A+
Driving business success
Issue 6 / Volume 14 / June 2018

Plus:

Bridge to Zhuhai
New opportunities across the delta for Hong Kong

Profile
Clement Chan, Managing Director at BDO Hong Kong

CPA ballers
The Institute's champion basketballers

IFRS 17 represents a fundamental change for the insurance sector. Are insurers ready?

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"The Council thank Raphael Ding for his service to the Institute, and wish him all the best for his future endeavours."

Dear members,

Further to my previous email in May and update in my column in the April issue of *A Plus* on the subject, I am using my column this month to update you on the actions of Council in relation to the extraordinary general meeting Resolutions.

Concerning Resolution 1 on the redistribution of the reserves held by the Institute.

Council has completed its holistic review of the fee structure and decided to introduce a membership fee waiver for 2019 and 2020 for members whose names were on the register at 31 December 2017. The fee waiver for 2019 will be for the full fee (i.e. HK$2,300), and a review will be conducted before 2020 to determine the appropriate level of the waiver, ensuring sufficient reserves are maintained for expected operating expenses.

In addition, fees for most CPD seminars will be reduced by 20 percent from 1 July 2018, non-PC holder partner's annual registration fees will be halved, and the eligible age for waiver of membership fee will be lowered to 65. For more details, please see the abridged Council minutes for the month of May 2018 available in the "Members' area" of the Institute's website.

Concerning Resolution 2 on implementing one member, one vote for the election of the president and vice-presidents.

A Taskforce has been set up and considered several options proposed by the management, with the objective of holding a poll of all members under the current Council election framework. The Taskforce is examining practicality and seeking legal advice. Given the resolution's potential bearing on the Professional Accountants Ordinance, amendment of the legislation will also be considered in parallel.

Concerning Resolution 3 on the recruitment of Chief Executive and Registrar.

The Search Committee has engaged Korn Ferry as the recruitment consultant for a global search. The committee will meet again in July to consider the list of potential candidates.

Raphael Ding will serve out his contract on 30 June 2018. The Council thank him for his service to the Institute, and wish him all the best for his future endeavours.

Jonathan Ng, Executive Director, Education and Training, will be the Acting Registrar from 1 July 2018.

Eric Tong
President

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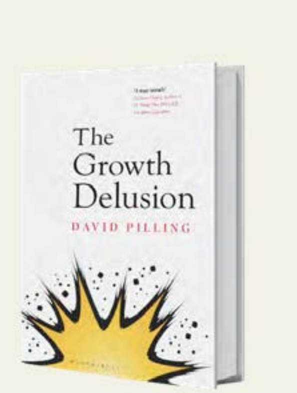

Book review

Driving business success

About our name
A Plus stands for excellence, a reference to our top-notch accountant members who are success ingredients in business and in society. It is also the quality that we strive for in this magazine — going an extra mile to reach beyond Grade A.

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News

Institute news   Accounting news

Institute news

Signing of RMA with CPA Canada

The Institute's reciprocal membership agreement (RMA) with CPA Canada (formerly Canadian Institute of Chartered Accountants) has been renewed with effect from 1 June, enabling eligible members of each body to apply for membership of the other body without further examination or test. Further details for Institute members interested in applying for CPA Canada membership can be found on the CPA Canada website, while CPA Canada members interested in joining the Institute may refer to our website.

Institute raises suggestions for effective implementation of the Greater Bay Area Initiative with representatives from Guangdong government

The Hong Kong Coalition of Professional Services (HKCPS) organized a delegation of its member bodies to visit Guangdong on 1 and 2 June. Patrick Law, Vice President of the Institute and a member of the board of HKCPS, led the Institute's delegation.

During the visit, the delegation met Guangdong government representatives and requested that the government relax the requirements that the partner of an accounting firm must reside in Mainland China for no less than six months every year; and the main shareholder/partner of an accounting firm must be a Mainland citizen. The Institute also asked to add Hong Kong CPAs who are Hong Kong permanent residents but not members of the Chinese Institute of Certified Public Accountants to the list of "Other Professionals" eligible to take up partner positions in special general partnership firms. In response, the government officials committed to making continuous efforts to open the Greater Bay Area (GBA) market.

The delegation also visited new transport infrastructure designed to support economic development in the GBA.

Becoming an insolvency specialist

The Specialist Designation in Insolvency is open to members with considerable experience and competencies in insolvency practice, and who have gained the SQ (Insolvency). Holders of the Specialist Designation in Insolvency are entitled to use "SD (Insolvency)" after their names. The current round of applications will close on 6 August.

Current Affairs Series

Over 370 members attended the Current Affairs Series seminar on 22 June where Matthew Cheung Kin-chung, Chief Secretary for Administration, shared his insights on how the new business opportunities brought by the Greater Bay Area and the Belt and Road initiatives will drive the continuous growth and prosperity of Hong Kong.

Hong Kong and Guangdong CPA alliance meeting

A meeting for the Hong Kong and Guangdong CPA Alliance firms, jointly organized by the Institute and Guangdong Institute of Certified Public Accountants (GDICPA), took place this month. Led by the Institute's Vice President, Johnson Kong, nearly 30 Hong Kong delegates including representatives from Alliance firms and SMP Committee members, were joined by over 40 of their

The Hong Kong and Guangdong CPA alliance meeting

RSCP Singing Competition winner Natalie Tam with Institute President Eric Tong

Guangdong counterparts led by Yuan Qing, Secretary General of GDICPA.

RSCP annual dinner and singing competition

Institute member Natalie Tam won the solo category at the Recreation and Sports Club for Hong Kong Professional Bodies Singing Competition on 26 May. The event featured exciting performances by singing contestants, including lawyers, barristers, doctors, dentists, architects and surveyors, infront of more than 180 attendees.

Institute's annual Sports and Recreation Night

Members are invited to join the fun and frivolities of the upcoming Sports and Recreation Night on 27 July. Meet your fellow CPA athletes or reconnect with old teammates at the dinner party. Enrol by 11 July.

Council meetings minutes

The abridged minutes from the April and May Council meetings are now available for members to read. They can be found in the "Members' area" of the Institute's website.

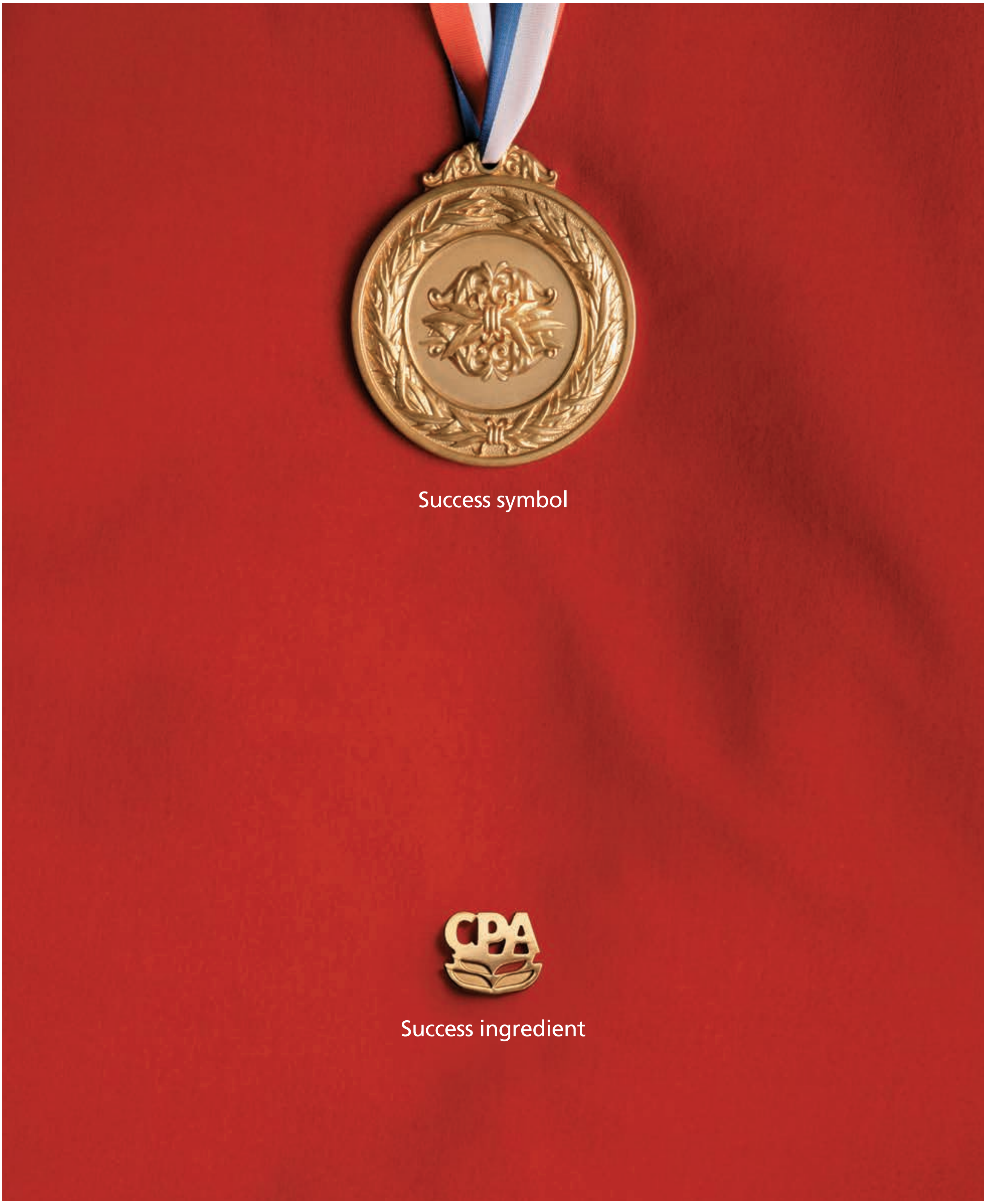
Disciplinary findings

Yan Kwok Ting, Sunny, CPA

Complaint: Being guilty of dishonourable conduct.

Yan was employed by Core Pacific-Yamaichi Capital Ltd. (CPYC) as personal assistant to the head of corporate finance. During that time he was a licensed person under the Securities and Futures Ordinance (Cap. 571). In January 2005, the Securities and Futures Commission (SFC) commenced an investigation into due diligence work performed by CPYC in sponsoring a listing on the Growth Enterprise Market board. The SFC started the investigation after finding CPYC's earlier submissions to the Stock Exchange of Hong Kong gave an unjustified impression that the due diligence work on the sponsored listing was sufficient.

During the SFC enquiries, CPYC's head of corporate finance submitted new evidence to the SFC which ostensibly allayed his responsibility for the earlier misleading submissions to the Stock Exchange. Yan provided information in a statutory declaration and in



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an interview with the SFC, which attempted to support the validity of the new evidence. The SFC determined that the new evidence was fabricated or forged, and the information provided by Yan was also false. On this basis, the SFC concluded Yan was guilty of providing false or misleading information to the SFC. He was prohibited from re-entering the industry for 4 years.

Yan later applied to the Securities and Futures Appeals Tribunal (SFAT) to review the decision of the SFC. The SFAT dismissed the application after an extensive hearing.

Decisions and reasons: Yan was removed from the register of CPAs for 5 years with effect from 13 June 2018 and was ordered to pay costs of the disciplinary proceedings of HK$262,499. When making its decision, the Disciplinary Committee noted that the SFAT based its conclusion on a careful and comprehensive survey of the evidence which indicated that Yan was aware of the falsity in the new evidence. The committee further noted it was clear from the SFAT's verdict that Yan had given materially false or misleading statements to the SFC, which was clearly dishonourable conduct. The committee found Yan's conduct amounted to a serious breach of integrity, which is a fundamental requirement of the profession. His failure to cooperate with the Institute at an early stage led to additional time and expense being incurred, warranting the award of full costs to the complainant.

Yeung Tat Kwong, CPA (practising)

Complaint: Failure or neglect to observe, maintain or otherwise apply professional standards issued by the Institute.

The Institute received a referral from The Law Society of Hong Kong about the Accountant's Reports issued by Yeung, in which he failed to report breaches of the Solicitors' Accounts Rules by a firm of solicitors over three years. The firm did not prepare client account reconciliations, client ledgers and office ledgers. During the Institute's enquiry, Yeung was unable to provide copies of his working papers, claiming that the hardcopies were misplaced and his computer hard disk had failed.

Decisions and reasons: Yeung was reprimanded and ordered to pay a penalty of HK$100,000 and costs of HK$49,335. When making its decision, the committee noted in particular that Yeung's reasons for the unavailability of the working papers were highly unsatisfactory, and his failure to act as a proper safeguard to monitor the compliance of solicitor firms involved public interest.

Chan Kin Cheong, CPA (practising)

Complaint: Failure or neglect to observe, maintain or otherwise apply (i) the fundamental principle of integrity under paragraphs 100.5(a), 110.1 and 110.2 of the Code of Ethics for Professional Accountants; (ii) Hong Kong Standard on Quality Control 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*; and (iii) Hong Kong Standard on Auditing 500 *Audit Evidence.*

Chan is the sole proprietor of Dynamic Dragons & Co., CPA and TCY CPA Limited (collectively "the practices"). He is responsible for the practices' quality control system and the quality of the practices' audit engagements. When carrying out a practice review, the reviewer found that the practices failed to implement adequate quality control systems. Also, a number of significant deficiencies were found in the reviewed engagements. In addition, Chan was found to have provided false and/or misleading answers in the practice review and in the electronic self–assessment questionnaire.

Decisions and reasons: Chan was reprimanded and ordered to pay a penalty of HK$60,000 and costs of the disciplinary proceedings of HK$34,175. When making its decision, the Disciplinary Committee took into consideration the particulars in support of the complaint, the parties' submissions, the conduct of Chan throughout the proceedings and his personal circumstances.

Details of the disciplinary findings are available at the Institute's website: *www.hkicpa.org.hk.*

Illustration by Harry Harrison

KPMG South Africa to cut up to 400 staff

KPMG South Africa announced this month that it is closing regional offices and cutting up to 400 staff as the scandal-hit firm aims to reshape its business after losing numerous clients this year.

The firm is closing offices in Mbombela, Polokwane, East London and Bloemfontein, and focusing on its operations in Johannesburg, Cape Town, Durban and Port Elizabeth. Newly appointed Chief Executive Officer of the South African firm, Nhlamulo Dlomu, said she regretted the decisions made, but deemed them necessary. “We are taking all possible steps to ensure these changes are managed in a caring manner and that everyone is treated with dignity,” she said.

KPMG’s South African branch has faced criticism since August 2017 over work done for a company owned by the politically influential Gupta family and its auditing of VBS Mutual Bank, which collapsed in March, leading KPMG to audit its own staff. Barclays Africa Group also cut ties with the firm amid the controversy. KPMG has appointed nine new executives in 2017 in a bid to restore trust in the firm.

SMPs in Singapore to receive grant

Small accounting firms in Singapore will receive a S$2.4 million (HK$13.8 million) boost to go digital, reported *The Straits Times* this month. The move is part of a new programme that aims to create 2,000 new accounting jobs in the next two years and help firms adopt new technologies and expand abroad. According to a census conducted by the Singapore Accountancy Commission, Big Four firms spent the most on technology while small- to-medium-sized firms spent the least mainly due to cost and a lack of knowledge, resulting in lower productivity. Lee Fook Chiew, Chief Executive Officer of the Institute of Singapore Chartered Accountants, said efforts to future-proof the accountancy profession are "especially vital in a time of rapid transformation and evolution of new skills."

Record number of SFC licensees in Hong Kong

Financial firms licensed by the Securities and Futures Commission (SFC) rose to a record number at the end of March, according to data by the Hong Kong regulator. "The total number of [individual] licensees in Hong Kong reached a historical high of 44,238, up 3 percent from the previous year, while the number of licensed corporations surpassed the 2,700 mark," said the SFC. Fund managers, private equity investors, brokers and other financial firms have been drawn to Asia's third-largest financial market as a number of companies are expected to launch their initial public offerings in Hong Kong this year, reported the media. The surge has improved the finances of the SFC, which collects fees from every transaction in the market. The watchdog reported a fiscal surplus of HK$242.86 million for the year ended in March.

PwC U.K. to scrap all-male job shortlists

In a bid to improve the percentage of female executives in the office, PwC U.K. announced it will ban all-male job shortlists, starting this month. The pay gap between men and women is 44 percent at PwC U.K., the highest of the Big Four firms, according to the firm's report on gender pay gap released in March. Laura Hinton, Chief People Officer at PwC U.K., was quoted as saying, "we are setting ourselves a 50/50 target for all direct recruitment activity. This is part of our wider action plan to promote diversity and inclusion in all forms, including gender, ethnicity and social mobility."

Credibility of U.K. accounting watchdog to be reviewed

The United Kingdom's business ministry formally launched a review of the country's accounting regulator this month. "The FRC's work is critical to financial markets, the economy and public confidence. Trust, quality and credibility are the questions at the heart of today's consultation," said John Kingman, who is chairing the review of the Financial Reporting Council (FRC). The FRC has long been scrutinized by lawmakers for being too slow in probing accounting scandals. The review will consider whether the FRC is using its existing powers sufficiently to levy fines and ban accountants involved in malpractice. It will also look at whether legislation is needed to give the watchdog stronger powers after the FRC said it cannot pursue company officials who are not members of professional accounting bodies, reported *Reuters*.

A world of numbers

1

921

The number of public companies EY audits out of 6,167 in the United States – more than any other Big Four firm. The firm has held the top spot in public company audit engagements for the past two years, according to a 2017 report by Audit Analytics.

£4 million

The tax bill owed by English football club Aston Villa. The club is working with Her Majesty's Revenue and Customs to resolve the issue and aims to pay in instalments, according to *The Guardian*.

¥91.8 billion

The amount of annual total revenue recorded by China's accounting firms at the end of 2017, according to the Chinese Institute of Certified Public Accountants. The sector has been growing rapidly, with 46 firms posting over 100 million yuan in revenue last year, and 12 seeing revenue above 1 billion yuan.

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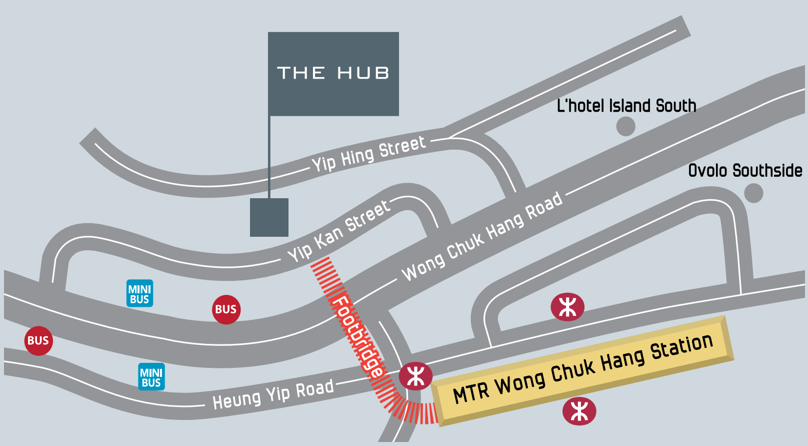

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Cristiano Ronaldo

1 Trump threatens Harley-Davidson with tax

United States President Donald Trump threatened Harley-Davidson with tax on Twitter on 26 June, a day after the motorcycle maker announced it was moving some production to Asia to mitigate the impact of Trump's tariffs on European steel and aluminium. Trump tweeted: "The Aura will be gone and they will be taxed like never before!" He was referring to tariffs Harley-Davidson would face on motorcycles produced overseas and shipped back to the U.S. for sale. Europe is Harley's second-largest market. The company said that the 31 percent tariff the European Union is imposing on its motorcycles would raise the cost of each bike it ships from the U.S. by around US$2,200.

2 KPMG U.K. introduces yoga to fight stress

KPMG U.K. has added yoga to its three-day training programme in a bid to help its staff reduce stress. The programme, called KPMG audit university, will focus on audit quality and involve sessions on resilience and management alongside wellbeing, according to *Economia*. "Auditors are under significant pressure to perform and I think stress levels are increasing," said Michelle Hinchcliffe, Head of Audit at the firm in the United Kingdom, who set up the programme. "The leadership have to help staff to deal with the criticism over the quality of audits, both technically and mentally." The course is open to new and current staff as well as partners from June until September.

3 Hong Kong tops IPO charts

Hong Kong initial public offerings (IPOs) have topped global rankings, with an estimated 98 IPOs in the first half of the year, according to EY's *Global IPO trends Q1 2018* report. The New York Stock Exchange saw 35 IPOs in the same period, according to *CNBC*. With Xiaomi planning to raise up to US$6.1 billion in its Hong Kong IPO and online services platform Meituan-Dianping's IPO seeking over US$4 billion, EY forecasts a total of HK$200 billion in funds to be raised by IPOs in the city this year. Asia-Pacific IPO Leader at EY, Ringo Choi, said, "We expect that the second half will be a very, very busy time for us."

4 Cristiano Ronaldo settles tax fraud charges

Footballer Cristiano Ronaldo agreed to a two-year suspended jail sentence and a €18.8 million (HK$171.5 million) fine to settle tax evasion charges. Prosecutors in Spain accused the Real Madrid footballer of defrauding the authorities of €14.8million (HK$135.2 million) in unpaid taxes between 2011 and 2014. He has denied the allegations. According to *Reuters*, the Portuguese player is unlikely to serve the prison sentence due to a Spanish rule that allows first offenders to serve probation if the sentence is fewer than two years. Ronaldo, who plays for his national team, was informed of the heavy fine before a World Cup match against Spain.

BRIDGE TO BUSINESS

With the opening of the Hong Kong-Zhuhai-Macau Bridge, Martin Evan-Jones reports on why Zhuhai is the new growth opportunity for Hong Kong businesses

A new highway to profitability for Hong Kong-based businesses focused on Mainland China – that's how senior Big Four executives describe the Hong Kong-Zhuhai-Macau Bridge (HKZMB), expected to open in the second half of this year.

Zhuhai, a prefecture-level city on the southern coast of Guangdong province, is seen as the next big opportunity on the Mainland across infrastructure, real estate development and services, which include high-end affordable living, hotels, tourism, medical and eco-areas and technology services. As the city jumps from "small to big," Hong Kong services are set to contribute to and facilitate Zhuhai's increasing foreign direct investment (FDI).

For Hong Kong-based CPAs, advisory services and initial public offerings (IPOs) are also part of China's latest goal to transform Zhuhai as a hub for the western Pearl River Delta and propel China's Greater Bay Area Initiative to become the largest and most lucrative "bay area" in the world.

"Out of the 11 cities in the Greater Bay Area, Hong Kong and Zhuhai have the first and tenth largest gross domestic profit (GDP), respectively. The HKZMB will offer a new dimension to boost Zhuhai's economy, and enhance connectivity to Hong Kong and other cities in the Greater Bay Area," says Ayesha Lau, Managing Partner for Hong Kong, KPMG China.

From small to big

The availability of space and generally lower property prices in Zhuhai spells profit for property developers in Hong Kong, who have been buying property within the Mainland city for the last three years.

They are likely to be rewarded with a great value deal by the opening of the HKZMB

Photo credit: AFP

creating more convenient transportation between Hong Kong and the western Pearl River Delta. Selected property prices are already beginning to rise from a low base on the prospect.

PwC's Assurance Partner Hong Kong, Loretta Fong, asserts: "Zhuhai's GDP compound annual growth rate is one of the highest in China at 11.7 percent from 2008 to 2017: it also ranks fifth in terms of GDP per capita at 153,000 yuan with a population of only 1.7 million."

Indeed, PwC's *Chinese Cities of Opportunities* report this year, covering 30 leading Mainland cities, assesses Zhuhai as top under transportation and urban planning criteria. The city was also rated first for culture and quality of life, with its urban development strategy scoring for scientific development, education goals, balanced industrial distribution and research and development, among other sub-categories.

Furthermore, Dennis Chow, Southern Region Managing Partner of Deloitte China describes Zhuhai's 9 percent annual GDP growth as "faster than most cities in China, with consumption growth leading other cities in Guangdong Province." Chow also says Zhuhai had 12,000 project starts over the past five years, representing some US$13 billion in FDI.

About 900 companies invested in by Hong Kong investors are established in Zhuhai's Hengqin special zone adjacent to Macau, according to Hong Kong-based news website *EJ Insight*, many engaged in innovation and technology as well as tourism. Faster and cheaper links to Hong Kong via the HKZMB are expected to energize those investments and broaden corporate opportunities.

Bridge work

With three bridges, three artificial islands and an undersea tunnel, the HKZMB stretches over 55 km to connect the three cities across traffic routes. The HKZMB reduces the road from Hong Kong to and from Macau and Zhuhai to within one hour, ensuring the western Pearl River Delta is within three-hours drive from Hong Kong.

The bridge's development challenges include 10 worker casualties, cost overruns of 10 billion yuan, an alleged "fake concrete" case, possible subsidence of artificial islands to support the bridge as well as protests over endangerment to ocean life. However, the bridge is still set to be the largest and most operationally efficient of its type in the world. Consultants for Hong Kong, Zhuhai and Macau expect daily traffic flows across the HKZMB to reach 29,100 vehicles in 2030 and 42,000 in 2037, with daily passenger trips of 126,000 and 175,000.

The main bridge in Mainland waters and the link roads and ports in Hong Kong, Zhuhai and Macau will be open 24 hours daily. The bridge link will include 24-hour transport services in Hong Kong, as well as cross-boundary shuttle bus services, coaches, hire cars, goods vehicles and private cars. However, coordinated information has yet to be released on the investment in and full gamut of transport services to be offered.

Cross-boundary shuttle bus services linking Hong Kong with Zhuhai will be operated by a consortium comprising the Hong Kong-Zhuhai-Macau Land Transportation (Macau) Corporation, the Zhuhai Yuegong Xinhai Transportation Company, and the Hong Kong Zhuhai Macau Bridge Shuttle Bus Services.

The *South China Morning Post* reported that a one way trip from Hong Kong to Zhuhai is to cost HK$80 via the joint venture transport shuttle bus

Consultants for Hong Kong, Zhuhai and Macau expect daily traffic flows across the HKZMB to reach 29,100 vehicles in 2030 and 42,000 in 2037.

Fireworks explode over the world's longest cross-sea bridge, the Hong Kong-Zhuhai-Macau Bridge, after the major work of the bridge was completed in Zhuhai city on 31 December 2017.

Photo credit: AFP

service, operating up to 140 buses daily between the three-city checkpoints – substantially lower than the current coach and ferry links between Hong Kong, Macau and Shenzhen.

One Bus Hong Kong Macau, operating 19 of 34 permits issued by the Hong Kong government and formed by nine investors, is expected to run a fleet of 19 luxury coaches – costing HK$95 million in total – to Macau and Zhuhai and charge between HK$160 and HK$180 per trip.

In addition, a consortium including Kwoon Chung Motors, China National Travel Service (HK) Group, Chu Kong Shipping, Shun Tak Group and the Motor Transport Company of Guangdong and Hong Kong have won a five-year extendable franchise to operate a 24-hour inter-city bus service with a total investment of HK$500 million, according to *EJ Insight*.

An investment centre

Zhuhai aims to establish itself as an innovation-driven city developing smart manufacturing, robotics and smart homes. The city has pillar industries including electronic information, bio-pharmaceutical products,

Tourists walk under a huge LED screen displaying videos of marine life at the Chimelong Ocean Kingdom, the largest ocean theme park in the world, in Hengqin island of Zhuhai

electrical appliances, petrochemicals and precision machinery, according to the Hong Kong Trade Development Council. There is also a significant agricultural and marine economy focused on its port with manufacturing accounting for 35.6 percent of its utilized FDI in 2017.

PwC's Fong says Zhuhai is uniquely situated on the western side of the Greater Bay Area, and is well connected, linking it within and outside the Mainland. "In [China's] 13th Five-Year Plan (2016-2020), the metropolis is expected to be connected to an integrated transportation network, including the Guangzhou-Foshan-Jiangmen-Zhuhai Intercity Railway with an investment of 40 billion yuan. It also has the convenience of having its own airport – Zhuhai Jinwan Airport – and is adjacent to the coastline. This certainly gives a great advantage for the import/export of goods in and out of the Chinese Mainland."

Much focus is on the Zhuhai's environmental and residential opportunities. "The HKZMB will enhance connectivity to Zhuhai, which will help develop a quality living environment in the city, encourage residential development, and create greater opportunities for new infrastructure and real estate players," says Lau of KPMG. She adds that Hong Kong developers have significant experience and

"It also has the convenience of having its own airport – Zhuhai Jinwan Airport – and is adjacent to the coastline. This certainly gives a great advantage for the import/export of goods in and out of the Chinese Mainland."

Photo credit: AFP

"We can envision bus-loads of CPAs travelling to Zhuhai."

capabilities to capitalize on these opportunities.

"Zhuhai is known as the 'garden city' with a lot of land – over 70 percent available – with ecological value. With a number of tourist spots and a theme park close by, it has a lot of potential to build an eco-tourism industry and receive a substantial uplift in GDP," says Fong.

Chow at Deloitte is particularly enthusiastic about opportunities for Hong Kong retirees – so-called "elderly tourism"– given the closer proximity to Hong Kong hospitals and medical centres with the opening of the HKZMB, believing that a number of Hong Kong companies are interested in creating and supporting new elderly-friendly property developments in Zhuhai.

A source in the Hong Kong insurance industry said that relocation of local elderly policy holders to Zhuhai will lower risk factors while increasing new insurance business, provided that appropriate residential accommodation is available, and immigration back and forth across the boundary checkpoints is smooth.

"Zhuhai is a very 'livable' city with good air quality and many places to go on packaged holidays. I strongly believe Hong Kong leisure and tourism companies will benefit from 'tourism in two cities' linking Zhuhai and Macau," Chow says. "Additionally, Hong Kong International Airport is already a hub for tourism in and out of the Mainland, and I believe it will become more significant still."

How CPAs can take part

As part of the Greater Bay Area Initiative, individual cities are encouraged to introduce policies that will reduce disparities in terms of industry focus and capabilities. "Hong Kong CPAs can assist in this policy setting by harmonizing education, social security and medical care, for example. The success of the initiative cannot be achieved without facilitating the movement of people within the bay area," says Fong of PwC.

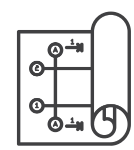
Lau adds, "development opportunities in Zhuhai will require financing, and Hong Kong's CPAs and professional services firms are well-placed to advise on a range of areas, including finance, tax and insurance."

State-level goals to develop Zhuhai's technology sector and port development, for example, will require domestic and international CPAs to facilitate success, and Chow sees opportunities for those in Hong Kong. "We can envision bus-loads of CPAs travelling to Zhuhai," he quips. With established centres in Macau and Shenzhen, Zhuhai is yet to be on the agenda for a new Deloitte office, and Chow says the firm is watching developments closely, with possible merger and acquisition prospects.

With international exposure, Hong Kong CPAs can assist in further promoting FDI into various industries in Zhuhai and arranging for Hong Kong-based IPOs. "While there are mutual exemptions on professional qualifications and work experience for Mainland and Hong Kong CPAs," says Fong, "the overall demand for CPAs is expected to increase, and further collaboration will be essential."

Edmund Wong, Practising Director at Patrick Wong C.P.A. Limited, and an Institute member, believes some of his clients might take this opportunity to establish their presence in Zhuhai and/or Macau to better serve customers in those areas. This, he says, is where Hong Kong CPAs come in. "As Institute members, we are well trained and equipped with a broadened global vision, and have international experience. We can serve as the middleman and bridge our clients to appropriate professional parties in China to explore new markets, providing valuable advice to our clients in the process," he says.

Wong, a member of the Institute's Small and Medium Practitioners (SMPs) Committee, says that with the opening of the bridge, this is the time for SMPs to differentiate themselves from the competition, and support the internationalization of small businesses. "I strongly encourage our fellow members to join Institute study missions and tours to different cities in China, establish relationships with local CPAs, and look for opportunities," he says. "Our connections, experience, knowledge and exposure are actually valuable assets and we should unleash them."



PwC's *Chinese Cities of Opportunities* report this year, covering 30 leading Mainland cities, rated Zhuhai first for culture and quality of life, with its urban development strategy scoring for scientific development, education goals, balanced industrial distribution and research and development.

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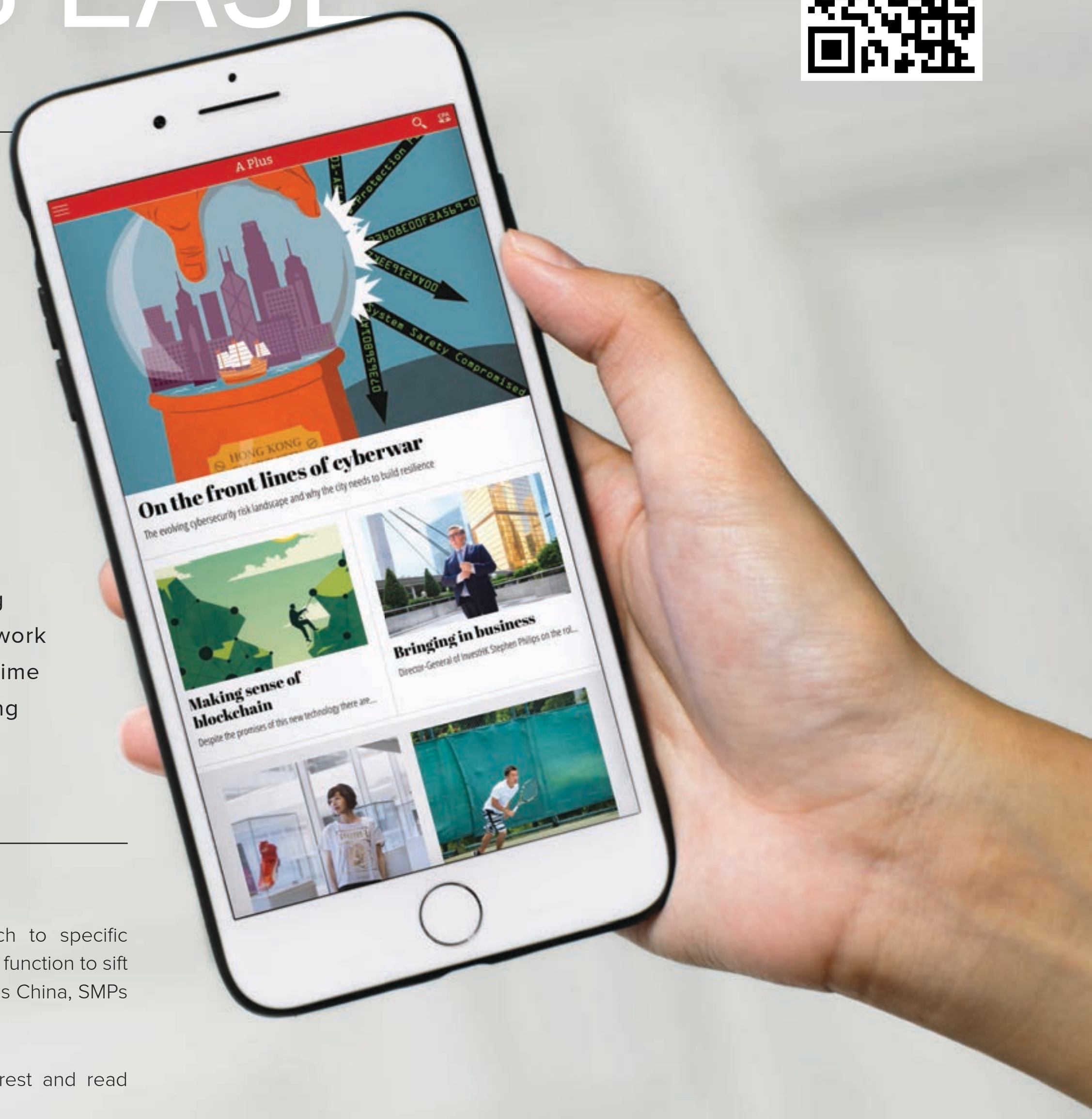

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Driving business success

The first in a series of thought leadership pieces based on the Institute's recently published *Report on Improving Corporate Governance in Hong Kong*

The importance of independent non-executive directors on corporate boards – a comparative review

This article discusses one of the recommendations from the report, prepared by Syren Johnstone and Say H Goo, on the independence of Independent Non-Executive Directors (INEDs), currently confirmed through a written confirmation to The Stock Exchange of Hong Kong (SEHK), should be made subject to the provisions of the Securities and Futures Ordinance (SFO) dealing with giving false or misleading information to regulatory agencies.

Importance of independence

The importance of independence in INEDs has risen with each corporate scandal. Over the years scandals at firms such as Arthur Andersen, Lehman Brothers, Enron and recently Wells Fargo, have demonstrated the importance of ensuring the board is aware of the activities of the management they are overseeing and are prepared to challenge executives. As Murray Steele, an experienced non-executive director who retired after over 30 years as a senior lecturer at Cranfield School of Management told the *Financial Times*, "When you look at some of the bigger disasters, you find the non-executives' mindset had become the same as the executives', therefore you don't get challenge."

Ensuring the independence of INEDs through written declarations that are accountable under the law provides greater assurance to shareholders that INEDs they elect are truly independent, and hence more likely to be in a position to challenge the executives of the firm, ensure they are meeting set targets and monitor performance against agreed goals. In general, shareholders can be more confident that the board is working in the interests of the company and their interests as owners.

International divide between board and regulatory responsibility

The Institute's report highlighted developments in Hong Kong and four markets namely, the United Kingdom, the United States, Mainland China and Singapore.

In three of these markets, the U.K., the U.S. and Singapore, the determination of independence is the responsibility of the boards, while in Hong Kong and Mainland China, independence is confirmed by regulatory agencies, the SEHK and the China Securities Regulatory Commission (CSRC), respectively. This divide in responsibility does not mean that the legal requirements are also equivalent in the relevant jurisdictions, however – with stricter rules in the U.S. and China, and relatively looser requirements in Hong Kong, the U.K. and Singapore.

Singapore's listing requirements call for INEDs to make up at least one third of the board, rising to over half when the Chairman and CEO are the same person, are closely related, or the Chairman is in the management team or not independent. Independence is described in the listing rules, but the board is responsible for identifying whether directors can be considered independent.

In the U.K., rules regarding independence are included in the Corporate Governance Code on a "comply or explain" basis, meaning that any deviation from the code is required to be explained by the company but is not prohibited. However, after six years of service on a board the reappointment should be subject to rigorous review, which increases to annual reviews after nine years.

In the U.S. however, the rules are different. The New York Stock Exchange Listed Companies Manual requires boards to be formed of a majority of independent directors and ensure that the independence of directors meets the requirements of the Exchange, which include general and specific situations where a director would be regarded as not independent. These rules are backed by disclosure obligations subject to Federal securities laws under Regulation S-K of the U.S. Securities Act of 1933, meaning that a false disclosure would be subject to liability under Federal law.

In Mainland China there is a rigid regime for determining independence, which includes a restriction that INEDs are not allowed to hold board positions for more than six consecutive years. Plus, the requirements set out by the CSRC mean that all directors need to apply to the agency in order to be confirmed, and those directors regarded as INEDs must confirm their independence through disclosers, with the threat of a fine for false or misleading information.

Recommendations for Hong Kong

In Hong Kong, at least one third of a board must be independent and the responsibility for determining independence falls to the SEHK. Like the CSRC in Mainland China, the SEHK requires INEDs to confirm their independence, and thus they rely on the accuracy of the information provided to them. However, unlike in Mainland China and the U.S., giving false or misleading disclosures in Hong Kong is merely a breach of listing rules with limited consequences, compared to the harsher penalties in other markets.

The Institute is therefore calling for these written confirmations to be brought under section 384(3) of the SFO, which would mean that individuals providing false or misleading information would be committing an offence. This does not require any change in the law as the SFO already recognizes the importance of regulatory agencies being provided with truthful information. Nor is it difficult or novel to implement: a form of written confirmation would merely need to include the requisite language - this is already done in relation to declarations made by independent initial public offering (IPO) sponsors in connection with listing applications. Should INEDs be subject to a lower standard of accountability than IPO sponsors?

ALWAYS AN AUDITOR

While the accounting profession is transforming to adapt to a world driven by technology, Clement Chan, Managing Director at BDO Hong Kong, tells Nicky Burridge that some things will never change

Photography by Calvin Sit

If there is one quality Clement Chan, Managing Director at BDO Hong Kong, thinks accountants need, it is the ability to be nimble.

In Hong Kong's dynamic business environment, with ever-changing regulations and fast-paced technological advancments, he believes accounting firms have to be ready to evolve. "We have to be flexible enough, to cater to the changes, to move on with the times, and try to maintain our relevance and competitiveness in the market," he says.

Chan's sentiment reflects his firm's efforts in recent years to maintain its position as a leader in mid-market businesses in a competitive marketplace. BDO, the world's fifth largest accounting network, recorded total global revenue of US$8.1 billion in 2017. BDO Hong Kong has over 50 directors and more than 1,000 members of staff. Its augmented digital transformation activities, investment in the digitization of its services, and merger and consolidation programme all contributed to its strong growth, according to the firm.

Technological change

Chan, a past president of the Hong Kong Institute of CPAs, thinks technological change is at the centre of the necessary evolution the profession must undergo. "The impact of technology is very important to how we do our work, and how our role is perceived. We should be making use of this to improve our level of service," he says.

While there is talk of artificial intelligence making accountants obsolete – including one prediction that auditors will be gone within 10 to 15 years – Chan is not worried. Instead, he thinks auditors will continue to have an important role to play, as long as they are able to transform their skills. "Perhaps auditing in the traditional sense such as looking at financial statements, relying purely on the information provided by our clients to do our work, selecting samples from the existing population of financial transactions and tracing them to the source will be gone," he says.

But he expects this work to be replaced by a whole new approach, as auditors have access to the full population of transactions done by a company for the first time. He suggests auditors can use this data to compare the performance of different firms in the same sector, to spot trends, and to offer higher-level services to companies. "All of this will bring unimaginable changes to the way we do business. We need to be absolutely prepared and properly trained to

BDO is the world's fifth largest accounting network. In 2017, it recorded a total global revenue of US$8.1 billion.

Clement Chan was previously managing director of Shu Lun Pan Horwath Hong Kong CPA, which merged with BDO Hong Kong in 2009, since the early 1990s.

deal with these kinds of changes, so as to maintain our skill set to be relevant in our role."

He thinks one of the key skills auditors will have to acquire is the ability to manage data, enabling them to reach meaningful and actionable conclusions. "We will be transforming from a traditional auditor, a number cruncher, to a data manager, interpreting data at a much higher level."

Chan sees the changes brought about by technological advances as one of the biggest challenges of his role. "Even for a firm of our size, we are definitely seeing a challenge in this area, but it is not something we can duck." he says. "We have to face it, embrace it and come up with the right strategy to deal with this development."

He adds that last month, BDO produced its strategic global plan for technology. "It brings a very strong message to the 165 countries within our network of member firms, that we have to converge on technology, and to be prepared to transform our existing means of communicating with clients to the next level in a digitized way," he says.

He points out that cybersecurity, having the right digital platforms and portals in place, and making the best use of data to perform additional services for clients will become increasingly critical in the future as firms handle more of their clients' data.

A smaller world

As well as embracing technology, Chan thinks it is important for medium-sized firms to be able to service their clients in different jurisdictions.

He points out that the world is getting smaller, and in today's business environment, firms need to be able to advise their clients on tax systems and regulations in countries in which they may want to expand. "Nowadays many companies are operating across jurisdictions, and it is very common when we, as auditors and business partners talk to our clients, for them to say they are planning to do an acquisition or listing in another place, not necessarily in our home jurisdiction. The ability to be connected and serve them at different locations is very important." He also notes that offering services with an international dimension is particularly important in Hong Kong, given its status as an international finance centre and regional finance hub. "Times have changed dramatically from 20 to 30 years ago, when

"Even for a firm of our size, we are definitely seeing a challenge in this area, but it is not something we can duck."

Hong Kong-listed companies had operations mainly in Hong Kong. Today a lot of companies listed on the Hong Kong Stock Exchange are foreign companies with operations outside of Hong Kong that don't have any local operations. If you don't have a good international network whereby you can provide your services to clients almost anywhere in the world, you are not going to be very competitive," he says. This edge, he asserts, has enabled the firm to advise European and United States-based companies wanting to expand into Greater China, as well as Mainland companies that want to make acquisitions in overseas markets. "I think our global presence and the regularity with which we do cross-jurisdictional projects within our network, actually makes us very recognizable in the market, particularly for clients with an international presence. We are one of a handful of firms around the

Chan was the president of the Hong Kong Institute of CPAs in 2014 and is a past chairman of the Asian-Oceanian Standard-Setters Group.

world who are able to serve clients with those kinds of needs."

Opportunities in China

Even if they do not have a global network, Chan thinks the Mainland offers significant opportunities for small- and medium-sized practitioners (SMPs) in Hong Kong. "We have an advantage because of our situation with Mainland China. We have such a big market in our backyard, and that market has a special relationship with Hong Kong, so we derive a lot of benefits and advantages from it," he says.

He points out that after over 30 years of opening up, many large companies no longer need to go through Hong Kong to get into Mainland China, but smaller companies still need help. "Small- and medium-sized enterprises (SMEs) might not have the resources and experience to go into the Mainland directly," he says. "Because of our peculiar advantage of knowing how business is done there and in the western world, medium-sized firms in Hong Kong can play a very meaningful role in holding the hands of SMEs."

Chan adds that many SMPs have already established their own bilateral relationship with accountants and service providers in the Mainland, serving as a bridge to the outside world.

A long-time auditor

Chan was born in Hong Kong and completed his early education here, transferring to the United Kingdom for his secondary education and university. After qualifying as an accountant, he came back to Hong Kong for five years, before moving to Australia and returning in 1990 to join Shu Lun Pan Horwath Hong Kong, which merged with BDO in 2009. "All my career, apart from a very short period of eight months during which I was seconded by my firm to a Japanese client to help them set up a plant in Shenzhen, I have primarily been working as an auditor."

"I never thought I would stay in this profession for over 30-something years, and right now, it looks very likely that it will be my lifetime career."

"Even right now I still regard myself very much as an auditor because I am the Managing Director of the assurance division at BDO Hong Kong," he says.

Chan was always interested in going into auditing, but he never imagined he would spend his whole career in this field. "When I started off fresh from university, I looked at it as a very interesting job through which you could poke your nose into a lot of other different industries," he says. "Auditing enables you to gain a fast track to building up knowledge in a whole lot of industries and disciplines within the business community," he says.

He adds: "To be honest, I never thought I would stay in this profession for over 30-something years, and right now, it looks very likely that it will be my lifetime career."

There is a lot more to auditing than some people think. "In our job, apart from looking at the numbers, we have to look at the reasons behind commercial decisions to see if it makes sense for the shareholders," he points out. "It is not just black and white decisions all the time, particularly with the current auditing standards – a lot of judgment is needed to do your work properly."

To Chan, auditing and being an accountant is very fulfilling. "It will give you a very stable and rewarding life," he says, pointing out that the chairmen and chief executives of many multinational corporations and banks are from accounting backgrounds.

"The profession is one where you can build up a lot of useful knowledge and experience that will carry you a long way, not just in accounting, but in a lot of other industries. Just like any profession, one has to invest time in getting qualified and in building up your experience. Once you have that, the sky is the limit."

For him, being nimble at work is not the only important thing. "I am a person who loves my sport. I believe that one of the reasons why I can stay so energized and interested in my work is because I do a lot of things outside of it," he says.

At the weekends he likes to hike and go horseback riding, while he is also a keen skier and runner. "Basically, every weekend if I am not travelling, I will either run or swim, and I go horseback riding on a Sunday afternoon. I usually go to the gym twice during the week.

"My activities outside of the office keep me very busy."

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by Wendy Chang

The Associate Director at Deloitte Risk Advisory looks at ways to effectively monitor third-party risks

How to manage third-party relationships

Today, companies rarely go to market alone. Corporate success is increasingly supported by complex supply chains, outsourcing and other third-party relationships, forming what we term the "extended enterprise." Products and services are now, more than ever, created, marketed and delivered through a network of strategic alliances and joint development arrangements. Greater reliance is being placed on business partners in opening up new markets, building brand value and growing revenues.

Yet the same third-party relationships that help bring value also carry substantial risk. Organizations' increased reliance on their extended enterprises effectively reduces their overall visibility over their critical operations. This is because the legal separation from their third parties affords lower transparency than with internal business functions. As can be seen with recent high-profile corporate scandals, which often have third-party issues as their root causes, organizations are highly susceptible to reputational damage based on the failings of their third parties. Essentially, the full spectrum of the risks of the third party have become the risks of the organization as well.

Furthermore, many regulatory regimes, especially in relation to anti-bribery and corruption, make companies responsible for the actions of their third parties, including in a cross-border context, where visibility and transparency is even lower.

These issues add to the difficulties in ensuring proper contractual performance by third parties, in terms of service delivery and quality, correct charging of costs and receipt of revenue streams, and can strain business relations in the extended enterprise, especially when economic conditions are tough.

Organizations therefore need to identify, prioritize, manage and monitor third-party risk as they would their own. Failure to do so adversely affects company performance and could potentially lead to total business failure. Effective management of third-party risk provides opportunities to create value.

With this in mind, organizations should consider the following key concepts:

Review your third-party relationships

A thorough review to identify all third parties, and the contracts that exist with them, helps an organization to understand its third-party landscape and contractual obligations. Such a review can help identify and address gaps in an organization's knowledge of its third parties and areas of duplication, and can also create opportunities to improve management of third parties or negotiate better contract terms.

Define the objectives for your third-party relationships

It is vital to ask what you want to achieve from your third-party relationships. Effective risk management programs of all types usually begin with the articulation of objectives which, in turn, helps determine the risks that could prevent those objectives from being achieved and that therefore need to be managed. This ensures the management of third-party relationships remains practical and relevant.

Assess your third-party risks

Unique risks lurk in all third-party relationships and so an effective risk assessment is required to identify and prioritize them. Some third parties will pose greater risk than others, depending on such factors as the extent of the dependence on third parties and the degree to which the operations of the two parties are interconnected, as well as the financial scale of the relationship. Risk assessment is critical in ensuring that scarce resources are properly applied to the selection and ongoing monitoring of the highest risk third parties.

Establish a compliance programme

After signing a contract, many executives assume that the third party will perform as required and that relationships are properly managed. Some even assume that their contracts transfer risks to the third party when, in fact, it generates new risks for their own organizations. This demonstrates the critical need for setting up risk-based comprehensive programmes to review third parties' compliance with their contracts and to address performance issues, whether service-related or financial.

Seek to make ongoing improvements

Reviews of third parties conducted under compliance programmes also provide opportunities for both parties to improve reporting processes, communication, controls, contractual terms and hence the overall relationship between them. In summary, third-party relationships depend on trust that is earned over time through ongoing dependability, fairness and sharing of accurate information, but tempered with an appropriate level of objectivity – the old adage, "Trust, but verify," comes to mind.

Insurance accounting **redefined**

IFRS 17 is recognized as one of the most significant changes to insurance accounting in decades. With less than three years before the new standard comes into effect, Nicky Burridge looks at the requirements of it and how implementation can help Hong Kong ensure its place as a leading financial hub.

Illustrations by Roberto Cigna

Imagine a global insurer with operations in several different countries preparing its annual results. It may be consolidating numbers produced under Hong Kong generally accepted accounting principles (GAAP) with ones from French GAAP and South African GAAP to create a set of financial statements that will then be issued in the United Kingdom.

While this scenario may sound unlikely, it is exactly what can happen under the existing insurance accounting standard International Financial Reporting Standard (IFRS) 4, which allows a significant variation in the treatment of insurance contracts for companies operating in different countries.

But this practice will end on 1 January 2021 when IFRS 17 comes into force. The standard, which replaces IFRS 4, will introduce consistent accounting standards for insurers in all IFRS jurisdictions for the first time.

The project has taken the International Accounting Standards Board (IASB) nearly 20 years to finalize, and, reflecting the complexity of IFRS 17, insurance companies have been given three and a half years to implement compliance with it – one of the longest ever lead-in times for an IFRS.

New requirements

At its heart, IFRS 17, or HKFRS 17 (the Hong Kong interpretation of the international standard), will make insurance companies more comparable by being more prescriptive about the way they treat insurance contracts on their balance sheets.

Hong Kong Institute of CPAs member Raymond Lo, Chief

"This is a much more economic approach to profit emergence and, in addition to being more reflective of economics, there is significant value in the improved consistency that IFRS 17 brings around the world."

Financial Officer at insurer FWD Hong Kong and Macau and a member of both the Hong Kong Federation of Insurer's IFRS 17 Taskforce and the Institute's Insurance Regulatory Advisory Panel, explains that IFRS 4 only defined the meaning of an insurance contract. "Consequently, there is a wide range of practices. Some companies use United States GAAP, while others favour the local statutory basis or prefer to follow the practice of their European parents," he says. IFRS 4 also led to some companies effectively using solvency valuations and practices to account for insurance contracts, with deposits often counted as revenue.

Stephen O'Hearn, Global Insurance Leader at PwC, explains that by contrast, IFRS 17 requires companies to determine the best estimate of cash flow on their products, and then change the accounting model so that profit emerges over the course of those cash flows. "This is a much more economic approach to profit emergence and, in addition to being more reflective of economics, there is significant value in the improved consistency that IFRS 17 brings around the world," he says.

IFRS 17 *Insurance Contracts* is based on a series of four building blocks looking at cash flows, discount rates, risk adjustments and the contractual service margin (CSM). Francesco Nagari, Global IFRS Insurance Leader at Deloitte, explains that the new standard requires insurance companies to estimate cash flow for an insurance contract, including factors such as payouts for insured events, potential policy lapses and surrenders.

When using discount rates, insurers must consider market rates of the same currency, duration and level of liquidity, while they must also make an explicit provision for prudence, something neither life nor general insurance companies had to do under IFRS 4, where prudence has been provided for implicitly. Nagari says: "Transparency under IFRS 17 means you have to do your best job in estimating your cash flows, and then you provide explicit risk adjustment to the level of prudence you believe is necessary to cope with the uncertainty – this is very, very, new."

He adds that the fourth building block, the CSM, changes the practice by reporting explicitly the expected profit an insurer believes would come from selling an insurance contract. The CSM is effectively the deferred profit on the insurance contracts in-force at the balance sheet date and the major source of revenue and profit as insurance services are rendered. "For the first time, when people read these financial statements, they can see all these components,"


IFRS 17

Nagari says. "IFRS 17 gives you the basis to take all of these building blocks period after period, making absolutely clear the reconciliation between the balance sheet and profit and loss statement for insurance contracts, which is a first in Hong Kong reporting standards."

Benefits and concerns

The most obvious benefit of IFRS 17 is the enhanced transparency and comparability it offers. "At the moment, the versatility and diversity in utilizing measurement models make profitability comparison difficult, if not impossible," Lo says. "Under the new standard, the underlying measurement models, presentation and disclosures have been transformed."

But despite the transparency it brings, insurers are concerned about the complexity of IFRS 17. He adds: "One overwhelming comment from the industry is that this standard is too complex to implement. Data requirements, down to individual contract level, dramatically change the whole finance and actuarial reporting processes." O'Hearn agrees: "This is a brand-new set of rules and they are very full, very extensive, but no one has done it before. They are untried and complex."

One particularly controversial aspect of the new standard relates to the timing of profits being recognized, with some companies complaining they will initially see a dip in profits under the new standard. Nagari thinks this is a distinct possibility. He says: "I am not surprised that some insurers will find that the emergence of profit under the new rules will be slower than they were under IFRS 4." But, he adds that other insurers may experience the opposite and see profits emerging faster.

Implementation challenges

Unsurprisingly, given the complexity of IFRS 17, the insurance sector foresees a number of challenges in implementing it. FWD is one of the world's first insurance companies to start the process of implementation. In February, it announced it had selected Aptitude Software, a global financial software specialist, to drive the changes required to deal with IFRS 17. Lo says the published standard is ambiguous at times.

"Our financial controller, who is leading this project at FWD Hong Kong and Macau, has also been actively participating in the Hong Kong Insurance Implementation Support Group (HKIISG) organized by the Institute. We have already observed heated debates in the [IASB's] Transition Resource Group regarding how to address the implementation challenges," he says.

Joyce Lau, Chief Financial Officer at Target Insurance and an Institute member, said her company had been given conflicting advice from advisors as to how it should implement IFRS 17, with some advisors saying that, as a general insurer, they could do it in a very simplified way, while others said they must fulfil the prescribed approach. "For us as a general insurer, we do not have as many resources to interpret the standard that some life insurers have. We are heavily reliant on our advisors as

"This is a brand-new set of rules and they are very full, very extensive, but no one has done it before. They are untried and complex."

Hong Kong Insurance Implementation Support Group

The Institute has established the Hong Kong Insurance Implementation Support Group (HKIISG) to support the implementation of IFRS 17. The objectives of the HKIISG are to:

(a) Solicit, analyse, and discuss stakeholder questions raised regarding implementation of IFRS 17;
(b) Provide a forum for stakeholders to follow the discussion of questions raised;
(c) Identify implementation issues which need to be brought to the attention of the IASB's Transition Resource Group on the standard;
(d) Identify areas of focus for educational activities; and
(e) Provide recommendations for the Institute's Financial Reporting Standards Committee to consider, which may include submitting a question to the IFRS Interpretations Committee or writing to the IASB.

The group welcomes questions from those implementing the new standard and the minutes from its meetings can be found on its dedicated webpage.

The Institute is organizing two workshops on IFRS/HKFRS 17 in July for life-insurers (16 July) and non-life insurers (25 July).

The workshops are targeted at industry professionals who have acquired the basic principles of the new standard and wish to develop a working knowledge, more information is available on the Institute's website.

to how we should proceed. We are looking for more clarity on what is the simplest way for us to adopt IFRS 17. It is pretty confusing." She adds that she is also concerned that general insurers were not well represented at IASB discussion groups around the new standard, and this is reflected in the way IFRS 17 is applied to general insurers.

Another challenge relates to the data infrastructure that companies need to put in place in order to comply with the standard. Lo says: "The data requirement is rather substantial and there is a certain level of complexity in developing software and changing existing processes to capture the required transaction details." He points out that data will need to be extracted from policy administration systems, distributors' compensation systems, investment management systems, general ledgers and actuarial models. It is not difficult to imagine the complications, considering the number of IT systems involved," he says.

There are also concerns that there may not be enough qualified professionals available to assist firms with the implementation of the new standard. "Although, Hong Kong is probably one of the richest pools of talent in Asia from an insurance accounting and actuarial perspective, demand for that talent will be very high and the possibility of a gap between the supply of Hong Kong actuaries and accountants and the demand from insurance companies is clearly a very real possibility," Nagari says. He explains that the new IFRS 17 requirements call for a greater level of transparency in the way actuarial calculations are reported, with separate risk adjustments and CSM. "Implementing the actuarial systems that deliver these new numbers on top of what was done before or instead of what was done before is a big effort that calls for actuarial expertise combined with deep IFRS 17 knowledge." Nagari adds that the fact that so many insurers have their regional headquarters in Hong Kong will have a multiplier effect, as companies look for talent to serve multiple geographies across the whole of Asia.

"We are heavily reliant on our advisors as to how we should proceed. We are looking for more clarity on what is the simplest way for us to adopt IFRS 17. It is pretty confusing."

The implementation timetable may also cause issues, especially for small- and medium-sized insurers that have a lack of resources. O'Hearn points out that while the standard will first be used for half-year results in 2021, these figures will be compared with numbers for 2020.

"Companies really need to accelerate their processes, so they can start generating and analysing numbers in 2019 to ensure they get their head around what the results mean, how to interpret them, and how to explain them internally to management and externally to investors and analysts," he says.

Investor advantages

While insurers are grappling with the complexities of IFRS 17, its introduction is expected to significantly simplify things for investors, who will be able to easily compare insurers both within the same market and different countries for the first time. O'Hearn thinks the consistency in reporting could also reduce the cost of capital for the sector. "That would be the ultimate benefit of this – if more capital flowed to the insurance industry because there was improved transparency on the economics of the product. I think that is a real possibility," he says.

But he adds the investment community has some way to go to fully comprehend the new standard. "They are going to want to understand, initially at least, how to reconcile the key performance indicators (KPIs) that they rely upon today to a whole new set of KPIs that have really yet to be developed. Then, ultimately, how valuations of companies are influenced by these new KPIs – and that is going to take some time," he says. He also anticipates increased volatility in company results following the introduction of the new standard. "Companies will need to be ready for that volatility and they will need to be able to explain it."

Melissa Brown, Partner at Daobridge Capital, a China-focused direct investment and financial advisory firm, and a government-

> **"Insurance companies have not yet really experienced the fully-fledged comparability that comes from IFRS."**

appointed lay member of the Institute's Council, thinks the new standard will be particularly helpful to investors in Hong Kong due to the presence of large Chinese insurers here. "This is a marketplace that really pays a great deal of attention to the largest Mainland Chinese insurance companies, as not only do they have organic growth potential, but they are also huge players in the economy," she said at the joint Institute-IFRS Foundation stakeholder dinner in January. But she added that from an investor perspective, Hong Kong is not endowed with a lot of analytical strength on insurance companies, so having a better accounting standard will be beneficial.

Importance for Hong Kong

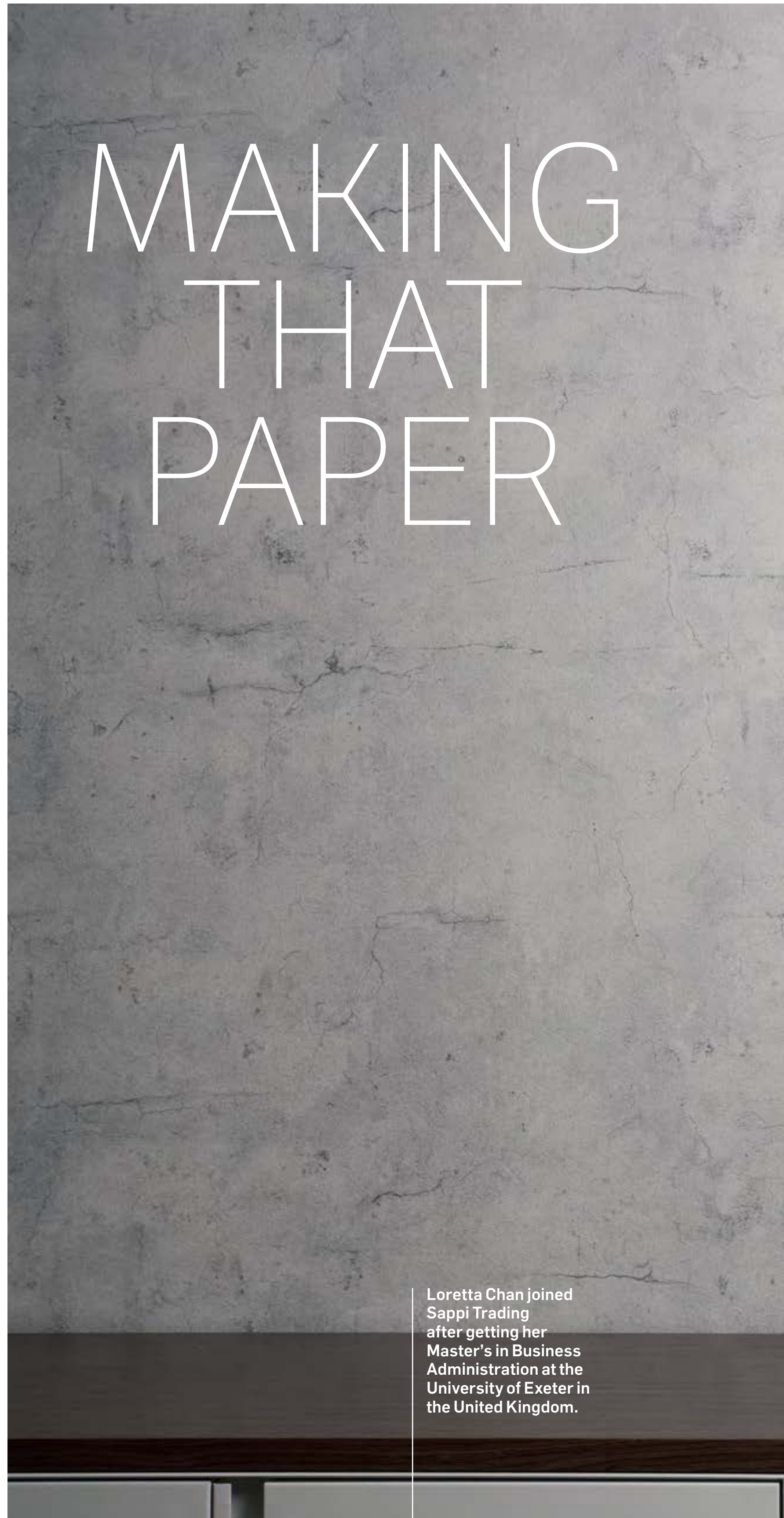
The introduction of IFRS 17 is important to cement Hong Kong's reputation as an international financial centre. O'Hearn thinks if Hong Kong wants the most advanced investment community, it must also have the most transparent financial reporting to provide to that investor community. Nagari agrees, pointing out that if Hong Kong is to retain its reputation as the leading financial services centre in Asia, investors need to be able to compare Hong Kong companies with other entities operating in the same sector globally.

He points out that one of the benefits, alongside more efficient capital markets, could be a higher level of transactions between insurance companies themselves, in terms of disposals and acquisitions. "Insurance companies have not yet really experienced the fully-fledged comparability that comes from IFRS," he says. "It is only now with IFRS 17 that the insurance sector will have the chance to reap the opportunity."

MAKING THAT PAPER

Hong Kong-based Sappi Trading has gone through some difficult times. Chief Financial Officer Loretta Chan tells Kate Whitehead how her CPA skills helped the emerging market multinational overcome challenges and become one of the word's leading paper companies

Photography by Calvin Sit



Loretta Chan joined Sappi Trading after getting her Master's in Business Administration at the University of Exeter in the United Kingdom.

Loretta Chan is used to the prompt efficiency of Asia, so when she began managing markets in Latin America there were a few cultural differences to get used to.

"They would tell me they'd get back to me mañana, so I expected to get an answer the next day, but in their culture mañana means "later" and I might get the answer 10 or 15 days later. This is a cultural thing. We have to understand each other in how we do business," says Chan, Chief Financial Officer of Sappi Trading, and a Hong Kong Institute of CPAs member.

Dealing with such cultural differences, as well as language issues, are expected when working at a company like Sappi Trading, part of the Sappi group, a leading global producer of dissolving wood pulp and paper-based solutions. The division operates a network for the sale and distribution of its products across multiple markets.

Founded in Johannesburg in 1936 as South African Pulp and Paper Industries, Sappi grew from manufacturing paper from straw at its first mill at Enstra in Springs, east of Johannesburg, to become a global player with operating units and sales offices on six continents and customers in more than 150 countries.

Success ingredient
Loretta Chan

According to Sappi's *2017 annual report*, they produce 5.4 million tonnes of paper a year, and its range of paper products includes flexible packaging, label, release liner, containerboard and fluting, coated fine papers and casting release papers, and serve the fashion, fast-moving consumer goods and industrial sectors. Its dissolving wood pulp products are used by converters to produce viscose fibre, pharmaceutical products as well as household and consumer products.

Although uncomfortable with the term "emerging market multinational corporation" (eMNC), Chan agrees Sappi does fall into that category – it's a South African company with large manufacturing assets in the United States and Europe and over 100 sales offices globally. EMNCs have traditionally been considered the low-cost competitors of their G7 counterparts. She maintains that the key to Sappi's success is the fact it's a low-cost producer. "That's our biggest advantage. We have a very healthy balance sheet that allows us to grow and take advantage of market opportunities. Due to the low cost of living in South Africa, the wages are not as high compared to the U.S.," says Chan.

Sappi Trading's Hong Kong office opened in 1986 and is the regional head office looking after the export market in Hong Kong, Singapore, Shanghai, Australia, Africa and Latin America. Chan joined the Hong Kong office in 1992 as a management accountant. "It was important to me at the time that it was a multinational company, I thought that would give me more scope to grow than a local company," recalls Chan. In 2000, she was promoted to financial controller and moved into her current position four years ago.

Strategic shifts

Chan's first 15 years at Sappi Trading were a golden period for the company, a period of consistent and

"Although it was a tough time, it was also exciting for me, and when I look back I realize how much I grew then."

steady growth, but the 2008 global financial crisis combined with falling demand for graphic paper – used to print magazines – led to some difficult times.

Forced to make tough calls, it was an opportunity for her to grow professionally. "It was a crisis period for the company. Although it was a tough time, it was also exciting for me, and when I look back I realize how much I grew then," she says.

She looked closely at the balance sheet and took steps to keep costs down to stay competitive. "If you see that something is not good, then you have to make a change – you can't drag on and on," she says.

One of the group's initial strategies was to shift dependence from products with low profit margins to ones with high returns. This meant decreasing its capacity in graphic paper (a sector that was already sliding following the trend of reading handheld devices rather than traditional print media) and increasing the production capacity of specialty paper, which is used for everything from the lids of yoghurt pots to boxes used to package cosmetics.

"It's not a commodity anymore because it's a niche. It's a growing market with generally higher profits," Chan says, adding that the group's recent acquisition of the speciality paper coated paper business of Swiss paper manufacturer Cham Paper increased Sappi's production of that paper by 160,000 tonnes. "Being the international division of the group, we will continue to add resources to drive for growth, increase sales, profitability and market share in the specialities packaging sector," she says.

The financial crisis also meant many employees were made redundant. The administration staff in the satellite sales offices were either transferred or dismissed, which led to operations being consolidating into two administration service centres, one in Hong Kong and one in Mexico City. Better use was made of technology to keep costs down – an element that only becomes more critical with the rise of big data.

The often volatile situation in Latin America – Brazil is only just emerging from a currency crisis from 2016 and there is political instability – means that Chan needs to keep a close eye on customers in that region. "Because of low profit margins, they aren't able to afford foreign exchange cover. It's very different from multinational companies because we buy hedging to protect our profit. However, because the hedging interest rate is so high in those countries, we need to be very careful by regularly checking the customers' financials to see how they are doing," says Chan.

Although she visits the regions periodically and calls on big customers of Sappi Trading to help develop sales and resolve business issues, she depends on her local team on the ground for regular updates. "It is very important that you have your own people there, to get close to the customer and find out exactly what is going on," says Chan. "They help us understand the financials and the business structure and performance of the customer, they have more in-depth market knowledge. If you used an agent, they wouldn't be able to give you that knowledge. What's more, if you use your own people they will fight for that extra dollar for you – and you will have a better connection with the customer."

Sappi produces 1.4 million tonnes of paper a year. According to the company, its range of paper products, including flexible packaging, label, release liner, containerboard and fluting, coated fine papers and casting release papers, serve the fashion, fast-moving consumer goods and industrial sectors.

Addressing sustainability

The forest products industry has long been plagued by negative public perceptions, with an image of environmental harm. Chan believes there's a strong need to correct such ideas. "The impression is that paper is bad for the environment but paper is one of the few truly sustainable products. It is renewable, recyclable and good for the economy. Some research even shows that reading and writing on paper can be better for the brain and benefit long-term memory," she says.

Sappi started focusing on sustainability in 2007. "It was initially due to the recognition that becoming more efficient in our use of water, energy and raw materials was not only good for the environment, but also helped lower costs, making us more profitable," explains Chan. "Today, increased focus on supply chain transparency and the life-cycle impacts of our products are driving our sustainability efforts as well as creating opportunities to revitalize the pulp and paper industry."

According to its *2017 Sappi North American Sustainability Report*, the organization has been seeking alternative energy sources, including reclaimed oil, construction, demolition wood and tire-derived fuel, resulting in a 22 percent reduction in greenhouse gas emissions compared to 2007.

The company has been certified by the three most internationally recognized forest products certification programmes: Forest Stewardship Council; Programme for the Endorsement of Forest Certification; and Sustainable Forestry Initiative.

Soaking up experience

Last year, Chan picked up her long-service award – 25 years with the company. She had joined the Hong Kong office fresh from earning her Master's in Business Administration at the University of Exeter in the United Kingdom.

Her early years with the company were personally challenging as she juggled childcare and a demanding full-time job, all while working towards her CPA qualification. She says the lost sleep was well worth it. "If you want to move up to a more senior role, you need a more professional qualification and accounting gives me the skills I want, and the knowledge I need."

She also commends the Institute's continuing professional development programme. "They help you to have updated information and see what is happening in the world – for example tax changes and developments," she says.

She encourages young accountants to step out of their comfort zone and diversify their skill set. "Don't worry about not understanding the figures or being criticized – it's more important to be inquisitive," Chan says. "I always tell my staff to be like a sponge, soak up what you can. Curiosity is a good thing, it is how you build your knowledge and confidence."

She credits her previous boss who served as her mentor for helping her grow. She says her current mentor, who helped her prepare for her current role, is also very supportive. "The more you learn, the more you want to learn – and it's fun," she says.

Acknowledging that she has spent more than 25 years on the job, she encourages young people to avoid a tendency to change jobs every one or two years. "If you really want to know a company and grow with it that's too short, you need to invest more time in it."

"I always tell my staff to be like a sponge, soak up what you can. Curiosity is a good thing, it is how you build your confidence."

Chan recommends finding a passion outside the office to maintain a healthy work-life balance. She plays tennis twice a week and goes ballroom dancing once a week.

The team practices at Po On Road Sports Centre in Sham Shui Po

A WHOLE NEW BALLGAME

RSCP championship winners six years in a row, the Institute's basketball team are a force to be reckoned with. The 17-strong squad of CPAs have their eyes set on gold again this year, and know it won't be easy. Members speak to Jeremy Chan on how to maintain their winning streak, the challenges they face and achieving balance in work and sport

Photography by Anthony Tung

"The physiotherapist said I couldn't play basketball for eight weeks," says Kurkye Wong, Vice President of Argyle Street Management. "But after three weeks, I started playing anyway." After sustaining a high ankle sprain following a heavy fall during a training session in 2016, he was determined to return to the court as shooting guard. His strength, perseverance and commitment to the team isn't restricted to him alone.

"Everyone has their status outside the basketball court, but on the court, we are one team. We need to work with each other," says his twin brother, Foreky Wong, Senior Director of Corporate Finance at FTI Consulting. Both are shooting guards and have played for the team for six years. They joined for the same reasons – pure love for the sport.

Little did they know the team would become somewhat of an extended family for the twins, one that would meet twice a week to dribble, pass and score. Rounding up the troops is the role of Thomas Lau, the team convenor, who teaches financial accounting and taxation as a lecturer at the Open University. He joined after becoming a CPA in 2011 and dedicated his time outside of work to the team. In addition to securing venues for practice and daily administrative work, Lau provides support and encouragement, ensuring spirits stay high.

Walking the tightrope

"In 2016, we beat [the Hong Kong Institute of Surveyors] by a 16 point lead, but last year it was only a nine point lead – so that gap is closing," Lau says. Despite having faced yet defeated the Hong Kong Institute of Surveyors twice in the finals of the Recreation and Sports Club for Hong Kong Professional Bodies (RCSP) Basketball Tournament, the Institute basketball team says it was no easy win. "The surveyors team is made up of some tall guys, and once they go near a basket they can make the shot," says Foreky.

The team employs a defence technique, known as the "full court press" – a method used to intercept the opponent's ball during a pass. The players note the risks and rewards of the move. "We have two players marking the dribbler, which is a gamble, because the farthest player is unmarked, but this causes the dribbler to make a bad pass or mistake, so then we can grab the ball and go straight into offence. That's exactly how we beat the surveyors." "No other team in the tournament uses the full court press," adds Kurkye. Lau says "we're not scared, but there is pressure. We have to play fast."

The players look back on their most memorable game – their first overseas tournament. They represented Hong Kong in the finals at the Integrity Cup Basketball Competition in Guangzhou, China in 2016. Involving 16 accounting associations' basketball teams from across Guangdong province, Hong Kong, and Macau, the semi-finals and finals took place across two weekends. The team fought their way through to

Kurkye Wong (right)

the finals, to play against a team from Zhaoqing.

Foreky recalls the challenges the team faced. "Our strategy was to stop their players from passing the ball to their best guy." Lau adds: "Zhaoqing had a very tall and powerful player who could run, jump and dunk."

Despite the Institute basketball team trailing in the first and second quarter, they recouped their losses towards the end. "Luckily, we had one player similar in size who could guard him throughout the whole game," Foreky recalls. "In the third quarter, he was too tired and had to rest, so we caught up during that period." Lau mentions, "our coach could see which players were not performing their best and would order a substitution to moderate the pace of the game."

Kurkye, who was still injured from his fall, flew into Guangzhou to play in the finals. "This game meant a lot to me because I was travelling and injured," he says. "I still went into the court and played as much as I could. I forgot about the pain and it was like my leg was fine." After a hard fought game, the team were winners of the competition.

Learning from the best

The team attributes a large part of their success to their coach, Ricky Ng Chu-yip, an 11-time basketball championship winner who played for Hong Kong basketball teams in the 1980s and 1990s. He is a former player for Winling, a local team established in 1980s and Regal, winners of the Asian Basketball Championship's Cup in 1997. Regarded as a living legend among the team and local basketball players, Ng has spent the last decade coaching the Institute's basketball team.

"He was one of the top players in Hong Kong," Foreky says. He coaches

"I still went into the court and played as much as I could. I forgot about the pain."

them on new concepts of offence and defence, and introduced the team to "full court press."

In addition to coaching, Ng has greatly influenced them. "His encouragement and teachings have inspired us to foster one another," he says. "He really knows how a game should be played and how a player fits into a team, and the culture of the team is influenced by him," Lau says. "His philosophy is trust and harmony, which is in our blood now."

The team prepares for matches weeks or months in advance. "During training, we talk about the next game, our opponents, how their key players play and how we should play," says Kurkye.

Lau adds: "we are familiar with a few of our opponents as we have played against some of them before, so we have a particular strategy – for example, some teams have very good three-point shooters, which means we need to focus on defence."

Time won't wait

Securing a practice base is a challenge for Lau, and he commends the Institute for booking courts for the team. "The Institute has been really supportive," he says. "A few years ago, they were able to secure a fixed place for us to practice at Kwun Chung Sports Centre in Jordan – and because we practiced there every Thursday from 9-11 p.m., our team was born."

However, due to changes in the Leisure and Cultural Services Department's (LCSD) deposit policies in 2015, they

"He really knows how a game should be played and how a player fits into a team, and the culture of the team is influenced by him."

The team strategizes mid-training

were not able to regularly ensure a court. "That's a challenge now as we need to find courts – weekly." Booking through service providers such as the LCSD, they are able to secure courts around the city. Lau recalls being assigned a court in Siu Sai Wan, far eastern side of Hong Kong Island – and though far away, his teammates still arrived after work. "I must acknowledge my teammates' dedication and contribution to the team – they are very disciplined and full of passion. A few players who lived all the way in the New Territories still came to practice, and I really appreciate their attendance and effort – it really motivates me."

Lau expresses admiration for the team's spirit and energy, aware most of them work long hours. Despite the lack of time, many of the players have methods when it comes to fitting in an intense training session after leaving the office. "When I get to work, I tend to not waste any time. I put all my effort into it and finish things. I free up time to play basketball – I usually get off at 8 or 8:30 p.m., so I'll grab something to eat in between, and start training at 9," Foreky says. "If I'm really busy, I'll work when I get home after training."

Kurkye adds, "I put in 100 percent at work. I work hard, I focus, I get things done. After work, we try to get the most out of the two hours of training as we don't want to waste time once we get there." As Foreky puts it: "it's all about how you allocate your own time. Everybody has 24 hours – what are you going to do with them?"

"When I get to work, I tend to not waste any time. I put all my effort into it and finish things. I free up time to play basketball."

One's true colours

Though the CPAs in the team work

Kurkye Wong (front row, third from left) Foreky Wong (front row, middle) Thomas Lau (front row, second from right)

in various industries and hold different positions, on the court, what matters the most is the game. "We are one team and we need to work with each other," he says. The training grounds has also doubled as networking ground, providing a place for players to discuss basketball – and business. "Basketball is an icebreaker," Kurkye says. "It is really easy to start a conversation with people with the same interests." By networking with different individuals, all members were able to bond over basketball as well as work. "We are kind of a family that supports each other," he says. "People get to know your personality outside of work and on the court," Foreky adds. "I've met a lot of senior guys on the basketball court and gone out with them for lunch to talk about work opportunities."

The three players encourage interested CPAs who share their passion for basketball to join the team. "Everyone is very welcoming," says Foreky. "We don't expect people to commit on the first day, because when you join a team and mingle with people, it takes time, but as long as you can allocate time to training and we see you're a good player, we'll recruit you."

Lau encourages a healthy lifestyle. "Anybody can squeeze time out of the week for exercise – it will become a habit, and part of your life."

"People get to know your personality outside of work and on the court."

With the next RSCP Basketball Tournament scheduled for September, the pressure is on the team to bring home the gold again. Feeling unabated and determined to bring the winning streak to seven, the team are training hard to achieve that goal. "One for all, and all for one," says Lau.

This year, the Institute's basketball team clinched its sixth consecutive championship in the Recreation and Sports Club for Hong Kong Professional Bodies Basketball Tournament. For more details on sports and recreational interest groups, visit *www.hkicpa.org.hk.*

Enhanced deduction for qualifying R&D expenditure will be introduced in Hong Kong

A look at the proposed research and development tax deduction regime

The bill proposing an enhanced tax deduction for research and development (R&D) expenditure in Hong Kong was gazetted on 20 April. Subject to certain conditions, there will be a 300 percent tax deduction for the first HK$2 million of qualifying R&D expenditure incurred by enterprises and a 200 percent tax deduction for the remaining amount, without limit. R&D expenditure that does not qualify for the enhanced deduction may continue to enjoy a normal 100 percent tax deduction subject to fulfilment of the specified conditions. Once the bill is enacted into law, the new R&D tax deduction regime will take retrospective effect for expenditure incurred or payment made on or after 1 April 2018.

The current tax deduction for R&D expenditure

The current tax deduction for R&D expenditure is provided in section 16B of the Inland Revenue Ordinance. Under this, R&D expenditure incurred by a taxpayer related to its trade, profession or business (including capital expenditure on plant or machinery but excluding capital expenditure on land or buildings or in acquiring any rights in, or arising out, of R&D) can be fully deducted (i.e. a 100 percent tax deduction) in the year of assessment in which the expenditure is incurred, subject to certain conditions.

Based on the Inland Revenue Department's (IRD) interpretation, in order to qualify for the deduction, the R&D expenditure must either be:

1. Incurred in respect of in-house R&D activities undertaken by the taxpayer itself; or
2. A payment made to an approved research institute (i.e. for subcontracted R&D activities).

For a cost sharing arrangement within a group, the IRD's view is that only the actual staff costs of the employees of the Hong Kong taxpayer participating in the R&D activities, instead of the full amount of the R&D costs allocated to the Hong Kong taxpayer, can qualify for the deduction.

For R&D expenditure incurred by a taxpayer outside Hong Kong (i.e. expenditure on R&D activities carried outside Hong Kong), an apportionment of the expenditure is required if the taxpayer's trade, profession or business is carried on partly in and partly outside Hong Kong (i.e. where only part of the taxpayer's profits are taxable in Hong Kong).

The proposed enhanced R&D tax deduction regime

To encourage more enterprises to invest in R&D in Hong Kong and promote local R&D activities, the government proposed in the 2017 Policy Address to introduce an enhanced tax deduction for R&D expenditure. The Inland Revenue (Amendment) (No.3) Bill 2018 (the Bill), which was gazetted on 20 April, set out the details of the proposed normal and enhanced tax deduction for R&D expenditure in Hong Kong. Once the bill is enacted into law, the new regime will take retrospective effect for qualifying expenditure incurred or qualifying payment made on or after 1 April 2018.

With the introduction of the enhanced R&D deduction, section 16B is revamped and a new schedule (i.e. Schedule 45) is introduced to specify the details for the deduction of R&D expenditure. As specified in Schedule 45, there are two types of tax deductible R&D expenditure, namely Type A expenditure (which qualifies for a 100 percent tax deduction) and Type B expenditure (which qualifies for enhanced tax deduction of 300 percent for the first HK$2 million and 200 percent for the remaining amount). One point that is worth to note is if any rights generated from the R&D activity are not, or will not be, fully vested in the taxpayer, no deduction (both Type A and Type B expenditures) will be granted. This requirement is not clearly specified in the existing section 16B.

Compared with other countries that also offer tax incentives for R&D activities, some features of the proposed regime in Hong Kong are more competitive whereas the others are less attractive. Taking Mainland China as an example, the current rates of enhanced tax deduction for qualifying R&D expenditure are only 175 percent (for qualified small- and medium-sized technological enterprises) or 150 percent (for other enterprises), which are lower than the 300/200 percent enhanced deduction rates in Hong Kong. On the other hand, while payments made for subcontracted R&D activities are generally not eligible for enhanced deduction in Hong Kong (unless the subcontractor is a designated local

research institution), 80 percent of the expenditure incurred for R&D activities subcontracted to a related or unrelated party (either an organization or individual) is eligible for enhanced tax deduction in Mainland China provided that the R&D activities are conducted by a local party in Mainland China.

Certain receipts in relation to R&D deemed as taxable trading receipts

In order to maintain tax symmetry, the following provisions (which are originally in section 16B) are retained in Schedule 45, with modifications to reflect the proposed enhanced R&D tax deduction:

- Proceeds from sale of plant or machinery used for an R&D activity where the capital expenditure on such plant or machinery has been allowed as a deduction under section 16B, with the deemed taxable amount limited to the amount of deduction previously allowed; and
- Proceeds from sale of any rights generated from one or more R&D activities for which the expenditure have been allowed as a deduction under section 16B, with the deemed taxable amount limited to the amount of deduction previously allowed.

The bill also introduces provisions that deem the following receipts as taxable Hong Kong sourced trading receipts:

- Royalties received for the use, or the right to use, outside Hong Kong of any intellectual property or know-how generated from any R&D activity in respect of which a R&D deduction is allowable under section 16B; and
- Sums received for imparting or undertaking to impart knowledge directly or indirectly connected to the use outside Hong Kong of any intellectual property or know-how generated from any R&D activity in respect of which a R&D deduction is allowable under section 16B.

Assessment of eligibility for the R&D tax deduction

For the purpose of assessing a claim or an advance ruling application made in relation to a deduction for R&D expenditure under section 16B, the Bill proposes to empower the Commissioner of Inland Revenue (CIR) to seek advice from the Commissioner for Innovation and Technology (CIT) in ascertaining whether (1) an activity falls within the scope of R&D activities qualifying for the tax deduction and (2) the expenditure should be regarded as incurred in relation to an R&D activity qualifying for the tax deduction. The CIR may disclose to the CIT any details which he considers necessary for the purpose of such consultation. The final decision on whether a deduction should be allowed for the R&D expenditure concerned will be made by the CIR.

The takeaway

While the Bill represents a significant move of the government in the right direction for promoting local R&D activities in Hong Kong, the proposed enhanced R&D tax deduction regime is considerably complex as it specifies numerous conditions for enjoying the enhanced deduction, introduces various deeming provisions that treat certain receipts in relation to R&D that would otherwise not subject to profits tax as taxable trading receipts and includes anti-avoidance provisions to safeguard against abuse of the tax deductions (both normal and enhanced) for R&D expenditure.

Hong Kong companies that are engaging in or planning to engage in R&D activities in and/or outside Hong Kong should review their R&D activity arrangements in light of the proposed regime and assess how to best structure their R&D activities for benefiting from the enhanced R&D tax deduction in Hong Kong.

This article was originally published in PwC's *Hong Kong Tax News Flash* (April 2018)

TechWatch 188

The latest standards and technical developments

Hong Kong updates

Implementing HKFRS 17 *Insurance Contracts*
The Institute has published a pocket summary on HKFRS 17 to provide insurers with a simple framework and general references for planning the implementation of the standard.

Summaries of the 20 March, 20 April and 27 April meetings of the Hong Kong Insurance Implementation Support Group are now available.

Invitation to comment
The Institute is seeking comments on the IESBA Consultation Paper *Professional Skepticism – Meeting Public Expectations* by 13 July.

International updates

IFRS Updates
- Report on the spring 2018 International Forum of Accounting Standard Setters meeting
- Summary and podcast of the May meeting of the IASB Transition Resource Group for Insurance Contracts
- Quiz on the revised Conceptual Framework
- April and May IASB Update
- May IFRIC Update

IESBA Update
- Podcast of the IESBA March meeting

Professional accountants in business

A vision for the finance professional and the finance function
Following the IFAC Professional Accountants in Business Committee meeting in March, the committee has recently released a report highlighting the meeting's key messages focused on the key elements of developing a vision and roadmap for the finance professional and finance function, and provided an update on current initiatives of the committee.

HKEX reviews listed issuers' implementation of ESG reporting guide
On 18 May, Hong Kong Exchanges and Clearing (HKEX) published the findings of its review of listed issuers' Environmental, Social and Governance (ESG) disclosures in a report entitled, *Analysis of Environmental, Social and Governance Practice Disclosure in 2016/2017*. The review involved analyzing disclosures made by 400 randomly selected issuers with financial year-end dates of 31 December 2016, 31 March 2017 and 30 June 2017.

HKEX recommends the inclusion of the following key information in listed issuers' ESG reports:
- The issuer's or the board's commitment as well as the management's approach to ESG and how they relate to the issuer's business.
- The board's evaluation and determination of ESG risks and how it ensures that appropriate and effective ESG risk management and internal control systems are in place.
- The process for stakeholder engagement, which is central to materiality assessment and enables the company and its directors to communicate with their stakeholders.

HKEX reviews listed issuers' financial reports
On 1 June, HKEX published a report summarizing key findings from its review of 100 periodic financial reports released by listed issuers between February 2017 and April 2018.

The report specially highlights the importance of the following:
- Providing investors with a meaningful management commentary
- Judgments and estimates
- Assessing impairment of tangible and intangible assets (including goodwill)
- Accounting for acquisitions
- Impact of applying key Hong Kong Financial Reporting Standards in issue but not yet effective
- New auditors' reporting

Members, especially those responsible for preparing financial reports of listed issuers, are encouraged to read the report.

Small and medium practitioners

IFAC guide to practice management helps SMPs thrive in the global economy
IFAC has recently released an updated (4th edition) Guide to Practice Management for Small- and Medium-Sized Practices (the guide) to help SMPs adopt good practices to better serve their clients in a digital, globalized world. The guide helps SMPs improve their management and operational efficiency and supports their sustainability and success.

The guide adds a new module on "Leveraging Technology," which covers how technology developments are fundamentally changing the way organizations operate, and recognizes that SMPs must adapt to service their clients that utilize technology. Relevant topics such as developing a technology strategy, hardware and software options, technology risks, new and emerging technologies, and leveraging technology for practice innovation are covered.

Corporate finance

Consultation Conclusions on Capital Raisings by Listed Issuers
On 4 May, HKEX published its consultation conclusions on Capital Raisings by Listed Issuers to restrict abusive practices relating to capital raisings by listed issuers and protect the interests of minority shareholders. The Institute made a submission to the proposals.

The changes to the Listing Rules include the rules on:

- Highly dilutive capital raisings
- Rights issues and open offers
- Placing of warrants or convertible securities under general mandate

There are also other rule amendments to enhance disclosure of the use of proceeds from equity fundraisings, and to impose an additional requirement for subdivisions and bonus issues of shares to ensure an orderly market.

The Listing Rule amendments will become effective on 3 July.

Consultation conclusions on delisting and other rule amendments
On 25 May, HKEX published its consultation conclusions on Delisting and Other Rule Amendments to establish a framework to facilitate timely delisting of issuers that no longer meet the continuing listing criteria and provide certainty to the market on the delisting process. The Institute made a submission to the proposals.

Changes to the Listing Rules include:
Main board Listing Rules

- Add a separate delisting criterion to allow HKEX to delist an issuer after a trading suspension of 18 continuous months.
- Allow HKEX to (i) publish a delisting notice stating its right to delist an issuer if the issuer fails to resume trading within the period specified in the notice, or (ii) delist the issuer immediately in appropriate circumstances.
- Remove Practice Note 17, which sets out a three stage delisting procedure for issuers without sufficient
- Operations or assets.

GEM Listing Rules

- Align the delisting process with that of the Main Board except for allowing HKEX to delist a GEM issuer after a trading suspension of 12 continuous months.

The new delisting process and Listing Rule amendments will become effective on 1 August. Interested parties can also read the guidance letter on long suspension and delisting (HKEX-GL95-18).

SFC Regulatory Bulletin: Listed Corporations
On 23 May, the Securities and Futures Commission (SFC) published the second edition of its Regulatory Bulletin: Listed Corporations to provide an update on how the SFC exercises its power under the Securities and Futures (Stock Market Listing) Rules (SMLR) to fulfill its statutory objective of protecting investors.

The newsletter highlights some of the SFC's actions to tackle market misbehaviour in the nine months ended 31 March 2018. Case studies are also included to illustrate the SFC's early intervention in serious corporate cases as well as the close relationship between the use of its regulatory tools under the SMLR and its enforcement actions against licensed firms and listed companies.

SFC consultation conclusions
New OFC Rules and OFC Code
On 18 May, the SFC released consultation conclusions on the proposed Securities and Futures (Open-ended Fund Companies) Rules and Code on Open-ended Fund Companies, which set out detailed legal and regulatory requirements for the new open-ended fund company (OFC) structure. This will enable investment funds to be established in corporate form in Hong Kong, in addition to the current unit trust form.

The SFC will implement the proposals set out in the consultation paper with certain modifications and clarifications. These include streamlining the approval requirements for private OFCs and setting out a one-stop arrangement for the establishment, ongoing corporate filings and termination of OFCs. The OFC regime is targeted to come into effect on 30 July.

Prescribing professional investors
On 18 May, the SFC also released consultation conclusions on proposed amendments to the Securities and Futures (Professional Investor) Rules to standardize the rules for prescribing professional investors. The amended rules are expected to come into effect on 13 July.

The amendments allow portfolios held in joint accounts with non-associates and in investment corporations wholly-owned by an individual to count towards meeting the threshold to qualify as a professional investor.

The categories of professional investors will be expanded to include corporations which have investment holding as their principal business and are wholly-owned by one or more professional investors, as well as corporations which wholly own another corporation which is a qualified professional investor.

In addition, alternative forms of evidence will be allowed to demonstrate qualification as a professional investor.

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Taxation

Annual meeting with the IRD
The annual meeting between representatives of the Institute's Taxation Faculty Executive Committee and the IRD took place on 18 May 2018. At the meeting, the IRD confirmed the due dates for lodging profits tax returns for the year of assessment 2017-18. These are highlighted for members' attention:

Accounting date	Extended due date	Further extended due date (if opted for e-filing)
"N" Code	3 May 2018 (no extension)	17 May 2018
"D" Code	15 August 2018	29 August 2018
"M" Code	15 November 2018	29 November 2019
"M" Code (current year loss cases)	31 January 2019	31 January 2019 (same as paper returns)

Institute's recent tax submissions
The Institute's Taxation Faculty has commented on Inland Revenue (Amendment) (No. 2) Bill 2018, which expands of the scope of specified intellectual property rights eligible for tax deductions on capital expenditure, and proposals to remove ring-fencing features from the tax regimes for funds.

Anti-money laundering notices

Members should note the following notices and publications in relation to anti-money laundering and counter-terrorist financing:

- Government notice (extraordinary) 26: An updated list of terrorists and terrorist associates has been specified under the United Nations Sanctions (Democratic People's Republic of Korea) Regulation.
- Government notice (extraordinary) 28: An updated list of terrorists and terrorist associates has been specified under the United Nations (Anti-Terrorism Measures) Ordinance.
- High-risk and non-cooperative jurisdictions: In May, the Financial Action Task Force (FATF) issued one document: Caribbean Financial Action Task Force (CTATF) Public Statement and Notice of exiting the Follow-up process May 2018, the CFATF Plenary agreed to remove Haiti from its special monitoring process given the forthcoming 4th Round Mutual Evaluation of Haiti. Saint Vincent and the Grenadines made significant progress in addressing the deficiencies identified in the 3rd round Mutual Evaluation and have successfully exited the follow-up process.
- Specially designated nationals and blocked persons list, published by the U.S. Treasury's Office of Foreign Assets Control. More details on the Resource Centre of the Treasury.

Please refer to the full version of TechWatch 188, available as a PDF on the Institute's website: *www.hkicpa.org.hk*

After hours

Book review **Life and everything** **Let's get fiscal**

Book review

GROWING PAINS

Title: **The Growth Delusion: Wealth, Poverty, and the Well-Being of Nations** Author: **David Pilling**
Publisher: **Bloomsbury (U.K.) Crown Archetype (U.S.)**

When the Hong Kong government released its first-quarter gross domestic product (GDP) figures in May, most media thought it was significant data. Newswires such as *Reuters* and *Bloomberg* flashed the information immediately, while *The Wall Street Journal* and the *Financial Times* considered the GDP data newsworthy enough to put on their home pages.

Why do we put so much effort into understanding GDP? It's basically a raw measure of output of goods and services and, as David Pilling describes in his new book, *The Growth Delusion: Wealth, Poverty, and the Well-Being of Nations*, an increasingly irrelevant figure in a world built on software, services and the so-called "sharing" economy.

The concept of GDP was developed in the 17th century and became more commonly used in the 1930s when it was used to measure the effects of the Great Depression in the United States. Simon Kuznets, the "father" of modern GDP reporting and a United States government economist, intended it as a very broad measure of physical materials, whether it be steel, timber, potatoes or tyres.

"Kuznets was striving for a measure that would reflect welfare rather than what he considered a crude summation of all activity," writes Pilling, a *Financial Times* correspondent. "He wanted to exclude illegal activities, socially harmful industries and most government spending."

Kuznets also had challenging ideas from an accounting point of view, such as ignoring the roads and rails that took people from their suburbs to work so they could produce things, because he thought for this is an input into production and not a final output.

He lost most of those battles, and GDP became the go-to figure to measure economic growth and a convenient yardstick to assess competition with rival nations.

GDP persists as a primary economic measure, even though its coverage of services – and even many goods – is spotty. Today, the U.S. counts gun sales but not the drug trade. Colombia's data include drugs but not guns, while The European Union adds the illegal activities of organized crime and other illicit activities.

In China, the concept of GDP as a positive data series is so pervasive that it has become an Internet meme, thanks to the obsession with economic growth of Communist Party chief Li Dakang, a character in the hit *CCTV* series *In the Name of the People*. Yet, China recorded erratic economic growth – some years above 10 percent; others of catastrophic recession – until the 1990s. Pilling notes that delivering year after year of rapid economic growth has become the party's principal source of legitimacy.

Pilling's economic discourse is punctuated by puzzled entrepreneurs of the new economy. Will Page, Director of Economics at Spotify, the Swedish music-streaming service, tells the author: “GDP faces a square peg, round hole dilemma” because it was “originally designed to measure tangible manufactured goods, which are losing relevance.” But as Pilling discovers, the modern world presents its own problems. Is looking at Facebook an economic activity? “Should we really put more of a value on watching a cat video,” he asks, “than, say…. watching a real cat?”

In Hong Kong, Pilling notes, “Australian opals are shipped, via Chungking Mansions, to southern China, where they are polished, sent back to Australia, and sold as souvenirs to Chinese tourists visiting Australia (who presumably take them back to China). In such a world, the idea of domestic production… becomes almost meaningless.”

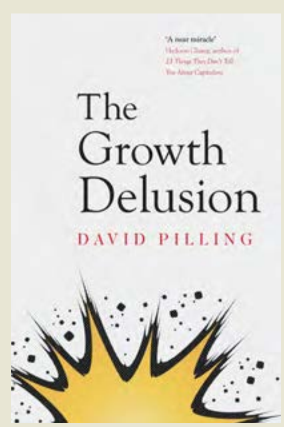
On a broader scale, Pilling tracks the growth of the U.S. economy. But then he surveys the despair pervading the American Rust Belt, with cities like Detroit and Milwaukee denuded of decent jobs, and white middle-aged men succumbing to suicide, drug and alcohol abuse, and other “deaths of despair.”

“It might be stating the obvious to say that raw growth statistics cannot capture intangible feelings, such as the loss of community, job security, well-being, or even identity,” Pilling writes, “but if that is the case, why have we made economic growth – measured by GDP – a proxy for what we are supposed to value in life?”

Author interview: David Pilling

David Pilling spends an awful lot of time explaining a concept he neither likes nor trusts. “When you think about the economy, you think about growth, and we have kind of put growth on a pedestal,” says the long-time *Financial Times* correspondent on a recent visit to Hong Kong.

A simple loaf of bread has become an economic conundrum. “You don’t just say that the loaf of bread is worth £3 and that’s the contribution to gross domestic product,” says Pilling.



“You have to know what went into the bread, so flour went into the bread and wheat went into the flour and each time you have to subtract that as an input so that you get a final figure for the value added.”

Currently the newspaper’s Africa editor, based in London, Pilling has seen the inadequacies of economic measurement. “GDP is terrible at measuring the informal economy, which is interesting when you get to countries that I cover in Africa.”

He also spent several years covering the Asia-Pacific region, based in Hong Kong. His previous book was *Bending Adversity: Japan and the Art of Survival*, published in 2014, which has become something of a primer for expatriates.

That book provided some of the impetus for his current volume. Post-World War II Japan was the ultimate lesson in economic growth. By the 1980s, Japanese diners would sprinkle gold leaf on their food like salt and pepper. Then came years of stagnation. First South Korea, then China overtook Japan economically.

As Japan’s fading international image became increasingly at odds with its very obvious prosperity, Pilling began to question the reality of economic growth and the way it was measured. “Part of what I’m trying to do is to look at the process,” he says. “How we come up with this number, what it means and what it doesn’t mean.”

Another goal is to vindicate Simon Kuznets, who saw his original concept of “national income” distorted and politicized. “It’s now used as the denominator of choice,” says Pilling. “We compare things to GDP – tax to GDP, debt to GDP, but GDP itself is fairly arbitrary.”

Pilling says Kuznets wanted to exclude military spending – “because he thought this didn’t really serve a purpose” – and financial speculation, “because he thought it was useless and possibly dangerous. Something which I would argue makes him ahead of his time.”

Arts

Xiaobaihua Yue Opera Troupe of Shaoxing

OPERATIC BRILLIANCE

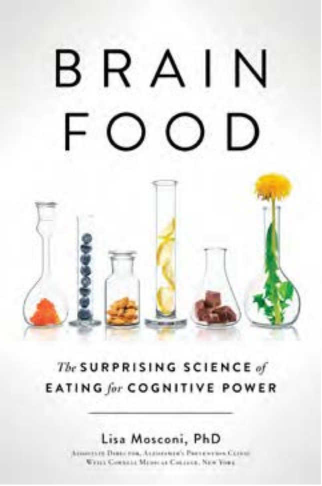
The Chinese Opera Festival 2018 continues its series of shows with Xiaobaihua Yue Opera Troupe of Shaoxing including the grand production of *Qu Yuan*. The plays centre around the tragic story of Qu Yuan, a Chinese poet and minister who lived during the Warring States period of ancient China. The four plays will be performed by an all-female cast, including Wu Fenghua, two-time winner of the Plum Blossom Award for Chinese Theatre and National Class One Performer. There will be lectures, film screenings and talks with artists and exhibitions, providing spectators an opportunity to learn more about the art of performing Chinese opera.

Dates: 19-22 July
Venues: Grand Theatre, Hong Kong Cultural Centre (19-21 July)
Auditorium, Tuen Mun Town Hall (22 July)
Tickets: *www.urbtix.hk*

Read

YOU ARE WHAT YOU EAT

In *Brain Food: The Surprising Science of Eating for Cognitive Power*, Lisa Mosconi, a neuroscientist and nutritionist, provides insight into how the food we consume influences the development of our brains. With her experience in brain imaging, nutrition and genetics, she outlines natural and organic foods responsible for improving memory and preventing cognitive decline.



Available at *www.amazon.com*
USD$15.53

Shopping

BOOK FAIR IS BACK

The 29th Hong Kong Book Fair will be held at the Hong Kong Convention and Exhibition Centre. The seven-day event, organized by the Hong Kong Trade and Development Council, will feature fiction and non-fiction books, storybooks for children and teenagers, religious books, as well as e-book readers, audio visual learning aids and educational software. This year's theme is romantic literature, and the fair will be holding seminars where four Hong Kong authors of romantic literature are to speak on their works.

Address: 1 Harbour Road, Wan Chai
Venue: Hong Kong Convention and Exhibition Centre
Opening hours: 10:00 a.m. - 10:00 p.m. (18 - 19 July), 10:00 a.m. - 12:00 a.m. (20 - 21 July), 10:00 a.m. - 10:00 p.m. (22 - 23 July), 9:00 a.m. - 5:00 p.m. (24 July)
Website: *http://hkbookfair.hktdc.com/en/index.html*

Eat

DOWN MEMORY LANE

Evoking memories of the past, Dragon Noodles Academy are treating guests to some of the best Chinese cuisine until 31 August with its new "A Tasting Journey in Nostalgic Guangzhou" menu. Diners can choose from hearty soups such as double-boiled whole winter melon with lobster and crab meat in soup, and savoury delights such as duck with salted egg yolks, shiitake mushrooms and chestnuts. The restaurant also pays tribute to Bruce Lee's love for liver with a platter of steamed siu mai pork dumplings with pork liver. The décor draws influence from retro Hong Kong and the city's herbal medicine shops, making it a classy yet rustic location for a dinner with friends or family.

Eight treasure duck

Double-boiled whole winter melon

Siu mai pork dumplings with pork liver

Address: G04, G/F, Man Yee Arcade, Man Yee Building, 68 Des Voeux Road Central, Central
Telephone: 2561-6688
Opening hours: Monday to Sunday 11:30 a.m. - 11:00 p.m.
Website: *www.dragon-noodles.com*

Accounting for every wobbly kilo

Hong Kong's humorist on the eye-opening parallels between dieting and accounting

My wife's magazines make me laugh. There are 30 pages of "learn to love yourself as you are," 20 pages of "lose 5kg in two weeks," 40 pages of anorexic models, and 20 pages of recipes.

When I told a colleague I wanted to lose two or three kilos, she offered a tip: "Put a large mirror by your dining table and eat all your meals naked." Nice idea, but it would be hard to get buy-in from my wife and children.

Looking for better advice led me to stumble on an interesting and true story.

A guy called Mike Lee, due to have a beach wedding, decided to get in shape. A fitness trainer handed him a pencil and a book of numbers, telling him: "Calculate the calories of everything you eat and deduct the energy burn of every physical movement you make."

DING! Mike had a flash of inspiration.

Getting in shape is accountancy! It's a bookkeeping exercise in which you maintain a live and continuously updated balance sheet with daily reports.

Being a nerd, he wrote a program that automated the process, calling it "my fitness pal," and later sold it for almost half a billion U.S. dollars.

What made it so popular?

Unlike calorie counting books, Mike's program is like a human accountant, getting to know you, anticipating what you'll get up to, and doing all the math. You don't have to keep typing in stuff because it learns your eating habits and takes your activity data from your phone or Fitbit.

A gym-bunny acquaintance told me that lots of fitness gurus use the accountancy analogy these days. "Your body is the company, your food the investment, the energy you burn the production, and the return is a healthy body," she said.

But of course almost everyone over-invests. "Eat too much food and move too little and you will end up with a budget surplus: fat," says Internet fitness writer Scott McDermott.

Ah! Is that where the analogy breaks down? Excess fat is bad for your body – but having too much money is good for your company, right?

No. "Research shows that having too much cash on hand is almost as bad as having too little," says a 2017 *CNBC* analysis of the subject.

Digression: Did you know that the Germans have a word for eating to de-stress yourself? "Kummerspeck" literally means "griefbacon." If you point at a German's bulging midriff, he or she will say: "My life is stressful: this is the bacon of grief."

"Your body is the company, your food the investment, the energy you burn the production, and the return is a healthy body."

Anyway, here's a list of Three Dieting Thoughts And Business Parallels.

1) "I dieted all morning. Am I skinny yet?" Business parallel: Both dieters and business people expect instant, visible results – and will be disappointed.
2) "I don't need a personal trainer as much as someone to follow me around and slap the doughnuts out of my hand." Business parallel: This is basically the CFO's job in any company, right? Saying "No" to the CEO's pet projects?
3) "I'm feeling fat today, so I am going to make myself feel better by eating this family-sized tub of ice-cream." Business parallel: If consumers don't like the CEO's product, he or she feels affronted and makes more!

The tough truth is that losing a couple of kilos is always harder than you expect. One colleague suggested that I buy that Samsung Galaxy smartphone that makes you look skinnier in photos. I said: "But the downside is that you can NEVER meet your family members face-to-face again."

"How is that a downside?" he asked.

In the end, I decided to skip the diet and take a philosophical stance instead. I shouldn't complain about carrying a couple of extra kilos because it wouldn't be fair to everyone else if I was this intelligent, good-natured, and humble – and slim too.

And if anyone comments, I shall simply point to my stomach and tell them: "This is the bacon of grief."

Nury Vittachi
is a bestselling author, columnist, lecturer and TV host. He wrote three storybooks for the Institute, *May Moon and the Secrets of the CPAs*, *May Moon Rescues the World Economy* and *May Moon's Book of Choices*

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