

**Hong Kong Institute of Certified Public Accountants
Regulatory Framework for Listed Company Audits Membership Consultation**

Key issues under the proposed framework

Features and regulatory functions	Framework proposals		HKICPA preferred outcome
	Responsibility of HKICPA	Responsibility of Independent Oversight Body (IOB)	
Principles and objectives	<p>Hong Kong's auditor oversight regime should be benchmarked against international standards whilst being appropriate in the local context.</p> <p>Secure membership of the International Forum of Independent Audit Regulators (IFIAR) and attain regulatory equivalence status with the European Commission (EC).</p> <p>Introduce an IOB responsible for oversight of auditors of listed companies in respect of six regulatory functions (see below for specific comments on each function).</p>		We agree with the principles and objectives subject to specific comments set out below.
	<p>Key questions to guide our response:</p> <ol style="list-style-type: none"> 1. Are you clear on the objectives of the reform exercise? 2. Do you agree that changes should be made to listed company regulation in Hong Kong to maintain the reputation of the capital market and the auditing profession? 		

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	<p>3. Do you understand that EC equivalence requirements are wider than IFIAR membership criteria and extend the responsibilities of the IOB to oversight of activities not mentioned in IFIAR membership activities (or core principles) – registration, continuing professional development and standard setting?</p> <p>4. Do you think that obtaining EC equivalence should be an objective of the reform exercise?</p>		
Exercise of oversight	<p>The framework addresses each of the six functions and includes separate oversight models for each of the three functions (registration, CPD and standard setting) that the IOB will not carry out directly.</p> <p>The framework includes options for the basis on which HKICPA carries out the three functions: (a) by delegation of powers from the IOB; or (b) by express assignment in law.</p>		<p>We accept that functions carried out by HKICPA will be subject to oversight by the IOB. We believe that the oversight models and the exercise of oversight should be consistent for all three areas.</p> <p>We believe that option (b) is the appropriate basis for HKICPA to carry out these functions.</p>
	<p>Key questions to guide our response:</p> <p>5. Do you understand our explanation that there is a range of ways to exercise oversight and support our argument that oversight should not be constructed such as to give the IOB ownership of registration, continuing professional development and standard setting?</p>		

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Registration	<p>Set and administer registration criteria for Hong Kong auditors of Hong Kong listed companies (no change to criteria as currently established by the PAO).</p> <p>Maintain the register of all auditors of Hong Kong listed companies (Hong Kong, Mainland and other non-Hong Kong) and specified individuals.</p> <p>HKICPA has the authority to carry out this function by either:</p> <p>(a) Direct assignment in law; or</p> <p>(b) Delegation from the IOB.</p>	<p>Set and administer recognition criteria for other (not Mainland) non-Hong Kong auditors.</p> <p><u>Oversight</u> of HKICPA activities in respect of registration criteria for Hong Kong auditors of Hong Kong listed companies and maintenance of the register of all auditors of Hong Kong listed companies.</p>	<p>We agree with the framework proposal.</p> <p>Authority should be by direct assignment.</p>

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	<p>Key questions to guide our response:</p> <p>6. Do you believe the IOB should have the explicit power to refuse renewal of registration of a firm on grounds other than those set out in the registration criteria in addition to general reserved powers?</p> <p>7. Do you agree that "fit and proper" criteria that have to be met for registration of firms and individuals should be the same as currently used for HKICPA membership and should not be used to introduce additional competency criteria?</p>		
Inspection	May directly inspect Hong Kong auditors of Hong Kong listed companies (systems of quality control and audit engagements) under delegation and direction by the IOB.	Directly inspect Hong Kong auditors of Hong Kong listed companies (systems of quality control and audit engagements).	We agree with the framework proposal.
Investigation	No powers to investigate complaints concerning audits of listed companies.	Powers to investigate complaints concerning audits of listed companies exist in	No change from the current situation.

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		the FRCO. Will continue to be an activity exclusive to the FRC.	
Enforcement/discipline	No remit for taking disciplinary action against Hong Kong listed company auditors.	<p>Responsible for taking disciplinary action against Hong Kong listed company auditors arising from inspection and investigation activities.</p> <p>Three options for a disciplinary mechanism:</p> <p>(a) Direct decision making and sanctioning by the IOB subject to appeal to an independent tribunal;</p> <p>(b) Cases arising from inspection or investigation sent to a fully independent disciplinary committee for decision</p>	<p>We agree in principle with the framework proposal. The IOB will need to have the ability to take effective action to address misconduct.</p> <p>We support option (b). Those responsible for investigation and inspection should not also be responsible for sanctioning.</p> <p>We have also proposed a fourth option allowing a matter to be resolved by the IOB offering, and the auditor accepting a sanction. If the auditor declines the offer the case should be taken to an independent disciplinary committee.</p>

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		<p>and sanctioning; or</p> <p>(c) Cases arising from inspection or investigation sent to a disciplinary committee chaired by a senior executive of the IOB with independent members for decision and sanctioning.</p> <p>The range of sanctions available includes reprimand, suspension or withdrawal of registration and monetary penalties. Monetary penalties will be capped at the greater of \$10,000,000 or three times the profit made or loss avoided in carrying out the audit.</p>	<p>We agree with the proposed range of sanctions with the exception of monetary penalties. They are a punitive measure rather than remedial or for public protection. The reputational damage, and potential civil action, following any regulatory sanction will far exceed the pain of a fine. If monetary penalties are included in the final framework we believe that three times profit or loss is not an appropriate measure and that \$10,000,000 is excessive.</p>

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	<p>Key questions to guide our response:</p> <p>8. Do you agree with our view that there should be a clear separation of responsibility between inspection and investigation and subsequent disciplinary action?</p> <p>9. Which of the three options for the structure of enforcement/disciplinary proceedings that are included in the draft framework do you support?</p> <p>10. Do you agree with our proposal of a "fourth option" which allows for disciplinary action to be concluded, with the consent of both parties, without proceeding to a formal disciplinary hearing?</p> <p>11. Do you agree with our position that in principle monetary fines are not necessary as a punitive measure if the IOB has the power to suspend or withdraw registration which have additional potentially serious consequences of reputational damage and civil action?</p> <p>12. If monetary penalties are included in sanctions available to the IOB do you agree that determining the level of penalty by a multiple of profit is inappropriate and that all penalties should be proportionate and determined by a range of factors including a firm's financial resources?</p> <p>13. What do you consider would be a reasonable amount for a cap to the level of monetary penalties?</p>		
Continuing professional development (CPD)	Set CPD requirements for all members, including listed company auditors, and	<u>Oversight</u> of HKICPA activities.	We agree with the framework proposal.

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	<p>monitor compliance.</p> <p>HKICPA has the authority to carry out this function by either:</p> <p>(a) Direct assignment in law; or</p> <p>(b) Delegation from the IOB.</p>		<p>Authority should be by direct assignment.</p>
Standard setting	<p>Set auditing standards and code of ethics in accordance with existing due process.</p> <p>HKICPA has the authority to carry out this function by either:</p> <p>(a) Direct assignment in law; or</p> <p>(b) Delegation from the IOB.</p>	<p><u>Oversight</u> of HKICPA activities.</p> <p>The framework is open about whether standards set by HKICPA would only become effective after endorsement by the IOB.</p>	<p>We agree with the framework proposal.</p> <p>There should not be a requirement for standards to be endorsed by the IOB.</p> <p>Authority should be by direct assignment.</p>

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	<p>Key questions to guide our response:</p> <p>14. Do you agree that endorsement of standards by the IOB goes beyond the requirements of oversight and believe that our arguments support our stance that it should not be included in the new system?</p> <p>15. Do you believe the framework should include any reference to the right of the IOB (and the HKICPA) to participate in international standard setting forum?</p>		