Hong Kong Institute of Certified Public Accountants
香港會計師公會

Minutes of the 237th meeting of the Financial Reporting Standards Committee held on Tuesday, 4 July 2017 at 8:30 a.m. in the Board Room of the Hong Kong Institute of Certified Public Accountants, 37/F., Wu Chung House, 213 Queen's Road East, Wanchai, Hong Kong.

Members present:	Ms.	Shelley So (Chairman), PricewaterhouseCoopers
	Mr.	Ernest Lee (Deputy Chairman), Elito Investment Limited
	Ms.	Elaine Chan, HSBC (on behalf of James Fawls)
	Ms.	Candy Fong, Foremost Advisers Ltd
	Ms.	Kelly Kong, Jardine Matheson & Co., Limited
	Ms.	Eros Lau, Deloitte Touche Tohmatsu
	Ms.	Susanna Lau, Securities and Futures Commission
	Mr.	Ben Lo, Stock Exchange of Hong Kong Limited (on behalf of Steve Ong)
	Mr.	Gary Poon, Poon & Co.
	Mr.	Simon Riley, BDO Limited
	Mr.	Gary Stevenson, RSM Hong Kong
	Ms.	Catherine Tang, Financial Reporting Council (on behalf of Florence Wong)
	Ms.	Sanel Tomlinson, KPMG
	Mr.	Guochang Zhang, The University of Hong Kong
Staff in attendance:	Ms.	Christina Ng, Director, Standard Setting
	Ms.	Winnie Chan, Associate Director, Standard Setting
	Ms.	Kam Leung, Associate Director, Standard Setting
	Ms.	Katherine Leung, Associate Director, Standard Setting
	Ms.	Eky Liu, Associate Director, Standard Setting
	Mr.	Anthony Wong, Associate Director, Standard Setting
	Ms.	Daisy Xia, Manager, Standard Setting
	Ms.	Iris Lin, Associate Manager, Standard Setting
	Ms.	Winnie Chan, Associate Director, Technical Learning & Support
Apologies:	Mr.	Joe Ng, Ernst & Young

Action

1. 2017 Annual Accounting Update

The Committee noted that the Annual Accounting Update (AAU) conference for 2017 has been scheduled to take place on 11 November 2017. The Committee also noted that the 2017 AAU will be in a dialogue format between a moderator and the presenter and will focus on three topics, particularly on transitioning to the new standards:

- HKFRS 9 *Financial Instruments*
- HKFRS 15 *Revenue from Contracts with Customers*
- HKFRS 16 *Leases*

2. Minutes, work program and liaison log

The Committee approved and the Chairman signed the minutes of the 236th meeting.

The Committee noted the developments outlined in the FRSC and SSD work program and liaison log, in particular in relation to the Definition of a Business Project. The Committee agreed that the SSD should write to the — SSD

IASB to reconsider two tentative decisions made in April:

- making the screening test optional on a transaction-by-transaction basis; and
- confirming that the screening test is determinative.

The Committee also agreed that the SSD should recommend the IASB to remove the screening test in its entirety or make the screening test a part of a holistic assessment to determine a business; and conduct a thorough Effects Analysis, particularly on providing an optional screening test, before finalising its decisions.

3. <u>Business Combinations under Common Control project</u>

The Committee considered and agreed with SSD's proposed next steps after considering the feedback received from its Request for Information on the Post-implementation Review of AG 5 *Merger Accounting for Common Control Combinations*. SSD

The proposed next steps include:

- Adding references of existing standards to AG 5 and a requirement to disclose who is the 'controlling party';
- Undertaking research on some areas to better understand the issues and corresponding impact, and the underlying basis for certain concepts within AG 5 before deciding on further actions;
- Conducting further outreach with regulators and investors on some areas to better understand their needs and concerns;
- Explaining the concepts of AG 5 through educational activities; and
- Sharing our findings and continuing discussions with the IASB staff to support their development of the IASB's BCUCC project.

4. <u>IFRS 17 *Insurance Contracts*</u>

The Committee received an update on IFRS 17, including the establishment of the IASB Resource Group (TRG) to support stakeholders in implementing the standard, and to inform the IASB of what action, if any, will be needed to address implementation concerns. The Committee is pleased that the IASB responded to stakeholder requests (including HKICPA's request in a letter dated 19 December 2016) to establish a TRG as IFRS 17 represents a fundamental change to existing practice for most entities issuing insurance contracts and will therefore require significant implementation effort.

The Committee considered a concern raised by a Hong Kong stakeholder on the adoption of IFRS 17 in Hong Kong soon after it is issued. The Committee considered and noted that, in principle, the due process for issuing and adopting IFRS 17, following HKICPA full convergence policy, has been fulfilled. The Committee requested SSD to assess the expressed concern through targeted outreach with other Hong Kong stakeholders. SSD

The Committee also considered and supported establishing a Hong Kong implementation support group when IFRS 17 is adopted; and endorsing representatives from Hong Kong who are seeking membership of the IASB TRG. One Committee member expressed a preference to endorse only TRG applicants from Hong Kong companies that issue insurance contracts on the assumption that each of the larger accounting firms would most likely have a member seat.

5. **Improvements to IFRS 8 *Operating Segments***

The Committee considered and broadly supported SSD's analysis on stakeholder feedback and the proposals in IASB ED/2017/2 *Improvements to IFRS 8 Operating Segments*. A letter to the IASB will be approved out-of-session. SSD

The Committee also supported the SSD's recommendation to respond to some concerns/views raised by stakeholders, in particular, those relating to the purpose and rationale underlying IFRS 8.

6. **HKFRS 15 – Revenue Recognition of Real Estate Sales**

The Committee received an update on a meeting held by SSD and the Revenue Project Advisory Panel (the "Panel") in June 2017. The main aim of the June Panel meeting was to consider the point in time at which an entity recognises revenue for the sale of properties that are completed and sale of properties under construction in Hong Kong (also known as properties 'off-the-plan'). The Panel also considered the points raised by members of the Real Estate Developers Association of Hong Kong (REDA) at a meeting with FRSC representatives in March 2017.

The Committee noted and concluded the following, taking into account the points raised by REDA and the Panel :

- Paragraph 31 of HKFRS 15 provides the principles for recognising revenue: an entity recognises revenue when (or as) the entity satisfies a performance obligation by transferring a promised good or service ('an asset') to a customer—a promised asset is transferred when (or as) the customer obtains control of the asset. Paragraph 33 explains that a customer has control of an asset when the customer (1) has the ability to direct the use of, and (2) obtain substantially all of the benefits from, the asset. Consequently:
  - the revenue recognition concept has changed from a 'risk and reward of ownership' model under HKAS 18 to a 'transfer of control from a customer perspective' model.
  - HKFRS 15 requires an entity to determine when the customer obtains control of the goods.
  - 'Risk and reward of ownership' has become one of the indicators of transfer of control, but it is not the only indicator.

- Regardless of whether the property for sale is complete or under construction at the time of entering the sale and purchase agreement, the good(s) being sold by a developer to its customer is a completed physical property—which is different from a contractual right to receive a property at a future date. Accordingly, the point in time at which revenue should be recognised should be based on when customers obtain control over the completed physical property.

- The Committee agreed with the rationale and conclusions of the August 2015 Aplus article HKFRS 15 – How the new standard affects revenue recognition of Hong Kong real estate sales before completion. That is, based on the fact pattern outlined in the article, which is based on a typical Hong Kong sale and purchase agreement, no revenue is recognised while the property is still under construction. In that fact pattern it is concluded that an entity transfers control of a completed physical property to a customer, and therefore recognise revenue, at a point when the customer obtains legal title.

- The Committee also considered the point in time when an entity recognises revenue for completed properties based on the following general contractual and legal terms in Hong Kong:
  - A sale and purchase agreement provides a customer with only a contractual right to receive a property. Because the promised asset stipulated in a sale and purchase agreement is a completed physical property, an entity must demonstrate that:
    - a customer has the ability to direct the use of a completed physical property (criterion 1 of HKFRS 15 control principle described above). Having a contractual right to receive a property does not satisfy this criterion as a customer only has the right to make plans for directing the use of a property at a future date, not the ability to direct the use of the completed physical property; and
    - a customer can obtain the benefits from a completed physical property (criterion 2 of HKFRS 15 control principle described above). Having a contractual right to receive a property does not satisfy this criterion as the right only entitles a customer to future benefits that the customer will enjoy when it receives the completed physical property. The customer therefore is enjoying the benefits of having the contractual right to receive a property, rather than the completed physical property itself.
  - A sale and purchase agreement is a legally unconditional document that obligates a customer to purchase a property at an agreed date and price. However, the legally binding agreement does not obligate a customer to make any payments to the developer before the completed physical property is legally assigned to the customer. Therefore, a developer usually does not have a present right to payment when the sale and purchase agreement is signed. The present right to payment is established at the time of legal assignment.
  - A sale and purchase agreement prohibits a developer from selling the property that is the subject of the agreement to another customer. However, a customer's ability to prevent other parties from purchasing the property by itself is not sufficient to fulfil the control assessment. That is because it still does not allow the customer to deal with the property in its own right.
  - Based on research on the legal environment in Hong Kong, it was noted that without a legal title a customer is usually unable to execute its plans for the property and unable to realise the benefits from the property.
  - The Committee concluded that it is therefore usually difficult for a developer to demonstrate that a customer has control of the completed physical property without right to access or physical use or a legal title.

In addition, the Committee noted that SSD had consulted the views of national standard-setters around the region and the staff of the IASB. The views of these standard-setting bodies are consistent with the conclusions of the Committee.

There being no further business, the meeting closed at 11:30 a.m.

SHELLEY SO
CHAIR

11 July 2017