

**Bills Committee on
Companies (Amendment) Bill 2004**

**Follow-up Actions Arising from the Discussion
at the Meeting on 8 November 2004**

PURPOSE

At the Bills Committee meeting held on 8 November 2004, Members requested the Administration to provide additional information on a number of matters relating to the Companies (Amendment) Bill 2004 (the Bill). We have consulted the Department of Justice and Hong Kong Institute of Certified Public Accountants (HKICPA), and set out the relevant information in the following paragraphs.

OVERSEAS EXPERIENCE

- (a) *Comparison of the proposals in the Bill and the relevant provisions in other jurisdictions, including but not limited to the following aspects –*
- (i) *application of the provision to parent undertakings which are incorporated or registered or formed locally and those which are not;*
 - (ii) *application of the provision to subsidiary undertakings which are incorporated or registered or formed locally and those which are not;*
 - (iii) *guidelines for company directors to exercise their discretion to apply the “true and fair view override” provisions, and the relevant authority responsible for ensuring compliance.*

2. A comparison table of the proposals in the Bill and the relevant provisions in three other jurisdictions with a similar company law system is at **Annex A**.

(b) *Experience of and problems encountered by other jurisdictions in implementing the relevant provisions.*

3. The definition of “subsidiary” which the Bill proposes to adopt aligns more closely with the same under the International Accounting Standard (IAS) 27 “Consolidated and Separate Financial Statements” promulgated by the International Accounting Standards Board (IASB) since 1990. Subsequently, many jurisdictions (including the United Kingdom, Australia and Singapore) following International Financial Reporting Standards¹ (IFRSs) have adopted this “control-based” approach² for the definition of “subsidiary”, in connection with the preparation of group accounts, in their company laws and accounting standards since the last decade. As far as we are aware, this definition of “subsidiary” has run well in these jurisdictions over these years. Moreover, according to the IASB, IFRSs have achieved wide recognition in over 90 jurisdictions which would have implemented these standards by 2005. Notably, the European Union (EU) requires all companies listed on the regulated markets in the EU to prepare their group accounts on the basis of IAS 27 starting from 1 January 2005. We envisage that by following suit we would enhance the quality of financial reporting for Hong Kong incorporated companies and thus their corporate governance, and facilitate comparison and interpretation of accounts of Hong Kong incorporated companies vis-à-vis those in other major financial markets in the world that adopt IFRSs.

¹ IASB publishes its standards in a series of pronouncements called International Financial Reporting Standards (IFRSs). IAS 27 “Consolidated and Separate Financial Statements” is one of these pronouncements.

² The “control-based” approach in determining the “parent-subsidiary” relationship looks also at the control of voting powers and the right to exercise a dominant influence over the financial and operating policy of the subsidiary undertaking, set aside the perspective relating to the economic ownership of the shares of the subsidiary undertaking.

SCOPE OF THE APPLICATION OF THE BILL

- (a) *Application of the Bill to parent undertakings which are –*
- (i) *incorporated or registered or formed in Hong Kong;*
 - (ii) *incorporated or registered or formed in the Mainland or other jurisdictions; or*
 - (iii) *listed in Hong Kong.*

4. At present, the requirement to lay in general meeting group accounts is provided under sections 124 of the Companies Ordinance (CO, Cap. 32). It applies to a “company” which has subsidiaries. Sections 125, 126, 128, and the Tenth Schedule govern the form and contents of the group accounts of such a company. As defined under section 2(1), the term “company” means a company formed **and** registered under the CO or an existing company³. The definition essentially refers to a “Hong Kong incorporated company”. Therefore, as far as the application of the CO is concerned, whether or not the “company” is listed in Hong Kong or any other places is **not** relevant. The Bill will not change the *status quo* that only Hong Kong incorporated companies are required to prepare group accounts in accordance with the requirements of the CO.

5. Although a non-Hong Kong company, including a company incorporated in the Mainland, that establishes a place of business in Hong Kong is required to be registered under section 333(1) of the CO, it is not formed or incorporated in Hong Kong and therefore falls outside the definition of “company” under section 2(1). Thus, a non-Hong Kong parent company does not need to comply with the relevant requirements of preparing group accounts under section 124. Nevertheless, section 336(1) of the CO requires a non-Hong Kong company to deliver to the Registrar of Companies a certified copy of the latest published accounts of the company that comply with the law of the place of incorporation of the non-Hong Kong company.

6. Separately, listed companies in Hong Kong are required to

³ In short, an “existing company” means a company formed and registered under the Companies Ordinance 1865, or the Companies Ordinance 1911.

comply with the Listing Rules⁴ of the Stock Exchange of Hong Kong Limited (SEHK). The Listing Rules require listed companies to prepare group accounts in accordance with either the Hong Kong Financial Reporting Standards⁵ (HKFRSs) or the IFRSs.

7. For illustrative purpose, the following table summarizes the financial reporting requirements for the relevant types of listed companies –

Types of Listed Companies	Accounting Requirements under CO	Accounting Requirements under Listing Rules
Hong Kong incorporated companies	Section 124 of the CO requires companies to prepare group accounts under the accounting requirements set out in CO.	The Listing Rules require all listed companies to prepare accounts in accordance with HKFRSs or IFRSs.
Non-Hong Kong companies	Section 336 requires non - Hong Kong companies to deliver to the Registrar of Companies published accounts that comply with the law of the place of incorporation.	Same as above.

Table 1: Comparison of financial reporting requirements of listed companies in Hong Kong

8. As there is, at present, a “gap” between the definition of “subsidiary” under the CO and that under the HKAS 27, the HKAS 27

⁴ The Listing Rules refer to the Rules Governing the Listing of Securities on the SEHK and Rules Governing the Listing of Securities on the Growth Enterprise Market of the SEHK. They are made by the SEHK, and are subject to approval by the Securities and Futures Commission under the Securities and Futures Ordinance (Cap. 571).

⁵ The HKICPA is empowered, pursuant to section 18A of the Professional Accountants Ordinance (Cap. 50) to issue accounting standards required to be observed, maintained or otherwise applied by any certified public accountants. These accounting standards are referred to as the “Hong Kong Financial Reporting Standards (HKFRSs)” collectively. Hong Kong Accounting Standard (HKAS) 27 “Consolidated and Separate Financial Statements” is one of the HKFRSs and is equivalent in all material aspects, including the definition of “subsidiary”, with IAS 27 “Consolidated and Separate Financial Statements”.

requires Hong Kong incorporated companies (including those listed on the SEHK) to disclose financial information of subsidiary undertakings, which fall outside the scope of CO but within that of HKAS 27, in the “notes to accounts” as an **interim** arrangement.

- (b) *Application of the Bill to subsidiary undertakings which are incorporated or registered or formed in Hong Kong; and*
- (c) *Application of the Bill to subsidiary undertakings which are not incorporated or registered or formed in Hong Kong, in particular those incorporated or registered or formed in the Mainland.*

9. In determining whether or not an undertaking is a subsidiary undertaking in relation to another undertaking under the existing provisions of the CO⁶ **and** the proposed Twenty-third Schedule in the Bill, the subsidiary undertaking’s place of incorporation, formation or registration is **not** relevant. Therefore, accounts of all subsidiary undertakings falling within the criteria set out in section 2(1) of the proposed Twenty-third Schedule, be they incorporated or registered or formed in Hong Kong or otherwise, are still subject to consolidation in the group accounts prepared by the relevant Hong Kong incorporated parent undertaking.

“DOMINANT INFLUENCE” TEST

- (a) *Operation of the “dominant influence” test in a situation where more than one parent undertaking exercise dominant influence over a subsidiary undertaking (i.e. “joint control” of a subsidiary).*

10. IAS / HKAS 27 provides that only one undertaking can have dominant influence or control over another undertaking. It is a question of facts to determine which undertaking ultimately has a dominant

⁶ Existing sections 2(4), (5), (6) and (7) of the CO set out the criteria whereby a company shall be regarded as the subsidiary of a parent company. Pursuant to sections 2(3) and (8), the company refers not only to a company incorporated in Hong Kong but also one outside Hong Kong. Hence, at present, accounts of a non-Hong Kong subsidiary company (including a Mainland subsidiary company) are already subject to consolidation in the group accounts of a Hong Kong incorporated parent company under the CO.

influence over another. If two undertakings concurrently but independently exert influence or control over another undertaking but each fails to demonstrate that it is a parent undertaking under the test for the “parent-subsidiary” relationship under the CO or IAS / HKAS 27, the two undertakings will be regarded as having a joint control over what the financial reporting standards call the “jointly controlled entity”⁷.

(b) *How group accounts in relation to a subsidiary undertaking under “joint control” are prepared.*

11. An undertaking having a joint control together with others over a jointly controlled entity does not need to prepare group accounts, as the undertaking cannot satisfy any of the tests which determines “parent-subsidiary” relationship (including the “dominant influence” test) under the CO and IAS / HKAS 27. However, under HKAS 31 “Investment in Joint Ventures”, the interests in a jointly controlled entity are accounted for by proportionate consolidation⁸ or equity accounting⁹ methods.

(c) *Operation of the “dominant influence” test in a situation where a parent undertaking has a dominant influence in respect of the operating policies of a subsidiary undertaking while another parent undertaking has a dominant influence in respect of the financial policies of the same subsidiary undertaking.*

⁷ A jointly controlled entity is defined under HKAS 31 as a joint venture in which each venturer has an interest. The entity operates in the same way as other entities, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity. For example, a jointly controlled entity can be owned by two venturers (each having 50% of the interests), or three venturers (each having one-thirds of the interests), or even more.

⁸ The proportionate consolidation method is, as defined under HKAS 31, a method of accounting whereby a venturer’s share of each of the assets, liabilities, income and expenses of a jointly controlled entity is combined line by line with similar items in the venturer’s accounts or reported as separate line items in the venturer’s accounts.

⁹ The equity method is, as defined under HKAS 31, a method of accounting whereby an interest in a jointly controlled entity is initially recorded at cost and adjusted thereafter for the post-acquisition change in the venturer’s share of net assets of the jointly controlled entity. The profit or loss of the venturer includes the venturer’s share of the profit or loss of the jointly controlled entity.

12. Section 5(a) of the proposed Twenty-third Schedule¹⁰ proposes to define “dominant influence” as “a right to give directions with respect to the operating and financial policies of that other undertaking which the directors are, or a majority of the directors is, obliged to comply with whether or not they are for the benefit of that other undertaking”. Both the “operating policy” and “financial policy” limbs have to be satisfied before this test is passed.

(d) *The meaning of “dominant influence”, and whether there are any practice directions or court directions on the application of the “dominant influence” test in determining “parent-subsidiary” relationship.*

13. We are not aware of any court case where the interpretation of “dominant influence” in this context was disputed. We propose, with reference to the UK Companies Act 1985, that -

- (a) the term “dominant influence” should be defined, under section 5(a) of the Twenty-third Schedule, in the way as set out in paragraph 12 above; and
- (b) the right to exercise a “dominant influence” should be derived, under section 2(1)(c) of the Twenty-third Schedule, from “the provisions contained in the subsidiary undertaking’s memorandum or articles or equivalent constitutional documents or a control contract”¹¹.

We consider that the provisions in the Bill provide sufficient clarity for application.

IMPACT OF THE BILL ON THE FINANCIAL REPORTING REQUIREMENTS

¹⁰ Section 5(a) of the proposed Twenty-third Schedule is modelled on paragraph 4(1) of Schedule 10A to the UK Companies Act 1985.

¹¹ Section 2(1)(c) of the proposed Twenty-third Schedule is modelled on section 258(2)(c) of the UK Companies Act 1985.

- (a) *Comparison of the existing and proposed requirements on companies, with concrete examples to show the impact of the change.*

14. To illustrate the impact of the change introduced by the Bill, the HKICPA has provided at **Annex B** three samples of group accounts (extract) of a hypothetical Hong Kong incorporated parent company which engages in securitization business and sets up a special-purpose entity (SPE) (falling within the proposed definition of “subsidiary”) which is not a body corporate *per se*. The first set of accounts shows the financial position of a company before setting up the SPE. The second set of accounts shows the position after the establishment of the SPE under the existing CO, whereas the third set shows the same position under the provisions of the Bill.

15. As demonstrated by these sample accounts, the changes introduced by the proposals in the Bill lie primarily in the format of presentation, instead of the content or amount of the disclosure in the accounts. This is because, notwithstanding the present reporting requirements in the CO, Hong Kong incorporated parent companies are already required under the HKAS 27 to disclose the financial information of their subsidiary undertakings in the form of “notes to accounts”.

- (b) *Cost implication of the proposed requirements for companies, in particular small companies; and*
- (c) *Impact of the proposed requirements on companies which are exempted from consolidation under the existing CO but will be required to file group accounts after the passage of the Bill.*

16. The proposal to amend the definition of “subsidiary” for the purposes of group accounts is expected to constitute little or no compliance burden on companies of any size. As companies complying with HKAS 27 are already disclosing financial information of their subsidiaries (which may include a body corporate, a partnership or an unincorporated body) in the notes to accounts now, we do not envisage that the mere change of the format of presentation will give rise to practical difficulties or a substantial increase in the cost of preparing

group accounts.

“TRUE AND FAIR VIEW OVERRIDE” PROVISION

- (a) *Whether the Financial Secretary (FS) has invoked the powers under sections 123(4) and 126(3) of CO to modify the requirements of the CO as to the matters to be stated in a company’s accounts or group accounts; and*
- (b) *Existing criteria for the FS to exercise the powers under section 123(4) and 126(3) of CO.*

17. According to our records, the powers of FS under sections 123(4) and 126(3) to modify the requirements of the CO as to the matters to be stated in a company’s accounts or group accounts have never been used. Nor have there been any existing criteria for the FS to exercise these powers.

- (c) *Impact of the proposed “true and fair view override” provisions on the responsibilities and liabilities of company directors and auditors in preparing company’s accounts or group accounts.*

18. According to sections 123(1) and 126(1) of the CO, the accounts or group accounts of a company shall give a “true and fair view” of the state of affairs and profit and loss of the company. By virtue of section 123(6), the statutory duty is put on the company directors, who will be liable if they fail to take all reasonable steps to secure compliance with section 123 and other requirements of the CO as to the matters to be stated in the accounts. In any case, this general requirement to present accounts giving a “true and fair view” has always been, and will continue to be, the ultimate objective of financial reporting, notwithstanding that the existing CO does not expressly require companies to disclose additional information or depart from the requirements of the CO so as to achieve a “true and fair view”¹².

¹² Section 123(3) states that “(s)ave as expressly provided in the following provisions of this section or in Part III of the Tenth Schedule, the requirements of subsection (2) and the said Schedule shall be without prejudice either to the general requirements of subsection (1) or to any other requirements of this Ordinance (emphasis added).” Thus, where compliance with the Tenth

19. We consider that the express “true and fair view override” provisions will enhance the transparency of financial reporting hence providing further guidance to company directors in order to discharge their duties of preparing accounts that give a true and fair view. We propose to expressly require disclosure of additional information that may be necessary to give a true and fair view of the financial position of the company. In addition, we propose that in the unlikely event where compliance with the relevant provisions of CO as stipulated in the proposed sections 123(4A) and 126(5) is inconsistent with the requirement to give a true and fair view, company directors shall depart from those relevant provisions to the extent as may be necessary to give a true and fair view, and disclose the reasons for and particulars and effects of such departure in the accounts or statement thereto.

20. Sections 141(1) and 141(3) require, *inter alia*, that the auditors of a company shall make a report to state whether in the auditors’ opinion the company’s balance sheet, profit and loss account and group accounts have been properly prepared in accordance with the CO and whether in their opinion a “true and fair view” is given. As this duty remains unchanged notwithstanding the “true and fair view override” provision, we do not consider the proposed amendments will change the responsibilities and liabilities of auditors.

(d) *Whether guidelines will be issued by the Administration or the HKICPA for company directors to apply the “true and fair view override” provisions so as to ensure that they would exercise their discretion in a reasonable manner.*

21. We envisage that “the true and fair view override” provision will be used only in an exceptionally rare occasion to cater for the unforeseen circumstances of a company. If necessary, the HKICPA will promulgate guidelines and interpretations as to the application of the “true and fair view override” provisions, taking into account the experience in the application of the provisions and the development of the

Schedule does not give a true and fair view of the company’s state of affairs, the company accounts should, say, disclose additional information as may be necessary to fulfill the “true and fair view” requirement in section 123(1).

IFRSs.

**Financial Services and the Treasury Bureau
December 2004**

**Comparison Table between Provisions in relation to Group Accounts
in the Hong Kong Companies Ordinance (CO) / Companies (Amendment) Bill 2004 vis-à-vis
International Financial Reporting Standards (IFRSs), Hong Kong Financial Reporting Standards (HKFRSs),
and Company Laws in the UK, Australia, and Singapore¹**

(A) Definitions

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
Definition of “Subsidiary”, “Parent”	A subsidiary is “an entity that is controlled by another entity (known as the parent)”. [Para. 4 of IAS 27 / HKAS 27]	An undertaking is a parent undertaking of a subsidiary undertaking if (a) the parent undertaking controls the subsidiary undertaking; or (b) the parent undertaking has	An undertaking is a parent undertaking of the subsidiary undertaking if (a) the parent undertaking controls the subsidiary undertaking; or (b) the parent undertaking has	Since s. 296(1) of Corporations Act 2001 requires that the financial report of a company must comply with the accounting standards, Australia’s financial reporting	A corporation is a subsidiary of another corporation if the parent fulfills the requirements on the control over the subsidiary. [s. 5]

¹ The information contained in this table is based on the best available information in published literature as well as from the relevant official contacts and accountancy bodies of the respective jurisdictions.

² The relevant provisions under UK Companies Act 1985 have been amended by the Companies Act 1989 and the Companies Act 1985 (International Accounting Standards and other Accounting Amendments) Regulations 2004.

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
		the right to exercise a dominant influence over the subsidiary undertaking. <i>[S. 2(4) to (7), proposed s. 2B & Twenty-third Schedule]</i>	the right to exercise dominant influence over it. <i>[s. 258(2)]</i>	standard AASB 127 (which is based on IAS 27) is relevant in determining the definition of “subsidiary” and “parent”. <i>[s.296]</i> A subsidiary is “an entity that is controlled by another entity (known as the parent)”. <i>[Para. 4 of AASB 127]</i>	
Determination of “control” and “dominant influence”	“Control” is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting rights	“Control” means controlling the composition of the board of directors (to appoint or remove a majority of its board of	“Control” means controlling the composition of the board of directors (to appoint or remove a majority of its board of	“Control” is presumed to exist when the parent owns, directly or indirectly through subsidiaries, more than half of the voting rights	“Control” means controlling the composition of the board of directors (to appoint or remove a majority of its board of

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
	<p>of an entity unless, in exceptional circumstances, it can be clearly demonstrated that such ownership does not constitute control.</p> <p>Control also exists when the parent owns half or less of the voting power of a subsidiary when there is –</p> <p>(a) power over more than half of the voting rights by virtue of an agreement with other investors; or</p> <p>(b) power to govern the financial and operating policies of the entity under a statute or an</p>	<p>directors), or controlling more than half of the voting rights, or controlling more than half of the issued share capital of the subsidiary undertaking.</p> <p>A parent undertaking shall not be regarded as having the right to exercise a dominant influence over the subsidiary undertaking unless the former has a right to give directions with respect to the operating and financial policies of the latter which the directors are, or a majority of the directors is, obliged to comply with whether or not</p>	<p>directors), or holding or controlling a majority of the voting rights, of the subsidiary undertaking.</p> <p>A parent undertaking shall not be regarded as having the right to exercise a dominant influence over the subsidiary undertaking unless the former has a right to give directions with respect to the operating and financial policies of the latter which the directors are obliged to comply with whether or not they are for the benefit of the subsidiary</p>	<p>of an entity unless, in exceptional circumstances, it can be clearly demonstrated that such ownership does not constitute control.</p> <p>Control also exists when the parent owns half or less of the voting power of a subsidiary when there is –</p> <p>(a) power over more than half of the voting rights by virtue of an agreement with other investors; or</p> <p>(b) power to govern the financial and operating policies of the entity under a statute or an</p>	<p>directors), or controlling half of the voting rights, or holding more than half of the issued share capital of the subsidiary.</p> <p>Since s. 201(3A) of the Companies Act requires that group accounts shall comply with accounting standards, FRS 27 (which is based on IAS 27) is relevant in determining “control” which also exists when there is the power to govern the financial and operating policies of the subsidiary under a statute or an agreement.</p>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
	<p>agreement; or</p> <p>(c) power to appoint or remove the majority of the members of the board of directors or equivalent governing body and control of the entity is by that board or body; or</p> <p>(d) power to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.</p> <p><i>[Para. 13 of IAS 27 / HKAS 27]</i></p>	<p>they are for the benefit of the subsidiary undertaking.</p> <p><i>[s. 2(4) to (7), proposed s. 2B & Twenty-third Schedule]</i></p>	<p>undertaking.</p> <p><i>[s. 258, and Schedule 10A]</i></p>	<p>agreement; or</p> <p>(c) power to appoint or remove the majority of the members of the board of directors or equivalent governing body and control of the entity is by that board or body; or</p> <p>(d) power to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.</p> <p><i>[Para. 13 of AASB 127]</i></p>	<p><i>[s. 5 & 201(3A) of Companies Act, para. 13 of FRS 27]</i></p>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
Scope of “undertaking”	An “entity” includes an unincorporated entity such as a partnership. <i>[para. 4 of IAS 27 / HKAS 27]</i>	“Undertaking” includes a body corporate or corporation; a partnership; an unincorporated body carrying on a trade or business, whether for profit or not. <i>[Proposed Twenty-third Schedule]</i>	“Undertaking” means a body corporate or partnership; or an unincorporated association carrying on a trade or business, with or without a view to profit. <i>[s. 259(1)]</i>	An “entity” includes an unincorporated entity such as a partnership. <i>[Para. 4 of AASB 127]</i>	The Companies Act is based on the concept of “company” but its accounting standard “FRS 27” uses the same concept of “entity” as in IAS 27. S. 201(3A) of the Companies Act requires that group accounts shall comply with accounting standards. Therefore, the scope of “subsidiary” includes an unincorporated entity such as a partnership. <i>[s. 5 & 201(3A) of Companies Act; para. 4 of FRS 27]</i>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK Companies Act 1985 ²	Australia (Corporations Act 2001)	Singapore (Companies Act)
Applications of the provisions to parent undertakings which are incorporated or registered or formed locally and those not	Not applicable.	“Company” means a company formed and registered under the CO or an existing company. “Hong Kong incorporated companies” are required to prepare group accounts under the CO. <i>[s. 2(1)]</i>	“Company” means a company formed and registered under the Act or an existing company. “UK incorporated companies” are required to prepare group accounts under the Act. <i>[s. 735(1)]</i>	All disclosing entities incorporated or formed in Australia, public companies, large proprietary companies, and all registered schemes shall prepare financial statements. <i>[s. 292(1)]</i>	“Company” means a company incorporated pursuant to the Companies Act or pursuant to any corresponding previous written law. “Singapore incorporated companies” are required to prepare group accounts under the Act. <i>[s. 4(1)]</i>
Application of the provisions to subsidiary undertakings which are incorporated or registered or formed locally and those not	The undertaking’s place of incorporation, formation, and registration is not relevant in determining whether it is a subsidiary undertaking.	Same as IFRSs/HKFRSs.	Same as IFRSs/HKFRSs.	Same as IFRSs/HKFRSs.	Same as IFRSs/HKFRSs.

(B) Preparation of Group Accounts and the “True and Fair View” Provision

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK (Companies Act 1985)	Australia (Corporations Act 2001)	Singapore (Companies Act)
Preparation of group accounts	<p>A parent shall present consolidated financial statements in which it consolidates the accounts of subsidiaries in accordance with IAS 27 / HKAS 27.</p> <p><i>[Para. 9 of IAS 27 / HKAS 27]</i></p>	<p>Where, at the end of its financial year, a company has subsidiaries, group accounts should be laid before the parent undertaking in general meeting, in addition to the parent undertaking’s own balance sheet and profit and loss account. The group accounts shall deal with the state of affairs and profit of loss of the company and subsidiaries.</p> <p><i>[s. 124(1)]</i></p>	<p>If at the end of a financial year a company is a parent company, individual accounts and group accounts for the year shall be prepared. The group accounts shall deal with the state of affairs and profit of loss of the parent company and subsidiary undertakings.</p> <p><i>[s. 227(1), 227A(1)]</i></p>	<p>The financial statements for the year shall include, if required by the accounting standards, a consolidated profit and loss statement and balance sheet.</p> <p><i>[s. 295(2)]</i></p>	<p>For a company that is a parent company, at the end of its financial year consolidated accounts dealing with the profit and loss and the state of affairs of the company and its subsidiaries must be laid before the company at its annual general meeting.</p> <p><i>[s. 201(3A)]</i></p>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK (Companies Act 1985)	Australia (Corporations Act 2001)	Singapore (Companies Act)
“True and fair view”	Financial statements shall give a true and fair view of the financial position and performance of an entity. The application of IFRSs / HKFRSs, with additional disclosure when necessary, is presumed to result in financial statements that give a true and fair view. <i>[Para. 13 of IAS 1 / HKAS 1]</i>	The group accounts laid before a company shall give a true and fair view of the state of affairs and profit or loss of the company and its subsidiaries dealt with thereby as a whole, so far as concerns members of the company. <i>[s. 126(1)]</i>	The accounts must give a true and fair view of the state of affairs and the profit or loss of the undertakings included in the consolidation as a whole, so far as concerns members of the parent company. <i>[s. 227A(2)]</i>	The consolidated financial statements must give a true and fair view of the financial position and performance of the consolidated entity. <i>[s. 297]</i>	The consolidated accounts shall comply with the requirements of the Accounting Standards and give a true and fair view of the accounts, so far as it concerns members of the holding company. <i>[s.201(3A)]</i>
“True and fair view override” and the corresponding disclosure requirement	If management concludes that compliance with a requirement in accounting standards would be so	Where compliance with the relevant provisions as to the matters to be included in a company’s group accounts or in a statement annexed to	Where compliance with the relevant provisions as to the matters to be included in a company’s group accounts would not be sufficient to	If the financial statements and notes prepared in compliance with the accounting standards would not give a true and fair	Where consolidated accounts prepared in accordance with any requirement of the Accounting Standards would not give a true

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK (Companies Act 1985)	Australia (Corporations Act 2001)	Singapore (Companies Act)
	<p>misleading that it would conflict with the objective of financial statements, the entity shall depart from that requirement if the relevant regulatory requirement requires, or otherwise does not prohibit, such a departure.</p> <p>When an entity departs from the requirements of accounting standards, it shall disclose –</p> <p>(a) that management has concluded that the financial statement gives a true and fair view of the entity’s financial position;</p> <p>(b) that it has complied</p>	<p>the group accounts would not be sufficient to give a true and fair view of the state of affairs or the profit or loss of the company and its subsidiaries, additional information as may be necessary to give a true and fair view thereof shall be given in the group accounts or statement.</p> <p>Where compliance with the relevant provisions is inconsistent with the requirement to give a true and fair view of the state of affairs or the profit or loss of a parent company and its subsidiaries, the directors shall depart</p>	<p>give a true and fair view, the necessary additional information must be given in the accounts or in a note to them.</p> <p>If in special circumstances where compliance with the relevant provisions is inconsistent with the requirement to give a true and fair view, the directors must depart from that provision to the extent necessary to give a true and fair view. Particulars of any such departure, the reasons for it and its effects must be given in a note to the accounts.</p>	<p>view, additional information must be included in the notes to the financial statements.</p> <p>[s. 297]</p>	<p>and fair view of any matter required, the consolidated accounts need not comply with that requirement to the extent that this is necessary for them to give a true and fair view of the matter.</p> <p>In the event of any non-compliance with a requirement of the Accounting Standards, there shall be included in the consolidated accounts, among other things,</p> <p>(a) particulars of the departure, the reason therefor and its effects, if any; and</p> <p>(b) such further</p>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK (Companies Act 1985)	Australia (Corporations Act 2001)	Singapore (Companies Act)
	<p>with the relevant accounting standards, except that it has departed from a particular requirement to give a true and fair view;</p> <p>(c) the title of the accounting standard from which the entity has departed, the nature of departure (including the treatment that the accounting standard would require, the reason why the treatment would be so misleading) and the treatment adopted;</p> <p>(d) the financial impact of the departure on</p>	<p>from those provisions to the extent as may be necessary, with reasons for and particulars and effects of such departure to be given in a statement annexed to the company's group accounts.</p> <p><i>[Proposed s. 126(4), (5)]</i></p>	<p><i>[s. 227A(4), (5), (6)]</i></p>		<p>information and explanations as will give a true and fair view of that matter.</p> <p><i>[s.201(14A), (14B)]</i></p>

	IFRSs / HKFRSs	Hong Kong (CO, Companies (Amendment) Bill 2004)	UK (Companies Act 1985)	Australia (Corporations Act 2001)	Singapore (Companies Act)
	<p>the financial statements that would have been reported from complying with the requirement.</p> <p><i>[Para. 17 and 18 of IAS 1 / HKAS 1]</i></p>				
Guidelines for directors to exercise discretion to apply the “true and fair view override” provisions, and the relevant authority responsible for ensuring compliance	No such guidelines.	No plan for such guidelines.	No such guidelines.	No such guidelines.	No such guidelines

**Sample of Group Accounts (Extract) Provided by the HKICPA
To Illustrate the Impact of the Changes Introduced by the Bill**

Scenario

Company H is a hypothetical Hong Kong incorporated company holding a portfolio of receivables it securitizes.

2. **Column (1)** shows the balance sheet of Company H before the receivables are “sold” to a special-purpose entity (SPE) set up for the purpose of securitization.

3. **Column (2)** shows the balance sheet of Company H after the receivables are “sold” to the SPE for \$100. With cash generated from the sale of receivables, Company H pays off the bank loan of \$50. An unincorporated SPE is set up, with Company H holding an interest which is worth \$1, to issue securitization bonds totalling \$100. In the context of section 2(4) of the CO, the SPE, due to the way it is structured, is not construed as the Group’s subsidiary. However, as required **under the existing HKAS 27**, Company H makes a disclosure in a **note** to the accounts in respect of the SPE that are excluded from consolidation by virtue of statutory requirements but would have been consolidated by virtue of the accounting standard requirements.

4. **Column (3)** shows the consolidated balance sheet of Company H after the receivables are “sold” to the SPE for the purpose of securitisation. The financial information of the SPE, which fulfills one of the criteria determining “a subsidiary undertaking” **as proposed in the Bill**, has been consolidated in the balance sheet of Company H.

Sample Accounts

Company H
(Consolidated) Balance Sheet (Extract)
As at 31 December 200X

	(1)	(2)	(3)
	\$	\$	\$
Assets:			
Cash at hand	-	49	50
Receivables	100	-	100
Other assets	20	20	20
Investment in SPE	-	1 <small>(Note 1)</small>	-
	-----	-----	-----
Total Assets	120	70	170
	=====	=====	=====
Liabilities:			
Bonds	-	-	100
Bank loan	50	-	-
Other liabilities	20	20	20
	-----	-----	-----
Total Liabilities	(70)	(20)	(120)
	-----	-----	-----
Net assets	50	50	50
	=====	=====	=====
Financed by:			
Share capital	10	10	10
Retained earnings	40	40	40
	-----	-----	-----
Total Equity	50	50	50
	=====	=====	=====

Note 1 [relevant to column (2) only]

In 200X, the Company launched a securitization programme, under which a special-purpose entity (SPE) was set up to issue securitization bonds. With regard to the receivables totalling \$100 sold by the Company to the SPE, this would be effected by way of a “clean sale” of such receivables to the SPE. All the receivables sold to the SPE would no longer be recognized as an asset in the balance sheet of the Group.

(Note 1 continued)

The major assets and liabilities of the SPE as at 31 December 200X are set out below -

	\$
Cash	1
Receivables	100
Total Assets	101
Bonds	100
Total Liabilities	100

In accordance with HKAS 27, the Group has set out below the significant items of the consolidated balance sheet of the Group and the SPE as at 31 December 200X -

	\$
Cash	50
Receivables	100
Total assets	170
Bonds	100
Total liabilities	120