APRIL 2013
WWW.BDO.COM.HK

APERCU

CONTENTS

GRANDMASTER MEDIATORS IN DEMAND

The Grandmaster

Famous movie director Wong Kar-Wai is a perennial topic of conversation in Hong Kong. Although enjoyed by a certain category of moviephiles, his filmography has long been controversial, in terms of his abstract ideology, trembling images and unhurried production.

The Grandmaster is an example of this. Most filmgoers enjoyed it a lot when it was finally released in January 2013, after an extremely lengthy period of dedicated orchestration. Especially the fantastic skirmishing motions and the romance between Tony Leung and Zhang Ziyi. As usual, Wong subconsciously delivered a distinctive philosophical message; one that appears to suggest that only excellence in their thinking can elevate individuals to the distinguished rank of grandmaster. A DVD will soon be released if you missed it in the cinema, and it will not cost you too much to revisit Wong's portrayal of the grandmaster's mind game involving Leung and Zhang.

While violent skirmishes are thankfully rare in the contemporary business world, disputes do occur often. Obviously, we cannot rely on a cowboy-style shoot out to resolve them. Ultimately, they result in only one survivor. Instead, we need some special mental talents to resolve disputes successfully. Patience and intelligence are the vital keys resolving such unpleasant matters. That somewhat echoes Wong's message in The Grandmaster.

Enactment of the Mediation Ordinance

However, few have noticed that, while the movie was being released, the Mediation Ordinance (MO) (Chapter 620 of The Laws of Hong Kong) was enacted on 1 January 2013. This legislation creates a new statutory platform for dispute resolution. In fact, Hong Kong has become the first jurisdiction in Asia to enact a mediation law. Other well-developed jurisdictions are still contemplating something similar. It sends an important message to the local community and the rest of world: Hong Kong has a modern and advanced law to facilitate the handling of disputes in an efficient and effective manner.

The MO is not a long and exhaustive piece of legislation. In fact, it contains only 11 Sections and two Schedules. These are mainly devoted to the structure and legal implications of any mediation that takes place in Hong Kong. While we are focusing on the business world here, we should not overlook the MO's potential application in non-commercial areas, such as matrimonial and family matters.

The MO's objectives are clear: (i) to promote, encourage and facilitate the resolution of disputes by mediation; and (ii) to protect the confidential nature of mediation communications (Section 3). So why is mediation suddenly emerging as an important character in the drama, and why is it being heavily promoted by the Government?

One must be aware of the judiciary's keen efforts to encourage the parties concerned to resolve their disputes out of court. However, legal practitioners have reservations about the actual success rate of mediation exercises, and there are no published statistics to support the argument that mediation has been extremely effective as a way to resolve legal disputes.

Perhaps, the Lehman Brothers Minibond saga was the catalyst to a certain extent. It fired up the Government's enthusiasm about promoting mediation in the community. Aside from the issue of costs, legal proceedings are indeed lengthy and technical exercises that may not speedily remedy the grievances of litigants. Mediation definitely has a role to play if the disputing parties want to resolve their issues amicably, even if its impact is actually difficult to quantify. At the very least, the disputing parties should not rule it out as a possible way to resolve matters.

Focusing on solutions

The core goal of mediation is to find a solution. That contrasts with arriving at a decision or delivering a judgement, which are the principal aims of judges when any proceedings take place before them. Once that is handed down, someone inevitably wins while another loses. And it is accompanied by frank comments and criticisms by the judges, which may humiliate and be regarded as unwelcome by the losing party.

On the other hand, mediation is a structured process that does not adjudicate a dispute or any aspect of it (Section 4(1) of the MO). It needs not determine the rights or wrongs of the matter. Instead, it focuses on identifying an amicable solution all the parties involved can agree to. This constructive approach can relieve and satisfy everyone with a minimal amount of hassle. Whereas a completed trial in a court is likely to produce a sore loser, successful mediation can often end up with everyone a satisfied winner.

From that angle, we can also begin to understand why mediation can be much more efficient than arbitration, even though neither type of process requires a court to resolve a dispute. Arbitration is common in specialised industries, such as construction, as well as commercial agreements, particularly ones with an international context. When they choose arbitration, the disputing parties agree to be bound by the arbitration's result. They can choose the place of arbitration and the arbitrator(s).

Unlike open court trials, arbitration proceedings shield the disputing parties and the details and information about their dispute behind a curtain of confidentiality. This can be a significant advantage. Nonetheless, even when it is conducted in private, arbitration delivers similar results as a court. The arbitrator(s) must make a decision, and there is inevitably a disappointed losing party at the end of the day. Arbitration proceedings also tend to follow courtroom procedures, which make them complex for the disputing parties.

Mediation can be a way to avoid the possible shortcomings of formal litigation in courts and arbitration. Its biggest advantages are its flexibility, swiftness and solution-seeking approach. One could perhaps argue that settlement negotiations via lawyers can serve the same purpose. But mediation offers a much more direct and broader platform, with opportunities for the parties to share and exchange ideas face to face. A let's-sit-down-and-talk approach can generate greater value in terms of reaching a settlement than exchanges of correspondences between lawyers.

Mediators show the way to the destination

One should nonetheless bear in mind that the right choice of process merely points one in the right direction. There still remains an important void to be bridged before one arrives at the destination. When we travel, of course we need a means of transport. If the parties decide to rely on mediation to resolve their dispute, they need a diligent mediator to help them complete the journey. A wise choice of mediator – one of the appropriate calibre and with the right experience – can greatly increase the chances of success.

The MO contains no concrete requirements for mediators, such as professional qualifications or experience. That is understandable, because the disputing parties are expected to agree freely on their choice of mediator. However, a mediator must ensure that he or she has no conflict of interest concerning the appointment: the MO highlights impartiality as an objective criterion for a mediator (Section 4(1) of the MO). Obviously, professionals in different disciplines are well trained in this risk assessment process, in view of the comprehensive principles set out in their respective professional guidelines.

In essence, the mediator's most important role is to manage the case. The MO sets out the steps of mediation as follows:

(1) Identify the issues in dispute;
(2) Explore and generate options;
(3) Communicate with one another; and
(4) Reach an agreement regarding the resolution of the whole, or part, of the dispute.

(Section 4(1))

Dynamic thinkers and efficient communicators

My experience with mediation is that it is not difficult to identify the issues in dispute. The real challenge for the mediator is to explore the possible solutions (which have to be acceptable to all the disputing parties) and to communicate and explain them well. This is like a work of art that the mediator must paint with due care. There are, of course, standard dialogues the mediator can use to break the ice during the mediation meeting, but it is impossible to predict with certainty how the parties will interact with each other as discussions continue. Circumstances may become heated if undesired emotions are unfortunately invoked.

A capable mediator should think openly and pre-emptively. Of course, he or she should know and understand the tiniest details of the case. The value that can be created for the disputing parties is not the delivery of an ultimate verdict. More precisely, a verdict approach will not enhance the chance of successful mediation. A wide and open mind can avoid digging deep into the roots of a dispute, which seems unnecessary and may discomfort the parties involved. The mediator should instead adopt a big picture approach and think out of the box. Otherwise, he or she could find the number of resolution options extremely limited, which would not be beneficial to the parties who are looking forward to reaching a sensible and agreeable solution.

Persuading everyone to accept an identified option also requires skill and patience. The mediator should not underestimate the possible reluctance of the parties to adopt it. They may not immediately understand and appreciate a good settlement deal when it is put on the table. In theory, a mediation process need not commence in the first place if the disputing parties could easily agree on a solution.

A capable mediator does not jump to conclusions. Instead, he or she clearly understands the positions of the parties in detail and prepares an appropriate speech that addresses any concerns that may possibly arise. This will bolster the parties' belief that a sensible solution has been identified, and thus enhance the chances of success. The parties should seek out a dynamic thinker and efficient communicator as their ideal mediator. You would expect to find such exceptional talents only in a grandmaster.

The success of mediation does not hinge on legal frameworks, but on the mediator's capability to endeavour diligently. If the Government is keen to promote mediation in Hong Kong, it should increase its efforts to train and maintain a pool of capable mediators. After all, grandmaster mediators will always be in demand.

WILFRED WU
Specialist advisory services
wilfredwu@bdo.com.hk

BDO SUPPORTS THE CHAMBER OF HONG KONG LISTED COMPANIES (CHKLC) DIRECTOR TRAINING SERIES 2013

香港上市公司商會
CHKLC THE CHAMBER OF HONG KONG LISTED COMPANIES

CHKLC DIRECTOR TRAINING SERIES 2013

A six-part training programme aiming at supporting directorship in Hong Kong

Programme Partner: BDO Limited

Dates:	13 March 2013	24 April 2013	11 June 2013
	10 July 2013	11 September 2013	6 November 2013

Company directors play a pivotal role in company success. With the increasing demand of corporate governance of listed companies both from the regulators and shareholders, coupled with the tightening of various sets of rules and regulations with more serious consequences, company directors operate in an increasingly challenging environment. Once again, the Chamber of Hong Kong Listed Companies is launching a training programme for company directors. Addressing the common issues faced by directors, the programme will equip directors with the most relevant information and updated knowledge about directorship and will help them discharge their duties effectively.

The whole programme comprises six sessions dealing with the important aspects of directorship for a listed company. These range from board effectiveness, corporate governance, internal control and risk management to rules updates. Experienced professionals as well as directors from listed companies will act as speakers to share their knowledge and first-hand experience, ensuring the practical value of this training programme. Attending this training series will fulfill the latest training requirements under the revised Code of Corporate Governance by the HKEx.

The Chamber is pleased to partner with BDO in offering this programme whose involvement ensures the relevance of the topics covered and adds depth to the discussion.

Time	4:00 pm 4:30 – 6:30 pm	Registration Course Session (2 CPT hours per session)
Venue:	BDO Limited 25/F, Wing On Centre, 111 Connaught Road Central, Hong Kong	
Language:	English	

REGISTRATION

	Full Course	Per Session
CHKLC Members / BDO Clients & Contacts	HK$2,500	HK$480
Non-members	HK$3,100	HK$580

Enquiry: CHKLC Secretariat ☎ (852)2970 0886 🖷 (852)2970 0555 @ info@chklc.org
Online Registration: http://www.chklc.org/web/eng/events.htm

BDO supports the CHKLC Director Training Series for the third consecutive year. Running from March to November, the six seminars are designed with common issues faced by directors in mind. They equip participants with relevant information and up-to-date knowledge about directorship, and helping them discharge their duties effectively.

BDO Directors Patrick Rozario and Senior Managers Eric Zegarra and Jason Wong, Manager Vivian Chow will be among the speakers on important aspects of directorship in listed companies for the Series.

The first session, "Corporate Governance Updates and Risk Management" by Patrick Rozario and Eric Zegarra, took place at BDO's premises on 13 March 2013.

The second session, "Disclosure of inside information" by Patrick Rozario and Jason Wong was done on 24 April 2013.

The schedule and topics for the four forthcoming sessions are shown below.

Date	Topic
11 June 2013	Effective Running of the Board
10 July 2013	Privacy and Data Security
11 September 2013	Latest Listing and Related Rules Updates
6 November 2013	Environmental, Social and Governance

RECENT BDO PUBLICATIONS

HKFRS/IFRS UPDATES

HKFRS/IFRS Update 2013/01: HKFRSs, HK(IFRIC) interpretations and amendments available for early adoption for 31 December 2013 year ends
HKFRS/IFRS update 2013/02: Classification and measurement: limited amendments to IFRS9
HKFRS/IFRS update 2013/03: Clarification of acceptable methods of depreciation and amortisation
HKFRS/IFRS update 2013/04: Sale or contribution of assets between an investor and its associate or joint venture
HKFRS/IFRS update 2013/05: Acquisition of an interest in a joint operation: proposed amendment to IFRS 11
HKFRS/IFRS update 2013/06: Recoverable amount disclosures for non-financial assets

TAX PUBLICATIONS

2013/14Hong Kong Budget Highlights

If you wish to obtain a copy of these publications, please visit www.bdo.com.hk

AVOID THE BIG ONES, BUT DON'T FORGET THE LITTLE ONES!

I am sure every reader can still recall the banking scandal that shocked the world in 1995 – the collapse of Barings Bank in England. This institution, which had a history going back more than 200 years ago – was brought down by Nick Leeson, who held the positions of both a floor trader and head of settlement operations. In brief, Leeson exploited his employer's lack of management oversight and loopholes in the segregation of duties to execute a series of future contracts for speculative purposes, details of which he hid in a special account. However, his hoped-for fortune did not materialise; and his losses amounted to £827 million by the time they were revealed. Barings was declared bankrupt in February 1995.

Fraudulent activities can take many forms. They can be as big as the Barings's case or as small as thefts of the company's assets by an employee. They usually start with small transactions and then snowball into an uncontrollable size. Apart from internal control weaknesses, the perpetrators can often override internal control mechanisms, or even act outside the company's control environment.

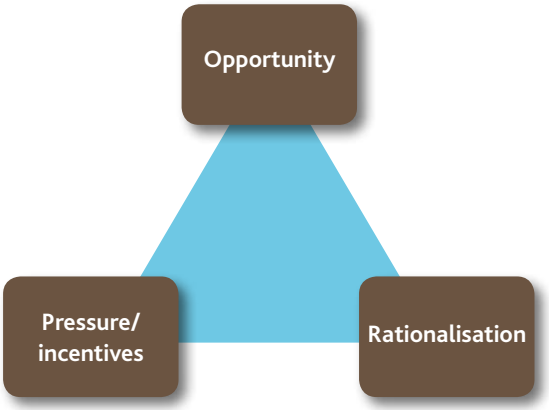
This article will look at some basic fraudulent practices and illustrate how they can be prevented or detected.

What are fraud and the fraud triangle?

According to the Institute of Internal Auditors, fraud is defined as:

"Any illegal acts characterised by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by parties and organisations to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage."

There must be some reasons why perpetrators resort to fraud to achieve such benefits or purposes. We usually refer these underlying motives as the "Fraud Triangle".



Source: Dr. Cressey, "Other People's Money - A study in the social psychology of embezzlement", 1973.

Pressure or incentive	The incentive an individual attempts to satisfy by committing fraud. It often comes from a significant financial need or problem, including the need to keep one's job or earn a bonus. In publicly traded companies, there may be pressure to meet or beat analysts' estimates. Alternatively, the perpetrator wishes to keep his or her position in the organisation, or maintain a certain standard of living relative to perceived peers.
Opportunity	The ability to commit fraud without being detected. Perpetrators do not want to be caught, so they must believe their activities will not be detected. Opportunity is created by weak internal controls, poor management, lack of board oversight, and/or the use of one's position and authority to override controls. Failure to establish adequate procedures to detect fraudulent activity also increases the opportunities for fraud to occur. Persons in positions of authority may be able to create opportunities to override existing controls because their subordinates or weak controls allow these to be circumvented.
Rationalisation	The ability of a person to justify his or her fraud is a crucial component in most cases. Rationalisation involves the perpetrator reconciling his or her behaviour (eg stealing) with commonly accepted notions of decency and trust. It includes simply labelling the theft as "borrowing" with the intention of repaying the stolen money later.

What does the world of fraud look like?

According to the Report to the Nations on Occupational Fraud and Abuse – 2012 Global Fraud Study (the "Report") published by the Association of Certified Fraud Examiners (ACFE), the most common type of occupational fraud was asset misappropriation. This accounted for about 87% of reported cases. It was followed by corruption and billing schemes, with about 50% of reported cases. Although financial statement fraud only accounted for about 8% of reported cases, it caused the greatest median loss at US$1 million. The sectors most commonly involved were banking and financial services, government and public administration, and manufacturing.

An employee at any level can defraud an organisation. The vast majority (77%) of all frauds covered by the Report involved individuals working in one of six functions: accounting, operations, sales, executive and upper management, customer service and purchasing. Those with a higher degree of authority tended to cause much larger losses.

However, the existence of anti-fraud controls had a significant correlation with decreases in the cost and duration of occupational fraud. Organisations with common anti-fraud controls in place suffered considerably lower losses and detected them more quickly than those that did not.

Some basic categories of fraud:

Corruption	Asset Misappropriation		Financial Statements
	Cash	Non-cash	
• Conflict of interest • Bribery • Illegal gratuities • Money laundering • Economic extortion	• Theft of cash on hand • Theft of cash receipts • Fraudulent disbursement	• Misuse • Larceny	• Asset/revenue overstatement • Asset/revenue understatement

The Report states that some fraudulent activities can continue for between 12 and 36 months before detection (see diagram).

Identifying fraud risks and red flag monitoring minor fraud can occur in many organisations. While the Report reveals the median loss through asset misappropriation is low (approximately US$120,000), the frequency of losses on such a scale is the highest.

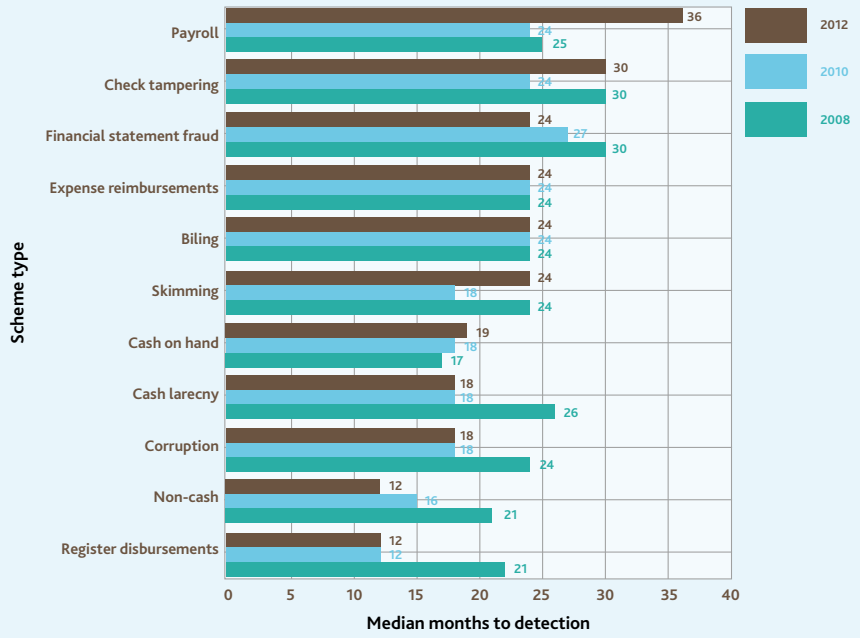
Organisations should deploy effective mechanisms to detect fraud. Their Audit Committee is responsible for overseeing the effectiveness of the company's risk management, financial reporting and internal controls. The external and internal auditors are the audit committee's left and right hands. During regular private meetings with both, the committee can enquire about any indications that fraud exists in the company. It can also demand additional assurances if any red flags become visible.

The losses arising from financial statement fraud can be huge. The external auditor plays an important role in ensuring that the financial statements are free from material misstatements.

Examples of procedures they carry out may include:

- reviews of the reasonableness of key financial ratios;
- verification of the business's development, in terms of examining the consistency of key financial figures, such as sales, purchases and inventories;
- reviews of cash and bank or inventory reconciliation, and requests for explanations of un-reconciled or unusual items;
- verification of the existence of customers by matching delivery documents with cash receipts for sales transactions, and by confirming sales transactions or receivable balances directly with customers; and

Duration of fraud based on scheme type



Source: Report to The Nations on Occupational Fraud and Abuse – 2012 Global Fraud Study by ACFE.

- comparisons of asset valuations by independent valuation firms with those by the management in order to detect any discrepancies.

IIA Standard 1200: Proficiency and Due Professional Care requires internal auditors to have sufficient knowledge to evaluate the risk of fraud and the manner in which the organisation manages that risk. But they are not expected to have the same level of expertise as someone whose primary responsibility is to detect and investigate fraud. Internal auditors normally conduct a fraud risk assessment at the planning stage of an internal audit review. To do this, they use a fraud risk control matrix to list areas that are prone to fraudulent activities. When making a risk assessment, they may also consider the following:

- Financial impact;
- Reputational impact;
- Loss of productivity;
- Potential criminal and civil actions, including those for regulatory non-compliance;
- Integrity and security of data;
- Loss of assets;
- Locations and sizes of operations/units;
- Corporate culture;
- Management/employee turnover;
- Liquidity of assets;
- Volume and/or size of transactions; and
- Outsourcing.

The potential for fraudulent schemes in every area of a company's operations will be considered in order to determine whether appropriate controls are in place to mitigate these specific risks. Additional internal audit procedures may also be designed if the residual fraud risk remains high.

Some examples of these scenarios are shown below.

Case study 1

Payroll misappropriation

ABC, a SME company, establishes a human resource (HR) department to be responsible for handling hiring, promotion and termination, performance reviews, payroll calculations and payroll payments. An HR director is employed to oversee all its operations. For confidentiality reasons, he alone has access to staff personnel records and payroll details. During the monthly payroll payment exercise, the HR director provides the finance department with a total payroll payment balance for journal preparation purposes, and he sends encrypted payroll details on a diskette directly to the bank that processes the payroll payments. The finance department does not have access to these details. Eventually, it is discovered that the HR director has been creating a "ghost employee" whenever a staff member resigns and is not replaced. Payroll payments are subsequently made to his personal bank accounts. In this way, the total headcount remains unchanged.

Internal audit recommendations include:

1. Regular reviews of HR and payroll functions, especially if the business is suffering from resource constraints or lack of segregation of duties;
2. Segregation of other HR and payroll functions;
3. Surprise headcount checks in selected departments, and comparisons with HR records;
4. A register of existing staff and staff movements (both in and out) maintained by the finance department, so this can be reconciled regularly with subsequent payroll details; and
5. Verification of the existence of staff with the HR department's personnel records before adding their details to the payroll register.

Case study 2

Fake sub-contractors

Listed company X's principal business is to provide contracted hygiene services to commercial buildings in the central business district. The company may sub-contract such services to other vendors if it is working at full capacity. These service contracts and the total sums involved are renewed annually, and payments are made quarterly to the sub-contractors.

The business is growing fast, and a money-laundering (ML) group approaches the CFO with a proposal to launder money in return for a share of the proceeds. The CFO accepts the deal and creates a "ghost" sub-contractor, of which he is the beneficial owner. He then prepares a fake service contract with this sub-contractor and subsequent fake services invoices.

The ML Group remits funds to company X as a fake customer, and the CFO applies these funds to ghost sub-contractor ledger account and at the same time, he issues a cheque for a smaller amount (less than HK$50,000) to this ghost sub-contractor in order to avoid needing the approval of senior management and to avoid a balance remaining at the period end.

Internal audit recommendations include:
1. Design procedures to reveal payments to the ghost sub-contractor that falls below the approval threshold;
2. Random checks of the registration documents and beneficial ownership of newly appointed sub-contractors; and
3. Regular anti-fraud reviews that include interviews with operational staff to identify red flags, such as changes in lifestyle and spending patterns.

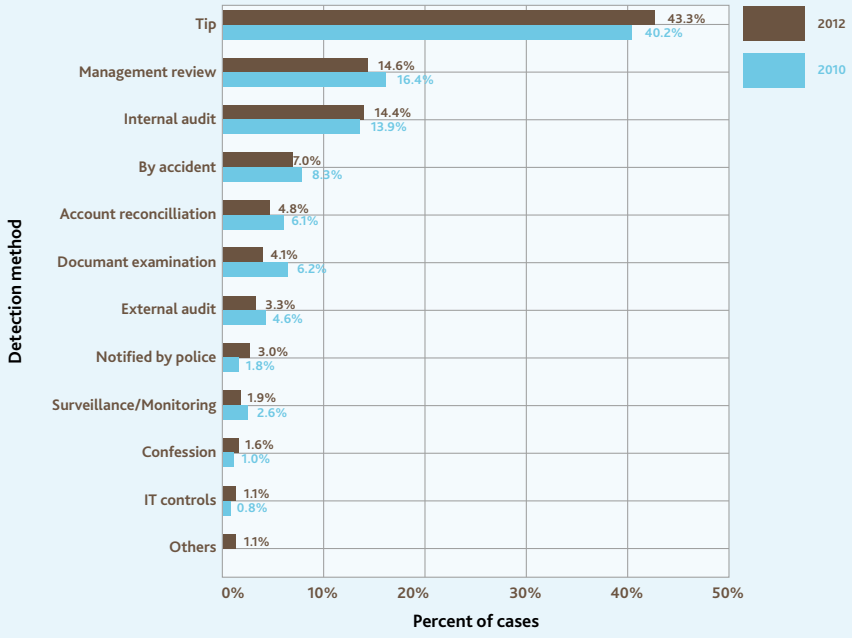
Monitoring red flags can sometimes be useful, as it can alert management to the existence of potential fraud before the scheme grows big and becomes uncontrollable. There are many types of red flags. They may involve employees, management, business cycles, personal lifestyles, changes in behaviour, etc. Internal auditors can also help management by searching for misappropriations and misrepresentations of information.

Some general types of red flags are:

- Unwillingness to take leave;
- Changes in lifestyle;
- Taking up the duties of subordinates;
- Reluctance to provide requested information;
- Conflicts of interest;
- Dissatisfied employees and managers; and
- Collusion between employees and third parties.

Internal auditors can detect fraud, as the Report's findings illustrate:

Initial detection of occupational frauds



Source: Report to The Nations on Occupational Fraud and Abuse – 2012 Global Fraud Study by ACFE.

Implementing fraud risk management programmes

Detecting fraud has always been difficult. Nobody will tell you that he or she is a perpetrator, and the culprits will resort to any method of concealing their wrongdoings from their superiors. They will also conspire with other employees or outsiders. As previously mentioned, effective anti-fraud controls cannot eliminate fraud, but they can make it more difficult to commit fraud, thereby reducing its potential impact on the organisation.

Internal auditors can help management implement an effective fraud risk management programme that may include:

- A company ethics policy — The senior management's "tone at the top" and enhance the formal fraud-prevention policy;
- Fraud awareness — Understanding the nature, causes, and characteristics of fraud;
- Fraud risk assessments — Evaluation of the risks of various types of fraud;
- Ongoing reviews — An internal audit activity that considers the risks of fraud in every audit and performs appropriate procedures based on these;
- Prevention and detection — Making efforts to reduce opportunities for fraud to occur, and to persuade individuals not to commit fraud, due to the likelihood of detection and punishment;
- Investigation — Procedures and resources to investigate fully and report suspected fraud;
- Whistleblowing — Establishing channels for reporting, and measures to protect the identity of whistleblowers; and
- Others — Effective management reviews, fraud training, surprise audits, etc.

RICKY CHENG
Risk advisory services
rickycheng@bdo.com.hk

References:
1. Barings Bank – Wikipedia Website
2. The Institute of Internal Auditors (IIA)
3. Report to The Nations on Occupational Fraud and Abuse – 2012 Global Fraud Study by ACFE
4. Hong Kong Auditing Standards 240

CLEMENT CHAN APPOINTED AS THE INAUGURAL MEMBER OF ACCOUNTING STANDARDS ADVISORY FORUM OF INTERNATIONAL ACCOUNTING STANDARDS BOARD (IASB)

BDO Managing Director – Assurance Clement Chan has been appointed to represent the HKICPA and the Asian-Oceanian Standard-Setters Group (AOSSG) as one of the 12 inaugural members of a newly formed technical advisory body to the IASB, Accounting Standards Advisory Forum (ASAF).

The other 11 members include regulators/ finance officials from other major economies in the world, namely China, Japan, Australia, UK, Germany, Spain, US, Canada, Latin America, South Africa and the European Financial Reporting Advisory Group.

This honourable appointment is a proven recognition of Clement's ongoing contribution to the profession, and his forthcoming participation in this important international accounting standard-setting community is also valuable.

More information about this can be seen at:
- Accounting Standards Advisory Forum (ASAF) http://www.ifrs.org/The-organisation/Advisory-bodies/Pages/Accounting-Standards-Advisory-Forum-%28ASAF%29.aspx
- press release announcing the ASAF membership http://www.ifrs.org/Alerts/Governance/Pages/Trustees-announce-membership-of-ASAF-March-2013.aspx

BDO NEW APPOINTMENTS

LESLEY YEUNG
Director
Head of Assurance

Lesley Yeung, a director of the firm, has been appointed as Head of Assurance.

Lesley has over 25 years of public accounting experience, serving both publicly-traded and privately-held organisations. Her clients include local companies as well as multinationals. Her professional involvement spans a broad scope of industries with companies engaged in manufacturing, distribution, retailing, shipping, construction, software development, healthcare and charitable organisations. Her experience includes statutory audits, initial public offerings, due diligence reviews and business consulting. She is also experienced in handling global practice clients in various industries, leading and coordinating global assignments.

Lesley is a Certified Public Accountant (Practising) in Hong Kong. She is also a member of the Institute of Chartered Accountants in England and Wales.

GARY STEVENSON
Director
Technical & Training

Gary Stevenson was promoted to be a director of the firm.

Gary provides advisory services to the BDO Assurance practice. He primarily focuses on the application of International Financial Reporting Standards (IFRS) and Hong Kong Reporting Standards (HKFRS) by listed issuers in Hong Kong and Singapore.

Prior to joining BDO, Gary worked for another major accounting network's technical department in its UK, China and Hong Kong member firms and also its international IFRS team. He has substantial experience of the application of IFRS by issuers listed on the AIM market in UK. He has accumulated 16 years of experience in major international accounting firms.

Gary is a Chartered Accountant and a Fellow of the Institute of Chartered Accountants in Ireland. He holds a Bachelor of Sciences degree in Economics from Queen's University in Belfast, Northern Ireland.

ANTHONY FONG
Principal
Quality Assurance

Anthony Fong rejoined the firm as a principal of quality assurance and mainly responsible for the areas of quality assurance of the firm.

Prior to joining the quality assurance unit, Anthony was an Assurance principal and had over 15 years of assurance experience especially in handling US listed issuer audits. Anthony's past clientele includes both local and multinational clients that cover a broad spectrum of industries, including manufacturing and trading of toys and gifts, packaging products, garment and apparel, semiconductors, sanitary papers, freight forwarding, recruitment and executive search; computer software and IT solutions, and trade fairs and exhibitions.

Anthony is a member of American Institute of Certified Public Accountants, a member of Certified Fraud Examiners, a fellow member of the Association of International Accountants and holds a Degree of Master of Business Administration from the University of North Carolina.

WHAT MATTERS TO EMPLOYERS IN 2013

Amendment to the Minimum Wage Ordinance

The Legislative Council has passed a legal amendment that will increase the statutory minimum wage (SMW) to HK$30 per hour, with effect from 1 May 2013.

The monetary cap for employers to keep records about the total number of hours their employees worked will also be revised to HK$12,300 per month from the same date.

The SMW rules before and after the amendments are summarised in Table 1.

Table 1

Details	Amendment to Statutory Minimum Wage	
	Before the amendment	With effect from 1 May 2013
Minimum Hourly Wage	HK$28	HK$30
Monetary cap for keeping records of hours employees worked	HK$11,500 per month	HK$12,300 per month

Increase of minimum and maximum income levels for MPF contributions

The Labour Advisory Board intends to propose an increase in the minimum monthly relevant income (RI) for Mandatory Provident Fund (MPF) contributions from HK$6,500 to HK$7,100, and the maximum RI from HK$25,000 to HK$30,000.

Responding to requests to reform the MPF system, the Mandatory Provident Fund Schemes Authority (MPFA) says it will consider reducing the interval for reviewing the minimum and maximum RI levels from once every four years to once every two years.

If the above increases are implemented, monthly MPF contributions will be as shown in Table 2.

Table 2

Monthly relevant income	Mandatory contribution amounts		
	Employer's contribution	Employee's contribution	Self-employed person's contribution
Less than HK$7,100	Relevant income x 5%	Not required	Not required
HK$7,100 - HK$30,000	Relevant income x 5%	Relevant income x 5%	Relevant income x 5%
More than HK$30,000	Capped at HK$1,500 per month	Capped at HK$1,500 per month	HK$1,500 per month or HK$18,000 per year

Forthcoming MPF revisions

MPF reform proposals

Hong Kong residents have criticised the MPF system since it was implemented, especially its "high fees and low returns". The MPFA has therefore recently proposed some reform measures that would require the following actions by the government:

- Legislation to cap fees associated with MPF funds;
- Consideration about mandating the inclusion of various types of low-fee funds that invest in equities or bonds in every MPF scheme;
- Provision of a basic, low-fee default fund arrangement as an option for scheme members who are unable to decide how to invest their MPF contributions; and
- Introduction of a not-for-profit operator (such as a trade union or social enterprise) to act as a members' advocate and operator of a simple, low-fee MPF scheme.

The MPFA hopes the introduction of the above-mentioned reforms would improve the MPF system, so that MPF management fees would be reduced, fund management systems would be streamlined and automated; and that an employee-driven MPF system can be introduced that will better safeguard the lifestyles of retired employees.

We must wait to see whether the government will give its full support to the MPFA's proposed reforms, which would involve amending the MPF Schemes Ordinance. Without such a fundamental change, the MPFA can only implement administrative measures that will have a relatively insignificant impact.

The long-term objective – full MPF portability

The Employee Choice Arrangement (ECA or MPF Semi-Portability) came into force on 1 November 2012. However, it is only a partial solution to demands by employees for the right to choose and manage their own MPF benefits entirely by themselves.

Further ahead, the MPFA is considering the feasibility of the MPF full-portability arrangement, which would further increase the power of employees to control both their own and their employer's MPF investments.

Recently, Professor KC Chan, Secretary for Financial Services and the Treasury, said he hoped the MPF full-portability arrangement can be implemented within the next three years. It would require a study of how it should be implemented and enhancement of the MPFA system.

Meanwhile, the Chief Executive pledged in his 2013 policy address to bring down MPF fees and charges. He also indicated that the practice of allowing employers to offset severance payment (SP) and long-service payments (LSP) against MPF contributions for their employees should be progressively reduced.

An employer that is required to pay SP or LSP under the Employment Ordinance can currently offset this against the accrued benefits derived from its contributions to a MPF scheme on behalf of the employee.

Some Executive Council members have voiced objections to the proposal to stop SP/LSP offsetting, as they are worried the change could adversely affect most small and medium-sized enterprises.

A number of controversial issues involving various stakeholders are expected to arise before the government implements the full-portability arrangement.

Paternity leave

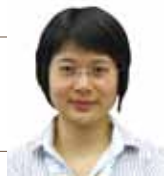
Since 1 April, 2012, all full-time government employees – including civil servants, non-civil service contract staff and political appointees – who have continuously served for 40 weeks or more immediately before the expected or actual date of their child's birth are eligible to enjoy five working days of paid paternity leave.

The number of private organisations providing paid paternity leave to employees is rising continuously. A survey has found the percentage of respondent organisations that voluntarily offer paid paternity leave to employees increased from 16% in 2006 to 38.7% in 2012.

The Labour Department (LD) has also conducted a study about legislating on paternity leave. It has looked into practices in other countries where statutory paternity leave is provided, and explored the issues the government must deal with if statutory paternity leave is introduced. Since most employers in Hong Kong are small and medium-sized enterprises that have less flexibility about staff management, the government must consider local circumstances in order to ensure a reasonable balance is struck between the interests of employees and affordability for employers. The LD will continue to evaluate the prevailing situation to consider whether to legislate on paternity leave. It seems such legislation is unlikely to happen in 2013.

JOSEPH HONG
Payroll services
josephhong@bdo.com.hk

YVONNE LIM
Payroll services
yvonneylim@bdo.com.hk



MANAGING DATA SECURITY AND PRIVACY

The increasing use of the internet and new technologies in the past decade has led to a growth in the volume of personal data being collected, stored and used by businesses and government agencies around the world. Concern about this issue is rising. To address the challenge, organisations should adopt certain measures that will allow them to use such information to their advantage. For instance, many companies find it very useful when they want to learn more about the interests and needs of consumers. But they must also ensure they respect and observe the rules and policies that govern data privacy and security.

In recent years, we have seen the emergence of new technologies, such as cloud computing, mobile devices (smart phones and tablets), document management and collaborative software and online applications. These developments are having a critical impact on data privacy and security.

Cloud computing is the use of resources that provide services over a network. It entrusts these remote services with data, software and computation. The range of online applications has been expanding in recent years, to the point where people can now use them with just a web browser and Internet connection. That allows access to the services without having to download anything onto their personal computer, which saves its disk space. Instead, the data – which may include sensitive personal information – are stored in remote sites.

One example of this is the growing use of mobile devices and smart cards for trading. In Hong Kong, you can access your bank account and do online trading with a smart device, a PIN number and a personal password. You can use these services via your mobile device and computer, as well as a tablet device. But the convenience comes with security risks. A survey of 768 IT professionals around the world conducted by Dimensional Research revealed that 71% of them think mobile devices have increased the incidence of security risks. It is therefore important that employers realise the dangers and train their staff about internet security and its importance.

Businesses can also take other actions to reduce the incidence and impact of such risks. They can consider conducting annual privacy compliance audits and review their responses to incidents and breach notifications, as well as their disaster recovery and crisis communication plans. They can establish a risk committee that is separate from the audit committee, and assign it to deal with all types of risks, including IT ones. They should ensure that its membership includes directors with IT governance and cyber-risk experience.

Conducting annual data security reviews would allow enterprises to identify and improve their strengths, while reducing their weaknesses. Companies can make sure they encourage and create a culture of security and respect for privacy by reviewing their top-level policies and actions. They should require regular reports on privacy and security risks from their senior management and asses them. Doing so will allow them to make certain that data security and privacy are being managed appropriately. Also, they should have cyber insurance that it is adequate to cover potential and unforeseen losses.

Hong Kong's Personal Data (Privacy) Ordinance has remained largely unchanged since its enactment in 1996. It looks at six principles concerning the collection, accuracy and duration of retention of personal data, as well as their use, security, availability and accessibility. An amendment to the Ordinance was passed in June 2012 and most of its provisions came into effect in October the same year. The amendment adds specific obligations about using personal data or providing them to third parties for direct-marketing purposes.

The Personal Data Protection Act (PDPA) was passed in Singapore on 15 October 2012. Its main objectives were to position Singapore as a global hub for data management and cloud computing, and to attract more data centres and data analytics firms to set up operations there. The PDPA's main features are general rules and exclusions concerning the use and/or disclosure of personal data and requests by individuals to access their own data. It also allows individuals to find out how organisations are using their personal data and to correct inaccurate data and seek redress for suspected breaches of the PDPA.

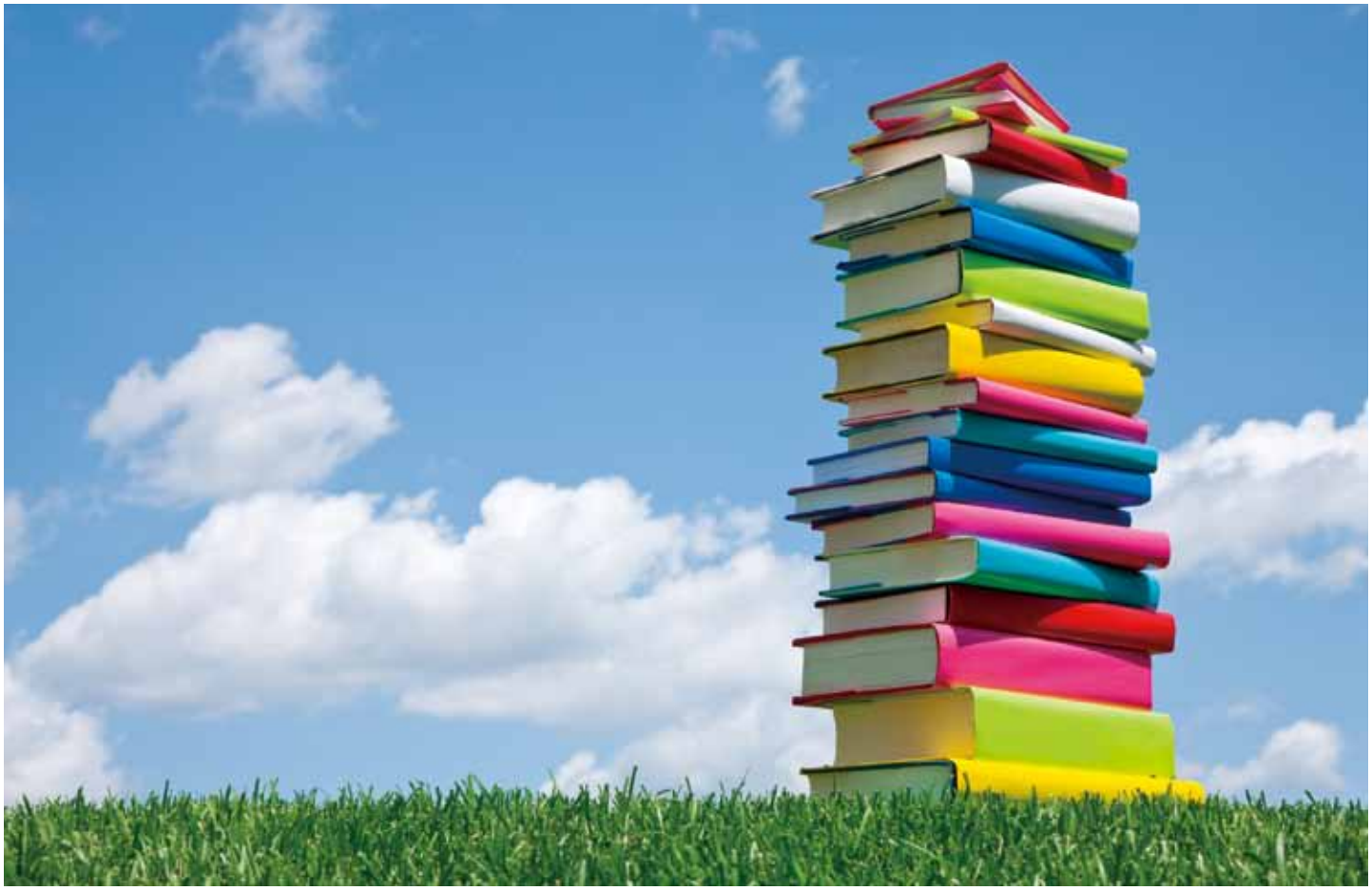
There are other provisions covering the introduction of a penalty and enforcement regime for breaches of the PDPA and the establishment of a "Do Not Call Registry" that allows consumers to stop calls from telemarketers. The Act also requires at least one individual in every organisation to be responsible for compliance with it.

It is important to have controls to safeguard the confidentiality, reliability and accessibility of information. Understanding and acting on these three fundamentals of information security can decrease IT risks by putting adequate IT organisation, infrastructure, physical controls and system access controls into place.

A Privacy Impact Assessment (PIA) is recommended for companies where privacy issues arise during business processes. This scrutinises how personal data are handled, to help ensure this is done legally and in accordance with the laws of the countries where a company operates and where the data are used. It is also used to determine the risks and consequences of gathering and retaining identifiable information in any electronic system. Finally, it is used to examine and evaluate the protection of this information, and alternative ways to reduce potential privacy risks.

In conclusion, it is important for both businesses and the public to understand how their personal data are being used, and to safeguard themselves against others misusing such data. Businesses should make certain they understand their rights about using the information, and that they do so in accordance with the various laws of the countries where they operate or get data from. They should be certain they have safeguards to ensure personal information is not leaked or misused. They should have a designated department or person/team in charge of dealing with the issue, which is becoming increasingly important as public awareness of it grows. They must respect and understand the concerns and wishes of their customers, so that the latter will trust them enough to give their personal details and information. That is especially important where online trading, banking and purchases are involved.

HERMES LIANG
Risk advisory services
hermesliang@bdo.com.hk



ARE YOU READY FOR THE COMPETITION LAW?

Amid recent regulatory enforcements around the globe, one of the latest trends in prosecutions includes the enforcement of anti-trust regulations against corporations which have been accused by regulators of price fixing.

The Chinese government recently prosecuted two of the largest producers of Chinese white wine for retail price maintenance. They were fined close to RMB450 million.

Also in China, the National Development and Reform Commission punished six LCD panel makers with penalties totalling approximately US$56 million, of which approximately US$27 million was reportedly paid in refunds to victimised TV manufacturers. The enterprises involved also had to extend the unpaid warranty periods they provided for some of the manufacturers.

The six included two Korean and four Taiwanese enterprises. The regulator said they had been involved in rigging the prices of display panels sold to Chinese TV manufacturers between 2001 and 2006. The firms were also alleged to have held meetings to negotiate or manipulate prices during this period, and their actions obstructed the legitimate rights and interests of other parties and consumers.

The two Korean electronics manufacturers were also penalised by their national regulator, the Fair Trade Commission. They were recently fined a total of approximately US$39 million for conspiring to fix the prices of TVs, washing machines and laptop computers. The regulator stated they had met secretly to agree on the prices of such products.

Enforcement agencies in other parts of the world have likewise been pursuing companies that reportedly conducted price fixing or cartel activities during the past few years. They include European, Korean, Japanese and Taiwanese enterprises that were sued by the US Department of Justice and the European Commission. The European Commission has stated the companies involved participated in cartels to fix prices, limit production or share markets and customers.

It is obvious that corporations must comply with relevant anti-monopoly regulations at all times; otherwise, they will suffer significant financial and reputational damage.

The rules

In Hong Kong, the Legislative Council voted to enact the city's first cross-sector competition law, the Competition Ordinance, in June 2012. The government has also announced that a Competition Commission and a corresponding Tribunal respectively will be set up during 2013. These will have investigative and enforcement powers, including authority to investigate enterprises and compel them to disclose information. These measures were announced in the Competition Ordinance (Commencement) Notice published in the Hong Kong Government Gazette in November 2012.

The Competition Ordinance prohibits the following categories of actions that have the objective or the effect of preventing, restricting or distorting competition in Hong Kong:

1) ***First Conduct Rule - Serious anti-competitive conduct / agreements with competitors / concerted practices (including informal arrangements, "gentlemen's agreements", tacit or expressly agreed co-ordination of conduct; decisions and actions of trade associations and professional bodies)***

The First Conduct Rule covers activities such as price fixing, market sharing, output restrictions or bid rigging. It also covers "horizontal" and "vertical" agreements that include the following:

a. Horizontal agreements between competitors, such as:
   - Joint ventures
   - R&D agreements
   - Joint purchasing / selling agreements
   - Commercialisation agreements
   - Establishment of joint technical / design standards
   - Restrictions on advertising
   - Sharing of information

b. Vertical agreements at functional levels (eg involving retailers, distributors, suppliers), such as:
   - Exclusive dealing arrangements
   - Resale price maintenance
   - Bundling / tying
   - Information sharing with distributors / retailers
   - Selective distribution
   - Franchise agreements

The law exempts enterprises with a global total annual turnover of HK$200 million or less from the First Conduct Rule.

2) Second Conduct Rule - Rule Against Abuse Of Substantial Market Power

The Second Conduct Rule applies to conduct such as:

- Predatory pricing – Charging below-cost prices to drive a competitor out of the market or prevent its entry
- Price discrimination – Charging different prices to similarly placed customers, or the same prices to differently placed customers
- Target or loyalty rebates / fidelity pricing or discounting – Making the prices of goods or services or the availability of discounts dependent on retaining all or part of a customer's business
- Bundling / tying – Making the purchase of products which the buyer wants conditional on the purchase of other unconnected products
- Exclusive dealing – Requiring the buyer to purchase goods only from the vendor
- Refusal to supply – Refusing to supply goods or services at all, or supplying them only on clearly unacceptable terms

There is also an exemption from the Second Conduct Rule for enterprises with a market share threshold of less than 25%, or a total global turnover of HK$40 million or less a year.

The penalties that may be imposed under the Competition Ordinance are hefty. They include fines of up to 10% of the annual turnover of companies or individuals in Hong Kong for every year they infringe the law, up to a maximum of three years. The directors of companies may be disqualified or banned from involvement in corporate affairs for up to five years.

Other sanctions include divestiture of assets, shares or businesses, voiding of agreements, imprisonment, injunctive orders, and the appointment of a third party to take control of property. Prohibitions can be imposed on the withholding of goods or services, and the exercise of voting rights attached to shares, stocks or securities.

Moreover, offenders may be required to disgorge their profits to the government, third party damages can be awarded, warning notices (such as orders to cease conduct within a specified period) and infringement notices (such as orders to commit themselves to complying with certain conditions) can be issued. Legally binding commitments can be imposed. Inevitably, the companies involved will also suffer adverse publicity, reputational damage or business downtime during legal proceedings.

The ordinance also contains a provision for cartel leniency applications by companies that proactively approach the regulator with evidence of unlawful conduct. Some legal advice notes that the sooner a company reports anti-competitive behaviour, the more likely it is to receive more lenient treatment. Nevertheless, leniency does not include immunity from actions seeking damage initiated by third parties.

Apart from the above exemptions, there are other exemptions as follows:

- Block exemptions – The Commission may, of its own volition or upon receipt of an application, grant block exemption orders for certain categories of agreements covered by the First Conduct Rule
- General exclusions – Instances when a company needs to comply with a legal requirement, or it has been entrusted by the government to provide services of general economic interest
- Efficiency exclusions – Activities covered by the First Conduct Rule (eg certain circumstances in which a cartel agreement improves production, distribution, technical or economic progress, or benefits consumers).
- Specific exemptions – Based on public policy grounds, avoidance of conflict with international obligations, or other situations

Steps to take in the meantime

Companies should immediately arrange an independent review of their existing policies and practices, pricing procedures, compliance manuals and any agreements with relevant parties, in order to assess whether there is any potential risk of breaching applicable anti-trust regulations. In particular, the independent review should assess the following areas:

- Participation by the company in any anti-competitive arrangements or cartels (eg being part of a syndicated group that cooperates or collaborates in pricing or market- sharing activities)
- Existence of any "vertical" or "horizontal" undertakings, either formal or informal, that restrain competition
- Possible misuse of a dominant market position
- Implementation and the effectiveness of policies that concern:
  - Restrictions on the disclosure of any confidential information (eg trade secrets, costing or pricing policies) to external parties;
  - Prohibitions on requesting the above information from competitors;
  - Restrictions on staff members engaging in or concluding any agreements relevant to competition;
  - Prohibitions on membership of any association or attendance at meetings or events that conclude agreements with competitors to prevent competition; and
  - Documentation of the rejection of such agreements.
- Continuous monitoring, educating and training of staff members about the prevention of cartels and other compliance issues.

E-discovery, data analytics and anti-corruption programmes

Independent consultants are increasingly using electronic information discovery and data mining and analytics when they review compliance with anti-trust regulations. E-discovery and data analytics involve collecting, analysing, searching and categorising substantial amounts of electronically stored information. This can include such data as emails, financial spreadsheets, and vendor and purchasing histories stored in ERP systems, accounting ledgers, etc.

Such methodology helps companies gain a better understanding of any relevant anti-competitive behaviour. It might involve costing and pricing information, dealings with suppliers and customers (such as transaction volumes, amounts, frequency and patterns) and correspondence with external parties that the company may previously be unaware of. E-discovery and data analytics can also detect signs of potential non-compliance and red flags in advance, and they can help identify anomalies and fraud, such as irregular round-tripping transactions or financial statement manipulation.

Companies also need to bear in mind that bribery and corruption can be closely linked to anti-competitive behaviour. For instance, individuals may collude to offer or accept illicit kickbacks in return for favouring a particular supplier or customer, thus hindering fair competition among players in the market. Businesses should therefore also ensure that the effectiveness and robustness of their anti-fraud and corruption policies and controls are regularly tested independently.

It is essential for businesses operating in Hong Kong, China, Asia or worldwide to make competition compliance a top priority.

GABRIEL WONG
Specialist advisory services
gabrielwong@bdo.com.hk

BDO GLOBAL NETWORK DEVELOPMENT AT A GLANCE

UK – BDO and PKF merger completes

BDO LLP in the UK has announced that its merger with PKF (UK) LLP has completed. The firm will operate as one, under the BDO brand and as part of BDO's international network, the largest global accountancy organisation aimed at the mid-market, with revenues of over $6bn operating in 138 countries worldwide.

The merged firm is a leading accountancy and business advisory firm generating revenues approaching £400million. It boasts a transformed regional network, employing 3,500 people across 24 UK locations.

New member firm in India

BDO has appointed a new member firm in India, effective 1 April 2013. The firm specialises in providing high-end services in tax, regulatory and audit assurance and is consistently rated as one of the leading tax firms in India. Their full service offering includes the full suite of tax services - from tax advisory and compliance, through indirect tax advisory to transfer pricing – as well as transaction advisory and support and business transformation services. Zulfiqar Shivji is the head of Transaction Advisory and Sagar Shah, is the head of Indirect Tax Advisory Group. Their client base is made up of both international organisations and domestic entities with a strong international focus, and includes pharmaceutical, engineering and construction companies, as well as automobile manufacturers.

BDO announces merger in Israel

BDO Israel is pleased to announce recent mergers with two local firms, Ehud Kish & co. and Assad Tannous & co., both effective 1 December 2012. The mergers include audit, accounting and tax practices based in Jerusalem and Tel–Aviv and bring a total number of 40 employees to BDO.

BDO announces admission of new firm in Mongolia

BDO has announced the admission of a new BDO Member Firm in Mongolia, effective 1 January 2013. BDO Mongolia has been created by the bringing together of audit firm Itgelt Audit and IT / Advisory firm Amar Incon. Amar Incon was established in 2005 by partners Yair Jacob Parot and Rentsenkhand Davagjantsan. The key services they provide are consulting, accounting and tax advisory, together with IT consulting and audit services, as well as e-banking security solutions. Both firms are based in Mongolia's capital, Ulaanbaatar, and together they bring four partners and about 40 staff members to the BDO network.

BDO strengthens its position in Morocco

BDO has concluded a merger with two auditing and accounting firms based in Rabat, Morocco. The two firms are owned by Salah El Ghazouli and Larbi El Oufir respectively, both of whom are former Presidents of the Regional Council of the Order of Chartered Accountants in Morocco. The firms have a total turnover of MAD 7 million (approximately €600,000) and 30 employees altogether.

RETIREMENT OF JENNIFER YIP

Jennifer Yip, Director and Head of Assurance of BDO Hong Kong stood down her role effective from 1 April 2013. Upon her retirement, Jennifer continues her contributions to BDO Hong Kong in a new capacity as an Advisor commencing 1 April 2013.

We would like to take this opportunity to thank Jennifer for her past invaluable contributions and continuing commitment to BDO.

CONTACT
25th Floor Wing On Centre
111 Connaught Road Central
Hong Kong
Tel: +852 2218 8288
Fax: +852 2815 2239
info@bdo.com.hk

www.bdo.com.hk