

BY HAND

Companies Bill Team
Financial Services and the Treasury Bureau
15/F, Queensway Government Offices
66 Queensway
Hong Kong

16th January 2012

Dear Sirs

Companies Bill – Consultation on the Qualifying Criteria for Private Companies to Prepare Simplified Financial and Directors’ Reports (the “Consultation”)

Ernst & Young is pleased to comment on the above Consultation.

Currently, the proposal in the Companies Bill (“the CB”) is that a private company or group (subject to certain exceptions) would be able to adopt the more simplified financial reporting covered by the Reporting Exemption in the CB and the Small and Medium-Sized Entity Financial Reporting Framework (and the related standard) (“the SME-FRF”) issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”), if certain size threshold criteria are met (Option 1 in the Consultation). The criteria included in Schedule 3 to the CB in respect of the Reporting Exemption are currently consistent with the criteria in the SME-FRF.

To address concerns that the current proposal in the CB will exclude larger private companies or groups from adopting simplified financial reporting, the Consultation addresses whether the scope for entities able to adopt simplified financial reporting in the CB should be extended to allow:

- a. Larger private companies/groups that are outside the threshold limits to adopt simplified reporting if at least 75% of members agree (with no members objecting) (Option 2 in the Consultation); or,
- b. Larger private companies/groups to adopt simplified reporting if not exceeding size criteria (to be determined) and at least 75% of members agree (with no members objecting) (Option 3 in the Consultation).

In our response of 6th August 2010 to the Second Phase Consultation on the draft Companies Bill (which at that time also proposed a similar approach to Option 2 above), we expressed concerns that larger private entities that do not meet the size criteria in the SME-FRF may have a broader range of stakeholders than smaller private entities, and so the SME-FRF may not be the most

appropriate framework for their needs and that the HKFRS for Private Entities will be the most appropriate accounting standard for the larger private entities, should they not wish to adopt the full HKFRSs. Therefore, we recommended restricting the SME-FRF to those entities that meet the size criteria only.

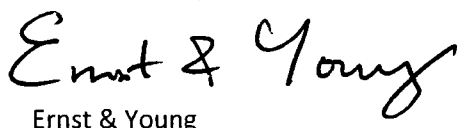
As noted above, the Consultation also introduces a new proposal (Option 3), which is a hybrid of Options 1 and 2, by proposing a threshold (which for revenue and assets would be higher than the threshold for the smaller private companies/groups), together with obtaining a shareholders' mandate. Whilst we are supportive of there being size criteria, we consider that also requiring an explicit agreement from the shareholders should not be necessary, as in any event even should the size criteria be met, the use of the SME-FRF framework will not be mandatory and entities will be able to adopt either the accounting standard for larger private entities or the full HKFRSs. In the absence of including a shareholders' mandate in Option 3, having different size criteria only becomes relevant when there is a distinction between the types of entities already covered in the SME-FRF criteria (for example, different size criteria for companies and groups). However, in light of the recent consultation exercise of the HKICPA (see below), we do not consider it necessary to introduce different size criteria for different categories of entities in the CB.

As noted in the Consultation, the HKICPA has currently issued a consultation paper on relaxing the SME-FRF size criteria ("the HKICPA consultation"). Should the proposals in the HKICPA consultation be adopted, the number of entities that would be able to adopt simplified accounting will significantly increase and this would help to address concerns about the scope of entities covered by the current criteria when adopting the SME-FRF being too narrow. The proposed criteria in the HKICPA consultation apply to both private companies and groups.

Whilst, in general, we are supportive of the objective of the Consultation to broaden the scope for entities able to adopt simplified financial reporting, we consider that this would be more appropriately achieved through increasing the thresholds in the SME-FRF itself (with a corresponding change to Schedule 3), rather than creating additional exemptions in the CB. Therefore, in light of the HKICPA consultation and the proposed relaxation of the criteria in the SME-FRF, we consider that Option 1 in the Consultation will be the most appropriate approach (i.e., no change to the proposal in the CB).

We shall be pleased to further discuss our comments with you at your convenience. For this purpose, please do not hesitate to contact Mr. Tommy Fung or Mr. Paul Hebditch.

Yours faithfully


Ernst & Young