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By email: commentletters@hki CPA.org.hk & post

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HKICPA

Dear Steve

International Accounting Standards Board's Exposure Draft of Investment Entities

We refer to your letter dated 15 November 2011 inviting our comments on the International Accounting Standards Board's Exposure Draft of Investment Entities issued in August 2011.

Our response to the specific questions raised in the exposure draft is attached. We would be pleased to further clarify or discuss any of our comments should you so wish.

Yours sincerely



Eva Wong
Secretary

Enc.

Chairman Bank of China (Hong Kong) Ltd
Vice Chairmen The Hongkong and Shanghai Banking Corporation Ltd
Standard Chartered Bank (Hong Kong) Ltd
Secretary Eva Wong Mei Seong

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Responses of the Hong Kong Association of Banks (“HKAB”) to the Specific Questions in the Exposure Draft of Investment Entities

Question 1

Do you agree that there is a class of entities, commonly thought of as an investment entity in nature, that should not consolidate controlled entities and instead measure them at fair value through profit or loss? Why or why not?

We agree with the proposal that an investment entity should measure its controlled entities at fair value through profit or loss which better aligns with its business model.

Question 2

Do you agree that the criteria in this exposure draft are appropriate to identify entities that should be required to measure their investments in controlled entities at fair value through profit or loss? If not, what alternative criteria would you propose, and why are those criteria more appropriate?

Agree.

However, it is unclear whether the condition “no party holds a controlling financial interest” stated in illustrative examples 1(d) and 4(d) is considered to be a requirement to identify an investment entity. This condition should be included as application guidance if reliance will be placed on the illustrative examples.

Question 3

Should an entity still be eligible to qualify as an investment entity if it provides (or holds an investment in an entity that provides) services that relate to:

(a) its own investment activities?
(b) the investment activities of entities other than the reporting entity? Why or why not?

(a) We conceptually support the Board’s proposal that an entity is eligible to qualify as an investment entity if it provides (or holds an investment in an entity that provides) services that relate to its own investment activities. However, we recommend the Board considers extending this proposal to providing services that related to investment activities of affiliates provided that this only constitutes an insignificant portion of its business.

(b) An entity is eligible if the investment services provided to entities other than the reporting entity are just for making better use of existing resources, for example to share existing research results, investment recommendations or comments with other companies, but not a new research or tailor-made services for those unrelated entities. And the services provided to these unrelated entities only constitute an insignificant portion of the service provider’s business. To avoid diversity in practice, the Board may provide further guidance on how to determine “insignificant portion”.



Question 4

(a) Should an entity with a single investor unrelated to the fund manager be eligible to qualify as an investment entity? Why or why not?

(b) If yes, please describe any structures/examples that in your view should meet this criterion and how you would propose to address the concerns raised by the Board in paragraph BC16.

(a) No. It would be easier for entity to establish an artificial corporate structure which qualifies as an investment entity with only one unrelated investor.

(b) N/A

Question 5

Do you agree that investment entities that hold investment properties should be required to apply the fair value model in IAS 40, and do you agree that the measurement guidance otherwise proposed in the exposure draft need apply only to financial assets, as defined in IFRS 9 and IAS 39 Financial Instruments: Recognition and Measurement? Why or why not?

We believe that fair value model should be applied for investment properties while IFRS 9 and IAS 39 should be adopted for financial assets if these assets are managed and their performance are evaluated on a fair value basis.

Question 6

Do you agree that the parent of an investment entity that is not itself an investment entity should be required to consolidate all of its controlled entities including those it holds through subsidiaries that are investment entities? If not, why not and how would you propose to address the Board's concerns?

We do not agree with the proposed consolidation treatment for a parent that is not an investment entity. We believe the rationale for reporting the investee at fair value should not change simply because it is consolidated with a parent that is not an investment entity. Furthermore, we will expect the financial statements of the non-investment entity parent to be fluctuating upon acquisition or disposal of the investments held through its subsidiaries that are investment entities. This frequent change will distort the financial performance of the non-investment entity parent which may not provide decision useful information to the users of the financial statements. Moreover, the inconsistent accounting treatment in parent level will increase burden to the preparer of the financial statements.

The financial statements users' need for additional information on controlled entities of investment entities can be satisfied by way of disclosure note in the financial statements.

Question 7

(a) Do you agree that it is appropriate to use this disclosure objective for investment entities rather than including additional specific disclosure requirements?

(b) Do you agree with the proposed application guidance on information that could satisfy the disclosure objective? If not, why not and what would you propose instead?

(a) and (b) Agree.

Question 8

Do you agree with applying the proposals prospectively and the related proposed transition requirements? If not, why not? What transition requirements would you propose instead and why?

Agree.

Question 9

(a) Do you agree that IAS 28 should be amended so that the mandatory measurement exemption would apply only to investment entities as defined in the exposure draft? If not, why not?

(b) As an alternative, would you agree with an amendment to IAS 28 that would make the measurement exemption mandatory for investment entities as defined in the exposure draft and voluntary for other venture capital organisations, mutual funds, unit trusts and similar entities, including investment-linked insurance funds? Why or why not?

We prefer alternative (b). Some entities define a venture capital organization as a “silo” within a legal entity that conducts investment activities that are distinct from other activities within that legal entity. In the proposed standard, these silos are no longer eligible for fair value measurement as they do not qualify as investment entities. Therefore, we suggest the Board extends the fair value option to investments in associates where fair value provides more useful and relevant information.