



24 November 2005

BY HAND

Our Ref.: C/PRMC

The Hon. Wong Yan Lung
Secretary for Justice
4th Floor, High Block
Queensway Government Offices
Hong Kong

Dear Mr. Wong,

**Hong Kong Institute of Certified Public Accountants
Proposed Proportionate Liability Framework for Hong Kong**

Firstly, on behalf of the Hong Kong Institute of Certified Public Accountants may I extend our warmest and most sincere congratulations to you on your being appointed Secretary for Justice.

Further to your meeting with the Hon. Mandy Tam on 14 November, I am writing to draw your attention to the accounting profession's urgent need for the government's support in determining policy and introducing legislation on **Proportionate Liability** for practising accountants.

During 2005, we have written a few letters to the Administration and the LegCo Panel on Administration of Justice and Legal Services requesting the introduction of Proportionate Liability in Hong Kong. Our last correspondence with the Administration is my letter dated 22 July 2005 to the Hon. Frederick Ma Si-hang, Secretary for Financial Services and the Treasury, a copy of which is attached for your reference. Please also find attached the Institute's Paper dated 14 March 2005 "A Case for Professional Liability Reform in Hong Kong" which explains the subject further.

I understand from the Hon. Mandy Tam that you have indicated to her that the Institute should now propose its preferred option for Proportionate Liability legislation to the Administration.

Before I discuss the Institute's preferred option for Proportionate Liability, I would like to draw to your attention that the Institute is Hong Kong's only statutory licensing body for accountants. It has more than 25,000 members and close to 10,000 registered students. The Institute operates in the public interest under the Professional Accountants Ordinance. It has the responsibility for regulating and promoting high quality and efficient accounting and auditing standards and practices to safeguard Hong Kong's increasingly important role as an international financial centre.



The Institute has a long history of acting in the public interest. The Institute adamantly believes that Hong Kong's liability framework is no longer in the public interest. Our liability framework has not evolved in step with developments in the economic, financial and increasingly litigious environment in which our members are currently practising. Public interest is not served when our practising members are increasingly reluctant to accept work where the responsibilities and associated risk exposure are considered disproportionate when compared with the rewards. Smaller accounting firms are avoiding accepting work associated with listed entities. This is not good for Hong Kong as the world's largest fund raising centre for Mainland companies as it is forcing fewer listings to materialise because relatively few accounting firms are prepared to offer these services.

With the introduction of Proportionate Liability, public interest will be better served while those supporting the public interest will be treated fairly. Auditors will continue to be responsible for the consequences of their actions and the courts will award appropriate damages against a negligent auditor for that proportion of the loss that reflects the extent of the auditor's responsibility for the damage suffered. Proportionate Liability will mean only that the auditor will not pay for the actions of others who are responsible for any losses but do not have the resources to meet their obligations. It is not economically efficient or fair for a market to operate on the expectation that all financial deficiencies will be compensated by one party. Proportionate Liability provides an equitable solution.

To address the current situation, the Institute is in favour of the approach as that adopted in Bermuda, which legislated on Proportionate Liability by amending their Companies Act. We consider this method to be the least complicated way of introducing Proportionate Liability in Hong Kong and explaining to the public why this is in the public interest. This proposal apportions liability fairly between corporate officers (including auditors) and others.

For the avoidance of doubt, the Institute reiterates that the introduction of Proportionate Liability will need to be supported by the introduction of Limited Liability Partnership (LLP). LLP legislation can proceed independently as it is not directly linked, in a legislative sense, with the introduction of Proportionate Liability. But LLP alone is not sufficient for the accounting profession because LLP does not equitably attribute liability among the relevant responsible parties.

The introduction of Proportionate Liability and LLP would protect Hong Kong as an international financial centre by significantly reducing the increasingly real risk that one of the larger audit firms could collapse as a result of a catastrophic claim, for which the audit firm might have a relatively small share of the responsibility.



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The Institute would welcome an opportunity to meet with you once you have had an opportunity to consider our request. We will be pleased to discuss and clarify any questions you may have on the work of the Institute's liability reform proposals in Hong Kong. If you have any questions, please contact Stephen Chan, our Executive Director, in the first instance at 2287 7026 or schan@hki CPA.org.hk.

I look forward to meeting you.

Yours sincerely,

Edward K.F. Chow
President
Hong Kong Institute of Certified Public Accountants

EC/SSLC/jc
Encl.

c.c. The Hon. Mandy Tam, Member of the LegCo for the Accountancy
Functional Constituency