

Hong Kong Company Reporting Exemption Guideline Note

For each financial year, the directors of a Hong Kong company must prepare financial statements and the financial statements must be audited. If the company is a holding company, it must prepare consolidated financial statements and include all subsidiary undertakings, including overseas subsidiaries. The generally applicable financial reporting standards are the HKFRS which are modelled after the IFRS.

The accounting standards to be adopted in the preparation of financial statements include HKFRS, HKFRS for Private Entities, SME-FRF & SME-FRS, Hong Kong Accounting Standards (HKAS) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants, are collectively called Hong Kong Financial Reporting Standards (HKFRS). HKFRS is virtually identical to IFRS Standards.

In accordance with the Companies Ordinance, a small company or small guarantee company, a company which is not a member of a group of company and a company which is an eligible private company (or a group of eligible private companies) and having sufficient shareholder support is eligible to prepare financial statements under the SME-FRF & SME-FRS (Revised) for financial years beginning on or after 3 March 2014 and are qualified to prepare simplified directors' reports. This simplified reporting regime is referred to as "the reporting exemption" in the ordinance.

The SME-FRS allow for the exclusion of subsidiaries from consolidation on the basis of disproportion of expense and delay to the value to members. This exclusion is in addition to the exclusions mentioned in the Companies Ordinance.

It should however be noted that the reporting exemption does not exempt companies from the preparation of financial statements or the audit requirement altogether, but rather means that certain information otherwise required to be disclosed in the financial statements will not be required in this instance.

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1. Preparation of Financial Statements

In accordance with the requirements of the Hong Kong Companies Ordinance, companies incorporated in Hong Kong must maintain proper accounting records, prepare financial statements annually and arrange to have the financial statements audited.

The provisions of the Companies Ordinance in respect of the preparation of financial statements are reproduced and shown in Schedule 1.

A FAQ regarding preparation of financial statements illustrated by the Companies Registry in its official website is reproduced and shown in Schedule 2.

Particularly, the directors of a Hong Kong registered company must prepare financial statements for each financial year end according to the provisions of the Hong Kong Companies Ordinance. In the case where a company is a holding companies, it is required to prepare consolidated financial statements unless the company is a partially owned subsidiary where no member requests for the preparation of consolidated accounts or all the members agree in writing to not prepare consolidated financial statements.

A company that is required to prepare financial statements under the new CO is required by section 380(4)(b) to comply with the accounting standards applicable to the financial statements. Section 380(8) of the CO defines “Accounting standards” as being those issued or specified by the HKICPA (as per the Companies (Accounting Standards (Prescribed Body)) Regulation).

2. Reporting Exemption

Hong Kong accounting standards, or Hong Kong Financial Reporting Standards (HKFRS) refer to a set of accounting rules set out by the Hong Kong Institute of Certified Public Accountants (HKICPA). This framework follows the Financial Reporting Standards (FRS), which has been applied in Hong Kong since January 2005. The FRS model is based upon the International Financial Reporting Standards (IFRS) under the International Accounting Standards Board (IASB).

Companies which meet the criteria set out under section 359 of the Companies Ordinance (“CO”) are eligible to prepare financial statements under the SME-FRF & SME-FRS (Revised) for financial years beginning on or after 3 March 2014 and are qualified to prepare simplified directors’ reports. This simplified reporting regime is referred to as “the reporting exemption” in the ordinance.

The following companies which are not engaged in those regulated business as listed in section 359(4) of the CO are eligible for this reporting exemption without taking any further action:

- (1) A small private company or small guarantee company;
- (2) The company is a private company which does not have any subsidiaries and is not a subsidiary of another Hong Kong incorporated company and has full shareholder support every financial year (section 359(1)(b));
- (3) The company is an eligible private company (or a group of eligible private companies) and gaining sufficient shareholder support (section 359(1)(c) and section 359(2)(c)(ii)).

2. Types of company are not eligible for the reporting exemption

The following types of company are not eligible for the reporting exemption under the CO and so are not permitted to prepare their financial statements in accordance with SME-FRF & SME-FRS:

- (1) companies that are authorized under the Banking Ordinance to carry out banking business;
- (2) companies that accept, by way of trade or business (other than banking business), loans of money at interest or repayable at a premium, other than on terms involving the issue of debentures or other securities;
- (3) companies that are licensed under Part V of the Securities and Futures Ordinance to carry on a regulated business; or
- (4) companies that carry on any insurance business, other than solely as an agent, and money lending business.

Groups which contain such companies are also not eligible for the reporting exemption and so cannot prepare consolidated financial statements under the SME-FRF and SME-FRS.

3. Eligibility for Application of FRS SME

- (1) Eligible private company

The private company must not exceed any two of the following:

- (a) Total annual revenue of HKD100 million
- (b) Total assets of HKD100 million at the end of the reporting period
- (c) 100 employees

Where a private company does not meet the criteria listed above but meets any two of the following conditions, it is still eligible to prepare its financial statements in accordance with SME-FRF and SME-FRS with approval from members:

- (a) Total annual revenue not more than HKD200 million
- (b) Total assets of not more than HKD200 million at the end of the reporting period
- (c) 200 employees

In that case, at least 75% of the voting rights must pass a resolution at a general meeting that the company is to fall within the reporting exemption for the financial year, with none objecting either at the meeting or otherwise in writing.

The resolution is defeated if any member objects either at the meeting or at any time by giving notice in writing to the company, provided that written notice is given at least 6 months before the end of the financial year to which the objection relates.

Alternatively, the company may pass a written resolution under section 548(1), which can be passed without a meeting and without any previous notice being required, for falling within the reporting exemption. A written resolution is passed when all eligible members have signified their agreement to it (section 556(a)).

(2) Group of eligible private companies

- (a) Each company in the group must meet either the size test of small private company or larger "eligible" private company; and
- (b) The aggregate amounts for the group in total must not exceed 2 out of 3 of the size tests for larger "eligible" private companies.

All the companies in the group individually, as well as the parent of the group, must have obtained the necessary shareholder approval (except for those subsidiaries within the group that fall within the "small private company" category).

(3) Eligible guarantee companies

The total annual revenue of the small company limited by guarantee must not exceed HKD25 million. Where it is a group:

- (a) Each company in the group must qualify as a small company limited by guarantee; and
- (b) The aggregate annual revenue of the group must not exceed HK\$25 million.

Approval from members is not required under the Companies Ordinance.

The below table summarises the various tests to qualify for simplified reporting:

Criteria	Small private company or group	Small guarantee company or group	Larger private company or group
Total Revenue	Not more than HKD100 million	Not more than HKD25 million	Not more than HKD200 million
Total Assets	Not more than HKD100 million	N/A	Not more than HKD200 million
Number of Employees	Not more than 100	N/A	Not more than 200
Shareholder Approval	Not required	Not required	Required (75%, with no objections)

Note 1: Must satisfy two out of the three quantitative tests for annual revenue, total assets and employees.

For the purposes of the size tests, the total revenue and total assets are those stated in the annual financial statements. In the case where the reporting period is shorter or longer than a year, the amount of total revenue for a financial year is to be calculated on a pro-rata basis as if the length of the financial year were 12 months. For example,

The aggregate total annual revenue and aggregate total assets are calculated after eliminating intragroup transactions and balances.

The number of employees is the average number of persons employed by the entity during the reporting period (irrespective of whether in full-time or part-time employment) and is arrived at by adding the number of employees at the end of each calendar month and divided by the number of months in the reporting period.

In general, a company will have to pass the size tests for two consecutive years in order to become eligible in the 3rd year. Similarly a company would generally have to fail the tests for two consecutive years in order to become ineligible in the 3rd year. However, there are specific transitional rules in this regard which apply in any year in which a group acquires a new subsidiary.

4. Non-Hong Kong Companies

Subject to any specific requirements imposed by the law of the company's place of incorporation and subject to its constitution, these companies qualify for reporting under the SME-FRF & SME-FRS (Revised) when they meet the same requirements that a Hong Kong incorporated company is required to meet under section 359 of the new Companies Ordinance.

Also, Practice Note (PN) 900 Revised issued by the HKICPA stipulates that:

- (1) Groups which include non-Hong Kong body corporates are eligible for the reporting exemption, and hence the use of Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard for financial reporting if they meet the qualifying criteria for the reporting exemption; and
- (2) A partially owned subsidiary of an entity can now be exempted from preparing consolidated financial statements if all members agree in writing before the end of the financial year.

5. Exemptions

The exemptions are set out in the following:

- (1) no requirement to disclose in the directors' report the following:
 - (a) business review (Section 388(3)(a))
 - (b) directors' interests in arrangements to enable directors to acquire benefits by the acquisition of shares or debentures (Section 3(3A) of Companies (Directors' Report) Regulation.
 - (c) donations (Section 4(3) of Companies (Directors' Report) Regulation.
 - (d) directors' reasons for resignation or refusal to stand for re-election (Section 8(3) of Companies (Directors' Report) Regulation.
 - (e) material interests of directors in transactions, arrangements or contracts of significance entered into by a specified undertaking of the company (Section 10(7) of Companies (Directors' Report) Regulation.
- (2) no requirement for financial statements to give a "true and fair view" (Section 380(7))
- (3) no requirement for auditor to express a "true and fair view" opinion on the financial statements (Section 406(1)(b))
- (4) no requirement to disclose auditor's remuneration in financial statements (Section 380(3) and Schedule 4 Part 2)
- (5) subsidiary undertakings may be excluded from consolidated financial statements in accordance with applicable accounting standards (Section 381(2))
- (6) no requirement to disclose in the notes to financial statements the material interests of directors in transactions, arrangements or contracts of significance entered into by the company (Section 23 of Companies (Disclosure of Information about Benefits of Directors) Regulation.

If an eligible company does not follow the SME-FRF and SME-FRS, then it must prepare financial statements which comply with another body of accounting standards issued or specified by the HKICPA, for example full HKFRSs, which is a body of accounting standards intended to give a true and fair view if properly complied with.

Schedule 1 : Extract of Companies Ordinance (CAP 622)

Sec.	Provision
367	Financial year
	<p>(1) A company's first financial year after the coming into operation of this section begins on the first day of its first accounting reference period and ends on— (<i>Amended 35 of 2018 s. 39</i>)</p> <p>(a) subject to paragraph (b), the last day of that period; or</p> <p>(b) another date, within 7 days before, or after, the end of that period, as specified by the directors. (<i>Amended 35 of 2018 s. 39</i>)</p> <p>(2) Every subsequent financial year of a company begins on the date immediately following the end of the previous financial year and ends on— (<i>Amended 35 of 2018 s. 39</i>)</p> <p>(a) subject to paragraph (b), the last day of the accounting reference period immediately following the one by reference to which the previous financial year is determined; or</p> <p>(b) another date, within 7 days before, or after, the end of that period, as specified by the directors. (<i>Amended 35 of 2018 s. 39</i>)</p> <p>(3) If an undertaking is not a company, a reference in this Ordinance to its financial year is a reference to a period in respect of which a profit and loss account of the undertaking is required, by its constitution or by the law under which it is established, to be made up, whether or not the period is a year.</p> <p>(4) A company's directors must secure that the financial year of each of its subsidiary undertakings coincides with the company's financial year unless, in the directors' opinion, there are good reasons against those financial years coinciding with each other.</p> <p>(5) In this section—</p> <p>undertaking (企業) means—</p> <p>(a) a body corporate;</p> <p>(b) a partnership; or</p> <p>(c) an unincorporated association carrying on a trade or business, whether for profit or not.</p>
373	Company must keep accounting records
	<p>(1) A company must keep accounting records that comply with subsections (2) and (3).</p> <p>(2) The accounting records must be sufficient—</p> <p>(a) to show and explain the company's transactions;</p> <p>(b) to disclose with reasonable accuracy, at any time, the company's financial position and financial performance; and</p> <p>(c) to enable the directors to ensure that the financial statements comply with this Ordinance.</p> <p>(3) In particular, the accounting records must contain—</p> <p>(a) daily entries of all sums of money received and expended by the company, and the matters in respect of which the receipt and expenditure takes place; and</p> <p>(b) a record of the company's assets and liabilities.</p>

373	Company must keep accounting records-cont'd
	<p>(4) If subsection (1) does not apply in relation to a subsidiary undertaking of a company, the company must take all reasonable steps to secure that the subsidiary undertaking keeps accounting records that are sufficient to enable the company's directors to ensure that any financial statements required to be prepared under Subdivision 3 of Division 4 comply with this Ordinance.</p> <p>(5) A director of a company who fails to take all reasonable steps to secure compliance with subsection (1) or (4) commits an offence and is liable to a fine of \$300,000.</p> <p>(6) A director of a company who wilfully fails to take all reasonable steps to secure compliance with subsection (1) or (4) commits an offence and is liable to a fine of \$300,000 and to imprisonment for 12 months.</p> <p>(7) If a person is charged with an offence under subsection (5), it is a defence to establish that the person had reasonable grounds to believe, and did believe, that a competent and reliable person—</p> <p>(a) was charged with the duty of ensuring that subsection (1) or (4) (as the case may be) was complied with; and</p> <p>(b) was in a position to discharge that duty.</p>
379	Directors must prepare financial statements
	<p>(1) Subject to subsection (2), a company's directors must prepare for each financial year statements that comply with sections 380 and 383.</p> <p>(2) Subject to subsection (3A), if the company is a holding company at the end of the financial year, the directors must instead prepare for the financial year consolidated statements that comply with sections 380, 381 and 383.</p> <p>(3) Subsection (3A) applies— (<i>Amended 35 of 2018 s. 42</i>)</p> <p>(a) if the company is a wholly owned subsidiary of another body corporate at the end of the financial year;</p> <p>(b) if—</p> <p>(i) the company is a partially owned subsidiary of another body corporate at the end of the financial year;</p> <p>(ii) at least 6 months before the end of the financial year, the directors notify the members in writing of the directors' intention not to prepare consolidated statements for the financial year, and the notification does not relate to any other financial year; and</p> <p>(iii) as at a date falling 3 months before the end of the financial year, no member has responded to the notification by giving the directors a written request for the preparation of consolidated statements for the financial year; or</p> <p>(c) if—</p> <p>(i) the company is a partially owned subsidiary of another body corporate at the end of the financial year; and</p> <p>(ii) all members agree in writing before the end of the financial year that consolidated statements will not be prepared for the financial year, and the agreement does not relate to any other financial year. (<i>Added 35 of 2018 s. 42</i>)</p> <p>(3A) If this subsection applies because of—</p> <p>(a) subsection (3)(a)—the directors must prepare for the financial year—</p> <p>(i) statements that comply with sections 380 and 383; or</p> <p>(ii) consolidated statements that comply with sections 380, 381 and 383; or</p>

379	<i>Directors must prepare financial statements-cont'd</i>
	<p>(b) subsection (3)(b) or (c)—the directors must prepare for the financial year statements that comply with sections 380 and 383. <i>(Added 35 of 2018 s. 42)</i></p> <p>(4) If, as respects any financial statements a copy of which is laid before a company in general meeting under section 429, or sent to a member under section 430 or otherwise circulated, published or issued by the company, a director of the company fails to take all reasonable steps to secure compliance with subsection (1), (2) or (3A), the director commits an offence and is liable to a fine of \$300,000.</p> <p>(5) If, as respects any financial statements a copy of which is laid before a company in general meeting under section 429, or sent to a member under section 430 or otherwise circulated, published or issued by the company, a director of the company wilfully fails to take all reasonable steps to secure compliance with subsection (1), (2) or (3A), the director commits an offence and is liable to a fine of \$300,000 and to imprisonment for 12 months.</p> <p>(6) If a person is charged with an offence under subsection (4), it is a defence to establish that the person had reasonable grounds to believe, and did believe, that a competent and reliable person—</p> <p>(a) was charged with the duty of ensuring that subsection (1), (2) or (3A) (as the case may be) was complied with; and</p> <p>(b) was in a position to discharge that duty. <i>(Amended 35 of 2018 s. 42)</i></p>
394	Auditor must be appointed for each financial year
	<p>(1) An auditor must be appointed for each financial year of a company.</p> <p>(2) An auditor may be appointed only under this Subdivision.</p>
395	Appointment of first auditor by directors
	<p>(1) This section applies to—</p> <p>(a) a company formed and registered under this Ordinance; and</p> <p>(b) a company formed and registered under a provision of the predecessor Ordinance having a continuing effect under Schedule 11 or by virtue of section 23 of the Interpretation and General Clauses Ordinance (Cap. 1).</p> <p>(2) If the company is required to hold an annual general meeting in accordance with section 610 in respect of its first financial year, the directors may appoint the auditor of the company for that first financial year at any time before the annual general meeting.</p> <p>(3) If, by virtue of section 612(1) or (2), the company is not required to hold an annual general meeting in accordance with section 610 in respect of its first financial year, the directors may appoint the auditor of the company for that first financial year at any time before the appointment period in relation to the next financial year.</p>
405	Auditor's duty to report
	A company's auditor must prepare a report for the members on any financial statements prepared by the directors, a copy of which is laid before the company in general meeting under section 429, or is sent to a member under section 430 or otherwise circulated, published or issued by the company, during the auditor's term of office.

Schedule 2: Extract of FAQ Illustration by Companies Registry

No.	(III) Financial Statement and Report
11	What are the general requirements for financial statement under the new CO?
	<p>The general requirements are –</p> <ul style="list-style-type: none"> • a company's directors must prepare for each financial year financial statements that comply with sections 380 and 383 (<i>section 379(1)</i>); • if the company is a holding company at the end of the financial year, consolidated financial statements must be prepared instead unless the company is a partially owned subsidiary where no member requests for the preparation of consolidated financial statements or all members agree in writing that consolidated financial statements will not be prepared (<i>sections 379(2), 379(3)(b) and (c) and 379(3A)(b)</i>); • if the company is a partially owned subsidiary where no member requests for the preparation of consolidated financial statements or all members agree in writing that consolidated financial statements will not be prepared, company level financial statements must be prepared (<i>section 379(1), 379(3)(b) and (c) and 379(3A)(b)</i>); • if the company is a wholly owned subsidiary, either company level financial statements or consolidated financial statements must be prepared (<i>section 379(3)(a) and 379(3A)(a)</i>); • subject to permitted exclusions, the consolidated financial statements must include all the subsidiary undertakings of the company (<i>section 381</i>); • unless the company falls within the reporting exemption, the financial statements must give a true and fair view of the financial position and financial performance of the company (<i>sections 380(1), (2) and (7)</i>); • the financial statements must comply with – <ul style="list-style-type: none"> o the accounting disclosure requirement in Schedule 4 (<i>section 380(3)</i>); o applicable accounting standards issued or specified by the Hong Kong Institute of Certified Public Accountants ("HKICPA") (<i>sections 357(1), 380(4) and the Companies (Accounting Standards (Prescribed Body) Regulation, Cap. 622C</i>); • the notes to financial statements must contain the information prescribed by the Companies (Disclosure of Information about Benefits of Directors) Regulation, Cap. 622G ("Cap. 622G") (<i>section 383</i>); and • THE FINANCIAL STATEMENTS MUST BE AUDITED (SECTION 405). <p>Other requirements are in relation to the laying, sending, publication (<i>sections 429 to 432 and 436</i>) and voluntary revision of financial statements (<i>section 449 and the Companies (Revision of Financial Statements and Reports) Regulation, Cap. 622F</i>).</p> <p>The above requirements do not apply to a company that is dormant (<i>section 447</i>).</p> <p><i>Companies Registry - FAQ - Companies Ordinance - Accounts and Audit (cr.gov.hk)</i></p>

If you wish to obtain more information or assistance, please visit our official website at www.kaizencpa.com or contact us through the following:

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