

贊助人 Patron

曾蔭權行政長官 The Hon Donald Tsang GMB

榮譽會長 Hon President

創會主席 Founder Chairman

鄭基智博士 Dr Moses Cheng GBS OBE JP

前任主席 Past Chairmen

許浩明博士 Dr Herbert H M Hui JP

黃紹開 Peter S H Wong MBA

榮譽顧問 Hon Advisers

劉華森博士 Dr Lau Wah Sum GBS LL.D. DBA JP

鄭海泉 Vincent Cheng GBS OBE JP

吳天海 Stephen T H Ng

劉國元 Liu Guoyuan JP

方正 Eddy Fong GBS JP

19 August 2011

Hon Paul Chan Mo-po, MH, JP
Chairman
Bills Committee on Companies Bill
Legislative Council
8 Jackson Road
Central
Hong Kong

Dear 

2011-2012 理事會 Council:-

主席 Chairman

黃天祐博士 Dr Kelvin Wong DBA

副主席 Deputy Chairmen

麥理思 George Magnus BBS OBE

梁廣灝 Edmund K H Leung SSS OBE JP

黃友嘉博士 Dr David Wong JP

司庫 Treasurer

文基良 Man Mo Leung

卸任主席 Immediate Past Chairman

黃紹開 Peter S H Wong MBA

行政總裁 Chief Executive Officer

徐尉玲博士 Dr Carlye Tsui BBS MBE JP

理事會成員 Council Members

陳心愉女士 Ms Bonnie S Y Chan

張惠彬博士 Dr Charles Cheung JP MBA DBA (Hon)

江偉 A F M Conway

范耀鈞教授 Prof Y K Fan BBS JP

孔敬權 Randy Hung

葉成慶 Ip Shing Hing JP

賴顯榮 Henry Lai

林潔蘭博士 Dr Cynthia Lam

李嘉士 Carmelo Lee

林宣亮 Alfred Lin

劉廷安 Liu Tingan

莫建輝教授 Ir Prof John Mok

莫兆光 Stanley Mok

譚學林博士 Dr Tommy Tam JP

鄧宛舜女士 Ms Cynthia Y S Tang

陶榮教授 Prof Christopher To

曾立基 Richard Tsang

唐華達 Jim Wardell

黃李鳳英女士 Mrs Alison Wong

王桂熾 Huen Wong JP

黃澤峰博士 Dr Peter C F Wong

楊俊偉 Anthony Yeung

翁月華女士 Ms Linda Y W Yung

容永祺 Samuel W K Yung SSS MH JP

Bills Committee on Companies Bill
Seeking views on preparation of simplified financial and
directors' report

The Hong Kong Institute of Directors (“HKIoD”) is pleased to respond on the captioned subject.

HKIoD is Hong Kong’s premier body representing professional directors working together to promote good corporate governance. We are committed to contributing towards the formulation of public policies that are conducive to the advancement of Hong Kong’s international status.

In developing the response, we have consulted our members and organised focused discussions.

Should you require further information regarding our response, please do not hesitate to contact me on tel no. 2889 9986.

With best regards

Yours sincerely
THE HONG KONG INSTITUTE OF DIRECTORS



Dr Carlye Tsui
Chief Executive Officer

cc: Dr Kelvin Wong, Chairman of Council, HKIoD
Mr Henry Lai, Council Member, HKIoD & Chairman,
Corporate Governance Policies Committee

CO Rewrite – Bills Committee on Companies Bill seeking views on preparation of simplified financial and directors’ reports

This is in reply to the letter dated 28 July 2011 inviting HKIoD to give written views on Clauses 358 to 362 (under Part 9) and Schedule 3 of the Companies Bill. Let it be known that we are delighted to have the opportunity to assist the Bills Committee on Companies Bill.

* * *

HKIoD previously commented on the issue of relaxing the criteria for small companies to prepare simplified financial and directors’ reports, in our 27 August 2010 submission (the “2010 submission”) in connection with the Draft Companies Bill Second Phase Consultation.

In respect of the treatment of the same issue under the Companies Bill, we comment as follows:-

- As we indicated in the 2010 submission, we generally support the notion of relaxing the qualifying criteria for private companies/groups to prepare simplified financial reports and simplified directors’ reports. We do, however, agree with the retention of the general notion that companies seeking simplified reporting should be entities that do not have “public accountability” concerns.
- We agree with the qualifying conditions previously put up for consultation and now included in the Companies Bill for “small private company” automatic qualification.

for companies limited by guarantees

- As we indicated in the 2010 submission, we generally support the proposal to relax the qualifying criteria for guarantee companies/groups to prepare simplified financial reports and simplified directors’ reports. Guarantee companies are required to file annual return but to require all these companies to follow HKFRS could be too burdensome on many of the smaller entities. We agree with the HK\$25 million annual revenue bright line test that was previously put up for consultation and is now included in the Companies Bill.

for companies not incorporated in Hong Kong

- As we indicated in the 2010 submission, we believe private companies not incorporated in Hong Kong should be permitted to qualify for or to adopt simplified reporting in the same way as companies incorporated in Hong Kong, so long as such would not be inconsistent with specific requirements imposed by the laws of the entity’s place of incorporation or any securities laws and regulations (to the extent applicable), or would not otherwise raise any “public accountability” concerns.

on removing the CO section 141D(3) prohibition

- As we indicated in the 2010 submission, we welcome the move to remove the prohibition preventing a private company that owns and operates ships or aircraft engaged in the carriage of cargo between Hong Kong and a place outside Hong Kong from qualifying for or adopting simplified reporting.

three-tier accounting system

- As we indicated in the 2010 submission, we generally support the notion of a three-tier accounting system comprising full HKFRS for publicly quoted companies, simplified HKFRS-PE for private entities with no public accountability concerns, and SME-FRF&FRS for SMEs meeting threshold requirements. We acknowledge that the HKFRS-PE is intended to be applicable to all companies and businesses that do not have public accountability concerns but do not or cannot apply SME-FRF&FRS.

We understand there are several issues relating to simplified reporting now before the Bills Committee. We address them in the following passages.

Let more private companies/groups opt for simplified reporting

We understand one of the issues is to consider whether to further relax the criteria so that more private companies can adopt SME-FRF&FRS. Essentially, the issue is whether private companies/groups of any size should be permitted to opt for simplified reporting, even though the HKFRS-PE is already available to larger private companies/groups as an alternative to full HKFRS.

We note that a similar proposal was previously put up for consultation in the Draft Companies Bill, but has not been included in the Companies Bill now before the committee. The proposal there provided that private companies that do not qualify as a “small private company” can take advantage of simplified reports if members holding at least 75% of the voting rights so resolve and no other member objects. The 75% super-majority and “no other member objects” requirements are mirrored in situations where a group of companies that do not qualify as a “small group” seeks to take advantage of simplified reports.

As we indicated in the 2010 submission, we do not object to the notion of letting those private companies (including groups of private companies) which would not qualify for automatic qualification to take advantage of simplified reporting if there is super majority (75% was the proposal) support among members and no other member objects.

As we indicated in the 2010 submission, we are also in support of the notion to dispense with the “no other member objects” restriction. A super-majority of 75% is already a high threshold and we ask if the “no other member objects” provision would translate into an unnecessarily high veto power even if the aim is to protect minority interest.

Individuals who come together to do business in the form of a private company/group should have as much freedom as possible to design the way they go about their internal affairs. Private companies/groups with no public accountability concerns should have that freedom to opt for simplified reporting.

If a private company/group is in a certain business or industry sector or otherwise conduct matters in particular circumstances that raises “public accountability” concerns, there should be targeted treatment rather than a broad brush ban for all private companies/groups. Under the bill, a banking/deposit-taking company, an insurance company or a stock-broking company are each excluded from qualifying for simplified reporting. This is consistent with the premise we subscribe to, that those companies seeking simplified reporting should be ones that do not have “public accountability” concerns.

We understand that the accounting profession objects, arguing that the simplified reporting under SME-FRF&FRS “generally has much simpler accounting requirements and might not be able to reflect, with the degree of transparency that would be expected, the state of affairs of sizeable companies/groups with more complex accounts.”

We note that, how company owners handle the company’s internal affairs among themselves ought to be considered a separate (though related) matter from how to protect outside parties the company deals with. Even if we were to let sizeable private companies/groups adopt SME-FRF&FRS, is there not a case for us to believe that their lenders and creditors, or business partners and equity investors will demand more transparency, as circumstances require? Will there not be a case for private companies/groups which opt for lesser reporting to eventually experience a higher cost of capital?

Fiddling with automatic qualification criteria to help more SMEs?

We understand that there were some calls during the bills committee deliberation to tinker with the automatic qualification criteria (i.e., the below \$50 million revenue, \$50 million total assets and the 50 employees threshold), with a view to make the qualifying conditions capture more SMEs.

We do not object to the notion of enabling more SMEs to qualify for simplified reporting, but it is not clear to us (yet) if fiddling with the thresholds would actually have a significant effect at capturing more SMEs.

No need for a specific right to trump simplified reporting automatic qualifications

We understand that there were some calls for stipulating in the Companies Bill a specific right for minority shareholders holding certain voting power to require the company to prepare fuller financial reports even when the company would automatically qualify for simplified reporting.

We first note the very important fact that the Companies Bill does not preclude a private company from adopting a fuller reporting framework even if it would qualify or be eligible for something less. Any “small private company” can elect to adopt a fuller standard for its purpose.

Protecting minority shareholders of private companies ought to be put into context. The situation for minority shareholders in private companies/groups is not quite the same as a small investor buying a few lots into a big publicly listed company. There, the small investor cannot be expected to have the same kind of weight and influence as he/she might have in the internal affairs of a private company/group.

But minority shareholders in private companies have much better opportunities and already have the means. Shareholders can by agreement among themselves (shareholder agreements and then the articles of association) stipulate the type of financial information on the company that they can obtain. Anyone investing into a minority interest of a private company/group would have had ample opportunity to consider the kind of information he/she would get from the company, and could have required particular types and forms of financial and other information as a term of the investment. No one is compelled to hold a minority interest in a private company if one does not like the way it goes about its internal affairs! But

in a free economy, anyone is free to “take the risk” for what might be a good financial return from investing in a private company.

**A case for restoring the “signaling effect”
through fuller financial reporting practices adopted on own volition**

For private companies that are by and large owner-managed, imposing fuller scale reporting framework might not serve much utility, and might just invite a formalistic approach to it using boilerplate verbiage. The “signaling effect” of a commitment to demonstrate corporate governance and internal control would have been lost if they were just barely trying to comply with the fuller reporting framework imposed on them.

Even if we were to let more private companies adopt simplified reporting, will it not be the case that these companies will find appreciable benefit in the form of a lower cost of capital if they opt for fuller reporting on their own volition?

It has indeed been our observation that many SMEs are ill-prepared to submit sound loan proposals. They need a better corporate governance scorecard to demonstrate that they have the proper level of internal control, and they need better corporate governance training in order to do. We should make it easier and make it more affordable for SME owners to obtain training to enhance their corporate governance practices.

But our company law should continue to respect the freedom of those who come together to form a business association as much freedom as possible to design how they want to handle internal affairs. The Companies Bill does not preclude members of a private company/group to set out their respective rights and responsibilities in their own constitution and private contracts. The initiatives among private company members to make use of the freedom provided under law to strive for their own protection and to drive for their own governance is what we want to encourage.

-- END --