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From: tsangwaihung
Sent: Tuesday, August 24, 2004 8:57 PM
To: P.T. Comment Letter
Subject: Comment on GAAP-SME

<<Comment on the consultation draft of SME financial reporting_Tsang Wai Hung (A10682).doc>> Dear Sir Attached please find my comments.

Best regards

Anthony Tsang Wai Hung (A10682)

**Comment on the Consultation Draft of
SMALL AND MEDIUM-SIZED ENTITY
FINANCIAL REPORTING FRAMEWORK (SME-FRF)**

Issue 1-The need for a SME Financial Reporting Framework (SME-FRF)

My view is that the needs of stakeholders other than SME owners should also be considered, such as SME employees, government departments and agencies, suppliers, as well as banks and other credit facilitators.

Even creditors can obtain additional information from SMEs (this point is mentioned in paragraph 2. of the consultation draft of SME-FRF), they are unaudited and may not be reliable, so the needs of creditors and other non-owner information users under the SME-FRF should also be taken into account.

Moreover, it is unclear that for the first time adoption of the SME-FRF, would companies need to satisfy the “two consecutive years” requirement mentioned in paragraph 18 and 19 of the consultation draft before they are qualified or not qualified for reporting under SME-FRF.

Issue 2-The principles underlying SME financial reporting

I disagree to the principle mentioned in paragraph 4.2.2b. of the consultation paper that “Compliance should be required only when the benefits of compliance exceed the costs”, and suggest to rewrite it as “Compliance should be required to the extent when the benefits of compliance equal to the costs”.

However, I would like to raise that for companies that are marginal to the size restriction, there may be cases that they have to switch between SME-FRF and main GAAP frequently even there exist the “two consecutive years” requirement. For the above-mentioned companies, their size of total revenue and total assets may be made known only in the last minute near the financial year-end. The new standard may not be able to reduce their account preparation cost as source data are always needed to be well prepared for the main GAAP, or on the other hand, the standard may discourage the eagerness of some companies to do more business near the year-end.

I also propose SMEs to disclose the fair value of properties and listed investment as notes to the accounts in addition to the historical cost measurement basis.

Issue 3-Whether SME financial statements should give a true and fair view

My view is that the opinion of “true and fair view” and “true and correct view” (or similar words to that effect) should have the equivalent level of audit assurance in order to enhance the confidence of financial statement users. It is also more desirable to have unique term for the sake of consistency and simplicity.

Issue 4-Which entities should qualify under the SME-FRF

Except for the basis of size, unanimity of owner agreement and absence of public accountability, the qualifying criterion should include the view of creditors. I suggest that if the gearing ratio of a SME is over certain threshold level, a no objection opinion should be seek from major unsecured (or not fully secured) creditors, other than the owners or their related parties, before the company can first time adopt the SME-FRF.

However, I would like to raise a point that the SME-FRF may act as a poison pill in the sense that SMEs may sacrifice their initiative to further develop their business in order to enjoy the continuing adoption of SME-FRF (the temptation of short term benefit may harm their long term well-beings).

Issue 5-Statutory requirements applicable to SME financial reporting

I suggest that the removal of the current group company restriction on applying s.141D should be subject to a size restriction (on consolidated basis). Companies on a consolidated basis exceed the size restriction should adopt the main GAAP. Otherwise, this may act as an incentive for sizable companies to split their operations into subsidiaries in order to avoid the main GAAP. Moreover, the level of audit assurance between the opinion of “true and fair view” and “true and correct view” should be the same.

Issue 6-Applicable financial reporting requirements

I agree that qualifying entity should prepare financial statements under either the SME-FRS or main GAAP, but not a hybrid of the two and the SME-FRS should be applied only in respect of a single entity's financial statements, but not consolidated financial statements. On first time adoption, I propose that the fair value of assets reported under the latest financial statements immediately preceding the adoption can be taken as the deemed cost, so that both the preparer and other information users can be more readily understand and adapt to the post-adopted accounts.

I also propose that aging analysis on the accounts receivable, accounts payable and inventories should be disclosed in the notes to the accounts together with fair valuation of properties and listed investments.