稅務局
香港灣仔告士打道5號
稅務大樓

INLAND REVENUE DEPARTMENT
REVENUE TOWER,
5 GLOUCESTER ROAD, WAN CHAI,
HONG KONG.

網址 Web site: www.ird.gov.hk

來函請寄「香港郵政總局郵箱132號稅務局局長收」
ALL CORRESPONDENCE SHOULD BE ADDRESSED TO:—
COMMISSIONER OF INLAND REVENUE,
G.P.O. BOX 132, HONG KONG.

來函編號：
Your Ref.: C/FRSC

來函請敍明本局檔案號碼
IN ANY COMMUNICATION PLEASE QUOTE OUR FILE NO.

檔案號碼：
File No.: HQ 502/141 Pt.23

電話：
Tel. No.: 2594 5037

傳真：
Fax No.: 2511 7414

電郵：
E-mail:

發出日期：
Date of Issue: 25 October 2013

Mr. Simon Riley
Director, Standard Setting
Hong Kong Institute of
Certified Public Accountants
37/F, Wu Chung House
213 Queen's Road East
Wanchai, Hong Kong

Dear Mr. Riley,

Re: Limited Invitation to Comment on Consultation Draft of Small and Medium-Sized Entity Financial Reporting Framework and Financial Reporting Standard (Revised)

Thank you for your letter dated 21 August 2013 inviting for comments on the above Consultation Draft ("CD"). I am pleased to offer comments of the Inland Revenue Department below.

Consultation Question

"Do you consider it is appropriate to include in the SME-FRF & SME-FRS an option to relieve a group from consolidating one or more subsidiary undertakings if the company's directors are of the opinion that their inclusion would involve expense or delay out of proportion to the value to members of the company? Why or why not? If not, what alternative approach would you propose and why?"

Comments of the Inland Revenue Department ("IRD")

Paragraph 19.1 of the CD provides that consolidated financial statements presented should include all subsidiaries of the parent. Paragraphs 19.1(a) & (b) provide for exceptions. More specifically, paragraph 19.1(b) proposes that one or more subsidiaries may be excluded from consolidation when their inclusion would involve expense and delay out of proportion to the value to members of the company. It is regarding this specific exception that HKICPA is now seeking comments.

In considering whether an exception to consolidation should be allowed, one may like to think first about the more fundamental issues, i.e. why consolidated financial statements are prepared and what they try to deliver. The key purpose of preparing consolidated financial statements is reporting the financial position and performance of a consolidated business group, which comprises the parent company and its subsidiaries. A consolidated financial statement should provide investors and other interested parties with a comprehensive overview of the financial operations of the business group. In this connection, exclusions which will undermine the usefulness of consolidated financial statements to users should not be allowed unless exceptionally justifiable.

Paragraph 19.1(a) of the CD already allows exclusion of one or more subsidiaries from consolidation when their exclusion measured on an aggregate basis is not material to the group as a whole. This is consistent with the general concept of materiality. However, we have reservation about the proposed exclusion in paragraph 19.1(b). As rightly pointed out by your Institute in the letter of 19 August 2013 that if a parent company were to take advantage of paragraph 19.1(b), material information could be omitted from that company's consolidated financial statements, such that they would not give a complete picture of the group as a whole.

Paragraph 19.1(b) brings forward the relief which is currently available in section 124(2)(b)(1) of the old CO, and which is no longer available under the NCO. In recent decades, the current development in company law and international accounting standards has increased the disclosure of information in financial statements. The discard of section 124(2)(b)(1) of old CO in the NCO appears to be an improvement and a positive step towards better information disclosure and enhancing creditors' protection. We do not support putting the provision in SME-FRF & FRS to permit omission of material information from the consolidated financial statements. Furthermore, the exclusion does not appear to be in line with international practice as there is no similar exception in the IFRS-SME.

It is proposed in paragraph 19.1 of the CD that a safeguard be included such that a parent may not exclude a subsidiary from consolidation on the grounds of undue expense and delay out of proportion to the value to members of the company unless the members of the company have been informed in writing about, and do not object to, this exclusion. Regrettably, the safeguard is in the sole interest of members of the company, and whether the expense and delay will be out of proportion to the value to members of the company is highly subjective and may reflect only the opinions of the company's directors. The interests of the users of the consolidated financial statements and the value of the excluded information to the users have not been duly considered.

In so far as tax administration is concerned, consolidated financial statements have been an important and ready source of information about the financial position and financial performance of non-Hong Kong subsidiary undertakings which may otherwise not be available to IRD. It is through examination of consolidated financial statements and related party transactions that the Department can identify tax arrangements and measure the taxation consequences thereof.

Notwithstanding the existence of provisions in the Inland Revenue Ordinance [e.g. sections 51(3) and 51(4)(a)] under which further information may be sought, the Department may not be able to obtain the necessary information efficiently and effectively in absence of consolidated financial statements which provide fuller and better information about the parent company and its subsidiaries. Enquiries, which can be avoided, have to be raised, simply because full consolidated financial statements are not prepared.

Paragraph 19.16(g) of the CD requires disclosure of a list of investments in subsidiaries that has been excluded from consolidation in accordance with paragraph 19.1, including the name, the principal place of operation and place of incorporation and an indication of the nature of business. Whilst we hope that paragraph 19.1(b) exclusion could be removed to maintain the quality of consolidated financial statements and its value to users, in the event that the exclusion is to be allowed, it is suggested that the disclosure requirements under paragraph 19.16(g) be expanded to include the significance of the subsidiary undertakings to the group as a whole in terms of amount and percentage of revenue and profits contribution as well as assets and liabilities, the identity of the directors thereof and their amount of remuneration etc. These proposed additional disclosure requirements would provide users of the financial statements, including this Department, with information about the financial position and performance of the subsidiary undertakings that have been excluded from consolidation.

I hope that our above comments would be kindly considered and I would appreciate it very much if you could keep me informed of the development in the SME-FRF & FRS.

Yours sincerely,

Lam Choi-wah

(Mrs WU LAM Choi-wah)
for Commissioner of Inland Revenue