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Accounting Profession in Hong Kong, Second Edition Revised; Professional Accounting in Foreign Country Series

KPMG Peat Marwick, Hong Kong

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PROFESSIONAL ACCOUNTING IN FOREIGN COUNTRIES SERIES

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The Professional Accounting in Foreign Countries series is designed to be educational and used as reference material for the members of the Institute and others interested in the subject. It is not intended to establish standards.

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SECOND EDITION, REVISED

The Accounting Profession in Hong Kong

PROFESSIONAL ACCOUNTING IN FOREIGN COUNTRIES SERIES

Prepared by
KPMG Peat Marwick
Certified Public Accountants
Hong Kong

STEVEN F. MOLITERNO, CPA
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AICPA
American Institute of Certified Public Accountants
This booklet is one of a series on professional accounting in foreign countries. The material is current as of April 1993. Changes after this date in the standards of either the United States or Hong Kong may alter the comparisons and references detailed in this publication.

Included are descriptions of the accounting profession, auditing standards, and accounting principles in Hong Kong. The booklet also presents brief descriptions of the various forms of business organizations, taxes, and requirements for stock exchange listings and securities offerings. Checklists comparing Hong Kong auditing standards and accounting principles with those generally accepted in the United States are included as appendixes to the text.

This booklet is not intended to be a comprehensive discussion of auditing standards and accounting principles in Hong Kong but is designed instead to focus primarily on differences from those of the United States.

John F. Hudson  
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The Accounting Profession

Requirements for Entry into the Profession

Domestic Functions and Licensing Requirements

1. In Hong Kong, anyone may use the title accountant and offer accounting and tax services. The only professional body is the Hong Kong Society of Accountants (herewith referred to as “the Society”). Qualified members are described as professional accountants, and are entitled to use the designation Associate or Fellow of the Hong Kong Society of Accountants. The Society can be contacted at the following address:

   Hong Kong Society of Accountants
   17th Floor, Belgian House
   77–79 Gloucester Road
   Wanchai, Hong Kong

2. Each company incorporated under the provisions of the Companies Ordinance, which regulates companies in Hong Kong, shall appoint an auditor who must be a professional accountant holding a practicing certificate issued by the Society. This practicing certificate bestows upon the holder the title of Certified Public Accountant. To qualify for issuance of a practicing certificate, which requires annual renewal, the professional accountant should have no less than four years of full-time approved accounting/auditing experience, be a resident of Hong Kong, and possess the experience and knowledge of law and practice as the Society considers necessary.
3. In Hong Kong, the Certified Public Accountant may also act as liquidator, receiver, or trustee of a company in bankruptcy. He or she may also act as company secretary, registrar, and share valuer.

Foreign Reciprocity

4. Under the Professional Accountants Ordinance, the Society has authority to admit as professional accountants—
   a. Members of the following “approved institutes”:
      • The Chartered Association of Certified Accountants
      • Australian Society of Certified Practicing Accountants
      • The Institute of Chartered Accountants in Australia
      • The Institute of Chartered Accountants in England and Wales
      • The Institute of Chartered Accountants in Ireland
      • The Institute of Chartered Accountants of Scotland
      • The Institute of Cost and Management Accountants
      • The Chartered Institute of Public Finance and Accounting
   b. Members of the following accountancy bodies accepted as having a standard similar to an approved institute:
      • Canadian Institute of Chartered Accountants
      • New Zealand Society of Accountants
      • The South African Institute of Chartered Accountants
      • The American Institute of Certified Public Accountants
      • The Institute of Chartered Accountants of Zimbabwe

ROLES AND RESPONSIBILITIES OF STANDARD-SETTING BODIES

Professional Standards Promulgated by Each Body

5. The Society is responsible for setting all professional standards. The Society is also responsible for the determination and publication of auditing and accounting standards and guidelines. Auditing standards prescribe the basic principles and practices that members of the Society are expected to follow in the conduct of an audit. Auditing guidelines provide guidance on—
• The procedures by which the auditing standards may be applied.
• The application of the auditing standards to specific items appearing in the financial statements.
• The application of auditing standards to particular sectors, industries, and service organizations.
• Specific types of reporting engagements other than audits.
• Other matters relating to the proper performance of audit work.

6. The Society prepares and promulgates Statements of Standard Accounting Practice (SSAPs). The SSAPs define standard practice on particular aspects of accounting. Before auditing and accounting standards and guidelines are issued, they are usually preceded by exposure drafts, and members are invited to comment on the contents of such drafts.

7. The Society is a member of the International Federation of Accountants and of the International Accounting Standards Committee and supports the objectives of these organizations. The Society publishes all international accounting standards and encourages their adoption for financial statements.

8. It also attempts to persuade government and authorities controlling the securities market and the business and industrial community that financial statements should comply with international accounting standards in all material respects. The Society has also agreed to incorporate the principles of international standards on auditing into its own auditing standards and guidelines.

Ethics Requirements

9. The Society has adopted statements of professional ethics similar to those of the Institute of Chartered Accountants in England and Wales. The statements cover a wide range of matters including independence, confidentiality, publicity, obtaining professional work, changes in a professional appointment, fees, and clients' monies. Rules regarding advertising are more stringent than those of the United Kingdom. It basically is not permitted in Hong Kong.

10. In the statements and accompanying guidelines, particular emphasis is placed on the requirements that a member of the Society must have integrity, be objective and competent, follow technical and professional standards, act with courtesy and consideration,
follow the ethical guidance, and generally maintain the good reputation of the profession and the Society.

PROFESSIONAL PUBLIC ACCOUNTING ORGANIZATIONS

Requirements for Membership

11. To qualify as a professional accountant, a person should be over twenty-one years of age and of good character. In addition, the person must have passed all the examinations of the Society and have acquired the prescribed period of practical experience in accounting, or be a member of one of the "approved institutes" listed in paragraph 4.

Rights of Membership

12. Only members of the Society holding the practicing certificate can undertake audits of financial statements of companies incorporated under the Companies Ordinance or other statutes.

Number of Members

13. The number of members in the Society is approximately 6,500, of which approximately 1,500 are holders of practicing certificates. There are about 590 registered firms of certified public accountants or public accountants.

CPE Requirements

14. The Society, through its CPE committee and its director for CPE, provides guidance regarding CPE and offers seminars and lectures. Although the Society has not made CPE compulsory, members are encouraged to stay abreast of professional developments and to maintain a certain level of technical knowledge.
Purpose of the Statutory Audit

15. Auditors have a statutory responsibility to report to the members of the company whether, in their opinion, the financial statements give a true and fair view of the company's affairs and whether such statements have been properly prepared in accordance with the Companies Ordinance (or other relevant legislation). There is also a professional responsibility to report if the financial statements do not comply in any material respect with the Statements of Standard Accounting Practice issued by the Society, except when, in the opinion of the auditor, such noncompliance is justified.

Entities That Are Required to Be Audited

16. The Companies Ordinance requires that every company incorporated under the Companies Ordinance must appoint an auditor whose report shall be attached to the financial statements previously approved by the company's board of directors.

Appointment and Qualifications of Auditors

17. Every company shall, at each annual general meeting of a company, appoint an auditor or auditors to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting of the company. When, at the annual general meeting of a company, no auditors are appointed or reappointed, the
court may, on the application of any member of the company, appoint a person to fill the vacancy.

18. The first auditors of a company may be appointed by the directors at any time before the first annual general meeting of the company, and auditors so appointed shall hold office until the conclusion of that meeting. If the directors fail to exercise their power to appoint an auditor, such power may be exercised by the company at the general meeting.

19. The appointment of a firm of auditors shall be deemed to be the appointment of the partners of that firm.

20. Special notice shall be given for a resolution at a general meeting concerning the removal of auditors or the appointment of auditors other than the retiring auditors. On receipt of this notice, the company must notify the auditors who have been proposed to be removed or not reappointed and, where applicable, notify the persons proposed to be appointed auditors. The auditors who have been proposed to be removed or not reappointed may present a written representation to the company and request that this representation be circulated to members to whom notice of the general meeting and the resolution are to be or have been sent. These same auditors are also entitled to attend and speak at the general meeting.

**Auditing and Reporting Responsibilities**

21. It is the auditor's responsibility to report to the members of the company whether the financial statements presented by the company's management are properly prepared in accordance with the Companies Ordinance, and whether the statements present a true and fair view of the state of the affairs of the company and its profit or loss. The audit must be conducted in accordance with auditing standards promulgated by the Society.

22. The responsibility for maintaining proper books and records and for preparing a proper set of financial statements rests with management.

23. The auditor also has a professional responsibility to note in the report all significant departures from statements of standard
accounting practice in preparing the financial statements, unless the auditor concurs with such departures and they are adequately explained in the financial statements. If the auditor considers that a departure is not justified and that the true and fair view shown by the financial statements is therefore impaired, the auditor should, in addition to referring to the notes and disclosing the necessary information in the report, express a qualified opinion and, unless it is impracticable, quantify the financial effect of the departure.

24. Under the Companies Ordinance, the auditor is also required to report by exception if he or she is unable to satisfy himself or herself that—
   a. Proper books of account have been kept.
   b. Proper returns adequate for the purposes of his or her audit have been received from branches not visited.
   c. The financial statements are in agreement with the books and the returns received from branches.
   d. He or she has obtained all the necessary information and explanations.

25. The financial statements are usually accompanied by a directors’ report, which is required under the Companies Ordinance, and may include a chairman’s statement and other information supplementary to the financial statements. To indicate that the auditor neither is responsible for nor is reporting on such a report or statements, it is usual for the auditor to be specific in his or her report as to the financial statements on which he or she is reporting by identifying the page numbers of such financial statements. Although the auditor is not responsible for the aforementioned directors’ report, he or she should ensure that the information contained therein does not conflict with financial statement disclosures.

**Filing of Reports**

26. For public companies, the audit report and the certified true copy of the financial statements are required to be filed with the Registrar of Companies, who is responsible for the registration of companies under the Companies Ordinance. Members of the general public may inspect such financial statements upon payment
of a fee. Private companies are exempted from such filing requirements. The financial statements of private companies are not required to be submitted and thus are not available to the general public.

27. The auditor's report and the financial statements are also required to be submitted to the Inland Revenue Department in support of tax returns.

SUMMARY OF SIGNIFICANT AUDITING STANDARDS AND COMPARISON WITH U.S. GENERALLY ACCEPTED AUDITING STANDARDS (GAAS)

Standards Issued

28. The Society has issued auditing standards and auditing guidelines regarding audit approach and reporting. Auditing standards prescribe the basic principles and practices that members are expected to follow in the conduct of an audit. Auditing guidelines give guidance on the procedures and techniques being applied during the audit. A list of auditing standards and guidelines is contained in appendix A.

29. While the substance in U.S. auditing standards tends to be more codified, Hong Kong standards tend to allow for more professional judgment. Various Hong Kong auditing standards and procedures are described in the following paragraphs.

30. In Hong Kong, there is no requirement to obtain written representation from the client's attorneys and legal advisors unless there are pending lawsuits or other actions against the client.

31. At present, there is no local standard or guideline on audit sampling. The auditor may apply either statistical or nonstatistical methods.

32. There is also no standard or guideline requiring the auditor to perform procedures to identify and disclose related-party transactions or to determine the impact on the financial statements of an illegal act.

33. In Hong Kong, the principal auditor is fully responsible for his or her opinion on the group's consolidated financial statements.
and, for this reason, should not refer in his or her report to the fact that the financial statements of some subsidiaries or associated companies have been audited by other auditors. Because the shareholders of the holding company are entitled to know that the financial statements of some of the companies in the group have been audited by other auditors, and also to know the materiality of those companies to the group, the appropriate information is usually disclosed in the accounting notes.

34. Auditing standards in Hong Kong do not require that the auditor's report state whether the financial statements are presented in accordance with generally accepted accounting principles. However, when expressing a true and fair opinion, the auditor should be satisfied that all relevant statements of standard accounting practice have been complied with, except in situations in which, for justifiable reasons, they should not be applied.

35. Auditing standards also do not require an auditor's report to express an opinion on consistency; however, this fundamental concept is assumed unless the contrary is stated.

36. Auditing standards in Hong Kong require either a subject to or disclaimer rather than an except for qualification when there is an audit scope limitation. The standards also require an audit qualification when there is material uncertainty.

General Standards

37. The Society has set forth guidance on professional ethics, including independence, that are similar to those in the United States. The auditing guideline on quality control advocates adequate training and competence.

38. In Hong Kong, an auditor can provide other types of services apart from an audit. However, a practice should not participate in the preparation of the accounting records of a public company audit client other than in exceptional circumstances. In all cases in which a practice is involved in the preparation of the accounting records of an audit client, particular care must be taken to ensure that the client accepts full responsibility for such records and that objectivity in conducting the audit is not impaired.
39. Although the Society has not issued an explicit auditing guideline on due care on the performance of work, it has always emphasized the need for due care in the performance of work.

**Standards of Fieldwork**

40. The Society has issued an auditing standard and guidelines concerning many areas covered by the U.S. Standards of Fieldwork, as follows:

a. *Planning, controlling, and recording*—The auditor should adequately plan, control and record his or her work.

b. *Accounting systems*—The auditor should ascertain the entity's system of recording and processing transactions and assess its adequacy as a basis for the preparation of financial statements.

c. *Internal control*—If the auditor wishes to place reliance on any internal controls, he or she should ascertain and evaluate those controls and perform compliance tests on their operation.

d. *Audit evidence*—The auditor should obtain relevant and reliable audit evidence sufficient to enable him or her to draw reasonable conclusions therefrom.

e. *Review of financial statements*—The auditor should carry out a sufficient review of the financial statements, in conjunction with the conclusions drawn from the other audit evidence obtained, to give him or her a reasonable basis for an opinion on the financial statements.

**Standards of Reporting**

41. The Society has issued an auditing standard on the audit report that applies to all reports in which the auditor expresses an opinion on financial statements intended to give a true and fair view of the company's affairs. Although the standard is not primarily intended to apply to other forms of report provided by auditors, many of the principles of this standard will normally be applicable to such reports.

42. If noncompliance with SSAPs results in impairing the true and fair position of the financial statements, the auditor should express a qualified opinion. The auditor should ensure adequate disclosures of significant departures.
43. Auditing guidelines on the auditor's report on financial statements and audit report examples have been issued to give guidance on how to apply the standard on reporting. An illustrative auditor's report is included in appendix C.

**Qualifications in Audit Reports**

44. The auditing standard on the audit report also outlines the circumstances under which a qualified report is to be issued and explains the form of qualification required. An uncertainty or audit scope limitation that is considered material but is not fundamental requires a *subject to* opinion. If the potential impact of the uncertainty or scope limitation on the financial statements is so great as to render them meaningless, a disclaimer of opinion should be issued.

45. If a qualified opinion is issued because of disagreement, an *except for* opinion will be required for a material but not fundamental item. If the impact of the disagreement on the financial statements is so great as to render them misleading, an adverse opinion should be issued.

**Dating of Audit Reports**

46. Statement of Standard Accounting Practice 9, *Accounting for Post Balance Sheet Events*, states that the date on which the financial statements are approved by the Board of Directors should be disclosed in the financial statements. In Hong Kong, the date of the auditor's report should be that on which the auditor signs his or her report on the financial statements. The auditor should not sign and date the report until the financial statements have been approved by the management and he or she has completed the audit, which includes performing procedures relating to events occurring up to the date of the report.
47. Accounting principles are set forth in Statements of Standard Accounting Practice (SSAPs) and Accounting Guidelines (AGs) issued by the Hong Kong Society of Accountants (see appendix B for a list of SSAPs and AGs). The Companies Ordinance Tenth Schedule sets forth the minimum statutory disclosure requirements for financial statements.

**FORM AND CONTENT OF FINANCIAL STATEMENTS**

**Presentation of Statements**

48. The directors of a company are required by the Companies Ordinance to submit, in every calendar year, a directors' report and audited financial statements to the members (shareholders) for their approval at the annual general meeting. The directors are also required to file with the Registrar of Companies the annual return, which provides data on the company such as its address, directors, shareholders, and composition of its share capital and debt. Public companies should also file a directors' report, auditors' report, and a certified copy of the financial statements. The filing should be made within forty-two days after the annual general meeting for the year.
49. The directors' report attached to the financial statements shall be approved by the Board of Directors and signed on behalf of the board either by the chairman of the meeting at which the financial statements are approved or by the secretary of the company. The directors' report shall include the following:

- The principal activities of the company and of its subsidiaries in the course of the financial year and any significant changes in those activities in that year
- The state of the company's affairs and its profit or loss
- The amount of dividend recommended by directors
- The proposed transfer to reserves
- Significant changes in the fixed assets of the company (or any of its subsidiaries)
- Details of issues of shares or debentures, stating the reason for the issue, the class and amount, and the consideration received for the issue
- Names of directors who held office at any time during the period
- A description of any significant contract with the company, its holding company, or subsidiary during the period in which a director was materially interested
- A statement of the existence and duration of any contract in force during the period for management and administration of the company's business, together with the name of any director's interest therein
- A description of directors' rights to acquire shares in or debentures of the company
- Total amount of donations in excess of HK$1,000 (including those made by subsidiaries). This requirement does not apply if the company is itself a wholly owned subsidiary of another company incorporated in Hong Kong
- Any other matters providing insight into the company's state of affairs

50. For private companies that claim exemption under Section 141D of the Hong Kong Companies Ordinance, certain disclosure requirements to the financial statements are waived. All the members of a private company must agree in writing that the company is to claim exemption under Section 141D with respect to the current financial year of that company.
51. The Tenth Schedule to the Companies Ordinance states the items of a limited company that should be disclosed separately in the balance sheet and profit and loss account. It requires separate disclosure of fixed assets, current assets, current liabilities, and share capital. The net current assets/current liabilities are commonly shown to disclose the working capital of the company. Special types of companies, namely banking, insurance, and shipping companies, are also exempted from certain disclosure requirements of the Tenth Schedule.

52. The Companies Ordinance does not require a statement of changes in financial position. However, SSAP 4, Statement of Changes in Financial Position, requires that, to ensure a true and fair view, such a statement should be included in the audited financial statements both for the period under review and for the corresponding previous period. Certain companies are exempted from this requirement.

53. A new statement, SSAP 15, Cash Flow Statements, has recently been issued, replacing SSAP 4. The move is in line with international accounting developments and makes the Hong Kong requirement similar to that in the United States. SSAP 15 is mandatory for accounting periods commencing on or after March 31, 1992. Entities exempted from the requirement of SSAP 15 include—

a. Unlisted entities with an annual gross income of less than HK$20 million (subject to certain exceptions).

b. A wholly owned subsidiary whose holding company prepares consolidated financial statements, including a consolidated cash flow statement in accordance with SSAP 15.

c. Banking, insurance, and shipping companies claiming exemptions under Part III of the Tenth Schedule to the Companies Ordinance.

d. Charities and nonprofit entities whose financial statements are prepared on a cash basis.

Types of Statements Prepared

54. Companies incorporated under the Companies Ordinance must prepare their financial statements in compliance with the provisions of the Companies Ordinance and SSAPs.

55. A company with subsidiaries is required by the Companies Ordinance to present group accounts at the general meeting.
Although the Companies Ordinance accepts alternative forms of presentation of group accounts, SSAP 7, *Group Accounts*, states that consolidated financial statements are generally the best means of achieving the objective of group accounts, which is to give a true and fair view of the profit or loss and of the group state of affairs. A separate profit and loss account of the holding company is not required, provided the financial statements disclose how much of the consolidated profit or loss relates to the holding company. Section 125(1)(a) of the Companies Ordinance basically requires the group financial statements to be prepared in a consolidation format.

56. A company is not required to present group financial statements if the company is itself a wholly owned subsidiary of another company. The Companies Ordinance also allows group accounts not to consolidate a subsidiary in certain circumstances including dissimilar activities, insignificant amount involved, or if the result would be misleading or harmful to the business. SSAP 7 requires a subsidiary to be excluded from consolidation in case of dissimilar activities, lack of effective control, severe restrictions on the operations of the subsidiary, or temporary control.

57. When group financial statements are not submitted (including when a company is not required to prepare group accounts, because it is a wholly owned subsidiary) or a subsidiary has not been included in the consolidated financial statements, the following details need to be disclosed:

- The reasons for exclusion
- Any qualification in audit reports on the financial statements of the subsidiaries not consolidated
- If any of this required information is not available, a statement to that effect

58. In addition, for any subsidiaries omitted from consolidated financial statements, the consolidated balance sheet must show—

- Shares in and amounts due to and from such subsidiaries.
- Number, description, and amount of shares in and debentures of the company held by such subsidiaries or their nominees.

59. Apart from these disclosure requirements, when a subsidiary is excluded from consolidation because of dissimilar activities,
the group accounts should include separate financial statements that include the following:

- Details of the holding company's interest
- Details of intragroup balances
- The nature of transactions with the group
- A reconciliation with the amount included in the consolidated financial statements for the group's investment in the subsidiary stated under the equity method of accounting

60. When a subsidiary is excluded from consolidation due to lack of effective control, it should normally be recorded in the consolidated financial statements under the equity method of accounting.

61. When a subsidiary is excluded from consolidated financial statements because of severe restrictions on control, it should normally be recorded under the equity method at the date the restrictions became effective, with no further accruals of its profits or losses. If there has been a permanent impairment in the value of the investment, a loss should be provided. The following should be disclosed regarding such a subsidiary:

- Its net assets
- Its profits or losses for the period
- Any amounts included in the consolidated profit and loss account of dividend received and writedown of the investment

62. When a subsidiary is excluded from consolidation because control is intended to be temporary, the investment should be shown as a current asset at the lower of cost or net realizable value.

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**SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES AND COMPARISON WITH U.S. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP)**

63. The fundamental accounting concepts in Hong Kong are going concern, accruals, consistency, and prudence. Significant Hong Kong accounting principles are discussed in the following paragraphs.
64. Although there is no specific pronouncement regarding the historical cost basis of recording assets and liabilities in Hong Kong, it is the predominant practice.

Alternative Accounting Methods

65. In Hong Kong, alternative accounting methods permit investments and tangible and intangible fixed assets (other than goodwill) to be stated at values other than cost. SSAP 13, *Accounting for Investment Properties*, requires that, except in certain specified circumstances, investment properties must be stated at market value determined by suitably qualified persons and not be subject to depreciation. Any changes in the value of investment properties should be treated as an adjustment to an investment property revaluation reserve, unless the total of this reserve is insufficient to cover a deficit on a portfolio basis, in which case the amount by which the deficit exceeds the total amount in the investment property revaluation reserve should be charged to the profit and loss account. Investment properties with an outstanding lease term of twenty years or less are required to be depreciated.

66. Tangible fixed assets may be recorded at a revalued amount. Except for investment properties, the valuation may be based on the directors' valuation, which is to be disclosed in notes to the financial statements.

67. If assets (other than investment properties) are revalued and effect is given to the revaluation in the financial statements, depreciation should be based on the revalued amount. Any deficit or surplus arising from a revaluation must be recorded through the revaluation reserve on an individual basis. A deficit arising from revaluation of an individual asset (to the extent not covered by reserve arising on a previous revaluation of the same asset) should be charged to the profit and loss account. In the case of assets revalued during the financial year, the name or qualification of the valuer and the basis of valuation used must be disclosed in the financial statements.

Stocks and Work in Progress

68. Stocks and work in progress should be stated at the lower of cost or net realizable value. Cost is the expenditure incurred during
the normal course of business in bringing the product or service to its present location and condition. Appropriate costing methods include: FIFO, average cost, or unit cost; methods such as base stock and LIFO are not regarded as appropriate. Net realizable value is the actual or estimated selling price less further costs to completion and all direct costs to be incurred in marketing, selling, and distributing.

69. The valuation of long-term contract work in progress is based on cost plus any attributable profit, less any foreseeable losses and progress payments received and receivable. If the outcome of the contract cannot be estimated with reasonable certainty, the completed contract method is normally used.

Depreciation

70. All fixed assets with a limited useful economic life (other than investment properties, as mentioned in paragraph 65) are required to be depreciated over their useful economic life. The depreciation should be allocated to the profit and loss account on a systematic basis for each accounting period during the useful life of the asset. The useful lives of major depreciable assets should be reviewed periodically and depreciation rates for current and future accounting periods adjusted if current expectations are significantly different from previous estimates.

71. In Hong Kong, land cannot be owned; it is, instead, leased. Leasehold land with remaining terms in excess of fifty years need not be depreciated. Leasehold land with terms under fifty years must be amortized.

Goodwill

72. Accounting Guideline Statement 2.204, Accounting for Goodwill, recommends various ways of treating goodwill. Positive goodwill arising in an acquisition may be either written off immediately against reserves or amortized through the profit and loss account. Negative goodwill should be credited directly to reserves.

Segmental Reporting

73. In Hong Kong, there is no statutory requirement to disclose information in the financial statements for each industry segment,
but there is an accounting guideline on the subject. Listed companies are required to disclose certain segmental information in their annual reports.

Receivables

74. Although there is no SSAP or AG regarding provision for doubtful receivables, it is general practice to make adequate provision for them in accordance with the concept of prudence.

Liabilities

75. Provision is made for all known liabilities. Revenue and profits are not anticipated but are only recognized when realized (in the form of either cash or other assets, the ultimate cash realization of which can be assessed with reasonable certainty).

Accounting for Leases

76. SSAP 14, *Accounting for Leases and Hire Purchase Contracts*, states the method of accounting for operating leases and finance leases as well as the disclosure requirements in the financial statements.

Pension Costs and Other Postretirement Benefits

77. There is no accounting standard on pension costs or other postretirement benefits, but for companies with a pension scheme (plan), appropriate pension costs will normally be provided for in the financial statements.

Deferred Taxes

78. SSAP 12, *Accounting for Deferred Tax*, states that timing differences should be accounted for to the extent that it is probable that a liability or asset will crystallize. Any net deferred tax debits should be recognized as assets only to the extent they are expected to be recoverable.

Foreign Currency Translation

79. SSAP 11, *Foreign Currency Translation*, states the method of translation of an entity's foreign operations in its own financial statements and translation of the financial statements of its foreign subsidiaries for consolidation purposes.
80. For individual companies, transactions denominated in a foreign currency should be translated into the reporting currency at the rate applicable on the date of the transactions. Apart from the situation discussed in the following paragraph, no subsequent translation should normally be made once nonmonetary assets have been translated and recorded. At the balance sheet date, monetary assets and liabilities denominated in a foreign currency should generally be translated using closing rates.

81. When a company has used foreign currency borrowings or forward contracts to finance or provide a hedge against its foreign currency assets, provided the conditions stated below apply, the foreign currency assets should be denominated in the appropriate foreign currencies and the carrying amounts translated at the end of each accounting period at closing rates for inclusion in the company's financial statements. Any exchange differences should be recorded in a reserve account and the exchange gains or losses arising on the borrowings or the forward contracts should then be offset as a reserve adjustment.

82. When preparing group accounts, the closing rate/net investment method of translating the financial statements should normally be used. Under this method, the amounts in the balance sheet of a foreign enterprise should be translated into the investing company's reporting currency using the closing rate of exchange. Exchange differences should be recorded as a change in reserves.

83. The profit and loss account of a foreign enterprise accounted for under the closing rate/net investment method should be translated either at the closing rate or at an average rate for the period. Any exchange difference should be recorded as a change in reserves.

84. In cases where the trade of the foreign enterprise is more dependent on the economic circumstances of the investing company's reporting currency than on its own reporting currency, the temporal method should be used. SSAP 11 defines the temporal method of translation as requiring translation of all assets, liabilities, revenue, and expenses at the exchange rate at the date on which the amount recorded in the financial statements was established. At the balance sheet date, monetary assets and liabilities are retranslated at the closing rate and any resulting exchange difference is recorded in the profit and loss account.
85. SSAP 11 also sets out the accounting treatment for speculative and nonspeculative forward exchange contracts.

86. The following disclosures are required for foreign currency translation:
   a. The method used in the translation of the financial statements of foreign enterprises and the treatment of exchange differences
   b. The net amount of exchange gains and losses on foreign currency borrowings less deposits, identifying separately those offset in reserves and those recorded in the profit and loss account
   c. The net amount of exchange gains or losses on forward contracts and any associated discount or premium offset in reserves
   d. The net change in reserves arising from exchange differences

*Capitalization of Borrowing Costs*

87. AG 2.205, *Capitalization of Borrowing Costs*, recommends the accounting practice of capitalization of borrowing costs incurred in acquiring an asset that requires a substantial period of time to prepare for use or sale.

*Mergers and Acquisitions*

88. Merger accounting is not allowed for companies incorporated in Hong Kong and there is no accounting standard on mergers and acquisitions.

*Other Accounting Issues*

89. There are no accounting standards on the following issues:
   a. Related-party disclosures
   b. Effects of inflation
   c. Research and development costs
   d. Debt extinguishments
   e. Nonmonetary transactions
90. The forms of business organization existing in Hong Kong include limited liability company, unlimited liability company, partnership, and sole proprietorship.

**Entities With Corporate Attributes**

91. A company may be registered as—

a. A limited company, that is, a company limited by shares for which the liability of a member to contribute is limited to the amount of the unpaid capital on his or her shares in the company.

b. A company limited by guarantee for which the liability of a member is limited to the amount the member has agreed to contribute in the event of the company's cessation.

c. An unlimited company in which the liability of a member is unlimited. Such companies are rare in Hong Kong.

92. Companies limited by shares are distinguished between public and private companies. A private company restricts the right of transfer of its shares, limits the number of its members to fifty, and prohibits any invitation to the public to subscribe for any shares in or debentures of the company. A public company is not necessarily a listed company, but a listed company will always be a public company.

93. A limited company must hold a general shareholders’ meeting once a year. The first annual general meeting should be held within eighteen months after its incorporation, but otherwise no
more than fifteen months may elapse between the date of one annual general meeting and the next (unless authorized by the Registrar of Companies).

94. Extraordinary general meetings may be convened at the request of directors, shareholders, auditors, liquidators, the official receiver, or the court. If requisitioned by the members, it must be made by members holding not less than one-tenth of the paid-up capital of the company.

95. Certain matters (such as a change in the authorized share capital, a change in the company's name, or alterations to the memorandum or articles of association) can only be effected with the approval of the members.

96. Although the liability of a member of a limited company is limited, a director will be penalized for failure to carry out his or her obligations as stated in the Companies Ordinance, such as the keeping of proper books and records, the presentation of audited financial statements to the members in the general meeting, and the filing of the annual return with the Companies Registrar. If the company is a listed company, the behavior of a director is also governed by other laws and nonstatutory rules and codes. A director faces unlimited liability when a company has traded fraudulently with his or her knowledge.

97. The Companies Ordinance requires a company to set up a share premium account (for shares issued at a premium) and a capital redemption reserve (for shares redeemed out of profit). These are reserves not available for dividends.

98. The Companies Ordinance defines a company's distributable profit as its accumulated undistributed realized profits less its accumulated realized losses. There are provisions in the Companies Ordinance allowing a company to purchase or redeem its own shares, or to give financial assistance for an acquisition of shares in the company.

Branch of a Foreign Company

99. A foreign corporation that establishes a place of business in Hong Kong shall, within one month of such establishment, deliver
to the Companies Registrar for registration the following:

a. A certified copy of the charter, statutes, or memorandum and articles of association of the company or other instrument defining the constitution of the company and, if the instrument is not written in English, a certified translation

b. A list of the directors and secretary of the company and other details, such as their residential addresses and nationalities

c. Name and address of the company's authorized representative resident in Hong Kong and the address of the company's principal place of business in Hong Kong

d. A memorandum of appointment or power of attorney or other document (in English or a certified translation) under the company seal, authorizing someone to act as the company's representative

e. A certified copy of the company's certificate of incorporation (or if it is not the practice where an overseas company is incorporated to issue a certificate of incorporation, such other evidence of incorporation as the Registrar of Companies deems sufficient), together with a certified translation, if the certificate is not in English

f. A certified copy of the latest financial statements of the company, unless the company is deemed equivalent to a private company

100. If there is any alteration of these documents, the company shall deliver to the Companies Registrar for registration a return containing the prescribed particulars of the alteration. Further, the foreign entity shall confirm to the Companies Registrar, at least once in every calendar year and at intervals of not more than fifteen months, that there has been no alteration to the documents discussed previously apart from any alteration already noted to the registrar.

101. A foreign entity shall also deliver annually to the Companies Registrar certified copies of—

a. Its balance sheet as of its last financial year.

b. Its profit and loss account for that year.

c. Its group accounts, if applicable.

d. Its directors' report for that year, if applicable.

e. The auditor's report on the financial statements, if any.

102. The annual confirmation as to changes and copies of audited
financial statements is not required to be filed if the company is a private company, if it was incorporated under the Companies Ordinance, or if in the opinion of the Companies Registrar the company has the same general characteristics as a private company and is not required by its local law to publish its accounts or to deliver copies to any person in whose office they may be inspected. The Companies Registrar has issued circulars specifying the information required to make a determination as to whether a foreign entity is equivalent to a private company for these purposes.

**Partnership Entities**

103. There are two types of partnerships in Hong Kong: the partnership governed by the Partnership Ordinance and the limited partnership governed by the Limited Partnership Ordinance.

104. For partnerships other than limited partnerships, each partner is liable jointly and severally with the other partners for all debts and obligations the firm incurred while he or she is a partner. The Partnership Ordinance requires partners to render true accounts and full information of all matters affecting the partnership. There are no specific accounting, auditing, and disclosure rules regarding partnerships. In the case of a limited partnership, the number of partners shall not exceed twenty and must consist of one or more general partners who shall be liable for all debts and obligations of the firm, and one or more limited partners whose liabilities are limited to the amount of their contributions. A limited partner shall not take part in the management of partnership business; otherwise, he or she shall be liable for all debts and obligations of the firm incurred while he or she takes part in the management as a general partner.

**Other Forms of Business Organization—Sole Proprietor**

105. A sole proprietor is an individual engaged in a business or profession on his or her own. As with any other form of business organization, a sole proprietor must be registered with the business registration office of the Inland Revenue Department. The financial statements of a sole proprietor need not be audited or publicly disclosed.
Registration Requirements for Public Sale

106. An offer for the sale of securities made to the public must be accompanied by a prospectus complying with the Third Schedule to the Companies Ordinance. The prospectus must be authorized (see paragraph 107) prior to being registered with the Registrar of Companies and must be accompanied by the following reports:

a. A report by the auditors and any guarantor corporation referred to in the prospectus regarding—
   - Profits and losses for the last three years and current year end assets and liabilities for the company and any guarantor corporation.
   - The rates of dividends paid by the company for each class of shares for the last three years.

b. If the proceeds of the issue of securities are to be applied directly or indirectly in the purchase of any business, a report by accountants (who shall be named in the prospectus) on—
   - The profits or losses of the business for the last five years.
   - The assets and liabilities of the business at the date of its latest financial statements.

c. A valuation report regarding the company's interests in land or buildings if such assets exceed 10 percent of the value of the company's assets, or if the value of the company's land or buildings, as reflected in the most recent financial statements, exceeds HK$3 million.

107. The authorization of a company's prospectus rests with the Securities and Futures Commission (SFC). However, the SFC has transferred to the Stock Exchange this function for shares and debentures that have been approved for listing on the Exchange.

Requirements for Listing Securities on the Stock Exchange

Requirements for Listed Companies

108. The rules governing the listing of securities on the Stock Exchange of Hong Kong Limited (the Listing Rules) define the
application procedures and requirements for the listing of securities, the contents of the listing agreement, which is an agreement to be signed between the Stock Exchange and the listed company, describing the latter's obligations, and the contents of a prospectus.

*Preparation and Filing of a Listing Application*

109. An application made to the Stock Exchange for a listing of any securities issued or to be issued must comply with the Listing Rules and any provision of law applicable and contain information that, based on the company and the securities for which application for listing is requested, is necessary to enable an investor to make an informed assessment of the company and the rights attached to such securities.

110. The Listing Rules also specify certain documents that must be submitted to the Stock Exchange for the application.

111. Once a company is listed, it must send to the Exchange, to every member of the company, and to every holder of securities (except bearer securities) the following:

a. A copy of the company's statements, together with the directors' report and auditor's report, not less than twenty-one days before the company's annual general meeting and no later than six months after the end of the financial year

b. An interim report (unaudited) for the first six months of each financial year, no later than four months from the end of that period. The interim report should also be published in the newspapers

112. The information that should be disclosed in the interim reports and annual reports are described in the Listing Rules.

**SELECTED ECONOMIC DATA**

113. Key demographic and social factors, based on 1992 Hong Kong census data, follow.

<table>
<thead>
<tr>
<th>Area (in square kilometers)</th>
<th>1,075.7</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (in millions)</td>
<td>5.8</td>
</tr>
<tr>
<td>Annual population increase</td>
<td>1.0%</td>
</tr>
</tbody>
</table>
Population under age 15 20.5%
Labor force (in millions) 2.7
Birth rate (per 1,000 population) 12.3

114. The major Hong Kong trading partners, as of 1992, are as follows:

<table>
<thead>
<tr>
<th>Country</th>
<th>Imports (HK$ million)</th>
<th>Exports (HK$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>354,348</td>
<td>61,959</td>
</tr>
<tr>
<td>Japan</td>
<td>166,191</td>
<td>10,997</td>
</tr>
<tr>
<td>Taiwan</td>
<td>87,019</td>
<td>6,500</td>
</tr>
<tr>
<td>United States</td>
<td>70,594</td>
<td>64,600</td>
</tr>
<tr>
<td>Singapore</td>
<td>39,087</td>
<td>10,360</td>
</tr>
<tr>
<td>Germany</td>
<td>21,911</td>
<td>15,956</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>19,221</td>
<td>12,541</td>
</tr>
<tr>
<td>Other</td>
<td>196,923</td>
<td>51,211</td>
</tr>
<tr>
<td></td>
<td>955,294</td>
<td>234,124</td>
</tr>
</tbody>
</table>

115. Hong Kong imports and exports for 1992 and 1991 are as follows:

<table>
<thead>
<tr>
<th>Imports (HK$ million) 1992</th>
<th>1991</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer goods</td>
<td>394,543</td>
</tr>
<tr>
<td>Raw materials</td>
<td>329,950</td>
</tr>
<tr>
<td>Capital goods</td>
<td>167,798</td>
</tr>
<tr>
<td>Food products</td>
<td>45,350</td>
</tr>
<tr>
<td>Fuel</td>
<td>17,653</td>
</tr>
<tr>
<td></td>
<td>955,294</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Exports (HK$ million) 1992</th>
<th>1991</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clothing</td>
<td>77,156</td>
</tr>
<tr>
<td>Textile yarn, fabrics, and related products</td>
<td>17,226</td>
</tr>
<tr>
<td>Watches and clocks</td>
<td>15,476</td>
</tr>
<tr>
<td>Telecommunications equipment</td>
<td>10,991</td>
</tr>
<tr>
<td>Other</td>
<td>113,275</td>
</tr>
<tr>
<td></td>
<td>234,124</td>
</tr>
</tbody>
</table>
The Accounting Profession in Hong Kong

**TAXES**

**Principal Types**

116. There is no general income tax in Hong Kong. There are three distinct taxes on income:

a. Property tax, assessed on the owners of buildings in Hong Kong

b. Salaries tax, assessed on income from any employment or pension in Hong Kong

c. Profits tax, assessed on Hong Kong source profits arising from a business conducted in Hong Kong

117. The Inland Revenue Ordinance (IRO) and Inland Revenue Rules cover the law for the three taxes. Following are certain fundamental principles common to all three taxes:

- There is no total income concept; each of the taxes is assessed without regard for other sources of the taxpayer's income. However, there are exceptions to this rule in that an individual may, in appropriate circumstances, elect for a personal assessment, which has the effect of combining all sources of his or her income into a single assessment for which he or she must file a separate total income return. Accordingly, unless an individual elects for a personal assessment, he or she does not file a return of total income but files separate returns and declarations for each of the three taxes under which he or she has income sources. The individual's total sources of income are therefore not immediately brought to the attention of the Inland Revenue Department (IRD).

- Except for the salaries tax and a personal assessment, tax is levied at a fixed standard rate and is nonprogressive.

- The extent of exposure to tax is not governed by residency status for either individuals or companies. Residency status is of certain limited relevance in specific circumstances; otherwise liability under each of the taxes is based on income that is derived from Hong Kong and certain other sources deemed by the IRO to be taxable.

- There is no provision in the Inland Revenue Ordinance that renders all items of income taxable. A feature of the system is that any item of income that does not fall within one of the three categories is not subject to tax.
• There is no tax on capital gains. A profits tax is charged on the profits on asset disposal if they are part of normal trading or constitute a speculative transaction in the nature of trade.

• There are no withholding taxes on dividends or any other source of income, other than in the case of royalties for the use of copyrights and certain other intellectual property in Hong Kong. However, there are instances when a nonresident may be assessed through an agent or certain other persons in Hong Kong, who are entitled to retain such taxes out of payments due to the nonresident.

**Year of Assessment**

118. The year of assessment begins on April 1. Each of the three taxes has its own rules regarding what income and deductions form the basis for determining assessable amounts.

**Property Tax**

119. The property tax is chargeable at the rate of 15 percent to owners of buildings situated in Hong Kong on the "net assessable value" of the buildings. Not all buildings in Hong Kong fall within the scope of the property tax. Certain areas in the New Territories are not taxed until the Governor makes a declaration in a public notice.

120. The assessable value is the actual rental income. There are various forms of exemption and relief from the property tax, for example—

• When the owner is the Hong Kong Government, a club, or a professional association.

• When the owner carries on a trade, profession, or business in Hong Kong and brings the income from the property into its profits tax computation, or the buildings are occupied for the purpose of producing profits subject to the profits tax. (A corporation carrying on a business in Hong Kong always has this exemption but is subject to the profits tax on net rental income.)

**Salaries Tax**

121. The salaries tax is imposed upon an individual's income derived in Hong Kong from any profits, pensions, and any income from services rendered in Hong Kong. Tax is levied on the actual income received for that year of assessment. The tax is the lower of
(a) assessable remuneration less expenses wholly, exclusively, and necessarily incurred, depreciation allowances, allowable charitable donations, losses computed under the salaries tax rules and personal allowances, charged at progressive rates of tax from 2 percent to 25 percent, or (b) the same net income before personal allowances, charged at the standard rate of 15 percent.

122. The salaries tax is collected by direct assessment based on a return filed at the end of the year of assessment. There is a system of provisional salaries tax for the current year of assessment, which is based on the previous year’s agreed assessment, and is normally payable in two installments.

Profits Tax

123. The profits tax is imposed on all trades, professions, and businesses in Hong Kong. The tax is based on the assessable profits arising in or derived from such enterprises in Hong Kong. There is no distinction between residents and nonresidents. The current tax rate is as follows:

<table>
<thead>
<tr>
<th>Category</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporations</td>
<td>17.5%</td>
</tr>
<tr>
<td>Others</td>
<td>15%</td>
</tr>
</tbody>
</table>

124. The taxability of profits in Hong Kong is essentially ascertained by determining whether—

a. A business is conducted in Hong Kong

b. The profits are derived from Hong Kong

125. Assessable profits are arrived at in accordance with generally accepted accounting principles as adjusted to comply with the requirements of the IRO (for example, the difference between depreciation for accounting purposes and depreciation allowance for tax purposes, or the exclusion of non-Hong Kong-sourced profits and other adjustments).

126. The general rule for deductibility of expenditure is stated in Section 16(1) of the IRO to include all expenses incurred during the year of assessment in the production of profits. Apart from this general rule for deductibility, Section 16 provides a number of circumstances where a certain expenditure is specifically deductible.

127. The IRO includes specific provisions relating to special types of business including financial institutions, life and other
insurance companies, shipping companies, airlines, and clubs and trade associations.

**Taxation of Income**

128. Certain types of receipts are deemed to be subject to the profits tax whether or not an actual trade or business is being conducted in Hong Kong. These include—

- Income from exhibition in Hong Kong of cinema, television, sound recording, or any related advertising material.
- Sums received or accrued to a person for the use or right to use patents, copyrights, designs and trademarks, and so forth.
- Sums received or accrued for hire, or rental, or similar charges for the use of or the right to use moveable property.

**Income Excluded**

129. Certain income is excluded from the profits tax, including (a) all dividend income and (b) profits or income from the sale of capital assets.

**Deductions**

130. Generally, expenses will qualify as allowable deductions in the computation of assessable profits if they have been incurred for the purpose of earning profits. A deduction for a capital expenditure is specifically excluded.

131. The following expenditures qualify as allowable deductions:

- **a.** Bad debts (subject to certain conditions)
- **b.** The cost of purchasing patent rights and certain information from a nonassociated person
- **c.** Scientific research, including payments to an approved research institute and payments for technical education
- **d.** Subject to certain limitations, contributions to an approved retirement plan
- **e.** Payments over HK$100 to approved Hong Kong charities and not exceeding 10 percent of the assessable profits for the year
- **f.** Interest paid and borrowing expenses, subject to certain restrictions
- **g.** Depreciation allowances
Statutory Disallowances

132. The following expenditures are excluded from qualifying as allowable deductions in the computation of the assessable profits:

a. An expense that has not been incurred for the purpose of producing profits chargeable to tax
b. Any expenditure of a capital nature or any loss or withdrawal of capital
c. Tax paid on behalf of any employee, except the salaries tax
d. The payment of a salary to, or interest on capital or loans to, an individual proprietor or spouse, or in the case of a partnership, payment to any partner or any partner's spouse

Deduction for Interest

133. A deduction for interest is allowed if the interest was incurred in earning assessable profits and is paid on any of the following:

a. Borrowings from a person (other than a Hong Kong or overseas financial institution) who is subject to profits tax on that interest
b. Borrowings from a financial institution (either in Hong Kong or overseas), provided that the loan is not secured or guaranteed against a deposit made with that or any other financial institution, where any interest payable on the deposit is not chargeable to Hong Kong tax
c. Borrowings wholly and exclusively to finance (provided the lender is not associated with the borrower), including—
   • Capital expenditure incurred on machinery or plant that qualifies for depreciation allowances for profits tax purposes
   • The purchase of trading stock that is used in the production of profits chargeable to the profits tax
d. Borrowings on certain publicly quoted debentures and certain commercial paper

Depreciation Allowances

134. Depreciation allowances represent the statutory means of expensing a capital expenditure, and in effect replace the depreciation charge in the financial statements.
Industrial Building Allowance

135. Qualifying expenditure must be capital expenditure incurred for the construction of an industrial building or structure occupied for a qualifying trade. An initial allowance (20 percent of the capital expenditure) is given as a deduction against taxable income. An annual allowance (4 percent of the capital expenditure) is granted for any year of assessment for which the building was in use. An offsetting allowance or charge arises when—
   a. The interest in the building is sold.
   b. The building is demolished, destroyed, or ceases to be used.
   c. If the interest is a leasehold interest, the lease ends other than in circumstances where the leaseholder acquires the reversionary interest.

Plant and Machinery

136. Plant and machinery has the largest allowance for depreciation. To qualify for these allowances, the capital expenditure must be incurred by a person carrying on a trade, profession, or business for the purposes of producing profits chargeable to the profits tax or by an employee, the use of which is essential to the production of income assessable under the salaries tax. The initial allowance is 60 percent of the qualifying expenditure. It is not necessary for the asset to be used in the basis period; it is sufficient that the expenditure is incurred while a trade, profession, or business is conducted.

137. An annual allowance is available when, at the end of a basis period for a year of assessment, a person owns and has had use of the assets for the purpose of producing profits assessable to the profits tax. This allowance is granted annually for three asset classes at rates of 10, 20, and 30 percent. Items qualifying for the same rate of annual allowance are normally grouped under one pool. The annual allowance is calculated by applying the relevant percentage on the reducing value of the asset, which is the qualifying expenditure less—
   a. The initial allowance taken on that expenditure.
   b. Previous annual allowances taken.

Sale and Leaseback and Leveraged Lease

138. Plant or equipment acquired by a lessor under a sale and leaseback arrangement will not qualify for depreciation allowances
unless the price for such acquisition is not greater than the original price paid by the vendor and no depreciation allowances on such plant and machinery have been taken by the vendor. The IRO contains the following specific measures for leveraged leases:

a. Ships and aircraft—Depreciation allowances are not available to the lessor if the lessee is not a “Hong Kong operator” (as defined) of ships or aircraft, or the lessor’s acquisition is predominantly funded by nonrecourse debt.

b. Other assets—Depreciation allowances are not available to the lessor if either—
   a. The asset is used wholly or mainly outside Hong Kong.
   b. The lessor’s purchase is predominantly funded by non-recourse debt.

For the purpose of both a and b, if the lessor contributes or is at risk for at least 50 percent of the cost of the asset, the financing is not regarded as nonrecourse debt.

**Balancing Charge or Allowance**

139. A balancing charge or allowance does not normally arise when there is a disposal. Sale proceeds are deducted from the reducing value of the relevant class of assets.

140. A balancing charge arises when, at the end of a basis period for a year of assessment, the reducing value of a class of assets is negative because the disposal proceeds for that period exceed the reducing value brought forward plus additions. The negative amount then becomes a balancing charge for the year of assessment related to the basis period.

141. When a business ceases, the reducing value of each class of assets is reduced by the sale proceeds. If this is a positive amount, it becomes a balancing allowance; if negative, it becomes a balancing charge.

**Tax Returns**

142. An assessor can under the IRO require any person to submit a return within a reasonable time. This applies to returns
for each of the three taxes and for those who choose personal assessment. Normally, one month is allowed for the submission of income tax returns.

143. There is an automatic extension available for tax representatives filing profits tax returns, provided they submit a list of clients requesting such extension. The automatic extensions are as follows:
   a. Accounting periods ending in December are extended to July 31.
   b. Accounting periods ending between January 1 and March 31 are extended to November 15.

144. An individual may apply for an additional extension, but extensions are at the discretion of the assessor. Profits tax returns usually must be submitted within one month of issue, which is normally April 1, following the year of assessment.

145. When profits tax returns are filed, they are accompanied by signed financial statements of the company. In the case of corporations, an audit report must be submitted together with the financial statements.

146. Any person receiving taxable income is obliged to inform the Commissioner of Inland Revenue in writing of such income within four months after the end of the assessment period of that income, unless he or she has already received a tax form.

147. Under the Companies Ordinance, employers are obligated to report information regarding employees and their remuneration, to ensure effective collection of the salaries tax.

Personal Assessment

148. Because the tax system does not involve a computation of total income upon which tax is charged, and only the salaries tax has personal allowances and is charged at progressive tax rates, there can be circumstances in which assessment under a total income computation would produce a smaller overall tax liability than would separate combined taxes.

149. An election for total income assessment can only be made by an individual who is either a permanent or a temporary resident. The election must be made in writing.
OTHER MATTERS OF IMPORTANCE

Anti-Avoidance Provisions

150. Section 61 of the IRO provides an assessor with the authority to disregard a transaction if it is deemed artificial or fictitious.

151. Section 61A, which confers additional powers to an Assistant Commissioner, applies to any transaction that has the effect of providing a tax benefit to the taxpayer. This occurs when it is determined that the taxpayer entered into the transaction primarily to obtain a tax benefit.

152. The following items are considered in making this determination:

a. The manner in which the transaction was entered into or carried out
b. The form and substance of the transaction
c. The tax result of the transaction without Section 61A
d. Any change in the financial position of the taxpayer that has resulted or will result from the transaction
e. Whether the transaction has created rights or obligations that would not normally be created between persons dealing with each other at arm's length under a transaction of the kind in question
f. The participation of a corporation resident in the transaction or the carrying on of a business outside of Hong Kong

153. If a transaction is covered by Section 61A, an Assistant Commissioner may assess a tax liability to the individual who has received the tax benefit in either of the following ways:

a. As if the transaction had not been entered into.
b. In such other manner as the Assistant Commissioner considers appropriate to counteract the tax benefit that would otherwise be obtained.

154. Section 61A is only intended for tax-motivated transactions. It is not intended to prohibit normal commercial transactions by which taxpayers legitimately take advantage of available tax opportunities.
APPENDIX A

Statements of Auditing Standards and Guidelines

The audit statements issued by the Hong Kong Society of Accountants as of April 1993 are as follows:

Statements of Auditing Standards

3.101 Audit Approach
3.102 The Audit Report

Statements of Auditing Guidelines

3.210 Planning, Controlling and Recording
3.211 Quality Control
3.220 Accounting Systems
3.230 Audit Evidence
3.231 Auditing Stocks and Work in Progress
3.232 Verification of Debtor Balances: Confirmation by Direct Communication
3.233 Representations by Management
3.234 Contingent Liabilities Arising From Pending Legal Matters
3.235 Analytical Review
3.240 Internal Controls
3.250 Review of Financial Statements
3.251 The Auditor’s Considerations Regarding Going Concern
3.252 Events After the Balance Sheet Date
3.253 Amounts Derived From the Preceding Financial Statements
3.254 Reports to Management
3.255 Financial Information Issued With Audited Financial Statements
3.260 Auditing in an EDP Environment—General Principles
3.261 The Effects of an EDP Environment on the Study and Evaluation of the Accounting System and Related Internal Controls
3.262 Computer-Assisted Audit Techniques (CAATs)
3.270 Engagement Letters
3.271 The Auditor’s Responsibility in Relation to Fraud, Other Irregularities and Errors
3.280 Group Financial Statements—Reliance on the Work of Other Auditors
3.281 Reliance on Internal Audit
3.282 Reliance on Other Specialists
3.283 Guidance for Internal Auditors
3.290 Audit Approach to Companies Applying Section 141D of Companies Ordinance
3.310 Reports by Auditors on Financial Statements
3.340 Prospectuses and the Reporting Accountant
3.341 Accountants’ Report on Profit Forecasts
3.401 Industry Guideline—Authorized Institutions in Hong Kong
3.402 Industry Guideline—Insurance Companies
3.403 Industry Guideline—The Audit of Commodities Dealers
3.404 Industry Guideline—The Audit of Dealers in Securities
3.405 Industry Guideline—The Audit of Solicitors’ Accounts
3.406 Industry Guideline—Banks and Deposit-Taking Companies—The Amended Section 161B and Section 161BA of the Companies Ordinance
APPENDIX B

Statements of Standard Accounting Practice and Accounting Guidelines

The accounting statements and guidelines issued by the Hong Kong Society of Accountants as of April 1993 are as follows:

Statements of Standard Accounting Practice

<table>
<thead>
<tr>
<th>SSAP</th>
<th>Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Disclosure of Accounting Policies</td>
</tr>
<tr>
<td>2</td>
<td>Extraordinary Items and Prior Year Adjustments</td>
</tr>
<tr>
<td>3</td>
<td>Stocks and Work in Progress</td>
</tr>
<tr>
<td>4</td>
<td>Statements of Changes in Financial Position</td>
</tr>
<tr>
<td>5</td>
<td>Earnings per Share</td>
</tr>
<tr>
<td>6</td>
<td>Depreciation Accounting</td>
</tr>
<tr>
<td>7</td>
<td>Group Accounts</td>
</tr>
<tr>
<td>8</td>
<td>Accounting for Contingencies</td>
</tr>
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<td>9</td>
<td>Accounting for Post Balance Sheet Events</td>
</tr>
<tr>
<td>10</td>
<td>Accounting for Associated Companies</td>
</tr>
<tr>
<td>11</td>
<td>Foreign Currency Translation</td>
</tr>
<tr>
<td>12</td>
<td>Accounting for Deferred Tax</td>
</tr>
<tr>
<td>13</td>
<td>Accounting for Investment Properties</td>
</tr>
<tr>
<td>14</td>
<td>Accounting for Leases and Hire Purchase Contracts</td>
</tr>
<tr>
<td>15</td>
<td>Cash Flow Statements (this SSAP, which supersedes SSAP 4,</td>
</tr>
<tr>
<td></td>
<td>became mandatory for accounting periods beginning on or</td>
</tr>
<tr>
<td></td>
<td>after March 31, 1992)</td>
</tr>
</tbody>
</table>

Accounting Guidelines

- **Statement 2.201** Preparation and Presentation of Accounts From Incomplete Records
- **Statement 2.202** The Effect of International Accounting Standards
The Accounting Profession in Hong Kong

Statement 2.203  *Accounts of Dealers in Securities*
Statement 2.204  *Accounting for Goodwill*
Statement 2.205  *Capitalization of Borrowing Costs*
Statement 2.206  *Reporting Financial Information by Segment*
Statement 2.207  *Accounting for Textile Quota Entitlement*
Illustrative Auditor’s Report and Financial Statements

The following financial statements are intended for illustrative purposes only. The statements presented are not intended to include all information that Hong Kong law requires. (All references to financial statement page numbers were deleted for this illustration.)

AUDITORS’ REPORT TO THE MEMBERS OF XYZ LIMITED

We have audited the accounts in accordance with Auditing Standards.

In our opinion, the accounts give a true and fair view of the state of affairs of the company and the group at June 30, 199X and of the profit and cash flows of the group for the year ended on that date, and have been properly prepared in accordance with the Companies Ordinance.

KPMG Peat Marwick,
Certified Public Accountants

Hong Kong, September 26, 199X
**XYZ LTD.**  
**CONSOLIDATED PROFIT & LOSS ACCOUNT**  
For the Year Ended June 30, 199X  
(*in Hong Kong dollars*)

<table>
<thead>
<tr>
<th>Note</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Turnover</td>
<td>1,084,895</td>
<td>985,240</td>
</tr>
<tr>
<td>Operating profit</td>
<td>130,531</td>
<td>119,583</td>
</tr>
<tr>
<td>Share of profits less losses of associated companies</td>
<td>5,500</td>
<td>4,500</td>
</tr>
<tr>
<td>Profit before taxation</td>
<td>136,031</td>
<td>124,083</td>
</tr>
<tr>
<td>Taxation</td>
<td>(22,287)</td>
<td>(20,971)</td>
</tr>
<tr>
<td>Profit after taxation</td>
<td>113,744</td>
<td>103,112</td>
</tr>
<tr>
<td>Minority interest</td>
<td>(416)</td>
<td>(167)</td>
</tr>
<tr>
<td>Profit after taxation and minority interest</td>
<td>113,328</td>
<td>102,945</td>
</tr>
<tr>
<td>Extraordinary item</td>
<td>(8,716)</td>
<td>—</td>
</tr>
<tr>
<td>Profit attributable to shareholders</td>
<td>104,612</td>
<td>102,945</td>
</tr>
<tr>
<td>Dividends</td>
<td>(90,000)</td>
<td>(76,500)</td>
</tr>
<tr>
<td>Retained profit for the year</td>
<td>14,612</td>
<td>26,445</td>
</tr>
<tr>
<td>Earnings per share</td>
<td>1.13</td>
<td>1.03</td>
</tr>
</tbody>
</table>

**Profit for the year is retained as follows:**

By the company and its subsidiaries  
13,112  
By associated companies  
1,500  
14,612  
26,445

Retained profits at July 1  
169,823  
Retained profit for the year  
14,612  
26,445  
184,435  
169,823

Less: Amount capitalized on issue of bonus shares  
10,000  
Retained profits on June 30  
174,435  
169,823

*The notes form part of these accounts.*
### CONSOLIDATED GROUP BALANCE SHEET

**At June 30, 199X**

(in Hong Kong dollars)

<table>
<thead>
<tr>
<th>Note</th>
<th>199X $'000</th>
<th>199Y $'000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed assets</td>
<td>267,369</td>
<td>213,110</td>
</tr>
<tr>
<td>Interest in associated companies</td>
<td>43,209</td>
<td>32,263</td>
</tr>
<tr>
<td>Other investments</td>
<td>6,295</td>
<td>11,604</td>
</tr>
<tr>
<td>Current assets</td>
<td>495,860</td>
<td>450,358</td>
</tr>
<tr>
<td>Less: Current liabilities</td>
<td>(289,860)</td>
<td>(250,114)</td>
</tr>
<tr>
<td>Net current assets</td>
<td>206,000</td>
<td>200,244</td>
</tr>
<tr>
<td></td>
<td>522,873</td>
<td>457,221</td>
</tr>
<tr>
<td>Long-term liabilities</td>
<td>(73,989)</td>
<td>(71,073)</td>
</tr>
<tr>
<td>Deferred taxation</td>
<td>(7,884)</td>
<td>(6,344)</td>
</tr>
<tr>
<td></td>
<td>441,000</td>
<td>379,804</td>
</tr>
</tbody>
</table>

**Representing:**

| | 199X $'000 | 199Y $'000 |
| Share capital | 100,000 | 90,000 |
| Reserves | 338,918 | 287,789 |
| Shareholders' funds | 438,918 | 377,789 |
| Minority interest | 2,082 | 2,015 |
| | 441,000 | 379,804 |

*Approved by the board of directors on September 26, 199X.*

W.S. CHAN, Director

H.C. FONG, Director

*The notes form part of these accounts.*
The Accounting Profession in Hong Kong

XYZ LTD.
CONSOLIDATED COMPANY BALANCE SHEET
At June 30, 199X
(in Hong Kong dollars)

<table>
<thead>
<tr>
<th>Note</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Fixed assets</td>
<td>10</td>
<td>112,138</td>
</tr>
<tr>
<td>Interest in subsidiaries</td>
<td>11</td>
<td>169,037</td>
</tr>
<tr>
<td>Interest in associated companies</td>
<td>12</td>
<td>4,630</td>
</tr>
<tr>
<td>Other investments</td>
<td>13</td>
<td>6,295</td>
</tr>
<tr>
<td>Current assets</td>
<td>14</td>
<td>221,545</td>
</tr>
<tr>
<td>Less: Current liabilities</td>
<td>16</td>
<td>(141,675)</td>
</tr>
<tr>
<td>Net current assets</td>
<td></td>
<td>79,870</td>
</tr>
<tr>
<td>Long-term liabilities</td>
<td>17</td>
<td>(30,164)</td>
</tr>
<tr>
<td>Deferred taxation</td>
<td>21</td>
<td>(2,560)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>339,246</td>
</tr>
</tbody>
</table>

Representing:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital</td>
<td>22</td>
<td>100,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>23</td>
<td>239,246</td>
</tr>
<tr>
<td>Shareholders' funds</td>
<td></td>
<td>339,246</td>
</tr>
</tbody>
</table>

Approved by the board of directors on September 26, 199X.

W.S. CHAN, Director
H.C. FONG, Director

The notes form part of these accounts.
XYZ LTD.
CONSOLIDATED CASH FLOW STATEMENT
For the Year Ended June 30, 199X
(in Hong Kong dollars)

<table>
<thead>
<tr>
<th>Note</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Net cash inflow from operating activities</td>
<td>25(a)</td>
<td>121,105</td>
</tr>
<tr>
<td>Returns on investments and servicing of finance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from listed investments</td>
<td>610</td>
<td>572</td>
</tr>
<tr>
<td>Interest received</td>
<td>3,200</td>
<td>4,000</td>
</tr>
<tr>
<td>Interest paid</td>
<td>(19,418)</td>
<td>(15,079)</td>
</tr>
<tr>
<td>Interest element of finance lease rentals</td>
<td>(285)</td>
<td>(270)</td>
</tr>
<tr>
<td>Dividends received from associated companies</td>
<td>3,000</td>
<td>—</td>
</tr>
<tr>
<td>Ordinary dividends paid</td>
<td>(79,500)</td>
<td>(75,000)</td>
</tr>
<tr>
<td>Dividend paid to minority interest</td>
<td>(349)</td>
<td>(87)</td>
</tr>
<tr>
<td>Net cash outflow from returns on investments and servicing of finance</td>
<td></td>
<td>(92,742)</td>
</tr>
<tr>
<td>Taxation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>HK profits tax paid</td>
<td>(12,797)</td>
<td>(11,112)</td>
</tr>
<tr>
<td>Overseas tax paid</td>
<td>(7,150)</td>
<td>(6,950)</td>
</tr>
<tr>
<td>Tax paid</td>
<td>(19,947)</td>
<td>(18,062)</td>
</tr>
<tr>
<td>Investing activities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase of fixed assets</td>
<td>(21,267)</td>
<td>(19,822)</td>
</tr>
<tr>
<td>Sale of fixed assets</td>
<td>749</td>
<td>1,008</td>
</tr>
<tr>
<td>Loans to associated companies</td>
<td>(12,005)</td>
<td>(7,197)</td>
</tr>
<tr>
<td>Loans from associated companies</td>
<td>1,759</td>
<td>906</td>
</tr>
<tr>
<td>Sale of unlisted investments</td>
<td>7,960</td>
<td>—</td>
</tr>
<tr>
<td>Purchase of subsidiary companies</td>
<td>25(c)</td>
<td>(3,145)</td>
</tr>
</tbody>
</table>

(Continued on next page)
XYZ LTD.
CONSORTIATED CASH FLOW STATEMENT (cont.)
For the Year Ended June 30, 199X
(In Hong Kong dollars)

<table>
<thead>
<tr>
<th>Note</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
</table>
|      | $'000 | $'000 | $'000 | $'000 |$
| Net cash outflow from investing activities | (25,949) | (25,105) |
| Net cash outflow before financing | (17,533) | (32,058) |
| Financing | | | |
| Capital element of finance lease rentals | | | |
| 25(c) | (1,833) | — |
| New bank loans | 25(c) | 1,100 | 2,890 |
| Net cash (outflow)/inflow from financing | (733) | 2,890 |
| Decrease in cash and cash equivalents | (18,266) | (29,168) |
| Effect of foreign exchange rates | (3,250) | 1,525 |
| Cash and cash equivalents at July 1, 199Y | 25(b) | 48,385 | 76,028 |
| Cash and cash equivalents at June 30, 199X | 25(b) | 26,869 | 48,385 |
1. **Significant Accounting Policies**

   **a. Basis of Consolidation**

   The consolidation accounts include the accounts of the company and its subsidiaries as of June 30, 199X. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from or to the date of their acquisition or disposal, as appropriate. All material intragroup transactions are eliminated in consolidation.

   **b. Associated Companies**

   The consolidated profit and loss account includes the group's share of the results of its associated companies for the year. In the consolidated balance sheet, investments in associated companies are stated at the group's share of their net assets plus any goodwill.

   **c. Goodwill or Capital Reserve on Consolidation**

   Goodwill arising in consolidation represents the excess of the cost of investments in subsidiaries and associated companies over the fair value of their separable net assets on acquisition. Goodwill is amortized on a straight-line basis to the profit and loss account over its economic life. The excess of the fair value of the net assets of subsidiaries and associated companies acquired over the cost of investments in these companies is credited to capital reserve.

   **d. Other Investments**

   Other investments are held for long-term purposes and are stated at cost less provision if the directors believe there has been a permanent diminution in the underlying value of the investment.

   **e. Properties**

     **i. Investment properties** are stated in the balance sheet at their market value. Surpluses arising from revaluations are credited to the investment property revaluation reserve; deficits arising from revaluations are first offset against any previous revaluation surpluses and are thereafter taken to the profit and loss account.

     **ii. Properties under development** are stated at cost, including interest capitalized less provisions considered necessary by the directors.

     **iii. Properties held for sale** are stated at the lower of cost or estimated net realizable value. In the case of properties developed by the
group. Cost is determined by apportionment of the total development costs attributable to unsold properties. Net realizable value represents the estimated selling price less costs to be incurred in selling the property.

*vi. Profit is recognized upon the sale of property or the issue of an occupation permit by the government, whichever is later.*

**f. Leased Assets**

Where assets are acquired under finance leases, the amounts representing the outright purchase price are included in fixed assets and the corresponding liabilities, net of finance charges, are recorded as obligations under finance leases. Depreciation is provided at rates designed to write off the cost of the assets in equal annual amounts over the shorter of the period of the leases or the anticipated useful lives of the assets as described in note 1(g). Finance charges implicit in the lease payments are charged to the profit and loss account over the period of the leases so as to produce a constant periodic rate of charge on the remaining balances of the obligations for each accounting period.

**g. Amortization and Depreciation**

1. **Investment properties.** No depreciation is provided for investment properties with an unexpired lease term of over 20 years, since the valuation takes into account each property at the date of valuation.

2. **Other properties.** No amortization is provided on freehold land and land held on long-term leases. Land held on medium- and short-term leases is amortized in equal annual installments over the remaining period of the relevant lease. Depreciation is provided to write off the cost or valuation of buildings on a straight-line basis over the remaining terms of the lease or 50 years, if shorter.

3. **Other fixed assets.** Depreciation is calculated to write off the cost of other fixed assets on a straight-line basis over their anticipated useful lives as follows:

   - Plant and machinery—10 years
   - Other fixed assets—3 to 5 years

**h. Stocks**

Stocks are valued at the lower of cost or net realizable value. Cost includes the cost of materials computed using the average-cost method and, in the case of work in progress and finished goods, direct labor and an appropriate proportion of production overhead. Net realizable value is determined by reference to the sales proceeds of items sold in the ordinary course of business subsequent to the balance sheet date or to management estimates based on prevailing market conditions.
i. **Deferred Taxation**

Deferred taxation is calculated under the liability method regarding the tax effect arising from all timing differences that are expected with reasonable probability to crystallize in the foreseeable future.

j. **Translation of Foreign Currencies**

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates at the transaction dates. Monetary assets and liabilities in foreign currencies and nonmonetary assets financed by foreign currency borrowings are translated into Hong Kong dollars at the exchange rates at the balance sheet date. Exchange gains and losses are recognized in the profit and loss account, except for those arising from the translation at closing rates of nonmonetary assets and the related foreign currency borrowings, which are taken directly to reserves.

The accounts of subsidiaries expressed in foreign currencies are translated at the rates of exchange at the balance sheet date. Exchange differences arising thereon are accounted for as a change in reserves.

k. **Operating Leases**

Rental receivables and payables under operating leases are accounted for on a straight-line basis over the period of the respective leases.

**2. Turnover**

Turnover represents the invoiced value of goods supplied to customers, rental income, and income from property trading.

**3. Operating Profit**

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>$'000</td>
<td></td>
<td>$'000</td>
</tr>
<tr>
<td>Interest on bank advances and other borrowings repayable within five years</td>
<td>19,318</td>
<td>14,779</td>
</tr>
<tr>
<td>Interest on other loans</td>
<td>400</td>
<td>400</td>
</tr>
<tr>
<td>Less: Interest capitalized</td>
<td>(3,780)</td>
<td>(3,030)</td>
</tr>
<tr>
<td>Operating profit is arrived at after charging:</td>
<td>15,938</td>
<td>12,149</td>
</tr>
</tbody>
</table>
4. Taxation

Taxation on the consolidated profit and loss account represents:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision for Hong Kong profits tax at 17.5% for the year (16.5% for 199Y)</td>
<td>13,000</td>
<td>12,500</td>
</tr>
<tr>
<td>(Overprovision)/underprovision regarding prior years</td>
<td>(403)</td>
<td>1,721</td>
</tr>
<tr>
<td>Overseas taxation</td>
<td>7,150</td>
<td>6,950</td>
</tr>
<tr>
<td>Deferred taxation (note 21)</td>
<td>1,540</td>
<td>(1,000)</td>
</tr>
<tr>
<td>Share of associated companies' taxation</td>
<td>1,000</td>
<td>800</td>
</tr>
</tbody>
</table>

Total: 22,287                      20,971

Taxation in the balance sheets represents:

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Provision for Hong Kong profits tax for the year</td>
<td>13,000</td>
<td>12,500</td>
</tr>
<tr>
<td>Provisional profits tax paid</td>
<td>(5,250)</td>
<td>(5,290)</td>
</tr>
<tr>
<td>Balance of profits tax provision relating to prior years</td>
<td>7,750</td>
<td>7,210</td>
</tr>
<tr>
<td>Less: Tax Reserve Certificate purchased under order of the Commissioner of Inland Revenue</td>
<td>(1,000)</td>
<td>(1,000)</td>
</tr>
<tr>
<td></td>
<td>6,750</td>
<td>6,950</td>
</tr>
</tbody>
</table>

5. Directors' Remuneration

Directors' remuneration disclosed pursuant to section 161 of the Companies Ordinance is as follows:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fees</td>
<td>170</td>
<td>170</td>
</tr>
<tr>
<td>Other compensation</td>
<td>5,295</td>
<td>4,387</td>
</tr>
<tr>
<td></td>
<td>5,465</td>
<td>4,557</td>
</tr>
</tbody>
</table>
6. Extraordinary Item

The extraordinary item in the consolidated profit and loss account represents the loss incurred on the closure of the electronic toys division. No tax saving arises from the loss.

7. Profit Attributable to Shareholders

The profit attributable to shareholders includes the amount of $102,764,000 ($96,270,000 for 199Y), which has been reflected in the accounts of the company.

8. Dividends

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interim dividend paid of 30 cents per share</td>
<td>$30,000</td>
<td>$27,000</td>
</tr>
<tr>
<td>(30 cents per share for 199Y)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Final dividend proposed of 60 cents per share</td>
<td>$60,000</td>
<td>$49,500</td>
</tr>
<tr>
<td>(55 cents per share for 199Y)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>$90,000</td>
<td>$76,500</td>
</tr>
</tbody>
</table>

9. Earnings per Share

The calculation of earnings per share is based on the profit after taxation and minority interest of $113,328,000 ($102,945,000 for 199Y) and 100,000,000 shares outstanding after the capitalization issued on December 8, 199Y. The earnings per share for 199Y have been restated.

10. Fixed Assets

<table>
<thead>
<tr>
<th></th>
<th>Land and Buildings</th>
<th>Investment Properties</th>
<th>Plant, Machinery, and Other Fixed Assets</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>The group</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost or valuation:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>At July 1, 199Y</td>
<td>136,434</td>
<td>58,000</td>
<td>97,690</td>
<td>292,124</td>
</tr>
<tr>
<td>Exchange adjustments</td>
<td>(1,041)</td>
<td>-</td>
<td>(1,230)</td>
<td>(2,271)</td>
</tr>
<tr>
<td>Additions</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>–Through acquisition of subsidiaries</td>
<td>-</td>
<td>-</td>
<td>2,756</td>
<td>2,756</td>
</tr>
<tr>
<td>–Other</td>
<td>10,574</td>
<td>-</td>
<td>13,632</td>
<td>24,206</td>
</tr>
<tr>
<td>Disposals</td>
<td>-</td>
<td>(4,570)</td>
<td>(4,570)</td>
<td></td>
</tr>
<tr>
<td>Surplus revaluation</td>
<td>19,488</td>
<td>26,000</td>
<td>-</td>
<td>45,488</td>
</tr>
<tr>
<td>At June 30, 199X</td>
<td>165,455</td>
<td>84,000</td>
<td>108,278</td>
<td>357,733</td>
</tr>
</tbody>
</table>

(Continued on next page)
### 10. Fixed Assets (cont.)

<table>
<thead>
<tr>
<th></th>
<th>Land and Buildings</th>
<th>Investment Properties</th>
<th>Plant, Machinery, and Other Fixed Assets</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Representing:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost</td>
<td>49,170</td>
<td>–</td>
<td>108,278</td>
<td>157,448</td>
</tr>
<tr>
<td>Valuation—199V</td>
<td>18,130</td>
<td>–</td>
<td>–</td>
<td>18,130</td>
</tr>
<tr>
<td>— 199W</td>
<td>43,960</td>
<td>–</td>
<td>–</td>
<td>43,960</td>
</tr>
<tr>
<td>— 199X</td>
<td>54,195</td>
<td>84,000</td>
<td>–</td>
<td>138,195</td>
</tr>
<tr>
<td></td>
<td>165,455</td>
<td>84,000</td>
<td>108,278</td>
<td>357,733</td>
</tr>
<tr>
<td>Aggregate amortization and depreciation:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>At July 1, 199Y</td>
<td>17,733</td>
<td>–</td>
<td>61,281</td>
<td>79,014</td>
</tr>
<tr>
<td>Exchange adjustments</td>
<td>(133)</td>
<td>–</td>
<td>(526)</td>
<td>(659)</td>
</tr>
<tr>
<td>Through acquisition of subsidiaries</td>
<td>–</td>
<td>–</td>
<td>2,000</td>
<td>2,000</td>
</tr>
<tr>
<td>Charge for the year</td>
<td>3,431</td>
<td>–</td>
<td>11,996</td>
<td>15,427</td>
</tr>
<tr>
<td>Written back on disposal</td>
<td>–</td>
<td>–</td>
<td>(3,738)</td>
<td>(3,738)</td>
</tr>
<tr>
<td>Transfer to capital reserves</td>
<td>(1,680)</td>
<td>–</td>
<td>–</td>
<td>(1,680)</td>
</tr>
<tr>
<td>At June 30, 199X</td>
<td>19,351</td>
<td>–</td>
<td>71,013</td>
<td>90,364</td>
</tr>
<tr>
<td>Net book value:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>At June 30, 199X</td>
<td>146,104</td>
<td>84,000</td>
<td>37,265</td>
<td>267,369</td>
</tr>
<tr>
<td>At June 30, 199Y</td>
<td>118,701</td>
<td>58,000</td>
<td>36,409</td>
<td>213,110</td>
</tr>
<tr>
<td>The company</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost or valuation:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>At July 1, 199Y</td>
<td>17,470</td>
<td>58,000</td>
<td>62,265</td>
<td>137,735</td>
</tr>
<tr>
<td>Additions</td>
<td>–</td>
<td>–</td>
<td>7,610</td>
<td>7,610</td>
</tr>
<tr>
<td>Disposal</td>
<td>–</td>
<td>–</td>
<td>(2,042)</td>
<td>(2,042)</td>
</tr>
<tr>
<td>Surplus revaluation</td>
<td>–</td>
<td>26,000</td>
<td>–</td>
<td>26,000</td>
</tr>
<tr>
<td></td>
<td>17,470</td>
<td>84,000</td>
<td>67,833</td>
<td>169,303</td>
</tr>
<tr>
<td>Representing:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost</td>
<td>3,200</td>
<td>–</td>
<td>67,833</td>
<td>71,033</td>
</tr>
<tr>
<td>Valuation—199W</td>
<td>14,270</td>
<td>–</td>
<td>–</td>
<td>14,270</td>
</tr>
<tr>
<td>— 199X</td>
<td>–</td>
<td>84,000</td>
<td>–</td>
<td>84,000</td>
</tr>
<tr>
<td></td>
<td>17,470</td>
<td>84,000</td>
<td>67,833</td>
<td>169,303</td>
</tr>
</tbody>
</table>
The analysis of cost or valuation of properties is as follows:

<table>
<thead>
<tr>
<th>Land and Buildings</th>
<th>Investment Properties</th>
<th>Plant, Machinery, and Other Fixed Assets</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
</tr>
</tbody>
</table>

Aggregate amortization and depreciation:

At July 1, 199Y
Charge for the year
written back on disposal
At June 30, 199X

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
</tr>
</tbody>
</table>

Net book value:

At June 30, 199Y
At June 30, 199X

The analysis of cost or valuation of properties is as follows:

<table>
<thead>
<tr>
<th>The Group</th>
<th></th>
<th>The Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>199X</td>
<td>199Y</td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
</tr>
</tbody>
</table>

In Hong Kong
- Long leases
- Medium-term leases
- Freehold outside Hong Kong

Certain leasehold land and buildings of the subsidiaries were revalued as of June 30, 199X, by Chow and Associates on an existing use basis. The revaluation surplus of $21,168,000 has been transferred to capital reserve (note 23).

Investment properties of the company were revalued as of June 30, 199X, by Lang and Associates on a market value basis calculated on net rental income. The revaluation surplus of $26,000,000 has been transferred to investment property revaluation reserve (note 23).

The net book value of fixed assets of the group and the company of $267,369,000 and $112,138,000, respectively, includes an amount of $10,354,000 ($8,975,000 for 199Y) regarding assets held under finance leases.
11. Interest in Subsidiaries

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Unlisted shares, at cost</td>
<td>55,773</td>
<td>48,497</td>
</tr>
<tr>
<td>Amounts due from subsidiaries</td>
<td>147,922</td>
<td>150,172</td>
</tr>
<tr>
<td>Less: Provision</td>
<td>(7,000)</td>
<td>(7,000)</td>
</tr>
<tr>
<td>Amounts due to subsidiaries</td>
<td>196,695</td>
<td>191,669</td>
</tr>
<tr>
<td></td>
<td>169,037</td>
<td>171,040</td>
</tr>
</tbody>
</table>

12. Interest in Associated Companies

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Unlisted shares, at cost</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Shares of net assets other than goodwill</td>
<td>11,873</td>
<td>10,373</td>
</tr>
<tr>
<td>Goodwill</td>
<td>400</td>
<td>1,200</td>
</tr>
<tr>
<td></td>
<td>12,273</td>
<td>11,573</td>
</tr>
<tr>
<td>Less: Provision</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td></td>
<td>12,273</td>
<td>11,573</td>
</tr>
<tr>
<td>Loans to associated companies</td>
<td>33,601</td>
<td>21,596</td>
</tr>
<tr>
<td></td>
<td>45,874</td>
<td>33,169</td>
</tr>
<tr>
<td>Loans from associated companies</td>
<td>(2,665)</td>
<td>(906)</td>
</tr>
<tr>
<td></td>
<td>43,209</td>
<td>32,263</td>
</tr>
</tbody>
</table>
13. Other Investments

<table>
<thead>
<tr>
<th></th>
<th>The Group and the Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
</tr>
<tr>
<td>Unlisted shares</td>
<td>$000</td>
</tr>
<tr>
<td></td>
<td>200</td>
</tr>
<tr>
<td>Listed shares</td>
<td></td>
</tr>
<tr>
<td>In Hong Kong</td>
<td>3,362</td>
</tr>
<tr>
<td>Outside Hong Kong</td>
<td>2,733</td>
</tr>
<tr>
<td></td>
<td>6,095</td>
</tr>
<tr>
<td></td>
<td>6,295</td>
</tr>
<tr>
<td>Market value of listed investments</td>
<td>7,472</td>
</tr>
</tbody>
</table>

14. Current Assets

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Properties under development</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Properties held for resale</td>
<td>91,150</td>
<td>72,520</td>
</tr>
<tr>
<td>Stocks (note 15)</td>
<td>34,265</td>
<td>40,909</td>
</tr>
<tr>
<td>Debtors, bills receivable, deposits, and prepayments</td>
<td>201,003</td>
<td>160,873</td>
</tr>
<tr>
<td>Deposits with banks and other financial institutions</td>
<td>101,584</td>
<td>79,679</td>
</tr>
<tr>
<td>Cash at bank and in hand</td>
<td>42,248</td>
<td>53,010</td>
</tr>
<tr>
<td></td>
<td>25,610</td>
<td>43,367</td>
</tr>
<tr>
<td></td>
<td>495,860</td>
<td>450,358</td>
</tr>
</tbody>
</table>

15. Stocks

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Raw materials</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Work in progress</td>
<td>72,900</td>
<td>75,133</td>
</tr>
<tr>
<td>Finished goods</td>
<td>33,675</td>
<td>40,251</td>
</tr>
<tr>
<td>Finished goods</td>
<td>84,770</td>
<td>42,166</td>
</tr>
<tr>
<td>Goods in transit</td>
<td>9,658</td>
<td>3,323</td>
</tr>
<tr>
<td></td>
<td>201,003</td>
<td>160,873</td>
</tr>
</tbody>
</table>
16. Current Liabilities

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Bank loans and overdrafts</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>(note 18)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>— secured</td>
<td>18,266</td>
<td>32,789</td>
</tr>
<tr>
<td>— unsecured</td>
<td>22,723</td>
<td>15,203</td>
</tr>
<tr>
<td></td>
<td>40,989</td>
<td>47,992</td>
</tr>
<tr>
<td>Bills payable</td>
<td>105,744</td>
<td>73,938</td>
</tr>
<tr>
<td>Creditors and accrued charges</td>
<td>67,177</td>
<td>63,034</td>
</tr>
<tr>
<td>(note 19)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amounts due to holding company and subsidiaries</td>
<td>9,200</td>
<td>8,700</td>
</tr>
<tr>
<td>Taxation (note 4)</td>
<td>6,750</td>
<td>6,950</td>
</tr>
<tr>
<td>Proposed final dividend</td>
<td>60,000</td>
<td>49,500</td>
</tr>
<tr>
<td></td>
<td>289,860</td>
<td>250,114</td>
</tr>
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</table>

17. Long-Term Liabilities

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Bank loans (note 18)</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>— secured</td>
<td>7,680</td>
<td>9,054</td>
</tr>
<tr>
<td>— unsecured</td>
<td>43,003</td>
<td>41,023</td>
</tr>
<tr>
<td></td>
<td>50,683</td>
<td>50,077</td>
</tr>
<tr>
<td>Obligations under finance leases (note 19)</td>
<td>8,430</td>
<td>7,547</td>
</tr>
<tr>
<td>Unsecured loan stock 8% 199Z</td>
<td>5,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Provision for retirement funds (note 20)</td>
<td>9,876</td>
<td>8,449</td>
</tr>
<tr>
<td></td>
<td>73,989</td>
<td>71,073</td>
</tr>
</tbody>
</table>

|                         | 199X       | 199Y        |
|                         | $000       | $000        |

Bank loans and overdrafts (note 18)

- secured
- unsecured

Bills payable

Creditors and accrued charges (note 19)

Amounts due to holding company and subsidiaries

Taxation (note 4)

Proposed final dividend

Bank loans (note 18)

- secured
- unsecured

Obligations under finance leases (note 19)

Unsecured loan stock 8% 199Z

Provision for retirement funds (note 20)
18. Bank Loans and Overdrafts

At June 30, 199X, the bank loans and overdrafts were payable as follows:

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Dollar</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Within 1 year or on demand</td>
<td>40,989</td>
<td>47,992</td>
</tr>
<tr>
<td>After 1 year but within 2 years</td>
<td>43,003</td>
<td>40,473</td>
</tr>
<tr>
<td>After 2 years but within 5 years</td>
<td>2,680</td>
<td>3,000</td>
</tr>
<tr>
<td>After 5 years</td>
<td>5,000</td>
<td>6,604</td>
</tr>
<tr>
<td></td>
<td>50,683</td>
<td>50,077</td>
</tr>
<tr>
<td></td>
<td>91,672</td>
<td>98,069</td>
</tr>
</tbody>
</table>

The banking facilities of certain subsidiaries are secured by mortgages on their land and buildings and other assets.

19. Obligations Under Finance Leases

At June 30, 199X, the group and the company had obligations under finance leases as follows:

<table>
<thead>
<tr>
<th></th>
<th>The Group and the Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
</tr>
<tr>
<td>Dollar</td>
<td>$000</td>
</tr>
<tr>
<td>Within 1 year</td>
<td>1,450</td>
</tr>
<tr>
<td>After 1 year but within 2 years</td>
<td>2,405</td>
</tr>
<tr>
<td>After 2 years but within 5 years</td>
<td>2,820</td>
</tr>
<tr>
<td>After 5 years</td>
<td>4,205</td>
</tr>
<tr>
<td></td>
<td>10,880</td>
</tr>
<tr>
<td>Finance charges relating to future periods</td>
<td>(1,240)</td>
</tr>
<tr>
<td></td>
<td>9,640</td>
</tr>
</tbody>
</table>

Amount due within one year included under "Creditors and accrued charges" (note 16)

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(1,210)</td>
<td>(987)</td>
</tr>
<tr>
<td></td>
<td>8,430</td>
<td>7,547</td>
</tr>
</tbody>
</table>
20. Provision for Retirement Funds

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th></th>
<th>The Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>At July 1</td>
<td>8,449</td>
<td>7,342</td>
<td>7,350</td>
<td>5,966</td>
</tr>
<tr>
<td>Add: Provision for the year</td>
<td>2,765</td>
<td>2,115</td>
<td>2,042</td>
<td>1,997</td>
</tr>
<tr>
<td></td>
<td>11,214</td>
<td>9,457</td>
<td>9,392</td>
<td>7,963</td>
</tr>
<tr>
<td>Less: Payments during the year</td>
<td>(1,338)</td>
<td>(978)</td>
<td>(658)</td>
<td>(613)</td>
</tr>
<tr>
<td>At June 30</td>
<td>9,876</td>
<td>8,449</td>
<td>8,734</td>
<td>7,350</td>
</tr>
</tbody>
</table>

The long-term liabilities represent funds set aside to provide for noncontractual retirement payments and long service payments in accordance with Part VB of the Employment Ordinance for the employees of the group.

21. Deferred Taxation

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th></th>
<th>The Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Balance at July 1</td>
<td>6,344</td>
<td>7,344</td>
<td>2,040</td>
<td>2,528</td>
</tr>
<tr>
<td>Transfer from/to the profit and loss account (note 4)</td>
<td>1,540</td>
<td>(1,000)</td>
<td>520</td>
<td>(488)</td>
</tr>
<tr>
<td>Balance at June 30</td>
<td>7,884</td>
<td>6,344</td>
<td>2,560</td>
<td>2,040</td>
</tr>
</tbody>
</table>

Major components of deferred tax of the group:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th></th>
<th>199Y</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Provided</td>
<td>$000</td>
<td>Potential Liabilities</td>
<td>$000</td>
<td>Potential Liabilities</td>
</tr>
<tr>
<td>Unprovided</td>
<td>$000</td>
<td>Unprovided</td>
<td>$000</td>
<td>Unprovided</td>
</tr>
<tr>
<td>Excess depreciation</td>
<td>9,354</td>
<td>10,440</td>
<td>7,830</td>
<td>2,660</td>
</tr>
<tr>
<td>General provision</td>
<td>(1,470)</td>
<td>-</td>
<td>(1,530)</td>
<td>-</td>
</tr>
<tr>
<td>Other</td>
<td>-</td>
<td>44</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>7,884</td>
<td>10,440</td>
<td>6,344</td>
<td>2,660</td>
</tr>
</tbody>
</table>
Major components of deferred tax of the company:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th></th>
<th>199Y</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Provided</td>
<td>$000</td>
<td>Unprovided</td>
<td>$000</td>
</tr>
<tr>
<td>Excess depreciation</td>
<td>3,540</td>
<td>6,585</td>
<td>3,120</td>
<td>2,295</td>
</tr>
<tr>
<td>General provision</td>
<td>(980)</td>
<td>—</td>
<td>(1,124)</td>
<td>—</td>
</tr>
<tr>
<td>Other</td>
<td>—</td>
<td>44</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>2,560</td>
<td>6,585</td>
<td>2,040</td>
<td>2,295</td>
</tr>
</tbody>
</table>

22. Share Capital

Authorized:
150,000,000 (100,000,000 for 199Y)
ordinary shares of $1 each
150,000 150,000

Issued and fully paid:
100,000,000 (90,000,000 for 199Y)
ordinary shares of $1 each
100,000 90,000

By a resolution passed at the annual general meeting held on December 8, 199Y, the company's authorized share capital was increased to $150,000,000 by the creation of an additional 50,000,000 ordinary shares of $1 each.

23. Reserves

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th>The Company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Capital reserves</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at July 1</td>
<td>17,966</td>
<td>18,561</td>
</tr>
<tr>
<td>Surplus on revaluation of land and buildings (note 10)</td>
<td>21,168</td>
<td>—</td>
</tr>
<tr>
<td>Arising on acquisition of subsidiaries</td>
<td>661</td>
<td>—</td>
</tr>
</tbody>
</table>

(Continued on next page)
23. Reserves (cont.)

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th></th>
<th>The Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td>Exchange differences on</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>translation of:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts of overseas</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>subsidiaries</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Related borrowings</td>
<td>(1,806)</td>
<td>(803)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Balance at June 30</td>
<td>38,483</td>
<td>17,966</td>
<td>13,912</td>
<td>13,912</td>
</tr>
</tbody>
</table>

Investment property revaluation reserve
At July 1
Surplus arising on revaluation of investment properties (note 10)
At June 30

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>General reserve</td>
<td>85,000</td>
<td>85,000</td>
<td>85,000</td>
<td>85,000</td>
</tr>
<tr>
<td>Retained profits at June 30</td>
<td>174,435</td>
<td>169,823</td>
<td>99,334</td>
<td>96,570</td>
</tr>
<tr>
<td></td>
<td>338,918</td>
<td>287,789</td>
<td>239,246</td>
<td>210,482</td>
</tr>
</tbody>
</table>

24. Capital and Lease Commitments

Capital commitments outstanding at June 30, 199X, not provided for in the accounts were as follows:

<table>
<thead>
<tr>
<th></th>
<th>The Group</th>
<th></th>
<th>The Company</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>199X</td>
<td>199Y</td>
<td>199X</td>
<td>199Y</td>
</tr>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Contracted for</td>
<td>1,539</td>
<td>6,376</td>
<td>500</td>
<td>374</td>
</tr>
<tr>
<td>Authorized but not contracted for</td>
<td>23,000</td>
<td>660</td>
<td>—</td>
<td>660</td>
</tr>
<tr>
<td></td>
<td>24,539</td>
<td>7,036</td>
<td>500</td>
<td>1,034</td>
</tr>
</tbody>
</table>

In addition, the company was committed at June 30, 199X, to enter into a finance lease, the capital value of payments under which amount to $1,500,000 ($1,350,000 for 199Y).
At June 30, 199X, the group and the company had commitments under operating leases to make payments in the next year as follows:

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Properties</td>
<td>Others</td>
</tr>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Leases expiring:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Within 1 year</td>
<td>—</td>
<td>800</td>
</tr>
<tr>
<td>After 1 year but within 5 years</td>
<td>1,700</td>
<td>960</td>
</tr>
<tr>
<td>After 5 years</td>
<td>—</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>1,700</td>
<td>2,760</td>
</tr>
</tbody>
</table>

25. Notes to the Cash Flow Statement

a. Reconciliation of Operating Profit to Net Cash Inflow From Operating Activities

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$000</td>
<td>$000</td>
</tr>
<tr>
<td>Operating profit</td>
<td>130,531</td>
<td>119,583</td>
</tr>
<tr>
<td>Extraordinary item</td>
<td>(8,716)</td>
<td>—</td>
</tr>
<tr>
<td>Interest and finance lease charges</td>
<td>16,243</td>
<td>12,439</td>
</tr>
<tr>
<td>Interest income</td>
<td>(3,500)</td>
<td>(4,200)</td>
</tr>
<tr>
<td>Income from listed investments</td>
<td>(610)</td>
<td>(572)</td>
</tr>
<tr>
<td>Depreciation</td>
<td>15,427</td>
<td>13,392</td>
</tr>
<tr>
<td>Loss on sale of fixed assets</td>
<td>83</td>
<td>—</td>
</tr>
<tr>
<td>Amortization of goodwill</td>
<td>800</td>
<td>920</td>
</tr>
<tr>
<td>Profit on sale of unlisted investments</td>
<td>(2,651)</td>
<td>—</td>
</tr>
<tr>
<td>Provision for retirement funds</td>
<td>2,765</td>
<td>2,115</td>
</tr>
<tr>
<td>Payments to retirement fund</td>
<td>(1,338)</td>
<td>(978)</td>
</tr>
<tr>
<td>Increase in properties under development</td>
<td>(14,850)</td>
<td>(14,450)</td>
</tr>
<tr>
<td>Decrease in properties held for resale</td>
<td>6,644</td>
<td>4,160</td>
</tr>
<tr>
<td>Increase in stocks</td>
<td>(27,835)</td>
<td>(42,790)</td>
</tr>
<tr>
<td>Increase in debt</td>
<td>(10,200)</td>
<td>(28,046)</td>
</tr>
<tr>
<td>Increase in bills payable</td>
<td>31,506</td>
<td>30,024</td>
</tr>
<tr>
<td>Decrease in other creditors</td>
<td>(16,750)</td>
<td>7,436</td>
</tr>
<tr>
<td>Increase in amounts due to group companies</td>
<td>500</td>
<td>(200)</td>
</tr>
<tr>
<td>Foreign exchange</td>
<td>3,056</td>
<td>(1,860)</td>
</tr>
<tr>
<td>Net cash inflow from operating activities</td>
<td>121,105</td>
<td>96,973</td>
</tr>
</tbody>
</table>

(Continued on next page)
25. Notes to the Cash Flow Statement (cont.)

b. Analysis of the Balances of Cash and Cash Equivalents as Shown in the Consolidated Balance Sheet

<table>
<thead>
<tr>
<th></th>
<th>199X</th>
<th>199Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposits with banks and other financial institutions</td>
<td>42,248</td>
<td>53,010</td>
</tr>
<tr>
<td>Cash at bank and in hand</td>
<td>25,610</td>
<td>43,367</td>
</tr>
<tr>
<td>Bank loans and overdrafts repayable within three months</td>
<td>(40,989)</td>
<td>(47,992)</td>
</tr>
<tr>
<td></td>
<td>26,869</td>
<td>48,385</td>
</tr>
</tbody>
</table>

c. Analysis of Changes in Financing During the Year

<table>
<thead>
<tr>
<th></th>
<th>Long-Term Bank Loans</th>
<th>Finance Lease Obligations</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$'000</td>
<td>$'000</td>
</tr>
<tr>
<td>Balance at July 1</td>
<td>50,077</td>
<td>8,534</td>
</tr>
<tr>
<td>Cash flows from financing</td>
<td>1,100</td>
<td>(1,833)</td>
</tr>
<tr>
<td>Inception of finance lease contracts</td>
<td>—</td>
<td>2,939</td>
</tr>
<tr>
<td>Effect of foreign exchange rates</td>
<td>(494)</td>
<td>—</td>
</tr>
<tr>
<td>Balance at June 30</td>
<td>50,683</td>
<td>9,640</td>
</tr>
</tbody>
</table>

d. Purchase of Subsidiaries

Net assets acquired

<table>
<thead>
<tr>
<th></th>
<th>$'000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed assets</td>
<td>756</td>
</tr>
<tr>
<td>Stocks</td>
<td>12,295</td>
</tr>
<tr>
<td>Debtors, bills receivable, deposits, and prepayments</td>
<td>11,405</td>
</tr>
<tr>
<td>Cash at bank and in hand</td>
<td>9,498</td>
</tr>
<tr>
<td>Creditors and accruals</td>
<td>(20,650)</td>
</tr>
<tr>
<td>Capital reserve arising on consolidation</td>
<td>(661)</td>
</tr>
</tbody>
</table>

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Satisfied by: cash paid</td>
<td>12,643</td>
</tr>
</tbody>
</table>
**e. Analysis of the Net Outflow of Cash and Cash Equivalents in Respect of the Purchase of Subsidiaries**

<table>
<thead>
<tr>
<th>Description</th>
<th>$000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash consideration</td>
<td>12,643</td>
</tr>
<tr>
<td>Cash at bank and in hand acquired</td>
<td>(9,498)</td>
</tr>
<tr>
<td>Net outflow of cash and cash equivalents in respect of the purchase of subsidiaries</td>
<td>3,145</td>
</tr>
</tbody>
</table>
# Checklist for Comparison of Generally Accepted Auditing Standards (GAAS) in the United States With Auditing Standards in Hong Kong

## General Information

<table>
<thead>
<tr>
<th>General Information</th>
<th>Answer</th>
<th>Comments</th>
</tr>
</thead>
</table>
| 1. Is a primary purpose of an audit—  
   a. To attest to information used by investors, creditors, etc.?  
   b. To satisfy statutory requirements (for example, the Companies Act)?  
   c. For tax purposes? | No  
Yes  
No | 1b. The primary purpose of an audit is to satisfy statutory requirements in the Hong Kong Companies Ordinance.  
2A. The Hong Kong Society of Accountants has issued auditing standards that prescribe the basic principles and practices that members are expected to follow in the conduct of an audit. Auditing guidelines are also issued to provide information on—  
• Procedures regarding application of the auditing standards.  
• The application of the auditing standards to specific items in the financial statements. |
| 2. A. The United States has ten generally accepted auditing standards including general standards, standards of field work, and standards of reporting. Those standards and their interpretations constitute U.S. generally accepted auditing standards, which have been published in *Codification of Statements on Auditing Standards*. Do generally accepted auditing standards exist in Hong Kong? | Yes | |
The application of auditing standards to particular industries and service organizations.

Specific types of engagements other than normal audits.

Other matters relating to the proper performance of audit work.

3. The Hong Kong Society of Accountants.

<table>
<thead>
<tr>
<th>U.S. Generally Accepted Auditing Standards</th>
<th>Required by Government or Professional Pronouncements</th>
<th>Predominant Practice</th>
<th>Minority Practice</th>
<th>Not Done</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>5. Do auditors observe inventory counts? (AU 331)</td>
<td>Yes. Auditing Guideline 3.231</td>
<td>✔️</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Do auditors receive written representations from management? (AU 333)</td>
<td>Yes. Auditing Guideline 3.233</td>
<td>✔️</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Notes:

Checklist was completed from the perspective of performing a local audit, not a referral audit.

AU numbers refer to sections in the Codification of Statements on Auditing Standards, unless otherwise noted.

This checklist does not include the latest GAAS pronouncements issued in the United States.

<table>
<thead>
<tr>
<th>U.S. Generally Accepted Auditing Standards</th>
<th>Required by Government or Professional Pronouncements</th>
<th>Predominant Practice</th>
<th>Minority Practice</th>
<th>Not Done</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>7. Do auditors receive written representa-tions from management's legal counsel? (AU 337)</td>
<td>No</td>
<td></td>
<td></td>
<td>✓</td>
<td>7. Normally obtained only when there are pending lawsuits or other actions against the company.</td>
</tr>
<tr>
<td>8. A. Do auditors prepare and maintain working papers? (AU 339)</td>
<td>Yes. Auditing Guideline 3.210</td>
<td></td>
<td></td>
<td>✓</td>
<td>8B. Written audit programs are usually included in the audit work papers.</td>
</tr>
<tr>
<td>B. If so, do they include a written audit program outlining procedures to be performed? (AU 339)</td>
<td>See Comment</td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>9. Do auditors obtain a sufficient understanding of the internal control structure to plan the audit and determine the nature, extent, and timing of tests to be performed? (AU 319)</td>
<td>Yes. Auditing Guideline 3.240</td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>10. A. Do auditors communicate reportable conditions in the internal control structure to the audit committee? (AU 325)</td>
<td>Yes. Auditing Guideline 3.240</td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>B. If so, is the communication documented? (AU 325)</td>
<td>Yes. Auditing Guidelines 3.240 and 3.254</td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>11. In obtaining evidential matter, does the auditor apply either statistical or nonstatistical procedures? (AU 350)</td>
<td>No</td>
<td></td>
<td></td>
<td>✓</td>
<td>11. The auditor may apply statistical or nonstatistical sampling methods.</td>
</tr>
<tr>
<td>12. Is the auditor responsible for designing the audit to provide reasonable assurance of detecting errors and irregularities that are</td>
<td>Yes. Auditing Guideline 3.271</td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
</tbody>
</table>
13. A. Does the auditor perform procedures to identify related-party transactions and their effects on the financial statements? (AU 334)

No

B. If so, list the procedures.

13B. Although not required, procedures may include—

- Obtaining management representations concerning the names of all related parties, including details of the affiliation of directors and officers with other entities.
- Reviewing the register of members to identify substantial shareholders if they have not made use of nominees to hold the shares.
- Reviewing minutes of board meetings, with particular reference to any declaration of interest by a director.
- Reviewing the previous year's audit file and discussing the situation with the auditors of other group companies.

14. Does the auditor consider the adequacy of cutoff procedures to ensure that movements into and out of inventories are properly identified in the accounting records? (AU 313)

Yes. Auditing Guideline 3.231
<table>
<thead>
<tr>
<th>U.S. Generally Accepted Auditing Standards</th>
<th>Required by Government or Professional Pronouncements</th>
<th>Predominant Practice</th>
<th>Minority Practice</th>
<th>Not Done</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>15. A. Are specific auditing procedures applied to transactions occurring after the balance-sheet date? (AU 560)</td>
<td>Yes. Auditing Guideline 3.252</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Are other auditing procedures applied to ascertain the occurrence of subsequent events that require adjustment to or disclosure in the financial statements? (AU 560)</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>16. The concept of &quot;joint auditors&quot; in certain countries (e.g., U.K., Canada, and Australia) is that two auditors or audit firms jointly audit the financial statements of a company and issue a single report signed by the two firms. This practice is not generally followed in the U.S. Does the concept of &quot;joint auditors&quot; exist in Hong Kong?</td>
<td>See Comment</td>
<td></td>
<td></td>
<td></td>
<td>16. The concept of &quot;joint auditors&quot; exists and is similar to the concept in the U.K., Canada, and Australia. Very few companies appoint joint auditors.</td>
</tr>
<tr>
<td>17. When a principal auditor is reporting on financial statements that include one or more subsidiaries, divisions, branches, or investees: (AU 543)</td>
<td>Yes. Auditing Guidelines 3.280 and 3.310</td>
<td></td>
<td></td>
<td></td>
<td>17A. In order to ensure that the other auditor has conducted a proper audit, the principal auditor may send out a questionnaire to the other auditor or may examine his or her audit work papers.</td>
</tr>
</tbody>
</table>
B. May the principal auditor decide not to assume that responsibility by making reference to the other auditor and indicating the division of responsibility?

No. Auditing Guidelines 3.280 and 3.310

17B. Reference in the audit report to other auditors would not reduce the principal auditor's responsibility for his or her opinion on the financial statements of the group.

18. A. Is there a standard form of auditor's report? (AU 508)

Yes. Auditing Guideline 3.310

18B. See paragraphs 44 and 45 of text.

B. List the circumstances that require a departure from the standard report and indicate the type of report required. (AU 508)

19A,B. The auditor is not required to express an opinion on the consistency of application of accounting principles. However, any change in significant accounting principles and its effect on the financial statements are required to be disclosed in the notes to the financial statements.

19. A. Does the auditor's report require an explanatory paragraph for a change in accounting principles or in the method of their application? (AU 508)

No

B. If not, does it imply that either consistency exists or the financial statements disclose the inconsistency?

See Comment

20A,B. The date of the audit report will normally be as near as possible to the date of actual approval and signing of the financial statements by the directors. The auditor can never date the report earlier than the date on which the financial statements are approved by the directors.

20. A. Is the auditor's report dated as of the last day of fieldwork? (AU 530)

No. Auditing Guideline 3.252

B. If not, what date is used?

See Comment

21. To express an opinion, must the auditor be independent?

Yes

21. Professional independence is a fundamental concept.
22. The standards are as follows:

a. Standards for certain specialized industries (for example, deposit-taking companies, commodities dealers, solicitors).

b. Audit approach to companies applying section 141D of the Companies Ordinance, under which some disclosure requirements are waived for certain private companies.
# APPENDIX E

## Checklist for Comparison of Generally Accepted Accounting Principles (GAAP) in the United States With Accounting Principles in Hong Kong

**General Information**

1. Are there generally accepted accounting principles in Hong Kong? If so, are they codified?
   - **Answer:** Yes
   - **Comments:** The generally accepted accounting principles in Hong Kong are codified in Statements of Standard Accounting Practice and Accounting Guidelines.

2. Who is responsible for promulgating accounting principles (for example, the profession, a governmental body, etc.)?
   - **Answer:** The profession
   - **Comments:** The Hong Kong Society of Accountants is responsible for promulgating Statements of Standard Accounting Practice.

<table>
<thead>
<tr>
<th>U.S. Generally Accepted Accounting Principles</th>
<th>Required by Government or Professional Pronouncements</th>
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<th>Minority Practice</th>
<th>Not Done</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>3. Are assets and liabilities recorded on the historical-cost basis?</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Notes:**

References in the U.S. Generally Accepted Accounting Principles column are to sections in the *FASB Current Text*, unless otherwise noted.

This checklist does not include the latest GAAP pronouncements issued in the United States.

SSAPs — Statements of Standard Accounting Practice issued by the Hong Kong Society of Accountants.
4. Are interest costs, incurred while activities that are necessary to get an asset ready for its intended use are in progress, capitalized as part of the historical cost of an asset? (167)  
   - Required by Government or Professional Pronouncements: Recommended in Accounting Guideline 2.205

5. A. Is a general revaluation (either upward or downward) of assets permitted? (D40)  
   - Yes. SSAPs 6 and 13
   - B. If so, define the basis.

6. Are nonmonetary transactions that culminate an earnings process accounted for on the basis of the fair market value of the assets involved when that value is determinable within reasonable limits? (N35)  
   - No

7. Is revenue recognized when it is earned and its realization is reasonably assured (rather than when money is received)? (Statement of Financial Accounting Concepts No. 5)  
   - Yes. SSAP 1

5A. It is generally permitted to revalue assets; however, except for investment properties, there is no specific accounting standard.

5B. SSAP 13 requires investment properties to be valued annually at their market value. The basis for revaluing other assets is not mentioned in SSAPs, but the general practice is to use fair value.
8. Are costs recorded when incurred rather than when money is paid? (Statement of Financial Accounting Concepts No. 5) Yes. SSAP 1

9. A. Are consolidated financial statements required when one company has a controlling financial interest over another company? (C51) Yes. SSAP 7

B. Is control usually indicated by ownership of over 50 percent of the outstanding voting shares? If not, how is control indicated? Yes. SSAP 7

10. A. Are there instances when an entity would not be consolidated even though control is present? (C51) Yes. SSAP 7

B. If so, list them.

10B. An entity would not be consolidated—

a. When the activities of the subsidiaries are very dissimilar to those of other companies within the group.

b. When the subsidiaries operate under severe restrictions that significantly impair control of the holding company over the subsidiaries' assets and operations for the foreseeable future.

c. When control is intended to be temporary.

d. If the controlling company itself is 100 percent owned by another company.
<table>
<thead>
<tr>
<th>Question</th>
<th>Required by Government or Professional Pronouncements</th>
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<th>Not Done</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>11. If consolidation is not otherwise appropriate, is the equity method used for unconsolidated subsidiaries, corporate joint ventures, and other investees if the investments give the investor the ability to exercise significant influence over the investees' operating and financial policies? (I82)</td>
<td>Yes. SSAPs 7 and 10</td>
<td></td>
<td></td>
<td></td>
<td>12. Hong Kong does not have an accounting standard regarding accounting for mergers and acquisitions. It does, however, prescribe procedures to use in allocating purchase consideration for purchased subsidiaries.</td>
</tr>
<tr>
<td>13. Is the method used to account for a business combination disclosed? (B50)</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>14. A. Do criteria exist for treatment of business combinations as a pooling of interests? (B50)</td>
<td>No</td>
<td></td>
<td></td>
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<tr>
<td>B. If so, list the criteria.</td>
<td></td>
<td></td>
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</tbody>
</table>
| 15. A. Is goodwill arising from a business combination accounted for as an asset? (I60) | Yes. Accounting Guideline 2.204                        |                      |       |          | 15A. Under Accounting Guideline 2.204 goodwill may be—
  • Written off at the time of acquisition to reserves.
  • Amortized over a defined period.                                       |
16. Are the following disclosures made for related-party transactions: (R36)
   a. The nature of the relationship? Yes. Accounting Guideline 2.204
   b. A description of the transactions for the period presented? Yes.
   c. The amounts of the transactions for the period presented? Yes.
   d. The amounts due to or from related parties at the balance sheet date? Yes.

17. Is an estimated loss from a loss contingency accrued only if it is probable that an asset has been impaired or a liability incurred and the amount of loss can be reasonably estimated? (C59)
   Yes. SSAP 8

18. If a loss contingency is not accrued because both conditions for accrual listed in question 17 are not met, is disclosure of the contingency required when there is at least a reasonable possibility that a loss may have been incurred? (C59)
   Yes. SSAP 8 and Tenth Schedule to the Companies Ordinance

16a-d. There are limited requirements for the disclosure of some specified related-party information in the Companies Ordinance. These include loans to officers, intergroup balances, directors' interests in significant contracts, and directors' rights to acquire shares in or debentures of the company. The Stock Exchange's Listing Rules require the disclosure of material transactions with directors and chief executives and substantial shareholders (10 percent or more of voting shares) and their associates. Disclosure of other related-party transactions is relatively rare.
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<thead>
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</tr>
</thead>
<tbody>
<tr>
<td>19. Are guarantees of the indebtedness of others or other loss contingencies disclosed in financial statements even though the possibility of loss may be remote? (In the U.S., guarantees are usually disclosed as loss contingencies even if the possibility of loss is remote.) (C59)</td>
<td>Yes. SSAP 8 and Tenth Schedule to the Companies Ordinance</td>
<td>✓</td>
<td></td>
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<tr>
<td>20. Are the following items disclosed in a public enterprise's financial statements for each industry segment: (S20)</td>
<td></td>
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</tr>
<tr>
<td>a. Sales to outsiders and inter-segment sales?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td>✓</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b. Operating profit or loss?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td>✓</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c. Identifiable assets and related depreciation, depletion, and amortization expense?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>d. Capital expenditures?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>e. Equity in net income and net assets of unconsolidated subsidiaries and other investees?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>f. Effect of a change in accounting principle?</td>
<td>Yes. Accounting Guideline 2.206</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>21. A. Are there any requirements or recommendations to disclose the effects of inflation? (C28)</td>
<td>No</td>
<td></td>
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<tr>
<td>B. If so, list the disclosures required.</td>
<td></td>
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</tbody>
</table>
22. Are assets segregated into current and noncurrent classifications with a total for current assets presented? (B05)
   Yes. In accordance with the Companies Ordinance

23. A. Are noncurrent assets those not expected to be realized within one year or the current operating cycle? (B05)
   No

   B. If not, how are noncurrent assets defined?
   See Comment

24. A. Is an allowance established for uncollectible receivables? (C59)
   No

   B. If so, what is the basis (e.g., percentage of sales, aging of receivables, etc.) for calculating the allowance?

25. Are receivables and payables not arising in the normal course of business or subject to normal trade terms, recorded at an amount that takes imputed interest into account? (I69)
   No

26. A. Is inventory stated at the lower of cost or market (or net realizable value)? (I78)
   Yes. SSAP 3

   B. If not, how is inventory stated?
   Yes. SSAP 3

   C. Is the basis disclosed?
   Yes. SSAP 3

27. Does cost for inventory purposes include: (I78)
   a. Materials? Yes. SSAP 3
   b. Direct labor? Yes. SSAP 3
   c. Factory overhead? Yes. SSAP 3

22. See paragraph 51 of text.

23A, B. Though not statutorily defined, noncurrent assets are generally regarded as those not expected to be realized within one year or the current operating cycle.

24A. Although not required, in practice an allowance is established for receivables if collection is considered doubtful.
<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>d.  If the answer to c is yes, is an allocable share of all factory overhead included?</td>
<td>Yes. SSAP 3</td>
<td>✓</td>
<td></td>
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</tr>
</tbody>
</table>

28. A. Are the following cost methods permitted for reporting purposes: (I78)
   a. First-in, first-out (FIFO)? Yes. SSAP 3  ✓
   b. Last-in, first-out (LIFO)? No
   c. Average cost? Yes. SSAP 3  ✓

B. Are the same methods permitted for tax purposes?

29. Is the inventory costing method used disclosed? (I78) Yes. SSAPs 1 and 3  ✓

30. A. Are fixed assets depreciated over their estimated useful lives by systematic charges to income? (D40) Yes. SSAP 6  ✓
   B. If so, is an accumulated depreciation account used? Yes  ✓

31. Are disclosures made of—(D40)
   a. Depreciation expense for the period? Yes. SSAP 6 and Tenth Schedule to the Companies Ordinance  ✓
   b. Balances of major classes of depreciable assets? Yes. SSAP 6 and Tenth Schedule to the Companies Ordinance  ✓
<p>| | |</p>
<table>
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</thead>
<tbody>
<tr>
<td><strong>c.</strong> The methods used to compute depreciation for the major asset classes?</td>
<td>Yes. SSAP 6 and Tenth Schedule to the Companies Ordinance</td>
</tr>
<tr>
<td><strong>d.</strong> Accumulated depreciation, either by major class of assets or in total?</td>
<td>Yes. SSAP 6 and Tenth Schedule to the Companies Ordinance</td>
</tr>
</tbody>
</table>

32. **A.** Do criteria exist for classifying leases as operating leases? (L10)  
   **B.** If so, list the criteria and disclosure requirements.  
   Yes. SSAP 14

33. **A.** Do criteria exist for classifying leases as other than operating leases for the lessor and lessee? (L10)  
   **B.** If so, list the criteria, type of lease, and disclosure requirements.  
   Yes. SSAP 14

34. Are liabilities segregated into current and noncurrent classifications with a total for current liabilities presented? (B05)  
   No

35. **A.** Are noncurrent liabilities those whose liquidation is not expected to require the use of current assets or the creation of current liabilities? (B05)  
   No  
   **B.** If not, how are noncurrent liabilities defined?  
   See Comment

32A,B. The standard defines an operating lease as other than a finance lease, and a finance lease is one that transfers substantially all the risks and rewards of ownership of an asset to the lessee.

33A,B. See response to question 32.

34. The general practice is to segregate liabilities into current and noncurrent classifications. See paragraph 51 of text.

35B. Though not defined, noncurrent liabilities are generally regarded as those not due within twelve months of the balance sheet date.
<table>
<thead>
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</thead>
<tbody>
<tr>
<td>36. For notes payable, is disclosure made of— (C32)</td>
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<td></td>
<td></td>
<td></td>
<td>36. For loans exceeding 5 years, disclosure is required of the repayment terms and the interest rate.</td>
</tr>
<tr>
<td>a. Interest rates?</td>
<td>Yes. Companies Ordinance</td>
<td></td>
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<tr>
<td>b. Maturities?</td>
<td>Yes. Companies Ordinance</td>
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<tr>
<td>c. Assets pledged as collateral?</td>
<td>Yes. Companies Ordinance</td>
<td></td>
<td></td>
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<tr>
<td>d. Covenants to reduce debt?</td>
<td>Yes</td>
<td></td>
<td></td>
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<tr>
<td>e. Minimum working capital requirements?</td>
<td>Yes</td>
<td></td>
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<tr>
<td>f. Dividend restrictions?</td>
<td>Yes</td>
<td></td>
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</tr>
<tr>
<td>37. A. For long-term construction-type contracts, are the percentage-of-completion and completed-contract methods used? (Co4)</td>
<td>Yes. SSAP 3</td>
<td></td>
<td></td>
<td></td>
<td>37A,B. SSAP 3 states that the percentage-of-completion method should be used unless the contract's outcome is uncertain and therefore it would be prudent not to recognize income. Losses are always recognized immediately.</td>
</tr>
<tr>
<td>B. If so, what are the criteria for determining the method to be used?</td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>38. A. Are research costs charged to expense when incurred? (R50)</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
<td>38A. Various treatments exist. They are often capitalized together with development costs, and the aggregate value evaluated for recoverability.</td>
</tr>
<tr>
<td>B. Are such costs disclosed?</td>
<td>See Comment</td>
<td></td>
<td></td>
<td></td>
<td>38B. Not disclosed, unless they are extraordinary.</td>
</tr>
<tr>
<td>39. A. Are development costs charged to expense when incurred? (R50)</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
<td>39A. Various treatments exist. See comment to question 38A.</td>
</tr>
</tbody>
</table>
B. Are such costs disclosed?

39B. Not disclosed unless they are extraordinary.

40A. Extraordinary items are material events or transactions outside the ordinary activities of the business and not expected to recur regularly.

40. A. In the U.S., events and transactions are presented in the income statement as extraordinary items when they are unusual in nature and are of the type that would not reasonably be expected to recur in the foreseeable future. Do similar criteria for identifying extraordinary items exist in Hong Kong? (I17)

41. Are material events or transactions that are unusual in nature or expected to occur infrequently, but not both (and thus do not meet the criteria for classification as extraordinary), shown as a separate component of income or expense? (I22)

42. A. Are disclosures required for—
   a. Extraordinary items? (I17)
   b. Material events or transactions not classified as extraordinary items? (I22)
   c. Disposal of a segment of a business? (I13)

B. Indicate the financial statement presentation of these items.

83
43. A. Are pension costs provided for covered employees over the term of employment? (P16) No

B. If so, do they include charges for costs assigned under the actuarial method used for years prior to the plan's inception?

44. A. Are specific disclosures required relating to pension plans? (P16) No

B. If so, list them.

45. A. When accounting income and taxable income differ, are deferred income taxes recorded for temporary differences (as opposed to permanent differences)? (I25) Yes. SSAP 12

B. If so, are deferred taxes provided for all temporary differences (as opposed to only those meeting certain criteria)? Yes. SSAP 12

c. Profit after extraordinary items

Other material events or transactions, including disposals, could be disclosed as an exceptional item or in a note to the financial statements.

43A. There are no accounting standards for pension costs. Due to the absence of any standard, various treatments exist.

45A,B. SSAP 12 requires deferred tax accounting using the liability method. Deferred taxes should be recognized for all timing differences resulting in a future asset or liability.
46. A. Are deferred taxes determined on the basis of current tax rates? (I25)
   B. If not, on what basis?

47. A. Is specific information related to income taxes required to be disclosed? (I25)
   B. If so, list the requirements.

48. A. Are operating losses reported on the income tax return allowed to be carried back to earlier periods? (I25)
   B. If so, are the tax effects of a loss carryback included in the income in the period?

49. A. Are operating losses reported on the income tax return allowed to be carried forward? (I25)
   B. If so, are the tax effects of a loss carryforward included in the income in the period realized?

50. Are financial statements of a foreign entity prepared for consolidated purposes measured in the currency of the primary economic environment in which the entity operates? (F60)

51. Are all elements of financial statements translated at current exchange rates? (F60)

46B. Rate expected when timing differences reverse.

47A,B. Required disclosure: (a) Hong Kong tax and basis of computation and (b) overseas tax and any special circumstances affecting the tax liability for the period or succeeding periods.

48A. Tax losses can only be used to set off assessable profit in future periods.

49A. Tax losses can be used to set off assessable profit in future periods.

49B. They are normally included as a reduction of the tax charge for the period.
<table>
<thead>
<tr>
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<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>52. A. Are translation adjustments reported separately? (F60)</td>
<td>Yes. SSAP 11</td>
<td></td>
<td></td>
<td></td>
<td>52A-C. See paragraphs 79 through 85 of text.</td>
</tr>
<tr>
<td>B. Are they accumulated in a separate component of stockholders' equity until ultimately realized?</td>
<td>No</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>C. Is there an analysis of the changes during the period in the component of stockholders' equity relating to translation adjustments?</td>
<td>Yes. SSAP 11</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>53. A. Are gains and losses resulting from transactions denominated in a currency other than that of the environment in which the entity operates included in determining net income for the period in which the exchange rate changes? (F60)</td>
<td>Yes. SSAP 11</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Is the aggregate transaction gain or loss included in determining net income for the period disclosed in the financial statements or notes?</td>
<td>See Comment</td>
<td></td>
<td></td>
<td></td>
<td>53B. SSAP 11 requires disclosure only of exchange differences on foreign currency borrowings less deposits.</td>
</tr>
<tr>
<td>54. Are gains or losses on foreign currency transactions that are intended to hedge a foreign currency commitment deferred and included in the related transactions? (F60)</td>
<td>Yes. SSAP 11</td>
<td></td>
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</tr>
</tbody>
</table>
55. What information is disclosed about foreign currency restrictions? (F60)

56. Are significant events arising subsequent to the balance sheet date reflected in the financial statements or notes thereto? (C59)

57. Please list any standards in Hong Kong for which there are no corresponding U.S. standards.

55. There should be disclosure of limitations on a subsidiary's or associated company's ability to distribute its retained profits because of exchange control restrictions.

57. None
Bibliography

The information in this booklet was compiled from many sources in Hong Kong. Significant references follow.

- Companies Ordinance
- Inland Revenue Ordinance
- Hong Kong Society of Accountants
  - Auditing Standards and Guidelines
  - Statements of Standard Accounting Practice and Accounting Guidelines
- Stock Exchange: Rules governing the listing of securities
- Securities (Stock Exchange Listing) Rules
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