

Financial Accounting Standards Committee

Meeting summary – June 2002

The Society's Financial Accounting Standards Committee (Committee) met on 12 June 2002 and discussed the following items:

- ✓ Business Combinations
- ✓ Investment Property
- ✓ Exposure Draft of a proposed revision to SSAP 12, Income Taxes
- ✓ Exposure Draft of a proposed limited revision to SSAP 34, Employee Benefits
- ✓ Interpretations of Hong Kong SSAPs
- ✓ True and fair view

Business Combinations

The Committee discussed transitional issues surrounding a proposed revision of SSAP 30 consequent on the IASB's impending revision of IAS 22.

Goodwill that arose before SSAP 30 became effective, and which was taken to reserves as a matter of accounting treatment (written off), is required under SSAP 30 to remain as a separately analysed and reported component of equity. This treatment is not permitted under IAS 22 and, as a result, the Hong Kong transitional provision will be less straightforward than that expected to be adopted in the pending IFRS.

The Committee considered that the underlying principle in transition to a revised Business Combinations SSAP should be that the Hong Kong equivalent of the new IFRS should apply on a basis that is converged with the IFRS, and that goodwill be subject to only one accounting treatment going forward (currently there are at least 2 treatments in Hong Kong, depending on when the goodwill arose).

The Committee considered:

- Whether goodwill recognised as an asset on the balance sheet should, at the point of transition, be measured at its carrying amount (that is, original gross carrying amount less accumulated amortisation less accumulated impairment losses); and
- Whether there is a rebuttable presumption that goodwill previously taken to reserves, and which prior to the application of the revised Statement was reported as a separate component of equity, can be identified with a cash-generating unit and consequently should be reinstated as an asset on the balance sheet, and whether, in rare cases where the presumption is rebutted, goodwill should remain adjusted against shareholders' interests and no longer reported as a separate component of equity.

The Committee tentatively agreed that:

- Goodwill not identifiable to a cash-generating unit should be treated as being fully impaired.
- The Invitation to Comment, issued concurrently with the IASB's exposure draft revision to IAS 22, should seek comment on whether either goodwill presently reported in equity should be reinstated on the balance sheet as an asset at either the carrying amount current at the point of transition (which excludes the impact of amortisation) or the amount that would have been the carrying amount had the goodwill been previously carried as an asset and amortised under the requirements currently applying in SSAP 30.
- In respect of goodwill (including negative goodwill) currently reported as assets (liabilities) on Hong Kong SSAP-based balance sheets, it would appear appropriate for that goodwill to be subject to the same transitional provision likely to be proposed by the IASB.

Investment Property

The Committee considered a proposed revision of SSAP 13, Investment Property, based on the requirements of the equivalent International Accounting Standard, IAS 40.

The earlier introduction into Hong Kong of investment property accounting requirements converged with IAS 40 had effectively been prevented by the requirement under IAS 17, Leases, for lessees to treat leases of land and building as operating leases when title does not pass at the expiry of the lease term.

In its improvements exposure draft, the IASB proposes a more accommodating approach to categorising leases of land and building and, as a consequence, the Committee considers that it is now possible to consider revising SSAP 13 so that Hong Kong's accounting standards on investment property and leases become converged with the corresponding International Accounting Standards.

The Committee noted the following significant differences between SSAP 13 and IAS 40:

- IAS 40 permits an initial policy election between a fair value model (gains and losses between balance sheet dates are recognised in the income statement) and a cost model. In the case of an investment property held under lease, however, the IASB proposes in its improvements exposure draft that the choice be between the fair value model and applying the standard on leases. SSAP 13 requires, with limited exception, a revaluation model (gains and losses typically recognised in a revaluation reserve).
- SSAP 13 permits an exemption from measuring investment property at open market value when an enterprise's total investment property portfolio is below a specified threshold. IAS 40 does not provide for such an exemption.
- SSAP 13 requires valuations to be undertaken by a professionally qualified valuer, which is encouraged, but not required, under IAS 40.
- SSAP 13 requires an individual enterprise within a group to treat investment property on the same basis as reported by the group. IAS 40 requires an individual enterprise to apply the Standard independently.

The Committee agreed to review a proposed exposure draft revision of SSAP 13 prior to its next meeting. In the Invitation to Comment to accompany the exposure draft, the Committee agreed that views would be sought primarily on issues arising from where SSAP 13 presently differs from IAS 40.

Income Taxes

The 9 comment letters received on the exposure draft of a proposed SSAP "Income taxes" were considered in detail. The Committee agreed a number of changes to the proposed SSAP, which includes:

- Clarifying that the method used in the examples for calculating the tax bases of an asset or a liability may not be the only method that can be used;
- Adding further examples to illustrate the calculation of the tax base of an asset or liability; and
- Deleting certain guidance in a box, which is considered to be a repetition of the guidance in the body of the proposed SSAP.

In reviewing a revised proposed SSAP which incorporates the above changes, the Committee decided to issue separate Hong Kong interpretations based on SIC-21, Income Taxes – Recovery of Revalued Non-Depreciable Assets, and SIC-25, Income Taxes – Changes in the Tax Status of an Enterprise or its Shareholders, rather than incorporating the conclusions in the proposed SSAP. The Committee considered this treatment is more consistent with the Society's policy to converge SSAPs with IASs. Subject to this, the Committee agreed to recommend the revised proposed SSAP to Council for approval to be issued as a final Standard for accounting periods beginning on or after 1 January 2003. In the light of the fact that the issue of the proposed SSAP will involve a number of consequential changes to the cross-references in other SSAPs, the Committee decided to deal with these changes in the forthcoming exposure draft on convergence.

Exposure Draft of a limited revision to SSAP 34, Employee Benefits

The Committee noted that the International Accounting Standards Board had recently amended IAS 19 following the exposure draft of a proposed limited revision issued for comment in March 2002. The Committee had published the IASB's exposure draft concurrently with an Invitation to Comment. No comments were received and the Committee agreed to recommend that SSAP 34 be amended to maintain convergence with IAS 19.

Interpretations of Hong Kong SSAPs

Following a report from the Urgent Issues and Interpretations Sub-Committee consideration of comment letters received on Draft Interpretations 14 – 18, the Committee agreed to propose the following changes to Draft Interpretation 15:

- Reinstate the SIC-28 guidance on determining the fair value of a large or small block of equity instruments; and
- Include a footnote to cross-refer to the guidance on determining the fair value of an equity instrument under IAS 39, Financial Instruments, Recognition and Measurement.

The Committee agreed to recommend to Council that these Interpretations be issued as final with effect from the following dates:

- Interpretation 14, Evaluating the Substance of Transaction Involving the Legal Form of a Lease (based on SIC-27), proposed to become effective on 30 June 2002.
- Interpretation 15, Business Combinations – "Date of Exchange" and Fair Value of Equity Instruments (based on SIC-28) proposed to become effective for acquisitions given initial accounting recognition on or after 30 June 2002.

- Interpretation 16, Disclosure – Service Concession Arrangements (based on SIC-29) proposed to become effective on 30 June 2002.
- Interpretation 17, Revenue – Barter Transactions Involving Advertising Services (based on SIC-31) proposed to become effective on 30 June 2002.
- Interpretation 18, Consolidation and Equity Method – Potential Voting Rights and Allocation of Ownership Interests (based on SIC-33) proposed to become effective for annual financial periods beginning on or after 1 July 2002.

True and fair view

In relation to the project on improvements, the Committee considered an issue regarding the use of the term “fair presentation” (which is the term used in IAS 1) as opposed to “true and fair view” in SSAP 1. Having considered that:

1. Paragraph 46 of the IASB Framework states that both expressions are equivalent; and
2. The standard opinion paragraph in ISA 700 (on which the HK SAS 600 is based) uses both “true and fair view” and “fair presentation” and considers both expressions to be equivalent but both expressions must be followed by the words “in accordance with” the identified financial reporting framework;

the Committee concluded that using the term “true and fair view” in SSAP 1 would not result in a difference between SSAP 1 and IAS 1. In view of this and given that “true and fair view” is the term used in the Companies Ordinance, the Committee considered that the term “true and fair view” should continue to be used in SSAP 1.

Date of Next Meeting

The Committee’s next meeting will be held on 10 July 2002.

This meeting summary is provided for the information and convenience of those who wish to follow the Committee’s deliberations. All conclusions reported are tentative and may be changed at future meetings.

The IASB publishes summaries of its meetings and these can be found on the IASB’s website at <http://www.iasb.org.uk>.

The Committee welcomes comments on its technical agenda. Please e-mail us at commentletters@hksa.org.hk.