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HKSA Proposes Implementation of a Financial Reporting Framework for Small and Medium-Sized Entities in Hong Kong

The **Hong Kong Society of Accountants** (HKSA) has today released proposals for the introduction of a financial reporting framework for SMEs.

The proposals are intended to provide – for the first time – a comprehensive basis of accounting for qualifying SMEs: to establish requirements that are appropriate both in terms of the compliance cost borne by the entities preparing financial statements and the usefulness of the financial information provided to those often-limited number of parties who make use of an SME's annual financial statements.

This consultation follows on from the proposed Framework for Differential Reporting released by the HKSA for public comment in August 2002. The development of financial reporting requirements relevant for SMEs was widely supported in the first consultation. There were, however, some issues raised at this time which did necessitate a review of the proposals by the Society's GAAP for Small Businesses Working Group and which we now believe have been addressed in this latest consultation.

The following six issues are raised in the Consultation Paper:

- ✓ The need for a separate financial reporting framework for qualifying entities
- ✓ The principles underlying SME financial reporting
- ✓ Whether SME financial statements need give a true and fair view
- ✓ Which entities should qualify to prepare financial statements under the SME financial reporting framework
- ✓ Statutory requirements applicable to SME financial reporting
- ✓ Applicable financial reporting requirements, fully contained within a separate financial reporting standard

The Consultation Paper is accompanied by a draft SME Financial Reporting Framework and SME Financial Reporting Standard. All three documents are available on the HKSA website at: <http://www.hksa.org.hk/professionaltechnical/accounting/exposedraft>.

Of note, the Consultation Paper proposes that companies currently qualifying under section 141D of the Companies Ordinance would qualify to apply the Small GAAP Standard. Currently, these companies must be private companies, have neither a holding company nor subsidiary companies, and all owners must agree to apply that section.

For non-corporate entities, the Consultation Paper proposes that entities should qualify on the basis of size thresholds set out in the paper. Comments are also invited on whether the HKSA should lobby for a change in the Companies Ordinance to amend section 141D to become consistent with the size requirements and to permit small non-listed groups applying the SME financial reporting standard.

Commenting on the proposals in the Consultation Paper, **Mr. Paul M.P. Chan**, HKSA Vice-president and Chairman of the Society's GAAP for Small Businesses Working Group said: "With the introduction of a separate set of financial reporting requirements for small and medium-sized entities, including companies that currently qualify for limited financial reporting relief under the Companies Ordinance, we are looking to put into place a comprehensive basis of accounting that meets the information needs of users of these entities' financial statements while at the same time reducing what we believe is an unduly high and growing compliance cost burden faced by these entities. Our conservative estimate is that at least 80% of Hong Kong companies will qualify to apply the proposed new SME financial standard. The Society also proposes to lobby for a change in the law, which would permit small groups to apply the simplified requirements."

Public comment is invited by 31 August 2004 on the issues raised in the Consultation Paper and on the draft SME Financial Reporting Framework and Financial Reporting Standard.

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The HKSA is the only statutory licensing body of accountants in Hong Kong responsible for the regulation of the accounting profession, with a membership of over 22,000 and close to 11,000 registered students.

Issued by the HKSA. For further information, please contact the following:

Ms. Florence Chan
Assistant Director – Public Relations
Direct line : 2287 7036
Mobile : 9877 2915
Fax no. : 2865 6776
Email : fchan@hksa.org.hk

Ms. Cynthia Lee
Administrative Officer - Public Relations
Direct line : 2287 7002
Mobile : 9322 3456
Fax no. : 2865 6776
Email : cynthialee@hksa.org.hk