

# MEMBERS' HANDBOOK

## Update No. 103

(Issued 23 December 2010)

This Update relates to the issuance of:

- Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards* – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters

<b><u>Document Reference and Title</u></b>	<b><u>Instructions</u></b>	<b><u>Explanations</u></b>
<b><u>VOLUME II</u></b>		
Contents of Volume II	Discard existing page ii & replace with revised page ii.	Revised contents page
<b>HONG KONG FINANCIAL REPORTING STANDARDS (HKFRS)</b>		
HKFRS 1 <a href="#"><u><i>First-time Adoption of Hong Kong Financial Reporting Standards</i></u></a> (Standard)	Replace cover page with revised cover page. Insert pages 32 – 34 after page 31.	- Note
HKFRS 1 <a href="#"><u><i>First-time Adoption of Hong Kong Financial Reporting Standards</i></u></a> (Basis for Conclusions)	Replace cover page with revised cover page. Insert pages 30 – 31 after page 29.	- Note
HKFRS 9 <a href="#"><u><i>Financial Instruments</i></u></a>	Replace cover page, pages 66 & 68 with revised cover page, pages 66 & 68.	- Note

### Note:

1. The amendments to HKFRS 1 *First-time Adoption of HKFRSs* confirm proposals that were published as separate exposure drafts for public comment in August and September.

The first amendment replaces references to a fixed date of '1 January 2004' with 'the date of transition to HKFRSs', thus eliminating the need for companies adopting HKFRSs for the first time to restate derecognition transactions that occurred before the date of transition to HKFRSs. The second amendment provides guidance on how an entity should resume presenting financial statements in accordance with HKFRSs after a period when the entity was unable to comply with HKFRSs because its functional currency was subject to severe hyperinflation.

The amendments to HKFRS 1 are set out in *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* and are effective from 1 July 2011. Earlier application is permitted.

		<i>Issue/(Review date)</i>
HKAS 29	<a href="#">Financial Reporting in Hyperinflationary Economies</a> .....	3/04(4/10)
HKAS 31	<a href="#">Interests in Joint Ventures</a> .....	12/04(5/10)
HKAS 32	<a href="#">Financial Instruments: Presentation</a> .....	11/04(5/10)
HKAS 33	<a href="#">Earnings per Share</a> .....	3/04(3/10)
HKAS 34	<a href="#">Interim Financial Reporting</a> .....	10/04(5/10)
HKAS 36	<a href="#">Impairment of Assets</a> .....	8/04(3/10)
HKAS 37	<a href="#">Provisions, Contingent Liabilities and Contingent Assets</a> .....	11/04(3/10)
HKAS 38	<a href="#">Intangible Assets</a> .....	8/04(3/10)
HKAS 39	<a href="#">Financial Instruments: Recognition and Measurement</a> .....	1/06(5/10)
HKAS 40	<a href="#">Investment Property</a> .....	11/05(6/10)
HKAS 41	<a href="#">Agriculture</a> .....	12/04(6/10)
<b>HONG KONG FINANCIAL REPORTING STANDARDS (HKFRS)</b>		
HKFRS 1 Revised	<a href="#">First-time Adoption of Hong Kong Financial Reporting Standards</a> .....	12/08(12/10)
HKFRS 2	<a href="#">Share-based Payment</a> .....	4/04(2/10)
HKFRS 3 Revised	<a href="#">Business Combinations</a> .....	3/08(5/10)
HKFRS 4	<a href="#">Insurance Contracts</a> .....	3/06(2/10)
HKFRS 5	<a href="#">Non-current Assets Held for Sale and Discontinued Operations</a> .....	8/04(2/10)
HKFRS 6	<a href="#">Exploration for and Evaluation of Mineral Resources</a> .....	2/05(2/10)
HKFRS 7	<a href="#">Financial Instruments: Disclosures</a> .....	9/05(10/10)
HKFRS 8	<a href="#">Operating Segments</a> .....	3/07(11/09)
HKFRS 9	<a href="#">Financial Instruments</a> .....	11/09 (12/10)
IMPROVEMENTS TO HKFRSs 2010	<a href="#">Improvements to HKFRSs 2010</a> .....	5/10

HKFRS 1 (Revised)  
Revised ~~October~~ December 2010

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Effective for annual periods  
beginning on or after 1 July 2009

*Hong Kong Financial Reporting Standards 1 (Revised)*

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# First-time Adoption of Hong Kong Financial Reporting Standards

An entity shall apply amendments resulting from [Improvements to HKFRSs](#) issued in May 2010 for annual periods beginning on or after 1 January 2011.



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## **Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards*—Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (issued in December 2010) - effective for annual periods beginning on or after 1 July 2011**

After paragraph 31B a heading and paragraph 31C are added.

### **Presentation and disclosure**

#### **Explanation of transition to HKFRSs**

##### **Use of deemed cost after severe hyperinflation**

31C If an entity elects to measure assets and liabilities at fair value and to use that fair value as the deemed cost in its opening HKFRS statement of financial position because of severe hyperinflation (see paragraphs D26–D30), the entity's first HKFRS financial statements shall disclose an explanation of how, and why, the entity had, and then ceased to have, a functional currency that has both of the following characteristics:

- (a) a reliable general price index is not available to all entities with transactions and balances in the currency.
- (b) exchangeability between the currency and a relatively stable foreign currency does not exist.

### **Appendix B**

#### **Exceptions to the retrospective application of other HKFRSs**

Paragraph B2 is amended (new text is underlined and deleted text is struck through).

##### **Derecognition of financial assets and financial liabilities**

B2 Except as permitted by paragraph B3, a first-time adopter shall apply the derecognition requirements in HKAS 39 *Financial Instruments: Recognition and Measurement* prospectively for transactions occurring on or after 1 January 2004 the date of transition to HKFRSs. ~~In other words~~ For example, if a first-time adopter derecognised non-derivative financial assets or non-derivative financial liabilities in accordance with its previous GAAP as a result of a transaction that occurred before 1 January 2004 the date of transition to HKFRSs, it shall not recognise those assets and liabilities in accordance with HKFRSs (unless they qualify for recognition as a result of a later transaction or event).

### **Appendix D**

#### **Exemptions from other HKFRSs**

Paragraphs D1 and D20 are amended (new text is underlined and deleted text is struck through)

D1 An entity may elect to use one or more of the following exemptions:

- (a) ...
- (o) transfers of assets from customers (paragraph D24); ~~and~~

(p) extinguishing financial liabilities with equity instruments (paragraph D25); and

(q) severe hyperinflation (paragraphs D26–D30).

An entity shall not apply these exemptions by analogy to other items.

### **Fair value measurement of financial assets or financial liabilities at initial recognition**

D20 Notwithstanding the requirements of paragraphs 7 and 9, an entity may apply the requirements in the last sentence of HKAS 39 paragraph AG76 and in paragraph AG76A, in either of the following ways:

(a) prospectively to transactions entered into on or after the date of transition to HKFRSs ~~25 October 2002; or~~

(b) ~~prospectively to transactions entered into after 1 January 2004.~~

A heading and paragraphs D26–D30 are added.

### **Severe hyperinflation**

D26 If an entity has a functional currency that was, or is, the currency of a hyperinflationary economy, it shall determine whether it was subject to severe hyperinflation before the date of transition to HKFRSs. This applies to entities that are adopting HKFRSs for the first time, as well as entities that have previously applied HKFRSs.

D27 The currency of a hyperinflationary economy is subject to severe hyperinflation if it has both of the following characteristics:

(a) a reliable general price index is not available to all entities with transactions and balances in the currency.

(b) exchangeability between the currency and a relatively stable foreign currency does not exist.

D28 The functional currency of an entity ceases to be subject to severe hyperinflation on the functional currency normalisation date. That is the date when the functional currency no longer has either, or both, of the characteristics in paragraph D27, or when there is a change in the entity's functional currency to a currency that is not subject to severe hyperinflation.

D29 When an entity's date of transition to HKFRSs is on, or after, the functional currency normalisation date, the entity may elect to measure all assets and liabilities held before the functional currency normalisation date at fair value on the date of transition to HKFRSs. The entity may use that fair value as the deemed cost of those assets and liabilities in the opening HKFRS statement of financial position.

D30 When the functional currency normalisation date falls within a 12-month comparative period, the comparative period may be less than 12 months, provided that a complete set of financial statements (as required by paragraph 10 of HKAS 1) is provided for that shorter period.

## Effective date

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Paragraph 39H is added.

39H *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (Amendments to HKFRS 1), issued in December 2010, amended paragraphs B2, D1 and D20 and added paragraphs 31C and D26–D30. An entity shall apply those amendments for annual periods beginning on or after 1 July 2011. Earlier application is permitted.

HKFRS 1 (Revised) BC  
Revised February–December 2010

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Effective for annual periods  
beginning on or after 1 July 2009

*Basis for Conclusions on  
Hong Kong Financial Reporting Standards 1 (Revised)*

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# First-time Adoption of Hong Kong Financial Reporting Standards



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## **Amendments to HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards*—Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (issued in December 2010) - effective for annual periods beginning on or after 1 July 2011**

Paragraphs BC22A and BC83A are amended (new text is underlined and deleted text is struck through) and a heading and paragraphs BC63F–BC63J are added.

**BC22A** The Board reconsidered this issue in completing the revision of IAS 39 in 2003. The Board decided to retain the transition requirements as set out in IFRS 1, for the reasons given in paragraph BC20. However, the Board amended the date from which prospective application was required to transactions that occur on or after 1 January 2004 in order to overcome the practical difficulties of restating transactions that had been derecognised before that date. In 2010 the Board was asked to reconsider whether 1 January 2004 is the appropriate date from which a first-time adopter should be required to restate past derecognition transactions. Constituents were concerned that, as time passes, the fixed transition date of 1 January 2004 becomes more remote and increasingly less relevant to the financial reports as additional jurisdictions adopt IFRSs. The Board accepted that the cost of reconstructing transactions back in time to 1 January 2004 was likely to outweigh the benefit to be achieved in doing so. It therefore amended the fixed date of 1 January 2004 in paragraph B2 to ‘the date of transition to IFRSs’. The Board also amended the wording of the illustration in paragraph B2, in order to clarify that it is providing an example.

### **Severe hyperinflation**

**BC63F** In 2010 the Board was asked to clarify how an entity should resume presenting financial statements in accordance with IFRSs after a period of severe hyperinflation, during which the entity had been unable to comply with IAS 29 *Financial Reporting in Hyperinflationary Economies*. An entity would be unable to comply with IAS 29 if a reliable general price index is not available to all entities with that same functional currency, and exchangeability between the currency and a relatively stable foreign currency does not exist. However, once the functional currency changes to a non-hyperinflationary currency, or the currency ceases to be severely hyperinflationary, an entity would be able to start applying IFRSs to subsequent transactions.

**BC63G** The Board noted that IFRSs did not provide sufficient guidance in these circumstances. The Board therefore decided to amend IFRS 1 to provide guidance on how an entity can present IFRS financial statements after its currency ceases to be severely hyperinflationary, by presenting an opening IFRS statement of financial position on or after the functional currency normalisation date. The Board believed that allowing an entity to apply the exemption when presenting an opening IFRS statement of financial position after, and not just on, the functional currency normalisation date, would address practical concerns that may arise if the functional currency normalisation date and the entity’s date of transition to IFRSs are different. The Board decided that this amendment would also be available to entities that were emerging from a period of severe hyperinflation but had not applied IFRSs in the past.

**BC63H** The Board decided to permit an entity emerging from a period of severe hyperinflation to elect to measure its assets and liabilities at fair value. That fair value could then be used as the deemed cost in its opening IFRS statement of financial position. The Board believed that this approach would expand the scope of the deemed cost exemptions in IFRS 1 to enable them to be applied in these specific circumstances. However, because severe hyperinflation is a specific set of circumstances, the Board wanted to ensure that the fair value measurement option was applied only to those assets and liabilities that were held before the functional currency normalisation date, and not to other assets and liabilities held by the entity at the time it made the transition to IFRSs. Furthermore, where a parent entity’s functional currency has been subject to severe hyperinflation, but its subsidiary company’s functional currency has not been subject to severe hyperinflation, the Board decided it was inappropriate for such a subsidiary company to be able to apply this exemption.



BC63I The Board decided that any adjustments arising on electing to measure assets and liabilities at fair value in the opening IFRS statement of financial position arise from events and transactions before the date of transition to IFRSs. Consequently, those adjustments should be accounted for in accordance with paragraph 11 of IFRS 1, and an entity should recognise those adjustments directly in retained earnings (or, if appropriate, in another category of equity) at the date of transition to IFRSs.

BC63J The Board observed that entities are required to apply paragraph 21 of IFRS 1 and prepare and present comparative information in accordance with IFRSs. The Board noted that preparation of information in accordance with IFRSs for periods before the functional currency normalisation date may not be possible; hence the exemption refers to a date of transition on or after the functional currency normalisation date. This may lead to a comparative period of less than 12 months. The Board identified that entities should consider whether disclosure of non-IFRS comparative information and historical summaries, in accordance with paragraph 22 of IFRS 1, would provide useful information to users of financial statements. The Board also noted that an entity should clearly explain the transition to IFRSs in accordance with paragraphs 23–28.

BC83A IFRS 1 originally required retrospective application of the 'day 1' gain or loss recognition requirements in IAS 39 paragraph AG76. After the revised IAS 39 was issued, constituents raised concerns that retrospective application would diverge from the requirements of US GAAP, would be difficult and expensive to implement, and might require subjective assumptions about what was observable and what was not. In response to these concerns, the Board permitted entities to apply the requirements in the last sentence of IAS 39 paragraph AG76 and in paragraph AG76A, in any one of the following ways:

- (a) retrospectively;
- (b) prospectively to transactions entered into after 25 October 2002; or
- (c) prospectively to transactions entered into after 1 January 2004.

In 2010 the Board was asked to reconsider whether the fixed dates of 25 October 2002 and 1 January 2004 continued to be appropriate for first-time adopters. Constituents were concerned that, as time passes, these fixed dates become more remote and increasingly less relevant to the financial reports as additional jurisdictions adopt IFRSs. The Board accepted that the cost of reconstructing transactions back in time to 25 October 2002 or 1 January 2004 was likely to outweigh the benefit to be achieved in doing so. It therefore amended the fixed dates included in paragraph D20 of IFRS 1 to permit a first-time adopter to apply the 'day 1' gain or loss recognition requirement in IAS 39 paragraphs AG76 and AG76A prospectively from 'the date of transition to IFRSs'.\*

\* IFRS 9 *Financial Instruments* issued in October 2010 incorporated the guidance from paragraphs AG76 and AG76A of IAS 39 into paragraphs B5.4.8 and B5.4.9 of IFRS 9 respectively.

HKFRS 9  
Revised ~~November~~ December 2010

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Effective for annual periods  
beginning on or after 1 January 2013

*Hong Kong Financial Reporting Standard 9*

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# Financial Instruments



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## Derecognition of financial assets and financial liabilities

- B2 Except as permitted by paragraph B3, a first-time adopter shall apply the derecognition requirements in HKFRS 9 *Financial Instruments* prospectively for transactions occurring on or after ~~1 January 2004~~ the date of transition to IFRSs. ~~In other words~~ For example, if a first-time adopter derecognised non-derivative financial assets or non-derivative financial liabilities in accordance with its previous GAAP as a result of a transaction that occurred before ~~1 January 2004~~ the date of transition to IFRSs, it shall not recognise those assets and liabilities in accordance with HKFRSs (unless they qualify for recognition as a result of a later transaction or event).
- B3 Despite paragraph B2, an entity may apply the derecognition requirements in HKFRS 9 retrospectively from a date of the entity's choosing, provided that the information needed to apply HKFRS 9 to financial assets and financial liabilities derecognised as a result of past transactions was obtained at the time of initially accounting for those transactions.

## Hedge accounting

- B4 As required by HKFRS 9, at the date of transition to HKFRSs an entity shall:
- (a) measure all derivatives at fair value; and
  - (b) eliminate all deferred losses and gains arising on derivatives that were reported in accordance with previous GAAP as if they were assets or liabilities.
- B5 An entity shall not reflect in its opening HKFRS statement of financial position a hedging relationship of a type that does not qualify for hedge accounting in accordance with HKAS 39 (for example, many hedging relationships where the hedging instrument is a cash instrument or written option; or where the hedged item is a net position). However, if an entity designated a net position as a hedged item in accordance with previous GAAP, it may designate an individual item within that net position as a hedged item in accordance with HKFRSs, provided that it does so no later than the date of transition to HKFRSs.

## Classification and measurement of financial assets

- B8 An entity shall assess whether a financial asset meets the conditions in paragraph 4.1.2 of HKFRS 9 on the basis of the facts and circumstances that exist at the date of transition to HKFRSs.

## Embedded derivatives

- B9 A first-time adopter shall assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative on the basis of the conditions that existed at the later of the date it first became a party to the contract and the date a reassessment is required by paragraph B4.3.11 of HKFRS 9.
- C3 In Appendix D, paragraphs D1(j), D14, D15, D19 and D20 are amended to read as follows and paragraphs D19A–D19D are added:
- D1 An entity may elect to use one or more of the following exemptions:
- (a) ...

### Fair value measurement of financial assets or financial liabilities at initial recognition

D20 Despite the requirements of paragraphs 7 and 9, an entity may apply the requirements in the last sentence of paragraph B5.4.8 and in paragraph B5.4.9 of HKFRS 9, ~~in either of the following ways:~~

- ~~(a) prospectively to transactions entered into on or after the date of transition to IFRSs~~25 October 2002~~; or~~
- ~~(b) prospectively to transactions entered into after 1 January 2004.~~

C4 In Appendix E, a heading and paragraphs E1 and E2 are added:

### Exemption from the requirement to restate comparative information for HKFRS 9

E1 In its first HKFRS financial statements, an entity that (a) adopts HKFRSs for annual periods beginning before 1 January 2012 and (b) applies HKFRS 9 shall present at least one year of comparative information. However, this comparative information need not comply with HKFRS 7 *Financial Instruments: Disclosures* or HKFRS 9, to the extent that the disclosures required by HKFRS 7 relate to items within the scope of HKFRS 9. For such entities, references to the 'date of transition to HKFRSs' shall mean, in the case of HKFRS 7 and HKFRS 9 only, the beginning of the first HKFRS reporting period.

E2 An entity that chooses to present comparative information that does not comply with HKFRS 7 and HKFRS 9 in its first year of transition shall:

- (a) apply the recognition and measurement requirements of its previous GAAP in place of the requirements of HKFRS 9 to comparative information about items within the scope of HKFRS 9.
- (b) disclose this fact together with the basis used to prepare this information.
- (c) treat any adjustment between the statement of financial position at the comparative period's reporting date (ie the statement of financial position that includes comparative information under previous GAAP) and the statement of financial position at the start of the *first HKFRS reporting period* (ie the first period that includes information that complies with HKFRS 7 and HKFRS 9) as arising from a change in accounting policy and give the disclosures required by paragraph 28(a)–(e) and (f)(i) of HKAS 8. Paragraph 28(f)(i) applies only to amounts presented in the statement of financial position at the comparative period's reporting date.
- (d) apply paragraph 17(c) of HKAS 1 to provide additional disclosures when compliance with the specific requirements in HKFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

### HKFRS 3 *Business Combinations*

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C5 Paragraphs 16, 42, 53, 56 and 58(b) are amended to read as follows, paragraph 64A is deleted and paragraph 64D is added: