DECEMBER 2018 AND JUNE 2019 SUPPLEMENT

Qualification Programme

Module A
Financial Reporting

Hong Kong Institute of
Certified Public Accountants
香港會計師公會

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Introduction

This Supplement is to be used in conjunction with the sixth edition of the Learning Pack, and it will bring you fully up to date for developments that have occurred in the period since publication of the Learning Pack and 31 May 2018, the cut-off date for examinable standards and legislation for the December 2018 and June 2019 examinations. You will find a list of the standards that are examinable in your examination session by logging onto the HKICPA online QP Learning Centre.

The Supplement comprises a technical update on developments that will be examinable in December 2018 and June 2019 examination session that are not currently covered in the Learning Pack. The topics covered are listed on the contents page, and again are covered in chapter order.

In each case the text in the Supplement explains how the Learning Pack is affected by the change, for example whether the new material should be read in addition to the current material in the Learning Pack, or whether the new material should be regarded as a replacement.

Good luck with your studies!

Errata – Learning Pack

Chapter 6	Investment property
Answer to self-test question Answer 1 (a) 1 **Page 159**	**The final bullet point is amended to read:** • Therefore Tennant House is outside the scope of HKAS 40.

Chapter 9	Leases
Answers to self-test questions Answer 5 **Page 255**	**The workings under the lease liability amortisation table are amended as follows:**

The right-of-use asset is initially measured at:

	$
Lease liability	216,473
Initial deposit	30,000
Estimated dismantling costs ($20,000 × 1/1.05^5)	15,671
	262,144

It is subsequently depreciated over the lease term resulting in an annual depreciation charge of $52,429 ($262,144/5).

Extracts from the financial statements

Statement of financial position at 30 June 20X8

	$
Right-of-use asset (262,144 – 52,429)	209,715
Non-current liabilities	
Lease liability	136,162
Current liabilities	
Lease liability (50,000 – 8,865)	41,135

Statement of profit or loss for the year ended 30 June 20X8

	$
Depreciation expense	52,429
Finance cost	10,824

Chapter 29	Changes in group structures
Section 2.2 **Page 875**	**The second sentence is amended to read:** Any gain or loss arising from the remeasurement will be recognised in profit or loss or other comprehensive income, as appropriate.
Section 2.2 Example **Page 876**	**The first sentence of the solution is amended to read:** In 20X8, a gain of $500 arises on remeasurement of the 15% equity interest to fair value. As the investment was classified as a financial asset at fair value through other comprehensive income, this is recognised in other comprehensive income.

Technical Update – Learning Pack

Chapter 1	Legal environment
Section 3.6 **Page 20**	**The following bullet points are added at the start of the list of bullet points within this section:** • S.369 – a company prepares financial statements to its accounting reference date. For a new company, the primary accounting reference date must be on or before the last day of the month of the anniversary of the company's incorporation. • S.370 – subsequently the accounting reference date is the anniversary of the primary accounting reference date. • S.371 – the accounting reference date may be changed for the current year and subsequent years or for the previous year and subsequent years. This change will result in an accounting reference period that is either shorter or longer than 12 months. A longer period may not be more than 18 months.

Chapter 2	Financial reporting framework

Section 8
Page 49
	The text prior to section 8.1 is replaced with the following:
	In June 1997 the HKICPA produced a document, *Framework for the Preparation and Presentation of Financial Statements* (the *Framework*). This is, in effect the **conceptual framework** upon which all HKFRS are based and hence it determines how financial statements are prepared and the information they contain.
	Amendments to the *Framework* were issued in October 2010 and, as a result, the updated document, renamed the *Conceptual Framework for Financial Reporting*, contains some new (2010) chapters and some old (1997) chapters.
	The chapters, which follow on after a preface and introduction, are:
	• The objective of general purpose financial reporting (issued 2010)
	• Qualitative characteristics of useful financial information (issued 2010)
	• The Framework (1997): The Remaining Text
	  – Underlying assumption
	  – The elements of financial statements
	  – Recognition of elements of financial statements
	  – Measurement of the elements of financial statements
	  – Concepts of capital and capital maintenance
	Much of the content of the chapters is also included in HKAS 1 (Revised), and covered in sections 10 to 12 of this chapter. As you read through them, think about the impact the *Conceptual Framework* has had on HKFRS, particularly the definitions.

Section 13	**Section 13 is replaced with the following:**
Page 61	**The 2018 *Conceptual Framework***

The IASB issued a revised *Conceptual Framework* in March 2018; this will, in due course, be adopted by the HKICPA. The revised document improves on the 2010 *Conceptual Framework* by:

- 'Filling the gaps' by providing guidance on presentation and disclosure;
- Updating the content; and
- Clarifying certain areas.

The chapters of the new *Conceptual Framework* are:

(1) The objective of general purpose financial reporting
(2) Qualitative characteristics of useful financial information
(3) Financial statements and the reporting entity
(4) The elements of financial statements
(5) Recognition and derecognition
(6) Measurement
(7) Presentation and disclosure
(8) Concepts of capital and capital maintenance

The following sections consider some of the changes in the new *Conceptual Framework.*

13.1 The objective of general purpose financial reporting

The general objective of general purpose financial reporting of the 2010 *Conceptual Framework* is retained, however there is a greater emphasis on providing information that allows users to assess the stewardship of management i.e. how effectively and efficiently management has used the reporting entity's resources.

13.2 Qualitative characteristics of useful financial information

The two fundamental and four enhancing characteristics of the 2010 *Conceptual Framework* are retained, however there is additional emphasis in the following areas:

- In order to faithfully represent financial information, economic substance must be reflected rather than legal form.

- Neutrality (an element of faithful representation) is supported by the exercise of prudence i.e. the exercise of caution when making judgments under conditions of uncertainty. Prudence does not allow for the understatement or overstatement of items in the financial statements. Prudence as a concept was referred to in the original *Framework* but was not included in the 2010 *Conceptual Framework.*

- Measurement uncertainty affects whether information is useful; it does not prevent information from being useful, however in some cases the most relevant information has such a high level of measurement uncertainty that the most useful information is less relevant but subject to lower measurement uncertainty.

The guidance in the remaining chapters of the *Conceptual Framework* is heavily related to the characteristics of relevance and faithful representation.

13.3 Financial statements and the reporting entity

Neither the original *Framework* nor the 2010 *Conceptual Framework* included guidance on the reporting entity. The new *Conceptual Framework* clarifies that a reporting entity is an entity that is required to, or chooses to, prepare financial statements. It can be a single entity or a proportion of an entity or it can comprise more than one entity (i.e. a group). A reporting entity is not necessarily a legal entity.

13.4 The elements of financial statements

The definitions of asset and liability have been refined and the definitions of income and expenses updated to reflect this.

The definition of an asset is refined to:

- Clarify that an asset is the economic resource related to economic benefits rather than the actual inflow of benefits.
- Remove the requirement for an inflow of economic benefits to be 'expected'; the new definition makes it clear that there is no requirement for economic benefits to be certain or even likely.
- Clarify that a low probability of economic benefits may affect recognition decisions and the measurement of an asset.

The definition of a liability is refined to:

- Clarify that a liability is the obligation to transfer economic resource rather than the actual outflow of economic benefits.
- Remove the requirement for an outflow of economic benefits to be 'expected'.
- Identify that an obligation is a duty or responsibility that an entity has 'no practical ability to avoid'.

13.5 Recognition and derecognition

The 2018 *Conceptual Framework* requires that an item is recognised in the financial statements if recognition would result in both relevant information and a faithful representation. There is no longer a recognition criterion that an in- or outflow of economic benefits should be probable.

New derecognition guidance is also introduced:

- An asset is derecognised when the entity loses control of all or part of the asset.
- A liability is derecognised when the entity no longer has a present obligation for all or part of the recognised liability.

13.6 Measurement

Two main measurement bases are referenced in the *Conceptual Framework*:

- Historical cost; and
- Current value (which includes fair value, value in use, fulfilment value and current cost).

Guidance on choosing a measurement basis is provided, with an emphasis on providing relevant information that faithfully represents an item. Faithful representation is affected by measurement inconsistency and measurement uncertainty.

13.7 Presentation and disclosure

Guidance on presentation and disclosure is new to the 2018 version of the *Conceptual Framework.*

There is particular consideration of presenting income and expenses within profit or loss or other comprehensive income:

- In principle all income and expenses are included within profit or loss;
- In exceptional circumstances the IASB may include income or expenses arising from a change in value of an asset or liability as OCI if this results in more relevant information or a more faithful representation;
- In principle items of OCI are recycled to profit or loss in a future period when this results in more relevant information or a more faithful representation.

13.8 Concepts of capital and capital maintenance

This chapter comprises material carried forward from the 2010 *Conceptual Framework* with minor changes for consistency of terminology.

Section 15

Page 66

The following is inserted as new section 15; subsequent sections are renumbered:

15 Materiality

The IASB issued Practice Statement 2: *Making Materiality Judgements* in September 2017. This is a tool to aid management in using judgment to decide what information is material and what is not; it is a non-mandatory document and does not have the status of an IFRS (HKFRS); it may be applied with immediate effect.

15.1 General characteristics of materiality

The Statement refers to the definition of materiality contained within the 2010 *Conceptual Framework:*

'Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.'

(*Conceptual Framework for Financial Reporting*: para. QC11)

Materiality is pervasive to the preparation of financial statements and affects recognition, measurement, presentation and disclosure.

When considering whether information is material, a company should consider its own circumstances and the needs of primary users of its financial statements, i.e. investors, lenders and other creditors.

15.2 Interaction with local laws and regulations

The Practice Statement clarifies that:

- A company's financial statements must comply with requirements of IFRS (HKFRS), including those relating to materiality.
- Providing additional information to meet local legal or regulatory requirements is allowed by IFRS (HKFRS), even if that information is not material, provided that it does not obscure material information.

15.3 Making materiality judgments

The practice statement includes a four-step process that entities may find useful in making materiality judgments:

Step 1

Identify information that has the potential to be material. This step requires consideration of IFRS (HKFRS) requirements and the common information needs of primary users.

Step 2

Assess whether the information identified is material. Both quantitative and qualitative factors should be considered.

Step 3

Organise the information within the draft financial statements so that it supports clear and concise communication.

Step 4

Review the information provided as a whole, considering whether it is material individually and in combination with other information. At this stage information may need to be added or removed.

15.4 Specific topics

Specific guidance is provided on how to make materiality judgments on prior period information, errors, covenants and in interim reporting.

Prior period information

An assessment of whether prior period information is material to current period financial statements may result in a company providing either more or less prior period information than was provided in the prior year financial statements, depending on what level of information is necessary to understand current period financial statements.

Errors

In order to assess whether an error is material, the Practice Statement clarifies that the materiality process described in section 15.3 should be applied.

Covenants

When considering the materiality of information related to covenants, a company should consider:

- The consequences of a breach in covenant; and
- The likelihood of such a breach occurring.

Interim reporting

When preparing interim financial statements, a company should consider the same materiality factors that it considers when preparing its annual financial statements, however it should also take into consideration that the purpose of an interim report differs from the purpose of an annual financial report.

Section 15.1 **Page 67**	**A new section 15.1.3 is added:** **15.1.3 Current developments** The IASB has added a project to its work plan to update the *Management Commentary* practice statement. The update process will consider; • Developments from other narrative reporting initiatives; and • Acknowledged gaps in narrative reporting practice, such as reporting forward-looking information.
Section 17 **Page 71**	**The following replaces the final sentence of the introductory section:** The following project is general and does not relate to specific standards.
Section 17.1 **Page 71**	**This section is deleted.**
Section 17.2 **Page 72**	**The final paragraph is amended to be:** A PIR of IFRS 13 (HKFRS 13) was initiated during 2017. To date no feedback statement has been issued, however the IASB has concluded that no follow-up activities are required as a result of the findings of the PIR. PIRs are also planned for IFRS 10–12 (HKFRS 10–12) (financial standards relating to consolidation) and IFRS 5 (HKFRS 5) *Non-current Assets Held for Sale and Discontinued Operations* in due course.

Chapter 5	**Property, plant and equipment**
Section 1.4 **Page 125**	**A new section 1.4.4 is added:** **1.4.4 Current developments** In 2017 the IASB issued an exposure draft proposing to amend guidance contained within IAS 16 (HKAS 16) relating to elements of the cost of an asset. It is proposed that the standard is amended to require that proceeds from the sale of items produced while bringing an asset to the location and condition necessary for it to be capable of operating as intended by management, together with the costs of producing the items, are recognised in profit or loss.

Chapter 12	**Share-based payment**
Example at the end of section 3.1.1 **Page 318**	**The example is replaced with the following:** **Example: Group equity-settled share-based transaction** On 1 January 20X1, Principal Co. implemented a share incentive scheme for the five members of senior management at its subsidiary Sublime Co. Principal granted ten share options to each senior manager on this date, each with a fair value of $80. The fair value of each option at 31 December 20X1 is $70 and at 31 December 20X2 is $90. All five senior managers are expected to remain in employment until the settlement date. *Required* What entries are required to record this transaction in the financial statements of Principal, Sublime and the Group?

Solution

Principal

Principal is the entity responsible for settling the transaction. As the transaction will be settled in Principal's own equity instruments it must be recognised as an equity-settled share-based payment transaction.

On initial recognition of the liability, a debit is made to the cost of investment in Sublime. The amount is measured in the same way as we have seen for an equity-settled payment previously i.e. at the fair value of the award at the grant date.

			$	$
20X1	DEBIT	Cost of investment in Sublime (5 × 10 options × $80)/2 years	2,000	
	CREDIT	Equity – share-based payment reserve		2,000

To record the share-based payment after one year's service based.

			$	$
20X2	DEBIT	Cost of investment in Sublime (5 × 10 options × $80) – 2,000	2,000	
	CREDIT	Equity – share-based payment reserve		2,000

To record the share-based payment after the second year's service.

Sublime

Sublime is the entity receiving the services of the five senior managers. It has no obligation to settle the transaction itself and therefore it must be recognised as an equity-settled share-based payment transaction:

			$	$
20X1	DEBIT	Remuneration expense (5 × 10 SARs × $80)/2 years	2,000	
	CREDIT	Equity – share-based payment reserve		2,000

To record the first year's service expense and corresponding increase in equity.

			$	$
20X2	DEBIT	Remuneration expense (5 × 10 SARs × $80)/2 years	2,000	
	CREDIT	Equity – share-based payment reserve		2,000

To record the second year's service expense and corresponding increase in equity.

Group

In the consolidated accounts the transaction is accounted for as equity-settled:

In 20X1 it records:

(i) A remuneration expense of $2,000
(ii) A share-based payment reserve of $2,000

This is achieved by posting the following consolidation journal:

			$	$
20X1	DEBIT	Equity – share-based payment reserve	2,000	
	CREDIT	Cost of investment in Sublime		2,000

To eliminate the cost of investment in Sublime against equity in that company.

In 20X2 The Principal Group again records:

(i) A remuneration expense of $2,000
(ii) An increase in the share-based payment reserve of $2,000 to $4,000

This is achieved by posting the following consolidation journal:

			$	$
20X1	DEBIT	Equity – share-based payment reserve (2,000 + 2,000)	4,000	
	CREDIT	Cost of investment in Sublime (2,000 + 2,000)		4,000

To eliminate the cost of investment in Sublime against equity in that company.

Chapter 14 Income taxes

Section 6.1 **This section should be retitled and the text replaced with the following:**

Page 411 **6.1 Income tax consequences of dividends**

HKAS 12.57A

An entity should recognise the income tax consequences of dividends when it recognises a liability to pay a dividend. As a dividend is a distribution of profits resulting from past transactions and events, the related tax effect should be recognised in the same manner as the underlying transaction or event, in profit or loss, other comprehensive income or equity.

Section 11.3 **The section is replaced with the following:**

Page 428 **HK(IFRIC) Int-23 *Uncertainty over Income Tax Treatments***

The Interpretation provides guidance on accounting for current and deferred tax liabilities and assets where there is uncertainty as to the application of tax law to a transaction or circumstance.

In this situation:

- If it is probable that tax authorities will accept an uncertain tax treatment, tax amounts are determined based on that treatment.
- If it is not probable that tax authorities will accept an uncertain tax treatment, the effect of uncertainties must be reflected in the determination of tax amounts. Tax uncertainties should be reflected using one of two approaches:
  - The most likely amount (the single most likely amount in a range of possible outcomes); or
  - The expected value (the sum of probability weighted amounts in a range of possible amounts).

If uncertain treatment affects both current and deferred tax amounts, consistent judgments and estimates should be applied.

Chapter 15	Employee benefits
Section 5.7.1 **Page 459** HKAS 19.99,101A	**The fourth sentence is amended to be:** In either case the past service cost is the resulting change in the present value of the defined benefit plan. The past service cost may be positive where new benefits are introduced or negative where existing benefits are withdrawn. The amount is advised by an actuary who must calculate the amount by measuring the defined benefit plan liability (or asset) using updated assumptions, but ignoring the effect of the asset ceiling if the plan is in surplus (see section 5.8).
Section 5.7.2 **Page 459**	**Point (a) is amended to be:** (a) The **present value of the defined benefit obligation** being settled, as valued on the date of the settlement, using updated assumptions; and
Section 5.7 **Page 459** HKAS 19.122A, 123A	**A new section 5.7.3 is added before Self-test question 2** **5.7.3 Current service cost and net interest after curtailment, amendment or settlement** When a defined benefit plan has been amended, curtailed or settled, updated assumptions from the remeasurement of the plan are used to determine current service cost and interest for the remainder of the reporting period after the change to the plan. Therefore, after the amendment, net interest is calculated by multiplying the net defined benefit liability (or asset) as remeasured with the discount rate used in the remeasurement.
Section 5.12 **Page 465**	**This section should be deleted.**

Chapter 16	Borrowing costs
Section 1.2.1 **Page 476**	**The following is added immediately after self-test question 1:** If specific borrowings remain outstanding after the qualifying asset to which they relate is ready for use or sale, the borrowings are transferred to be part of general funds for the purposes of calculating a capitalisation rate, as described below.
Section 1.2.1 **Page 476** HKAS 23.14	**The final paragraph on the page is amended to be:** The **capitalisation rate** is computed as the weighted average of the borrowing costs applicable to the entity's outstanding borrowings during the period, excluding borrowing costs related to borrowings made specifically for the purpose of obtaining a qualifying asset before it is ready for use or sale. The amount of borrowing costs calculated as eligible for capitalisation must not exceed actual borrowing costs incurred.
Section 1.3 **Page 480**	**This section should be deleted.**

Chapter 17	Financial instruments
Section 1.2 **Page 492** HKFRS 9 Appendix A	**A new section 1.2.3 is added as follows:** **1.2.3 Financial guarantee contracts** A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. For example, if a parent company guarantees a subsidiary's bank loan and reimburses the bank for losses incurred if the subsidiary fails to make payments, the parent company has issued a financial guarantee contract. A guarantee over the general obligations of another entity is not a financial guarantee contract because it does not relate to specified payments or a specified debtor. Financial guarantee contracts may be viewed as insurance contracts, and if the issuer of such a contract has explicitly asserted this previously, it may choose to apply HKFRS 17 *Insurance Contracts* to the contract. In all other cases the issuer must treat a financial guarantee contract as a **financial liability** within the scope of HKAS 32, HKFRS 9 and HKFRS 7. Financial guarantee contracts and the applicable accounting is explained in more detail in section 6.
Section 3.2.4 **Page 503** HKFRS 9.B4.1.10-B4.1.12A	**The section is replaced with the following:** **Prepayment features with negative compensation** Some financial asset debt instruments have a prepayment feature with negative compensation: • A prepayment feature is the option to terminate the instrument before maturity; • Negative compensation arises where the party exercising the early termination option receives compensation from the other party rather than paying it to the other party. HKFRS 9 was amended in 2017 to clarify that where a debt instrument has a prepayment feature with negative compensation, its contractual terms can still give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. Therefore a financial asset with such a feature is not necessarily measured at fair value through profit or loss.
Section 3.4.2 **Page 504**	**The following sentence is added immediately before the example:** Where a financial liability is modified or exchanged but this does not lead to derecognition, if the carrying amount of the instrument is changed, this leads to an immediate gain or loss in profit or loss.
Section 5 **Page 515**	**The final bullet point within the introduction to section 5 is amended to be:** • Financial guarantee contracts not measured at FVTPL (see section 6).

Section 6

Page 521

A new section 6 is inserted and the remaining sections of the chapter are renumbered 7–9.

6 Financial guarantee contracts

Topic highlights

A financial guarantee contract is initially measured at fair value and subsequently measured at the higher of the HKFSR 9 expected credit loss allowance and the initial measurement less any cumulative income or amortisation recognised.

HKFRS 9.Appendix A

As explained in section 1.2.3, a financial guarantee contract (FGC) is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due.

HKFRS 9 provides specific guidance for accounting for financial guarantee contracts.

6.1. Initial recognition

HKFRS 9.B2.5

An FGC is recognised by the issuer as a **financial liability** when the guarantee is issued, and initially measured at **fair value**.

The issuer may receive a premium in consideration for the issue of the FGC. This is likely to be the case where FGC was issued to an unrelated party in a standalone, arm's-length transaction. The issuer is less likely to receive a premium where the debtor is a member of the same group as the issuer.

- Where the issuer receives a premium this premium is equal to the fair value of the instrument on the date of initial recognition, unless there is evidence to the contrary.
- Where no premium is received by the issuer, the fair value must be measured using a different method. This method should quantify the economic benefit of the FGC to the debtor. For example, if a guaranteed loan carries an interest rate of 6% and the same loan without a guarantee carried an interest rate of 10%, then fair value is determined as the present value of the difference in interest amounts over the loan term.

6.2 Subsequent measurement

In accordance with HKFRS 9, an FGC may be designated at fair value through profit or loss if:

- There is an accounting mismatch; or
- If it is part of a portfolio that is managed and has its performance evaluated on a fair value basis.

HKFRS 9.4.2.1

Where this designation is not made, an FGC is subsequently measured at the higher of:

(a) The HKFRS 9 expected credit loss allowance; and

(b) The amount initially recognised less any cumulative income recognised in accordance with the principles of HKFRS 15.

HKFRS 9.B5.5.8, B5.5.32

6.2.1 Expected credit loss allowance

As explained in section 5, credit losses are measured at the present value of cash shortfalls. In the case of FGC, cash shortfalls are the difference between:

- Expected payments to reimburse the holder for a credit loss that it incurs; and
- Any amounts that the entity expects to receive from the holder, the debtor or any other party.

When considering whether lifetime expected credit losses should be recognised due to a significant increase in the risk of default, the reporting entity should consider changes in the risk that the **specified debtor** will default on the contract.

Example

On 1 January 20X7, Eastern Bank provided a $10 million loan to Hartley Holt Company (HHC). The loan carried an annual interest rate of 6%. HHC's parent company, Whitaker Smee Company (WSC) provided a guarantee to Eastern Bank for any losses incurred if HHC defaulted on payments due over the three-year term of the loan. If the guarantee had not been provided, the annual interest rate attached to the loan would have been 9%.

At 31 December 20X7 there is a 2% probability that HHC will default on the loan in the next 12 months and WSC will be required to reimburse Eastern Bank with $10 million; at 31 December 20X8 there is a significant increase in the risk of default and the probability of default within the remaining term of the loan is 70%, again with the result that WSC would have to reimburse Eastern Bank with $10 million. In the case of a default, WSC does not anticipate receiving any amounts in respect of the guarantee.

An appropriate discount rate to use throughout is 9%.

Required

How should WSC account for the guarantee provided over the two years to 31 December 20X8?

Solution

The guarantee is a financial guarantee contract because WSC guarantees specified amounts to Eastern Bank in relation to a specified debtor, HHC.

1 January 20X7

WSC recognises the FGC on 1 January 20X7 at fair value. As no premium is received, fair value is calculated as the present value of the difference between contractual interest and interest if there were no guarantee

	Without guarantee	*With guarantee*	*Difference*	*Discount factor*	*Present value*
	$	$	$		$
31.12.X7	900,000	600,000	300,000	1/1.09	275,229
31.12.X8	900,000	600,000	300,000	$1/1.09^2$	252,504
31.12.X9	10,900,000	10,600,000	300,000	$1/1.09^3$	231,655
					759,388

The FGC is initially recognised by WSC by:

		$'000	$'000
DEBIT	Investment in subsidiary	759	
CREDIT	Financial liability		759

To recognise the FGC at fair value.

The debit entry is not to WSC's profit or loss as the transaction does not represent an expense of that company. Instead WSC is providing a form of capital to its subsidiary and so recognises the transaction as an investment in its subsidiary.

31 December 20X7

The FGC is measured at the higher of:

- The initial fair value less cumulative income (i.e. the present value of remaining cash flows):

	$'000
Initial fair value	759
Amortisation ($300,000/1.09^3)	(232)
	527

- The expected credit loss allowance:

  $10,000,000 × 2% = $200,000

Therefore the FGC is measured at fair value less cumulative income. The change in carrying amount is recognised by:

		$'000	$'000
DEBIT	Financial liability	232	
CREDIT	Finance income		232

To recognise the amortisation of the liability for the FGC.

31 December 20X8

The FGC is measured at the higher of:

- The initial fair value less cumulative income (i.e. the present value of remaining cash flows):

	$'000
Initial fair value	759
Amortisation in 20X7 ($300,000/1.09^3)	(232)
Amortisation in 20X8 ($300,000/1.09^2)	(253)
	274

- The expected credit loss allowance:

  $10,000,000 × 70% = $7,000,000

Therefore the FGC is measured at the expected credit loss allowance. The change in carrying amount of $6,473,000 ($7,000,000 – $527,000) is recognised by:

		$'000	$'000
DEBIT	Profit or loss	6,726	
CREDIT	Financial liability		6,473
CREDIT	Finance income		253

To recognise amortisation of the liability for the FGC and adjust carrying amount to be the amount of the loss allowance.

Note: In this example the amortisation of the FGC is equal to the present value of cash flows that no longer form part of the fair value of the instrument. As an approximation amortisation may be calculated on a straight-line basis (i.e. $253,000 per annum).

Chapter 21	Accounting policies, changes in accounting estimates and errors; events after the reporting period

Section 5

Page 634

A new section 5 is added and the existing section 5 is renumbered to be section 6.

5 Current developments

The IASB is currently engaged in three projects relating to IAS 8 (HKAS 8). When amendments are complete, it is likely that they will be adopted by the HKICPA.

Accounting Policy Changes – proposed amendments to IAS 8

This project addresses the issue of changes in accounting policy made by reporting entities as a result of agenda decisions issued by the IFRS Interpretations Committee. As agenda decisions are not mandatory, such a change in policy is voluntary and so IAS 8 (HKAS 8) requires it to be applied retrospectively. In order not to discourage accounting policy changes in these circumstances, the proposed amendments would allow relief from full retrospective application if the costs of determining the effects of the change in policy exceed the expected benefits of applying it retrospectively.

Accounting Policies and Accounting estimates – proposed amendments to IAS 8

This project was the result of inconsistency in practice in the way in which entities distinguish between accounting policies and accounting estimates. As a result the IASB is proposing to amend the definition of accounting policies within IAS 8 (HKAS 8) and add a definition of accounting estimates.

The proposed definition of accounting policies is 'the specific principles, measurement bases and practices applied by an entity in preparing and presenting financial statements' (ED/2017/5, p. 6). This definition is more concise than the existing definition and more consistent with the wording used in other standards.

The proposed definition of accounting estimates is 'judgements or assumptions used in applying an accounting policy when, because of estimation uncertainty, an item in financial statements cannot be measured with precision' (ED/2017/5, p. 6).

It is also proposed that a paragraph is added to IAS 8 (HKAS 8) to clarify that the cost formula used for inventories (either first-in, first-out or weighted average cost) is an accounting policy rather than an accounting estimate.

Definition of Material – proposed amendments to IAS 1 and IAS 8

The IASB is proposing to align the definitions of material in IAS 1 (HKAS 1) and IAS 8 (HKAS 8). In due course this definition will be extended to the Materiality Practice Statement and the new *Conceptual Framework.*

The proposed definition is: 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of a specific reporting entity's general purpose financial statements make on the basis of those financial statements' (ED/2017/6, p. 7).

This improves on the basic existing definition by:

- Referring to 'obscuring' information, so indicating that immaterial information could obscure material information;
- Referring to a reasonable expectation of influencing decisions, which is a higher threshold than the previous 'could influence'; and
- Referring to primary users, so emphasising investors and lenders.

Chapter 23	Operating segments
Section 1.7.1 **Page 679**	**This section is to be deleted as the IASB has decided not to proceed with the proposed amendments to IFRS 8 (HKFRS 8) on the basis that the costs of implementation would exceed the expected benefits.**

Chapter 28	Consolidated accounts: accounting for associates and joint arrangements
Section 1.6 **Page 840**	**The third bullet point is amended to be:** • Other long-term interests such as long-term loans or preference shares (see section 1.8)
Section 1.8 **Page 842** HKAS 28.14A, 38	**The current section 1.8 is renumbered to be section 1.9 and the following new section 1.8 is inserted:** **1.8 Other long-term interests in associates** An associate interest is usually determined by reference to equity (voting) shares, and it is this investment to which equity accounting is applied. An investor may have other long-term interests in an entity that is classified as an associate, for example, long-term loans to the associate or an investment in its preference shares or other non-voting shares. The accounting treatment applied to these other long-term interests is as follows: (1) HKFRS 9 is applied to recognise and measure other long-term interests (including the impairment requirements of HKFRS 9). (2) These other long-term interests are aggregated with the equity investment to form a total, being the net investment in the associate. (3) HKAS 28 requirements regarding recognition of losses (section 1.6) and impairment losses (section 1.7) are applied to the net investment in the associate, meaning that the recognition of trading/impairment losses may reduce the individual carrying amount of other long-term interests within the scope of HKFRS 9 as well as the carrying amount of the equity investment in the associate. Losses are applied first to the equity investment in the associate and then to the other investments in the reverse order of their priority in liquidation. When applying HKFRS 9 requirements to other long-term interests, an entity should not take into account any adjustments to their carrying amounts due to the allocation of losses required by HKAS 28.
Section 1.9 **Page 842**	**This section is to be deleted.**

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Chapter 29	Changes in group structures
Section 2.5 **Page 887** HKFRS 3.42A HKFRS 11.B33CA	**This section is renamed and the text amended as follows:** **1.5 Acquisition of additional shares in a joint operation** HKFRS 3 and HKFRS 11 address two situations involving an increase in shares held in a joint operation: (1) Where a joint operator gains control of a joint operation that is a business, the acquirer should apply the HKFRS 3 requirements for a business combination achieved in stages. It should therefore remeasure the previously held interest in the joint operation to fair value at the acquisition date. (2) Where a party that participates in a joint operation gains joint control of that joint operation, it should not remeasure previously held interest upon gaining joint control.

Chapter 30	Consolidation of foreign operations
Section 2.5 **Page 916**	**This section is renamed 'HK(IFRIC) Int-22 *Foreign Currency Transactions and Advance Consideration'***
Section 2.5 **Page 916**	**The first sentence is deleted and the second sentence amended to be:** HK(IFRIC) Int-22 deals with the issue of non-refundable consideration received or paid in advance of a foreign currency transaction.

Errata – Flashcards

Chapter 29	Changes in group structures
Page 197	**The final sentence in the 'Goodwill' box is amended to read:** The gain or loss on remeasurement of the previously held interest to fair value is recognised in profit or loss or OCI as appropriate.

Technical Update – Flashcards

Chapter 2	Financial reporting framework
Page 18	**An additional section is added:** **Making materiality judgments** • Materiality is pervasive to the preparation of financial statements; when considering whether information is material, a company should consider the needs of primary users of its financial statements. • A four-step process is suggested to assess materiality: – Identify information that has the potential to be material. – Assess whether information identified is material. – Organise the information within the draft financial statements. – Review and consider whether to add/remove information.
Page 19	**Delete Practice Statement: Materiality box and amend Improved Conceptual Framework box to read:** **2018 *Conceptual Framework*** • Issued in 2018 to fill gaps, update content and clarify certain areas. • Chapters are: (1) The objective of general purpose financial reporting (2) Qualitative characteristics of useful financial information (3) Financial statements and the reporting entity (4) The elements of financial statements (5) Recognition and derecognition (6) Measurement (7) Presentation and disclosure (8) Concepts of capital and capital maintenance

Chapter 17	Financial instruments
Page 115	**New text is inserted below the two existing text boxes:** **Financial guarantee contracts [HKFRS 9]** • A contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due. • Recognised by the issuer as a **financial liability** and initially measured at **fair value (**= premium, if received) • Subsequently measured at: – FVTPL if designation made; – Higher of HKFRS 9 expected credit loss or initial fair value less cumulative income.

Chapter 28	Consolidated accounts: accounting for associates and joint arrangements
Page 188	**New text is added as follows:** **Other long-term interests in associate** E.g. Long-term loans to associates or preference shares held • Measure in accordance with HKFRS 9 • Form part of the net investment in associate and are allocated trading and impairment losses