

# APERCU

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## KEY VALUATION FACTORS TO CONSIDER FOR LONG SERVICE PAYMENTS



### Overview

The value of higher education and qualifications in the workplace has risen like never before over the past decade. As qualification requirements for workers continue to increase, employees also demand better rewards and benefits. Competitive employee benefit policies have therefore become a prerequisite for companies seeking to retain good employees. However, employee benefits constitute large liabilities that need to be reported in companies' financial statements. It is therefore important for employers to understand the impact of certain types of benefits on their companies' financial statements, to ensure that they are aware of the impact of benefits on their business.

Employee benefits refer to various kinds of benefit/compensation that an employer provides to employees in addition to normal wages and salaries. These may be in the form of a defined contribution plan, a defined benefit plan, a multi-employer plan, etc. This article focuses on long service payments (LSP), one of the most common forms of post-employment benefit required by law in Hong Kong.

### Long service payments

LSP is a form of defined benefit plan that employers in Hong Kong are obligated to honour under the Employment Ordinance<sup>1</sup>. Hong Kong Accounting Standard 19 (HKAS 19) requires a company to make provision for defined benefit plans by reporting the defined benefit obligations (DBO) and the relevant service costs in the company's financial statements. In this regard, valuations of the DBOs and the relevant costs are required.

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<sup>1</sup> Hong Kong e-legislation, Cap. 57 Employment Ordinance – Part VB Long Service Payments, <https://www.elegislation.gov.hk/hk/cap57>

LSP is effectively the benefits payable by the employer at the end of the employment term. Employee-specific factors such as length of employment and relevant salaries are usually critical input required when valuing the LSP. In an actuarial valuation exercise, the fair value of the LSP is equal to the sum of the present values of these post-employment benefit payments, after applying the probabilities for occurrence of different benefit payment scenarios and the applicable discount rates.

### Valuation methodology

When companies perform valuations of their DBOs, it is recommended that they adopt the projected unit credit method. This is the common actuarial valuation method accepted under HKAS 19. This method should be adopted for the measurement of the present value of employee benefits attributable to service to date, as it calculates each additional unit of benefit entitlement for each period of service by employees. The sum of each unit of benefit entitlement is then discounted by the applicable discount rate to derive the present value of the DBOs and the amount of service costs plus interest costs to be recognised for the reporting period.

Employees are usually eligible to receive LSP if they are employed for not less than five years under continuous contracts. This article includes a simplified example of how valuations of LSP

can be conducted using the projected unit credit method.

### Valuation factors in assessing LSP

In accordance with requirements from the Labour Department of the Government of the Hong Kong Special Administrative Region, an employee under a continuous contract for not less than five years may receive LSP under the circumstances outlined below:

- (i) When he/she is dismissed (except by reasons of redundancy or employee's serious misconduct);
- (ii) When his/her fixed term employment contract expires without being renewed;
- (iii) When he/she dies during employment;
- (iv) When he/she has been issued a certificate by a registered medical practitioner, certifying that he/she is permanently unfit for his/her present job and he/she resigns; or
- (v) When he/she is aged 65 or above and resigns on grounds of old age.

Guidelines<sup>2</sup> from the Labour Department also suggest that the LSP is to be calculated as follows:

The final monthly salary commonly refers to the last month of salary that would be paid to the employee prior to termination of employment. The reckonable years of service refers to the number of years that the employee provided services for his/her employer. In Hong Kong, the maximum amount of LSP payable to any employee is HK\$390,000.

In a complete LSP valuation, the actuary/valuation professionals construct a valuation model that is based on a set of actuarial and financial assumptions. These assumptions are estimated variables that affect the total costs of providing post-employment benefits. Common actuarial assumptions comprise demographic assumptions about future characteristics of current and retired employees, including mortality rate, rate of employee turnover, rate of annual salary adjustment, disability and early retirement, and eligibility for benefits as defined by schemes. Financial assumptions include the applicable discount rate, benefit payment amounts and relevant costs relating to employees' service for the reporting period.

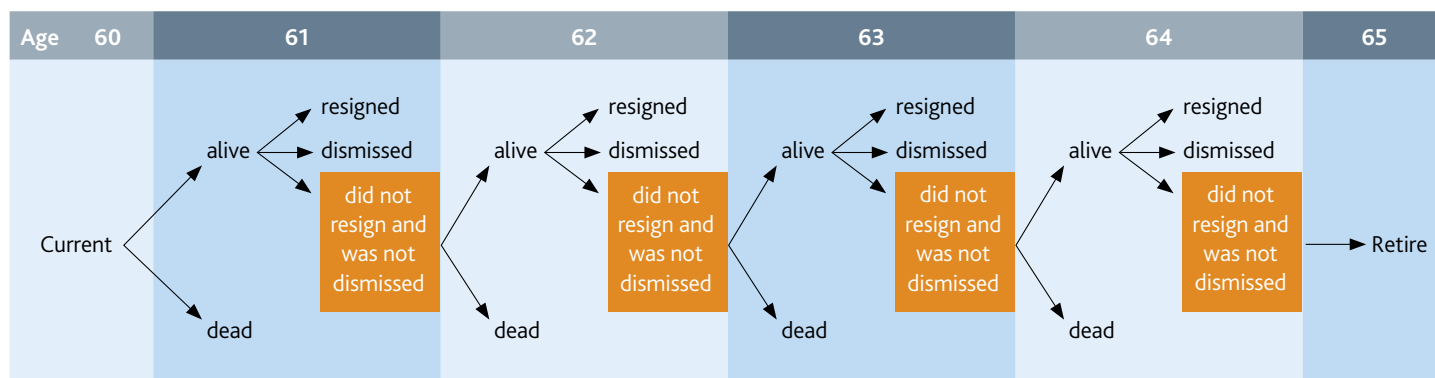
$$LSP = \text{Final monthly salary} \times \frac{2}{3} \times \text{Reckonable years of service}$$

Table 1

| Time                                  |                                                                        | 1           | 2           | 3           | 4           | 5           |
|---------------------------------------|------------------------------------------------------------------------|-------------|-------------|-------------|-------------|-------------|
| Age                                   |                                                                        | 61          | 62          | 63          | 64          | 65          |
| Years of service                      |                                                                        | 21          | 22          | 23          | 24          | 25          |
|                                       | <b>Note</b>                                                            | <b>HK\$</b> | <b>HK\$</b> | <b>HK\$</b> | <b>HK\$</b> | <b>HK\$</b> |
| Total DBO                             | <b>a</b>                                                               | 231,855     | 231,855     | 231,855     | 231,855     | 231,855     |
| Benefit attributable to: current year | <b>b = a ÷ 25</b>                                                      | 9,274       | 9,274       | 9,274       | 9,274       | 9,274       |
| Opening balance of DBO                | <b>c<sub>t-1</sub></b>                                                 | 174,745     | 185,684     | 196,860     | 208,278     | 219,941     |
| Net interest cost                     | <b>d = c<sub>t-1</sub> × f<sub>t</sub></b>                             | 2,097       | 2,228       | 2,362       | 2,499       | 2,639       |
| Current service cost                  | <b>e = b ÷ g<sub>t</sub></b>                                           | 8,842       | 8,948       | 9,056       | 9,164       | 9,274       |
| Ending balance of DBO                 | <b>c<sub>t</sub> = c<sub>t-1</sub> + d<sub>t</sub> + e<sub>t</sub></b> | 185,684     | 196,860     | 208,278     | 219,941     | 231,855     |
| Discount rate                         | <b>f</b>                                                               | 1.2%        | 1.2%        | 1.2%        | 1.2%        | 1.2%        |
| Discount factor                       | <b>g = (1 + f)<sup>(5-t)</sup></b>                                     | 1.05        | 1.04        | 1.02        | 1.01        | 1           |

<sup>2</sup> Labour Department, Chapter 11: Severance Payment and Long Service Payment, <https://www.labour.gov.hk/eng/public/wcp/ConciseGuide/11.pdf>

Chart 1



**LSP: example of DBO valuation and relevant financial reporting components**

In this example, we focus on the scenario in which the LSP is payable as the employee retires. The fair value for the LSP obligation derived from this scenario usually accounts for the largest portion of the total fair value of the DBO. This is because the LSP is most likely to be payable to the employee as he/she retires.

We are assuming that a male employee is currently earning a monthly salary of HK\$12,000. He has worked in the firm for 20 years. His current age is 60 and the expected retirement age is 65. An actuarial estimate of the annual salary increment rate should be 3% per annum and the applicable discount rate should be 1.2%.

As a result, the reckonable years of service is 25 years (65 - 60 + 20). The projected salary and total DBO at retirement age are HK\$13,911 ( $HK\$12,000 \times (1 + 3.0\%^{(65-60)})$ ) and HK\$231,855 ( $HK\$13,911 \times 2/3 \times 25$ ), respectively. The opening balance of the DBO at the age of 61 is HK\$174,745. In order to calculate the opening balance, the DBO has to be calculated from the first year of service (ie age 40) until the age of 61.

Table 1 provides an illustration of how the DBO builds up over the next five years. For simplicity, we have assumed there is no change in actuarial assumption over the course of the following five years, and any additional adjustments to reflect the probability that the employee may leave the entity at an earlier or later date are excluded.

**Other valuation factors in assessing LSP**

1. Probability of the employee remaining alive up to retirement age;
2. Probability of the employee remaining employed up to retirement age; and
3. The amount of mandatory provident fund scheme benefit that will be used to offset the DBO.

Since we are focusing in the above example on the scenario in which the LSP is payable as the employee retires, the impact of the probabilities (the other valuation factors 1 and 2) on the final DBO at retirement age using the chart is set out in Chart 1.

The final DBO at retirement age should take into account the accumulative probabilities from the employee's current age to the retirement age.

**Accounting Treatment**

**1. Balance sheet statement (ie ending balance of DBO)**

According to HKAS 19, the present value of a DBO is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

At the age of 61, the ending balance of HK\$185,684 will be recorded as the present value of DBO in the balance sheet of that financial year.

**2. Income statement (ie current service cost and net interest cost)**

According to HKAS 19, the current service cost is the increase in the present value of a DBO resulting from employee service in the current period.

The interest cost is the increase in the present value of a DBO that arises because the benefits are one period closer to settlement.

At the age of 61, the current service cost of HK\$8,842 and net interest cost of HK\$2,097 will be recorded in the income statement of that financial year.

**3. Other comprehensive income (ie adjustment to experience and changes in financial assumption)**

According to HKAS 19, the actuarial gain and losses are comprised of two items: adjustment to experience and the effect of changes in actuarial assumption. The adjustment to experience refers to the effects of differences between the previous actuarial assumptions and what has actually occurred. The changes in actuarial assumption refer to the effect of changing the actuarial assumption such as the discount rate.

Since we have assumed there is no change in actuarial assumption and excluded any additional probability adjustment, there is no actuarial gain and loss in the other comprehensive income in our illustrative example.

**Overview**

The above example is intended to illustrate the key factors and issues that actuary/valuation professionals need to consider when conducting valuations of DBO arising from post-employment benefit schemes. A more complete LSP valuation should take into account the LSP payable upon the death of the employee and the LSP payable upon involuntary dismissal by the employer.

Our experience with DBO valuations tells us that scenarios for employees to receive benefit payments and factors to consider can vary greatly from one company to another, as this is dependent on the benefit schemes being offered by a company to its employees. DBO valuation in general requires high level of skills in model building and data analysis. Employee benefit schemes in different countries can vary substantially. This tends to further complicate the valuation of DBO.

Given the complexities of employee benefit valuations, companies should discuss with their consultants/actuaries how structures and terms of employee benefits affect their financial statements before making decisions regarding employee benefit policies.

**How can BDO help?**

BDO's Specialist Advisory Services team in Hong Kong offers a wide range of tailor-made transaction support solutions including financial due diligence, business valuations and M&A advisory. We have assisted hundreds of clients in this respect in their transactions in the past few years.

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# CLEMENT CHAN WAS AWARDED THE MEDAL OF HONOUR AND HIS RECENT APPOINTMENT



**B**DO in Hong Kong is pleased to advise you that our Managing Director of Assurance **Clement Chan** was awarded the Medal of Honour (MH) by the Chief Executive of the Hong Kong Special Administrative Region (HKSAR) Government on 1 July 2019 under the 2019 Honours List.

Clement is awarded MH in recognition of his dedicated public and community service, particularly his valuable contributions to the West Kowloon Cultural District Authority.

Please join us in congratulating Clement and wishing him every success in his public and community services endeavours.

In addition, Clement has been also appointed as Non-Executive Director (NED) of the Hong Kong Mortgage Corporation Limited (HKMC) by the Financial Secretary Mr Paul Chan.

The Hong Kong Mortgage Corporation is wholly owned by the HKSAR Government through the Exchange Fund. The HKMC strives to promote stability of the banking sector, wider home ownership, as well as development of the local debt market and retirement planning market.

## BDO SUPPORTS THE CHKLC DIRECTOR TRAINING SERIES FOR THE NINTH CONSECUTIVE YEAR

**R**unning from May to November, the programme launched by CHKLC comprises six sessions dealing with the important aspects to directorships for a listed company, ranging from corporate governance, risk management to the latest updates in various applicable rules and laws. The programme will also address common issues faced by directors.

BDO's Principals of Risk Advisory **Peter Pang** and **Vivian Chow**, and Senior Manager of Risk Advisory **Roger Lo** are invited to speak on some of the important aspects of directorship for a listed company.

The schedule and topics for the forthcoming sessions are shown below:

| Dates              | Topics                                                                     |
|--------------------|----------------------------------------------------------------------------|
| 17 September (Tue) | A New Dimension to Risk Management                                         |
| 29 October (Tue)   | Data Governance & Protection and Emerging Solution - Blockchain Technology |
| 7 November (Thu)   | Annual Regulatory Update 2019                                              |

If you are interested in attending the programme, please enroll with CHKLC directly. For more information, please visit their website at [www.chkcl.org](http://www.chkcl.org).





## DON'T UNDERPAY YOUR EMPLOYEES OR YOU MIGHT PAY EVEN MORE

**T**he continuing changes to the Hong Kong Employment Ordinance can make hiring and compensating employees increasingly complicated. Employers can be hard pressed to ensure their compliance with the updated employment laws of Hong Kong in respect of the local workforce. In particular, multinational organisations who have expanded their business into Hong Kong have found a lack of knowledge makes it difficult to comply with the local employment-related legislation.

Over the past few years, a number of labour disputes have touched upon various aspects concerning the incorrect calculations of wages, holiday pay and annual leave pay due to employees by employers. In one recent case, the chief executive of a restaurant chain voluntarily revealed that, since 2007, the company had underpaid holiday wages due to employees. It was believed that up to 3,000 employees had been affected to whom the chief executive had sent an apology letter and promised to settle the underpaid amounts within a specific timeline. The Labour Department expressed concern regarding this incident and stressed that employers must pay wages to employees

in an accurate, complete and timely manner by strictly adhering to the requirements stipulated in the Employment Ordinance.

It is not uncommon that labour disputes involve mistakes in the calculation of an employee's Daily Average Wages (DAW), which applies to the computation of the seven relevant statutory entitlements - holiday pay, annual leave pay, sickness allowance, maternity leave pay, paternity leave pay, end of year payment and payment in lieu of notice.

Employers should pay special attention to the provisions under the Employment (Amendment) Ordinance 2007 (the E(A)O 2007) relating to the calculation of the seven relevant statutory entitlements. The main objective of this amendment is to ensure that all types of remuneration defined as wages under the Employment Ordinance are included in the computation of the seven relevant statutory entitlements.

### Who is eligible for the seven relevant statutory entitlements?

In accordance with the Employment Ordinance,

as long as the employee is employed under a continuous contract under which he/she has been employed continuously by the same employer for four weeks or more, with at least 18 hours worked in each week and whether an employee's wages are paid monthly, daily or calculated by piece, job, hour or week, he/she is eligible for the seven statutory entitlements. The calculation of these entitlements shall be computed on the basis of his/her 12-month average wage.

### What is covered by the definition of 'wages' by the Employment Ordinance?

According to the Employment Ordinance, 'wages' refers to:

- all types of remuneration items that are payable to an employee in respect of work performed and work to be performed;
- allowances (inclusive of attendance or travelling or housing allowances) (see **Note 1** below);
- tips, earnings and service charges;
- commission and overtime pay (see **Note 1** below)

#### Note 1

Please note that overtime pay should also be included as wages for computing the relevant statutory entitlements if:

- it is of a constant character; or
- the monthly average amount over the past 12 months is not less than 20% of the average monthly wages of the employee during that same period

and:

- commission, good attendance bonus and travelling allowance are required to be included in the calculation of the end of year payment, maternity leave pay, paternity leave pay, severance payment, long service payment, sickness allowance, holiday pay, annual leave pay and payment in lieu of notice. However, the end of year payment can be the amount as specified in the employment contract. If the amount is not specified, it will be a sum equivalent to one month's average wages.

Yet, it *does not include* the following:

- employer's contribution to any retirement scheme;
- the value of any accommodation, education, food, fuel, water, light or medical care provided by the employer;
- non-recurrent travelling allowances or the value of any travelling concession or travelling allowance for actual expenses incurred by the employment;
- a gratuity payable on completion or termination of a contract of employment;
- any sum payable to the employee to defray special expenses incurred by him/her by the nature of his/her employment;
- commission, attendance allowances or attendance bonus which is of a gratuitous nature or is payable only at the discretion of the employer;
- end of year payment or annual bonus which is of a gratuitous nature or is payable only at the discretion of the employer.

#### How to define the 12-month period?

The relevant statutory entitlements shall be computed based on the average daily (or monthly) wages earned by an employee in the past 12-calendar month period preceding the specified dates\*. If an employee is employed by the company for less than 12 months, the calculation shall be based on the shorter period.

#### What wages and periods are to be disregarded for the computation of daily average wages (DAW)?

One of the points usually overlooked in the calculation of DAW is that, in computing the employee's average daily wages, in any periods when employees are not paid a full salary or are paid no salary at all, both the amount of salary and the number of days of that period shall not be included in computing the employee's 12-month average daily (or monthly) wages, which is explained in more detail below:

- (a) Rest days, statutory holiday, annual leave, maternity leave, paternity leave or sickness days taken by an employee with no pay or not paid in full by the employer. This also includes sick leave due to work injuries as provided for under the Employees' Compensation Ordinance; or leave taken with the agreement of the employer.
- (b) An employee who is not provided with work by the employer on any normal working day. Please note that an employer does not have to exclude an employee's full-paid leave (regardless of whether it is a statutory holiday, annual leave, maternity leave, paternity leave or any other leave taken with the agreement of the employer) and the amount received for such leave in computing average wages.

Please refer to the examples below.

### Example 1

#### Holiday pay

Employee A, having been employed under a continuous contract for not less than three months immediately preceding a statutory holiday, is entitled to holiday pay. Holiday pay should be paid to Employee A no later than the day on which he is next paid his wages following that statutory holiday.

#### Computing holiday pay for 1 July 2019

- Remuneration: basic salary of HK\$20,000 per month with paid rest days
- Total amount of commission earned for Employee A for the past 12-month period from 1 July 2018 to 30 June 2019: HK\$200,000
- 12-month wages earned by the employee for the period from 1 July 2018 to 30 June 2019: HK\$438,000 (this amount has already excluded three days unpaid pay sick leave and only includes leave where full wages were payable)
- Three days unpaid sick leave at HK\$666.67 per day  
(ie HK\$2,000 = HK\$666.67 x 3 days)

#### Periods and wages to be disregarded

Rest days, statutory holidays and annual leave have all been taken by Employee A in the past 12-month period with full pay, except for three days of unpaid sick leave. As such, three days and the respective amount received by Employee A have to be excluded.

#### Wages to be excluded

Since no payment was made for the three sick days, no amount has to be excluded but the three days have to be excluded.

#### Period to be excluded

365 days - 3 days = 362 days

Holiday pay computation according to the average daily wage of the past 12-month period.

#### Average daily wage

Total wages in the 12-month period minus three days of unpaid sick leave/(365 days - 3 days)

Total wages in 12-month period - three-day unpaid sick leave = (HK\$240,000 + HK\$200,000) - HK\$2,000 = HK\$438,000

Average daily wage = HK\$438,000/362 days = HK\$1,209.94 per day

#### Holiday pay for 1 July 2019 is calculated as HK\$1,209.94

An error is possible in the calculation of holiday pay by using only the monthly basic salary/31 days = HK\$20,000/31 days = HK\$645.16 per day.

Therefore the amount underpaid to Employee A would be: **HK\$564.78** (ie HK\$1,209.94 - HK\$645.16).

\* The specified dates of the relevant statutory entitlements are the day of the statutory holiday/annual leave/sickness day/maternity leave/paternity leave. If there is more than one day of such leave entitlement, the first day of such leave entitlement would be regarded as the specified date.

For the end of year payment, the specified date is the due day of the payment.

For payment in lieu of notice, the specified date is the day when a notice of termination of contract is given.

## Example 2

### Annual leave pay

Annual leave pay should be paid to Employee B no later than the normal pay day after the period of annual leave was taken.

### Calculating three days of annual leave pay (annual leave to be taken from 25 to 27 March 2019)

- Remuneration: Basic salary of HK\$30,000 per month with paid rest days
- Total amount of commission earned for Employee B for the past 12-month period from 1 March 2018 to 28 February 2019: HK\$300,000.
- 12-month wages earned before the first day of annual leave from 25 March 2019: HK\$657,000 (This amount already includes the total amount of commission but excludes five days of special concession leave pay for which the employee received pay at HK\$600 per day and only includes fully paid leave)
- Five days special concession leave commencing 10 September 2018 with special concession leave pay at HK\$600 per day (ie HK\$3,000 = HK\$600 x 5 days).

### Periods and wages to be disregarded

The three days annual leave pay shall be calculated on the basis of Employee B's average daily wage in the past 12 months (ie from 1 March 2018 to 28 February 2019).

Rest days, statutory holidays and annual leave have all been taken by Employee B in the past 12-month period with full pay, except for five days of special concession leave and the respective amount received has to be excluded in computing the average daily wage.

### Wages to be excluded

The five days of special concession leave pay from the total wages earned in the preceding 12-month period.

### Periods to be excluded

The period of five days of special concession leave from the preceding 12-month period (ie 365 days - 5 days).

### Average daily wage

Total wages in the 12-month period minus five days special concession leave pay / (365 days - 5 days)

Total wages in 12-month period - five days special concession leave pay = (HK\$360,000 + HK\$300,000) - HK\$3,000 = HK\$657,000

Average daily wage = HK\$657,000 / 360 days = HK\$1,825 per day

### Annual leave pay of three days = HK\$1,825 x 3 days = HK\$5,475

An error is possible in the calculation of annual leave pay by using only the monthly basic salary / 31 days = HK\$30,000 / 31 days = HK\$967.74 per day.

Therefore the amount underpaid to Employee B would be: HK\$857.26 (ie HK\$1,825 - HK\$967.74) x 3 days = **HK\$2,571.78**.

The above two examples show only the details of the computation of holiday pay and annual leave pay as per the requirements of the Employment Ordinance. If you require additional information regarding the requirements for the calculation of other statutory entitlements, please speak to our payroll professionals for specific advice.

It is imperative that employers strictly adhere to the Employment Ordinance requirements for the computation of DAW applicable for

the calculation of the seven relevant statutory entitlements for their employees. This will avoid any possible labour disputes, penalties or prosecution. Please rest assured that full compliance with the law offers the best protection of the rights of both employers and employees for the duration of employment.

### Speak to our payroll professionals

Feel free to get in touch to find out how we can help you with a tailored payroll outsourcing solution.

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## STRICTER REQUIREMENTS ON GREEN FUNDS

There is a growing global trend for asset managers to consider climate change, sustainability and environmental, social and governance (ESG) factors in the investment process, and to offer green or ESG-related investment products. As the development of green and ESG-related investment products is gaining traction, authorities around the globe are adopting initiatives that require the enhanced disclosure of the sustainable features of those products. The aim is to enable investors to understand and assess whether green and ESG-related products will meet their investment needs.

In Hong Kong, several funds authorised by the Securities and Futures Commission (SFC) have a climate, green, environmental or sustainable development focus. An initial review by the SFC has revealed that the quality of the disclosure varies widely among these funds and that the majority do not specifically disclose how the management companies are incorporating their stated green or ESG factors into their investment selection process.

To narrow the disclosure gap among SFC-authorized green and ESG funds and for better comparison of disclosures among similar types of funds, the SFC has issued a circular: **Circular to management companies of SFC-**

**authorized unit trusts and mutual funds - Green or ESG funds.** The circular, issued on 11 April 2019, focuses on enhancing the quality of disclosure in SFC-authorized green and ESG funds. It is the first step towards developing green guidelines that will support the growth of the green finance market in Hong Kong and enhance the credibility and transparency of the market.

### Who needs to comply?

SFC-authorized funds must fulfil the following obligations in the circular if they integrate one or more of the globally recognised criteria and principles for green or ESG funds (see **Chart 1**) as their key investment focus, and reflect that in their name and their investment objective or strategy.

### Name of the scheme

In line with the existing requirements set out in the Code on Unit Trusts and Mutual Funds (the UT Code), a green or ESG fund should invest primarily in investments that reflect the particular green or ESG investment focus of the fund.

### Requirements for disclosure

The SFC expects the offering documents (including the product key fact statements) of SFC-authorized green or ESG funds to disclose,

as a minimum, the following details so that investors can make an informed investment analysis and judgement:

1. The key investment focus and targeted objective of the green or ESG fund, and how that focus is considered to be green or ESG-related.
2. The investment strategies adopted by the green or ESG fund, including but not limited to:
  - a) The relevant green or ESG criteria and principles considered;
  - b) The expected exposure to securities or other investments that reflect the stated green or ESG investment focus;
  - c) The investment selection process and criteria adopted by the green or ESG fund (eg the assessment criteria of the underlying investments, the ESG analysis and evaluation methodology, and the characteristics and general composition of the benchmark).
3. The exclusion policy adopted by the green or ESG fund, and types of exclusion.
4. The risks associated with the green or ESG fund's investment theme.
5. Other information that the management company considers necessary.



Chart 1

### Globally recognised criteria and principles for green or ESG funds

- United Nations Global Compact Principles
- United Nations Sustainable Development Goals
- Common Principles for Climate Mitigation Finance Tracking
- Green Bond Principles of the International Capital Market Association
- Climate Bonds Taxonomy of the Climate Bonds Initiative

This list is not intended to be exhaustive. Other global and national green and ESG criteria and principles, reference benchmarks and indices may be considered on a case by case basis.

#### Ongoing monitoring

The company that is managing the green or ESG fund must monitor and assess the underlying investments on a regular basis, in order to make sure the fund continues to meet its stated investment objective and the requirements set out in the circular.

#### Action required

##### 1. Initial confirmation of compliance

For funds that need to meet the requirements of the circular (both existing SFC-authorized funds and new funds seeking SFC authorisation), the management company should:

- give the SFC either a self-confirmation of compliance or a confirmation supported by an independent third party certification or fund label; and
- demonstrate that the fund's primary investments focus, investment selection and ongoing monitoring process adheres to globally recognised criteria or principles for green or ESG funds.

##### 2. For existing SFC-authorized funds

- The management company must review the fund's existing offering documents in the light of the disclosure requirements set out in the circular and make any necessary updates and revisions by 31 December 2019.
- If the offering documents require updates or revisions, the management company should assess whether prior approval from the SFC is needed under section 11.1 of the UT Code and the relevant post-authorisation application requirements.

##### 3. For new funds seeking SFC authorisation

- The management company should meet the requirements set out in the circular in addition to the provisions that apply in the SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products (including the UT Code) and the circulars, guidelines and any other requirements that are issued by the SFC.
- Any requisition by the SFC will be part of the SFC's process for authorising new fund applications. Newly authorised green and ESG funds will be posted on the SFC's dedicated green and ESG fund webpage, which will be launched by the end of 2019.

#### How can BDO help?

BDO's Risk Advisory Services team in Hong Kong provides a wide range of professional services including ESG reporting and sustainability advisory, internal audit, corporate governance, IT, cybersecurity & e-Payment risk advisory, cyber health check services, and anti-money laundering and counter-terrorist financing advisory. If you have any questions on ESG or green funds as well as that related to the above services, please feel free to contact us for further discussion.

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# GLOBAL RISK LANDSCAPE 2019 REPORT

**B**DO Global Risk Landscape 2019 Report has been published to announce the survey results of over 500 C-suite executives and senior risk experts globally regarding their views towards the main global business risks in this year.

The survey results identified significant risk changes that social media and the 24-hours news cycle are putting business at risk as 'hype' and distracting organisations from real potential threats. These new business risks pose the greatest perceived risk to businesses, which have overtaken issues such as regulatory risk, cyberattacks and economic slowdown and slow recovery, for its high level of difficulty in prediction and preparation.

As identifying risk and coming up with a measured response from hype in an increasing complexity world is not an easy task, the report explores how organisations can create the right balance between mitigating short-term risks based on media hype and long standing risks which may affect their business operations.

As part of the Global Risk Landscape 2019 Report, our BDO Global Risk Advisory Teams have prepared three regional risk white papers that explore the differing business risks and attitudes to risk for the Americas, Asia-Pacific and EMEA.

If you would like to obtain a copy of Global Risk Landscape 2019 as well as the Asia-Pacific regional white paper, please visit <https://www.bdo.com.hk/en-gb/insights/publications/global-risk-landscape-2019>.





## TODAY'S HR CHALLENGES

**W**ith today's ever-changing economic landscape, technological advancements and demographic shifts, HR professionals in Hong Kong, as well as across the world, are facing a number of critical and unique challenges.

As talent acquisition and retention becomes an increasingly daunting task, HR practitioners are not only required to dig deep into their current pool of resources and expertise, but also to familiarise themselves with the current market environment and stay up-to-date with all the key market trends.

In this article, we are pleased to share with you our observations on some of the major challenges that HR is facing in Hong Kong today.

### 1. A fast-changing environment fostered by the continued evolution of digitalisation, data science and artificial intelligence (AI)

One of the major evolutions faced by HR practitioners is the advancement of technology. This means that the entire recruitment, retention and ongoing administrative processes, ranging from hiring, documenting and filing to analysing and even predicting employee performance and HR trends, can be performed

more efficiently. Moreover, many businesses have also started looking into, or have already implemented automation and digitalisation, making improvements to their internal processes.

Nowadays, a company with cutting-edge information technology is perceived as having visionary strategy. HR needs to work closely with management to identify and strategise on how it should adopt and use technology in the company's day-to-day business, and its plans for transforming the workplace. HR professionals will need to consider how technological advancements will require them to build or reskill the existing workforce, and help the company hire competent individuals to handle these tasks and make the best use of such technology.

### 2. Dealing with a multi-generational workforce

Never before has there been such a vast difference in job expectations among the various generations, namely baby boomers, Generation Xers and millennials.

Compared to the earlier generations, millennials in Hong Kong have grown up in rather a protective environment and have a different

set of values, whereby they regard building a long-term career or gaining a professional qualification as of less importance, and tend to change jobs frequently. They focus on flexibility, exposures and work-life balance instead of looking for monetary fulfilment. They value being involved in diverse tasks and projects that engage and excite them.

When it comes to managing employees with a range of different expectations and values, efforts need to be made to understand what motivates the different generational groups, and how each generation's strengths can complement those of the others, thereby allowing employers to tap into their best traits accordingly. HR practitioners should be prepared to put together a solution that addresses these cross-generational differences, or even conflicts that may occur when they work together.

### 3. Talent war

The current talent war has found HR scrambling for the best available talent given the fact that Hong Kong's labour market is now more a jobseeker's market. In order to source and hire the best talent and the best qualified candidates, HR professionals are now looking outwards to other countries in the APAC region,



or even globally. Nevertheless, we all have to admit that finding a 'perfect' candidate can be very time-consuming, putting a great deal of strain on HR professionals, and hindering them from performing more strategic tasks that could be more beneficial from a business perspective. It is necessary for HR to consider adopting a more versatile and cost-effective resourcing strategy, which provides flexibility and builds resilience in businesses.

#### 4. Global mobility

With candidates' desire for and the increasing ease of relocation, HR professionals no longer solely look for talent in local markets, but now broaden their searches regionally, or even globally. Apart from building up their resources and capabilities to source qualified international candidates, HR teams have also started to become more aware of the importance of potential compliance issues, such as visas and tax, in today's highly regulated world.

#### 5. The rising trend of the Gig Economy

With millennials set to make up 35% of the global workforce by 2020<sup>1</sup>, this generation is expected to make a positive and progressive impact on businesses. One such impact is the continued rise of the 'Gig Economy'.

The 'Gig Economy' is popularly defined as 'a labour market characterised by the prevalence of short-term contracts or freelance work, as opposed to permanent jobs'<sup>2</sup>.

Instead of job stability, millennials are seeking diversified experiences and a sense of fulfilment that comes from their work making a difference to themselves and the community. At the same time, permanent roles in a company have become less 'permanent'. Companies nowadays have a greater demand for specialists and niche skills on a project basis rather than generic professional roles.

According to a 2018 report by a global workforce solutions provider, Hong Kong is seen to be most actively embracing the free agent trend, with 55% of respondents agreeing that most people are looking for a flexible-contract based role rather than a traditional permanent full-time role<sup>3</sup>. Another growing trend is for multinational companies to significantly increase their hiring of contract workers to complement and bridge the gap in the skills of their existing workforce. A recent survey also revealed that 54% of employers in Hong Kong indicated that they have hired contingent staff in the past year<sup>4</sup>.

#### Conclusion: Hybrid resourcing model - an agile hiring and resourcing approach

In the face of all these challenges, rather than just relying on the traditional 'direct hire' that provides a stable workforce but is less flexible in keeping up with and managing ever-changing corporate strategies and projects, HR practitioners should start to consider adopting a **'hybrid resourcing' model** to meet their company's resourcing needs. Satisfying imminent resourcing needs, in particular, ignores other possible solutions such as mobilising internal resources, enabling the existing workforce to develop the required skills, etc, and thus can be a frustrating task for HR with limited time at its disposal. It is an undeniable fact that imminent resourcing needs are no longer rare events but take up a growing portion of the resourcing needs pie.

The 'hybrid resourcing' model is a blend of the various resourcing and recruitment strategies, such as interim management, staff augmentation and project support, in combination with direct hiring. We are glad to see that many HR professionals have started to become increasingly receptive to this resourcing model, which can give them sufficient flexibility when dealing with today's agile and ad-hoc resourcing needs.

#### How can BDO help?

BDO's Professional Resources Solutions and Business Services Outsourcing teams in Hong Kong offer a comprehensive range of HR-related professional services, from an initial current state assessment, to the provision of a tailor-made solution to lessen or close those gaps through the offering of blended business solutions. These may include outsourcing, process re-engineering, automation, digitalisation, and professional secondment (candidate/project placements), or a combination of these. We are confident that we are able to assist our clients in different stages of their business and transformation cycles. Please contact our Professional Resources Solutions team to find out more.

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<sup>1</sup> 'The millennial moment — in charts': an article published in 2018 by Financial Times.

<sup>2</sup> 'What is the "gig" economy?': an article published in 2017 by BBC News.

<sup>3</sup> 'Gig Economy: How Free Agents are Redefining Work': a survey published in 2018 by PERSOLKELLY, the regional headquarters of Kelly Services HK.

<sup>4</sup> 2016 Hays Asia Salary Guide.

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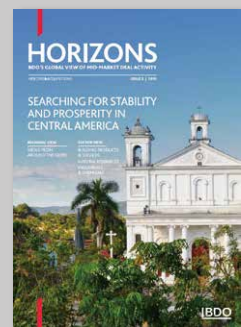


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