IAG 2
INDUSTRY ACCOUNTING GUIDELINE 2
FINANCIAL STATEMENTS OF RETIREMENT SCHEMES

(Issued April 1997; revised July 2001)

This Guideline sets out recommendations, intended to represent best practice, on the form and contents of the financial statements of retirement schemes.

The provisions of this Guideline should be read in conjunction with the Foreword to Statements of Standard Accounting Practice, Interpretations and Accounting Guidelines and need not be applied to immaterial items.

Part 1 - Introduction

Objective

1. The main aim in issuing this Guideline is to narrow areas of difference and variation in accounting treatment used in the preparation of financial statements of retirement schemes (hereafter referred to as the "scheme(s)") and to enhance the usefulness of publicly available financial information of schemes.

   It is also intended to assist schemes in meeting the legislative requirements on financial reporting contained in the Mandatory Provident Fund Schemes Ordinance ("MPFSO") and Occupational Retirement Schemes Ordinance ("ORSO"). The MPFSO and the ORSO both contain numerous specific disclosure requirements and the preparers of financial statements of schemes under those Ordinances would need to refer to the detailed disclosure requirements contained therein.

   This Guideline is based on the MPFSO and the ORSO in effect at 31 May 2001.

   This Guideline has general application to all scheme financial statements intended to give a true and fair view.

2. This Guideline deals with the contents of financial statements of schemes and is not concerned with accounting for the cost of retirement benefits in the financial statements of employers. It regards a scheme as a reporting entity separate from the employers of the members of the scheme.

3. Financial statements of a scheme are a stewardship report, intended to give a true and fair view of the financial transactions of the scheme during the financial year and of the disposition of its assets and liabilities at the financial year end.

4. To be of value to the users, the information for Mandatory Provident Fund schemes ("MPF schemes") and Occupational Retirement schemes ("ORSO schemes") would be provided on a timely basis. MPF schemes and ORSO schemes are required to submit their audited financial statements to the Mandatory Provident Fund Schemes Authority ("MPFA") not later than six months after the financial year end.

Form and context in which the financial statements appear

5. It is common for the financial statements to be presented as part of an annual report which provides additional information about the scheme. A description of the contents of the other parts of a typical annual report is set out in the Appendix for illustrative purposes.

6. The form and context in which the financial statements appear can have a significant effect on the overall message conveyed to the users. It is therefore important that where an annual report is prepared, the separate components of the report are consistent with each other and do not omit any information which could affect the view given by the annual report as a whole. For example, the review of the financial development of the scheme in the trustees'/administrator's report would need to be both a fair review and consistent with the financial statements.

7. When preparing scheme financial statements one would have to consider the contents of the remainder of the annual report in order to ensure that the financial statements submitted to members, employers and the MPFA are not misleading in form or context.

Types of schemes

8. Schemes are normally described as either defined contribution schemes or defined benefit schemes, each having their own distinctive characteristics. Occasionally schemes exist that contain characteristics of both. Such hybrid schemes are considered to be defined benefit schemes for the purposes of this Guideline.

Defined contribution schemes and defined benefit schemes

Defined contribution schemes

9. Under a defined contribution scheme, a member's benefits receivable on retirement or termination of employment are determined by the contributions paid by the employer, the member, or both and the investment earnings of the scheme. An employer's obligation is usually discharged by making contributions in accordance with the terms of the scheme. An actuary's advice is not normally required although such advice is sometimes used to estimate future benefits that may be achievable based on present contributions and varying levels of future contributions and investment earnings.

10. Members are interested in the activities of the scheme because the performance of the scheme directly affects the level of their future benefits. Members are also interested in knowing whether contributions have been received and whether proper control has been exercised to protect their rights. An employer is interested in the efficient and fair operation of the scheme.

11. The objective of reporting by a defined contribution scheme is periodically to provide information about the scheme and the performance of its investments.

Defined benefit schemes

12. Under a typical defined benefit scheme, members will receive benefits according to a formula which takes into account the duration of their employment and their remuneration at the time of retirement or termination of employment. An employer's obligation is to make sufficient contributions to the scheme in order that such contributions, plus the investment returns, will meet the payments of the promised retirement benefits.

13. A defined benefit scheme needs the periodic advice of an actuary to assess the financial condition of the scheme and recommend future contribution levels.

14. The objective of reporting by a defined benefit scheme is periodically to provide information about the financial resources and activities of the scheme that is useful in assessing the relationships between the accumulation of resources and the obligation to provide scheme benefits over time.

Scheme arrangements

15. There are many different types of scheme arrangements. It is particularly important to establish the precise arrangements in effect when drawing up the financial statements.

16. A scheme may be either "governed by a trust" or "the subject of or regulated by an insurance arrangement". An "insurance arrangement" is, in effect, a contract with an authorized insurer in respect of a scheme (see also paragraphs 19 and 20 below). Schemes which are the subject of or regulated by an insurance arrangement may be "insured" or "fully insured" schemes.

Directly invested schemes

17. A directly invested scheme is a scheme, generally governed by trust, whose assets will usually comprise one or more investments including shares, securities, holdings in unit trusts or investment funds. Such schemes may use "in-house" investment managers employed by the trustees or an external investment manager.

18. Some directly invested schemes invest in managed funds administered by insurance companies which are run on unit trust principles. They must not be confused with insured schemes.

Insured schemes

19. An "insured scheme" is one where the relevant employer pays premiums/contributions to the insurer in return for which the insurer undertakes to return the principal plus investment earnings in respect of members of the scheme. Under an insurance arrangement, premiums/contributions are paid to the insurer and become his property. An insurance arrangement will not necessarily guarantee the benefits promised under the scheme rules. These schemes will generally be insurance arrangements which fall within the definition of Class G or H of long term business as set out in Part 2 of the First Schedule to the Insurance Companies Ordinance.

20. A "fully insured scheme" is one where insurance policies, such as endowment policies, are effected in respect of each member which match and fully guarantee the benefits to be paid to individual members. These schemes fall within the definition of Class I of long term business as set out in Part 2 of the First Schedule to the Insurance Companies Ordinance.

21. Care needs to be taken as insurers also issue policies generally known as "managed fund" policies which are in substance investment management contracts, by which insurers contract with individual schemes to manage or invest their assets. Under such asset management contracts, assets of the schemes do not become the property of the insurer. Typically, the insurer offers participation in one or more funds operated on similar lines to unit trusts or other investment funds. Managed funds may be unitised (ie. represented by units in, or a proportion of, a fund which are valued periodically to take account of reinvested income and capital growth) or segregated, whereby the investments of particular schemes are distinguished from each other.

22. In each of the above contracts, the liability of the life assurance company depends upon the terms of the policy. However, the liability of the employer to his employees and pensioners is governed by the terms of the scheme the employer has set up. If it is a defined benefit scheme the contract will require periodic actuarial valuations to ensure that the funding is sufficient to meet the eventual liabilities promised by the employer.

23. Most small companies use insured schemes because the insurer will generally undertake much of the administration of the scheme.

Pooling agreement or arrangement

24. A "pooling agreement or arrangement" is a convenient way of administering two or more schemes together, as permitted by the ORSO. Under a pooling agreement a number of individual schemes can participate through a master trust deed or a master insurance policy depending on whether the pooling agreement is governed by a single trust or is the subject of or regulated by an insurance arrangement (or a series of insurance arrangements which are of the same class or description). In the case of a pooling agreement governed by trust, the assets of its participating schemes are vested with the administrator of the agreement. This kind of arrangement or agreement governed by a single trust must be managed by a registered trust company as required by the ORSO. In the case of a pooling agreement regulated by insurance arrangement, the administrator of the pooling agreement must be an insurer authorized to carry on business under the Insurance Companies Ordinance. In relation to a pooling agreement, and its participating schemes, the ORSO requires that proper accounts and records are kept, such that the value of the assets attributable to, and the liabilities of, each of its participating schemes are readily determinable from such accounts and records.

Forms of MPF schemes

25. A registered MPF scheme, which must be a defined contribution scheme, may take one of the following three forms as defined in section 2 of the MPFSO:

    a. master trust scheme;

    b. employer sponsored scheme; or

    c. industry scheme.

    MPF schemes are required to be "directly invested schemes established under trust". The MPFSO requires that every MPF scheme shall be administered, managed and maintained by an approved trustee.

Constituent funds

26. An MPF scheme may have one or more constituent funds, each of which must be approved by the MPFA and each of which will have a different investment policy, so that members of the scheme have a choice in investing their accrued benefits.

Part 2 - Definitions

27. The following terms are used in this Guideline with the meanings specified:

    a. *Accrued benefits*

       The benefits for service up to a given point in time, whether vested rights or not. They may be calculated in relation to current earnings or projected earnings.

    b. *Actuarial assumptions*

       The set of assumptions as to rates of return, inflation, increase in earnings, dividend increase, mortality etc, used by the actuary in an actuarial valuation or other actuarial calculations. There are both financial and demographical assumptions. Financial assumptions include the valuation rate of interest, the rate of earnings increases and the rate of any pension increases. Demographical assumptions include mortality and rates of early retirement and withdrawal.

c. Actuary's certificate

In the case of defined benefit schemes, an actuary's certificate is required. This is a statement by an actuary on the ability of the scheme assets to meet the aggregate vested liability of the scheme as well as the adequacy of the scheme assets plus future contributions to meet promised benefits.

The financial statements and the actuary's certificate are two separate reports, having fundamentally different objectives. The former is a record of the financial transactions and current size and disposition of the assets and liabilities of the scheme and the latter is a statement based on an investigation into, and report on, the present and future ability of the scheme to meet the accrued and prospective obligations to its members. These two reports would need to be presented in conjunction with each other.

d. *Additional voluntary contributions*

The contributions (over and above the mandatory or regular contributions, if any, required from a member by the scheme rules or law) which a member elects to pay in order to secure additional benefits.

e. *Administrator*

The term "administrator" refers to the trustee if a scheme is governed by trust or the insurer if a scheme is the subject of or regulated by an insurance arrangement or, in any other case, the person who is principally responsible for the management of the scheme and its assets otherwise than as a person who is solely concerned with the investment and custody of the assets.

f. *Aggregate past service liability*

As defined in section 2(1) of the ORSO.

g. *Aggregate vested liability*

As defined in section 2(1) of the ORSO.

h. *Associates*

As defined in section 2(1) of the ORSO and Schedule 8 to the MPFSO.

i. *Concentration of investment*

This arises when a significant proportion of the assets of the scheme is invested in one entity and any connected entities or persons, or in one property. For the purpose of this definition, an investment includes:

i. an interest in shares and securities of a company;

ii. mortgages on real property owned by a company or person;

iii. freehold and leasehold properties owned by the scheme and effectively leased to a company or person; and

iv. loans made to a company or person. This does not include a deposit made with an authorized institution within the meaning of the Banking Ordinance.

j. A *defined benefit scheme* is one which is not a defined contribution scheme.

k. A *defined contribution scheme* is one which provides that the amount of a benefit under the scheme is to be an amount determined solely by reference to:

i. the contributions to the scheme by or in respect of the member concerned and any declared return in respect of such contributions (where such return may be subject to a minimum guaranteed rate but is otherwise unascertainable before it is declared); and

ii. where appropriate the qualifying service and age of the employee.

l. *Past service liability*

As defined in section 2(1) of the ORSO.

m. *Self investment*

Investment of all or part of a scheme's assets in the business of the employer of members of the scheme and any associates, and includes money currently due to the scheme but held by the employer or any associates, such as employer and employee contributions.

n. *Vested liability*

As defined in section 2(1) of the ORSO.

Part 3 - Recommended practice

Scope

28. The recommendations contained in this Guideline are intended to be applicable to all schemes whose financial statements are intended to give a true and fair view. This includes all schemes registered under the MPFSO and the ORSO.

Primary users

29. The primary users of the financial statements of a scheme are the members, the beneficiaries of deceased former members who receive benefits under the scheme, the employers, and the MPFA.

Basis of accounting

30. The recommendations contained in this Guideline would be considered in conjunction with the fundamental accounting concepts described in SSAP 1 "Presentation of financial statements".

31. The financial statements would include details of all the transactions of the scheme during the financial year and the disposition of its assets and liabilities at the financial year end. The content of financial statements may vary according to the type or category of scheme.

32. The primary function of a scheme is to act as a vehicle for the accumulation of assets to pay benefits to members and beneficiaries. Measuring investments at market value as at the financial year end of the scheme provides more relevant information to users about the resources available to pay benefits than does the cost basis of measurement. The market value basis of measurement is therefore recommended for all investments except dated investment securities which the scheme has both the intention and the ability to hold until maturity which are to be measured in accordance with paragraphs 56 and 57 below.

33. All other assets and liabilities recognised in the statement of assets and liabilities would be stated in accordance with generally accepted accounting principles stipulated in SSAPs and Accounting Guidelines.

34. In the case of directly invested schemes, or schemes participating in a pooling agreement governed by a single trust, the statement of assets and liabilities will show the nature of the investments of the scheme. Where the investments of schemes participating in a pooling agreement are not individually identifiable for the purposes of this disclosure, it is recommended that the analysis of the investments, as indicated in Part 4 of this Guideline, would be provided in respect of the entire pool, in a note to the financial statements, together with disclosure of the scheme's share of that pool.

35. In the case of fully insured schemes, where policies have been purchased in the name or names of individual members and the scheme has no further obligations in respect of payment of benefits to those members, it is not appropriate for them to be included in the statement of assets and liabilities. Instead the cost of acquiring the policies would be treated as the cost of discharging the retirement obligation at the time of purchase. Where such policies constitute the entire assets of a scheme, the revenue statement of such schemes will be confined to a statement of the transactions of the scheme (ie. contributions received and passed to the insurance company and benefits paid by the insurance company to the beneficiaries).

36. In the case of insurance arrangements which fall within the definition of Class G or H of the Insurance Companies Ordinance, the insurance policies (or more accurately, the right to claim under such policies) will be reported as an asset in the statement of assets and liabilities. The financial statements will also disclose the obligation of the scheme to pay benefits. Such obligation is normally based on the total accumulated contributions and declared returns credited to the accounts of the members of the scheme at the date of the statement of assets and liabilities.

Content of financial statements

37. The financial statements of a scheme would normally comprise:

    a. a revenue statement which contains details of the results of the scheme's investment activities and the cost of its administration;

    b. a statement of assets and liabilities which:

        i. in the case of a defined contribution scheme, discloses the disposition of the assets and liabilities of the scheme at the financial year end;

        ii. in the case of a defined benefit scheme, discloses the disposition of the assets and liabilities of the scheme (other than the liability to pay benefits in future) at the financial year end;

    c. a statement of movement in capital account which contains the value of the fund at the beginning and the end of the year, contributions received and benefits paid, amounts transferred to and from the revenue statement and other changes in members' accounts;

    d. a cash flow statement in accordance with SSAP 15;

    e. notes thereto including disclosure (for ORSO schemes) of the aggregate past service liability and the aggregate vested liability at the financial year end;

    f. in the case of MPF schemes, the financial statements shall include, in addition to the financial statements of the scheme itself, for each constituent fund, a revenue statement, a statement of assets and liabilities and a statement of movement in capital account.

38. This Guideline adopts the terms "Revenue Statement" and "Statement of Assets and Liabilities" for all schemes except for defined benefit schemes where the latter statement is replaced by a "Statement of Net Assets Available for Benefits". Such terminology is not mandatory but would as far as possible be used consistently.

39. The financial statements would normally contain as a minimum the items set out in Part 4 of this Guideline insofar as such items are material and applicable to the scheme.

40. Comparatives would be disclosed. The accounting period will usually be one year in duration. If this is not the case for either the current or corresponding period, this fact would be clearly stated.

41. The financial statements would contain such additional information as is necessary to give a true and fair view of the financial transactions of the scheme for the financial year and of the disposition of its assets and liabilities at the financial year end. This will include, for example, information about capital commitments, events after the balance sheet date and contingencies.

Accounting policies

42. The accounting policies followed in dealing with items which are judged material or critical in accounting for or reporting on the transactions and assets and liabilities of the scheme would be explained in the notes to the financial statements. The explanations would need to be clear, fair and concise.

43. The following are examples of some areas where it will be appropriate to disclose the accounting policies adopted:

    a. the policies adopted in applying the accruals concept to significant categories of income and expenditure, such as contributions, investment income, transfer values and benefits;

    b. the bases adopted for the valuation of investments;

    c. the bases adopted for the valuation of other assets;

    d. the basis of foreign currency translation; and

    e. the bases adopted in accounting for investments in subsidiaries and associates.

44. It is a fundamental accounting concept that there is consistency of accounting treatment within each accounting period and from one period to the next. A change in accounting policy would not be made unless it can be justified on the ground that the new policy is preferable to the one it replaces because it will give a fairer presentation of the transactions and of the disposition of the assets and liabilities of the scheme. When changes are made they would be disclosed, along with the reasons for making the change. If the effect is material it would need to be applied retrospectively (see SSAP 2 "Net profit or loss for the period, fundamental errors and changes in accounting policies").

Accumulated scheme benefits

Liability for accrued benefits

45. Liabilities are, in general terms, present obligations of an enterprise arising from past events or transactions, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

46. The position taken in this Guideline is that, because a scheme has a present obligation to transfer assets (ie. to pay benefits) to scheme members and beneficiaries at a future date as a result of past events or transactions, the benefits which have accrued to members and beneficiaries as a result of their membership of the scheme up to the financial year end constitute a liability of the scheme at that date.

Aggregate past service liabilities

Defined contribution schemes

47. The aggregate past service liability to members and beneficiaries of a defined contribution scheme is the accumulated contributions and allocated net earnings of the scheme. This is normally equivalent to the difference between the carrying amounts of the assets and the other liabilities (including forfeitures) of the scheme as at the financial year end, less any reserves or other net earnings which have not been allocated for the benefit of members. This will normally be the amount shown as the balance of the capital accounts.

Defined benefit schemes

48. The liability for accrued benefits to members and beneficiaries of a defined benefit scheme is measured as the present value of expected future benefits which arise from membership of the scheme up to the financial year end as determined by an actuary. This is broadly represented by the aggregate past service liability as defined in the ORSO.

49. The ORSO requires defined benefit schemes to obtain actuarial valuations for funding purposes at least once every three years. The responsibility for reviewing the adequacy of the funding arrangements made to meet expected retirement and other future benefits from the scheme lies with the actuary to the scheme. This responsibility will normally be discharged by the preparation of an actuary's certificate (which is a separate and distinct report from the financial statements of the scheme), which although normally addressed to the trustees/administrator, is also made available to the members. A statement by the actuary based on this certificate will often be appended to the financial statements as a separate component of the annual report.

50. When an actuary's certificate is prepared, the ORSO requires that, among other things, the aggregate past service liability should be calculated. As indicated in paragraph 48, this figure is broadly representative of the liability to members and beneficiaries as at the date it is calculated. In view of the fact that an actuary's certificate may not be prepared each year, and when it is prepared, it may not necessarily coincide with the financial year end of the scheme, care needs to be taken to ensure that the presentation of the aggregate past service liability figure in the financial statements is not misleading to users. This Guideline does not, however, seek to impose any obligations with regard to the frequency of actuarial valuations which are not already imposed by the requirements of the ORSO.

51. It is therefore recommended that the latest available figure of the aggregate past service liability calculated by the actuary would be disclosed, together with a description of the principal features of the figure, in the notes to the financial statements. A description of the principal elements of such a note are set out in Part 4 of this Guideline. The figure of the aggregate past service liability would not be included in the statement of assets and liabilities.

Aggregate vested liability

52. Users of the financial statements of both defined contribution schemes and defined benefit schemes are also likely to be interested in assessing the ability of the scheme to meet benefits which have vested at the financial year end of the scheme. These are the benefits to which members would have been entitled in the event that they had resigned from membership of the scheme as at the financial year end date. It is therefore recommended that the aggregate vested liability would be disclosed in a note to the financial statements. Because disclosure of the aggregate vested liability of a scheme is inconsistent with the applicability of the "going concern" concept under which financial statements are prepared, this figure would not be included in the statement of assets and liabilities.

53. As regards the aggregate vested liability of defined benefit schemes, this figure will normally be calculated by the actuary and, for the reasons discussed in paragraphs 49 and 50 above, may not be calculated as at the financial year end of the scheme. In such cases, it is recommended that the guidance set out in paragraph 51 above would also be applied to the disclosure and treatment of the aggregate vested liability of defined benefit schemes.

Valuation of investments

54. Subject to paragraphs 57 and 60 below, investments would be included in the statement of assets and liabilities at their fair value at the financial year end of the scheme, where such a value is available, or if not available, at the net realisable value. The carrying amount of the principal categories of investment would be arrived at by applying the valuation bases set out below in paragraphs 56 to 60. The bases adopted would need to be disclosed in the notes to the financial statements.

55. Any significant restrictions affecting the ability of the scheme to realise its investments at the financial year end, either at all or at the value at which they are included in the financial statements, would be disclosed in a note. This will include, for example, legal or contractual restrictions on the surrender of units (eg. managed funds) or material penalties which would have been suffered if they had been surrendered at the financial year end. It will not include the inherent difficulties in disposing of a large investment, nor minor restrictions such as a one month delay between the application to surrender and the actual date of payment.

56. Quoted securities would be valued at recognised market prices which would normally be the mid-market price or the closing price if no mid-market price is quoted.

57. Where the scheme holds dated investment securities which have been purchased at a premium or discount and the scheme has both the intention and the ability to hold such securities until maturity, they would be stated at cost adjusted to give effect to the amortisation of premium and accretion of discounts over the period from the date of purchase to the date of maturity. The amortisation of premiums and the accretion of discounts would be dealt with in the revenue statement.

58. Investments in unit trusts/unitised funds would be valued at the bid prices at the financial year end.

59. Freehold and leasehold property would be valued in accordance with the requirements of SSAP 13 "Accounting for investment properties". The names of the persons making the valuation, or particulars of their qualifications, together with the bases of valuation used by them would be disclosed. If a person making a valuation is an employee or officer of the scheme, the trustee, the administrator or the employers, this fact would be stated.

60. In the case of a scheme constituted by a Class G or H insurance policy (as defined in the Insurance Companies Ordinance), the value attributed to that policy in the financial statements of the scheme is the value of the right to claim against the insurance company. This will normally be the accumulated scheme liabilities as shown on the statement issued by the insurance company as at the financial year end date of the scheme.

61. The gains or losses arising from the revaluation of investments would be dealt with in the revenue statement.

Accounting for subsidiaries and associates

62. Schemes may have investments in subsidiaries or associates. These companies will generally be investment-holding companies or trading companies. The associates may include joint ventures such as managed funds or pooled investments. Such investments are generally prohibited under the MPFSO and the ORSO.

63. In principle, such investments would be accounted for as follows:

    a. the results, assets and liabilities of subsidiaries would be consolidated with the transactions, assets and liabilities of the scheme in accordance with SSAP 32 "Consolidated financial statements and accounting for investments in subsidiaries";

    b. investments in joint ventures would be accounted for in accordance with SSAP 21 "Accounting for interests in joint ventures"; and

c. investments in associates would be accounted for in accordance with SSAP 10 "Accounting for investments in associates".

64. Uniform group accounting policies would be followed by a scheme in preparing its consolidated financial statements. Where such group accounting policies are not adopted by a subsidiary, adjustments would be made in preparing the consolidated financial statements.

65. The scheme's investment in trading subsidiaries would be included in the statement of assets and liabilities at fair value.

Long-term insurance policies

66. If long-term insurance policies are held which match, and fully guarantee, the retirement benefit obligations of the scheme in respect of specific individual members, the acquisition costs of the policy would be treated as the cost of discharging the obligations at the time of purchase. Such a policy would not be included in the statement of assets and liabilities.

67. All other long-term insurance policies would be included in the statement of assets and liabilities.

Forfeitures

68. Where an employee leaves a scheme, part or all of the employer's contributions plus the investment return thereon in respect of that member may not be paid to the member. These forfeitures may be applied (depending upon the rules of the scheme) in reducing the contributions of the employer, or be retained in the scheme for the benefit of members, or be returned to the employer. Forfeitures which have not been designated for the benefit of existing members of the scheme as at the financial year end and which have not been returned to the employer would be treated as liabilities of the scheme.

Additional voluntary contributions (AVCs)

69. Where AVCs are made to purchase added years or additional specific benefits within the provisions for benefits under the principal scheme, they would be included as contributions receivable from members in the scheme's statement of movement in capital account and the assets acquired with them would be included in the statement of assets and liabilities.

70. Where AVCs are separately invested in such a way that the proceeds from the investment determine the benefit to the members, they would be disclosed separately from the transactions and the assets and liabilities of the scheme but accounted for within the financial statements of the scheme or the notes thereto.

Disclosure items

71. If the assets of a scheme consist of restricted investments (as defined in the MPFSO or the ORSO as applicable), then this would be disclosed in a note to the financial statements, together with details of the nature and value of the investment involved.

72. Where there is a concentration of investment which exceeds 5% of the value of the net assets of the scheme, then this would be disclosed in a note to the financial statements, together with details of the amount and nature of the investment and the entity involved.

73. Where long-term insurance policies form a material part of the net assets of the scheme, the main characteristics relevant to the overall investment criteria, for instance whether the policies are with or without profits, would be disclosed.

74. Insurance policies purchased to match and guarantee a scheme's retirement benefit obligation in respect of specific individuals as stipulated in paragraph 66 would be disclosed by way of a note. Particulars of policies and the names of the insurer would also be disclosed.

Part 4 - Financial statement disclosures

75. The financial statements of a scheme would include the items listed below where they are material and are in addition to disclosures required under any applicable SSAPs and Accounting Guidelines, together with the disclosures recommended by paragraphs 42 and 71 to 74. These lists are not intended to prescribe either the layout or the order of these items.

76. It should be noted that some of the items which appear in the following lists may not be applicable or material to all schemes. It is therefore necessary to exercise judgement in deciding upon the most appropriate presentation for each scheme's financial statements.

Statement of assets and liabilities

77. In relation to the statement of assets and liabilities separate disclosure would be made of the following:

a. Investment assets:

i. interest-bearing securities analysed between public sector and other;

ii. equities;

iii. other securities;

iv. managed funds analysed between property and other;

v. unit trusts and shares in mutual fund corporations analysed between property and other;

vi. trading subsidiaries and joint ventures;

vii. freehold and leasehold properties;

viii. cash deposits;

ix. insurance policies;

x. other investments;

xi. debtors and creditors in respect of investment transactions where these form part of the net assets available for investment within the investment portfolio; and

xii. other assets and liabilities directly connected with investment transactions (eg. financial futures, options and forward dealings in currencies and, where appropriate, taxation).

Investments would be further analysed between "Hong Kong" and "overseas" and between "quoted" and "unquoted", and between freehold and leasehold property. Leasehold property would be further analysed between "short", "medium" and "long" leasehold.

b. Non-current assets other than investments.

c. Long-term borrowings:

   i. in reporting currency of the scheme; and

   ii. in foreign currency.

d. Other assets and liabilities:

   i. contributions due from employers;

   ii. unpaid benefits;

   iii. bank balances and cash;

   iv. dividends and other receivables;

   v. bank loans and overdrafts or other forms of borrowings;

   vi. forfeitures (which have not been designated for the benefit of members); and

   vii. other assets and liabilities (other than obligations to pay retirement and other benefits in the future).

Revenue statement

78. In relation to the revenue statement separate disclosure would be made of the following:

a. Investment income, broken down by category:

   i. income from interest-bearing securities including the amortisation of premium or accretion of discounts on dated investment securities where appropriate;

   ii. dividends from equities;

   iii. income from managed or unitised funds or mutual funds;

   iv. gross rents from properties;

   v. interest on cash deposits;

   vi. share of profits/losses of associates and joint ventures (if any);

   vii. income from other investments;

   viii. exchange gain/loss;

   ix. net realised gains or losses on investments; and

   x. net unrealised gains or losses on investments.

b. Other income

   Any other category of income which does not naturally fall into any of the above classifications, suitably described and analysed where material, including security lending.

c. Investment expenses:

   i. investment management fees;

   ii. trustee fees;

   iii. custodian fees;

iv. fees paid to any associates of the investment manager, trustee or custodian;

v. property expenses; and

vi. any other category of expenditure which does not naturally fall into the above classifications, suitably described and analysed where material.

d. Administrative and other expenses borne by the scheme:

i. auditors' remuneration;

ii. safe custody and bank charges;

iii. remuneration of the trustee/custodian;

iv. administrator's fee;

v. compensation fund levy paid to the MPFA;

vi. interest on borrowings; and

vii. legal and other professional fees.

Where such expenses are borne other than by the scheme that fact would be disclosed.

e. Taxes, showing separately Hong Kong taxes and overseas taxes (including withholding tax).

f. Amounts transferred to and from the capital account.

Statement of movement in capital account

79. In relation to the statement of movement in capital account separate disclosure would be made of the following:

a. Value of the fund at the beginning of the year.

b. Contributions received and receivable:

i. from employers:

- normal or mandatory;
- additional;

ii. from members:

- normal or mandatory;
- additional voluntary (see paragraphs 69 and 70);

iii. transfers in:

- group transfers in from other schemes;
- individual transfers in from other schemes.

c. Claims on insurance policies.

d. Benefits paid and payable:

i. death or disability benefits;

ii. pensions;

iii. commutation of pensions;

iv. lump sum retirement benefits; and

v. payments to and on account of leavers:

- refunds of contributions;
- purchase of annuities by the scheme to match preserved benefits;
- group transfers out to other schemes;
- individual transfers out to other schemes.

e. Premiums on insurance policies.

f. Forfeitures (together with a description of how they have been or are to be applied).

g. Amounts transferred to and from revenue account.

h. Value of the fund at the end of the year.

Cash flow statement

80. The cash flow statement would be prepared in accordance with the requirements of SSAP 15.

Constituent funds

81. In respect of each of the constituent funds of an MPF scheme, the following would be disclosed:

a. Statement of assets and liabilities

i. Total value of investments

ii. Bank balances

iii. Amounts of subscription receivable

iv. Dividends and other receivables

v. Amounts payable on redemption

vi. Other liabilities

vii. Bank loans and overdrafts or other borrowings

viii. Total value of all assets

ix. Total value of all liabilities

x. Net asset value

xi. Number of units in issue for a unitised fund

xii. Net asset value per unit for a unitised fund

b. Revenue statement

i. Total investment income, broken down by category as for the revenue statement of the scheme, set out above

ii. Total other income, broken down by category as for the revenue statement of the scheme, set out above

iii. Equalisation on issue and cancellation of units for a unitised fund

iv. Investment management fees

v. Trustee fees

vi. Custodian fees

vii. Compensation fund levy paid to the MPFA

viii. Fees paid to any associates of the trustee, custodian or investment manager

ix. Safe custody and bank charges

x. Auditors' remuneration

xi. Interest on borrowings

xii. Legal and other professional fees

xiii. Other expenses

xiv. Taxes

xv. Amounts transferred to and from the capital account

c. Statement of movement in capital account

i. Value of the constituent fund at the beginning of the year

ii. Number of units issued and the amounts received on issue (after equalisation if applicable) for unitised funds or amounts of subscriptions for non-unitised funds

iii. Number of units redeemed and the amounts paid on redemption (after equalisation if applicable) for unitised funds or amounts of redemptions for non-unitised funds

iv. Amounts transferred to and from the revenue account

v. Value of the constituent fund at the end of the year

Notes to the financial statements

82. The notes to the financial statements of an MPF scheme would be presented in respect of each constituent fund as well as for the scheme itself. It would therefore need to be made clear in the text of each note whether it applies to all funds and the scheme, or only to certain of them.

a. Transactions with associates

The following would be disclosed:

i. A description of the nature of any transactions entered into, during the financial year, with the investment manager of the constituent fund (including any of its delegates) or any entity in which those parties or their associates have a material interest, together with a statement confirming that these transactions have been entered into in the ordinary course of business and on normal commercial terms.

ii. - the total aggregate value of the transactions effected through brokers who are associates of the investment manager of the constituent fund or of the investment manager's delegates;

- the percentage of such transactions in value to the total transactions in value of the fund during the year;

- the total brokerage commission paid to such brokers in relation to transactions effected through them; and

- the average rate of commission effected through such broker.

iii. Details of all transactions which are outside the ordinary course of business or not on normal commercial terms entered into, during the financial year, with the investment manager of the constituent fund (including any of its delegates) or any entity in which these parties or their associates have a material interest.

iv. Name of the investment manager of the constituent fund (including any of its delegates) or any associates of such company if any of them becomes entitled to profits from management of the constituent fund and the amount of profits to which each of them becomes entitled.

v. Where the constituent fund does not have any transactions with associates of the investment manager or of its delegates during the year, a nil statement to that effect.

vi. The basis of the fee charged for the investment management of the constituent fund and the name of the investment manager of the constituent fund (including any of its delegates). In addition, where a performance fee is charged to the constituent fund, the basis of calculation and amount of performance fee charged would be separately disclosed.

b. Details of any soft commission arrangements relating to dealings in the property of the constituent fund or a nil statement if no such arrangements exist during the year.

c. State the amount of any advertising expenses, promotional expenses or commissions or brokerage fees payable to the MPF intermediaries of the registered scheme deducted from the constituent fund during the year.

d. State whether the borrowings entered into are secured or unsecured and the duration of the borrowings.

e. Details of any contingent liabilities and commitments of the constituent fund.

f. If the free negotiability of any asset is restricted by statutory or contractual requirements, this would be stated.

g. Defined contribution schemes

i. For a defined contribution scheme, the accumulated scheme benefits (aggregate past service liability) will normally be the amount shown as the balance of the capital account at the financial year end.

ii. The aggregate vested liability of a defined contribution scheme at the financial year end would be disclosed in a note to the financial statements.

h. Defined benefit schemes

i. The note to the financial statements referring to the aggregate past service liability of a defined benefit scheme would include the following:

- the name of the actuary of the scheme and his professional qualifications;

- a short statement regarding the main assumptions used by the actuary in determining the accumulated scheme benefits (past service liability) of the scheme. This disclosure would include assumptions such as those relating to salary increases, life expectancy of members and investment returns;

- a statement to the effect that the use of such actuarial assumptions gives rise to a figure that may not be directly comparable with the basis of valuation of net assets available for benefits which have been presented in accordance with generally accepted accounting principles in Hong Kong;

- where, in the opinion of the actuary, the assets of the scheme were not sufficient to meet its aggregate vested liability and/or its aggregate past service liability at the date of the actuarial review, the recommended funding rate and funding period(s) required to ensure that the assets of the scheme will be sufficient to meet its aggregate vested and/or aggregate past service liabilities, would be disclosed;

- the date as at which the actuary carried out his review;

- if the aggregate past service liability was not calculated as at the same date as the financial year end of the scheme, a note would be added to emphasise this fact; such a note might take the following form:

  "The aggregate past service liability was last calculated by the actuary of the scheme [name] as at [date]. The net assets available for benefits as shown on page [ ] of these financial statements are stated as at [date]. In considering these two figures, it should be borne in mind that changes in membership, contributions and other circumstances of the scheme between those dates will mean that these two figures are not comparable."

ii. The aggregate vested liability of a defined benefit scheme, as calculated by the actuary of the scheme, would be disclosed in a note to the financial statements. This note would state the date as at which the aggregate vested liability was calculated and, if that date was different from the financial year end of the scheme, a statement similar to that indicated in sub-paragraph (i) above would also be included. It may also be appropriate, in some circumstances, to refer to the information contained in sub-paragraph (i) above.

Part 5 - Notes on legal requirements in Hong Kong

83. MPF schemes are governed by the MPFSO and ORSO schemes are governed by the ORSO. The following paragraphs, based on the MPFSO and ORSO in effect at 31 May 2001, are for guidance only and are not a substitute for reference to the detailed requirements of the MPFSO and the ORSO.

MPFSO

84. Section 81 of Mandatory Provident Fund Schemes (General) Regulation ("General Regulation") provides that the approved trustee of a registered scheme must prepare a balance sheet of the scheme showing a true and fair view of its financial position and also a statement of account of the scheme showing a true and fair view of its financial transactions, for each of its financial periods.

85. Section 86 of the General Regulation provides that the approved trustee of a registered scheme must prepare a scheme report for the scheme for each of its financial periods.

86. Section 87 of the General Regulation provides that the approved trustee of a registered scheme must prepare an investment report of the scheme for each of its financial periods.

87. The financial statements, the auditor's report thereon, the scheme report and the investment report form part of the consolidated report prescribed under section 89 of the General Regulation. Section 110(3)(a) of the General Regulation stipulates that the consolidated report must be included in the annual statement prescribed under section 22A(1) of the MPFSO.

88. Guideline II.4 on Annual Statements of Registered Schemes prescribes:

a. the statistical information in relation to a registered scheme under section 110(2)(d) of the General Regulation; and

b. the information in relation to the constituent funds of a registered scheme which should be included in the financial statements and the investment report of the scheme under sections 81 and 87 of the General Regulation respectively.

89. An MPF scheme, whether employer sponsored, master trust or industry scheme, may consist of one or more constituent funds. Section 6 of Schedule 1 to the General Regulation provides that the assets of a constituent fund of a registered scheme may be invested in an approved pooled investment fund ("APIF"). Section 6(1) of the General Regulation provides that an investment fund is an APIF for the purposes of the Regulation if it is an insurance policy, authorized unit trust or authorized mutual fund that complies with the requirements set out in section 17(2) of Schedule 1 to the General Regulation and is approved by the MPFA. Section 17(2)(h) of Schedule 1 to the General Regulation stipulates that the financial statements, investment reports and auditor's reports of an APIF must be lodged with the MPFA and additional information relating to those statements and reports must be provided to the MPFA whenever the MPFA requests.

ORSO

90. Section 20(1)(a) of the ORSO requires the administrator of a registered scheme to keep proper accounts and records as regards all assets, liabilities and financial transactions of the scheme and to cause to be prepared financial statements in respect of each financial year.

91. Section 20(2) of the ORSO requires that the financial statements shall show a true and fair view of the financial transactions of the scheme during the financial year and of the disposition, at the last day of the financial year, of its assets and liabilities and shall contain any such other information as the Registrar of Occupational Retirement Schemes may specify in guidelines issued by him.

92. Under section 67(1C) of the ORSO,

a. "grouping of companies" means companies that are associated companies or are within a group of companies and includes associated companies of a member of a group of companies;

b. "group of companies" means a holding company and its subsidiaries;

c. companies are regarded as being associated companies if -

i. one of the companies holds, or is entitled to control the exercise of, 20% or more of the voting power in the other company's general meetings;

ii. one of the companies is a subsidiary of an associated company; or

iii. they are partners under a written partnership agreement.

93. For schemes participating in a pooling agreement, financial statements of each of the schemes, rather than the pooling agreement itself, would be prepared. Section 20(7C)(a) of the ORSO requires the appointment of a common accounting year for each of the schemes within the pooling agreement. Financial statements of such schemes would be prepared on the basis of the appointed common accounting year unless exemption has been given by the Registrar of Occupational Retirement Schemes under section 20(7C) of the ORSO.

Appendix
Annual report of a retirement scheme

This appendix does not form part of the Guideline and is included for illustrative purposes only. The contents of the reports below may not contain all the statutory requirements of the MPFSO and the ORSO. You are advised to refer to the MPFSO, the ORSO and the General Regulation for the detailed requirements.

Introduction

A.1 In some cases, the trustees/administrator of a retirement scheme may choose to present an annual report (in addition to the audited financial statements and the actuary's certificate) to provide scheme members with further information about its investment performance and financial position. Some of the principal features commonly found in such reports, where they are prepared, are set out in the paragraphs below.

For MPF schemes, the General Regulation requires a scheme report and an investment report to be prepared for each financial period. Section 86 of the General Regulation includes specific disclosure requirements for a scheme report. Section 87 of the General Regulation includes specific disclosure requirements for an investment report.

Trustees' (or Administrator's) report

A.2 The trustees' or administrator's report will commonly include a general description of the scheme, and a review of or comment on the following:

a. the names of the employers and the employee groups covered;

b. the number of members of the scheme, including individuals receiving benefits under the scheme;

c. the type of scheme - defined benefit or defined contribution;

d. the scheme arrangement - governed by trust or regulated by insurance arrangement and whether or not participating in a pooling arrangement;

e. a note as to the funding arrangements by employers and employees;

f. a commentary on the financial development of the scheme as disclosed in the financial statements;

g. a commentary on the actuarial position of the scheme as disclosed in the actuary's certificate in the case of defined benefit schemes;

h. a commentary on the investment criteria and performance of the scheme, including details of investment management responsibilities by the trustees or administrator; and

i. details of significant changes in items (a) to (h) during the period covered by the report.

It is not uncommon to refer to other documents that are readily available to users and in which the scheme is described and to include in the report only information on subsequent changes.

Investment report

A.3 The annual report would also include a detailed investment report which contains a greater analysis of the investment portfolio and returns than is disclosed in the financial statements. The preparation of an investment report is a requirement under the MPFSO, and the investment portfolio information is to be given for each constituent fund of an MPF scheme. Where such an investment report is prepared, it will often include the following:

Investment portfolio

a. number or quantity of each holding together with the description;

b. the market value of each holding:

   i. in the case of equities and warrants, categorized by country; and

   ii. in the case of debt securities and convertible debt securities, categorized by currency denomination;

c. the value of each holding as a percentage of the total net asset value;

d. the total investment stated at cost;

e. statement of movements in portfolio holdings since the end of the preceding year of the registered scheme. The trustees are expected to choose the most appropriate illustration of portfolio holdings taking into account the objective and nature of the fund. Any one of the following methods may be considered acceptable to the MPFA:

   i. detailed holdings in individual securities;

   ii. holdings in different sectors of a particular market;

   iii. holdings in different countries (in the case of, for example, a global equity fund); or

   iv. holdings in various kinds of securities such as equities, bonds, warrants and options etc. (in the case of diversified fund),

   except for (i) above, movements in portfolio holdings can be expressed in percentages;

f. details of the ten largest investments (which would include a description of the nature of the investment);

g. details of any investments which represent 10% or more of any class of shares of any company; and

h. details of the extent to which properties (if any) are subject to rent reviews.

Where an investment report is prepared, the totals shown are normally reconciled to the amounts shown in the statement of assets and liabilities.

Performance table

a. a comprehensive table covering the last 3 financial years and including, for each financial year, at the end of the financial year:

   i. the total net asset value; and

   ii. the net asset value per unit for unitised fund; and

b. a performance record over the last 10 financial years, or if the fund has not been in existence during the whole of that period, over the whole period in which it has been in existence, showing:

   i. the highest issue price and the lowest redemption price of the units during each of those years for unitised fund; and

   ii. the net annualized investment return (percentage change in unit price for unitised fund and the declared investment return for non-unitised fund) during each of those years.