

The Society's Financial Accounting Standards Committee (Committee) met on 15 May 2002 and discussed the following items:

- ✓ Business Combinations
- ✓ Land Use Rights Certificates issued in the People's Republic of China
- ✓ Improvements to IAS and Hong Kong SSAPs
- ✓ Proposed Framework for Differential Reporting

Business Combinations

The Committee noted progress made by the IASB on its project to revise IAS 22 and considered the following issues:

- ✓ The proposal to require goodwill to remain on the balance sheet, unamortised, but subject to an annual impairment review
- ✓ The proposed treatment for negative goodwill
- ✓ Transitional provisions required for Hong Kong

Goodwill and the impairment model

The impairment model currently under consideration by the IASB is broadly similar to the principles in IAS 36 (SSAP 31) in respect of the 'trigger' that gives rise to the need to conduct a detailed impairment review and, once triggered, the nature of the impairment review by reference to the recoverable amount of the underlying assets.

The Committee also considered the conceptual merit of permitting goodwill to remain unamortised on the balance sheet. Under the current (SSAP 30) approach to purchased goodwill, such goodwill is gradually replaced by goodwill generated internally through advertising, brand maintenance and other similar activities. The longer that goodwill stays on the books unamortised (and, in the case of a successful business), the more likely it is to actually have the nature of internally generated goodwill. The Committee agreed to address this apparent conceptual inconsistency with the IASB and whether, for example, this may open the door to argue that internally generated intangible assets should be able to be recognised on the balance sheet under IAS 38.

Negative goodwill

The IASB has indicated it intends to find a replacement term for "negative goodwill". The amount that represents the 'true' excess of the aggregate fair values of the identifiable net assets over the cost of acquisition – regardless of the underlying reason/s – is to be treated as a 'windfall gain' and recognised in income immediately.

The IASB proposal would simplify significantly the 'three tier' approach currently under IAS 22. The Committee agreed with the principles underlying the IASB proposal in respect of negative goodwill.

Transitional provisions

SSAP 30 differs from IAS 22 (1998) in respect of transition, most notably in relation to the treatment of goodwill previously written off directly to shareholders' interests (permitted in Hong Kong prior to SSAP 30 but the then IASC discontinued the practice following the 1993 revision to IAS 22).

The Committee noted that the implied transition from IAS 22 (1998) to a successor IFRS would not require goodwill to be reinstated on the balance sheet. The proposal appears to be similar to the transitional provision stated in SSAP 30 except that, in the case of the IASB, impairment would be required only in respect of goodwill actually carried on the balance sheet. With goodwill having been "written off" previously to reserves (but which remains as a separately analysed and reported component of equity subject to impairment) the Committee noted that the Hong Kong transitional provision would necessarily be less straightforward than that expected in the pending IFRS.

A paper on the potential transitional provisions applying under SSAP 30 would be discussed at the Committee's next meeting.

Land Use Rights Certificates issued in the People's Republic of China

The Committee considered a background paper on Land Use Rights Certificates (LURC) issued in China. The paper set out the generic terms and conditions of a LURC and discussed the appropriate accounting treatment for LURCs under Hong Kong SSAPs.

The Committee tentatively concluded that the typical LURC has the same characteristics as a lease and, as such, would usually be accounted for under SSAP 14.

The Committee noted that the specific exemption under SSAP 14 paragraph 11 accorded to leases of property owned by the Hong Kong SAR government would not apply in the case of a LURC issued in the PRC but that common practice in Hong Kong had been to extend the exemption to LURCs. This issue is expected to be only short term, however, with the impending proposal to amend the leasing and investment properties accounting standards.

The Committee agreed to review a revised draft of the paper at its next meeting.

Improvements to IAS and Hong Kong SSAPs

The Committee considered a draft version of the Hong Kong Invitation to Comment on the IASB's Exposure Draft Improvements to the International Accounting Standards. The Committee agreed that, prior to publication, the Invitation to Comment would be considered further by the Improvements and Convergence Sub-committee.

Proposed Framework for Differential Reporting

The Committee considered a draft Framework for Differential Reporting and Discussion Paper, on referral from the Society's GAAP for Small Businesses Working Group. The Framework seeks to set out criteria by which entities qualify for financial reporting exemptions from the SSAPs and to guide the standard setter in establishing differential reporting exemptions in those Statements.

The Committee agreed with the principles set out in the Exposure Draft and Discussion Paper but recorded comments on two significant issues:

First, the approach taken in maintaining the differential reporting requirements – there are essentially two approaches, namely:

- The “integrated approach”, of the type adopted in Canada and New Zealand, whereby differential reporting exemptions are highlighted in the Framework and in the body of each standard otherwise applicable on a generic basis; and
- The “separate approach”, of the type adopted in the United Kingdom, whereby a completely separate accounting standard is developed and maintained and which applies to qualifying entities exclusive of all other accounting standards.

The Committee indicated its strong support for the integrated approach and considers that the documents (in particular, the Discussion Paper) should not take a neutral stance. The Committee considers that if the separate approach was adopted in Hong Kong, this would create a significant drain on resources. The Committee is concerned that the Discussion Paper should not imply that the Society is willing to adopt an approach to setting differential reporting exemptions that it has no realistic way of meeting.

Second, whether certain limited measurement differences should be permitted under the proposed Framework. The draft Framework proposes primarily disclosure differences to the existing SSAPs but, in keeping with the principles outlined in the Framework and comparable measures put into place in countries such as Canada and New Zealand, the Exposure Draft and Discussion Paper proposes limited measurement differences in respect of SSAPs 12, 13 & 17. The Committee noted that in leading jurisdictions where differential reporting exemptions were in place (whether in Canada or the United Kingdom) measurement differences to one extent or other were permitted.

Date of Next Meeting

The Committee's next meeting will be held on 12 June 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.