CONSULTATION CONCLUSIONS

ON ACCEPTANCE OF MAINLAND ACCOUNTING AND AUDITING STANDARDS AND MAINLAND AUDIT FIRMS FOR MAINLAND INCORPORATED COMPANIES LISTED IN HONG KONG

December 2010

Hong Kong Exchanges and Clearing Limited
香港交易及結算所有限公司

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Summary of Abbreviations used

CASBE	China Accounting Standards for Business Enterprises
CIRC	China Insurance Regulatory Commission
CSQC5101	China Standards on Quality Control
CSRC	China Securities Regulatory Commission
Exchange	The Stock Exchange of Hong Kong Limited
FRC	Financial Reporting Council
GEM	Growth Enterprise Market
HKEx	Hong Kong Exchanges and Clearing Limited
HKFRS	Hong Kong Financial Reporting Standards
HKICPA	Hong Kong Institute of Certified Public Accountants
HKSA	Hong Kong Standards on Auditing
HKSQC1	Hong Kong Standards on Quality Control
IFRS	International Financial Reporting Standards
ISA	International Standards on Auditing
MOU	Memorandum of Understanding
MOF	Ministry of Finance
Rules	Main Board Listing Rules and GEM Listing Rules
SFC	Securities and Futures Commission

EXECUTIVE SUMMARY

1. This paper presents the results of the public consultation on our proposals to accept Mainland accounting and auditing standards and Mainland audit firms for Mainland incorporated companies listed in Hong Kong.

2. An overwhelming majority of the respondents supported our proposals. They agreed that the proposed framework should be introduced as Mainland accounting and auditing standards are substantially converged with Hong Kong accounting and auditing standards and the proposed framework will reduce compliance costs for Mainland incorporated issuers and increase efficiency in preparing financial statements.

3. Having considered the responses, we have decided to implement the proposals as set out in the Consultation Paper, which are:-

   (a) to allow Mainland incorporated Main Board and Growth Enterprise Market ("GEM") issuers to prepare their financial statements using Mainland accounting standards;

   (b) to allow Mainland audit firms approved by the Ministry of Finance ("MOF") of China and the China Securities Regulatory Commission ("CSRC") to service these issuers using Mainland auditing standards; and

   (c) to provide for a reciprocal arrangement to allow companies incorporated or registered in Hong Kong and listed in the Mainland to prepare their financial statements using Hong Kong Financial Reporting Standards ("HKFRS") / International Financial Reporting Standards ("IFRS") and audited by Hong Kong audit firms registered with the Hong Kong Institute of Certified Public Accountants ("HKICPA") using Hong Kong Standards on Auditing ("HKSA") or International Standards on Auditing ("ISA").

4. We have finalized the Rule amendments to implement the proposals. They have been approved by the Board of The Stock Exchange of Hong Kong Limited ("the Exchange") and the Securities and Futures Commission ("SFC"), and come into effect on 15 December 2010.

CHAPTER 1 INTRODUCTION

5. On 28 August 2009, the Exchange, a wholly-owned subsidiary of the Hong Kong Exchanges and Clearing Limited ("HKEx"), published a Consultation Paper on Acceptance of Mainland Accounting and Auditing Standards and Mainland Audit Firms for Mainland Incorporated Companies Listed in Hong Kong. The Consultation Paper sought views and comments on proposals to accept financial statements prepared under Mainland accounting standards and audited by Mainland auditors using Mainland auditing standards for Mainland incorporated companies listed in Hong Kong.

6. The consultation period ended on 23 October 2009. We received a total of thirty submissions from listed issuers, professional and industry associations, market practitioners and individuals. A list of respondents is provided at **Appendix 1** and the respondents are grouped into broad categories as follows:-

Category	Number of respondents
Main Board issuers	13
A+H share companies	*9*
H share companies	*3*
Others	*1*
GEM issuers	1
Professional and trade associations	6
Market practitioners	6
Retail investors	4
	30

7. The full text of all the submissions is available on the HKEx website at: http://www.hkex.com.hk/eng/newsconsul/mktconsul/responses/cp200908r.htm.

8. Of the thirty respondents, a majority expressed general support to our proposals. Chapter 2 summarises the major comments made by the respondents as well as our responses to these comments and our conclusions. This paper should be read in conjunction with the Consultation Paper, a copy of which is posted on the HKEx website at: http://www.hkex.com.hk/eng/newsconsul/mktconsul/documents/cp200908_e.pdf.

9. We have finalised the Rule amendments to implement the proposals which are available on the HKEx website at: http://www.hkex.com.hk/eng/rulesreg/listrules/mbrulesup/mb_ruleupdate.htm and at: http://www.hkex.com.hk/eng/rulesreg/listrules/gemrulesup/gemrule_update.htm. They have been approved by the Board of the Exchange and the SFC, and come into effect on 15 December 2010. For further details see paragraphs 71 and 72 below.

10. We would like to thank all those who shared their views with us during the consultation process.

CHAPTER 2 MARKET FEEDBACK AND CONCLUSIONS

11. We set out below the proposals, major comments made by the respondents as well as our responses to these comments and our conclusions on how we will proceed with the proposals.

Framework for Acceptance of Mainland Accounting and Auditing Standards and Mainland Audit Firms

12. We proposed a framework to provide Mainland incorporated companies listed in Hong Kong with a choice to prepare their financial statements using China Accounting Standards for Business Enterprises ("CASBE") and audited with Mainland auditing standards, and to accept Mainland audit firms approved by MOF and CSRC to act as auditors and reporting accountants of Mainland incorporated companies listed in Hong Kong. The framework also provides for a reciprocal arrangement to allow companies incorporated or registered in Hong Kong and listed in the Mainland to prepare their financial statements using HKFRS/IFRS and audited by Hong Kong audit firms registered with the HKICPA using HKSA or ISA. We set out below the major comments made by the respondents.

Overall response

13. Out of the thirty submissions received, twenty-four supported the proposal. One submission also provided the views and comments from the board secretaries of 14 Mainland companies. The supporting respondents provided the following reasons for their views:-

- Mainland accounting and auditing standards are substantially converged with Hong Kong and international standards and it is appropriate to accept Mainland accounting and auditing standards and Mainland audit firms.
- Consistent with the direction of global convergence.
- Reduce the cost of preparing financial statements and hence increase cost effectiveness.
- Encourage more timely disclosure of financial information to the market.
- Provide flexibility in the choice of auditors and reporting accountants.
- Create new opportunities for auditing and accounting professions in Hong Kong and the Mainland.
- Encourage more Mainland company listings in Hong Kong.

14. Five respondents disagreed with the proposed framework and their concerns included:-

- Mainland accounting standards are not fully converged with the HKFRS/IFRS.
- Hong Kong investors do not have a clear understanding of the regulatory regime over Mainland audit firms and this may have an impact on investors' confidence and the quality of the capital market in Hong Kong.
- Reduced regulatory power of Hong Kong regulators.
- The proposed framework will adversely affect the accounting profession in Hong Kong.

15. Respondents who supported the proposal also raised questions relating to:-

- On-going convergence of Mainland accounting standards with the Hong Kong and international standards and Hong Kong investors may not be familiar with CASBE
- Overall equivalence of practice review systems in Hong Kong and the Mainland
- Qualification requirements for Mainland audit firms to service Hong Kong listed companies
- Compliance with standards issued by the HKICPA in relation to investment circulars by Mainland audit firms
- Reciprocal arrangements
- Disclosures in the financial statements of the transition to CASBE
- Costs incurred by Hong Kong regulators and cost reduction effect of listed issuers
- Publicity of details of Hong Kong and Mainland regulatory systems over audit firms
- Sponsors' reliance on information provided by Mainland audit firms
- Comments on Rule amendments

16. One submission from a professional body presented the views based on a survey of its members. Of the hundred members of this professional body who completed the survey half of them supported the proposed framework and half did not.

17. We agree with the reasons provided by the supporting respondents and our responses to the concerns and questions received from respondents referred in paragraphs 14 and 15 are addressed below.

Convergence and continued convergence between Mainland accounting standards and Hong Kong and international standards

Comments received

18. Some respondents emphasized that there must be a mechanism to ensure the on-going convergence of Mainland accounting standards with HKFRS/IFRS as convergence was a basic condition on which the framework was developed. Any difference between the Mainland accounting standards and HKFRS/IFRS would make financial statements less comparable. One respondent pointed out that there were differences in the treatment of intangible assets, the treatment of a number of notes to the accounts and the recognition of financial instruments but did not give any examples of these differences.

Our response

19. We agree with the observation that there should be a mechanism to ensure on-going convergence and that mechanism has been put into place. The HKICPA and the China Accounting Standards Committee signed a Joint Declaration on 6 December 2007 which is available on the HKICPA's website at http://www.hkicpa.org.hk/en/standards-and-regulations/technical-resources/mainland-standards-convergence/financial-reporting-standards/. The Joint Declaration declared that there was substantial convergence between CASBE and HKFRS and included details of a mechanism for ensuring on-going convergence of CASBE and HKFRS. This mechanism has been in operation since December 2007 and regular meetings (at least twice yearly) are held by HKICPA, MOF and the International Accounting Standards Board on on-going convergence of CASBE and HKFRS/IFRS.

20. The Joint Declaration identified two remaining accounting differences at the time the declaration was signed. They related to the accounting standard on "related parties" and reversal of "impairment charges". In November 2009, a revised International Accounting Standard 24 "Related Party Disclosures" was released to remove the "related party" difference. On the latter issue, we understand that the Mainland accounting rules which disallow reversal of impairment charges are primarily applicable to property, plant and equipment and believe that such reversals should be rare. We believe the Mainland rules are in substance more prudent and are directed at preventing the manipulation of profits. We consider that although the CASBE rule on reversal of impairment charges is more restrictive, it is still consistent with HKFRS/IFRS.

21. The Joint Declaration did not indicate that there were differences in the treatment of intangible assets and the recognition of financial instruments. In the preparation of the financial statements of issuers that are listed in both the Mainland and Hong Kong, the accounting policies adopted on measurement and recognition of assets and liabilities should be the same given that such companies are managed by the same board and management. In respect of the fair value of intangible assets, we note that CASBE 6 “Intangible Assets” allows the cost model only while Hong Kong Accounting Standard 38/International Accounting Standard 38 “Intangible Assets” allows the cost model and as an alternative the revaluation model, where fair value can be determined by reference to a price quoted in an active market. We believe that an active market for intangibles and use of the revaluation model should be rare. Again, although the CASBE rule on measurement of intangible assets is more restrictive, we consider that it is still consistent with HKFRS/IFRS. In respect of recognition of financial instruments, no significant difference in this area between CASBE and HKFRS/IFRS was noted. In addition, financial statements should include disclosures of material and relevant information to meet the overall objective of providing a true and fair view of the issuer’s results and financial position.

22. Based on the Joint Declaration and subsequent developments since the declaration was signed, we believe that CASBE is substantially converged with HKFRS/IFRS and there will be continued convergence. The difference concerning reversal of impairment charges is not a significant difference. We appreciate that Hong Kong investors who choose to read CASBE statements may have initial concerns in familiarizing themselves with Mainland accounting standards which are normally in Chinese. However, there are English translations available and familiarity will develop over time. As required under the Rules, investors may elect to receive an English version of annual reports which should clearly describe the principal accounting policies adopted.

<u>Hong Kong investors do not have a clear understanding of the regulatory regime over Mainland audit firms and this may have an impact on investors’ confidence and the quality of the capital market in Hong Kong</u>

Comments received

23. Some respondents were concerned that Mainland audit firms lack the necessary knowledge and experience of Hong Kong rules and regulations and the quality of audits performed by Mainland audit firms may not be guaranteed. Some suggested that it is important to ensure that the proposed framework will not lead to a decline in financial reporting in Hong Kong which may downgrade the position of Hong Kong as an international financial centre.

Our response

24. Issuers have the primary responsibility to produce accurate financial information and independent external auditors act as an additional safeguard. Investors in making investment decisions should consider the risks they wish to accept and whether they are confident with the issuers' management as well as the degree of reliance they place on external auditors.

25. We explained in paragraph 71 of the Consultation Paper that Mainland auditors are required to comply with China Standards on Quality Control ("CSQC5101") which requires them to be knowledgeable of any relevant local rules, regulations and practices concerning their clients. Moreover, Mainland auditors are governed by the Law of the People's Republic of China on Certified Public Accountants and are subject to a system of practice review by the MOF and the China Institute of Certified Public Accountants to monitor and ensure audit quality. We concluded from the findings of the practice review comparison exercise conducted for HKEx by the HKICPA that the practice review systems in Hong Kong and the Mainland are similar (see paragraph 37 below).

26. In addition, the memoranda of understanding and co-operation agreements between the Hong Kong and Mainland regulators will enable efficient and effective monitoring and investigation of Mainland audit firms. With these safeguards, we believe that investors' confidence and the quality of capital market in Hong Kong would be maintained.

<u>Reduced regulatory power of Hong Kong regulators</u>

Comments received

27. Some respondents were concerned that the regulation of Mainland audit firms relies heavily on Mainland regulators and they felt that Hong Kong regulators did not possess adequate monitoring and oversight power.

28. A respondent suggested that Hong Kong regulators should adopt a similar system to that established in the United States, namely, the creation of an independent regulatory body such as The Public Company Accounting Oversight Board. Some respondents were unclear as to how liquidators or shareholders could pursue actions against Mainland audit firms and how preparers of financial information will be regulated. One respondent also commented that extreme sanctions such as removal of the license of an audit firm should only be exercised as a final and extreme option.

Our response

29. The framework was developed on the basis of the existing legislation and on the basis that there would be no change in legislation including the establishment of additional regulatory bodies. We believe the memoranda of understanding and co-operation agreements between Hong Kong and Mainland regulators will enable efficient and effective monitoring and investigation of Mainland audit firms by the regulators best positioned to do so.

30. The framework does not change the rights of investors as a body and liquidators to take legal actions against the company, its directors and its auditors.

31. In relation to preparers of financial information, i.e. issuers, there is no change in their position. The same rules and regulations currently available to take legal actions against issuers remain. Preparers of financial information are required to comply with the Rules and relevant accounting standards. The Financial Reporting Council ("FRC") was established to effectively regulate this area and the Exchange and the FRC have a memorandum of understanding in place for co-operation and cross-referrals. In addition to implement the proposals, the FRC has signed a new separate memorandum of understanding with the Mainland regulators.

32. If an issuer fails to produce financial statements as required under the Rules, the Exchange is able to suspend the share trading of the issuer and ultimately, if appropriate, to delist the issuer.

33. As discussed in paragraphs 80 to 82 of the Consultation Paper, any suspicion of possible misconduct by Mainland audit firms may be reported to the FRC who may seek assistance, as appropriate, from MOF to expeditiously investigate the matter.

<u>Impact on the accounting profession in Hong Kong</u>

Comments received

34. Some respondents raised concerns over the future employment of accountants or auditors in Hong Kong.

Our response

35. We accept that there would be an impact on the future employment of Hong Kong accounting firms but we believe that the choice of audit firms is a commercial matter to be decided between the listed issuer and the audit firm. The reciprocal arrangement to allow companies incorporated or registered in Hong Kong and listed in the Mainland to prepare their financial statements using HKFRS/IFRS and audited by Hong Kong audit firms registered with the HKICPA using HKSA or ISA should alleviate these concerns. The reciprocal arrangement would provide Hong Kong audit firms and accountants with possible business and employment opportunities in the Mainland and we note that some respondents indicated that this will likely happen as they move to place more focus on the Mainland market.

<u>Overall equivalence of practice review systems in Hong Kong and the Mainland</u>

Comments received

36. Certain respondents were concerned that at the time the Consultation Paper was released the HKICPA had not yet completed its comparison exercise and queried whether the Mainland's quality assurance and practice review system is similar to that in Hong Kong.

Our response

37. In late October 2009, the HKICPA completed the comparison exercise of the Hong Kong and Mainland practice review systems and provided its findings to the Exchange. The Hong Kong regulators, including the FRC, SFC, HKICPA, Financial Services and the Treasury Bureau and the Exchange have reviewed HKICPA's findings. The Exchange believes that although the two systems are not identical there are no substantive differences between the practice review systems in Hong Kong and the Mainland. We believe the Hong Kong system is more timely and efficient whereas the Mainland system is more thorough as the Mainland regulators take more time to complete their practice reviews and carry out surprise visits of audit firms and their work also involves re-performance of audit tests undertaken by the audit firms. Findings of HKICPA's comparison exercise are provided at **Appendix 2**.

<u>Qualification requirements for Mainland audit firms to service Hong Kong listed companies</u>

Comments received

38. Some respondents felt that the qualification requirements for Mainland audit firms should be made more transparent to enhance investors' confidence. Some suggested that qualification requirements should include considerations such as a minimum number of certified public accountants employed by the audit firm, experience in auditing listed companies and "H-share" companies and history of any disciplinary action against the audit firm. One respondent questioned whether Mainland audit firms should have a minimum professional indemnity insurance coverage and whether Hong Kong audit firms would be required to create a "professional risk fund" and make contributions to the fund, as required by the MOF for Mainland audit firms.

Our response

39. The qualification requirements suggested by respondents have already been considered by MOF and CSRC. MOF and CSRC intend to restrict Mainland audit firms that will be approved to service Hong Kong listed companies to the larger practices and in September 2009 it consulted 58 Mainland audit firms. Full details of the qualification requirements will also be available when a Mainland audit firm applies for registration with the MOF and CSRC.

40. HKICPA has no separate licensing regime for auditors eligible to service listed companies and does not propose to introduce any new requirements for auditors of Hong Kong companies seeking to list in the Mainland. The qualification criteria required by the HKICPA are available on its website and can be obtained when an audit firm applies for registration with the HKICPA.

41. The framework was developed based on mutual recognition. Audit firms only need to comply with the professional indemnity insurance and/or professional risk fund requirements imposed by their home registration jurisdiction.

42. We understand that in the Mainland the MOF requires that the sum of the accumulated professional indemnity insurance coverage and the accumulated "professional risk fund" of a Mainland audit firm that services listed companies should not be less than RMB6 million. The professional risk fund is determined at 5% of the practice's annual fee income from auditing services.

43. The HKICPA, under its statement No.1.103 "Corporate Practices (Professional Indemnity) Rules", has requirements for corporate practices. Such practices are required to have minimum professional indemnity insurance coverage of at least HK$5 million but this increases depending on the practice's fee income and the number of partners.

<u>Compliance with standards issued by HKICPA in relation to investment circulars by Mainland audit firms</u>

Comments received

44. A respondent questioned whether Mainland auditors would be required to comply with two specific HKICPA standards in relation to investment circulars, namely, Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" and Auditing Guideline 3.341 "Accountants' Report on Profit Forecasts".

Our response

45. Under the existing Rules, compliance with Auditing Guideline 3.340 "Prospectuses and the Reporting Accountant" has been retained under Main Board Rule 4.08(3) and GEM Rule 7.08(3). Auditing Guideline 3.341 "Accountants' Report on Profit Forecasts" deals with profit forecasts which are not mandatory. Moreover, China Standards on Quality Control ("CSQC5101") which is similar to Hong Kong Standards on Quality Control ("HKSQC1") requires that audit firms should be knowledgeable of any relevant local rules, regulations and practices concerning their clients. Breach of these standards may result in disciplinary actions taken by the relevant audit firm licensing body.

46. In addition, the Exchange has the power to reject documents. It pre-vets listed companies' / listing applicants' documents prior to their release (e.g. prospectuses) and has the power to reject documents that are not prepared properly.

Reciprocal arrangements

Comments received

47. A respondent suggested that Mainland regulators accept certain international audit firms who have affiliated firms registered with HKICPA and accepted by the Exchange on a case-by-case basis under Main Board Rule 19.20(2) for the purpose of their Hong Kong and Mainland listings, so that these audit firms need not be subject to further levels of audit and regulatory supervision for the purpose of their Mainland listing clients. Another respondent suggested that Mainland regulators should recognize audit firms registered with the equivalent bodies to HKICPA within the United Kingdom and the United States. Another respondent suggested that Mainland regulators should allow Hong Kong accountants to provide Mainland accounting, taxation and valuation services. A respondent also requested clarification of whether the reciprocal arrangements would apply to companies registered under Part XI of the Companies Ordinance.

Our response

48. We believe extending the services that may be provided by Hong Kong accounting firms beyond auditing and assurance services are decisions that can only be made by the Mainland regulatory authorities. The framework deals with reciprocal arrangements on auditing and assurance services only and the scope of the reciprocal arrangements on audit firms that may service relevant Hong Kong sourced Mainland listings are restricted to audit firms registered with HKICPA.

49. We would also clarify that the reciprocal arrangements apply to Mainland listings of companies incorporated or registered in Hong Kong. The reference to "registered in Hong Kong" covers non-Hong Kong incorporated companies registered under Part XI of the Companies Ordinance.

Disclosures in the financial statements of the transition to CASBE

Comments received

50. Certain respondents suggested that there should be specific disclosure requirements on the transition from one set of accounting standards to another and a reconciliation statement should be included in financial statements to reconcile the net profit or loss under CASBE to the figure under HKFRS/IFRS. Another respondent commented that once a listed issuer decides to change and prepare its financial statements under CASBE, the issuer should not be permitted to change back and if there is any change, reasons should be disclosed in the annual report.

Our response

51. We believe we addressed these issues in paragraph 47 of the Consultation Paper. An issuer who decides to change and prepare its financial statements under CASBE should release an announcement on the change and explain the reasons and show the financial impact, if any, of the change. We agree that an issuer should not normally change back once it decides to change to CASBE. Listed issuers should decide which set of accounting standards is most suitable to them and adopt that set of accounting standards continuously. There should not normally be any significant impact on the issuers' results or financial position on the adoption of CASBE.

<u>Costs incurred by Hong Kong regulators and cost reduction effect of listed issuers</u>

Comments received

52. A few respondents considered that costs incurred by regulatory authorities would increase and were concerned that these costs may be passed to listed issuers. One respondent commented that the cost savings expected may not be significant as A+H share companies would still have to produce and print two sets of annual reports for the Mainland and Hong Kong.

Our response

53. Although regulatory authorities would incur some additional costs to implement the framework, the cost will be borne by the Hong Kong regulators and not listed issuers.

54. We believe that printing costs would be significantly reduced as well as accounting and auditing costs. This view was also given by some respondents who supported the proposed framework. To reduce printing costs "A+H share" issuers that choose to adopt CASBE may consider printing one report rather than two separate annual reports so long as they comply with all the regulatory disclosure requirements in Hong Kong and the Mainland.

<u>Publicity of details of Hong Kong and Mainland regulatory systems over audit firms</u>

Comments received

55. One respondent suggested that a detailed analysis should be made public on (a) acceptance criteria for endorsing audit firms; (b) practice review systems; (c) investigation procedures; (d) extent of information sharing; and (e) sanction structures of both markets.

Our response

56. We understand that some aspects of these areas are currently available on the websites of relevant regulatory bodies in Hong Kong. The HKICPA has certain aspects of point (a), (b), (c) and (e) available on its website. The FRC also has some aspects of (c) and (d) on its website.

57. The extent of details regarding the regulation of audit firms made publicly available depends on that permitted by law and the decisions of the relevant regulatory bodies.

<u>Sponsors' reliance on information provided by Mainland audit firms</u>

Comments received

58. A respondent commented that sponsors may not feel comfortable to rely on the information provided by an audit firm registered in a jurisdiction that they are not familiar with.

Our response

59. We consider that whether a sponsor feels comfortable with a specific audit firm will be determined on a case-by-case basis and is a commercial matter that would need to be considered by a sponsor before accepting an engagement. If a sponsor does not feel comfortable with a specific audit firm, the sponsor can discuss the matter with the listing applicant to change the audit firm or alternatively to withdraw from the engagement.

<u>Comments on Rule amendments</u>

Comments received

60. A respondent commented that the reference to "business segments" in Notes 2(b) and 2(c) to Main Board Rule 14.04 in the Rule amendments included in the Consultation Paper is out of date and suggested the word "business" be removed. A respondent suggested amending Main Board Rules 19A.33 and 19A.35 and GEM Rules 25.26 and 25.29 to require the audit firms to report on whether the financial statements "…give a true and fair view <u>or to present fairly in all material respects</u>…" of the results and financial position of the issuer.

Our response

61. We agree with the comment in relation to the reference to "business segments" and have amended the Rule to delete the word "business".

62. On the latter point relating to adding the phrase "present fairly in all material respects" we note that paragraph 35 of HKSA 700 (Clarified)/ISA 700 "Forming an Opinion and Reporting on Financial Statements" states that the phrases "present fairly in all material respects" and "give a true and fair view" are regarded as being equivalent. On this basis, we consider that adding the phrase "present fairly in all material respects" to the relevant Main Board and GEM Rules is not necessary.

63. After taking into consideration the above matters set out in paragraphs 12 to 62, we have decided to adopt the proposed framework to accept Mainland accounting and auditing standards and Mainland audit firms for Mainland incorporated companies listed in Hong Kong and a reciprocal arrangement for Mainland listings of companies incorporated or registered in Hong Kong.

Effective commencement date

64. In our Consultation Paper, we suggested that if the proposed framework is adopted, the proposed effective commencement date for the new rules would be 1 January 2010 and would apply to annual accounting periods beginning on or after 1 January 2010.

Overall response

65. A majority of the respondents supported the proposed effective commencement date of 1 January 2010. Out of the thirty submissions received, eighteen agreed to our proposal and eight did not agree.

Comments received

66. Some of the respondents who did not agree to the proposed effective commencement date suggested that the commencement date should be delayed at least three to five years. They considered that the timeframe was too short for the Mainland and Hong Kong regulators to complete the preparation work necessary to implement the framework. Some respondents from the insurance industry also suggested deferring the commencement date until the China Insurance Regulatory Commission ("CIRC") has finalised the timetable for the proposed new computation method for insurance reserves, which they indicated may have a significant impact on the financial statements of insurance companies.

67. Some respondents commented that it was not clear how the effective commencement date of 1 January 2010 should be applied in prospectuses and circulars where financial information presented is required to cover more than one financial year.

Our response

68. The framework provides Mainland incorporated companies listed in Hong Kong with a choice of accounting standards and audit firms. The proposed amendments to the Rules are enablers rather than requirements and the changes do not automatically require any immediate actions to be taken by issuers. As mentioned in the Consultation Paper, if an issuer is considering a change it should carefully study the possible impact before deciding on a change.

69. The original timetable to introduce the framework on 1 January 2010 was agreed between the Hong Kong and Mainland regulators and a majority of respondents to the public consultation agreed with the proposed commencement date. Another year has lapsed. All the preparation work including the practice review comparison and all the memoranda of understanding are now in place.

70. In relation to the request for a delay until the new computation method for insurance reserves is released by the CIRC, we consider that issuers whose business is in a regulated industry, such as banks and insurance companies, would need to comply with any specific additional requirements which are imposed by their industry regulators. As mentioned above our proposals are enablers to facilitate a choice and issuers have the freedom to decide whether they wish to change and if so, the appropriate timing for the change.

71. After taking into consideration the matters noted in paragraphs 65 to 70 above, we have decided to adopt the new rules with a commencement date of 15 December 2010. CASBE may be used for the preparation of periodic financial reports commencing from annual accounting periods ending on or after 15 December 2010.

72. If a Mainland incorporated listing applicant or issuer has decided to adopt CASBE for its annual accounting periods ending on or after 15 December 2010, in the preparation of financial information to be included in a prospectus or a circular issued on or after 15 December 2010, the financial information for all periods presented in the prospectuses or circular should also be prepared under CASBE.

CONSULTATION CONCLUSIONS

73. We have adopted the proposals as proposed in the Consultation Paper. We have finalised the revised Rules to implement the proposals which are available on HKEx’s website.

APPENDIX 1 LIST OF RESPONDENTS

Main Board issuers

1 HSBC Holdings plc
2 PICC Property and Casualty Company Limited
3 Main Board issuer 1 (name not disclosed at the respondent's request)
4 Main Board issuer 2 (name not disclosed at the respondent's request)
5 Main Board issuer 3 (name not disclosed at the respondent's request)
6 Main Board issuer 4 (name not disclosed at the respondent's request)
7 Main Board issuer 5 (name not disclosed at the respondent's request)
8 Main Board issuer 6 (name not disclosed at the respondent's request)
9 Main Board issuer 7 (name not disclosed at the respondent's request)
10 Main Board issuer 8 (name not disclosed at the respondent's request)
11 Main Board issuer 9 (name not disclosed at the respondent's request)
12 Main Board issuer 10 (name not disclosed at the respondent's request)
13 Main Board issuer 11 (name not disclosed at the respondent's request)

GEM issuer

14 GEM issuer (name not disclosed at the respondent's request)

Professional and trade associations

15 ACCA Hong Kong
16 CPA Australia – Hong Kong China Division
17 The Chamber of Hong Kong Listed Companies
18 The Hong Kong Institute of Certified Public Accountants
19 The Hong Kong Institute of Chartered Secretaries
20 The Hong Kong Society of Financial Analysts

Market practitioners

21 Hermes Equity Ownership Services Limited
22 KPMG
23 Latham & Watkins
24 Linklaters
25 PricewaterhouseCoopers
26 The Professional Commons

Retail investors

27 Paul Mok
28 Suen Chi Wai
29 Fanny Wong
30 Retail investor (name not disclosed at the respondent's request)

APPENDIX 2 COMPARISON BETWEEN HKICPA PRACTICE REVIEW PROGRAMME AND THE MAINLAND AUDITOR MONITORING PROGRAMMES

1)	Regulator	**Hong Kong Institute of Certified Public Accountants ("HKICPA")**	**Ministry of Finance ("MOF")**	**Chinese Institute of Certified Public Accountants ("CICPA")**
2)	Responsible department	Quality Assurance Department ("QAD")	Supervision and Inspection Department	Supervision Department
3)	Source of authority	Professional Accountants Ordinance Section 32C	PRC accounting law and PRC CPA law	Section 37 of PRC CPA law and Section 3 of the Articles of CICPA
4)	Targets	Approximately 2,400 practice units in Hong Kong	Approximately 60 Licensed (for listed company audits) CPA firms in the PRC and other CPA firms with focus areas of inspection	Approximately 7,000 CPA firms in the PRC
5)	Selection basis	Risk-based approach: Big 4 are subject to review on annual basis; 3-year cycle for practices with listed companies; priority is given to practices with other public interest clients. Random selection of practices to ensure that all practices have a reasonable chance of being selected.	3-year cycle for Licensed CPA firms and random inspection on other CPA firms with focus areas, e.g, referral by other department, being complained; suspected violations of laws and regulations during daily supervision, etc.	3-year cycle for Licensed CPA firms and 5-year cycle for all other CPA firms in the form of random selection, focusing on special nature of issues or industry, e.g., public interest entities or accepting clients who frequently changes auditors, etc.
6)	Timing of review	Throughout the year	The bulk of the inspections are carried out in the period May to October each year, after the annual reports of listed entities are published. If MOF receives a complaint MOF will initiate an investigation immediately.	Usually from May to October each year, avoiding the peak season of the CPA firms
7)	Qualifications and experience of reviewers / inspectors	Full-time staff of HKICPA with a recognised university degree in accounting / finance / business and CPAs with a minimum of 5 years' post qualification experience gained in CPA firms	The review team should have 2 or more full-time personnel from the MOF or finance department and a number of professionals. The professionals should have the following qualifications: qualified CPA practising in CPA firms for 5 or more consecutive years; have strong operational skills and good professional ethics; not being penalized in the latest 3 years and do not have any relationships with the CPA firms under inspection	Inspectors should be engagement-in-charge in a CPA firm; have more than 5 years audit experiences; familiar with accounting and auditing standards and their applications and not being penalized in the latest 3 years
8)	Time spent on each review	1 day to 3 weeks	Approximately 3 - 4 months. Usually 1 - 2 months spent on site visit to the CPA firm and the other 1 - 2 months spent on the direct inspection of listed clients	Approximately 10 days for the licensed CPA firm's headoffice and 4 - 5 days on their branch offices

		HKICPA	MOF	CICPA
9)	Number of reviewer for each review	1 to 4 reviewers lead by a team leader	At least 2 full-time staff from MOF and a number of professionals depending on the workload. Lead by personnel from MOF	At least 3 inspectors and lead by a team leader from CICPA
10)	Scope of review	1) Review of system of quality control as required by HKSQC 1 and 2) review of completed engagement files to reach a conclusion on compliance with professional standards.	1) Quality of work performed by the CPA firm - must extend the inspection work to two listed clients of the CPA firm in order to verify the work performed; 2) Conditions required for setting up a CPA firm and other matters stipulated by laws and regulations	1) Review of system of quality control according to 5101 Standard on Quality Control for CPA firms and Engagements Quality Control and Guidance on Internal Management of CPA firm 2) Review of engagements files to assess engagement quality; 3) Inspection of compliance with professional ethical requirements.
11)	Review process	1) Notification letter sent to PU at least 6-week in advance of review; 2) Planning and on site review and enquiries with relevant personnel; 3) Exit meeting to agree findings; 4) Dated draft report for practice unit; 5) Practice unit response on dated draft report within 21 days; 6) Issuance of reviewer's report, incorporating the responses from practice unit, if necessary; 7) Quality Assurance Department submit recommendations for Practice Review Committee considerations; 8) Practice Review Committee issue decision letters to PU; 9) Follow-up on Practice Review Committee's decision.	1) MOF lead the overall inspection program and set out the planning; 2) Notification letters will be sent to CPA firms 3-days in advance of the inspection; 3) The CPA firm may be required to perform a self-inspection before the MOF inspection, though not compulsory; 4) Performance of on-site inspection by way of enquiries, review of documentation and other necessary procedures; 5) Team leader to draw a conclusion on the case and the non-compliance matters. Written response should be obtained from the CPA firm; 6) Inspection team consider the written response and prepare a written inspection report to MOF (within 10 working days after the field work and can be extended to 30 working days at maximum for special cases); 7) Hearing by a committee set up by MOF ; 8)The committee make a decision on the case and inform the CPA firm; 9) MOF will penalise the firms if necessary. MOF will also inform the CPA firm that it has the rights to conduct a hearing to explain the case further.	1) Preparation work - planning for the overall inspection program; sending out inspection notifications 5-day in advance of inspection, by way of enquiries and review of documentation. The CPA firm may be required to perform a self-inspection and make the necessary arrangement to accommodate the inspection; 2) Planning of the inspection field work 3) Performance of inspection field work covering the 3 areas mentioned in scope of review above; 4) Team discussions on inspection results and consolidation of inspection findings to a report. Obtain written response from the CPA firm on the inspection findings; 5) Drafting of final inspection report which incorporates the response from the CPA firm; 6) Assembly of inspection working paper files and submit to CICPA; 7) Expert panel to discuss the inspection case; 8) Actions for improvements provided to CPA firms 9) Penalties determined by the Disciplinary Committee will be imposed on CPA firm with serious non-compliances.

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12) Outcome of review	1) Practice Review Committee issue instructions and recommendations to PU to act upon 2) follow-up on the practice unit's proposed action plan 3) follow-up visit 4) raise complaint against the PU	1) instruct the CPA firm to carry out remedial actions; 2) continuous monitoring / follow-up visits 3) advises / reminders to CPA firm by interviews or refer to CICPA for disciplinary actions within the profession 4) To pay a large sum penalty 5) Suspension of practising license 6) Cancellation of CPA qualification 7) Cancellation of CPA firm registration	1) Advise for improvements 2) Criticism within the profession 3) Public reprimand 4) Grading from Outstanding to Bad assigned to CPA firm
13) Review / Inspection manual	HKICPA practice review programme (with reviewer's manual and working paper templates and checklists)	The MOF has a set of rules for supervision and inspection of CPA firms <會計師事務所監督檢查工作規程> and the existing inspection manual <檢查工作指引> is in the process of revision to provide additional detailed guidance	Practice quality inspection system inspection manual (with inspection guides and 7 categories of working paper templates and questionnaires) <會計師事務所執業質量檢查手冊>