Governance structure - Oversight





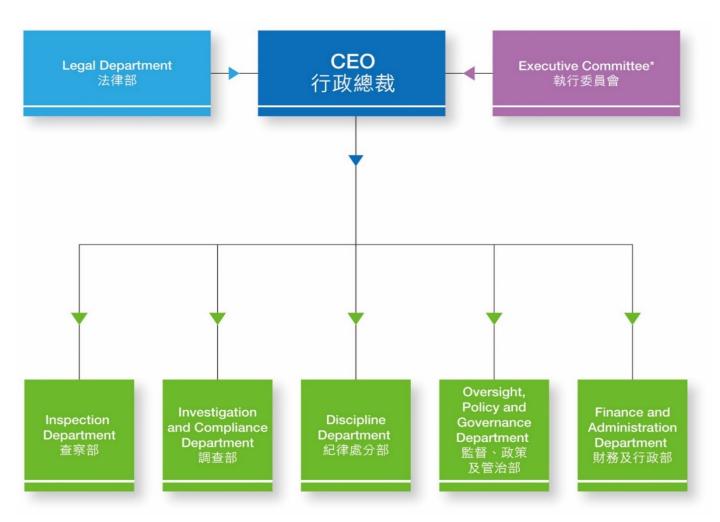
### **Board composition**

- 15 Directors appointed by the Chief Executive
  - The number of non-executive directors (NED) must exceed executive directors (ED)
    - 93% NED, 7% ED
    - Chairman non-executive director
    - 13 other non-executive directors
    - 1 executive director
  - > All are non-practitioners\*
    - 53% (8) non-accounting/audit professionals
      - ❖ 20% (3) legal professionals
      - ❖ 33% (5) bankers/financiers/businessmen
    - 47% (7) accounting/audit professionals

<sup>\*</sup> A non-practitioner – a person who is not, or has not within the previous 3 years been, a CPA (practising); or a partner, director, agent or employee of a practice unit



### Management process



<sup>\*</sup> The Executive Committee comprises CEO, Heads of Departments and General Counsel



# Scaling up the talent pool

Date	Investigation and Compliance	Inspection	Oversight, Policy & Governance	Discipline	Legal	Finance & Administration	Total
1 Apr 2019	17.5#	-	-	-	1	7.5#	26
30 Sep 2019	17.5#	-	-	-	1	6.5#	25
31 Mar 2020	13.5#	8	4	1	2	9.5#	38

<sup>#</sup> One management staff is both Head of Investigation and Compliance and Head of Finance and Administration and therefore the headcount is split between the two departments.

Continue to scale up talent pool across different functions



### Developing policies and procedures

- Developed policies and procedures for statutory functions:
  - > Recognition of overseas auditors
  - > Inspection
  - > Investigation
- Thorough consultations with stakeholders at meetings and briefings
- Published on website on 30 Sep 2019
- Avoid over-regulation or under-regulation to deliver effective regulatory outcome



### **Process Review Panel ("PRP")**

- 6 complaint/investigation/enquiry cases (covering ongoing cases lasted for more than one year and those completed in 2018) were selected for review in the 11<sup>th</sup> review cycle
- 24 April: Concluded all cases had been handled in accordance with internal procedures of the FRC
- FRC to submit new procedure manuals of regulatory functions for review and advice







### Report on Major Work Done

Presented by

Ms Florence Wong

Acting CEO

### Oversight, Policy and Governance

- 27 Sep 2019: Signed a Statement of Protocol on Oversight Arrangements with HKICPA
- 1 Oct 2019 31 Mar 2020: Observed 6 committee meetings of HKICPA
- 1 Oct 2019 31 Mar 2020: Approved 78 recognition applications of non-Hong Kong auditors



# Inspection

- Jan 2020: Approval of inspection manual by the Board
  - > 3-year inspection cycle aligned with international practice
- Jan Feb 2020: 8 individual meetings and 3 group briefings were arranged for PIE auditors to explain inspection scope, process, reporting and arrangements for 2020
- Mar 2020: Discussions with HKEX and SFC on information sharing for better discharge of regulatory duties



# **Investigation and Enquiry**

#### Handling of pursuable complaints

	1 Apr 2019 – 31 Mar 2020
Brought forward	13
Received	52
Completed with no follow-up action	(36)
Referred to specified enforcement agencies	(1)
Initiated investigation and/or enquiry	(5)
Carried forward	23



# **Investigation and Enquiry**

### **Investigation**

	1 Apr 2019 – 31 Mar 2020
Brought forward	45
Initiated*	9
Completed	(11)
Carried forward	43



<sup>\*</sup> The number of cases initiated is dependent on the substance of the underlying issues of complaints and financial statements reviews

# **Investigation and Enquiry**

### **Enquiry**

	1 Apr 2019 – 31 Mar 2020
Brought forward	2
Initiated	1
Completed	(1)
Carried forward	2



# **Discipline**

- Mar Apr 2019: Consultation on proposed sanctions guidelines
- May 2019: Comments considered and sanctions guidelines revised appropriately
- Sep 2019: Sanctions guidelines approved by the Board and published on website and communicated to stakeholders
- Sep 2019: Guidelines for Exercising the Power to Impose a Pecuniary Penalty as required under S37H of the FRCO gazetted



# Connections with local, overseas and Mainland regulators

#### Local

• Regular liaison meetings with SFC (3), HKEX (4) and HKICPA (4)

#### Overseas

 Attended meetings/conferences (6) with overseas regulators, including IFIAR and UK Financial Reporting Council



# Connections with local, overseas and Mainland regulators (cont'd)

#### Mainland

- 22 May 2019: Signed a Memorandum of Understanding with PRC's MoF on gaining access to audit working papers
- 14 Nov 2019, 24 Feb and 25 Mar 2020: Requests for assistance for 11 investigation cases made to MoF
- 15 Jan and 19 Mar 2020: Discussions on future cooperation in inspection and investigation



# Stakeholder engagement and media relation

- Stakeholder engagement:
  - Discussion with SFC, HKEX and the Hong Kong Institute of Directors (HKIoD) on regulatory issues arising from outbreak of COVID-19 including ensuring audit quality and independence
  - ➤ 6 Feb 2020: Published e-news to provide advice to auditors, preparers of financial statements and audit committees
  - > 29 Feb 2020: Being a panelist at HKIoD Webinar



# Stakeholder engagement and media relation (cont'd)

- Revamped website to provide up-to-date information about the FRC and our statutory functions
- Media relations:
  - ➤ 6 interviews with newspapers and official magazines of professional bodies to introduce the new FRC
  - > Responded swiftly to media enquiries
  - > Published press releases, e-newsletters and annual report
  - ➤ 120 positive news clippings/reports (43% up from previous reporting period)







Work Plan (1 Apr 2020 – 31 Mar 2021)

Presented by

Ms Florence Wong

Acting CEO

# To deliver effective regulatory outcomes

#### **Efficient Process Effective Outcome**

### **Inspection**

 Carry out inspection of 18 PIE auditors, covering their firm-wide quality control systems and 40 PIE engagements completed after 1 Oct 2019

### Investigation and enquiry

- Handle complaints, enquiry and investigation cases by following internal policies and procedures, setting targets
- Review how to further enhance efficiency and regulatory outcomes



# To deliver effective regulatory outcomes (cont'd)

#### Oversight of HKICPA

- 1 Apr 31 Dec 2020: Observe 14 committee meetings of HKICPA
- Apr May 2020: On-site assessment of HKICPA
- Aug/Sep 2020: Performance report

#### Recognition of overseas auditors

- Review new applications
- Review renewal applications of 25 overseas auditors whose recognition will expire by end of 2020



# To deliver effective regulatory outcomes (cont'd)

### **Discipline**

- Develop the procedure manual for handling possible misconduct cases
- Research into enforcement practice of other financial regulators
- Expected to finalise in Aug 2020



# To promote good corporate governance

- Conduct in-depth research on audit and financial reporting issues so as to:
  - > Set policies and provide guidance which are conducive to achieving effective regulatory outcome;
  - Add value to the long-term development of the financial industry of Hong Kong



# To strengthen international relations

- Continue strengthening relationship with local, international and Mainland regulators
- Organise a forum on independent auditor oversight at the end of 2020 or beginning of 2021







# Funding Arrangement and Financial Position

Presented by

Ms Florence Wong

Acting CEO

### **Funding arrangement**

- Before 1 Oct 2019: jointly funded by the Companies Registry Trading Fund, HKEX, HKICPA and SFC
- 8 Aug 2019: Seed capital of HK\$400 million from HKSAR Government
- From 1 Jan 2022: funded by levies from
  - > Sellers and buyers of securities transactions (50%)
  - > PIEs (25%)
  - > PIE auditors (25%)



### Financial position

# Income and expenditure

	1 Oct 2019 – 31 Mar 2020 HK\$ (Million)	1 Jan 2019 – 30 Sep 2019 HK\$ (Million)
Grant income Annual contribution Other income	28.11 N/A 5.29	1.08 33.99 2.51
	33.4	37.58
Recurring operating expenditure	(30.02)	(30.75)
Depreciation of capital expenditure for new office and IT infrastructure	(0.79)	(0.0)
Staff recruitment expenses for new functions	(2.59)	(0.0)
Surplus for the period*	0.0	6.83

<sup>\*</sup> As the operations of the FRC during the levy exemption period were financed by the grant income, no surplus or deficit was recorded from 1 Oct 2019 to 31 Mar 2020



# Financial position – Usage of seed capital

	HK\$ (Million)
Seed capital received from the Government on 8 Aug 2019	400
Less:	
- Capital expenditure	13.94
- Staff recruitment and other expenses for new functions	3.67
- Subsidy of net operating expenses during the period of levy exemption (Oct 2019 – Mar 2020)	24.73*
Balance as at 31 Mar 2020	357.66



<sup>\*</sup> Represented recurring operating expenditure of HK\$30.02 million (comprised mainly salaries and bonus of HK\$18.87 million and premises related expenses of HK\$6.2 million) less income of HK\$5.29 million (comprised mainly interest income of HK\$4.6 million)





# Concluding Remarks and Vote of Thanks

Presented by

Dr Kelvin Wong

Chairman

# **Concluding remark**

- Challenging financial and socio-economic outlook ahead
- Committed to upholding quality of financial reporting, enhancing investor protection and strengthening Hong Kong's position as a competitive international financial centre
- Efficient Process, Effective Outcome



#### Vote of thanks

- LegCo members
- FSTB for staunch support over the years
- Funding parties Companies Registry, HKEX, HKICPA, SFC
- Process Review Panel for oversight of our policies and procedures and suggestions for improvement







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