

**SUMMARY OF SMPC TECHNICAL ISSUES WORKING GROUP MEETING**  
**Request for Information on Post-implementation Review: Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (SME Standard)**

Date: 20 November 2018

Time: 14:30 – 15:45

Venue: HKICPA Board Room, 37/F Wu Chung House, Wanchai

**Present:**

Gary Poon, Poon & Co

Sharon Chan, Grant Thornton

Colin Chau, RSM Hong Kong

Philip Fung, Lak & Associates CPA

Anntice Lai, Baker Tilly

Kenneth Lau, Crowe Horwath

Thomas Wong, Nexia Charles Mar Fan & Co.

Anthony Wong, Standard Setting, HKICPA

1. The SMPC Technical Issues Working Group (TIWG) observed that some SMEs have been transitioning from full HKFRS to the SME Standard in recent years due to significant changes to full HKFRS requirements for financial instruments, revenue and leases. The TIWG noted that SMEs prepare financial statements under the SME Standard unless users of their financial reports specifically request that they prepare full HKFRS financial statements.
2. The TIWG observed that some private groups prepare consolidated financial statements under full HKFRS while using the SME Standard to prepare the subsidiaries' financial statements. Preparing subsidiaries' financial statements under the SME Standard is more cost-effective than under full HKFRS.
3. The TIWG discussed and provided their feedback on the questions in the [Request for Information](#) on the post-implementation review (PIR) of the SME Standard (see paragraphs 4 to 15 below).

***Extract of Question 2 in the Request for Information***

- |  |
|--|
| (a) <i>(This question is for lessors) As the SME Standard currently does not include accounting requirements for lessors, how have you accounted for leases?</i> |
| (b) <i>Do you support adding accounting requirements for lessors to the SME</i>  |

*Standard? Why, or why not?*

4. The TIWG considered that there was no urgent need to add accounting requirements for lessors to the SME Standard unless there was strong demand from other stakeholders. This is not consistent with the views of targeted stakeholders<sup>1</sup> in the first phase of the PIR which would prefer to add such requirements. The TIWG commented that, applying paragraph 2.1<sup>2</sup> of the SME Standard, most SME lessors adopted the principles from the Statements of Standard Accounting Practices (SSAP), the predecessor standards similar to the SME Standard, to account for leases. The TIWG considered that most SME lessors only lease out investment properties under operating leases. Hence, accounting requirements for finance leases from the perspective of lessors would generally not be applicable for most SMEs.

***Extract of Question 3 in the Request for Information***

- (a) *Have you been impacted by the SME Standard which currently does not explicitly allow or include a 'presentation currency' concept as in HKAS 21?*
- (b) *Do you support adding the 'presentation currency' concept to the SME Standard? Why, or why not?*

5. The TIWG observed that, applying paragraph 2.1 of the SME Standard, some SMEs select an accounting policy based on the 'presentation currency' concept in HKAS 21 *The Effects of Changes in Foreign Exchange Rates* if they have operations that are based outside of Hong Kong but report Hong Kong dollars as their reporting currency. The TIWG supported adding the 'presentation currency' concept to the SME Standard to avoid confusion only if doing so would not significantly affect how the majority of the SMEs currently translate balances and transactions of their foreign operations. Some members stated that they followed the general principles of the relevant SSAP when converting local currencies to presentation currencies. In general, this is consistent with the views of targeted stakeholders in the first phase of the PIR.

***Extract of Question 4 in the Request for Information***

- (a) *Have you been impacted by the SME Standard which currently does not include accounting and/or disclosure requirements for derivatives?*

<sup>1</sup> The first phase of the PIR was targeted outreach with the Financial Reporting Standards Committee's SME Standard Advisory Panel and a few other interested parties, including other auditors from small and medium-sized accounting firms and users of financial statements prepared under the SME Standard.

<sup>2</sup> According to paragraph 2.1 of the SME Standard, "Management should use its judgment in developing an accounting policy resulting in information that is relevant to the needs of users of the financial statements and is reliable in nature. Management should select and apply an entity's accounting policies so that the financial statements comply with all the requirements of the SME-FRS and are consistent with the historical cost convention."

- |   |
|---|
| <p>(b) <i>Do you support adding accounting and/or disclosure requirements for derivatives to the SME Standard? Why, or why not?</i></p> <p>(c) <i>Are there other accounting and/or disclosure requirements that are not currently in the SME Standard with which you have experienced issues? Please provide sufficient details and explains about the items you encountered issues in accounting and why accounting and/or disclosure requirements are necessary.</i></p> |
|---|

6. The TIWG observed that most SMEs are applying paragraph 2.1 and Section 6 *Investments* of the SME Standard to account for derivatives. The TIWG expected SMEs might be open to disclosing information about significant terms of the derivatives contracts (for example, maturity, notional amount, background of transactions) if such disclosures do not require undue cost or effort. However, the TIWG strongly opposed introducing fair value accounting and fair value disclosure requirements for derivatives because these would be departures from the cost-based approach adopted in the SME Standard and would also result in undue cost or effort for SMEs. In general, the TIWG's views are consistent with the views of targeted stakeholders in the first phase of the PIR, but with more focus on undue cost or effort concerns.

<b><i>Extract of Question 5 in the Request for Information</i></b>
--

<i>Have you experienced difficulties in applying the disclosure requirements in paragraph 19.16 of the SME Standard? If yes, please explain in detail.</i>
--

7. The TIWG thought that the financial information of subsidiaries excluded from consolidation can be presented on an aggregated basis because the subsidiaries are generally not material to the group. This is consistent with the views of targeted stakeholders in the first phase of the PIR. In addition, the TIWG suggested that SMEs should have the option to present the financial information of excluded subsidiaries either on a combined or consolidated basis. The TIWG also suggested that the HKICPA can consider HKFRS 12 *Disclosure of Interests in Other Entities* when simplifying the relevant requirements in paragraph 19.16(g)(vi) of the SME Standard in the future. One member suggested adding a requirement to disclose transactions between an excluded subsidiary and the consolidated group that are not eliminated in the consolidated group.
8. The TIWG supported clarifying whether the disclosure requirements in paragraphs 19.16(b), (c), (d) and (g) are applicable to company-level financial statements. This is consistent with the views of targeted stakeholders in the first phase of the PIR.

**Extract of Question 6 in the Request for Information**

*Have you experienced challenges in restating comparative information of property, plant, equipment, intangible asset or any other financial statement item when an entity transitioned from a different reporting framework to the SME Standard? If yes, please explain in detail.*

9. The TIWG observed that some SMEs have experienced significant difficulties in locating the historical cost information and restating comparative information for property, plant, equipment and intangible assets when transitioning from a different reporting framework to the SME Standard in the absence of transitional provisions (like the transitional provisions in full HKFRS and the *HKFRS for Private Entities*). The TIWG suggested that transition could be better facilitated by allowing an entity to use the carrying amount of the property, plant, equipment or intangible asset under the previous reporting framework at the date of transition as the item's deemed cost on transition, similar to the transitional provisions available in full HKFRS. Since full HKFRS has become much more complex in recent years, more SMEs are expected to adopt the simplified frameworks, namely SME Standard or *HKFRS for Private Entities*. Thus, sufficient and appropriate transitional provisions should be in place. This view is consistent with the views of targeted stakeholders in the first phase of the PIR.

**Extract of Question 7 in the Request for Information**

*Have you experienced difficulties with or have any other comments about applying a useful life of five years for goodwill accounting? If yes, please explain in detail.*

10. The TIWG considered that a five year amortisation period is reasonable because it is the average payback period of investments in Hong Kong. Hence, the TIWG did not consider there is a need to change the rebuttable presumption of 5 years to 10 years to align with paragraph 19.23 of the *HKFRS for Private Entities*. This is not consistent with the views of targeted stakeholders in the first phase of the PIR who would like to change to a rebuttable presumption of 10 years to limit the transitional adjustments if the entity is converting from the SME Standard to the *HKFRS for Private Entities*.

**Extract of Question 8 in the Request for Information**

*Would you recommend clarifying/simplifying other accounting requirements of the SME Standard? Please explain the requirements you propose to be clarified/simplified and why it is necessary.*

11. The TIWG did not provide any other recommendations for clarifying/simplifying

other accounting requirements of the SME Standard.

**Extract of Question 9 in the Request for Information**

- (a) *Have you experienced any other challenges or benefits when applying the SME Standard? If you are a user of financial reports prepared under the SME Standard, have you experienced any challenges or benefits with such reports? Please explain in detail, for example, whether you found a predominantly cost-based measurement reporting useful?*
- (b) *Do you have other comments, including feedback on the HKICPA's PIR process?*

12. The TIWG have not experienced any other challenges or benefits when applying the SME Standard.
13. The TIWG supports the HKICPA's PIR process. However, it advised that the PIR process should be undertaken no more frequently than every five years and not be conducted too frequently unless there is a change in regulatory requirements (e.g. Companies Ordinance).

**Extract of Question 10 in the Request for Information**

*Do you have comments on the FRSC's approach to wait for a review of implementation experience of the major new HKFRS standards before considering whether to introduce the relevant new requirements into the SME Standard? Please explain why and when is an appropriate time, if you disagree with the FRSC's decision.*

14. The TIWG considered that many of the new and major HKFRSs involve complicated fair value and forward-looking concepts that do not appear to be warranted in a simple cost-based accounting framework like the SME Standard. Moreover, the current SME Standard appears to be more comprehensive than its counterparts in other jurisdictions such as the standard in Mainland China for financial reporting of micro-entities. In general, the TIWG agreed that there should be a due process to consider whether to introduce the relevant new HKFRS requirements into the SME Standard, which includes reviewing their financial reporting objectives and consistency with the cost-based framework, benchmarking them against counterparts in different jurisdictions, and considering their implementation experience.
15. Overall, the TIWG considered that any amendments to the SME Standard should:
- (a) minimise disruption,
  - (b) have the overall objective of producing useful information for users of SME

financial statements and the cost of providing that information should not exceed the benefits to users; and

- (c) be written in simple, clear understandable language.