



25 November 2016

To: **Members of the Hong Kong Institute of CPAs**
All other interested parties

**INVITATION TO COMMENT
ON EXPOSURE DRAFT OF REVISED ACCOUNTING BULLETIN 3
GUIDANCE ON DISCLOSURE OF DIRECTORS' REMUNERATION**

Comments to be received by 24 January 2017

The Financial Reporting Standards Committee (FRSC) of the Hong Kong Institute of Certified Public Accountants (Institute) is seeking comments on the Exposure Draft of Accounting Bulletin 3. You may access the Exposure Draft from the Institute's website: <http://www.hkicpa.org.hk/en/standards-and-regulations/standards/financial-reporting/exposure-drafts/>

The new Hong Kong Companies Ordinance, Cap. 622 (CO) has been effective since 3 March 2014. Section 383 of the new CO requires that the financial statements of a company incorporated in Hong Kong contain, in the notes to the financial statements, the information prescribed by Companies (Disclosure of Information about Benefits of Directors) Regulation, Cap. 622G (the Regulation) in relation to the following:

- (a) directors' emoluments;
- (b) directors' retirement benefits;
- (c) payments made or benefit provided in respect of the termination of the service of directors; and
- (d) consideration provided to or receivable by third parties for making available the services of a person as director.

Many of the requirements of the Regulation have been brought forward from section 161 of the predecessor Companies Ordinance, Cap. 32. However, the Regulation clarified, and in some cases broadened, the scope of the requirements.

In January 2000, Accounting Bulletin 3 was prepared and issued by the Institute to provide general guidance on the requirements concerning the disclosure as set out in the predecessor Companies Ordinance. It also provided general guidance on common practical issues encountered in preparing the required information.

Accounting Bulletin 3 has been revised for section 383 of the new CO and the Regulation, but it does not distinguish between whether any requirement is a new requirement introduced by the Regulation or is a requirement derived from the predecessor Companies Ordinance.

In accordance with the Institute's due process, comments on revised Accounting Bulletin 3 are invited from any interested parties. The FRSC would like to hear from both those who agree and those who do not agree with the guidance contained in the revised Bulletin. Comments should be supported by specific reasoning and should be submitted in written form.

Any comments should be submitted to the Institute on or before **24 January 2017**.



Comments may be sent by mail, fax or e-mail to:

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Comments will be acknowledged and may be made available for public review unless otherwise requested by the respondent.



25 November 2016
Exposure Draft

Response Due Date
24 January 2017

Exposure Draft of Accounting Bulletin 3

Guidance on Disclosure of Directors' Remuneration

CONTENTS

Exposure Draft of Guidance on Disclosure of Directors' remuneration

The Exposure Draft can also be found on the Institute's website at:
<http://www.hkicpa.org.hk/en/standards-and-regulations/standards/financial-reporting/exposure-drafts/>

Accounting Bulletin 3

Guidance on Disclosure of Directors' Remuneration

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ACCOUNTING BULLETIN 3 GUIDANCE ON DISCLOSURE OF DIRECTORS' REMUNERATION

(Revised in [] 2017)

Accounting Bulletins reflect the views of the Financial Reporting Standards Committee on subjects of topical interest. They are intended to assist members or to stimulate debate on important accounting issues. They do not have the authority as either Accounting Standards or Accounting Guidelines.

This Accounting Bulletin supersedes Accounting Bulletin 3 issued in January 2000. It provides general guidance on the requirements of the Hong Kong Companies Ordinance Cap. 622 and Companies (Disclosure of Information about Benefits of Directors) Regulation Cap. 622G with respect to the disclosure of directors' remuneration in notes to the financial statements. It does not introduce additional accounting, disclosure or legal requirements. This Accounting Bulletin has been developed in consultation with Companies Registry in so far as the provisions in Cap. 622 and Cap. 622G are concerned. However, users of this Accounting Bulletin should consider taking their own legal advice if in doubt as to their obligations under the Hong Kong Companies Ordinance as the HKICPA and the authors do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this Accounting Bulletin, whether such loss is caused by negligence or otherwise.

CONTENTS

	Paragraphs
INTRODUCTION.....	1 - 4
STATUTORY AND OTHER REQUIREMENTS.....	5 - 23
General requirements.....	5 - 15
Supplementary provisions in the Regulation.....	16
Auditor's responsibilities under section 407(4) of the Companies Ordinance	17 - 18
Listed companies in Hong Kong.....	19 - 23
PRACTICAL ISSUES.....	24 - 65
An employee acting as an alternate director.....	24 - 25
A person is a director for only part of a financial year.....	26 - 27
A company is a subsidiary undertaking for only part of a financial year	28 - 29
Other matters relating to timing of disclosure.....	30 - 34
Consideration provided to or receivable by third parties or making available the director's services.....	35 - 37
Distinguishing between services 'as a director' and 'otherwise in connection with the management of the affairs'.....	38 - 42
Apportioning payments between holding company and subsidiary undertakings..	43 - 53
Expenses allowance.....	54
Guidance on valuing and disclosing benefits in kind.....	55 - 61
Presentation in the financial statements.....	62 - 65
APPENDIX: EXAMPLES OF DISCLOSURES IN NOTES TO FINANCIAL STATEMENTS	

INTRODUCTION

1. Section 383 of the new Hong Kong Companies Ordinance, Cap. 622 (CO) requires that the financial statements of a company incorporated in Hong Kong must contain, in the notes to the financial statements, the information prescribed by Companies (Disclosure of Information about Benefits of Directors) Regulation, Cap. 622G (the Regulation) in relation to the following¹:
 - (a) directors' emoluments;
 - (b) directors' retirement benefits;
 - (c) payments made or benefit provided in respect of the termination of the service of directors; and
 - (d) consideration provided to or receivable by third parties for making available the services of a person as director.
2. This Accounting Bulletin is prepared and issued by the Institute to provide general guidance on the requirements concerning the disclosure of directors' emoluments, retirement benefits, and payments in respect of termination of directors' services (collectively referred to in this Bulletin as directors' remuneration) and consideration for making available the directors' services in the notes to the financial statements, as set out in section 383 of the CO and the Regulation. This Accounting Bulletin also provides general guidance on common practical issues encountered in preparing the required information. **Hereafter, all references to sections are to sections of the Regulation unless otherwise stated.**
3. Many of the requirements of the Regulation in this area have been brought forward from section 161 of the predecessor Companies Ordinance (Cap. 32). However, the Regulation has clarified, and in some cases broadened, the scope of the requirements. This Accounting Bulletin is intended as guidance for complying with the Regulation. It therefore does not distinguish between whether any requirement is a new requirement introduced by the Regulation or is a requirement derived from the predecessor Ordinance. For further information on the changes made to the requirements in this area, reference can be made to the Briefing Notes prepared by the Companies Registry and available on its website at [http://www.cr.gov.hk/en/companies_ordinance/docs/BN-\(DIBD\)R-e.pdf](http://www.cr.gov.hk/en/companies_ordinance/docs/BN-(DIBD)R-e.pdf) .
4. The requirements of section 383 of the CO and the Regulation are effective for financial years beginning on or after 3 March 2014.²

STATUTORY AND OTHER REQUIREMENTS

General requirements

5. The disclosure requirements relating to this topic are set out in section 383 of the CO and the Regulation. These require a company to show, in the notes to the financial statements, the following information:
 - (a) the aggregate amount of **directors' emoluments** paid to or receivable by the directors of the company in respect of their qualifying services;
 - (b) the aggregate amount of **retirement benefits** paid to or receivable by the directors or former directors of the company in respect of their qualifying services;

¹ Section 383 of the CO also requires information in connection with dealings with directors and material interests of directors in transactions, arrangements or contracts that are significant in relation to the company's business to be disclosed in the notes to the financial statements (e.g. loans or quasi-loans in favour of directors, transactions, arrangements etc., such as were previously required by sections 161B and 161BA of the predecessor Companies Ordinance, Cap. 32.) These other discloseable transactions are outside the scope of this Accounting Bulletin.

² The requirements of section 161 of the predecessor Ordinance (Cap. 32) are effective for financial years beginning before that date.

- (c) the aggregate amount of the **payments or benefits in respect of termination of directors' services** made or provided to or receivable by the directors, former directors or shadow directors of the company in respect of the termination of the qualifying services of the directors, former directors or shadow directors distinguishing further into sums paid by or receivable from:-
 - (i) the company;
 - (ii) the company's subsidiary undertakings; and
 - (iii) any other person³.
 - (d) The aggregate amount of **consideration provided to or receivable by any third party** for making available the qualifying services of a person as a director of the company or in any other capacity while as director.
6. In the case of items a, b and c above, the aggregate amount is required to be distinguished between information relating to
- (a) services as (or, in the case of c, loss of the office as) a director; and
 - (b) other services in connection with the management of the affairs of the company or its subsidiary undertakings (or, in the case of c, in respect of the termination of such services).

In addition, if any of the amounts to be disclosed under a, b, c or d consists of a benefit paid otherwise than in cash, then the nature of that non-cash benefit needs to be disclosed.

Meaning of 'qualifying services'

7. 'Qualifying services' are defined in section 3(1) as:
- (a) services as a director of the company concerned; or;
 - (b) while a director of the company concerned, services as:
 - (i) a director of a subsidiary undertaking of the company concerned; or
 - (ii) other services in connection with the management of the affairs of the company concerned or its subsidiary undertaking.

The distinction in the definition between providing services 'as a director' (i.e. categories (a) and (b)(i) above) and providing services 'in connection with the management of the affairs of the company or its subsidiary undertakings' (i.e. category (b)(ii) above) is an important one for disclosure purposes, as each type of remuneration is required to be distinguished between these two broad categories. See paragraphs 38 to 42 below for further guidance on this area.

³ Section 3 of the Interpretation and General Clauses Ordinance (Cap. 1) defines 'person' to include any body of persons, corporate or unincorporated. 'Any other person' could therefore include the company's holding companies, fellow subsidiaries, associates or in fact any other company, as well as including other persons, such as natural persons or partnerships.

8. The definition of 'qualifying services' focuses on the services of a person while he or she is a director of the company which is preparing the financial statements. There is no distinction made in the Regulation between the disclosures to be made in the consolidated financial statements or company-level statements of that company. To illustrate, consider this example:

Company H has one subsidiary, company S. Mr A is a director of both company H and company S while Mr B is only a director of company S. Mr A's compensation is \$2million, \$500,000 of which relates to his services to company S, while Mr B's compensation is \$600,000. In this example the Regulation would require the following amounts to be disclosed in respect of these two individuals:

- In company H's financial statements the directors' emoluments to be disclosed are \$2 million i.e. relating only to Mr A's services to the group headed by company H. It is irrelevant whether company H is preparing consolidated or company-level financial statements: in both cases the amount to be disclosed is \$2 million. This disclosure includes the amount relating to the services that Mr A provides to company S.
- In company S's financial statements the amount of directors' emoluments to be disclosed is \$1.1 million i.e. the emoluments receivable by Mr A and Mr B for being directors of company S. The remainder of Mr A's emoluments are not discloseable by company S.

See paragraphs 28 to 29 and 43 to 53 below for further guidance on this area.

Meaning of 'subsidiary undertaking' is extended to non-controlled entities

9. Section 16 of the CO states that a reference to 'subsidiary undertaking' is to be construed in accordance with Schedule 1 of the CO. As Schedule 1 differs in certain key respects from the requirements of Hong Kong Financial Reporting Standard (HKFRS) 10 *Consolidated Financial Statements*, it is possible that the term 'subsidiary undertaking' as used in the Regulation may include entities that would not fall within the definition of a controlled 'subsidiary' under HKFRS 10. This could be the case, for example, when a company owns more than 50% of the equity shares of another company but a shareholders' agreement restricts the company's ability to exercise unilateral control. In this case the investee is a 'subsidiary undertaking' within the meaning of Schedule 1, even though for accounting purposes the investee is a joint venture or an associate, not a subsidiary.
10. Section 3(4) of the Regulation extends this definition further for the purposes of disclosure requirements for directors' remuneration set out in sections 3 to 12 of the Regulation⁴. According to sections 3(4) for this purpose, the term 'subsidiary undertaking' also includes any other undertaking, whether or not it is or was a subsidiary undertaking of the company as defined in Schedule 1 of the CO, if in relation to a person who, while a director of the company, is or was also a director of that undertaking by virtue of the company's nomination (whether direct or indirect). Section 2(c) says that a reference to an undertaking has the meaning given by section 1 of Schedule 1 of the CO i.e. a body corporate, a partnership or an unincorporated association carrying on a trade or business, whether for profit or not.

⁴ Section 3(4) refers to these sections collectively as "this Part" i.e. Part 2 of the Regulation.

11. This means that if a company has nominated one or more of its directors to sit on the boards of any of the company's investees, whether they are subsidiaries, joint ventures, associates or other investments, then any remuneration paid to or receivable by that person or persons in respect of that extra role may need to be included in the directors' remuneration disclosed by the investor company, unless the director occupies that position for reasons other than because of nomination rights held by the company. To illustrate, consider this example:

Company A has nominated one of its directors to the board of its associate, company B. Company B pays \$250,000 per year to the director in respect of his services to the company.

As the director has been nominated by company A as a director of the associate, the associate is deemed (for the purposes of directors' remuneration disclosure) to be a subsidiary undertaking. The director is performing qualifying services for company A by being its representative on company B's board. So, in this situation, the director must disclose to company A, the \$250,000 that he receives as remuneration from company B. Company A includes the \$250,000 in its aggregate disclosure of emoluments paid to or receivable by its directors in respect of their qualifying services under section 4(2) and (3)(a).

If the \$250,000 were paid directly to company A (that is, as a sum to be accounted for to the company) and not to the director personally, this amount would not be included as directors' emoluments in company A's financial statements (section 11(1)(a)). Company B should disclose the payment of \$250,000 in its own financial statements as a sum paid to a third party in respect of the director's services (section 7).

Although, nomination rights are more likely to be held where the company is an investor this may not necessarily be the case and section 3(4) applies wherever a company nominates one of its directors to be a director of any other undertaking. For example, an asset management company may nominate one of its directors to be a director of one or more of the funds, which it manages but in which it has no investment.

Details on the four categories of disclosures

<p>12. Directors' emoluments (section 4)</p>	<p>Directors' emoluments relate to amounts paid to or receivable by a person in respect of qualifying services provided during the financial year while he or she was a director of the company.</p> <p>Per section 4(6) these amounts include:</p> <ul style="list-style-type: none"> • fees, percentages, salaries and bonuses; • expense allowances (less the amounts actually spent on the expenses for which the allowances were made); • contributions paid under a retirement benefits scheme, by any person other than the director, in respect of the director; and • other benefits whether in cash or otherwise (in the case of non-cash benefits, the amount discloseable is the estimated money value of the non-cash benefit⁵) <p>but exclude any retirement benefits to which the director is entitled under any retirement benefits scheme⁶.</p> <p>Section 10(2) also states that a reference to a payment to or receivable by a director includes -</p> <ul style="list-style-type: none"> • a payment to or receivable by a connected entity of the director; and • a payment to a person made or to be made at the direction of, or for the benefit of, the director or a connected entity of the director. <p>The practical effect of section 10(2) is that when the payment directly or indirectly benefits the director or an entity connected to him (such as his family or business associates), it should be categorized as directors' emoluments and not as a payment to a third party. See paragraph 16(c) below for further guidance on this area.</p>
<p>13. Directors' retirement benefits (section 5)</p>	<p>Directors' retirement benefits relate to amounts paid to or receivable by a person in connection with their retirement as a director⁷ who earned the entitlement to the retirement benefits by providing qualifying services while he or she was a director of the company.</p> <p>Per section 3(1) this category includes</p> <ul style="list-style-type: none"> • any lump sum, allowance, gratuity, periodical payment or other like benefits, any other property, or any other benefit whether in cash or otherwise given or to be given:

⁵ See paragraphs 55 to 61 below for further guidance on this requirement.

⁶ These may be discloseable under section 5 instead. For example, where a payment is made to top up a retirement benefits scheme for a director's benefit on his retirement or the company enhanced his pension by giving the director extra years of pensionable service funded out of a surplus in the scheme. See paragraph 13 below.

⁷ Per section 3(2)(a) for the purposes of section 5 a reference to a director includes a former director.

<p>13. Directors' retirement benefits (section 5)</p> <p>(continued)</p>	<p>(i) on or after the retirement or death of the person (including any annuity or other benefit paid or payable under any insurance policy on or after the retirement or death of the person);</p> <p>(ii) in anticipation of the retirement of the person; or</p> <p>(iii) in connection with the person's service rendered before the retirement or death of that person; and</p> <ul style="list-style-type: none"> • any benefits paid or to be paid under the Mandatory Provident Fund Schemes Ordinance (Cap. 485)⁸. <p>It is clear from section 5 of the Regulation that the amount to be disclosed would include the estimated money value of any non-cash benefits. For example, if the company allowed retiring directors to retain share options which would normally lapse on leaving the company, or continued to provide free or subsidised accommodation to retired directors, or to buy medical insurance for them, then these would fall under the heading 'retirement benefits'. However, retirement benefits as defined in section 3 do not include:</p> <ul style="list-style-type: none"> • any benefit for personal injury or death by accident arising out of and in the course of employment; and • any retirement gift of a value (or, in the case of a retirement gift made otherwise than in cash, an estimated money value) not exceeding HK\$50,000. <p>The above sets out the definition of 'retirement benefits' as per section 3. However, in terms of the actual disclosure of retirement benefits under section 5, the following sections are also important to note:</p> <ul style="list-style-type: none"> • Section 10(2) effectively requires that the disclosure of retirement benefits should include retirement benefits paid to an entity connected with the director (such as his/her family or business associates) (see paragraph 16(c) below for further guidance on this area). • Section 5(4) states that retirement benefits paid out of a retirement benefit scheme are disregarded if the contributions made under the scheme were substantially adequate to maintain the scheme⁹.
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⁸ In practice, although MPF benefits explicitly fall within the definition of 'retirement benefits' under section 3(1), they are exempted from actual disclosure under section 5, as section 5(4) states that any amount of retirement benefits paid or receivable under a retirement benefits scheme is disregarded if the contributions made under the scheme are substantially adequate for the maintenance of the scheme. As the MPF scheme is a defined contribution scheme, then this exclusion always applies to these benefits. Instead, the employer's contribution to the MPF scheme made during the years of the director's qualifying services would be disclosed as part of directors' emoluments under section 4. See also the footnote immediately below.

⁹ This exclusion is stated in section 5(4) and effectively means that benefits receivable from a fully funded retirement benefit scheme would be excluded from this category of directors' retirement benefits. This exclusion avoids double-counting, as the contributions paid into the scheme would already have been disclosed as directors' emoluments in the years when the director was providing the qualifying services as per paragraph 12 above. As a result of this exclusion, the retirement benefits paid out from a scheme to be disclosed under section 5 would be limited to payments from under-funded schemes, or gratuitous payments.

<p>14. Payments in respect of termination of service (section 6)</p>	<p>This category includes amounts payable or benefits provided to directors or former directors or shadow directors¹⁰ in respect of the termination of qualifying services.</p> <p>The information to be disclosed under section 6(2) is in respect of the amounts of 'payments for loss of office' within the meaning of section 517 of the CO. So far as payments in respect of termination of service are concerned¹¹, 'payment for loss of office' refers to a payment to a director or former director: -</p> <ul style="list-style-type: none">• by way of compensation for loss of office as director of the company;• by way of compensation for loss, while a director of the company, in or connection with ceasing to be director of it, of –<ul style="list-style-type: none">(i) any other office or employment in connection with the management of the affairs of the company; or(ii) any office (as director or otherwise) or employment in connection with the management of the affairs of any subsidiary undertaking of the company. <p>It is clear from section 6 of the Regulation that the amount to be disclosed would include the estimated money value of any non-cash benefits. Section 517(2) of the CO also states that payment for loss of office would include any excess payments made on buying back the directors' shares over and above the price that could have been obtained by other holders of like shares at the time.</p> <p>Payments made on losing office would include payments or benefits of a gratuitous nature¹². Also, a payment in lieu of notice would be included under payments in respect of termination of service rather than under directors' emoluments, as this would be a form of benefit provided in exchange for the termination, rather than a payment for services performed while a director.</p>
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¹⁰ Per section 2(1) of the CO, the term 'shadow director', in relation to a body corporate, means a person in accordance with whose directions or instructions (excluding advice given in a professional capacity) the directors, or a majority of the directors, of the body corporate are accustomed to act.

¹¹ Section 517(1)(c) and section 517(1)(d) of the CO relate to payments in connection with retirement, not in respect of the termination of service (section 517(5) of the CO). As explained above, section 6 relates to payments for loss of office in respect of termination of directors' services for which section 517(1)(a) and section 517(1)(b) are relevant (section 517(4) of the CO). Consequently, section 517(1)(c) and section 517(1)(d) of the CO are not relevant for the purposes of determining what to disclose under section 6. Instead, the types of payments listed in section 517(1)(c) and section 517(1)(d) of the CO would fall to be disclosed under section 5, as these are covered by the definition of retirement benefits set out in section 3(1) (see paragraph 13 above).

¹² Unlike for retirement benefits disclosed under section 5, there is no exemption in section 6 for a gift of a value not exceeding HK\$50,000. All such gifts on termination of services are therefore discloseable, regardless of their value.

<p>15. Consideration provided to or receivable by any third party (section 7)</p>	<p>This category captures consideration provided to or receivable by certain 'third parties' for making available the services of a person as a director of a company, or in any other capacity while a director. This would include the estimated money value if the payments are otherwise than in cash.</p> <p>The reference to 'any third party' in this section is a reference to any person other than:</p> <ul style="list-style-type: none">• the director;• a connected entity of the director (see paragraph 16(c) below for the definition);• the company; or• a subsidiary undertaking of the company. <p>This list of excluded entities is much shorter than the list of entities which fall within the definition of 'related party' under Hong Kong Accounting Standard (HKAS) 24. This means that some parties which would be regarded as 'related parties' under HKAS 24 will nevertheless fall within the scope of section 7, as under section 7 they are regarded as 'third parties'. For example, a parent company or fellow subsidiary of the company would fall within the scope of this section as a 'third party', even though HKAS 24 would regard it as a related party.</p> <p>It follows that management fees payable to other group companies, may be discloseable under this section. See paragraphs 35 to 37 and 51 to 53 below for further guidance on this area.</p> <p>However, note that, as stated above, pursuant to section 10(2) a payment would not be classified as a 'payment to third parties', when the payment is directly or indirectly made to or receivable by an entity connected to the director (such as his/her family or business associates). Instead, the amounts should be included in 'directors' emoluments', 'retirement benefits' or 'payment in respect of termination of services depending on the circumstances surrounding the payment. See paragraph 16(c) below for further guidance on this area.</p>
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Supplementary provisions in the Regulation

16. Sections 8 to 12 of the Regulation contain supplementary provisions relating to the above requirements:

(a) *Section 8: Only information contained in company's records to be given*

Section 8 states that the Regulation only requires information to be disclosed in the financial statements only in so far as:

- (a) the information is contained in the company's records (as defined in section 838(1) of the CO); or
- (b) the company has the right to obtain it from the persons concerned¹³.

¹³ Section 383(5) of the CO states that a person who is, or has been during the preceding 5 years, a director or shadow director of a company must give notice to the company of any matter that -

- (a) is prescribed by the Regulation;
- (b) relates to the person; and
- (c) is necessary for the purposes of subsection (1), i.e. for the purposes of making disclosure in the financial statements in compliance with the Regulation.

Section 383(6) of the CO states that any person who contravenes section 383(5) commits an offence and is liable to a fine at level 5. This statutory obligation to disclose information to the company is in addition to any other obligation to disclose information contained in any contract with the director.

(b) *Section 9: Amounts paid or receivable in which period to be shown*

Section 9 states that an amount required to be shown in the notes to the financial statements for a financial year must be the amount of -

- (a) All relevant sums receivable in respect of that year (whenever paid); or
- (b) In the case of sums not receivable in respect of a period, the sums paid during that year.

Section 9 also states that if an amount is disclosed for the financial year then the corresponding amount for the immediately preceding financial year must also be shown in the notes. See paragraphs 30 to 34 below for further guidance.

(c) *Section 10: Payments made by or to which person to be shown*

Section 10 states that the amounts to be disclosed should include all relevant sums, whether paid by or receivable from the company, the subsidiary **or any other person** (emphasis added). Section 10(3) states that this also includes payments made by another person at the direction of the person. In other words, when identifying relevant payments to be disclosed, the focus should be on what the payment is for, not on who made the payment.

In addition, section 10(2) states that a reference to a payment to or receivable by a director includes -

- (a) a payment to or receivable by a connected entity of the director; and
- (b) a payment to a person made or to be made at the direction of, or for the benefit of, the director or a connected entity of the director.

As explained in paragraph 15 above, pursuant to section 10(2) a payment would not be classified as a payment to third parties when the payment is directly or indirectly made to or receivable by the director or an entity connected with him/her (such as his/her family or business associates).

For example, Company A appoints one of its employees as a director of one of its investee companies. The obligation of the employee to give notice under s.383(5) of the CO to the investee company will depend on whether any sum paid to him by, or receivable by him from, Company A is "in respect of his qualifying services" rendered to the investee company (section 4(2)(a)). If it is stated expressly in the employment contract of the employee with Company A that a certain sum is paid for his services as a director in the investee, the employee must give a notice to the investee under s.383(5) of the CO. However, if the employee acts as a director of the investee company incidental to his services to Company A and no emolument is received by him from Company A for such service to the investee company, the employee is not required to give a notice under s.383(5) of the CO to the investee company. Each case will depend on the facts of the particular case.

The term 'connected entity' is defined in section 486 of the CO. Under section 486 of the CO, a reference to a 'connected entity' of a director or former director is a reference to any of the following individuals or entities:

- (a) a member of the director's or former director's family, as defined in section 487 of the CO i.e. the spouse, child¹⁴ or parent of the director or former director;
- (b) a person who is in a cohabitation relationship¹⁵ with the director or former director;
- (c) a minor¹⁶ child of a person falling within paragraph (b) (i.e. a cohabitee) who—
 - (i) is not a child of the director or former director; and
 - (ii) lives with the director or former director;
- (d) a body corporate with which the director or former director is associated¹⁷;
- (e) a person acting in the capacity as trustee of a specified trust¹⁸; other than a trust for the purpose of an employee share scheme or a pension scheme; or
- (f) a person acting in the capacity as partner¹⁹ of—
 - (i) the director or former director;
 - (ii) the spouse of the director or former director;
 - (iii) a minor child of the director or former director; or
 - (iv) another person who, by virtue of paragraph (e), is an entity connected with the director or former director.

¹⁴ 'Child' is defined in section 484(1) of the CO as including a step-child, an illegitimate child and a child adopted in any manner recognized by the law of Hong Kong. As section 487 of the CO refers to 'child' and not 'minor child', the director or former director's 'family' as referred to in section 486(1)(a) of the CO and defined in section 487 of the CO should be understood to include that person's children of any age i.e. regardless of whether the children are minors or adults. It is also irrelevant whether these family members are dependent on, or independent of, the director.

¹⁵ 'Cohabitation relationship' is defined in section 484(1) of the CO as meaning 'a relationship between 2 persons (whether of the same sex or of the opposite sex) who live together as a couple in an intimate relationship'.

¹⁶ A 'minor child' is defined in section 484(2) of the CO as being a child who is under 18 years of age.

¹⁷ Section 488 of the CO sets out the meaning of 'associated' in this context. The focus is on the extent of voting power controlled by the director/former director and certain of his/her connected entities in excess of 30%. Reference should be made to this section for the full definition.

¹⁸ Section 488 of the CO sets out the meaning of 'associated' in this context. The focus is on the extent of voting power controlled by the director/former director and certain of his/her connected entities in excess of 30%. Reference should be made to this section for the full definition.

¹⁹ Section 486(2) of the CO sets out the meaning of 'specified trust' in this context. The focus is on the extent to which the director/former director or certain of his/her connected entities are beneficiaries of the trust. Reference should be made to this section for the full definition.

- (d) *Section 11: Payments accounted for not to be included until liability released or not enforced*

Section 11 covers the situation where the payments are to be accounted for to the company or any subsidiary undertaking.

Such amounts are not disclosable as a director's benefits unless the liability is wholly or partly released or not enforced within two years after the date on which the payment was received by the person. If the liability is so released or not enforced, then this benefit to the director is disclosable as part of directors' benefits, separate from all other amounts of remuneration.

For example, if a company made a personal loan to a director and the loan was repayable within the next 18 months, the loan would be disclosed under Part 3 of the Regulation (specifically section 15 of the Regulation), as a loan to a director, rather than under Part 2 as an emolument. However, if the director fails to repay the loan on the due date and the company decides not to pursue the matter, then the amount of the loan becomes disclosable under Part 2 of the Regulation (specifically section 11) at the latest two years after the time when the loan was first made.

Occasionally, some directors' remuneration is not included in the notes to the financial statements, either because the director is liable to account for it to the company or to any subsidiary undertaking of the company, or because it is considered to be an expense allowance for business expenses. In either of these cases, where the reasons are subsequently found not to be justified, the previously omitted remuneration is disclosed in a note to the first financial statements in which it is practicable to do so, and is identified separately.

- (e) *Section 12: How to distinguish between different payments*

Section 12 states that, subject to any express provision to the contrary, if any distinction is required to be made in any information to be shown in accordance with this Part of the Regulation, the directors may, for the purpose of complying with the requirement, apportion any payment between the matters in respect of which the payment is made or receivable in the manner that the directors see fit. See paragraphs 43 to 53 below for further guidance on this area.

Auditors' responsibilities under section 407(4) of the Companies Ordinance

17. Section 407(4) of the CO states that if the financial statements do not comply with section 383(1) of the CO (i.e. do not make the disclosures required by the Regulation), then the auditor must include in the auditor's report, so far as the auditor is reasonably able to do so, a statement giving the particulars that are required to be, but have not been, contained in the financial statements.
18. This requirement is in addition to the general requirement to express an opinion under section 406(1)(a) of the CO on whether the financial statements have been properly prepared in compliance with the Companies Ordinance. In such cases of non-compliance by the company with section 383(1) of the CO the auditor would give a qualified opinion.²⁰

²⁰ Refer to Practice Note 600.1(Revised) *Reports by the Auditor under the Hong Kong Companies Ordinance* (Cap. 622) for further guidance

Listed companies in Hong Kong

19. All companies whose securities are listed on the Stock Exchange of Hong Kong Limited are also required by the Main Board Listing Rules and GEM Listing Rules to make disclosures required by section 383 of the CO and the Regulation, irrespective of whether or not they are incorporated in Hong Kong (Main Board Listing Rules Appendix 16, paragraphs 28(1)(a) and (c); GEM Listing Rules paragraph 18.07A(1)(a) and (c)). In addition, listed companies in Hong Kong are required to comply with the Main Board Listing Rules (Appendix 16, paragraphs 24 to 25) or GEM Listing Rules (paragraphs 18.28 to 18.30), as appropriate, to include the following additional disclosures:
- (a) a general description of the emolument policy and any long-term incentive schemes of the group headed by the listed company;
 - (b) the basis of determining the emoluments payable to directors of the listed company; and
 - (c) the following particulars of emoluments in the financial statements for directors and past directors, for each director by name:
 - (i) the director's fees for the financial year;
 - (ii) the director's basic salaries, housing allowances, other allowances and benefits in kind;
 - (iii) the contributions to pension schemes for the director or past director for the financial year;
 - (iv) the bonuses paid or receivable by the director which are discretionary or are based on the listed company's or the group's (headed by the listed company) or any member of the group's (headed by the listed company) performance (excluding amounts disclosed in (v) and (vi) below) for the financial year;
 - (v) the amounts paid during the financial year or receivable by the director as an inducement to join or upon joining the listed company; and
 - (vi) the compensation paid during the financial year or receivable by director or past director for the loss of office as a director of any member of the group (headed by the listed company) or of any other office in connection with the management of the affairs of any member of the group (headed by the listed company) distinguishing between contractual and other payments (excluding amounts disclosed in (ii) to (v) above).
20. For the above disclosure, 'director' includes a chief executive who is not a director. In the case of a PRC issuer, directors and past directors also include supervisors and past supervisors.
21. The Main Board Listing Rules and the GEM Listing Rules also require particulars of any arrangement under which a director has waived or agreed to waive any emoluments. Where a director has agreed to waive future emoluments, particulars of such waiver must be given together with those relating to emoluments which accrued during the past financial year. This applies in respect to emoluments from the listed issuer or any of its subsidiaries or other person.

22. Where a director is contractually entitled to bonus payments which are fixed in amount such that the payments are more in the nature of basic salary, these bonus payments should be disclosed under paragraph 19(c)(ii) above in accordance with the Main Board Listing Rules or the GEM Listing Rules, as appropriate. Further, all bonus payments to which a director is contractually entitled and which are not fixed in amount (e.g. bonus payments are determined as a percentage of revenue or profits of the group headed by the listed company), together with the basis upon which they are determined, should be disclosed under paragraph 19(c)(iv) above.
23. It is understood that the intention of the above Listing Rules is to provide a further breakdown and analysis of the total amount of directors' remuneration disclosed under the Companies Ordinance, particularly the discretionary elements thereof, notwithstanding the fact that the Listing Rules only adopt the term 'directors' emoluments'.

PRACTICAL ISSUES

An employee acting as an alternate director

24. The Companies Ordinance does not define 'alternate director' but in practice this term is generally used to refer to an individual who attends meetings on behalf of a director on occasions when the director is unable to attend. The ability to appoint such an alternate and the limits on the powers of the alternate may be set out in the articles of the company and may therefore vary from one company to the next.²¹
25. It is not clear from the Companies Ordinance how amounts paid or payable to alternate directors should be dealt with in the disclosure of directors' remuneration. The Committee is of the view that remuneration of such a person would be included as directors' remuneration only to the extent of any specific incremental amount received or receivable by the person in respect of acting as an alternate director, if any. It would not be appropriate to include the full amounts payable to the individual in their primary role of being an employee of the company, even if the individual is considered to be part of the management of the company or its subsidiary undertakings, as, by definition, an alternate director has not been appointed as a director of the company.²²

A person is a director for only part of a financial year

26. In general, where part way through a financial year an employee becomes a director of the company, the amount to be disclosed as directors' emoluments is the amount related to qualifying services provided by the person during the period when he/she served as a director. The amount to be disclosed would include sums paid or receivable as an inducement to become a director and also that individual's salary from then on, as the salary would be a form of payment 'in connection with the management of the affairs of the company' while being a director. But the amount to be disclosed would not include amounts that related to the individual's period of service before he/she was appointed as a director.

²¹ Section 478 of the CO states that, unless the articles contain any provision to the contrary, an alternate director is deemed to be an agent of the director who appoints the alternate and a director who appoints an alternate is vicariously liable for any tort committed by the alternate director while acting in the capacity of alternate director.

²² Where the person's role as alternate director extends beyond merely attending board meetings on the ad hoc occasions when the director has a scheduling conflict, then it may be necessary to seek legal advice on the extent to which the person should be regarded as a director for the purposes of the Companies Ordinance, rather than as an alternate director. For example, this may be necessary in cases where an executive director is absent for an extended period due to serious illness and the alternate director takes over that person's additional powers and responsibilities on a day-to-day basis. In this regard it is noted that section 2(1) of the CO defines a director as including 'any person occupying the position of director (by whatever name called)'.

27. Similarly, if a person ceases to be a director of the company during the year but continues as an employee, then the amounts discloseable as directors' remuneration would be those amounts which fall under the definition of directors' emoluments, retirement benefits or compensation for loss of office, to the extent that the amounts relate to the person's qualifying services as defined in paragraph 7 above, and not in respect of the person's subsequent employment when no longer a director.

A company is a subsidiary undertaking for only part of a financial year

28. Section 3(4)(b) and (c) clarifies that the references to 'subsidiary undertakings' or to any other undertaking captured as a subsidiary undertaking under section 3(4)(a) refer to an entity that was, or deemed to have been, a subsidiary undertaking at the times that the director was rendering qualifying services or, in the case of payments for loss of office, was, or deemed to have been, a subsidiary undertaking immediately before the loss of office as director of the company.
29. For example, company H acquires a new subsidiary company S on 15 June 201X. Mr C was a longstanding director of company S at the time of the acquisition and on 1 October 201X he was appointed to the board of company H, as well as continuing to be a director of company S. Both company H and company S have 31 December financial year ends.

Mr C is paid \$1 million per annum by company S. In addition, as from 1 October 201X Mr C receives an additional \$200,000 per annum from company H related solely to his additional new responsibilities.

In this example, the amounts to be disclosed in respect of Mr C's emoluments in financial statements for the year ended 31 December 20X1 are as follows:

- Company S should disclose a full year of emoluments for Mr C, but the amount disclosed should relate only to the services that Mr C has provided to company S and not for his additional responsibilities as a director of company H. Company S should therefore disclose \$1 million as Mr C's emoluments.
- Company H should disclose Mr C's emoluments for being a director of company H and, while he was a director of company H, for also being a director of company S. The amount to be disclosed by company H therefore relates only to the period starting from 1 October 20X1. On a pro rata basis the amount to be disclosed would be $\frac{3}{12} \times \$1.2 \text{ million}$ i.e. \$300,000, irrespective of whether company H is preparing consolidated financial statements or company-level financial statements.

Other matters relating to timing of disclosure

30. According to section 9(1), the amounts shown in the notes to the financial statements for a financial year must be the amount of -
- (a) all relevant sums receivable in respect of that year (whenever paid); or
 - (b) in the case of sums not receivable in respect of a period, the sums paid during that year.
31. The timing of disclosure under section 9(1)(a) focuses on when the director becomes entitled to the amount i.e. it is requiring the accruals concept to be applied when determining in which period the remuneration should be disclosed. The timing of disclosure under section 9(1)(b) focuses on when the payments were made i.e. it is requiring a cash basis of accounting to be applied when determining in which period the remuneration should be disclosed. In both cases the timing may, or may not, coincide with the time of recognition of an expense in accordance with HKFRSs.

Determining whether an amount falls under section 9(1)(a) or 9(1)(b)

32. In most cases, a director's emoluments are based on a period of time served. These clearly fall under section 9(1)(a) and should be disclosed on an accruals basis consistent with the principles of HKAS 19 *Employee benefits*. However, the Committee also considers that amounts may be judged to be 'in respect of that year' (i.e. to fall under section 9(1)(a)) if the director's entitlement to the amount is conditional on meeting certain targets and those targets are first met in the year.

For example, if a director is entitled to receive a bonus conditional on achieving the sale of a business at or above a target sales price, then the director's entitlement to that bonus arises in the year in which the sale is achieved. Therefore, in the Committee's view, such amount also falls under section 9(1)(a) and would be disclosed in that year, even if the payment is made to the director in a subsequent period.

Similar principles would be applied to payments to third parties for making available the service of a director.

33. In the case of payments for termination of service and directors' or past directors' retirement benefits, it is common practice for the amounts to be disclosed as follows:
- payments or benefits provided for termination of service are typically disclosed in the year in which the director loses his/her office; and
 - retirement benefits are typically disclosed in the year, or years, in which the benefit becomes payable. For example, if the director is entitled to a lump sum payment on retirement, then the lump sum would be disclosed in the year of retirement, whereas if a retired director is entitled to a monthly pension from the company for the rest of his/her natural life, then the amount to be disclosed in the year would be the sum of the monthly amounts payable in that financial year. If any of the amounts paid or receivable are made out of a fully funded retirement benefit scheme, in accordance with the provisions of that scheme, then no disclosure is required (section 5(4)).

In practice, these amounts are typically paid in the same period in which the director becomes entitled to them and therefore the question of whether these payments fall under section 9(1)(a) or 9(1)(b) does not arise. If there is some delay in paying these amounts, then in the Committee's view, such amounts fall under section 9(1)(a) and would be disclosed in the financial year in which the entitlement was established, rather than the year in which the amounts were paid. If in doubt about whether this satisfies section 9 then additional disclosure should be provided on the payment terms and/or legal advice should be sought.

34. Any payments which do not fall under section 9(1)(a) would fall under section 9(1)(b). For example, payments or benefits which are subject to an extended vesting period, and are forfeited if the vesting conditions are not met, may fall under section 9(1)(b) and would be disclosed in the year in which the payment or benefit vests. This could apply to long service payments or share-based payment grants which are subject to vesting conditions.

Consideration provided to or receivable by third parties for making available the director's services

35. Section 7 of the Regulation requires separate disclosure of the aggregate amount of the consideration provided to or receivable by any third party, whether in cash or otherwise, for making available the qualifying services of a person who is a director of a company.

For example, company A borrows money from a venture capital company. As part of the financing arrangement, a director of the venture capital company has been appointed to the board of company A. Company A pays \$120,000 per year to the venture capital company in respect of the director's services. The director is remunerated by the venture capital company and does not personally receive the money paid in respect of his services by company A. In this situation, the amount of \$120,000 is disclosed in company A's financial statements as sums paid to third parties in respect of directors' services.

However, the disclosure does not apply to other services supplied by third parties. For example, where the fees paid by company B to a 'head hunter' relate solely to services to the company for finding and introducing the person, the Committee considers that a 'head hunter' is not 'making available' the services of the person as a director. The 'head hunter' receives a fee for finding the person whom company B appoints to perform the services but the 'head hunter' is not paid in respect of the services.

36. According to section 7(3), the reference to 'third party' in this section is a reference to any person other than:
- (a) the director;
 - (b) a connected entity of the director²³;
 - (c) the company; or
 - (d) a subsidiary undertaking of the company.
37. This definition of 'third party' effectively sets the scope of this disclosure requirement as follows:
- (a) This disclosure requirement applies to payments made to unrelated third party management service companies. However, it does not apply when the payment has been made to a connected entity of the director (for example, to a company with which the director is associated through an ownership interest of more than 30%, or a partnership in which the director is a partner). Instead, any such amounts are deemed to be receivable by the director and therefore fall directly under sections 4, 5 or 6 as emoluments, retirement benefits or payments for loss of office, depending on the circumstances in which the payment arose.
 - (b) As well as applying to unrelated third party management services companies, this disclosure requirement also applies to intra group payments, other than those between the company and its own subsidiary undertakings. For example, if a company makes a payment to its holding company in return for the holding company providing the services of one of the company's directors, then such payment falls under section 7 as a 'payment to third parties'. Further guidance apportioning payments within groups can be found in paragraphs 43 to 53 below.

²³ See paragraph 16(c) above for the definition of 'connected entity'.

Distinguishing between service 'as a director' and 'otherwise in connection with the management of the affairs'

38. As introduced in paragraph 7 above, the Regulation requires each type of directors' remuneration to be distinguished between:
- (a) remuneration in respect of services as director of the company or as a director of its subsidiary undertakings; and
 - (b) remuneration for the management of the affairs of the company or its subsidiary undertakings.
39. Remuneration in respect of services as a director are normally those fees which are paid to directors in their capacity as such and not in any managerial or executive capacity. Typically these would be fees fixed either by the Articles of Association or by the company in general meeting, including sums paid for special services, for example serving on or chairing board committees such as the company's audit committee.
40. The remainder of the remuneration of an executive director is generally assumed to be those sums which are paid to directors of the company in connection with the management of the affairs of the company or its subsidiary undertakings. This other remuneration normally includes salaries, bonuses and other benefits paid to executive directors, for instance, for acting as a managing director, or being responsible for a business segment.

Services provided by a director which are neither 'as a director' nor 'otherwise in connection with the management of the affairs'

41. All payments made to a director, except for reimbursement of expenses²⁴, would generally fall within one of these categories of directors' remuneration ie 'as a director' or 'in connection with the management of the affairs', unless it can clearly be demonstrated otherwise. This is not expected to be common but may be the case when the director has specific technical skills, such as a professional valuer or legal adviser. In such cases, payments may also be made to a director in a self-employed or an independent professional capacity for the provision of technical services that are not connected with qualifying services as a director or otherwise in connection with managing the company or its subsidiary undertakings. Typically, such payments will be made under a 'contract for services' that a director has with the company.
42. Where it can be clearly established that the payments are genuinely for technical services and separately distinguishable, then the amounts paid should not be disclosed as directors' remuneration. However, if the director's 'contract for services' is considered significant in relation to the company's business, and the director's interest in the contract is material, then details of the transaction would need to be disclosed in the notes to the financial statements (if the contract is entered into by the company²⁵) or in the directors' report (if the contract is entered into by the holding company of the company, a fellow subsidiary of the company or a subsidiary of the company²⁶) in accordance with the requirements relating to disclosure of a director's material interest in a contract. In addition, the transaction might need to be disclosed as a related party transaction in accordance with HKAS 24.

Apportioning payments between holding company and subsidiary undertakings

²⁴ See paragraph 54 below.

²⁵ See sections 22-23 of the Regulation.

²⁶ See section 10 of the Companies (Directors' report) Regulation (Cap. 622D).

43. As introduced in paragraph 8 above, when a person is a director of more than one company within a group it may be necessary to identify which amounts of the person's remuneration relate to which company.
44. A common example of this is where an executive director of a holding company is also appointed as director of a number of that company's subsidiaries, either in an executive or non-executive role.
45. In such cases, all of that individual's remuneration relating to the group will be discloseable in the holding company's financial statements. However, in each of the subsidiaries' financial statements, the amount to be disclosed should relate only to the qualifying services provided by that individual to that subsidiary (and to that subsidiary's subsidiaries, if any). This distinction is illustrated in the simple examples in paragraphs 8 and 29.
46. In practice, there may be practical difficulties in making such a distinction, as it is not uncommon in groups for directors to be remunerated solely by the holding company (either as director or employee) or by one of the group companies for their services to the group as a whole.
47. According to section 12, if any distinction is required to be made for directors' remuneration disclosure, the directors may, for the purpose of complying with the requirement, apportion any payment between the matters in respect of which the payment is made or receivable in the manner that the directors think fit.

In this regard the following points should be noted:

- The power to apportion under section 12 is given to the directors collectively. That is, it is for the board to decide collectively how to comply with the requirements of the Regulation, having considered the factual information available to them concerning the payments.
- An individual director may also use the power to apportion when he or she receives payments from other parties (such as the company's holding company or other shareholder), some of which relates to services that the individual provides to the company.
- The power to apportion is a limited power to apportion a payment 'between the matters in respect of which the payment is made or receivable'. That is, the power to apportionment is only available to the directors when a payment relates to more than one matter, which are required to be disclosed separately under Part 2 of the Regulation or some of which fall outside the scope of disclosure.
- The power to apportion is a power to apportion 'in the manner that the directors see fit'. This indicates that the directors are expected to use their judgment to consider what would be a reasonable apportionment, based on the circumstances in which the payment was made and the qualifying services received by the company.

Is apportionment optional?

48. As noted in the footnote to paragraph 16(a) above, section 383(5) of the CO states that a person who is, or has been during the preceding 5 years, a director or shadow director of a company must give notice to the company of any matter that -
- (a) is prescribed by the Regulation;
 - (b) relates to the person; and
 - (c) is necessary for the purposes of subsection (1), i.e. for the purposes of making disclosure in the financial statements in compliance with the Regulation.

Given this, any director who receives payments from other parties (such as the company's holding company or other group company or third parties), some or all of which relates to services that the individual provides to the company or its subsidiary undertakings, is under a duty to provide such information to the company and the relevant subsidiary undertakings as will enable those companies to comply with section 4 of the Regulation.

In order to meet this duty, the director may therefore need to use his or her judgment to apportion the payments received, if that individual receives a single remuneration package from elsewhere in the group in respect of services provided to more than one group company. One common method of apportioning a package in such circumstances would be by reference to the number of working hours that the individual is engaged on each of his or her different roles in the group, where the number of working hours are more than insignificant. Where the number of working hours are insignificant the qualifying services may be regarded as incidental to their roles and responsibilities to the larger group.

49. So far as the directors' collective responsibility is concerned, as the power to apportion arises 'if any distinction is required to be made in any information to be shown in accordance with this Part', this implies that, if it is necessary to exercise the power to apportion in order to provide the information required by the Regulation relating to directors' remuneration, then the directors would need to exercise the power if a reasonable apportionment can be made.

However, it should also be noted that section 8 states the following:

'This Part requires information to be given by a company only in so far as –

- (a) the information is contained in the company's records (as defined by section 838(1) of the Ordinance; or
- (b) the company has the right to obtain it from the persons concerned.²⁷

Given section 8, the duty of the directors to apportion payments made by others to the directors of the company, or to disclose unapportioned payments made by others in order to comply with the Regulation, only exists to the extent that sufficient information is properly available to the company about the amounts involved and the purpose for which the payments were made.

²⁷ See footnote to paragraph 16(a).

50. In the case of directors being paid solely by the holding company or by a service company in the larger group, the following is typically disclosed by the company:
- the fact that the directors of the company are also directors/employees of the holding company/fellow subsidiaries and are remunerated by the holding company/a fellow subsidiary in respect of their services to the group as a whole; and
 - an estimation of a reasonable amount of remuneration, for example based on an estimate of number of working hours spent on providing qualifying services to the company or its subsidiaries, if the director spends more than an insignificant amount of time on such activities and thus those services are more than just incidental.

Apportionment in respect of section 7 (consideration provided to or receivable by third parties for making available directors' services)

51. As discussed above in paragraphs 35 to 37, disclosure of a 'payment to third parties' under section 7 may also be necessary if the company pays a management fee to the holding company or a fellow subsidiary, some or all of which relates to that other company (or those other companies) making available the qualifying services of one or more of the company's directors.
52. The amount disclosed under section 7 need not be the same as the amount disclosed under section 4, as section 7 relates to the amounts paid to the group company, whereas the disclosure under section 4 relates to the amounts receivable by the director from that other company.

For example, company A pays a management fee of \$1.5 million per annum to company B in return for company B making available the qualifying services of Mr X, a director of company A. Mr X is paid \$1 million per annum by company B for taking on the role of being a director of company A. In this case, company A should include \$1 million in its aggregate directors' emoluments disclosure under section 4, and \$1.5 million in its disclosure of amounts paid to third parties for providing the services of a director under section 7. It would be advisable if the disclosure in such cases explained that the director's emoluments were paid by the third party to whom the amounts disclosed were paid.

53. If the management fee also includes other matters (such as office space rental or shared administration costs) then the apportionment provisions of section 12, as discussed above, also apply to this payment. In this case, the directors of the company should have a reasonable knowledge of the basis of the management fee re-charge payable by the company and be able to use this knowledge in order to apportion the payment between amounts for directors' qualifying services and other matters.

Expenses allowance

54. According to section 4(6) emoluments do not include expense allowances, provided that the allowance is actually spent on the expenses for which the allowance was made. In this respect, the Committee is of the view that this exemption only applies in the case of allowances that are spent on expenses of a business nature (for example, travel to overseas business meetings). Care would need to be exercised to ensure that such expenditure is of the nature permitted under section 506 of the CO. In the Committee's view, allowances for personal expenditures (for example, a housing allowance) are in substance part of the salary package and therefore should be included under directors' remuneration, irrespective of whether the amounts are actually spent on the designated purpose.

Guidance on valuing and disclosing benefits in kind

55. According to sections 4(5), 5(5), 6(5) and 7(4), if any emoluments, retirement benefits, payments for loss of office or consideration payable to third parties consist of a benefit otherwise than in cash, then the amounts disclosed for that category should include the estimated money value of that benefit. Such benefits in kind might include provision of accommodation at below market rates, or provision of a car or health benefit or golf or other club membership or life assurance cover.
56. Where the company has paid a third party to provide the benefit to the director (or the director's connected entity), then the estimated money value of that benefit is usually the cost incurred by the company. For example, if a house or flat is rented by the company from an unrelated third party and occupied by a director, the estimated money value is the rent paid to the owner and any other related charges borne by the company less any amount contributed by the director. Similarly, if the company pays for the school fees of a director's child, then the estimated money value is usually the amount of the fees that the director would otherwise need to pay. In the case of life assurance cover for a director, with the beneficiary being the next of kin of the director, the estimated money value is the insurance premium paid to the insurance company.
57. In some cases, the money value may not be readily apparent from a transaction with third parties. In such cases, the directors should estimate the value from the perspective of the director as a market participant. This amount will not necessarily coincide with the cost borne by the company in providing such benefits, or the amount of expense recognized for financial reporting purposes in accordance with HKFRS.
58. The above principle is illustrated in the examples below.
- (a) Property transferred to a director
- If a company transfers the title of a property to a director, the estimated money value of the benefit is the property's fair value less any amount paid by the director.
- (b) Property owned by the company, used by a director
- If a company allows a director to use a flat or house owned by the company, then the estimated money value is the market rental of the property as if it were let on arms' length terms plus any related charges (for example, rates, utilities and building management fees) borne by the company less any amount contributed by the director. In Hong Kong an approximation of the annual market rental may be noted from the property's rateable value as set by the Rating and Valuation Department of the Hong Kong Government²⁸.
- (c) Property rented by a company, used by a director
- A house or flat is rented by a company from an unrelated third party and occupied by a director, the "estimated money value" is the rent paid to the owner and any other related charges borne by the company less any amount contributed by the director.

²⁸ http://www.rvd.gov.hk/en/public_services/rates.html

(d) Company's product transferred to a director

The estimated money value of a product transferred to a director would be the normal selling price of an equivalent product sold in an arm's length transaction.

Care would need to be exercised to ensure that any of the transactions with directors in a to c above are considered as to whether they may be 'credit transactions' (as defined in section 494 of the CO) and do not contravene the prohibitions on such transactions with directors (see section 503 of the CO) and are properly disclosed in accordance with section 383 of the CO and Part 3 of the Regulation.

(e) Subsidised loans advanced to a director

The estimated money value of the benefit is the difference between the contractual interest payable by the director on the loan and the market interest otherwise payable by the director in obtaining the funding in the market himself/herself at the time when the loan was advanced to the director. Care would need to be exercised to ensure that any loans made to directors do not contravene the prohibitions on transactions with directors (see section 500 of the CO) and are properly disclosed in accordance with section 383 of the CO and Part 3 of the Regulation.

If any part of the contractual interest or principal on the loan is subsequently waived, then these additional amounts of benefit would become disclosable as part of directors' remuneration in accordance with section 11 of the Regulation (see paragraph 16(d) above).

(f) Share options granted by the company to a director

Due to the lack of specific guidance on how to determine the timing of disclosure under section 9 (see paragraphs 30 to 34 above), the Committee acknowledges that there are a number of different acceptable approaches to estimating the money value of share options granted to directors for the purposes of disclosure under the Regulation. These include the following approaches:

- the amount recognized as an expense in the period in accordance with HKFRS 2 *Share-based Payment*, or
- the amount of the gain if the options are exercised, or as if they were exercised, at the time of vesting, for those options which vested during the year. The amount of the gain is the difference between the market price of the shares on the day of vesting and the price paid, if any, for the shares.

However, the Committee does not consider it appropriate to use approaches which would include changes in the fair value of the options after they had vested, as by definition these changes in value arose after the period of service which entitled the director to the option.

For example, the Committee does not consider it appropriate to adopt an approach of measuring the money value of the benefit on the basis of gains realized by directors on the exercise of options at the time of their exercise, as such amounts would include gains or losses experienced by the directors after the vesting period had ended. The Committee considers that once the options have vested, any further gains or losses are experienced by the directors as holders of the options, rather than in their capacity as directors of the company.

When determining the amounts to be disclosed in the directors' emoluments note in relation to share options, companies should apply a consistent approach, from one director to the next and from one year to the next in accordance with the general principles set out in HKAS 1 *Presentation of Financial Statements*. The emoluments note should also disclose the approach chosen.

59. Where a director is provided with an asset (for example, a motor vehicle, an aircraft, or pleasure vessel) for a mixture of business and private use, an apportionment between business and private usage would be required. It is not necessary to apportion the cost between business and private use in absolute accuracy but it would need to be on a reasonable and consistent basis as discussed in paragraphs 43 to 53 above.

Disclosing the nature of a non-cash benefit

60. The amount of non-cash benefits is not required to be disclosed separately from cash benefits. However, sections 4, 5, 6 and 7 each require respectively that when any of the amounts of that category consist of a benefit otherwise than in cash, then the nature of that benefit must be disclosed. For example, if the director has been provided with accommodation, then this fact should be disclosed. Examples of possible disclosure notes are included in the Appendix for illustrative purposes.
61. It is the Committee's view that neither the money value nor the nature of the benefit is required to be included in the disclosure when the payment to a third party is reimbursed by the director. For example, if a director uses the company's credit card to settle personal expenses, the personal items bought using the credit card would not be a form of non-cash benefit, if the company seeks reimbursement from the director. This might be achieved by the company deducting the amount of any such spending from the director's salary payment. However, use of the company's credit card for personal expenditure may qualify as a 'quasi-loan' (as defined in section 493 of the CO). Care would need to be exercised to ensure that any 'quasi-loans' made to directors do not contravene the prohibitions on transactions with directors (see section 501 of the CO) and are properly disclosed in accordance with section 383 of the CO and Part 3 of the Regulation.

Presentation in the financial statements

62. Since some of the amounts included in directors' remuneration may not represent actual charges borne by the company (for example, amounts paid by third parties but not charged to the company and in relation to the disclosure of estimated money value as explained in paragraph 57 above), it is advisable that the company's financial statements have a separate note dealing with directors' remuneration rather than it being included in a general note covering items which are described as having been charged in arriving at profit before taxation.
63. This is particularly relevant in the financial statements of a holding company where the disclosure relates not only to directors' remuneration in respect of the directors' services as directors of the holding company but also to directors' remuneration in respect of their services as directors of the subsidiary undertakings (see the examples in paragraphs 8 and 29). Examples of possible disclosure notes are included in the Appendix for illustrative purposes.
64. Although there is no specific requirement to disclose the situation of nil directors' remuneration, it is advisable for the sake of clarity that such fact be disclosed.

65. According section 9(2), if an amount is shown for a financial year in the notes to the financial statements for that year in relation to the information prescribed by the Regulation regarding directors' remuneration, the corresponding amount for the immediately preceding financial year should also be disclosed. That means, comparative information is required to be disclosed by the Regulation²⁹. This is consistent with the requirements of paragraph 38 of HKAS 1 *Presentation of Financial Statements*.

²⁹ See HKICPA Q&As on financial reporting issues relating to the transition from the old to new Companies Ordinance – Part C – Disclosure in annual reports for financial years beginning on or after 3 March 2014 – Question C1.

APPENDIX: EXAMPLES OF DISCLOSURES IN NOTES TO FINANCIAL STATEMENTS

1. Illustrative disclosure by an unlisted company in the notes to the financial statements

Note X: Directors' Remuneration

Remuneration of the Company's directors disclosed pursuant to section 383 of the Companies Ordinance (Cap. 622) and the Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G) is as follows:

	201X	201Y
	HK\$	HK\$
Directors' emoluments for services as directors of the Company [and its subsidiary undertakings]*		
Directors' fees	50,000	40,000
Other emoluments in connection with the management of the affairs of the Company [and its subsidiary undertakings]*	3,000,000	2,500,000
Amount paid to third parties for making available the services of persons as directors	250,000	120,000
Payments in respect of termination of service	600,000	-
Retirement benefits given to retired directors	<u>15,000</u>	<u>12,000</u>
	3,915,000	2,672,000
	=====	=====

Other emoluments disclosed above include the estimated money value of accommodation provided by the company to the directors and their families. The money value of the accommodation is estimated to be the annual market rental of the accommodation less any amounts paid for by the directors personally and not reimbursed by the Company.**

In connection with a financing arrangement, the Company paid \$120,000 in both 201X and 201Y to Company Z for the services of Mr A as a director of the Company. In 201X, the Company also paid \$130,000 to its holding company for the services of Ms B as a director of the Company.

The retirement benefits given to retired directors consist primarily of continuing medical cover under the Company's group insurance plan. The money value is estimated based on the premiums paid for the cover provided to the retired directors.**

Payments in respect of termination of service were paid by the following parties:-

	201X	201Y
	HK\$	HK\$
The Company	500,000	-
Subsidiary undertakings of the Company	100,000	-
Others	-	-
	600,000	-
	=====	=====

The payments in respect of termination of service disclosed above includes the estimated money value of the company's car which was given to the director as part of his severance package. This amount has been estimated based on the second hand value of the car, taking into account its condition at the time of transfer of ownership.**

* to be added in the case of holding companies, where applicable

** When benefits other than cash are given to directors, the Regulation requires the nature of the benefits to be disclosed. It may also be useful to disclose how the estimated money value is arrived at. However, it is not necessary to separately disclose the amounts of non-cash benefits.

2. Illustrative wording for when directors receive no remuneration

'Directors' remuneration disclosed pursuant to section 383 of the Companies Ordinance (Cap. 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G) for the year is HK\$nil (201Y: HK\$nil).'

3. Illustrative wording for when some directors are paid by another group company, and no apportionment is made

(The following may be added after the above disclosure)

'In addition to the directors' remuneration disclosed above, certain directors are not paid directly by the Company but receive remuneration from the Company's holding company, in respect of their services to the larger group which includes the Company and its subsidiaries. No apportionment has been made as the qualifying services provided by these directors to the Company and its subsidiaries are incidental to their responsibilities to the larger group.***

*** *No apportionment is made as the number of working hours spent by the individual directors on their services to the Company [and its subsidiary undertakings] are judged to be insignificant and thus they are regarded as incidental to their roles and responsibilities to the larger group.*