

Speaker : Raphael Ding (Chief Executive and Registrar)
Organization : Hong Kong Institute of CPAs
Event : Members' forum

Regulatory Framework for Listed Company Audits

Information Paper and
Request for Comment



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Regulatory Framework for Listed Company Audits

- Regulation of listed company auditors is important
- It is part of the overall system of regulation of the Hong Kong capital market
- Existing responsibility for auditor regulation rests primarily with the Hong Kong Institute of CPAs
- Internationally, over the last ten years there has been a trend of establishing independent auditor regulatory and oversight bodies



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Regulatory Framework for Listed Company Audits

- International Forum of Independent Audit Regulators (IFIAR) was established in 2006
- IFIAR's membership criteria accepts regulatory bodies that have:
 - Responsibility for oversight of inspection of audits of public interest entities; and
 - Funding and governance independent from the audit profession
- IFIAR's international influence increases along with its growth of membership
- Hong Kong needs to become a member of IFIAR



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- Without an independent oversight body Hong Kong can't gain recognition as an equivalent regulatory system by European Commission
- As a result Hong Kong audit firms with clients listed on EU exchanges have to register with and may be subject to direct inspection by EU regulators
- The direct impact will be felt by only a few firms but there will be a reputational effect on the Hong Kong capital market and audit profession
- Relevant jurisdictions that are recognised as equivalent by the EC include China, Singapore and Australia



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- HKICPA took an early lead in identifying necessary reform by research and outreach activities in 2008 and 2009
- In early 2010 a committee and a working group were set up to develop proposals for reform
- An initial proposal was submitted to the HKSAR Government at the end of 2011
- In early 2012 a joint proposal and timeline was developed with the Government and the Financial Reporting Council



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- The overall aim of reform is to establish an independent oversight body so that the regulatory system of listed company auditors in Hong Kong meets IFIAR membership requirements and is recognized by EU (*p.1*)
- We need to be in line with international development and cater to Hong Kong situation
- HKICPA, the Government and the FRC have been involved in extensive dialogue to develop a proposed draft framework



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Regulatory Framework for Listed Company Audits

- The Government will conduct a public consultation subsequent to HKICPA's member consultation
- The framework addresses the objectives of the reform exercise and six recognized elements of auditor regulation



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Oversight (p.2)

- Six elements of regulation are registration, inspection, investigation, discipline, continuing professional development and standard setting
- Any of the activities not carried out directly by the independent body may be carried out by HKICPA and subject to oversight by the independent body
- We prefer that any activities carried out by HKICPA are directly assigned by law



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Oversight (cont'd)

- The independent body will have reserved powers to direct the HKICPA to take certain action if HKICPA fails to act in public interest
- The proposed oversight arrangements for the three areas of work to be undertaken directly by HKICPA are not the same



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	IFIAR (Public Interest Entities)	EC (oversight) (Listed companies)
Registration		✓
Inspection	✓ (membership criteria)	✓
Investigation		✓
Discipline	✓ (core principles)	✓
CPD		✓
Standard Setting		✓



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Regulatory Framework for Listed Company Audits

1. Registration (p. 3-4)

- HKICPA to remain responsible for registration of members and member firms
- Also to maintain a separate register of firms that audit listed companies and specified individuals in those firms
- These include Mainland and non-Hong Kong auditors who are allowed to audit Hong Kong listed companies
- The new system must ensure effective regulation of these auditors



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1. Registration (cont'd)

- The proposals include provisions for the independent body to direct HKICPA to refuse a first time application or renewal of registration on grounds other than specified registration criteria
- Including "fit and proper" in registration criteria should not be used by the independent body to introduce additional competence requirements.



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2. Inspection (p.4)

- The independent body will take over responsibility for inspection of audits of listed companies and quality control systems of listed company auditors
- It may delegate any of its inspection responsibilities to the HKICPA
- HKICPA continues to be responsible for inspection of audits of non-listed companies



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3. Investigation (p.4)

- Power to investigate listed company auditors was moved from the HKICPA and taken up by the FRC on its formation in 2006



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4. Discipline and sanctions (p. 5-7)

- The proposed framework contains three options for disciplinary proceedings against listed company auditors:
 - a) Decision made internally by the independent body, subject to appeal
 - b) Referral to an independent disciplinary committee
 - c) Referral to a disciplinary committee with independent members but chaired and convened by a senior executive of the independent body
- HKICPA supports option b).



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4. Discipline and sanctions (cont'd)

- HKICPA has proposed a "4th option" that would allow resolution of cases by the independent body offering a sanction
- If the audit firm declines to accept the offered sanction the case would go to an independent disciplinary committee



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4. Discipline and sanctions (cont'd)

- The independent body will need to have sanctions available that allow it to take timely and proportionate action to address poor quality audit work
- Notwithstanding the need to ensure an effective and efficient disciplinary mechanism the fundamental principle of natural justice and fairness must always guide its development



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4. Discipline and sanctions (cont'd)

- Unresolved cases should be heard before a fully independent disciplinary committee or tribunal that should strictly abide by the following principles:
 - No sanction should be exercised without due process
 - There should be absolute transparency of process
 - Those responsible for the inspection or investigation of the matter should not be part of the independent disciplinary committee or tribunal



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4. Discipline and sanctions (cont'd)

- Range of sanctions proposed is similar to those available to audit regulators in other jurisdictions
- Clear guidance should be developed on sanctioning procedures
- Financial penalty, particularly one based upon a multiple of profit or loss in an audit engagement, would not be appropriate



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4. Discipline and sanctions (cont'd)

- Where a fine is to be imposed, it should be proportionate in relation to audit failing and should take into such factors as financial resources of auditor, previous record and admission of failing and there should be a cap
- If a party to a review is dissatisfied with the determination of the review, it should have the unrestricted right to appeal to the Court of Appeal



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5. Standard setting (p. 8-9)

- Setting auditing standards should remain the responsibility of HKICPA
- The HKICPA has the experience, skills, resources and international contacts necessary to carry out this function and a very good track record of introducing high quality auditing standards



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5. Standard setting (cont'd)

- The exercise of oversight should be no different from that on the areas of registration and continuing professional development
- There is no need for standards to be endorsed by the independent body before introduction



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6. Continuing professional development

(p. 7-8)

- HKICPA will continue to mandate CPD requirements for its members and monitor compliance, subject to oversight by the independent body



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Funding

- HKICPA supports that funding should primarily come from listed companies and investors
- A registration fee should be charged to listed company auditors to cover administration costs of maintaining the register



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Regulatory framework for listed company audits

- Letter to members 
- Information paper and request for comment 
- Draft proposed framework 

Members' forums

- 18 October 2013 
- 28 October 2013 
- 20 November 2013 
- 27 November 2013 

Media interview

- Chief Executive at Metro Radio  (15 October 2013)

Press briefing (8 October 2013)

- Press release 
- Photos 



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