



羅兵咸永道

BY EMAIL: commentletters@hkiipa.org.hk

Simon Riley
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Hong Kong Institute of Certified Public Accountants
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5 November 2013

Dear Sir,

***LIMITED INVITATION TO COMMENT ON CONSULTATION DRAFT OF
SMALL AND MEDIUM-SIZED ENTITY FINANCIAL REPORTING
FRAMEWORK AND FINANCIAL REPORTING STANDARD (REVISED)***

We welcome this limited invitation to comment on the proposed use of section 381(2) of the new Companies Ordinance (CO) to specify circumstances in which one or more subsidiaries may be excluded from consolidation by those companies that fall within the reporting exemption regime.

Consultation question

Do you consider it is appropriate to include in the SME-FRF & SME-FRS an option to relieve a group from consolidating one or more subsidiary undertakings if the company's directors are of the opinion that their inclusion would involve expense or delay out of proportion to the value to members of the company? Why or why not? If not, what alternative approach would you propose and why?

Response

We find the proposal to revitalise the abovementioned option somewhat surprising by including it in the SME-FRF & SME-FRS; not least that the option in the current CO [s124(2)(b)(i)] has become redundant in recent times. Although the option has existed in Hong Kong companies legislation for many decades it has nonetheless not been widely used, if at all, in practice. This is because the option is not relevant to companies entitled to use s141D of the current CO and other companies required to prepare consolidated financial statements cannot use the option (to exclude material subsidiaries) and still comply with Hong Kong Accounting / Financial Reporting Standards.

We appreciate that directors of companies that fall within the reporting exemption regime of the new CO do not have to prepare annual financial statements or annual consolidated financial statements that give a true and fair view [s380(7)], although the financial statements must be properly prepared in accordance with the accounting standards applicable to the financial statements (SME-FRF & SME-



FRS) [s381(2)]. Nonetheless, financial statements prepared under the SME-FRF & SME-FRS should provide information about the financial position and performance of the entity that is useful to users of such information and which show the results of management's stewardship of and accountability for the resources entrusted to them [SME-FRF.5]. Exclusion of one or more subsidiaries from consolidation that are or could be material to the group's financial position or performance would seem to be inconsistent with the aforementioned stewardship and accountability, even if obtaining information from the subsidiary(ies) necessary for the preparation of consolidated financial statements is disproportionately costly or subject to lengthy delay.

Consequently, if the proposed grounds for exclusion from consolidation are to be included in the revised SME-FRF & SME-FRS, it is essential that the proposed safeguard is also included. **Absent the safeguard of members of the parent company being informed of the proposed exclusion and having the ability to object, we would not agree to the proposed grounds for exclusion unless it were limited to those subsidiaries that are immaterial (individually or collectively) to the consolidated financial statements.** Permission to use the option should be sought from members each year that it is intended to be used. That is, permission should not be applied for multiple years at once.

The revised SME-FRS should specify the time period prior to the end of the financial year in which the directors of a parent company need to write to its members to inform them of the proposed use of the exclusion, that the reasons for use of the exclusion must be clearly addressed and prescribe the period that members have to object. Methods for informing the members should be the same as those permitted by the new Companies Ordinance. We suggest that the members of the parent company should be informed of the proposed exclusion no later than 6 months before the year end and that any member wishing to object has until three months before the year end. We consider that the use of the proposed exclusion should fail if any member objects. These proposals are similar to those contained in s379(b) of the new CO when the directors of a partially owned intermediate parent company wish to avoid preparing consolidated financial statements for the financial year concerned. Such requirements should be made clear in the revised SME-FRF & SME-FRS.

We also believe that guidance should also be given in the SME-FRF & SME-FRS as to how 'value to the members of the company' is to be judged? Is this a materiality test based on quantitative measures or does it involve qualitative aspects as well? Alternatively, to avoid having to provide such guidance, paragraph 19.1(b) could be expressed as:

'(b) the collection of information necessary for the preparation of consolidated financial statements cannot be obtained without disproportionate expense or undue delay'

In circumstances where the abovementioned option is used, we consider that the SME-FRF & SME-FRS should specify that the consolidated financial statements for the financial year concerned should include a statement that the option has been used, the names of the subsidiaries so excluded, the reasons for so doing and some financial information relevant to the excluded subsidiaries. We note that even if s124(2)(b)(i) of the current CO is used to exclude subsidiaries from consolidation, nonetheless, paragraph 24 of Schedule 10 to the current CO still requires financial information to be provided in relation to any subsidiaries not dealt with by the consolidated financial statements.

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If you wish to discuss any of the content of this letter, please contact Nigel Dealy (+852 2289 1221) or Shelley So (+852 2289 2955). We apologise for the lateness of this response and hope that it does not cause you undue inconvenience.

Yours faithfully

A handwritten signature in blue ink that reads "PricewaterhouseCoopers". The signature is written in a cursive, flowing style with a long horizontal stroke at the end.

PricewaterhouseCoopers

