

MEMBERS' HANDBOOK

Update No. 193

(Issued 29 December 2016)

VOLUME II

The following amendments were previously set out in the Appendix to the Standards as they were not yet effective. These amendments are applicable for annual financial reporting periods beginning on or after 1 January 2016.

- *Disclosure Initiative* (Amendments to HKAS 1 *Presentation of Financial Statements*) are designed to further encourage companies to apply professional judgement in determining what information to disclose in their financial statements. Furthermore, the amendments clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures.
- *Accounting for Acquisitions of Interests in Joint Operations* (Amendments to HKFRS 11 *Joint Arrangements*) addresses the accounting for interests in joint ventures and joint operations. The amendments add new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business. The amendments specify the appropriate accounting treatment for such acquisitions.
- *Annual Improvements to HKFRSs 2012-2014 Cycle* is a series of amendments to HKFRSs in response to the International Accounting Standards Board's annual improvements project to make necessary, but non-urgent, amendments to HKFRSs that will not be included as part of any other project.

Document Reference and Title	Instructions	Explanations
Contents of Volume II	Insert the revised pages i - ii. Discard the replaced pages i - ii.	Revised contents pages

HONG KONG ACCOUNTING STANDARDS (HKAS)

HKAS 1 <i>Presentation of Financial Statements</i>	Replace the cover page and pages 2, 4, 11, 14-15, 19-21, 26, 31-32, 37, 56-57, 65, 67-68, 73-74, 78, 88, 91-94 and 105A-105B with the revised cover page and revised pages 2, 4, 11,	Amendments due to <i>Disclosure Initiative</i>
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14-15, 19-21, 26, 31-32, 37, 56-57, 65, 67-68, 73-74, 78, 88, 91-94 and 105A-105B. Insert page 26A after page 26, pages 65A-65B after page 65, page 67A after page 67, page 74A after page 74, page 78A after page 78 and page 83A after page 83. Discard Pages 55A-55G, 85A-G and pages 105C-105F.

[HKAS 19 \(2011\)](#)
[Employee Benefits](#)

Replace the cover page and pages 4-5, 29, 47, 54, 89, 91 and 117 with the revised cover page and revised pages 4-5, 29, 47, 54, 89, 91 and 117. Insert pages 91A-91C after page 91.

Amendments due to *Annual Improvements to HKFRSs 2012-2014 Cycle*

[HKAS 34](#)
[Interim Financial Reporting](#)

Replace the cover page and pages 2-3, 6, 8 and 13 with the revised cover page and revised pages 2-3, 6, 8 and 13. Insert page 13A after page 13 and page 14A after page 14.

Amendments due to
- *Disclosure Initiative*
- *Annual Improvements to HKFRSs 2012-2014 Cycle*

[HKAS 36](#)
[Impairment of Assets](#)

Replace the cover page and pages 2 and 14 with the revised cover page and revised pages 2 and 14.

Amendments due to *Accounting for Acquisitions of Interests in Joint Operations*

HONG KONG FINANCIAL REPORTING STANDARDS (HKFRS)

[HKFRS 1 \(Revised\)](#)
[First-time Adoption of Hong Kong Financial Reporting Standards \(Standard\)](#)

Replace the cover page and pages 15, 21, 25 and 30 with the revised cover page and revised pages 15, 21, 25 and 30.

Amendments due to
- *Accounting for Acquisitions of Interests in Joint Operations*

[HKFRS 1 \(Revised\)](#)
[First-time Adoption of Hong Kong Financial Reporting Standards \(Basis for Conclusions\)](#)

Replace the cover page and pages 3 and 34 with the revised cover page and revised pages 3 and 34.

- *Annual Improvements to HKFRSs 2012-2014 Cycle*

[HKFRS 4](#)
[Insurance Contracts \(Revised Guidance on Implementing\)](#)

Replace the cover page and pages 2 and 25-26 with the revised cover page and revised pages 2 and 25-26.

Amendments due to *Disclosure Initiative*

[HKFRS 5](#)
[Non-current Assets Held for Sale and Discontinued Operations \(Standard\)](#)

Replace the cover page and pages 2-3, 11-12 and 16 with the revised cover page and revised pages 2-3, 11-12 and 16. Insert page 12A after page 12 and page 16A after page 16.

Amendments due to *Accounting for Acquisitions of Interests in Joint Operations*

<p><u>HKFRS 5</u> <u>Non-current Assets Held for Sale and Discontinued Operations</u> <u>(Basis for Conclusions)</u></p>	<p>Replace the cover page and pages 2 and 17-17A with the revised cover page and revised pages 2 and 17-17A. Insert page 2A after page 2 and pages 17B-17C after page 17A.</p>	
<p><u>HKFRS 7</u> <u>Financial Instruments: Disclosures</u> <u>(Standard)</u></p>	<p>Replace the cover page and pages 2, 13, 23-24, 29 and 35 with the revised cover page and revised pages 2, 13, 23-24, 29 and 35. Insert page 35A after page 35.</p>	<p>Amendments due to</p> <ul style="list-style-type: none"> - <i>Disclosure Initiative</i> - <i>Annual Improvements to HKFRSs 2012-2014 Cycle</i>
<p><u>HKFRS 7</u> <u>Financial Instruments: Disclosures</u> <u>(Basis for Conclusions)</u></p>	<p>Replace the cover page and pages 3 and 31-34 with the revised cover page and revised pages 3 and 31-34. Insert pages 35-36 after page 34.</p>	
<p><u>HKFRS 8</u> <u>Operating Segments</u> <u>(Guidance on Implementing)</u></p>	<p>Replace the cover page and page 3 with the revised cover page and revised page 3.</p>	<p>Amendments due to <i>Disclosure Initiative</i></p>
<p><u>HKFRS 11</u> <u>Joint Arrangements</u> <u>(Standard)</u></p>	<p>Replace the cover page and pages 2-5, 8 and 23-31 with the revised cover page and revised pages 2-5, 8 and 23-31. Discard page 29A and pages 32-43.</p>	<p>Amendments due to <i>Accounting for Acquisitions of Interests in Joint Operations</i></p>
<p><u>HKFRS 11</u> <u>Joint Arrangements</u> <u>(Basis for Conclusions)</u></p>	<p>Replace the cover page and pages 2-3, 12, and 16-21 with the revised cover page and revised pages 2-3, 12, and 16-21. Insert pages 12A-12C after page 12. Discard pages 16A, 20A and pages 22-27.</p>	
<p><u>HKFRS 11</u> <u>Joint Arrangements</u> <u>(Illustrative Examples)</u></p>	<p>Replace the cover page and pages 2 and 10-14 with the revised cover page and revised pages 2 and 10-14. Discard page 15.</p>	
<p><i>Annual Improvements to HKFRSs 2012-2014 Cycle</i></p>	<p>Discard the document.</p>	<p>Amendments have been incorporated into relevant HKFRSs</p>

VOLUME III

<i>Document Reference and Title</i>	<i>Instructions</i>	<i>Explanations</i>
<u>Contents of Volume III</u>	Discard the existing pages i, iv and replace with the revised pages i, iv.	Revised contents page

HONG KONG STANDARDS ON INVESTMENT CIRCULAR REPORTING ENGAGEMENTS

<u>HKSIR 200 Accountants' Reports on Historical Financial Information in Investment Circulars</u>	Insert before HKSIR 400 (Revised).	Note 1
<u>HKSIR 400 (Revised) Comfort Letters and Due Diligence Meetings</u>	Discard HKSIR 400 issued in October 2005 and revised in December 2012 and replace with HKSIR 400 (Revised).	Note 2

Notes:

1. The key objective of the new HKSIR 200 is to provide an up to date guidance to the profession for the preparation of an accountants' report under the current Listing Rules of The Stock Exchange of Hong Kong Limited by codifying existing practice. HKSIR 200 is effective for engagements where the investment circular is dated on or after 1 July 2017 and early application is permitted. The extant AG 3.340 will be superseded when HKSIR 200 becomes effective.
2. HKSIR 400 (Revised) is further revised to include guidance regarding oral due diligence and the key revisions are set out in Appendices 5A and 5B. The revisions made are effective upon issuance. In order for readers to easily identify all changes, a marked-up version is posted at:
http://www.hkicpa.org.hk/file/media/section6_standards/technical_resources/pdf-file/handbook/trackstds193.pdf



MEMBERS' HANDBOOK CONTENTS OF VOLUME II

(Updated to December 2016)

		<i>Issue/(Review date)</i>
PREFACE AND FRAMEWORK		
PREFACE	Preface to Hong Kong Financial Reporting Standards	10/06(4/15)
CONCEPTUAL FRAMEWORK	Conceptual Framework for Financial Reporting	10/10
HONG KONG ACCOUNTING STANDARDS (HKAS)		
HKAS 1 Revised	Presentation of Financial Statements	12/07 (12/16)
HKAS 2	Inventories	3/04(2/14)
HKAS 7	Statement of Cash Flows	12/04(6/16)
HKAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	9/04(2/14)
HKAS 10	Events after the Reporting Period	3/04(2/14)
HKAS 11	Construction Contracts	12/04(3/10)
HKAS 12	Income Taxes	11/04(6/16)
HKAS 16	Property, Plant and Equipment	11/05(11/16)
HKAS 17	Leases	12/04(2/14)
HKAS 18	Revenue	11/04(5/14)
HKAS 19 (2011)	Employee Benefits	7/11(12/16)
HKAS 20	Accounting for Government Grants and Disclosure of Government Assistance	12/04(2/14)
HKAS 21	The Effects of Changes in Foreign Exchange Rates	3/04(5/14)
HKAS 23 Revised	Borrowing Costs	6/07(3/10)
HKAS 24 Revised	Related Party Disclosures	11/09 (11/16)
HKAS 26	Accounting and Reporting by Retirement Benefit Plans	8/04
HKAS 27 (2011)	Separate Financial Statements	6/11(09/14)
HKAS 28 (2011)	Investments in Associates and Joint Ventures	6/11(1/16)

		<i>Issue/(Review date)</i>
HKAS 29	Financial Reporting in Hyperinflationary Economies	3/04(4/10)
HKAS 32	Financial Instruments: Presentation	11/04(11/14)
HKAS 33	Earnings per Share	3/04(5/14)
HKAS 34	Interim Financial Reporting	10/04(12/16)
HKAS 36	Impairment of Assets	8/04(12/16)
HKAS 37	Provisions, Contingent Liabilities and Contingent Assets	11/04(11/16)
HKAS 38	Intangible Assets	8/04(11/16)
HKAS 39	Financial Instruments: Recognition and Measurement	1/06(11/16)
HKAS 40	Investment Property	11/05(11/16)
HKAS 41	Agriculture	12/04(8/14)
HONG KONG FINANCIAL REPORTING STANDARDS (HKFRS)		
HKFRS 1 Revised	First-time Adoption of Hong Kong Financial Reporting Standards	12/08(12/16)
HKFRS 2	Share-based Payment	4/04(11/16)
HKFRS 3 Revised	Business Combinations	3/08(11/16)
HKFRS 4	Insurance Contracts	3/06(12/16)
HKFRS 5	Non-current Assets Held for Sale and Discontinued Operations	8/04(12/16)
HKFRS 6	Exploration for and Evaluation of Mineral Resources	2/05(2/10)
HKFRS 7	Financial Instruments: Disclosures	9/05(12/16)
HKFRS 8	Operating Segments	3/07(12/16)
HKFRS 9	Financial Instruments	11/09 (09/14)
HKFRS 9	Financial Instruments (Hedge Accounting)	12/13
HKFRS 9 (2014)	Financial Instruments	09/14
HKFRS 10	Consolidated Financial Statements	6/11(1/16)
HKFRS 11	Joint Arrangements	6/11(12/16)
HKFRS 12	Disclosure of Interests in Other Entities	6/11(1/15)
HKFRS 13	Fair Value Measurement	6/11(11/16)
HKFRS 14	Regulatory Deferral Accounts	2/14
HKFRS 15	Revenue from Contracts with Customers	7/14(6/16)
HKFRS 16	Leases	5/16

HKAS 1 (Revised)
Revised January 2015 December 2016

Effective for annual periods
beginning on or after 1 January 2009

Hong Kong Accounting Standard 1 (Revised)

Presentation of Financial Statements



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

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Notes	112
Structure	112
Disclosure of accounting policies	117
Sources of estimation uncertainty	125
Capital	134
Puttable financial instruments classified as equity	136A
Other disclosures	137
TRANSITION AND EFFECTIVE DATE	139
WITHDRAWAL OF HKAS 1 (ISSUED 2004)	140
APPENDICES:	
A Amendments to other pronouncements	
B Comparison with International Accounting Standards	
C Notes on legal requirements in Hong Kong	
BASIS FOR CONCLUSIONS	
APPENDIX:	
Amendments to the Basis for Conclusions on other IFRSs	
DISSENTING OPINIONS	
IMPLEMENTATION GUIDANCE	
APPENDICES:	
Amendments to guidance on other IFRSs	
Amendments to the guidance on implementing IAS 1 <i>Disclosure Initiative</i>	
TABLE OF CONCORDANCE	

Hong Kong Accounting Standard 1 *Presentation of Financial Statements* (HKAS 1) is set out in paragraphs 1–140 and Appendix A. All the paragraphs have equal authority. HKAS 1 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Conceptual Framework for Financial Reporting*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

This revised Standard was issued in December 2007 and revised in ~~January 2015~~ December 2016. It supersedes HKAS 1, issued in 2004, as amended in 2005.

- (e) **notes, comprising a ~~summary of~~ significant accounting policies and other explanatory information; and**
- (ea) **comparative information in respect of the preceding period as specified in paragraphs 38 and 38A; and**
- (f) **a statement of financial position as at the beginning of the preceding period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements in accordance with paragraphs 40A - 40D.**

An entity may use titles for the statements other than those used in this Standard. For example, an entity may use the title 'statement of comprehensive income' instead of 'statement of profit or loss and other comprehensive income'.

- 10A An entity may present a single statement of profit or loss and other comprehensive income, with profit or loss and other comprehensive income presented in two sections. The sections shall be presented together, with the profit or loss section presented first followed directly by the other comprehensive income section. An entity may present the profit or loss section in a separate statement of profit or loss. If so, the separate statement of profit or loss shall immediately precede the statement presenting comprehensive income, which shall begin with profit or loss.**
- 11 An entity shall present with equal prominence all of the financial statements in a complete set of financial statements.**
- 12 [Deleted]
- 13 Many entities present, outside the financial statements, a financial review by management that describes and explains the main features of the entity's financial performance and financial position, and the principal uncertainties it faces. Such a report may include a review of:
- (a) the main factors and influences determining financial performance, including changes in the environment in which the entity operates, the entity's response to those changes and their effect, and the entity's policy for investment to maintain and enhance financial performance, including its dividend policy;
 - (b) the entity's sources of funding and its targeted ratio of liabilities to equity; and
 - (c) the entity's resources not recognised in the statement of financial position in accordance with HKFRSs.
- 14 Many entities also present, outside the financial statements, reports and statements such as environmental reports and value added statements, particularly in industries in which environmental factors are significant and when employees are regarded as an important user group. Reports and statements presented outside financial statements are outside the scope of HKFRSs.

Going concern

- 25** When preparing financial statements, management shall make an assessment of an entity's ability to continue as a going concern. An entity shall prepare financial statements on a going concern basis unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so. When management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity shall disclose those uncertainties. When an entity does not prepare financial statements on a going concern basis, it shall disclose that fact, together with the basis on which it prepared the financial statements and the reason why the entity is not regarded as a going concern.
- 26 In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the end of the reporting period. The degree of consideration depends on the facts in each case. When an entity has a history of profitable operations and ready access to financial resources, the entity may reach a conclusion that the going concern basis of accounting is appropriate without detailed analysis. In other cases, management may need to consider a wide range of factors relating to current and expected profitability, debt repayment schedules and potential sources of replacement financing before it can satisfy itself that the going concern basis is appropriate.

Accrual basis of accounting

- 27** An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting.
- 28 When the accrual basis of accounting is used, an entity recognises items as assets, liabilities, equity, income and expenses (the elements of financial statements) when they satisfy the definitions and recognition criteria for those elements in the *Framework*.

Materiality and aggregation

- 29** An entity shall present separately each material class of similar items. An entity shall present separately items of a dissimilar nature or function unless they are immaterial.
- 30 Financial statements result from processing large numbers of transactions or other events that are aggregated into classes according to their nature or function. The final stage in the process of aggregation and classification is the presentation of condensed and classified data, which form line items in the financial statements. If a line item is not individually material, it is aggregated with other items either in those statements or in the notes. An item that is not sufficiently material to warrant separate presentation in those statements may warrant separate presentation in the notes.
- 30A When applying this and other HKFRSs an entity shall decide, taking into consideration all relevant facts and circumstances, how it aggregates information in the financial statements, which include the notes. An entity shall not reduce the understandability of its financial statements by obscuring material information with immaterial information or by aggregating material items that have different natures or functions.
- 31 Some HKFRSs specify information that is required to be included in the financial statements, which include the notes. An entity need not provide a specific disclosure required by a HKFRS if the information resulting from that disclosure is not material. This is the case even if the HKFRS contains a list of specific requirements or describes them as minimum requirements. An entity shall also consider whether to provide additional disclosures when compliance with the specific requirements in HKFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

* replaced by the *Conceptual Framework* in October 2010.

Offsetting

- 32 An entity shall not offset assets and liabilities or income and expenses, unless required or permitted by an HKFRS.**
- 33 An entity reports separately both assets and liabilities, and income and expenses. Offsetting in the statement(s) of profit or loss and other comprehensive income or financial position, except when offsetting reflects the substance of the transaction or other event, detracts from the ability of users both to understand the transactions, other events and conditions that have occurred and to assess the entity's future cash flows. Measuring assets net of valuation allowances—for example, obsolescence allowances on inventories and doubtful debts allowances on receivables—is not offsetting.
- 34 HKAS 18 *Revenue* defines revenue and requires an entity to measure it at the fair value of the consideration received or receivable, taking into account the amount of any trade discounts and volume rebates the entity allows. An entity undertakes, in the course of its ordinary activities, other transactions that do not generate revenue but are incidental to the main revenue-generating activities. An entity presents the results of such transactions, when this presentation reflects the substance of the transaction or other event, by netting any income with related expenses arising on the same transaction. For example:
- (a) an entity presents gains and losses on the disposal of non-current assets, including investments and operating assets, by deducting from the proceeds on disposal the carrying amount of the asset and related selling expenses; and
 - (b) an entity may net expenditure related to a provision that is recognised in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and reimbursed under a contractual arrangement with a third party (for example, a supplier's warranty agreement) against the related reimbursement.
- 35 In addition, an entity presents on a net basis gains and losses arising from a group of similar transactions, for example, foreign exchange gains and losses or gains and losses arising on financial instruments held for trading. However, an entity presents such gains and losses separately if they are material.

Frequency of reporting

- 36 An entity shall present a complete set of financial statements (including comparative information) at least annually. When an entity changes the end of its reporting period and presents financial statements for a period longer or shorter than one year, an entity shall disclose, in addition to the period covered by the financial statements:**
- (a) the reason for using a longer or shorter period, and
 - (b) the fact that amounts presented in the financial statements are not entirely comparable.
37. Normally, an entity consistently prepares financial statements for a one-year period. However, for practical reasons, some entities prefer to report, for example, for a 52-week period. This Standard does not preclude this practice.

Comparative information*Minimum comparative information*

- 38 Except when HKFRSs permit or require otherwise, an entity shall present comparative information in respect of the preceding period for all amounts reported in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information if it is relevant to an understanding of the current period's financial statements.**

- 52 An entity meets the requirements in paragraph 51 by presenting appropriate headings for pages, statements, notes, columns and the like. Judgement is required in determining the best way of presenting such information. For example, when an entity presents the financial statements electronically, separate pages are not always used; an entity then presents the above items to ensure that the information included in the financial statements can be understood.
- 53 An entity often makes financial statements more understandable by presenting information in thousands or millions of units of the presentation currency. This is acceptable as long as the entity discloses the level of rounding and does not omit material information.

Statement of financial position

Information to be presented in the statement of financial position

- 54 ~~As a minimum, the~~ **The statement of financial position shall include line items that present the following amounts:**
- (a) **property, plant and equipment;**
 - (b) **investment property;**
 - (c) **intangible assets;**
 - (d) **financial assets (excluding amounts shown under (e), (h) and (i));**
 - (e) **investments accounted for using the equity method;**
 - (f) **biological assets;**
 - (g) **inventories;**
 - (h) **trade and other receivables;**
 - (i) **cash and cash equivalents;**
 - (j) **the total of assets classified as held for sale and assets included in disposal groups classified as held for sale in accordance with HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*;**
 - (k) **trade and other payables;**
 - (l) **provisions;**
 - (m) **financial liabilities (excluding amounts shown under (k) and (l));**
 - (n) **liabilities and assets for current tax, as defined in HKAS 12 *Income Taxes*;**
 - (o) **deferred tax liabilities and deferred tax assets, as defined in HKAS 12;**
 - (p) **liabilities included in disposal groups classified as held for sale in accordance with HKFRS 5;**
 - (q) **non-controlling interests, presented within equity; and**
 - (r) **issued capital and reserves attributable to owners of the parent.**

- 55** **An entity shall present additional line items (including by disaggregating the line items listed in paragraph 54), headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position.**
- 55A** When an entity presents subtotals in accordance with paragraph 55, those subtotals shall:
- (a) be comprised of line items made up of amounts recognised and measured in accordance with HKFRS;
 - (b) be presented and labelled in a manner that makes the line items that constitute the subtotal clear and understandable;
 - (c) be consistent from period to period, in accordance with paragraph 45; and
 - (d) not be displayed with more prominence than the subtotals and totals required in HKFRS for the statement of financial position.
- 56** **When an entity presents current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position, it shall not classify deferred tax assets (liabilities) as current assets (liabilities).**
- 57** This Standard does not prescribe the order or format in which an entity presents items. Paragraph 54 simply lists items that are sufficiently different in nature or function to warrant separate presentation in the statement of financial position. In addition:
- (a) line items are included when the size, nature or function of an item or aggregation of similar items is such that separate presentation is relevant to an understanding of the entity's financial position; and
 - (b) the descriptions used and the ordering of items or aggregation of similar items may be amended according to the nature of the entity and its transactions, to provide information that is relevant to an understanding of the entity's financial position. For example, a financial institution may amend the above descriptions to provide information that is relevant to the operations of a financial institution.
- 58** An entity makes the judgement about whether to present additional items separately on the basis of an assessment of:
- (a) the nature and liquidity of assets;
 - (b) the function of assets within the entity; and
 - (c) the amounts, nature and timing of liabilities.
- 59** The use of different measurement bases for different classes of assets suggests that their nature or function differs and, therefore, that an entity presents them as separate line items. For example, different classes of property, plant and equipment can be carried at cost or at revalued amounts in accordance with HKAS 16.
- Current/non-current distinction**
- 60** **An entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position in accordance with paragraphs 66–76 except when a presentation based on liquidity provides information that is reliable and more relevant. When that exception applies, an entity shall present all assets and liabilities in order of liquidity.**
- 61** **Whichever method of presentation is adopted, an entity shall disclose the amount expected to be recovered or settled after more than twelve months for each asset and liability line item that combines amounts expected to be recovered or settled:**
- (a) **no more than twelve months after the reporting period, and**
 - (b) **more than twelve months after the reporting period.**

- 62 When an entity supplies goods or services within a clearly identifiable operating cycle, separate classification of current and non-current assets and liabilities in the statement of financial position provides useful information by distinguishing the net assets that are continuously circulating as working capital from those used in the entity's long-term operations. It also highlights assets that are expected to be realised within the current operating cycle, and liabilities that are due for settlement within the same period.
- 63 For some entities, such as financial institutions, a presentation of assets and liabilities in increasing or decreasing order of liquidity provides information that is reliable and more relevant than a current/ non-current presentation because the entity does not supply goods or services within a clearly identifiable operating cycle.
- 64 In applying paragraph 60, an entity is permitted to present some of its assets and liabilities using a current/non-current classification and others in order of liquidity when this provides information that is reliable and more relevant. The need for a mixed basis of presentation might arise when an entity has diverse operations.
- 65 Information about expected dates of realisation of assets and liabilities is useful in assessing the liquidity and solvency of an entity. HKFRS 7 *Financial Instruments: Disclosures* requires disclosure of the maturity dates of financial assets and financial liabilities. Financial assets include trade and other receivables, and financial liabilities include trade and other payables. Information on the expected date of recovery of non-monetary assets such as inventories and expected date of settlement for liabilities such as provisions is also useful, whether assets and liabilities are classified as current or as non-current. For example, an entity discloses the amount of inventories that are expected to be recovered more than twelve months after the reporting period.

Current assets

- 66 **An entity shall classify an asset as current when:**
- (a) **it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle;**
 - (b) **it holds the asset primarily for the purpose of trading;**
 - (c) **it expects to realise the asset within twelve months after the reporting period; or**
 - (d) **the asset is cash or a cash equivalent (as defined in HKAS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.**

An entity shall classify all other assets as non-current.

- 67 This Standard uses the term 'non-current' to include tangible, intangible and financial assets of a long-term nature. It does not prohibit the use of alternative descriptions as long as the meaning is clear.
- 68 The operating cycle of an entity is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. When the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months. Current assets include assets (such as inventories and trade receivables) that are sold, consumed or realised as part of the normal operating cycle even when they are not expected to be realised within twelve months after the reporting period. Current assets also include assets held primarily for the purpose of trading (examples include some financial assets classified as held for trading in accordance with HKAS 39) and the current portion of non-current financial assets.

Current liabilities

- 69 **An entity shall classify a liability as current when:**
- (a) **it expects to settle the liability in its normal operating cycle;**
 - (b) **it holds the liability primarily for the purpose of trading;**

Information to be presented in the other comprehensive income section

- 82A** ~~The other comprehensive income section shall present line items for the amounts of other comprehensive income in the period, classified by nature (including share of the other comprehensive income of associates and joint ventures accounted for using the equity method) and grouped into those that, in accordance with other HKFRSs for the period of:~~
- ~~(a) items of other comprehensive income (excluding amounts in paragraph (b)), classified by nature and grouped into those that, in accordance with other HKFRSs:~~
 - ~~(a)(i) will not be reclassified subsequently to profit or loss; and~~
 - ~~(b)(ii) will be reclassified subsequently to profit or loss when specific conditions are met.~~
 - ~~(b) the share of the other comprehensive income of associates and joint ventures accounted for using the equity method, separated into the share of items that, in accordance with other HKFRSs:~~
 - ~~(i) will not be reclassified subsequently to profit or loss; and~~
 - ~~(ii) will be reclassified subsequently to profit or loss when specific conditions are met.~~
- 83** [Deleted]
- 84** [Deleted]
- 85** **An entity shall present additional line items (including by disaggregating the line items listed in paragraph 82), headings and subtotals in the statement(s) presenting profit or loss and other comprehensive income when such presentation is relevant to an understanding of the entity's financial performance.**
- 85A** When an entity presents subtotals in accordance with paragraph 85, those subtotals shall:
- (a) be comprised of line items made up of amounts recognised and measured in accordance with HKFRS;
 - (b) be presented and labelled in a manner that makes the line items that constitute the subtotal clear and understandable;
 - (c) be consistent from period to period, in accordance with paragraph 45; and
 - (d) not be displayed with more prominence than the subtotals and totals required in HKFRS for the statement(s) presenting profit or loss and other comprehensive income.
- 85B** An entity shall present the line items in the statement(s) presenting profit or loss and other comprehensive income that reconcile any subtotals presented in accordance with paragraph 85 with the subtotals or totals required in HKFRS for such statement(s).
- 86** Because the effects of an entity's various activities, transactions and other events differ in frequency, potential for gain or loss and predictability, disclosing the components of financial performance assists users in understanding the financial performance achieved and in making projections of future financial performance. An entity includes additional line items in the statement(s) presenting profit or loss and other comprehensive income and it amends the descriptions used and the ordering of items when this is necessary to explain the elements of financial performance. An entity considers factors including materiality and the nature and function of the items of income and expense. For example, a financial institution may amend the descriptions to provide information that is relevant to the operations of a financial institution. An entity does not offset income and expense items unless the criteria in paragraph 32 are met.

- 87 An entity shall not present any items of income or expense as extraordinary items, in the statement(s) presenting profit or loss and other comprehensive income or in the notes.**

Profit or loss for the period

- 88 An entity shall recognise all items of income and expense in a period in profit or loss unless an HKFRS requires or permits otherwise.**

- (c) provide information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.
- 113 **An entity shall, as far as practicable, present notes in a systematic manner. In determining a systematic manner, the entity shall consider the effect on the understandability and comparability of its financial statements. An entity shall cross-reference each item in the statements of financial position and in the statement(s) of profit or loss and other comprehensive income, and in the statements of changes in equity and of cash flows to any related information in the notes.**
- 114 ~~An entity normally presents notes in the following order, to assist users to understand the financial statements and to compare them with financial statements of other entities: Examples of systematic ordering or grouping of the notes include:~~
- (a) giving prominence to the areas of its activities that the entity considers to be most relevant to an understanding of its financial performance and financial position, such as grouping together information about particular operating activities;
 - (b) grouping together information about items measured similarly such as assets measured at fair value; or
 - (c) following the order of the line items in the statement(s) of profit or loss and other comprehensive income and the statement of financial position, such as:
 - (a)(i) statement of compliance with HKFRSs (see paragraph 16);
 - (b)(ii) ~~summary of significant accounting policies applied (see paragraph 117);~~
 - (e)(iii) supporting information for items presented in the statements of financial position and in the statement(s) of profit or loss and other comprehensive income, and in the statements of changes in equity and of cash flows, in the order in which each statement and each line item is presented; and
 - (d)(iv) other disclosures, including:
 - (i)(1) contingent liabilities (see HKAS 37) and unrecognised contractual commitments;¹ and
 - (ii)(2) non-financial disclosures, eg the entity's financial risk management objectives and policies (see HKFRS 7).
- 115 ~~[Deleted] In some circumstances, it may be necessary or desirable to vary the order of specific items within the notes. For example, an entity may combine information on changes in fair value recognised in profit or loss with information on maturities of financial instruments, although the former disclosures relate to the statement(s) presenting profit or loss and other comprehensive income and the latter relate to the statement of financial position. Nevertheless, an entity retains a systematic structure for the notes as far as practicable.~~
- 116 An entity may present notes providing information about the basis of preparation of the financial statements and specific accounting policies as a separate section of the financial statements.
- Disclosure of accounting policies**
- 117 **An entity shall disclose in the summary of its significant accounting policies comprising:**
- (a) the measurement basis (or bases) used in preparing the financial statements, and

(b) the other accounting policies used that are relevant to an understanding of the financial statements.

- 118 It is important for an entity to inform users of the measurement basis or bases used in the financial statements (for example, historical cost, current cost, net realisable value, fair value or recoverable amount) because the basis on which an entity prepares the financial statements significantly affects users' analysis. When an entity uses more than one measurement basis in the financial statements, for example when particular classes of assets are revalued, it is sufficient to provide an indication of the categories of assets and liabilities to which each measurement basis is applied.
- 119 In deciding whether a particular accounting policy should be disclosed, management considers whether disclosure would assist users in understanding how transactions, other events and conditions are reflected in reported financial performance and financial position. Each entity considers the nature of its operations and the policies that the users of its financial statements would expect to be disclosed for that type of entity. Disclosure of particular accounting policies is especially useful to users when those policies are selected from alternatives allowed in HKFRSs. An example is disclosure of whether an entity applies the fair value or cost model to its investment property (see HKAS 40 *Investment Property*). Some HKFRSs specifically require disclosure of particular accounting policies, including choices made by management between different policies they allow. For example, HKAS 16 requires disclosure of the measurement bases used for classes of property, plant and equipment.
- 120 ~~[Deleted] Each entity considers the nature of its operations and the policies that the users of its financial statements would expect to be disclosed for that type of entity. For example, users would expect an entity subject to income taxes to disclose its accounting policies for income taxes, including those applicable to deferred tax liabilities and assets. When an entity has significant foreign operations or transactions in foreign currencies, users would expect disclosure of accounting policies for the recognition of foreign exchange gains and losses.~~
- 121 An accounting policy may be significant because of the nature of the entity's operations even if amounts for current and prior periods are not material. It is also appropriate to disclose each significant accounting policy that is not specifically required by HKFRSs but the entity selects and applies in accordance with HKAS 8.
- 122 **An entity shall disclose, ~~in the summary of~~ along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph 125), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.**
- 123 In the process of applying the entity's accounting policies, management makes various judgements, apart from those involving estimations, that can significantly affect the amounts it recognises in the financial statements. For example, management makes judgements in determining:
- (a) whether financial assets are held-to-maturity investments;
 - (b) when substantially all the significant risks and rewards of ownership of financial assets and lease assets are transferred to other entities; and
 - (c) whether, in substance, particular sales of goods are financing arrangements and therefore do not give rise to revenue.
- 124 Some of the disclosures made in accordance with paragraph 122 are required by other HKFRSs. For example, HKFRS 12 *Disclosure of Interests in Other Entities* requires an entity to disclose the judgements it has made in determining whether it controls another entity. HKAS 40 requires disclosure of the criteria developed by the entity to distinguish investment property from owner-occupied property and from property held for sale in the ordinary course of business, when classification of the property is difficult.

139L *Annual Improvements 2009–2011 Cycle*, issued in June 2012, amended paragraphs 10, 38 and 41, deleted paragraphs 39–40 and added paragraphs 38A–38D and 40A–40D. An entity shall apply that amendment retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.

139M-O [This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]

139P *Disclosure Initiative (Amendments to HKAS 1)*, issued in January 2015, amended paragraphs 10, 31, 54–55, 82A, 85, 113–114, 117, 119 and 122, added paragraphs 30A, 55A and 85A–85B and deleted paragraphs 115 and 120. An entity shall apply those amendments for annual periods beginning on or after 1 January 2016. Earlier application is permitted. Entities are not required to disclose the information required by paragraphs 28–30 of HKAS 8 in relation to these amendments.

Withdrawal of HKAS 1 (issued 2004)

140 This Standard supersedes HKAS 1 *Presentation of Financial Statements* issued in 2004, as amended in 2005.

BASIS FOR CONCLUSIONS ON IAS 1 PRESENTATION OF FINANCIAL STATEMENTS

This Basis for Conclusions accompanies, but is not part of, IAS 1.

HKAS 1 is based on IAS 1 *Presentation of Financial statements*. In approving HKAS 1, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IAS 1. Accordingly, there are no significant differences between HKAS 1 and IAS 1. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IAS 1 referred to below generally correspond with those in HKAS 1.

CONTENTS

from paragraph

BASIS FOR CONCLUSIONS ON IAS 1 PRESENTATION OF FINANCIAL STATEMENTS

INTRODUCTION	BC1
The Improvements project—revision of IAS 1 (2003)	BC2
Amendment to IAS 1— <i>Capital Disclosures</i> (2005)	BC5
Amendment to IAS 32 and IAS 1— <i>Puttable Financial Instruments and Obligations Arising on Liquidation</i> (2008)	BC6A
<i>Presentation of Items of Other Comprehensive Income</i> (Amendments to IAS 1)	BC6B
Financial statement presentation—Joint project	BC7
DEFINITIONS	BC11
General purpose financial statements	BC11
FINANCIAL STATEMENTS	BC14
Complete set of financial statements	BC14
Titles of financial statements	BC14
Equal prominence	BC22
Departures from IFRSs	BC23
<u>Materiality and aggregation</u>	<u>BC30A</u>
Comparative information	BC31
A statement of financial position as at the beginning of the earliest comparative period	BC31
Clarification of requirements for comparative information	BC32A
IAS 34 <i>Interim Financial Reporting</i>	BC33
Criterion for exemption from requirements	BC34
Reporting owner and non-owner changes in equity	BC37
STATEMENT OF FINANCIAL POSITION	BC38A
<u>Information to be presented in the statement of financial position</u>	<u>BC38A</u>
Current assets and current liabilities	BC38AH
Classification of the liability component of a convertible instrument	BC38EL
Effect of events after the reporting period on the classification of liabilities	BC39
STATEMENT OF COMPREHENSIVE INCOME	BC49
Reporting comprehensive income	BC49

Results of operating activities	BC55
Subtotal for profit or loss	BC57
Minority interest	BC59
Extraordinary items	BC60
Other comprehensive income—related tax effects	BC65
Reclassification adjustments	BC69
STATEMENT OF CHANGES IN EQUITY	BC74
Effects of retrospective application or retrospective restatement	BC74
Reconciliation for each component of other comprehensive income	BC74A
Presentation of dividends	BC75
STATEMENT OF CASH FLOWS	BC76
<i>IAS 7 Cash Flow Statements</i>	BC76
NOTES	BC776A
<u>Structure</u>	<u>BC76A</u>
<u>Disclosure of accounting policies</u>	<u>BC76F</u>
Disclosure of the judgements that management has made in the process of applying the entity's accounting policies	BC77
Disclosure of major sources of estimation uncertainty	BC79
Disclosures about capital	BC85
Objectives, policies and processes for managing capital	BC90
Externally imposed capital requirements	BC92
Internal capital targets	BC98
Puttable financial instruments and obligations arising on liquidation	BC100A
Presentation of measures per share	BC101
TRANSITION AND EFFECTIVE DATE	BC105
DIFFERENCES FROM SFAS 130	BC106
APPENDIX	
Amendments to the Basis for Conclusions on other IFRSs	
DISSENTING OPINIONS	
GUIDANCE ON IMPLEMENTING	
IAS 1 PRESENTATION OF FINANCIAL STATEMENTS	

- BC30 In view of the strict criteria for departure from a requirement in an IFRS, IAS 1 includes a rebuttable presumption that if other entities in similar circumstances comply with the requirement, the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the *Framework*.

Materiality and aggregation (paragraphs 29–31)

- BC30A The Board was informed at the Discussion Forum *Financial Reporting Disclosure* in January 2013, in its related survey and by other sources, that there are difficulties applying the concept of materiality in practice. Some are of the view that these difficulties contribute to a disclosure problem, namely, that there is both too much irrelevant information and not enough relevant information in financial statements. A number of factors have been identified for why materiality may not be applied well in practice. One of these is that the guidance on materiality in IFRS is not clear.
- BC30B Some think that the statement in IAS 1 that an entity need not provide a specific disclosure if the information is not material means that an entity does not need to present an item in the statement(s) of profit or loss and other comprehensive income, the statement of financial position, the statement of cash flows and the statement of changes in equity, but must instead disclose it in the notes. However, the Board noted that the concept of materiality is applicable to financial statements, which include the notes, and not only to those statements.
- BC30C Some are of the view that when IFRS states that a specific disclosure is required, the concept of materiality does not apply to those disclosure requirements, ie disclosures specifically identified in IFRS are required irrespective of whether they result in material information. In addition, some people think that when a line item is presented, or a material item is otherwise recognised, in the statement(s) of profit or loss and other comprehensive income and the statement of financial position, all the disclosures in IFRS specified for that item must be disclosed. The Board observed that paragraph 31 of IAS 1 is clear that the concept of materiality applies to specific disclosures required by an IFRS and therefore an entity does not have to disclose information required by an IFRS if that information would not be material.
- BC30D The Board understands that these misconceptions may have arisen because of the wording that is used when specifying presentation or disclosure requirements in IFRS; for example, the use of the words 'as a minimum'. For this reason, the Board removed the phrase 'as a minimum' in paragraph 54 of IAS 1, which lists line items for presentation in the statement of financial position. This also makes the requirement broadly consistent with the corresponding requirement in paragraph 82 of IAS 1 for the profit or loss section of the statement of comprehensive income or the statement of profit or loss.
- BC30E On the basis of its observations and conclusions set out in paragraphs BC30A–BC30D, the Board added a new paragraph, paragraph 30A, and amended paragraph 31 of IAS 1.
- BC30F Paragraph 30A was added to IAS 1 to highlight that when an entity decides how it aggregates information in the financial statements, it should take into consideration all relevant facts and circumstances. Paragraph 30A emphasises that an entity should not reduce the understandability of its financial statements by providing immaterial information that obscures the material information in financial statements or by aggregating material items that have different natures or functions. Obscuring material information with immaterial information in financial statements makes the material information less visible and therefore makes the financial statements less understandable. The amendments do not actually prohibit entities from disclosing immaterial information, because the Board thinks that such a requirement would not be operational; however, the amendments emphasise that disclosure should not result in material information being obscured.

- BC30G The Exposure Draft *Disclosure Initiative* (Proposed amendments to IAS 1) (the 'March 2014 Exposure Draft'), which was published in March 2014, also proposed that an entity should not 'disaggregate' information in a manner that obscures useful information. Disaggregation is often used to describe the process of expanding totals, subtotals and line items into further items that themselves may reflect the aggregated results of transactions or other events. Because the process of expanding totals, subtotals and line items is more likely to increase the transparency of information rather than obscuring it, the Board decided not to include the term disaggregation in paragraph 30A of IAS 1. In addition, the Board was of the view that items resulting from the process of disaggregation that themselves reflect the aggregated results of transactions would be covered by paragraphs 29–31 of IAS 1.
- BC30H The Board amended paragraph 31 of IAS 1 to highlight that materiality also applies to disclosures specifically required by IFRS. In addition, to highlight that materiality not only involves decisions about excluding information from the financial statements, the Board amended paragraph 31 to reiterate the notion already stated in paragraph 17(c) of IAS 1 that materiality also involves decisions about whether to include additional information in the financial statements. Consequently, an entity should make additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users of financial statements to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.
- BC30I The Board noted that the definition of 'material' in paragraph 7 of IAS 1 discusses omissions or misstatements of items being material if they could individually or collectively influence economic decisions. The Board considered making amendments to paragraph 31 of IAS 1 to say that an entity need not provide a specific disclosure if the information provided by that disclosure is not material, either individually or collectively. However, the Board decided not to make that change since the definition of material already incorporates the notions of individual and collective assessment and, therefore, reference to the term material in paragraph 31 is sufficient to incorporate this concept.
- BC30J In the March 2014 Exposure Draft the Board proposed to use the term 'present' to refer to line items, subtotals and totals on the statement(s) of profit or loss and other comprehensive income, the statement of financial position, the statement of cash flows and the statement of changes in equity, and the term 'disclose' to mean information in the notes. However, respondents to the March 2014 Exposure Draft did not support the distinction between present and disclose because they considered that the terminology has not been used consistently throughout IAS 1 and that any changes in how these terms are used should be done as part of a comprehensive review of IAS 1. Because of this, and because making such comprehensive changes to IAS 1 would be outside the scope of these amendments, the Board did not finalise the proposed changes regarding use of the terms present and disclose.

Comparative information

A statement of financial position as at the beginning of the earliest comparative period (paragraph 39)

- BC31 The exposure draft of 2006 proposed that a statement of financial position as at the beginning of the earliest comparative period should be presented as part of a complete set of financial statements. This statement would provide a basis for investors and creditors to evaluate information about the entity's performance during the period. However, many respondents expressed concern that the requirement would unnecessarily increase disclosures in financial statements, or would be impracticable, excessive and costly.

BC32 By adding a statement of financial position as at the beginning of the earliest comparative period, the exposure draft proposed that an entity should present three statements of financial position and two of each of the other statements. Considering that financial statements from prior years are readily available for financial analysis, the Board decided to require only two statements of financial position, except when the financial statements have been affected by retrospective application or retrospective restatement, as defined in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, or when a reclassification has been made. In those circumstances three statements of financial position are required.

Clarification of requirements for comparative information

BC32A In *Annual Improvements 2009–2011 Cycle* (issued in May 2012) the Board addressed a request to clarify the requirements for providing comparative information for:

- (a) the comparative requirements for the opening statement of financial position when an entity changes accounting policies, or makes retrospective restatements or reclassifications, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and
- (b) the requirements for providing comparative information when an entity provides financial statements beyond the minimum comparative information requirements.

Opening statement of financial position

BC32B In *Annual Improvements 2009–2011 Cycle* (issued in May 2012) the Board addressed a request to clarify the appropriate date for the opening statement of financial position. The Board decided to amend the current requirements in IAS 1 that relate to the presentation of a statement of financial position for the beginning of the earliest comparative period presented in cases of changes in accounting policies, retrospective restatements or reclassifications to clarify that the appropriate date for the opening statement of financial position is the beginning of the preceding period.

BC32C The Board also decided to change the previous requirements so that related notes to this opening statement of financial position are no longer required to be presented. The Board's decision to give this relief was based on the fact that circumstances in which an entity changes an accounting policy, or makes a retrospective restatement or a reclassification in accordance with IAS 8, are considered narrow, specific and limited. However, the circumstances in which an entity chooses to provide additional financial statements (ie on a voluntary basis) can be viewed as more generic and may arise for different reasons. Accordingly, this relief is not available when additional financial statements are provided on a voluntary basis.

- BC35 The exposure draft of 2002 proposed a different criterion for exemption from particular requirements. For the reclassification of comparative amounts, and its proposed new requirement to disclose key assumptions and other sources of estimation uncertainty at the end of the reporting period (discussed in paragraphs BC79–BC84), the exposure draft proposed that the criterion for exemption should be that applying the requirements would require undue cost or effort.
- BC36 In the light of respondents' comments on the exposure draft, the Board decided that an exemption based on management's assessment of undue cost or effort was too subjective to be applied consistently by different entities. Moreover, balancing costs and benefits was a task for the Board when it sets accounting requirements rather than for entities when they apply them. Therefore, the Board retained the 'impracticability' criterion for exemption. This affects the exemptions now set out in paragraphs 41–43 and 131 of IAS 1. Impracticability is the only basis on which IFRSs allow specific exemptions from applying particular requirements when the effect of applying them is material*.

Reporting owner and non-owner changes in equity

- BC37 The exposure draft of 2006 proposed to separate changes in equity of an entity during a period arising from transactions with owners in their capacity as owners (ie all owner changes in equity) from other changes in equity (ie non-owner changes in equity). All owner changes in equity would be presented in the statement of changes in equity, separately from non-owner changes in equity.
- BC38 Most respondents welcomed this proposal and saw this change as an improvement of financial reporting, by increasing the transparency of those items recognised in equity that are not reported as part of profit or loss. However, some respondents pointed out that the terms 'owner' and 'non-owner' were not defined in the exposure draft, the *Framework* or elsewhere in IFRSs, although they are extensively used in national accounting standards. They also noted that the terms 'owner' and 'equity holder' were used interchangeably in the exposure draft. The Board decided to adopt the term 'owner' and use it throughout IAS 1 to converge with SFAS 130, which uses the term in the definition of 'comprehensive income'.

Statement of financial position

Information to be presented in the statement of financial position (paragraphs 54–55A)

- BC38A Paragraph 54 of IAS 1 lists line items that are required to be presented in the statement of financial position. The Board has been informed that some have interpreted that list as prescriptive and that those line items cannot be disaggregated. There is also a perception by some that IFRS prevents them from presenting subtotals in addition to those specifically required by IFRS.
- BC38B Paragraph 55 of IAS 1 requires an entity to present additional line items, headings and subtotals when their presentation is relevant to an understanding of the entity's financial position. This highlights that the line items listed for presentation in paragraph 54 of IAS 1 should be disaggregated and that subtotals should be presented, when relevant. Paragraphs 78 and 98 of IAS 1 give examples of potential disaggregations of line items in the statement of financial position and the statement(s) of profit or loss and other comprehensive income.

* In 2006 the IASB issued IFRS 8 *Operating Segments*. As explained in paragraphs BC46 and BC47 of the Basis for Conclusions on IFRS 8, that IFRS includes an exemption from some requirements if the necessary information is not available and the cost to develop it would be excessive.

BC38C Consequently, the Board:

- (a) removed the wording ‘as a minimum’ from paragraph 54 of IAS 1 (see paragraph BC30D) to address the possible misconception that this wording prevents entities from aggregating the line items specified in paragraph 54 if those specified line items are immaterial; and
- (b) clarified that the presentation requirements in paragraphs 54–55 may be fulfilled by disaggregating a specified line item.

BC38D The Board noted that there are similar presentation requirements in paragraph 85 of IAS 1 for the statement(s) of profit or loss and other comprehensive income. The Board therefore amended those requirements to make them consistent.

BC38E Some respondents to the proposals suggested that the Board should make clear that the line items listed in paragraph 54 of IAS 1 are required ‘when material’. The Board decided not to state that the line items are only required when material, because materiality is generally not referenced specifically in disclosure requirements in IFRS and so including a specific reference in this case could make it less clear that materiality applies to other disclosure requirements.

BC38F The Board understands that some are concerned about the presentation of subtotals, in addition to those specified in IFRS, in the statement of financial position and the statement(s) of profit or loss and other comprehensive income. Those with this concern think that some subtotals can be misleading, for example, because they are given undue prominence. The Board noted that paragraphs 55 and 85 of IAS 1 require the presentation of subtotals when such presentation is relevant to an understanding of the entity’s financial position or financial performance.

BC38G The Board therefore included additional requirements in IAS 1 to help entities apply paragraphs 55 and 85. These additional requirements supplement the existing guidance on fair presentation in paragraphs 15 and 17 of IAS 1. They are designed to clarify the factors that should be considered when fairly presenting subtotals in the statement of financial position and the statement(s) of profit or loss and other comprehensive income. Specifically, the subtotal should:

- (a) be comprised of line items made up of amounts recognised and measured in accordance with IFRS.
- (b) be understandable. It should be clear what line items are included in the subtotal by the way that the subtotal is presented and labelled. For example, if an entity presents a commonly reported subtotal, but excludes items that would normally be considered as part of that subtotal, the label should reflect what has been excluded.
- (c) be consistent from period to period. The subtotal should be consistently presented and calculated from period to period (in accordance with paragraph 45 of IAS 1), subject to possible changes in accounting policy or estimates assessed in accordance with IAS 8.
- (d) not be displayed with more prominence than those subtotals and totals required in IFRS for either the statement(s) of profit or loss and other comprehensive income or the statement of financial position.

Current assets and current liabilities (paragraphs 68 and 71)

BC38AH As part of its improvements project in 2007, the Board identified inconsistent guidance regarding the current/non-current classification of derivatives. Some might read the guidance included in paragraph 71 as implying that financial liabilities classified as held for trading in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* are always required to be presented as current.

BC38B~~I~~ The Board expects the criteria set out in paragraph 69 to be used to assess whether a financial liability should be presented as current or non-current. The ‘held for trading’ category in paragraph 9 of IAS 39 is for measurement purposes and includes financial assets and liabilities that may not be held primarily for trading purposes.

BC38G~~J~~ The Board reaffirmed that if a financial liability is held primarily for trading purposes it should be presented as current regardless of its maturity date. However, a financial liability that is not held for trading purposes, such as a derivative that is not a financial guarantee contract or a designated hedging instrument, should be presented as current or non-current on the basis of its settlement date. For example, derivatives that have a maturity of more than twelve months and are expected to be held for more than twelve months after the reporting period should be presented as non-current assets or liabilities.

BC38D~~K~~ Therefore, the Board decided to remove the identified inconsistency by amending the examples of current liabilities in paragraph 71. The Board also amended paragraph 68 in respect of current assets to remove a similar inconsistency.

Classification of the liability component of a convertible instrument (paragraph 69)

BC38E~~L~~ As part of its improvements project in 2007, the Board considered the classification of the liability component of a convertible instrument as current or non-current. Paragraph 69(d) of IAS 1 states that when an entity does not have an unconditional right to defer settlement of a liability for at least twelve months after the reporting period, the liability should be classified as current. According to the *Framework*, conversion of a liability into equity is a form of settlement.

BC38F~~M~~ The application of these requirements means that if the conversion option can be exercised by the holder at any time, the liability component would be classified as current. This classification would be required even if the entity would not be required to settle unconverted instruments with cash or other assets for more than twelve months after the reporting period.

BC38G~~N~~ IAS 1 and the *Framework* state that information about the liquidity and solvency positions of an entity is useful to users. The terms ‘liquidity’ and ‘solvency’ are associated with the availability of cash to an entity. Issuing equity does not result in an outflow of cash or other assets of the entity.

BC38H~~O~~ The Board concluded that classifying the liability on the basis of the requirements to transfer cash or other assets rather than on settlement better reflects the liquidity and solvency position of an entity, and therefore it decided to amend IAS 1 accordingly.

BC38I~~P~~ The Board discussed the comments received in response to its exposure draft of proposed Improvements to IFRSs published in 2007 and noted that some respondents were concerned that the proposal in the exposure draft would apply to all liabilities, not just those that are components of convertible instruments as originally contemplated in the exposure draft. Consequently, in *Improvements to IFRSs* issued in April 2009, the Board amended the proposed wording to clarify that the amendment applies only to the classification of a liability that can, at the option of the counterparty, be settled by the issue of the entity’s equity instruments.

- BC54F In the responses to the exposure draft of May 2010 many of the respondents objected to the proposals to remove the option to present all items of income and expense in two statements. The arguments used by those objecting were much the same as those received on the discussion paper. However, many respondents, regardless of their views on the proposed amendments, said that the Board should establish a conceptual basis for what should be presented in OCI. Those opposed to a continuous statement cited OCI's lack of a conceptual definition and therefore believed that OCI should not be presented in close proximity to profit or loss because this would confuse users. However, users generally said that the lack of a conceptual framework made it difficult to distinguish the underlying economics of items reported in profit or loss (net income) from items reported in other comprehensive income. Although users also asked for a conceptual framework for OCI, most supported the notion of a single statement of comprehensive income.
- BC54G Another issue on which many respondents commented was the reclassification (recycling) of OCI items. Those respondents said that in addition to addressing the conceptual basis for the split between profit or loss and OCI the Board should set principles for which OCI items should be reclassified (recycled) to profit or loss and when they should be reclassified. The Board acknowledges that it has not set out a conceptual basis for how it determines whether an item should be presented in OCI or in profit or loss. It also agrees that it has not set out principles to determine whether items should be reclassified to profit or loss. Those matters were not within the scope of this project, which focused on presentation, and therefore the Board has not addressed them at this time. However, the Board is consulting on its future agenda, which could lead to those matters becoming part of the work programme.
- BC54H In the light of the response the Board confirmed in June 2011 the requirement for items of OCI to be classified into items that will not be reclassified (recycled) to profit or loss in subsequent periods and items that might be reclassified.
- BC54I The Board also decided not to mandate the presentation of profit or loss in a continuous statement of profit or loss and other comprehensive income but to maintain an option to present two statements. The Board did this in the light of the negative response to its proposal for a continuous statement and the resistance to this change signified by a majority of respondents.
- BC54J The FASB also proposed in its exposure draft to mandate a continuous statement of comprehensive income but decided in the light of the responses not to go as far as mandating a single statement and instead to allow the two-statement option. Nevertheless, the changes made by the FASB are a significant improvement for US GAAP, which previously allowed an option to present OCI items in stockholders' equity or in the notes to the financial statements.
- BC54K In 2013 the IFRS Interpretations Committee reported to the Board that there was uncertainty about the requirements in paragraph 82A of IAS 1 for presenting an entity's share of items of other comprehensive income of associates and joint ventures accounted for using the equity method. The Board agreed that paragraph 82A allowed for diverse interpretations, and therefore decided to amend IAS 1 as follows:
- (a) to clarify that paragraph 82A requires entities to present the share of other comprehensive income of associates and joint ventures accounted for using the equity method, separated into the share of items that:
 - (i) will not be reclassified subsequently to profit or loss; and
 - (ii) will be reclassified subsequently to profit or loss when specific conditions are met.
 - (b) to amend the Guidance on Implementing IAS 1 to reflect the clarification of paragraph 82A.

The Board noted that whether an amount is reclassified to profit or loss is determined by the nature of the underlying item. It also noted that the timing of reclassification is usually determined by the actions of the investee. It may however also be triggered by the investor, which would be the case on the disposal of the investee by the investor.

- BC54L The feedback received on the March 2014 Exposure Draft included requests for the Board to clarify whether the investor's share of the other comprehensive income of its associate or joint venture should be presented net or gross of tax and the applicability of the guidance in paragraphs 90–91 of IAS 1 in this regard. The Board noted that an investor's share of other comprehensive income of associates or joint ventures is after tax and non-controlling interests of the associate or joint venture, as illustrated in the Guidance on Implementing IAS 1. It also noted that the disclosure requirements in paragraphs 90–91 do not apply to the tax of the associate or joint venture that is already reflected in the investor's share of other comprehensive income of the associate or joint venture. However, the Board noted that if the investor itself is liable for tax in respect of its share of other comprehensive income of the associate or joint venture, then paragraphs 90–91 would apply to this tax. Therefore, the Board decided not to add additional guidance to IAS 1 on this topic.

Results of operating activities

- BC55 IAS 1 omits the requirement in the 1997 version to disclose the results of operating activities as a line item in the income statement. 'Operating activities' are not defined in IAS 1, and the Board decided not to require disclosure of an undefined item.
- BC56 The Board recognises that an entity may elect to disclose the results of operating activities, or a similar line item, even though this term is not defined. In such cases, the Board notes that the entity should ensure that the amount disclosed is representative of activities that would normally be regarded as 'operating'. In the Board's view, it would be misleading and would impair the comparability of financial statements if items of an operating nature were excluded from the results of operating activities, even if that had been industry practice. For example, it would be inappropriate to exclude items clearly related to operations (such as inventory write-downs and restructuring and relocation expenses) because they occur irregularly or infrequently or are unusual in amount. Similarly, it would be inappropriate to exclude items on the grounds that they do not involve cash flows, such as depreciation and amortisation expenses.

Subtotal for profit or loss (paragraph 82)

- BC57 As revised, IAS 1 requires a subtotal for profit or loss in the statement of comprehensive income. If an entity chooses to present comprehensive income by using two statements, it should begin the second statement with profit or loss—the bottom line of the first statement (the 'income statement')—and display the components of other comprehensive income immediately after that. The Board concluded that this is the best way to achieve the objective of equal prominence (see paragraph BC22) for the presentation of income and expenses. An entity that chooses to display comprehensive income in one statement should include profit or loss as a subtotal within that statement.
- BC58 The Board acknowledged that the items included in profit or loss do not possess any unique characteristics that allow them to be distinguished from items that are included in other comprehensive income. However, the Board and its predecessor have required some items to be recognised outside profit or loss. The Board will deliberate in the next stage of the project how items of income and expense should be presented in the statement of comprehensive income.

Information to be presented in the profit or loss section or the statement of profit or loss (paragraphs 85–85B)

- BC58A** In December 2014 the Board issued *Disclosure Initiative (Amendments to IAS 1)*. Those amendments included amendments to paragraph 85 of IAS 1 and the addition of paragraph 85A. These amendments are consistent with similar amendments to the requirements for the statement of financial position and therefore the Basis for Conclusions for these amendments has been included in the section dealing with that statement (see paragraphs BC38A–BC38G).
- BC58B** In addition to those amendments, the Board decided to require entities to present line items in the statement(s) of profit or loss and other comprehensive income that reconcile any subtotals presented in accordance with paragraphs 85–85A of IAS 1 with those that are required in IFRS for the statement(s) of profit or loss and other comprehensive income. Consequently, it added paragraph 85B to IAS 1. The purpose of this requirement is to help users of financial statements understand the relationship between the subtotals presented in accordance with paragraph 85 and the specific totals and subtotals required in IFRS to address concerns that that relationship would not be clear. The Board noted that such a requirement is already implicit in existing IFRS requirements. IFRS requires entities to present aggregated information as line items when such presentation provides material information. Consequently, because all recognised items of income and expense must be included in the statement(s) of profit or loss and other comprehensive income totals, any intervening line items and subtotals necessarily reconcile. However, the Board decided to make the requirement more explicit for the statement(s) of profit or loss and other comprehensive income to help users of financial statements understand the relationship between subtotals and totals presented in the statement(s) of profit or loss and other comprehensive income.

Minority interest (paragraph 83)*

- BC59** IAS 1 requires the ‘profit or loss attributable to minority interest’ and ‘profit or loss attributable to owners of the parent’ each to be presented in the income statement in accordance with paragraph 83. These amounts are to be presented as allocations of profit or loss, not as items of income or expense. A similar requirement has been added for the statement of changes in equity, in paragraph 106(a). These changes are consistent with IAS 27 *Consolidated and Separate Financial Statements*, which requires that in a consolidated balance sheet (now called ‘statement of financial position’), minority interest is presented within equity because it does not meet the definition of a liability in the *Framework*.

* In January 2008 the IASB issued an amended IAS 27 *Consolidated and Separate Financial Statements*, which amended ‘minority interest’ to ‘non-controlling interests’. The consolidation requirements in IAS 27 were superseded by IFRS 10 *Consolidated Financial Statements* issued in May 2011. The term ‘non-controlling interests’ and the requirements for non-controlling interests were not changed.

Notes

Structure (paragraphs 112–116)

- BC76A The Board is aware that some had interpreted paragraph 114 of IAS 1 as requiring a specific order for the notes. Paragraph 114 stated that ‘an entity normally presents notes in the [following] order’ and then listed a particular order for the notes. Some think that the use of ‘normally’ makes it difficult for an entity to vary the order of the notes from the one that is listed in paragraph 114; for example, by disclosing the notes in order of importance or disclosing related information together in sections.
- BC76B Investors’ feedback indicates that some investors prefer an entity to vary the order of the notes from the one that is listed in paragraph 114 of IAS 1. Other investors would prefer entities to use that order because they think it will increase comparability between periods and across entities.
- BC76C The Board considered the use of the word normally in paragraph 114 of IAS 1 and concluded that it was not intended that entities be required to disclose their notes in that order. Instead, it thinks that the order listed was intended to provide an example of how an entity could order the notes and that the term normal was not meant to imply that alternative ordering of the notes is ‘abnormal’. The Board therefore amended IAS 1 to clarify that the order listed in paragraph 114 is an example of how an entity could order or group its notes in a systematic manner. The Board also made amendments to clarify that significant accounting policies do not need to be disclosed in one note, but instead can be included with related information in other notes.
- BC76D The Board also noted the requirement in paragraph 113 of IAS 1 for entities to, as far as practicable, present the notes in a systematic manner. In the Board’s view, this means that there must be a system or reason behind the ordering and grouping of the notes. For example, notes could be ordered by importance to the entity, in the order line items are presented in the financial statements or a combination of both. The Board amended paragraph 113 to clarify that an entity should consider the effect on the understandability and comparability of its financial statements when determining the order of the notes. The Board acknowledged that there is a trade-off between understandability and comparability; for example, ordering notes to increase understandability could mean that comparability, including consistency, between entities and periods is reduced. In particular, the Board acknowledged that consistency in the order of the notes for a specific entity from period to period is important. The Board noted that it would generally be helpful for users of financial statements if the ordering of notes by an entity is consistent and noted that it does not expect the order of an entity’s notes to change frequently. A change in the order of the notes previously determined to be an optimal mix of understandability and comparability should generally result from a specific event or transaction, such as a change in business. The Board also noted that the existing requirements in paragraph 45 of IAS 1 for consistency of presentation still apply.
- BC76E The Board also observed that electronic versions of financial statements can make it easier to search for, locate and compare information within the financial statements, between periods and between entities.

Disclosure of accounting policies (paragraphs 117–121)

- BC76F Paragraph 117 of IAS 1 requires significant accounting policies to be disclosed and gives guidance, along with paragraphs 118–124 of IAS 1, about what a significant accounting policy could be. That guidance includes, as examples of significant accounting policies, the income taxes accounting policy and the foreign currency accounting policy.

BC76G Some suggested that it is not helpful to provide the income taxes accounting policy as an example of a policy that users of financial statements would expect to be disclosed. Being liable to income taxes is typical for many entities and it was not clear, from the example, what aspect of the entity's operations would make a user of financial statements expect an accounting policy on income taxes to be disclosed. Consequently, the example does not illustrate why an accounting policy on income taxes is significant. The Board also thought that the foreign currency accounting policy example in paragraph 120 of IAS 1 was unhelpful for the same reasons and therefore deleted the income taxes and foreign currency examples.

Disclosure of the judgements that management has made in the process of applying the entity's accounting policies (paragraphs 122–124)

BC77 The revised IAS 1 requires disclosure of the judgements, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements (see paragraph 122). An example of these judgements is how management determines whether financial assets are held-to-maturity investments. The Board decided that disclosure of the most important of these judgements would enable users of financial statements to understand better how the accounting policies are applied and to make comparisons between entities regarding the basis on which managements make these judgements.

BC78 Comments received on the exposure draft of 2002 indicated that the purpose of the proposed disclosure was unclear. Accordingly, the Board amended the disclosure explicitly to exclude judgements involving estimations (which are the subject of the disclosure in paragraph 125) and added another four examples of the types of judgements disclosed (see paragraphs 123 and 124).

Disclosure of major sources of estimation uncertainty (paragraphs 125–133)

BC79 IAS 1 requires disclosure of the assumptions concerning the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. For those assets and liabilities, the proposed disclosures include details of:

- (a) their nature, and
- (b) their carrying amount as at the end of the reporting period (see paragraph 125).

BC80 Determining the carrying amounts of some assets and liabilities requires estimation of the effects of uncertain future events on those assets and liabilities at the end of the reporting period. For example, in the absence of recently observed market prices used to measure the following assets and liabilities, future-oriented estimates are necessary to measure the recoverable amount of classes of property, plant and equipment, the effect of technological obsolescence of inventories, provisions subject to the future outcome of litigation in progress, and long-term employee benefit liabilities such as pension obligations. These estimates involve assumptions about items such as the risk adjustment to cash flows or discount rates used, future changes in salaries and future changes in prices affecting other costs. No matter how diligently an entity estimates the carrying amounts of assets and liabilities subject to significant estimation uncertainty at the end of the reporting period, the reporting of point estimates in the statement of financial position cannot provide information about the estimation uncertainties involved in measuring those assets and liabilities and the implications of those uncertainties for the period's profit or loss.

Disclosure Initiative (Amendments to IAS 1)

BC105C The Board decided that *Disclosure Initiative* (Amendments to IAS 1) should be applied for annual periods beginning on or after 1 January 2016 with early application permitted.

BC105D The Board noted that these amendments clarify existing requirements in IAS 1. They provide additional guidance to assist entities to apply judgement when meeting the presentation and disclosure requirements in IFRS. These amendments do not affect recognition and measurement. They should not result in the reassessment of the judgements about presentation and disclosure made in periods prior to the application of these amendments.

BC105E Paragraph 38 of IAS 1 requires an entity to present comparative information for all amounts reported in the current period financial statements and for narrative or descriptive information 'if it is relevant to understanding the current period's financial statements'. If an entity alters the order of the notes or the information presented or disclosed compared to the previous year, it also adjusts the comparative information to align with the current period presentation and disclosure. For that reason, IAS 1 already provides relief from having to disclose comparative information that is not considered relevant in the current period and requires comparative information for new amounts presented or disclosed in the current period.

BC105F The March 2014 Exposure Draft proposed that if an entity applies these amendments early that it should disclose that fact. However, the Board removed this requirement and stated in the transition provisions that an entity need not disclose the fact that it has applied these amendments (regardless of whether the amendments have been applied for annual periods beginning on or after 1 January 2016 or if they have been applied early). This is because the Board considers that these amendments are clarifying amendments that do not directly affect an entity's accounting policies or accounting estimates. Similarly, an entity does not need to disclose the information required by paragraphs 28–30 of IAS 8 in relation to these amendments. The Board noted that if an entity decides to change its accounting policies as a result of applying these amendments then it would be required to follow the existing requirements in IAS 8 in relation to those accounting policy changes.

Guidance on implementing IAS 1 *Presentation of Financial Statements*

This guidance accompanies, but is not part of, IAS 1.

Illustrative financial statement structure

- IG1 IAS 1 sets out the components of financial statements and minimum requirements for disclosure in the statements of financial position, profit or loss and other comprehensive income and changes in equity. It also describes further items that may be presented either in the relevant financial statement or in the notes. This guidance provides simple examples of ways in which the requirements of IAS 1 for the presentation of the statements of financial position, profit or loss and other comprehensive income and changes in equity might be met. An entity should change the order of presentation, the titles of the statements and the descriptions used for line items when necessary to suit its particular circumstances.
- IG2 The guidance is in three sections. Paragraphs IG3–IG6 provide examples of the presentation of financial statements. Paragraphs IG7–IG9 provide an example of the determination of reclassification adjustments for available-for-sale financial assets in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*. Paragraphs IG10 and IG11 provide examples of capital disclosures.
- IG3 The illustrative statement of financial position shows one way in which an entity may present a statement of financial position distinguishing between current and non-current items. Other formats may be equally appropriate, provided the distinction is clear.
- IG4 The illustrations use the term ‘comprehensive income’ to label the total of all items of profit or loss and other comprehensive income. The illustrations use the term ‘other comprehensive income’ to label income and expenses that are included in comprehensive income but excluded from profit or loss. IAS 1 does not require an entity to use those terms in its financial statements.
- IG5 Two statements of profit or loss and other comprehensive income are provided, to illustrate the alternative presentations of income and expenses in a single statement or in two statements. The statement of profit or loss and other comprehensive income illustrates the classification of income and expenses within profit or loss by function. The separate statement (in this example, ‘the statement of profit or loss’) illustrates the classification of income and expenses within profit by nature.
- IG5A Two sets of examples of statements of profit or loss and other comprehensive income are shown. One shows the presentation while IAS 39 *Financial Instruments: Recognition and Measurement* remains effective and is applied; the other shows presentation when IFRS 9 *Financial Instruments* is applied.
- IG6 The examples are not intended to illustrate all aspects of IFRSs, nor do they constitute a complete set of financial statements, which would also include a statement of cash flows, a ~~summary of disclosures about~~ significant accounting policies and other explanatory information.

Examples of statement of profit or loss and other comprehensive income**XYZ Group – Statement of profit or loss and other comprehensive income for the year ended 31 December 20X7****(illustrating the presentation of profit or loss and other comprehensive income in one statement and the classification of expenses within profit or loss by function)**

(in thousands of currency units)

	20X7	20X6
Revenue	390,000	355,000
Cost of sales	(245,000)	(230,000)
Gross profit	145,000	125,000
Other income	20,667	11,300
Distribution costs	(9,000)	(8,700)
Administrative expenses	(20,000)	(21,000)
Other expenses	(2,100)	(1,200)
Finance costs	(8,000)	(7,500)
Share of profit of associates ^(a)	35,100	30,100
Profit before tax	161,667	128,000
Income tax expense	(40,417)	(32,000)
Profit for the year from continuing operations	121,250	96,000
Loss for the year from discontinued operations	–	(30,500)
PROFIT FOR THE YEAR	121,250	65,500
Other comprehensive income:		
Items that will not be reclassified to profit or loss:		
Gains on property revaluation	933	3,367
Remeasurements of defined benefit pension plans	(667)	1,333
Share of gain (loss) on property revaluation other comprehensive income of associates ^(b)	400	(700)
Income tax relating to items that will not be reclassified ^(c)	(166)	(1,000)
	500	3,000
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translating foreign operations ^(d)	5,334	10,667
Available-for-sale financial assets ^(d)	(24,000)	26,667
Cash flow hedges ^(d)	(667)	(4,000)
Income tax relating to items that may be reclassified ^(c)	4,833	(8,334)
	(14,500)	25,000
Other comprehensive income for the year, net of tax	(14,000)	28,000
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	107,250	93,500

continued...

(d) This illustrates the aggregated presentation, with disclosure of the current year gain or loss and reclassification adjustment presented in the notes. Alternatively, a gross presentation can be used.

XYZ Group – Statement of profit or loss for the year ended 31 December 20X7

(illustrating the presentation of profit or loss and other comprehensive income in two statements and the classification of expenses within profit or loss by nature)

(in thousands of currency units)

	20X7	20X6
Revenue	390,000	355,000
Other income	20,667	11,300
Changes in inventories of finished goods and work in progress	(115,100)	(107,900)
Work performed by the entity and capitalised	16,000	15,000
Raw material and consumables used	(96,000)	(92,000)
Employee benefits expense	(45,000)	(43,000)
Depreciation and amortisation expense	(19,000)	(17,000)
Impairment of property, plant and equipment	(4,000)	–
Other expenses	(6,000)	(5,500)
Finance costs	(15,000)	(18,000)
Share of profit of associates ^(a)	35,100	30,100
Profit before tax	161,667	128,000
Income tax expense	(40,417)	(32,000)
Profit for the year from continuing operations	121,250	96,000
Loss for the year from discontinued operations	–	(30,500)
PROFIT FOR THE YEAR	121,250	65,500
Profit attributable to:		
Owners of the parent	97,000	52,400
Non-controlling interests	24,250	13,100
	121,250	65,500
Earnings per share (in currency units):		
Basic and diluted	0.46	0.30

(a) This means the share of associates' profit attributable to owners of the associates, ie it is after tax and non-controlling interests in the associates.

XYZ Group – Statement of profit or loss and other comprehensive income for the year ended 31 December 20X7

(illustrating the presentation of profit or loss and other comprehensive income in two statements)

(in thousands of currency units)

	20X7	20X6
Profit for the year	121,250	65,500
Other comprehensive income:		
Items that will not be reclassified to profit or loss:		
Gains on property revaluation	933	3,367
Remeasurements of defined benefit pension plans	(667)	1,333
Share of gain (loss) on property revaluation <u>other comprehensive income</u> of associates ^(a)	400	(700)
Income tax relating to items that will not be reclassified ^(b)	(166)	(1,000)
	500	3,000
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translating foreign operations	5,334	10,667
Available-for-sale financial assets	(24,000)	26,667
Cash flow hedges	(667)	(4,000)
Income tax relating to items that may be reclassified ^(b)	4,833	(8,334)
	(14,500)	25,000
Other comprehensive income for the year, net of tax	(14,000)	28,000
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	107,250	93,500
Total comprehensive income attributable to:		
Owners of the parent	85,800	74,800
Non-controlling interests	21,450	18,700
	107,250	93,500

Alternatively, items of other comprehensive income could be presented, net of tax. Refer to the statement of profit or loss and other comprehensive income illustrating the presentation of income and expenses in one statement.

(a) This means the share of associates' ~~gain (loss) on property revaluation~~ other comprehensive income attributable to owners of the associates, ie it is after tax and non-controlling interests in the associates. In this example, the other comprehensive income of associates consists only of items that will not be subsequently reclassified to profit or loss. Entities whose associates' other comprehensive income includes items that may be subsequently reclassified to profit or loss are required by paragraph 82A(b) to present that amount in a separate line.

(b) The income tax relating to each item of other comprehensive income is disclosed in the notes.

Amendments to the guidance on implementing IAS 1 *Disclosure Initiative*

The following sets out amendments required for this Implementation Guidance resulting from amendments to IAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Guidance and this appendix will be deleted.

The versions of IAS 1 that include examples of statement of profit or loss and other comprehensive income when IFRS 9 *Financial Instruments* is applied are amended. Deleted text is struck through and new text is underlined.

...

(illustrating the presentation of profit or loss and other comprehensive income in one statement and the classification of expenses within profit or loss by function)

...

	20X7	20X6
...		
Other comprehensive income:		
Items that will not be reclassified to profit or loss:		
Gains on property revaluation	933	3,367
Investments in equity instruments	(24,000)	26,667
Remeasurements of defined benefit pension plans	(667)	1,333
Share of gain (loss) on property revaluation <u>other comprehensive income</u> of associates ^(b)	400	(700)
Income tax relating to items that will not be reclassified ^(c)	5,834	(7,667)
	(17,500)	23,000

...

Alternatively, items of other comprehensive income could be presented in the statement of profit or loss and other comprehensive income net of tax.

Other comprehensive income for the year, after tax:

Items that will not be reclassified to profit or loss:

Gains on property revaluation	600	2,700
Investments in equity instruments	(18,000)	20,000
Remeasurements of defined benefit pension plans	(500)	1,000
Share of gain (loss) on property revaluation <u>other comprehensive income</u> of associates	400	(700)
	(17,500)	23,000

...

(a) ...

(b) This means the share of associates' ~~gain (loss) on property revaluation~~ other comprehensive income attributable to owners of the associates, ie it is after tax and non-controlling interests in the associates. In this example, the other comprehensive income of associates consists only of items that will not be subsequently reclassified to profit or loss. Entities whose associates' other comprehensive income includes items that may be subsequently reclassified to profit or loss are required by paragraph 82A(b) to present that amount in a separate line.

(c) The income tax relating to each item of other comprehensive income is disclosed in the notes.

(d) ...

...

(illustrating the presentation of profit or loss and other comprehensive income in two statements)

...

	20X7	20X6
Profit for the year	121,250	65,500
Other comprehensive income:		
Items that will not be reclassified to profit or loss:		
Gains on property revaluation	933	3,367
Investments in equity instruments	(24,000)	26,667
Remeasurements of defined benefit pension plans	(667)	1,333
Share of gain (loss) on property revaluation <u>other comprehensive income</u> of associates ^(a)	400	(700)
Income tax relating to items that will not be reclassified ^(b)	<u>5,834</u>	<u>(7,667)</u>
	(17,500)	23,000

...

Alternatively, items of other comprehensive income could be presented, net of tax. Refer to the statement of profit or loss and other comprehensive income illustrating the presentation of income and expenses in one statement.

(a) This means the share of associates' ~~gain (loss) on property revaluation~~ other comprehensive income attributable to owners of the associates, ie it is after tax and non-controlling interests in the associates. In this example, the other comprehensive income of associates consists only of items that will not be subsequently reclassified to profit or loss. Entities whose associates' other comprehensive income includes items that may be subsequently reclassified to profit or loss are required by paragraph 82A(b) to present that amount in a separate line.

(b) The income tax relating to each item of other comprehensive income is disclosed in the notes.

HKAS 19 (2011)
Revised ~~November~~ December 2016

Effective for annual periods
beginning on or after 1 January 2013

Hong Kong Accounting Standard 19 (2011)

Employee Benefits



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

Recognition and measurement: plan assets	113–119
Fair value of plan assets	113–115
Reimbursements	116–119
Components of defined benefit cost	120–130
Net interest on the net defined benefit liability (asset)	123–126
Remeasurements of the net defined benefit liability (asset)	127–130
Presentation	131–134
Offset	131–132
Current/non-current distinction	133
Components of defined benefit cost	134
Disclosure	135–152
Characteristics of defined benefit plans and risks associated with them	139
Explanation of amounts in the financial statements	140–144
Amount, timing and uncertainty of future cash flows	145–147
Multi-employer plans	148
Defined benefit plans that share risks between entities under common control	149–150
Disclosure requirements in other IFRSs	151–152
OTHER LONG-TERM EMPLOYEE BENEFITS	153–158
Recognition and measurement	155–157
Disclosure	158
TERMINATION BENEFITS	159–171
Recognition	165–168
Measurement	169–170
Disclosure	171
TRANSITION AND EFFECTIVE DATE	172–173
APPENDICES	
A Application Guidance	
B Amendments to other HKFRSs	
C Comparison with International Financial Reporting Standards	
BASIS FOR CONCLUSIONS	
APPENDIX	
Amendments to the Basis for Conclusions on other HKFRSs	
DISSENTING OPINIONS	
AMENDMENTS TO GUIDANCE ON OTHER HKFRSs	
TABLE OF CONCORDANCE	

EMPLOYEE BENEFITS

Hong Kong Accounting Standard 19 *Employee Benefits* (HKAS 19) is set out in paragraphs 1–1757 and the Appendix. All the paragraphs have equal authority. HKAS 19 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Conceptual Framework for Financial Reporting*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

- (iii) in the case of medical benefits, future medical costs, including claim handling costs (ie the costs that will be incurred in processing and resolving claims, including legal and adjuster's fees) (see paragraphs 96–98); and
 - (iv) taxes payable by the plan on contributions relating to service before the reporting date or on benefits resulting from that service.
- 77 Actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative.
- 78 Actuarial assumptions are mutually compatible if they reflect the economic relationships between factors such as inflation, rates of salary increase and discount rates. For example, all assumptions that depend on a particular inflation level (such as assumptions about interest rates and salary and benefit increases) in any given future period assume the same inflation level in that period.
- 79 An entity determines the discount rate and other financial assumptions in nominal (stated) terms, unless estimates in real (inflation-adjusted) terms are more reliable, for example, in a hyperinflationary economy (see HKAS 29 *Financial Reporting in Hyperinflationary Economies*), or where the benefit is index-linked and there is a deep market in index-linked bonds of the same currency and term.
- 80 Financial assumptions shall be based on market expectations, at the end of the reporting period, for the period over which the obligations are to be settled.**

Actuarial assumptions: mortality

- 81 **An entity shall determine its mortality assumptions by reference to its best estimate of the mortality of plan members both during and after employment.**
- 82 In order to estimate the ultimate cost of the benefit an entity takes into consideration expected changes in mortality, for example by modifying standard mortality tables with estimates of mortality improvements.

Actuarial assumptions: discount rate

- 83 **The rate used to discount post-employment benefit obligations (both funded and unfunded) shall be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. In countries where For currencies for which there is no deep market in such high quality corporate bonds, the market yields (at the end of the reporting period) on government bonds denominated in that currency shall be used. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations.**
- 84 One actuarial assumption that has a material effect is the discount rate. The discount rate reflects the time value of money but not the actuarial or investment risk. Furthermore, the discount rate does not reflect the entity-specific credit risk borne by the entity's creditors, nor does it reflect the risk that future experience may differ from actuarial assumptions.
- 85 The discount rate reflects the estimated timing of benefit payments. In practice, an entity often achieves this by applying a single weighted average discount rate that reflects the estimated timing and amount of benefit payments and the currency in which the benefits are to be paid.

Transition and effective date

- 172 An entity shall apply this Standard for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies this Standard for an earlier period, it shall disclose that fact.
- 173 An entity shall apply this Standard retrospectively, in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, except that:
- (a) an entity need not adjust the carrying amount of assets outside the scope of this Standard for changes in employee benefit costs that were included in the carrying amount before the date of initial application. The date of initial application is the beginning of the earliest prior period presented in the first financial statements in which the entity adopts this Standard.
 - (b) in financial statements for periods beginning before 1 January 2014, an entity need not present comparative information for the disclosures required by paragraph 145 about the sensitivity of the defined benefit obligation.
- 174 HKFRS 13, issued in June 2011, amended the definition of fair value in paragraph 8 and amended paragraph 113. An entity shall apply those amendments when it applies HKFRS 13.
- 175 *Defined Benefit Plans: Employee Contributions* (Amendments to HKAS 19), issued in December 2013, amended paragraphs 93–94. An entity shall apply those amendments for annual periods beginning on or after 1 July 2014 retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Earlier application is permitted. If an entity applies those amendments for an earlier period, it shall disclose that fact.
- 176 *Annual Improvements to HKFRSs 2012–2014 Cycle*, issued in October 2014, amended paragraph 83 and added paragraph 177. An entity shall apply that amendment for annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.
- 177 An entity shall apply the amendment in paragraph 176 from the beginning of the earliest comparative period presented in the first financial statements in which the entity applies the amendment. Any initial adjustment arising from the application of the amendment shall be recognised in retained earnings at the beginning of that period.

EMPLOYEE BENEFITS

Actuarial assumptions—discount rate	BC129–BC137
Actuarial assumptions—discount rate: exposure draft published in 2009	BC138–BC139
Actuarial assumptions—salaries, benefits and medical costs	BC140–BC141
Actuarial assumptions—mortality: amendments issued in 2011	BC142
Actuarial assumptions—risk-sharing: amendments issued in 2011	BC143–BC150
<u>Actuarial assumptions—discount rate: regional market issue</u>	<u>BC150A–BC150F</u>
CONTRIBUTIONS FROM EMPLOYEES OR THIRD PARTIES: AMENDMENTS ISSUED IN 2013	BC150AG–BC150KQ
Curtailments and settlements	BC151
Plan amendments, curtailments and settlements: amendments issued in 2011	BC152–BC173
Plan assets	BC174–BC177
Plan assets: amendments issued in 2000	BC178–BC190
Plan assets—measurement	BC191–BC194
Reimbursements: amendments issued in 2000	BC195–BC199
Defined benefit plans—presentation of assets and liabilities	BC200
Defined benefit plans—presentation of defined benefit cost: amendments issued in 2011	BC201–BC202
Defined benefit plans—disclosures: amendments issued in 2011	BC203–BC252
The Board’s approach to disclosures about defined benefit plans	BC207–BC211
Selecting disclosure objectives	BC212–BC214
Characteristics of the defined benefit plan and amounts in the financial statements	BC215–BC228
Amount, timing and uncertainty of future cash flows	BC229–BC243
Other disclosures considered but rejected by the Board	BC244
Multi-employer plans	BC245–BC252
OTHER LONG-TERM EMPLOYEE BENEFITS	BC253
Death-in-service benefits	BC253
TERMINATION BENEFITS: AMENDMENTS ISSUED IN 2011	BC254–BC261
Benefits payable in exchange for services	BC256–BC257
Recognition	BC258–BC260
Measurement	BC261
INTERACTION BETWEEN PLAN AMENDMENTS, CURTAILMENTS, SETTLEMENTS, TERMINATION BENEFITS AND RESTRUCTURING COSTS	BC262–BC268
TRANSITION	BC269–BC271
First-time adopters	BC270
Early application	BC271
Transition provisions for <i>Defined Benefit Plans: Employee Contributions</i>	BC271A–BC271B

Actuarial assumptions—salaries, benefits and medical costs

BC140 Some argue that estimates of future increases in salaries, benefits and medical costs should not affect the measurement of assets and liabilities until they are granted, on the grounds that:

- (a) future increases are future events; and
- (b) such estimates are too subjective.

BC141 IASC believed that the assumptions were used not to determine whether an obligation exists, but to measure an existing obligation on a basis that provides the most relevant measure of the estimated outflow of resources. If no increase was assumed, this was an implicit assumption that no change will occur and it would be misleading to assume no change if an entity did expect a change. IAS 19 maintains the requirement in IAS 19 before its revision in 1998 that measurement should take account of estimated future salary increases. IASC also believed that increases in future medical costs can be estimated with sufficient reliability to justify incorporation of those estimated increases in the measurement of the obligation.

Actuarial assumptions—mortality: amendments issued in 2011

BC142 The amendments made in 2011 make explicit that the mortality assumptions used to determine the defined benefit obligation are current estimates of the expected mortality rates of plan members, both during and after employment. In the Board's view, current mortality tables might need to be adjusted for expected changes in mortality (such as expected mortality improvement) to provide the best estimate of the amount that reflects the ultimate cost of settling the defined benefit obligation.

Actuarial assumptions—risk-sharing: amendments issued in 2011

BC143 The amendments made in 2011 clarify that:

- (a) the effect of employee and third-party contributions should be considered in determining the defined benefit cost, the present value of the defined benefit obligation and the measurement of any reimbursement rights.
- (b) the benefit to be attributed to periods of service in accordance with paragraph 70 of IAS 19 is net of the effect of any employee contributions in respect of service.*
- (c) any conditional indexation should be reflected in the measurement of the defined benefit obligation, whether the indexation or changes in benefits are automatic or are subject to a decision by the employer, the employee or a third party, such as trustees or administrators of the plan.
- (d) if any limits exist on the legal and constructive obligation to pay additional contributions, the present value of the defined benefit obligation should reflect those limits.

BC144 Some defined benefit plans include features that share the benefits of a surplus or the cost of a deficit between the employer and the plan participants. Similarly, some defined benefit plans provide benefits that are conditional to some extent on whether there are sufficient assets in the plan to fund them. Such features share risk between the entity and the plan participants and affect the ultimate cost of the benefits. Hence, the 2010 ED proposed to clarify that the present value of the defined benefit

* *Defined Benefit Plans: Employee Contributions*, issued in November 2013, clarified the requirements that relate to how contributions from employees or third parties that are linked to service should be attributed to periods of service. In addition, it permits a practical expedient if the amount of the contributions is independent of the number of years of service. See paragraphs BC150A–BC150K, BC150G–BC150Q.

determined in accordance with paragraph 80. Paragraph 80 requires financial assumptions to be based on market expectations at the end of the reporting period for the period over which the obligations are to be settled.

Other clarifications

BC150 The Board clarified the following points in the light of responses to the 2010 ED:

- (a) Contributions from employees in respect of service should be attributed to periods of service in accordance with paragraph 70 using the benefit formula, or on a straight-line basis (ie the back-end loading test and attribution in paragraph 70 should be based on the net benefit).^{*} This reflects the Board's view that contributions from employees can be viewed as a negative benefit. In addition, the Board noted that a portion of future employee contributions may be connected with salary increases included in the defined benefit obligation. Applying the same method of attribution to that portion of the contribution and the salary increases avoids an inconsistency.
- (b) An entity would apply judgement in determining whether a change in an input is a change in the terms of the benefit (resulting in past service cost) or a change in an assumption (resulting in an actuarial gain or loss). This clarification is consistent with guidance that existed in IAS 19 before 2011, describing how to address employee contributions for medical costs.
- (c) The best estimate of the ultimate cost of the benefits reflects the best estimate of the effect of terms of the plan that require or allow a change to the level of benefit, or that provide other benefit options, regardless of whether the benefits are adjustable by the entity, by the managers of the plan, or by the employees.
- (d) The measurement of the defined benefit obligation takes account of the effect of any limit on contributions by the employer (see paragraph 91). In the Board's view, this is consistent with the objective of determining the ultimate cost of the benefits. The Board concluded that the effect of such a limit should be determined over the shorter of the expected life of the plan and the expected life of the entity. Determining the limit over a period longer than the current period is necessary to identify whether the effect of the limit is temporary or permanent. For example, the service cost may be higher than the maximum contribution amount in the current period, but if in subsequent years the service cost is lower than the contribution amount, then the effect of the limit is more of a deferral of current period contributions than a limit on the total contributions required.
- (e) The amendments relating to risk-sharing are not intended to be limited to particular relationships. Some respondents noted that some plans' risks are shared not only with employees, but also with other parties (such as the government). In the Board's view, an entity should consider such arrangements in determining the defined benefit obligation. Nevertheless, entities need to consider whether those contributions are reimbursements as described in paragraphs 116–119 (and therefore must be recognised as reimbursement rights) or reductions in the defined benefit obligation.

^{*} *Defined Benefit Plans: Employee Contributions*, issued in November 2013, clarified the requirements that relate to how contributions from employees or third parties that are linked to service should be attributed to periods of service. In addition, it permits a practical expedient if the amount of the contributions is independent of the number of years of service. See paragraphs BC150A–BC150K, BC150G–BC150Q.

Actuarial assumptions—discount rate: regional market issue

- BC150A The Board was asked to clarify the requirements of IAS 19 to determine the discount rate in a regional market sharing the same currency (for example, the Eurozone). The issue arose because some think that the basket of high quality corporate bonds should be determined at a country level, and not at a currency level, because paragraph 83 of IAS 19 states that in countries in which there is no deep market in such bonds, the market yields at the end of the reporting period on government bonds shall be used.
- BC150B The Board noted that paragraph 83 of IAS 19 states that the currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations.
- BC150C The Board decided to amend paragraph 83 of IAS 19 in order to clarify that the depth of the market for high quality corporate bonds should be assessed at a currency level.
- BC150D Some respondents to the Exposure Draft *Annual Improvements to IFRSs 2012–2014 Cycle* (the '2013 Annual Improvements Exposure Draft'), published in December 2013, suggested to the Board that it should clarify the objectives and the rationale underlying the selection and use of the discount rate for post-employment benefit obligations. The Board noted that the IFRS Interpretations Committee (the 'Interpretations Committee') had already discussed a potential broader amendment relating to the discount rate and, after several meetings, recommended that the determination of the discount rate for post-employment benefit obligations should be addressed in the Board's research project on discount rates.
- BC150E Some respondents to the 2013 Annual Improvements Exposure Draft suggested to the Board that it should clarify whether the proposed amendment prohibits an entity that operates in a country/regional market in which there is a deep market for high quality corporate bonds from using only the high quality corporate bonds issued in its own country/regional market. The Board noted that the amendment only clarifies that the depth of the market for high quality corporate bonds should be assessed at a currency level and not a country/regional market level. It does not require that the basket of high quality corporate bonds used to determine the discount rate for post-employment obligations must include all the high quality corporate bonds issued in a currency.
- BC150F Some respondents to the 2013 Annual Improvements Exposure Draft expressed concerns about the potential effects of the amendment on countries that have adopted a currency as their official or legal currency without being members of a regional market or part of one with a common currency. They think that the proposed amendment could result in anomalous outcomes in these countries, because a discount rate determined from high quality corporate bonds denominated in a stronger currency could be inconsistent with the inflation rate (and the other assumptions) used in these countries to determine the cost of providing post-employment benefits. The Board noted that this anomaly is not unique to the fact pattern raised. Instead, inflation rates in one location may be different to those in another, even if they are in the same country, state or regional market with a shared currency. In the Board's view, an analysis of the potential effect of the amendment would not provide useful additional information. The Board concluded that the amendment is an improvement that should not be delayed for a narrow range of situations that the Board had already considered in proposing the amendment.

Contributions from employees or third parties: amendments issued in 2013

BC150AG In 2012, the ~~IFRS~~ Interpretations Committee (~~the 'Interpretations Committee'~~) received two submissions that requested clarification of the accounting requirements set out in paragraph 93 of IAS 19 for contributions from employees or third parties.

BC150BH The Interpretations Committee considered whether some types of contributions from employees or third parties to a defined benefit plan should reduce the cost of short-term employee benefits instead of reducing the cost of post-employment benefits. The Interpretations Committee observed that the wording in paragraph 93 of IAS 19 appeared to suggest that all employee contributions that are linked to service should be attributed to periods of service as a reduction of service cost (ie as a negative benefit). However, employee contributions that are linked solely to the employee's service rendered in the same period in which those contributions are payable (for example, contributions that are a fixed percentage of salary throughout the period of the employment) might also be considered to be a reduction of the cost of short-term employee benefits (ie a reduction in salary). Consequently, the Interpretations Committee recommended to the IASB that it should amend IAS 19 regarding the accounting for such contributions.

BC150CI In the IASB's view, contributions from employees or third parties that are required by the terms of a defined benefit plan should form part of the post-employment benefit rather than the short-term employee benefit. Consequently, such contributions should be attributed to periods of service as a reduction of service cost (ie as a negative benefit). However, the IASB acknowledged the general concern about the complexity of the required calculations that could result from the requirement to attribute the net benefit to periods of service. The IASB thus concluded that the costs of applying the attribution requirements to some simple types of contributory plans outweighed the benefits and so the IASB decided to add a practical expedient to paragraph 93.

BC150DJ Consequently, in March 2013, the IASB published the Exposure Draft ED/2013/4 *Defined Benefit Plans: Employee Contributions* ('ED/2013/4'), which proposed amendments to paragraph 93 of IAS 19. In ED/2013/4 the IASB proposed that some contributions from employees or third parties may be excluded from being attributed to periods of service as a negative benefit. Instead, those contributions could be recognised as a reduction in the service cost in the period in which they are payable if, and only if, they are linked solely to the employee's service rendered in that period. An example of such a situation would be contributions based on an employee's salary at a fixed percentage that does not depend on the number of years of service by the employee to the employer. On the other hand, if an employee is required to contribute a higher percentage of salary in later years of service, then the contributions are not linked solely to the employee's service that is rendered in the period in which the contributions are payable.

BC150EK When developing ED/2013/4, the IASB observed that paragraph 93 first states that contributions from employees or third parties in respect of service are attributed to periods of service as a negative benefit in accordance with paragraph 70, and then states that the net benefit is attributed in accordance with paragraph 70. The references to both the negative benefit and net benefit might cause confusion as to whether the back-end loading test in paragraph 70 is required to be performed on the net benefit, or on the gross benefit and the negative benefit separately. The IASB observed that performing the test on the net benefit would add complexity and that the outcome of that test would differ from the outcome of performing the test on the gross benefit and the negative benefit separately. Consequently, the

IASB proposed to specify in paragraph 93 that the contributions from employees or third parties that are not solely linked to current-year service should be attributed to periods of service using the same method of attribution as the gross benefit in accordance with paragraph 70.

BC150F A total of 63 respondents commented on ED/2013/4. The majority of respondents supported the proposed amendments, but about half of them requested either further clarification of the scope of the practical expedient or the addition of application guidance or examples.

BC150G Some respondents requested clarification of whether they could apply the proposed practical expedient if the amount of the contributions depended on the employee's age instead of the number of years of service (age-based contributions). The IASB observed that examples illustrating the proposed practical expedient in ED/2013/4 implied two criteria—one is whether contributions are a fixed percentage of salary and the other is whether the contributions are independent of the number of years of service.

BC150H The IASB considered whether contributions should have to meet either or both of the criteria to qualify for the practical expedient. In some circumstances, age-based contributions could approximate contributions that depend on the number of years of service, because both of the contribution formulas depend on time. However, age-based contributions are independent of the number of years of service. For example, the terms of a plan require employee contributions of four per cent of salary for the first ten years and then six per cent thereafter. The increase to six per cent is not only related to the service in the current year, but is also related to the first ten years of service, which is a prerequisite for the change in the contribution percentage. If the terms of the plan required employee contributions of four per cent of salary if the employee was 30 years old or younger and six per cent if the employee was more than 30 years old, then an employee would be required to contribute either four per cent or six per cent regardless of the length of their service. In other words, the contributions paid for each year are not dependent on prior service.

BC150I Consequently, the IASB decided that the practical expedient should be permitted if the amount of the contributions is independent of the number of years of service. This principle would also help to clarify whether the practical expedient would apply to other types of contribution arrangements, including contributions that are a fixed amount (as opposed to a fixed percentage) regardless of the number of years of service.

BC150J One respondent to ED/2013/4 was concerned that some might interpret the requirements to attribute contributions from employees or third parties to periods of service to mean that the accumulated value of contributions should be deducted from both the defined benefit obligation and the plan assets. The IASB noted that the plan assets and the defined benefit obligation would increase by the amount of the contributions paid. This is because the contributions that are paid increase the employer's obligation to the employees even if those contributions are attributed to other periods of service to reflect the net cost to the employer.

BC150K When developing the amendments, the IASB observed that paragraph 94 sets out requirements for the accounting for changes in employee or third-party contributions. The IASB noted that the requirements in that paragraph apply to contributions that are attributed to periods of service using the same attribution method that is required by paragraph 70 for the gross benefit. Consequently, the IASB decided to amend paragraph 94 to clarify the scope of the requirements in that paragraph.

- (b) In financial statements for periods beginning before 1 January 2014, an entity need not provide comparatives for the disclosures about the sensitivity of the defined benefit obligation. The Board provided this exemption to provide sufficient lead time for entities to implement the necessary systems.

First-time adopters

- BC270 For entities adopting IFRSs for the first time, the amendments made in 2011 are to be applied retrospectively as required by IFRS 1 *First-time Adoption of International Financial Reporting Standards*. The Board included a temporary exemption for entities adopting IFRSs to use paragraph 173(b) for the same reasons as given in paragraph BC269(b).

Early application

- BC271 The amendments made in 2011 will improve the accounting and, in particular, the disclosures provided by a reporting entity in relation to its participation in defined benefit plans. In addition, some of the amendments address existing problems in applying IAS 19 in practice. The Board noted that the majority of the amendments made in 2011 are permitted by the previous version of IAS 19. Consequently, the Board permitted early application of all the amendments made in 2011.

Transition provisions for *Defined Benefit Plans: Employee Contributions*

- BC271A In ED/2013/4, the IASB proposed retrospective application and to permit earlier application of the amendments. The majority of the respondents supported those proposals. Some respondents questioned whether retrospective application was practicable because some calculations might require information that is not readily available. The IASB observed that in current practice, contributions from employees or third parties are generally reduced from service cost without being attributed to periods of service. The proposed amendments are intended to provide relief so that entities can deduct contributions from service cost in the period in which the service is rendered, which was common practice prior to the 2011 amendments to IAS 19. The impact of retrospective application would therefore be minimal in those cases. Consequently, the IASB decided to retain the requirement for retrospective application.
- BC271B The amendments to IAS 19 published in 2011 are effective for annual periods beginning on or after 1 January 2013. In the IASB's view, the objective of the amendments published in 2013 is to provide relief in the accounting for contributions from employees or third parties and, therefore, the effective date should be set as early as possible, while allowing jurisdictions to have sufficient time to prepare for the new requirements. Consequently, the IASB decided that the effective date of the amendments should be 1 July 2014, with earlier application permitted.

Annual Improvements to IFRSs 2012–2014 Cycle

- BC271C Annual Improvements to IFRSs 2012–2014 Cycle, issued in September 2014, amended paragraph 83. The Board noted that for some entities a full retrospective application of the amendment could be burdensome. Consequently, the Board decided that the amendment should be applied from the beginning of the earliest comparative period presented in the first financial statements in which an entity applies the amendment. Any initial adjustment arising from the application of the amendment should be recognised in opening retained earnings of the earliest comparative period presented.

HKAS 34
Revised November 2014 ~~December 2016~~

Effective for annual periods
beginning on or after 1 January 2005

Hong Kong Accounting Standard 34

Interim Financial Reporting



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

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CONTENTS

	<i>from paragraph</i>
INTRODUCTION	IN1
HONG KONG ACCOUNTING STANDARD 34 INTERIM FINANCIAL REPORTING	
OBJECTIVE	
SCOPE	1
DEFINITIONS	4
CONTENT OF AN INTERIM FINANCIAL REPORT	5
Minimum components of an interim financial report	8
Form and content of interim financial statements	9
Significant events and transactions	15
Other disclosures	16A
Disclosure of compliance with HKFRSs	19
Periods for which interim financial statements are required to be presented	20
Materiality	23
DISCLOSURE IN ANNUAL FINANCIAL STATEMENTS	26
RECOGNITION AND MEASUREMENT	28
Same accounting policies as annual	28
Revenues received seasonally, cyclically, or occasionally	37
Costs incurred unevenly during the financial year	39
Applying the recognition and measurement principles	40
Use of estimates	41
RESTATEMENT OF PREVIOUSLY REPORTED INTERIM PERIODS	43
WITHDRAWAL OF SSAP 25	45A
EFFECTIVE DATE	46
BASIS FOR CONCLUSIONS	
ILLUSTRATIVE EXAMPLES	
A Illustration of periods required to be presented	
B Examples of applying the recognition and measurement principles	
C Examples of the use of estimates	
APPENDIX	
Comparison with International Accounting Standards	

Hong Kong Accounting Standard 34 *Interim Financial Reporting* (HKAS 34) is set out in paragraphs 1-5457. All the paragraphs have equal authority. HKAS 34 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Conceptual Framework for Financial Reporting*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

- (d) a statement of cash flows for the period;
- (e) notes, comprising ~~a summary of~~ significant accounting policies and other explanatory information;
- (ea) comparative information in respect of the preceding period as specified in paragraphs 38 and 38A of HKAS 1; and
- (f) a statement of financial position as at the beginning of the preceding period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements in accordance with paragraph 40A-40D of HKAS 1.

An entity may use titles for the statements other than those used in this Standard. For example, an entity may use the title 'statement of comprehensive income' instead of 'statement of profit or loss and other comprehensive income'.

- 6 In the interest of timeliness and cost considerations and to avoid repetition of information previously reported, an entity may be required to or may elect to provide less information at interim dates as compared with its annual financial statements. This Standard defines the minimum content of an interim financial report as including condensed financial statements and selected explanatory notes. The interim financial report is intended to provide an update on the latest complete set of annual financial statements. Accordingly, it focuses on new activities, events, and circumstances and does not duplicate information previously reported.
- 7 Nothing in this Standard is intended to prohibit or discourage an entity from publishing a complete set of financial statements (as described in HKAS 1) in its interim financial report, rather than condensed financial statements and selected explanatory notes. Nor does this Standard prohibit or discourage an entity from including in condensed interim financial statements more than the minimum line items or selected explanatory notes as set out in this Standard. The recognition and measurement guidance in this Standard applies also to complete financial statements for an interim period, and such statements would include all of the disclosures required by this Standard (particularly the selected note disclosures in paragraph 16A) as well as those required by other HKFRSs.

Minimum components of an interim financial report

- 8 **An interim financial report shall include, at a minimum, the following components:**
- (a) **a condensed statement of financial position;**
 - (b) **a condensed statement or condensed statements of profit or loss and other comprehensive income;**
 - (c) **a condensed statement of changes in equity;**
 - (d) **a condensed statement of cash flows; and**
 - (e) **selected explanatory notes.**
- 8A **If an entity presents items of profit or loss in a separate statement as described in paragraph 10A of HKAS 1 (as amended in 2011), it presents interim condensed information from that statement.**

Form and content of interim financial statements

- 9 **If an entity publishes a complete set of financial statements in its interim financial report, the form and content of those statements shall conform to the requirements of HKAS 1 for a complete set of financial statements.**

- (h) changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, whether those assets or liabilities are recognised at fair value or amortised cost;
 - (i) any loan default or breach of a loan agreement that has not been remedied on or before the end of the reporting period;
 - (j) related party transactions;
 - (k) transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments;
 - (l) changes in the classification of financial assets as a result of a change in the purpose or use of those assets; and
 - (m) changes in contingent liabilities or contingent assets.
- 15C Individual HKFRSs provide guidance regarding disclosure requirements for many of the items listed in paragraph 15B. When an event or transaction is significant to an understanding of the changes in an entity's financial position or performance since the last annual reporting period, its interim financial report should provide an explanation of and an update to the relevant information included in the financial statements of the last annual reporting period.

16-18 [Deleted]

Other disclosures

- 16A In addition to disclosing significant events and transactions in accordance with paragraphs 15–15C, an entity shall include the following information, in the notes to its interim financial statements, ~~if not disclosed or elsewhere~~ in the interim financial report. The following disclosures shall be given either in the interim financial statements or incorporated by cross-reference from the interim financial statements to some other statement (such as management commentary or risk report) that is available to users of the financial statements on the same terms as the interim financial statements and at the same time. If users of the financial statements do not have access to the information incorporated by cross-reference on the same terms and at the same time, the interim financial report is incomplete. The information shall normally be reported on a financial year-to-date basis.
- (a) a statement that the same accounting policies and methods of computation are followed in the interim financial statements as compared with the most recent annual financial statements or, if those policies or methods have been changed, a description of the nature and effect of the change.
 - (b) explanatory comments about the seasonality or cyclicity of interim operations.
 - (c) the nature and amount of items affecting assets, liabilities, equity, net income, or cash flows that are unusual because of their nature, size, or incidence.
 - (d) the nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years.
 - (e) issues, repurchases, and repayments of debt and equity securities.
 - (f) dividends paid (aggregate or per share) separately for ordinary shares and other shares.
 - (g) the following segment information (disclosure of segment information is required in an entity's interim financial report only if HKFRS 8 *Operating Segments* requires that entity to disclose segment information in its annual financial statements):
 - (i) revenues from external customers, if included in the measure of segment profit or loss reviewed by the chief operating decision maker or otherwise regularly provided to the chief operating decision maker.
 - (ii) intersegment revenues, if included in the measure of segment profit or loss reviewed by the chief operating decision maker or otherwise regularly provided to the chief operating decision maker.

- 45 To allow accounting changes to be reflected as of an interim date within the financial year would allow two differing accounting policies to be applied to a particular class of transactions within a single financial year. The result would be interim allocation difficulties, obscured operating results, and complicated analysis and understandability of interim period information.

Withdrawal of SSAP 25

- 45A This Standard supersedes SSAP 25 *Interim Financial Reporting* (revised in 2001).

Effective date

- 46 **This Standard becomes operative for financial statements covering periods beginning on or after 1 January 2005. Earlier application is encouraged.**
- 47 **HKAS 1 (as revised in 2007) amended the terminology used throughout HKFRSs. In addition it amended paragraphs 4, 5, 8, 11, 12 and 20, deleted paragraph 13 and added paragraphs 8A and 11A. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. If an entity applies HKAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.**
- 48 **HKFRS 3 (as revised in 2008) amended paragraph 16(i). An entity shall apply that amendment for annual periods beginning on or after 1 July 2009. If an entity applies HKFRS 3 (revised 2008) for an earlier period, the amendment shall also be applied for that earlier period.**
- 49 **Paragraphs 15, 27, 35 and 36 were amended, paragraphs 15A–15C and 16A were added and paragraphs 16–18 were deleted by *Improvements to HKFRSs* issued in May 2010. An entity shall apply those amendments for annual periods beginning on or after 1 January 2011. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.**
- 50 HKFRS 13, issued in June 2011, added paragraph 16A(j). An entity shall apply that amendment when it applies HKFRS 13.
- 51 *Presentation of Items of Other Comprehensive Income* (Amendments to HKAS 1), issued in July 2011, amended paragraph 8, 8A, 11A and 20. An entity shall apply those amendments when it applies HKAS 1 as amended in July 2011.
- 52 *Annual Improvements 2009-2011 Cycle*, Issued in June 2012, amended paragraph 5 as a consequential amendment derived from the amendment to HKAS 1 *Presentation of Financial Statements*. An entity shall apply that amendment retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.
- 53 *Annual Improvements 2009-2011 Cycle*, issued in June 2012, amended paragraph 16A. An entity shall apply that amendment retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.
- 54 *Investment Entities* (Amendments to HKFRS 10, HKFRS 12 and HKAS 27 (2011)), issued in December 2012, amended paragraph 16A. An entity shall apply that amendment for annual periods beginning 1 January 2014. Earlier application of *Investment Entities* is permitted. If an entity applies that amendment earlier it shall also apply all amendments included in *Investment Entities* at the same time.
- 55 *[This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]*

- 56 Annual Improvements to HKFRSs 2012–2014 Cycle, issued in October 2014, amended paragraph 16A. An entity shall apply that amendment retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.
- 57 Disclosure Initiative (Amendments to HKAS 1), issued in January 2015, amended paragraph 5. An entity shall apply that amendment for annual periods beginning on or after 1 January 2016. Earlier application of that amendment is permitted.

Other disclosures incorporated by cross-reference to information outside the interim financial statements

- BC7 The Board received a request to clarify the meaning of disclosure of information 'elsewhere in the interim financial report' as used in IAS 34. The submitter noted that the definition of 'interim financial report' in paragraph 4 of IAS 34 was not sufficiently clear with respect to whether the interim financial report covers only the information reported under IFRS (meaning the IFRS interim financial statements) or whether it also includes management reports or other elements in addition to IFRS interim financial statements.
- BC8 The Board observed that presenting information 'elsewhere in the interim financial report' in accordance with paragraph 16A of IAS 34 is unclear. In the Exposure Draft *Annual Improvements to IFRSs 2012–2014 Cycle* (the '2013 Annual Improvements Exposure Draft'), published in December 2013, the Board proposed to clarify that an entity discloses information elsewhere in the interim financial report when it incorporates disclosures by cross-reference to information in another statement. This information should be available to users of the interim financial statements on the same terms as the interim financial statements and at the same time.
- BC9 Some respondents to the 2013 Annual Improvements Exposure Draft observed that the proposed amendment seemed to suggest that the interim financial report was not a single report and that, instead, it included multiple documents. In response to these comments, the Board observed that in accordance with paragraphs 4 and 8 of IAS 34, an interim financial report is a single report that includes a set of condensed financial statements and selected explanatory notes. The Board further clarified that the amendment is not extending the scope of the interim financial report, because the disclosures required in paragraph 16A(a)–(k) of IAS 34 are part of the selected explanatory notes (and therefore part of the interim financial report), even if they are presented in another statement, such as a management commentary or risk report. If they are not presented, the interim financial report would be incomplete.
- BC10 In response to the comments received on the 2013 Annual Improvements Exposure Draft the Board decided to clarify what was meant by the requirement that disclosures incorporated by cross-reference should be made available 'on the same terms' as the financial statements. This means that users of the financial statements should have access to the referenced material on the same basis as they have for accessing the financial statements from where the reference is made.

Hong Kong Accounting Standard 36

Impairment of Assets



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11 The ability of an intangible asset to generate sufficient future economic benefits to recover its carrying amount is usually subject to greater uncertainty before the asset is available for use than after it is available for use. Therefore, this Standard requires an entity to test for impairment, at least annually, the carrying amount of an intangible asset that is not yet available for use.

12 **In assessing whether there is any indication that an asset may be impaired, an entity shall consider, as a minimum, the following indications:**

External sources of information

- (a) **there are observable indications that the asset's value has declined during the period significantly more than would be expected as a result of the passage of time or normal use.**
- (b) **significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.**
- (c) **market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially.**
- (d) **the carrying amount of the net assets of the entity is more than its market capitalisation.**

Internal sources of information

- (e) **evidence is available of obsolescence or physical damage of an asset.**
- (f) **significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include the asset becoming idle, plans to discontinue or restructure the operation to which an asset belongs, plans to dispose of an asset before the previously expected date, and reassessing the useful life of an asset as finite rather than indefinite.***
- (g) **evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.**

Dividend from a subsidiary, joint venture or associate

- (h) **for an investment in a subsidiary, ~~jointly controlled entity~~ joint venture or associate, the investor recognises a dividend from the investment and evidence is available that:**
 - (i) **the carrying amount of the investment in the separate financial statements exceeds the carrying amounts in the consolidated**

* Once an asset meets the criteria to be classified as held for sale (or is included in a disposal group that is classified as held for sale), it is excluded from the scope of this Standard and is accounted for in accordance with HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

HKFRS 1 (Revised)
Revised ~~November~~ December 2016

Effective for annual periods
beginning on or after 1 July 2009

Hong Kong Financial Reporting Standards 1 (Revised)

First-time Adoption of Hong Kong Financial Reporting Standards



Hong Kong Institute of
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- 39S *Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance* (Amendments to HKFRS 10, HKFRS 11 and HKFRS 12), issued in July 2012, amended paragraph D31. An entity shall apply that amendment when it applies HKFRS 11 (as amended in July 2012).
- 39T *Investment Entities* (Amendments to HKFRS 10, HKFRS 12 and HKAS 27 (2011)), issued in December 2012, amended paragraphs D16, D17 and Appendix C and added a heading and paragraphs E6–E7. An entity shall apply those amendments for annual periods beginning on or after 1 January 2014. Earlier application of *Investment Entities* is permitted. If an entity applies those amendments earlier it shall also apply all amendments included in *Investment Entities* at the same time.
- 39U-V [This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]
- 39W Accounting for Acquisitions of Interests in Joint Operations (Amendments to HKFRS 11), issued in June 2014, amended paragraph C5. An entity shall apply that amendment in annual periods beginning on or after 1 January 2016. If an entity applies related amendments to HKFRS 11 from Accounting for Acquisitions of Interests in Joint Operations (Amendments to HKFRS 11) in an earlier period, the amendment to paragraph C5 shall be applied in that earlier period.
- 39X-Z [This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]
- 39AA Annual Improvements to HKFRSs 2012–2014 Cycle, issued in October 2014, added paragraph E4A. An entity shall apply that amendment for annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.

Withdrawal of HKFRS 1 (issued 2003)

- 40 This HKFRS supersedes HKFRS 1 (issued in 2003 and amended at December 2008).

shall decrease the carrying amount of goodwill accordingly (and, if applicable, adjust deferred tax and non-controlling interests).

- (ii) Regardless of whether there is any indication that the goodwill may be impaired, the first-time adopter shall apply HKAS 36 in testing the goodwill for impairment at the date of transition to HKFRSs and in recognising any resulting impairment loss in retained earnings (or, if so required by HKAS 36, in revaluation surplus). The impairment test shall be based on conditions at the date of transition to HKFRSs.
- (h) No other adjustments shall be made to the carrying amount of goodwill at the date of transition to HKFRSs. For example, the first-time adopter shall not restate the carrying amount of goodwill:
- (i) to exclude in-process research and development acquired in that business combination (unless the related intangible asset would qualify for recognition in accordance with HKAS 38 in the statement of financial position of the acquiree);
 - (ii) to adjust previous amortisation of goodwill;
 - (iii) to reverse adjustments to goodwill that HKFRS 3 would not permit, but were made in accordance with previous GAAP because of adjustments to assets and liabilities between the date of the business combination and the date of transition to HKFRSs.
- (i) If the first-time adopter recognised goodwill in accordance with previous GAAP as a deduction from equity:
- (i) it shall not recognise that goodwill in its opening HKFRS statement of financial position. Furthermore, it shall not reclassify that goodwill to profit or loss if it disposes of the subsidiary or if the investment in the subsidiary becomes impaired.
 - (ii) adjustments resulting from the subsequent resolution of a contingency affecting the purchase consideration shall be recognised in retained earnings.
- (j) In accordance with its previous GAAP, the first-time adopter may not have consolidated a subsidiary acquired in a past business combination (for example, because the parent did not regard it as a subsidiary in accordance with previous GAAP or did not prepare consolidated financial statements). The first-time adopter shall adjust the carrying amounts of the subsidiary's assets and liabilities to the amounts that HKFRSs would require in the subsidiary's statement of financial position. The deemed cost of goodwill equals the difference at the date of transition to HKFRSs between:
- (i) the parent's interest in those adjusted carrying amounts; and
 - (ii) the cost in the parent's separate financial statements of its investment in the subsidiary.
- (k) The measurement of non-controlling interests and deferred tax follows from the measurement of other assets and liabilities. Therefore, the above adjustments to recognised assets and liabilities affect non-controlling interests and deferred tax.

C5 The exemption for past business combinations also applies to past acquisitions of investments in associates, ~~and of interests in joint ventures and interests in joint operations in which the activity of the joint operation constitutes a business, as defined in HKFRS 3.~~ Furthermore, the date selected for paragraph C1 applies equally for all such acquisitions.

D11 [Deleted]

Cumulative translation differences

D12 HKAS 21 requires an entity:

- (a) to recognise some translation differences in other comprehensive income and accumulate these in a separate component of equity; and
- (b) on disposal of a foreign operation, to reclassify the cumulative translation difference for that foreign operation (including, if applicable, gains and losses on related hedges) from equity to profit or loss as part of the gain or loss on disposal.

D13 However, a first-time adopter need not comply with these requirements for cumulative translation differences that existed at the date of transition to HKFRSs. If a first-time adopter uses this exemption:

- (a) the cumulative translation differences for all foreign operations are deemed to be zero at the date of transition to HKFRSs; and
- (b) the gain or loss on a subsequent disposal of any foreign operation shall exclude translation differences that arose before the date of transition to HKFRSs and shall include later translation differences.

Investments in subsidiaries, joint ventures and associates

D14 When an entity prepares separate financial statements, HKAS 27 (as amended in 2008) requires it to account for its investments in subsidiaries, ~~jointly controlled entities~~ ventures and associates either:

- (a) at cost; or
- (b) in accordance with HKAS 39.

D15 If a first-time adopter measures such an investment at cost in accordance with HKAS 27, it shall measure that investment at one of the following amounts in its separate opening HKFRS statement of financial position:

- (a) cost determined in accordance with HKAS 27; or
- (b) deemed cost. The deemed cost of such an investment shall be its:
 - (i) fair value (determined in accordance with HKAS 39) at the entity's date of transition to HKFRSs in its separate financial statements; or
 - (ii) previous GAAP carrying amount at that date.

A first-time adopter may choose either (i) or (ii) above to measure its investment in each subsidiary, joint venture or associate that it elects to measure using a deemed cost.

Appendix E

Short-term exemptions from HKFRSs

This appendix is an integral part of the HKFRS.

[Paragraphs E1 and E2 are amendments that are not yet effective and are therefore not included in this edition.]

Disclosures about financial instruments

- E3 A first-time adopter may apply the transition provisions in paragraph 44G of HKFRS 7.*
- E4 A first-time adopter may apply the transitional provisions in paragraph 44M of HKFRS 7.†
- E4A A first-time adopter may apply the transition provisions in paragraph 44AA of HKFRS 7.

Employee benefits

- E5 A first-time adopter may apply the transition provisions in paragraph 173(b) of HKAS 19.

Investment entities

- E6 A first-time adopter that is a parent shall assess whether it is an investment entity, as defined in HKFRS 10, on the basis of the facts and circumstances that exist at the date of transition to HKFRSs.
- E7 A first-time adopter that is an investment entity, as defined in HKFRS 10, may apply the transition provisions in paragraphs C3C–C3D of HKFRS 10 and paragraphs 18C–18G of HKAS 27 (2011) if its first HKFRS financial statements are for an annual period ending on or before 31 December 2014. The references in those paragraphs to the annual period that immediately precedes the date of initial application shall be read as the earliest annual period presented. Consequently, the references in those paragraphs shall be read as the date of transition to HKFRSs.

* Paragraph E3 was added as a consequence of *Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters* (Amendment to HKFRS 1) issued in February 2010. To avoid the potential use of hindsight and to ensure that first-time adopters are not disadvantaged as compared with current HKFRS preparers, first-time adopters should be permitted to use the same transition provisions permitted for existing preparers of financial statements prepared in accordance with HKFRSs that are included in *Improving Disclosures about Financial Instruments* (Amendments to HKFRS 7).

† Paragraph E4 was added as a consequence of *Disclosures—Transfers of Financial Assets* (Amendments to HKFRS 7) issued in October 2010. To avoid the potential use of hindsight and to ensure that first-time adopters are not disadvantaged as compared with current HKFRS preparers, first-time adopters should be permitted to use the same transition provisions permitted for existing preparers of financial statements prepared in accordance with HKFRSs that are included in *Disclosures—Transfers of Financial Assets* (Amendments to HKFRS 7).

HKFRS 1 (Revised) BC
Revised ~~November~~ December 2016

Effective for annual periods
beginning on or after 1 July 2009

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

First-time Adoption of Hong Kong Financial Reporting Standards



Hong Kong Institute of
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Borrowing costs	BC63E
Severe hyperinflation	BC63F
Joint Arrangements	BC63K
Other possible exemptions rejected	BC64
Embedded derivatives	BC65
Hyperinflation	BC67
Intangible assets	BC68
Transaction costs: financial instruments	BC72
Retrospective designation	BC74
Hedge accounting	BC75
Government loans	BC80A
Available-for-sale financial assets	BC81
Estimates	BC84
PRESENTATION AND DISCLOSURE	BC85
Comparative information	BC85
Historical summaries	BC90
Explanation of transition to IFRSs	BC91
Interim financial reports	BC96
Accounting policy changes in the year of adoption	BC97
<u>SHORT-TERM EXEMPTIONS FROM IFRSs</u>	<u>BC98</u>
<u>Disclosures about financial instruments</u>	<u>BC98</u>

Interim financial reports

BC96 IAS 34 *Interim Financial Reporting* states that the interim financial report is ‘intended to provide an update on the latest complete set of annual financial statements’ (paragraph 6). Thus, IAS 34 requires less disclosure in interim financial statements than IFRSs require in annual financial statements. However, an entity’s interim financial report in accordance with IAS 34 is less helpful to users if the entity’s latest annual financial statements were prepared using previous GAAP than if they were prepared in accordance with IFRSs. Therefore, the Board concluded that a first-time adopter’s first interim financial report in accordance with IAS 34 should include sufficient information to enable users to understand how the transition to IFRSs affected previously reported annual, as well as interim, figures (paragraphs 32 and 33 of the IFRS).

Accounting policy changes in the year of adoption

BC97 In *Improvements to IFRSs* issued in May 2010, the Board clarified unclear wording concerning how changes in accounting policies should be addressed by a first-time adopter when those changes occur after the publication of the entity’s first interim financial report. The Board decided that a first-time adopter is exempt from all the requirements of IAS 8 for the interim financial report it presents in accordance with IAS 34 for part of the period covered by its first IFRS financial statements and for its first IFRS financial statements. The Board concluded that to comply with IFRS 1’s requirement to explain its transition to IFRSs, an entity should be required to explain any changes in its accounting policies or the IFRS 1 exemptions it applied between its first IFRS interim financial report and its first IFRS financial statements. The Board decided that the most useful information it could require was updated reconciliations between previous GAAP and IFRSs.

Short-term exemptions from IFRSs

Disclosures about financial instruments

BC98 Paragraph E4A of IFRS 1 was added as a consequence of *Annual Improvements to IFRSs 2012–2014 Cycle* issued in September 2014. To avoid the potential use of hindsight when this amendment first took effect, the Board decided that first-time adopters should be permitted to use the same transition provisions permitted for existing preparers of financial statements prepared in accordance with IFRSs that are included in *Annual Improvements to IFRSs 2012–2014 Cycle*.

Revised Guidance on Implementing HKFRS 4

Insurance Contracts



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- (j) underwriting pools, coinsurance and guarantee fund arrangements.
- (k) insurance contracts acquired in business combinations and portfolio transfers, and the treatment of related intangible assets.
- (l) as required by IAS 1, the judgements, apart from those involving estimations, management has made in the process of applying the accounting policies that have the most significant effect on the amounts recognised in the financial statements. The classification of discretionary participation features is an example of an accounting policy that might have a significant effect.

IG18 If the financial statements disclose supplementary information, for example embedded value information, that is not prepared on the basis used for other measurements in the financial statements, it is appropriate to explain the basis. Disclosures about embedded value methodology might include information similar to that described in paragraph IG17, as well as disclosure of whether, and how, embedded values are affected by estimated returns from assets and by locked-in capital and how those effects are estimated.

Assets, liabilities, income and expense

IG19 Paragraph 37(b) of the IFRS requires an insurer to disclose the assets, liabilities, income and expenses that arise from insurance contracts. If an insurer presents its statement of cash flows using the direct method, paragraph 37(b) requires it also to disclose the cash flows that arise from insurance contracts. The IFRS does not require disclosure of specific cash flows. The following paragraphs discuss how an insurer might satisfy those general requirements.

IG20 IAS 1 requires ~~minimum~~ disclosures in the statement of financial position. An insurer might conclude that, to satisfy those requirements, it needs to present separately in its statement of financial position the following amounts arising from insurance contracts:

- (a) liabilities under insurance contracts and reinsurance contracts issued.
- (b) assets under insurance contracts and reinsurance contracts issued.
- (c) assets under reinsurance ceded. Under paragraph 14(d)(i) of the IFRS, these assets are not offset against the related insurance liabilities.

IG21 Neither IAS 1 nor the IFRS prescribes the descriptions and ordering of the line items presented in the statement of financial position. An insurer could amend the descriptions and ordering to suit the nature of its transactions.

IG22 IAS 1 requires disclosure, either in the statement of financial position or in the notes, of subclassifications of the line items presented, classified in a manner appropriate to the entity's operations. Appropriate subclassifications of insurance liabilities will depend on the circumstances, but might include items such as:

- (a) unearned premiums.
- (b) claims reported by policyholders.
- (c) claims incurred but not reported (IBNR).
- (d) provisions arising from liability adequacy tests.
- (e) provisions for future non-participating benefits.

INSURANCE CONTRACTS

- (f) liabilities or components of equity relating to discretionary participation features (see paragraphs 34 and 35 of the IFRS). If an insurer classifies these features as a component of equity, disclosure is needed to comply with IAS 1, which requires an entity to disclose 'a description of the nature and purpose of each reserve within equity.'
 - (g) receivables and payables related to insurance contracts (amounts currently due to and from agents, brokers and policyholders related to insurance contracts).
 - (h) non-insurance assets acquired by exercising rights to recoveries.
- IG23 Similar subclassifications may also be appropriate for reinsurance assets, depending on their materiality and other relevant circumstances. For assets under insurance contracts and reinsurance contracts issued, an insurer might conclude that it needs to distinguish:
- (a) deferred acquisition costs; and
 - (b) intangible assets relating to insurance contracts acquired in business combinations or portfolio transfers.
- IG23A Paragraph 14 of IFRS 7 *Financial Instruments: Disclosures* requires an entity to disclose the carrying amount of financial assets pledged as collateral for liabilities, the carrying amount of financial assets pledged as collateral for contingent liabilities, and any terms and conditions relating to assets pledged as collateral. In complying with this requirement, an insurer might also conclude that it needs to disclose segregation requirements that are intended to protect policyholders by restricting the use of some of the insurer's assets.
- IG24 IAS 1 lists ~~minimum~~ line items that an entity should present in its statement of comprehensive income. It also requires the presentation of additional line items when this is necessary to present fairly the entity's financial performance. An insurer might conclude that, to satisfy these requirements, it needs to present the following amounts in its statement of comprehensive income:
- (a) revenue from insurance contracts issued (without any reduction for reinsurance held).
 - (b) income from contracts with reinsurers.
 - (c) expense for policyholder claims and benefits (without any reduction for reinsurance held).
 - (d) expenses arising from reinsurance held.
- IG25 IAS 18 requires an entity to disclose the amount of each significant category of revenue recognised during the period, and specifically requires disclosure of revenue arising from the rendering of services. Although revenue from insurance contracts is outside the scope of IAS 18, similar disclosures may be appropriate for insurance contracts. The IFRS does not prescribe a particular method for recognising revenue and various models exist:
- (a) Under some models, an insurer recognises premiums earned during the period as revenue and recognises claims arising during the period (including estimates of claims incurred but not reported) as an expense.
 - (b) Under some other models, an insurer recognises premiums received as revenue and at the same time recognises an expense representing the resulting increase in the insurance liability.

HKFRS 5
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Hong Kong Financial Reporting Standard 5

Non-current Assets Held for Sale and Discontinued Operations



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CONTENTS

	<i>from paragraph</i>
INTRODUCTION	IN1
HONG KONG FINANCIAL REPORTING STANDARD 5	
<i>NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS</i>	
OBJECTIVE	1
SCOPE	2
CLASSIFICATION OF NON-CURRENT ASSETS (OR DISPOSAL GROUPS) AS HELD FOR SALE OR AS HELD FOR DISTRIBUTION TO OWNERS	6
Non-current assets that are to be abandoned	13
MEASUREMENT OF NON-CURRENT ASSETS (OR DISPOSAL GROUPS) CLASSIFIED AS HELD FOR SALE	15
Measurement of a non-current asset (or disposal group)	15
Recognition of impairment losses and reversals	20
Changes to a plan of sale <u>or to a plan of distribution to owners</u>	26
PRESENTATION AND DISCLOSURE	30
Presenting discontinued operations	31
Gains or losses relating to continuing operations	37
Presentation of a non-current asset or disposal group classified as held for sale	38
Additional disclosures	41
TRANSITIONAL PROVISIONS	43
EFFECTIVE DATE	44
WITHDRAWAL OF SSAP 33	45
APPENDICES	
A Defined terms	
B Application supplement	
Extension of the period required to complete a sale	
C Amendments to other HKFRSs	
D Comparison with International Financial Reporting Standards	
E Amendments resulting from other HKFRSs	

- 19 On subsequent remeasurement of a disposal group, the carrying amounts of any assets and liabilities that are not within the scope of the measurement requirements of this HKFRS, but are included in a disposal group classified as held for sale, shall be remeasured in accordance with applicable HKFRSs before the fair value less costs to sell of the disposal group is remeasured.

Recognition of impairment losses and reversals

- 20 An entity shall recognise an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell, to the extent that it has not been recognised in accordance with paragraph 19.
- 21 An entity shall recognise a gain for any subsequent increase in fair value less costs to sell of an asset, but not in excess of the cumulative impairment loss that has been recognised either in accordance with this HKFRS or previously in accordance with HKAS 36 *Impairment of Assets*.
- 22 An entity shall recognise a gain for any subsequent increase in fair value less costs to sell of a disposal group:
- (a) to the extent that it has not been recognised in accordance with paragraph 19; but
 - (b) not in excess of the cumulative impairment loss that has been recognised, either in accordance with this HKFRS or previously in accordance with HKAS 36, on the non-current assets that are within the scope of the measurement requirements of this HKFRS.
- 23 The impairment loss (or any subsequent gain) recognised for a disposal group shall reduce (or increase) the carrying amount of the non-current assets in the group that are within the scope of the measurement requirements of this HKFRS, in the order of allocation set out in paragraphs 104(a) and (b) and 122 of HKAS 36.
24. A gain or loss not previously recognised by the date of the sale of a non-current asset (or disposal group) shall be recognised at the date of derecognition. Requirements relating to derecognition are set out in:
- (a) paragraphs 67-72 of HKAS 16 for property, plant and equipment, and
 - (b) paragraphs 112-117 of HKAS 38 *Intangible Assets* for intangible assets.
- 25 An entity shall not depreciate (or amortise) a non-current asset while it is classified as held for sale or while it is part of a disposal group classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale shall continue to be recognised.

Changes to a plan of sale or to a plan of distribution to owners

- 26 If an entity has classified an asset (or disposal group) as held for sale or as held for distribution to owners, but the criteria in paragraphs 7–9 (for held for sale) or in paragraph 12A (for held for distribution to owners) are no longer met, the entity shall cease to classify the asset (or disposal group) as held for sale or held for distribution to owners (respectively). In such cases an entity shall follow the guidance in paragraphs 27–29 to account for this change except when paragraph 26A applies.
- 26A If an entity reclassifies an asset (or disposal group) directly from being held for sale to being held for distribution to owners, or directly from being held for distribution to owners to being held for sale, then the change in classification is considered a continuation of the original plan of disposal. The entity:
- (a) shall not follow the guidance in paragraphs 27–29 to account for this change. The entity shall apply the classification, presentation and measurement requirements in this HKFRS that are applicable to the new method of disposal.
 - (b) shall measure the non-current asset (or disposal group) by following the requirements in paragraph 15 (if reclassified as held for sale) or 15A (if reclassified as held for distribution to owners) and recognise any reduction or increase in the fair value less costs to sell/costs to distribute of the non-current asset (or disposal group) by following the requirements in paragraphs 20–25.
 - (c) shall not change the date of classification in accordance with paragraphs 8 and 12A. This does not preclude an extension of the period required to complete a sale or a distribution to owners if the conditions in paragraph 9 are met.
- 27 The entity shall measure a non-current asset (or disposal group) that ceases to be classified as held for sale or as held for distribution to owners (or ceases to be included in a disposal group classified as held for sale or as held for distribution to owners) at the lower of:
- (a) its carrying amount before the asset (or disposal group) was classified as held for sale or as held for distribution to owners, adjusted for any depreciation, amortisation or revaluations that would have been recognised had the asset (or disposal group) not been classified as held for sale or as held for distribution to owners, and
 - (b) its *recoverable amount* at the date of the subsequent decision not to sell or distribute. [footnote omitted]

- 28 The entity shall include any required adjustment to the carrying amount of a non-current asset that ceases to be classified as held for sale or as held for distribution to owners in profit or loss [footnote omitted] from continuing operations in the period in which the criteria in paragraphs 7–9 or 12A, respectively, are no longer met. Financial statements for the periods since classification as held for sale or as held for distribution to owners shall be amended accordingly if the disposal group or non-current asset that ceases to be classified as held for sale or as held for distribution to owners is a subsidiary, joint operation, joint venture, associate, or a portion of an interest in a joint venture or an associate. The entity shall present that adjustment in the same caption in the statement of comprehensive income used to present a gain or loss, if any, recognised in accordance with paragraph 37.
- 29 If an entity removes an individual asset or liability from a disposal group classified as held for sale, the remaining assets and liabilities of the disposal group to be sold shall continue to be measured as a group only if the group meets the criteria in paragraphs 7–9. If an entity removes an individual asset or liability from a disposal group classified as held for distribution to owners, the remaining assets and liabilities of the disposal group to be distributed shall continue to be measured as a group only if the group meets the criteria in paragraph 12A. Otherwise, the remaining non-current assets of the group that individually meet the criteria to be classified as held for sale (or as held for distribution to owners) shall be measured individually at the lower of their carrying amounts and fair values less costs to sell (or costs to distribute) at that date. Any non-current assets that do not meet the criteria for held for sale shall cease to be classified as held for sale in accordance with paragraph 26. Any non-current assets that do not meet the criteria for held for distribution to owners shall cease to be classified as held for distribution to owners in accordance with paragraph 26.

Presentation and disclosure

- 30 An entity shall present and disclose information that enables users of the financial statements to evaluate the financial effects of discontinued operations and disposals of non-current assets (or disposal groups).**

Presenting discontinued operations

- 31 *A component of an entity* comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity. In other words, a component of an entity will have been a cash-generating unit or a group of cash-generating units while being held for use.
- 32 A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and
- (a) represents a separate major line of business or geographical area of operations,

an entity applies HKAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.

- 44B HKAS 27 *Consolidated and Separate Financial Statements* (as amended in 2008) added paragraph 33(d). An entity shall apply that amendment for annual periods beginning on or after 1 July 2009. If an entity applies HKAS 27 (amended 2008) for an earlier period, the amendment shall be applied for that earlier period. The amendment shall be applied retrospectively.
- 44C Paragraphs 8A and 36A were added by *Improvements to HKFRSs* issued in October 2008. An entity shall apply those amendments for annual periods beginning on or after 1 July 2009. Earlier application is permitted. However, an entity shall not apply the amendments for annual periods beginning before 1 July 2009 unless it also applies HKAS 27 (as amended in March 2008). If an entity applies the amendments before 1 July 2009 it shall disclose that fact. An entity shall apply the amendments prospectively from the date at which it first applied HKFRS 5, subject to the transitional provisions in paragraph 45 of HKAS 27 (amended March 2008).
- 44D Paragraphs 5A, 12A and 15A were added and paragraph 8 was amended by Hong Kong (IFRIC) Interpretation 17 *Distributions of Non-cash Assets to Owners* in December 2008. Those amendments shall be applied prospectively to non-current assets (or disposal groups) that are classified as held for distribution to owners in annual periods beginning on or after 1 July 2009. Retrospective application is not permitted. Earlier application is permitted. If an entity applies the amendments for a period beginning before 1 July 2009 it shall disclose that fact and also apply HKFRS 3 *Business Combinations* (as revised in 2008), HKAS 27 (as amended in March 2008) and Hong Kong (IFRIC) Interpretation 17.
- 44E Paragraph 5B was added by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment prospectively for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.
- 44F *[This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]*
- 44G *HKFRS 11 Joint Arrangements, issued in June 2011, amended paragraph 28. An entity shall apply that amendment when it applies HKFRS 11.*
- 44H *HKFRS 13 Fair Value Measurement, issued in June 2011, amended the definition of fair value in Appendix A. An entity shall apply that amendment when it applies HKFRS 13.*
- 44I *Presentation of Items of Other Comprehensive Income (Amendments to HKAS 1), issued in July 2011, amended paragraph 33A. An entity shall apply that amendment when it applies HKAS 1 as amended in July 2011.*
- 44J *[This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]*
- 44K *[This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]*

44L Annual Improvements to HKFRSs 2012–2014 Cycle, issued in October 2014, amended paragraphs 26–29 and added paragraph 26A. An entity shall apply those amendments prospectively in accordance with HKAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to changes in a method of disposal that occur in annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

Withdrawal of ssap 33

45 This HKFRS supersedes SSAP 33 *Discontinuing Operations*.

*Basis for Conclusions on
Hong Kong Financial Reporting Standard 5*

Non-current Assets Held for Sale and Discontinued Operations



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HKFRS 5 is based on IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*. In approving HKFRS 5, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IFRS 5. Accordingly, there are no significant differences between HKFRS 5 and IFRS 5. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IFRS 5 referred to below generally correspond with those in HKFRS 5.

CONTENTS

from paragraph

BASIS FOR CONCLUSIONS ON IFRS 5 NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

INTRODUCTION	BC1
SCOPE OF THE IFRS	BC8
CLASSIFICATION OF NON-CURRENT ASSETS TO BE DISPOSED OF AS HELD FOR SALE	BC15
Plan to sell the controlling interest in a subsidiary	BC24A
Assets to be exchanged for other non-current assets	BC25
MEASUREMENT OF NON-CURRENT ASSETS HELD FOR SALE	BC28
The allocation of an impairment loss to a disposal group	BC39
Newly acquired assets	BC42
Recognition of subsequent increases in fair value less costs to sell	BC46
Recognition of impairment losses and subsequent gains for assets that, before classification as held for sale, were measured at revalued amounts in accordance with another IFRS	BC47
Measurement of assets reclassified as held for use	BC49
REMOVAL OF EXEMPTION FROM CONSOLIDATION FOR SUBSIDIARIES ACQUIRED AND HELD EXCLUSIVELY WITH A VIEW TO RESALE	BC52
PRESENTATION OF NON-CURRENT ASSETS HELD FOR SALE	BC56
TIMING OF CLASSIFICATION AS, AND DEFINITION OF, DISCONTINUED OPERATIONS	BC59
CHANGES TO A PLAN OF SALE (AMENDMENT 2011)	BC72A
<u>CHANGES TO A PLAN OF SALE OR TO A PLAN OF DISTRIBUTION TO OWNERS</u>	<u>BC72B</u>
PRESENTATION OF DISCONTINUED OPERATIONS	BC73
TRANSITIONAL ARRANGEMENTS	BC78
TERMINOLOGY	BC80
SUMMARY OF CHANGES FROM ED 4	BC84
COMPARISON WITH RELEVANT ASPECTS OF SFAS 144	BC85

DISSENTING OPINIONS

APPENDIX

Amendments resulting from other Basis for Conclusions

BC72 Lastly, the Board considered whether newly acquired subsidiaries that meet the criteria to be classified as held for sale should always be classified as discontinued. The Board concluded that they should be so classified because they are being disposed of for one of the following reasons:

- (a) the subsidiary is in a different line of business from the entity, so disposing of it is similar to disposing of a major line of business.
- (b) the subsidiary is required to be disposed of by regulators because the entity would otherwise have too much of a particular type of operation in a particular geographical area. In such a case the subsidiary must be a significant operation.

Changes to a plan of sale (amendment 2011)

BC72A During its redeliberation of the exposure draft ED 9 *Joint Arrangements* the Board decided that if a disposal group or non-current asset that ceases to be classified as held for sale is a subsidiary, a joint operation, a joint venture, an associate, or a portion of an interest in a joint venture or associate, an entity should amend its financial statements for the periods since the classification as held for sale was made.

Changes to a plan of sale or to a plan of distribution to owners

BC72B The Board received a request to clarify the accounting for a change in a disposal plan from a plan to sell to a plan to distribute a dividend in kind to its shareholders. Paragraph 26 of IFRS 5 was interpreted by some, but not all, as requiring this change to be considered as a change to a plan of sale that would be accounted for in accordance with paragraphs 27–29 of IFRS 5.

BC72C In analysing this issue the Board observed that there was no specific guidance in IFRS 5 for the discontinuation of held-for-distribution accounting, when an entity determines that the asset (or disposal group) is no longer available for immediate distribution to owners or that the distribution to owners is no longer ‘highly probable’, in accordance with paragraph 12A of IFRS 5.

BC72D The Board observed that IFRIC 17 *Distribution of Non-cash Assets to Owners* amended IFRS 5 by adding paragraphs 5A, 12A and 15A to provide guidance for the held-for-distribution classification. However, this amendment did not provide guidance for when an entity reclassifies an asset (or disposal group) from held for sale to held for distribution to owners (or vice versa), or when held-for-distribution accounting is discontinued. The Board noted that paragraphs 27–29 of IFRS 5 should have been considered for amendment by IFRIC 17 and the fact that they were not amended at the time was an oversight.

BC72E The Board observed that the current guidance in IFRS 5 could be read in a way that a change from a plan to sell a non-current asset (or disposal group) to a plan to distribute a non-current asset (or disposal group) automatically results in a change to a plan of sale and that the guidance in paragraphs 27–29 of IFRS 5 should be applied.

BC72F The Board observed that, consistently with paragraphs 5A of IFRS 5 and BC60 of IFRIC 17, it was the intention of the Board to have consistent criteria and accounting requirements for an asset (or disposal group) classified as held for sale and for an asset (or disposal group) classified as held for distribution to owners. In addition:

- (a) the conditions required by paragraph 8 of IFRS 5 for a sale to be considered highly probable are similar to the conditions required by paragraph 12A of IFRS 5 for a distribution to owners to be considered highly probable, so they should be accounted for in the same way; and
- (b) paragraph 5A of IFRS 5 confirms that the classification, presentation and measurement requirements in IFRS 5 that are applicable for an asset (or disposal group) that is classified as held for sale also apply to an asset (or disposal group) that is classified as held for distribution to owners.

BC72G The Board noted that, on the basis of the current guidance in paragraphs 5A, 8 and 12A of IFRS 5 and the explanations in the Basis for Conclusions on IFRIC 17, the change from being held for sale to held for distribution to owners (or vice versa) when an entity reclassifies an asset (or disposal group) directly from one method of disposal to the other should not be considered a new plan (to sell or distribute). Instead, it should be treated as a continuation of the original plan. This means that an entity moves from one method of disposal to the other without any time lag, so that there is no interruption of the application of the requirements in IFRS 5. This would involve applying the classification, presentation and measurement requirements required for each type of disposal in IFRS 5.

BC72H Consequently, when an entity reclassifies an asset (or disposal group) directly from held for sale to held for distribution to owners (or vice versa), the Board decided to clarify that such a reclassification shall not be treated as a change to a plan of sale (or distribution to owners) and an entity shall not follow the guidance in paragraphs 27–29 of IFRS 5 to account for this change.

BC72I In response to the comments received on the Exposure Draft *Annual Improvements to IFRSs 2012–2014 Cycle* (the ‘2013 Annual Improvements Exposure Draft’), published in December 2013, the Board clarified that at the time of the change in the disposal plan, an entity would need to measure the non-current asset (or disposal group) in accordance with paragraph 15 or 15A of IFRS 5, and recognise any write-down in value (impairment loss) or gain for the subsequent increase in the fair value less costs to sell/costs to distribute a non-current asset (or disposal group) in accordance with paragraphs 20–25 of IFRS 5.

BC72J In response to the comments received on the 2013 Annual Improvements Exposure Draft, the Board further clarified that a change from being held for sale to held for distribution to owners (or vice versa) via a direct reclassification is not a new plan of disposal and does not change the requirements in IFRS 5 to determine whether a sale (or a distribution to owners) is highly probable, in accordance with paragraph 8 (or 12A) of IFRS 5. Consequently, the determination of the 12-month period should not restart when such a change in the method of disposal occurs, but should instead continue to be the same as initially determined by management in its assessment of whether the sale and/or distribution to owners is highly probable. The Board also noted that the period required to complete a sale or distribution to owners can be extended if the conditions in paragraph 9 of IFRS 5 are met. The Board noted that when an entity changes its planned method of disposal via a direct reclassification, it does not restate prior periods to reflect the new method of disposal.

BC72K To address the lack of guidance in circumstances when an asset no longer meets the criteria for held for distribution to owners (without meeting the held-for-sale criteria), the Board decided to clarify that an entity should cease to apply held-for-distribution accounting in the same way as it ceases to apply the held-for-sale accounting when it no longer meets the held-for-sale criteria.

BC72L In response to the comments received on the 2013 Annual Improvements Exposure Draft, the Board concluded that the amendments to IFRS 5 are required to be applied, on a prospective basis, to changes in the method of disposal that occur after the first application of the amendments. This is because this requirement is consistent with the transition requirements provided by IFRIC 17 when it amended IFRS 5 (see paragraph 44D of IFRS 5). The Board considered that prospective application is also required to avoid the potential use of hindsight, because an entity might not have collected all the relevant information at the time of the change in the plan to allow the entity to account for this change.

Presentation of discontinued operations

BC73 SFAS 144 requires the results of a discontinued operation to be presented as a separate component in the income statement (net of income tax) for all periods presented.

BC74 IAS 35 did not require the results of a discontinuing operation to be presented as a net amount on the face of the income statement. Instead, specified items are disclosed either in the notes or on the face of the income statement.

BC75 In ED 4, the Board noted that it was considering the presentation of discontinued operations in the income statement in its project on reporting comprehensive income and that it did not wish to prejudge the outcome of that project by changing the requirements of IAS 35 in respect of the components to be disclosed. Given that the project on reporting comprehensive income will not be completed as soon as previously expected, the Board decided to proceed with its decisions on the presentation of discontinued operations in this IFRS.

BC76 The Board believes that discontinued operations should be shown in a section of the income statement separately from continuing operations because of the different cash flows expected to arise from the two types of operations. The Board concluded that it is sufficient to show a single net figure for discontinued operations on the face of the income statement because of the limited future cash flows expected to arise from the operations. The IFRS therefore permits an analysis of the single net amount to be presented either in the notes or in the income statement.*

* IAS *Presentation of Financial Statements* (as revised in 2007) requires an entity to present all income and expense items in one statement of comprehensive income or in two statements (a separate income statement and a statement of comprehensive income).

BC77 A substantial majority of the respondents to ED 4 supported such a presentation.

BC77A The Board considered the comments received on the draft amendments in the 2007 exposure draft of proposed *Improvements to International Financial Reporting Standards*. Some respondents asked the Board to clarify the effects of the proposed amendment on the income statement when the disposal group meets the definition of a discontinued operation. The Board concluded that when a subsidiary is a disposal group that meets the definition of a discontinued operation in accordance with paragraph 32, an entity that is committed to a sale plan involving loss of control of the subsidiary should disclose the information required by paragraphs 33-36. The Board agreed with respondents that presentation should not differ simply because of the form of the disposal group.

HKFRS 7
Revised November 2014 December 2016

Effective for annual periods
beginning on or after 1 January 2007

Hong Kong Financial Reporting Standard 7

Financial Instruments: Disclosures



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- (b) total interest income and total interest expense (calculated using the effective interest method) for financial assets or financial liabilities that are not at fair value through profit or loss;
- (c) fee income and expense (other than amounts included in determining the effective interest rate) arising from:
 - (i) financial assets or financial liabilities that are not at fair value through profit or loss; and
 - (ii) trust and other fiduciary activities that result in the holding or investing of assets on behalf of individuals, trusts, retirement benefit plans, and other institutions;
- (d) interest income on impaired financial assets accrued in accordance with paragraph AG93 of HKAS 39; and
- (e) the amount of any impairment loss for each class of financial asset.

Other disclosures

Accounting policies

- 21 In accordance with paragraph 117 of HKAS 1 *Presentation of Financial Statements* (as revised 2007), an entity discloses, ~~in the summary of its~~ significant accounting policies, comprising the measurement basis (or bases) used in preparing the financial statements and the other accounting policies used that are relevant to an understanding of the financial statements.

Hedge accounting

- 22 An entity shall disclose the following separately for each type of hedge described in HKAS 39 (ie fair value hedges, cash flow hedges, and hedges of net investments in foreign operations):
- (a) a description of each type of hedge;
 - (b) a description of the financial instruments designated as hedging instruments and their fair values at the end of the reporting period; and
 - (c) the nature of the risks being hedged.
- 23 For cash flow hedges, an entity shall disclose:
- (a) the periods when the cash flows are expected to occur and when they are expected to affect profit or loss;
 - (b) a description of any forecast transaction for which hedge accounting had previously been used, but which is no longer expected to occur;
 - (c) the amount that was recognised in other comprehensive income during the period;
 - (d) the amount that was reclassified from equity to profit or loss for the period, showing the amount included in each line item in the statement of comprehensive income; and
 - (e) the amount that was removed from equity during the period and included in the initial cost or other carrying amount of a non-financial asset or non-financial liability whose acquisition or incurrence was a hedged highly probable forecast transaction.

- 44G *Improving Disclosures about Financial Instruments* (Amendments to HKFRS 7), issued in March 2009, amended paragraphs 27, 39 and B11 and added paragraphs 27A, 27B, B10A and B11A–B11F. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. An entity need not provide the disclosures required by the amendments for:
- (a) any annual or interim period, including any statement of financial position, presented within an annual comparative period ending before 31 December 2009, or
 - (b) any statement of financial position as at the beginning of the earliest comparative period as at a date before 31 December 2009.

Earlier application is permitted. If an entity applies the amendments for an earlier period, it shall disclose that fact.

44H-44J [These paragraphs refer to amendments with an effective date after 1 January 2013, and are therefore not included in this edition.]

44K Paragraph 44B was amended by *Improvements to HKFRSs* issued in May 2010. An entity shall apply that amendment for annual periods beginning on or after 1 July 2010. Earlier application is permitted.

44L *Improvements to HKFRSs* issued in May 2010 added paragraph 32A and amended paragraphs 34 and 36–38. An entity shall apply those amendments for annual periods beginning on or after 1 January 2011. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

44M *Disclosures—Transfers of Financial Assets* (Amendments to HKFRS 7), issued in October 2010, deleted paragraph 13 and added paragraphs 42A–42H and B29–B39. An entity shall apply those amendments for annual periods beginning on or after 1 July 2011. Earlier application is permitted. If an entity applies the amendments from an earlier date, it shall disclose that fact. An entity need not provide the disclosures required by those amendments for any period presented that begins before the date of initial application of the amendments.

44N [This paragraph refers to amendments with an effective date after 1 January 2013, and is therefore not included in this edition.]

44O HKFRS 10 and HKFRS 11 *Joint Arrangements*, issued in June 2011, amended paragraph 3. An entity shall apply that amendment when it applies HKFRS 10 and HKFRS 11.

44P HKFRS 13, issued in June 2011, amended paragraphs 3, 28 and 29 and Appendix A and deleted paragraphs 27-27B. An entity shall apply those amendments when it applies HKFRS 13.

44Q *Presentation of Items of Other Comprehensive Income* (Amendments to HKAS 1), issued in July 2011, amended paragraph 27B. An entity shall apply that amendment when it applies HKAS 1 as amended in June 2011.

44R *Disclosures—Offsetting Financial Assets and Financial Liabilities* (Amendments to HKFRS 7), issued in December 2011, added paragraphs 13A-13F and B40-B53. An entity shall apply those amendments for annual periods beginning on or after 1 January 2013 ~~and interim periods within those annual periods~~. An entity shall provide the disclosures required by those amendments retrospectively.

Paragraph 44G was amended as a consequence of *Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters* (Amendment to HKFRS 1) issued in February 2010. The HKICPA amended paragraph 44G to clarify its conclusions and intended transition for *Improving Disclosures about Financial Instruments* (Amendments to HKFRS 7).

Withdrawal of HKAS 30

44X *Investment Entities* (Amendments to HKFRS 10, HKFRS 12 and HKAS 27 (2011)), issued in December 2012, amended paragraph 3. An entity shall apply that amendment for annual periods beginning on or after 1 January 2014. Earlier application of *Investment Entities* is permitted. If an entity applies that amendment earlier it shall also apply all amendments included in *Investment Entities* at the same time.

44Y-ZA [This paragraph refers to amendments that are not yet effective, and is therefore not included in this edition.]

44AA *Annual Improvements to HKFRSs 2012–2014 Cycle*, issued in October 2014, amended paragraphs 44R and B30 and added paragraph B30A. An entity shall apply those amendments retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for annual periods beginning on or after 1 January 2016, except that an entity need not apply the amendments to paragraphs B30 and B30A for any period presented that begins before the annual period for which the entity first applies those amendments. Earlier application of the amendments to paragraphs 44R, B30 and B30A is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

44BB *Disclosure Initiative* (Amendments to HKAS 1), issued in January 2015, amended paragraphs 21 and B5. An entity shall apply those amendments for annual periods beginning on or after 1 January 2016. Earlier application of those amendments is permitted.

45 This HKFRS supersedes HKAS 30 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*.

- (e) how net gains or net losses on each category of financial instrument are determined (see paragraph 20(a)), for example, whether the net gains or net losses on items at fair value through profit or loss include interest or dividend income.
- (f) the criteria the entity uses to determine that there is objective evidence that an impairment loss has occurred (see paragraph 20(e)).
- (g) when the terms of financial assets that would otherwise be past due or impaired have been renegotiated, the accounting policy for financial assets that are the subject of renegotiated terms.

Paragraph 122 of HKAS 1 (as revised in 2007) also requires entities to disclose, ~~in the summary of along with its~~ significant accounting policies or other notes, the judgements, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Nature and extent of risks arising from financial instruments (paragraphs 31-42)

- B6 The disclosures required by paragraphs 31-42 shall be either given in the financial statements or incorporated by cross-reference from the financial statements to some other statement, such as a management commentary or risk report, that is available to users of the financial statements on the same terms as the financial statements and at the same time. Without the information incorporated by cross-reference, the financial statements are incomplete.

Quantitative disclosures (paragraph 34)

- B7 Paragraph 34(a) requires disclosures of summary quantitative data about an entity's exposure to risks based on the information provided internally to key management personnel of the entity. When an entity uses several methods to manage a risk exposure, the entity shall disclose information using the method or methods that provide the most relevant and reliable information. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* discusses relevance and reliability.
- B8 Paragraph 34(c) requires disclosures about concentrations of risk. Concentrations of risk arise from financial instruments that have similar characteristics and are affected similarly by changes in economic or other conditions. The identification of concentrations of risk requires judgement taking into account the circumstances of the entity. Disclosure of concentrations of risk shall include:
- (a) a description of how management determines concentrations;
 - (b) a description of the shared characteristic that identifies each concentration (eg counterparty, geographical area, currency or market); and
 - (c) the amount of the risk exposure associated with all financial instruments sharing that characteristic.

Maximum credit risk exposure (paragraph 36(a))

- B9 Paragraph 36(a) requires disclosure of the amount that best represents the entity's maximum exposure to credit risk. For a financial asset, this is typically the gross carrying amount, net of:
- (a) any amounts offset in accordance with HKAS 32; and
 - (b) any impairment losses recognised in accordance with HKAS 39.

circumstances to make payments in respect of the transferred financial asset in the future. The term 'payment' in this context does not include cash flows of the transferred financial asset that an entity collects and is required to remit to the transferee.

B30A When an entity transfers a financial asset, the entity may retain the right to service that financial asset for a fee that is included in, for example, a servicing contract. The entity assesses the servicing contract in accordance with the guidance in paragraphs 42C and B30 to decide whether the entity has continuing involvement as a result of the servicing contract for the purposes of the disclosure requirements. For example, a servicer will have continuing involvement in the transferred financial asset for the purposes of the disclosure requirements if the servicing fee is dependent on the amount or timing of the cash flows collected from the transferred financial asset. Similarly, a servicer has continuing involvement for the purposes of the disclosure requirements if a fixed fee would not be paid in full because of non-performance of the transferred financial asset. In these examples, the servicer has an interest in the future performance of the transferred financial asset. This assessment is independent of whether the fee to be received is expected to compensate the entity adequately for performing the servicing.

B31 Continuing involvement in a transferred financial asset may result from contractual provisions in the transfer agreement or in a separate agreement with the transferee or a third party entered into in connection with the transfer.

Transferred financial assets that are not derecognised in their entirety (paragraph 42D)

B32 Paragraph 42D requires disclosures when part or all of the transferred financial assets do not qualify for derecognition. Those disclosures are required at each reporting date at which the entity continues to recognise the transferred financial assets, regardless of when the transfers occurred.

Types of continuing involvement (paragraphs 42E–42H)

B33 Paragraphs 42E–42H require qualitative and quantitative disclosures for each type of continuing involvement in derecognised financial assets. An entity shall aggregate its continuing involvement into types that are representative of the entity's exposure to risks. For example, an entity may aggregate its continuing involvement by type of financial instrument (eg guarantees or call options) or by type of transfer (eg factoring of receivables, securitisations and securities lending).

Maturity analysis for undiscounted cash outflows to repurchase transferred assets (paragraph 42E(e))

B34 Paragraph 42E(e) requires an entity to disclose a maturity analysis of the undiscounted cash outflows to repurchase derecognised financial assets or other amounts payable to the transferee in respect of the derecognised financial assets, showing the remaining contractual maturities of the entity's continuing involvement. This analysis distinguishes cash flows that are required to be paid (eg forward contracts), cash flows that the entity may be required to pay (eg written put options) and cash flows that the entity might choose to pay (eg purchased call options).

- B35 An entity shall use its judgement to determine an appropriate number of time bands in preparing the maturity analysis required by paragraph 42E(e). For example, an entity might determine that the following maturity time bands are appropriate:
- (a) not later than one month;
 - (b) later than one month and not later than three months;
 - (c) later than three months and not later than six months;
 - (d) later than six months and not later than one year;
 - (e) later than one year and not later than three years;
 - (f) later than three years and not later than five years; and
 - (g) more than five years.
- B36 If there is a range of possible maturities, the cash flows are included on the basis of the earliest date on which the entity can be required or is permitted to pay.

*Basis for Conclusions on
Hong Kong Financial Reporting Standard 7*

Financial Instruments: Disclosures



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Allowance account for credit losses	BC26
Compound financial instruments with multiple embedded derivatives	BC28
Defaults and breaches	BC32
Income statement and equity	BC33
Items of income, expenses, gains or losses	BC33
Fee income and expense	BC35
Other disclosures—fair value	BC36
DISCLOSURES ABOUT THE NATURE AND EXTENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS	BC40
Interaction between qualitative and quantitative disclosures	BC42A
Location of disclosures of risks arising from financial instruments	BC43
Quantitative disclosures	BC47
Information based on how the entity manages risk	BC47
Information on averages	BC48
Credit risk	BC49
Maximum exposure to credit risk	BC49
Collateral held as security and other credit enhancements	BC51
Credit quality of financial assets that are neither past due nor impaired	BC54
Financial assets with renegotiated terms	BC54A
Financial assets that are either past due or impaired	BC55
Collateral and other credit enhancements obtained	BC56
Liquidity risk	BC57
Market risk	BC59
Operational risk	BC65
DISCLOSURES RELATING TO TRANSFERS OF FINANCIAL ASSETS	BC65A
Background	BC65A
Transferred financial assets that are not derecognised in their entirety	BC65E
Transferred financial assets that are derecognised in their entirety	BC65I
EFFECTIVE DATE AND TRANSITION	BC66
<u>APPLICABILITY OF THE OFFSETTING AMENDMENTS TO IFRS 7 TO CONDENSED INTERIM FINANCIAL STATEMENTS</u>	<u>BC72B</u>
SUMMARY OF MAIN CHANGES FROM THE EXPOSURE DRAFT	BC73
APPENDIX	
A Amendments to Basis for Conclusions on other IFRSs	

BC65K The Board observed that IFRS 7 already requires certain disclosures by class of financial instrument or by type of risk. However, the IFRS requires the information at an aggregated level, so information specific to derecognition transactions is often not available. In response to requests from users and others the Board concluded that disclosures specific to derecognition transactions were necessary.

BC65L The Board concluded that the disclosures should focus on the risk exposure of an entity, and should provide information about the timing of the return and the cash outflow that would or may be required to repurchase the derecognised financial assets in the future. The Board reasoned that a combination of disclosures about the strike price or repurchase price to repurchase assets, the fair value of its continuing involvement, the maximum exposure to loss and qualitative information about an entity's obligations to provide financial support are relevant in understanding an entity's exposure to risks.

BC65M In addition, the Board concluded that information about an entity's gain or loss on derecognition and the timing of recognition of that gain or loss provides information about the proportion of an entity's profit or loss that arises from transferring financial assets in which the entity also retains continuing involvement. Such information is useful in assessing the extent to which an entity generates profits from transferring financial assets while retaining some form of continuing involvement and thus exposure to risk.

BC65N The Board observed that the total amount of proceeds from transfer activity (that qualifies for derecognition) in a reporting period may not be evenly distributed throughout the reporting period (eg if a substantial proportion of the total amount of transfer activity takes place in the closing days of a reporting period). The Board decided that if transfer activity is concentrated around the end of reporting periods, disclosure of this fact provides an indication of whether transfer transactions are undertaken for the purpose of altering the appearance of the statement of financial position rather than for an ongoing commercial or financing purpose. In such cases, the amendments require disclosure of when the greatest transfer activity took place within that reporting period, the amount recognised from the transfer activity in that part of the reporting period, and the total amount of proceeds from transfer activity in that part of the reporting period.

Application of the disclosure requirements to a servicing contract

BC65O Paragraphs 42A–42H of IFRS 7 require an entity to provide disclosures for all transferred financial assets that are not derecognised in their entirety and for any continuing involvement in a transferred asset that is derecognised in its entirety, existing at the reporting date, irrespective of when the related transfer transaction occurred.

BC65P The Board received a request to clarify whether servicing contracts constitute continuing involvement for the purposes of applying the disclosure requirements in paragraphs 42E–42H of IFRS 7. The question raised was whether paragraph 42C(c) of IFRS 7 excludes servicing contracts from the scope of those disclosure requirements.

BC65Q The Board observed that paragraph 42C(c) of IFRS 7 discusses arrangements whereby an entity retains the contractual rights to receive the cash flows of a financial asset but assumes a contractual obligation to pay the cash flows to one or more entities and the conditions in paragraph 3.2.5(a)–(c) of IFRS 9 are met; ie it is a 'pass-through arrangement'.* Paragraph 42C(c) of IFRS 7 confirms that the cash flows collected to be passed through are not themselves continuing involvement for the purposes of the transfer disclosure requirements. Consequently, the Board

* If IFRS 9 has not been applied early, the equivalent reference is paragraph 19(a)–(c) of IAS 39.

observed that the servicer's obligation to pass through to one or more entities the cash flows that it collects from a transferred financial asset is not in itself continuing involvement for the purposes of the disclosure requirements, because the activity of passing through cash flows does not in itself constitute an interest in the future performance of the transferred financial asset. The Board observed, however, that a servicing contract is generally continuing involvement for the purposes of the transfer disclosure requirements because, in most cases, the servicer has an interest in the future performance of the transferred financial assets as a result of that contract. That would be the case if the amount and/or timing of the servicing fee depended on the amount and/or timing of the cash flows collected from the transferred financial asset. This would be true irrespective of how the servicer receives its servicing fee; ie whether the servicer retains a portion of the cash flows collected from the transferred financial asset as its fee or it passes through all of the cash flows collected and receives its fee separately from the transferee or another entity.

BC65R On the basis of these observations, the Board noted that paragraphs 42C and B30 of IFRS 7 are considered to determine whether a servicing contract gives rise to continuing involvement for the purposes of the transfer disclosure requirements. The Board decided to add guidance to the Application Guidance of IFRS 7 to clarify how the guidance in paragraph 42C of IFRS 7 is applied to servicing contracts.

BC65S During its discussions on this issue, the Board noted that for the purpose of applying the disclosure requirements in paragraphs 42E–42H of IFRS 7, continuing involvement as described in paragraph 42C of IFRS 7 has a different meaning from that used in paragraphs 3.2.6(c)(ii) and 3.2.16 of IFRS 9.* The Board considered, but decided against, making a clarification in respect of this point because it thought that this difference was already clear from the description of continuing involvement in the two IFRSs.

Effective date and transition (paragraphs 43 and 44)

BC66 The Board is committed to maintaining a “stable platform” of substantially unchanged Standards for annual periods beginning on or before 1 January 2005, when many entities will adopt IFRSs for the first time. In addition, some preparers will need time to make the system changes necessary to comply with the IFRS. Therefore, the Board decided that the effective date of IFRS 7 should be annual periods beginning on or after 1 January 2007, with earlier application encouraged.

BC67 The Board noted that entities that apply IFRS 7 only when it becomes mandatory will have sufficient time to prepare comparative information. This conclusion does not apply to entities that apply IFRS 7 early. In particular, the time would be extremely short for those entities that would like to apply IFRS 7 when they first adopt IFRSs in 2005, to avoid changing from local GAAP to IAS 32 and IAS 30 when they adopt IFRSs and then changing again to IFRS 7 only one or two years later. Therefore, the Board gave an exemption from providing comparative disclosure in the first year of application of IFRS 7 to any entity that both (a) is a first-time adopter of IFRSs and (b) applies IFRS 7 before 1 January 2006. The Board noted that such an exemption for first-time adopters exists in IAS 32 and IFRS 4 and that the reasons for providing the exemption apply equally to IFRS 7.

BC68 The Board also considered whether it should provide an exemption from presenting all or some of the comparative information to encourage early adoption of IFRS 7 by entities that already apply IFRSs.

* If IFRS 9 has not been applied early, the equivalent references are paragraphs 20(c)(ii) and 30 of IAS 39.

- BC69 The Board noted that IFRS 7 contains two types of disclosures: accounting disclosures (in paragraphs 7-30) that are based on requirements previously in IAS 32 and new risk disclosures (in paragraphs 31-42). The Board concluded that existing users of IFRSs already will have complied with the requirements of IAS 32 and will not encounter difficulty in providing comparative information for the accounting disclosures.
- BC70 The Board noted that most of the risk disclosures, in particular those about market risk, are based on information collected at the end of the reporting period. The Board concluded that although IFRS 7 was published in August 2005, it will still be possible for entities to collect the information that they require to comply with IFRS 7 for accounting periods beginning in 2005. However, it would not always be possible to collect the information needed to provide comparative information about accounting periods that began in 2004. As a result, the Board decided that entities that apply IFRS 7 for accounting periods beginning in 2005 (ie before 1 January 2006) need not present comparative information about the risk disclosures.
- BC71 The Board also noted that comparative disclosures about risk are less relevant because these disclosures are intended to have predictive value. As a result information about risk loses relevance more quickly than other types of disclosure, and any disclosures required by previous GAAP are unlikely to be comparable with those required by IFRS 7. Accordingly, the Board decided that an entity that is not a first-time adopter and applies IFRS 7 for annual periods beginning before 1 January 2006 need not present comparative disclosures about the nature and extent of risks arising from financial instruments. In reaching this conclusion, the Board noted that the advantages of encouraging more entities to apply IFRS 7 early outweighed the disadvantage of the reduced information provided.
- BC72 The Board considered and rejected arguments that it should extend the exemption:
- (a) from providing comparative information to first-time adopters that applied IFRS 7 before 1 January 2007 (rather than only those that applied IFRS 7 before 1 January 2006). The Board concluded that an entity that intends to adopt IFRSs for the first time on or after 1 January 2006 will have sufficient time to collect information for its accounting period beginning on or after 1 January 2005 and, thus, should not have difficulty in providing the comparative disclosures for accounting periods beginning on or after 1 January 2006.
 - (b) from providing comparative disclosures about the significance of financial instruments to all entities adopting the IFRS for annual periods beginning before 1 January 2006 (rather than only to first-time adopters). The Board concluded that only first-time adopters warranted special relief so that they would be able to adopt IFRS 7 early without first having to adopt IAS 32 and IAS 30 for only one period. Entities that are not first-time adopters already apply IAS 32 and IAS 30 and have no particular need to adopt IFRS 7 before 1 January 2007.
 - (c) from providing comparative disclosures about risk to periods beginning before 1 January 2007 (rather than 2006). The Board noted that entities adopting IFRS 7 after 1 January 2006 would have a full calendar year to prepare after the publication of the IFRS.

BC72A Annual Improvements to IFRSs 2012–2014 Cycle, issued in September 2014, amended paragraph B30 and added paragraph B30A of IFRS 7. The Board considered whether the amendment should apply to any period presented that begins before the annual period for which the entity first applies the amendment. The Board noted that paragraph 42E(b) of IFRS 7 requires disclosure of the fair value of the assets and liabilities that represent the entity's continuing involvement in the derecognised financial assets. Application of the amendment to such a period might therefore require an entity to determine the fair value as at the end of the period for a servicing asset or servicing liability, which the entity might not have previously determined. It might be impracticable for an entity to determine the fair value of such a servicing asset or servicing liability without using hindsight. The Board also noted that paragraph 44M of IFRS 7 provides transition relief by which the entity need not apply the transfer disclosure requirements to comparative periods. Consequently, to avoid the risk of hindsight being applied, the Board decided to require the application of the amendment only to annual periods beginning on or after the beginning of the annual period for which the amendment is applied for the first time. Furthermore, for the same reason, the Board observed that those transition provisions should be available to first-time adopters. The Board has characterised the transition provisions in paragraph 44AA of IFRS 7 as retrospective despite this relief, because entities are required to look back to past derecognition events to determine whether a servicing asset or servicing liability needs to be disclosed.

Applicability of the offsetting amendments to IFRS 7 to condensed interim financial statements

BC72B The Board was asked to clarify the applicability of the amendments to IFRS 7 *Disclosure–Offsetting Financial Assets and Financial Liabilities* (the 'amendments to IFRS 7 concerning offsetting'), issued in December 2011, to condensed interim financial statements. It was asked to clarify the meaning of the reference to 'interim periods within those annual periods', used in paragraph 44R of IFRS 7. There was uncertainty about whether the disclosures required by paragraphs 13A–13F and B40–B53 of IFRS 7 were required to be included in condensed interim financial statements prepared in accordance with IFRS and, if so, whether those disclosures should be presented in every set of condensed interim financial statements, or only in those interim financial statements presented in the first year in which the disclosure requirements are effective or for which disclosure would be required under the principles in IAS 34 *Interim Financial Reporting*.

BC72C The Board noted that IAS 34 was not consequentially amended upon issue of the amendments to IFRS 7 concerning offsetting and that when the Board intends to require an entity to provide a disclosure in condensed interim financial statements in all circumstances it amends IAS 34. Consequently, the Board decided to amend paragraph 44R of IFRS 7 within the *Annual Improvements to IFRSs 2012–2014 Cycle* in order to clarify that the additional disclosure required by the amendments to IFRS 7 concerning offsetting is not specifically required for all interim periods. However, when considering this amendment, the Board noted that the additional disclosure is required to be given in condensed interim financial statements prepared in accordance with IAS 34 when its inclusion would be required in accordance with the general requirements of that IFRS. IAS 34 requires the disclosure of information in condensed interim financial statements when its omission would make the condensed interim financial statements misleading. The Board noted that in accordance with paragraph 15 of IAS 34 "an entity shall include in its interim financial report an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period". The Board further noted that in accordance with paragraph 25 of IAS 34: "The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding an entity's financial position and performance during the interim period".

Summary of main changes from the exposure draft

BC73 The main changes to the proposals in ED 7 are:

- (a) ED 7 proposed disclosure of the amount of change in the fair value of a financial liability designated as at fair value through profit or loss that is not attributable to changes in a benchmark interest rate as a proxy for the amount of change in fair value attributable to changes in the instrument's credit risk. The IFRS permits entities to determine the amount of change in fair value attributable to changes in the instrument's credit risk using an alternative method if the entity believes that its alternative method gives more faithful representation. The proxy disclosure has been amended to be the amount of change in fair value that is not attributable to changes in market conditions that give rise to market risk. As a result, entities may exclude factors other than a change in a benchmark interest rate when calculating the proxy.
- (b) a requirement has been added for disclosures about the difference between the transaction price at initial recognition (used as fair value in accordance with paragraph AG76 of IAS 39) and the results of a valuation technique that will be used for subsequent measurement.
- (c) no disclosure is required of the fair value of collateral pledged as security and other credit enhancements as was proposed in ED 7.
- (d) the sensitivity analysis requirements have been clarified.
- (e) the exemption from presenting comparatives has been widened.
- (f) the capital disclosures are a stand-alone amendment to IAS 1, rather than part of the IFRS. No disclosure is required of whether the entity has complied with capital targets set by management and of the consequences of any non-compliance with those targets.
- (g) the amendments to IFRS 4 related to IFRS 7 have been modified to reduce systems changes for insurers.

APPENDIX A

Amendments to Basis for Conclusions on other IFRSs

This appendix contains amendments to the Basis for Conclusions on other IFRSs that are necessary in order to ensure consistency with IFRS 7. In the amended paragraphs, new text is underlined and deleted text is struck through.

* * *

The amendments contained in this appendix when this Basis for Conclusions was issued have been incorporated into the relevant Basis for Conclusions.

HKFRS 8 IG
Issued March 2007 Revised December 2016

*Guidance on Implementing
Hong Kong Financial Reporting Standard 8*

Operating Segments



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

Guidance on implementing HKFRS 8 *Operating Segments*

This guidance accompanies, but is not part of, HKFRS 8.

Introduction

IG1 This implementation guidance provides examples that illustrate the disclosures required by HKFRS 8 and a diagram to assist in identifying reportable segments. The formats in the illustrations are not requirements. The Board encourages a format that provides the information in the most understandable manner in the specific circumstances. The following illustrations are for a single hypothetical entity referred to as Diversified Company.

Descriptive information about an entity's reportable segments

IG2 The following illustrates the disclosure of descriptive information about an entity's reportable segments (the paragraph references are to the relevant requirements in the HKFRS).

Description of the types of products and services from which each reportable segment derives its revenues (paragraph 22(b))

Diversified Company has five reportable segments: car parts, motor vessels, software, electronics and finance. The car parts segment produces replacement parts for sale to car parts retailers. The motor vessels segment produces small motor vessels to serve the offshore oil industry and similar businesses. The software segment produces application software for sale to computer manufacturers and retailers. The electronics segment produces integrated circuits and related products for sale to computer manufacturers. The finance segment is responsible for portions of the company's financial operations including financing customer purchases of products from other segments and property lending operations.

Measurement of operating segment profit or loss, assets and liabilities (paragraph 27)

The accounting policies of the operating segments are the same as those described in the ~~summary~~ of significant accounting policies except that pension expense for each operating segment is recognised and measured on the basis of cash payments to the pension plan. Diversified Company evaluates performance on the basis of profit or loss from operations before tax expense not including non-recurring gains and losses and foreign exchange gains and losses.

Diversified Company accounts for intersegment sales and transfers as if the sales or transfers were to third parties, ie at current market prices.

Factors that management used to identify the entity's reportable segments (paragraph 22(a))

Diversified Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different technology and marketing strategies. Most of the businesses were acquired as individual units, and the management at the time of the acquisition was retained.

HKFRS 11
Revised June 2014 ~~December 2016~~

Effective for annual periods
beginning on or after 1 January 2013

Hong Kong Financial Reporting Standard 11

Joint Arrangements



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

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CONTENTS

	<i>from paragraph</i>
INTRODUCTION	IN1
HONG KONG FINANCIAL REPORTING STANDARD 11 JOINT ARRANGEMENTS	
OBJECTIVE	1
Meeting the objective	2
SCOPE	3
JOINT ARRANGEMENTS	4
Joint control	7
Types of joint arrangement	14
FINANCIAL STATEMENTS OF PARTIES TO A JOINT ARRANGEMENT	20
Joint operations	20
Joint ventures	24
SEPARATE FINANCIAL STATEMENTS	26
APPENDICES	
A Defined terms	
B Application guidance	
C Effective date, transition and withdrawal of other HKFRSs	
D Amendments to other HKFRSs	
E Comparison with International Financial Reporting Standards	
BASIS FOR CONCLUSIONS (<i>see separate booklet</i>)	
APPENDIX	
Amendments to the Basis for Conclusions on other IFRSs	
ILLUSTRATIVE EXAMPLES (<i>see separate booklet</i>)	

Hong Kong Financial Reporting Standard 11 *Joint Arrangements* (HKFRS 11) is set out in paragraphs 1–27 and Appendices A–D & F. All the paragraphs have equal authority. Paragraphs in **bold type** state the main principles. Terms defined in Appendix A are in *italics* the first time they appear in the Standard. Definitions of other terms are given in the Glossary for Hong Kong Financial Reporting Standards. HKFRS 11 should be read in the context of its objective and the Basis for Conclusions, the *Preface to Hong Kong Financial Reporting Standards* and the *Conceptual Framework for Financial Reporting*. HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

Overview

- IN1 Hong Kong Financial Reporting Standard 11 *Joint Arrangements* establishes principles for financial reporting by parties to a joint arrangement.
- IN2 The HKFRS supersedes HKAS 31 *Interests in Joint Ventures* and HK(SIC)-Int 13 *Jointly Controlled Entities—Non-Monetary Contributions by Venturers* and is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted.

Reasons for issuing the HKFRS

- IN3 The HKFRS is concerned principally with addressing two aspects of HKAS 31: first, that the structure of the arrangement was the only determinant of the accounting and, second, that an entity had a choice of accounting treatment for interests in jointly controlled entities.
- IN4 HKFRS 11 improves on HKAS 31 by establishing principles that are applicable to the accounting for all joint arrangements.
- IN4A In June 2014 the HKICPA amended HKFRS 11 to provide guidance on the accounting for acquisitions of interests in joint operations in which the activity constitutes a business.

Main features of the HKFRS

- IN5 The HKFRS requires a party to a joint arrangement to determine the type of joint arrangement in which it is involved by assessing its rights and obligations arising from the arrangement.

General requirements

- IN6 The HKFRS is to be applied by all entities that are a party to a joint arrangement. A joint arrangement is an arrangement of which two or more parties have joint control. The HKFRS defines joint control as the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities (ie activities that significantly affect the returns of the arrangement) require the unanimous consent of the parties sharing control.
- IN7 The HKFRS classifies joint arrangements into two types—joint operations and joint ventures. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement (ie joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement (ie joint venturers) have rights to the net assets of the arrangement.

JOINT ARRANGEMENTS

- IN8 An entity determines the type of joint arrangement in which it is involved by considering its rights and obligations. An entity assesses its rights and obligations by considering the structure and legal form of the arrangement, the contractual terms agreed to by the parties to the arrangement and, when relevant, other facts and circumstances.
- IN9 The HKFRS requires a joint operator to recognise and measure the assets and liabilities (and recognise the related revenues and expenses) in relation to its interest in the arrangement in accordance with relevant HKFRSs applicable to the particular assets, liabilities, revenues and expenses.
- IN9A This HKFRS requires the acquirer of an interest in a joint operation in which the activity constitutes a business, as defined in HKFRS 3 *Business Combinations*, to apply all of the principles on business combinations accounting in HKFRS 3 and other HKFRSs except for those principles that conflict with the guidance in this HKFRS. In addition, the acquirer shall disclose the information required by HKFRS 3 and other HKFRSs for business combinations.
- IN10 The HKFRS requires a joint venturer to recognise an investment and to account for that investment using the equity method in accordance with HKAS 28 *Investments in Associates and Joint Ventures*, unless the entity is exempted from applying the equity method as specified in that standard.
- IN11 The disclosure requirements for parties with joint control of a joint arrangement are specified in HKFRS 12 *Disclosure of Interests in Other Entities*.

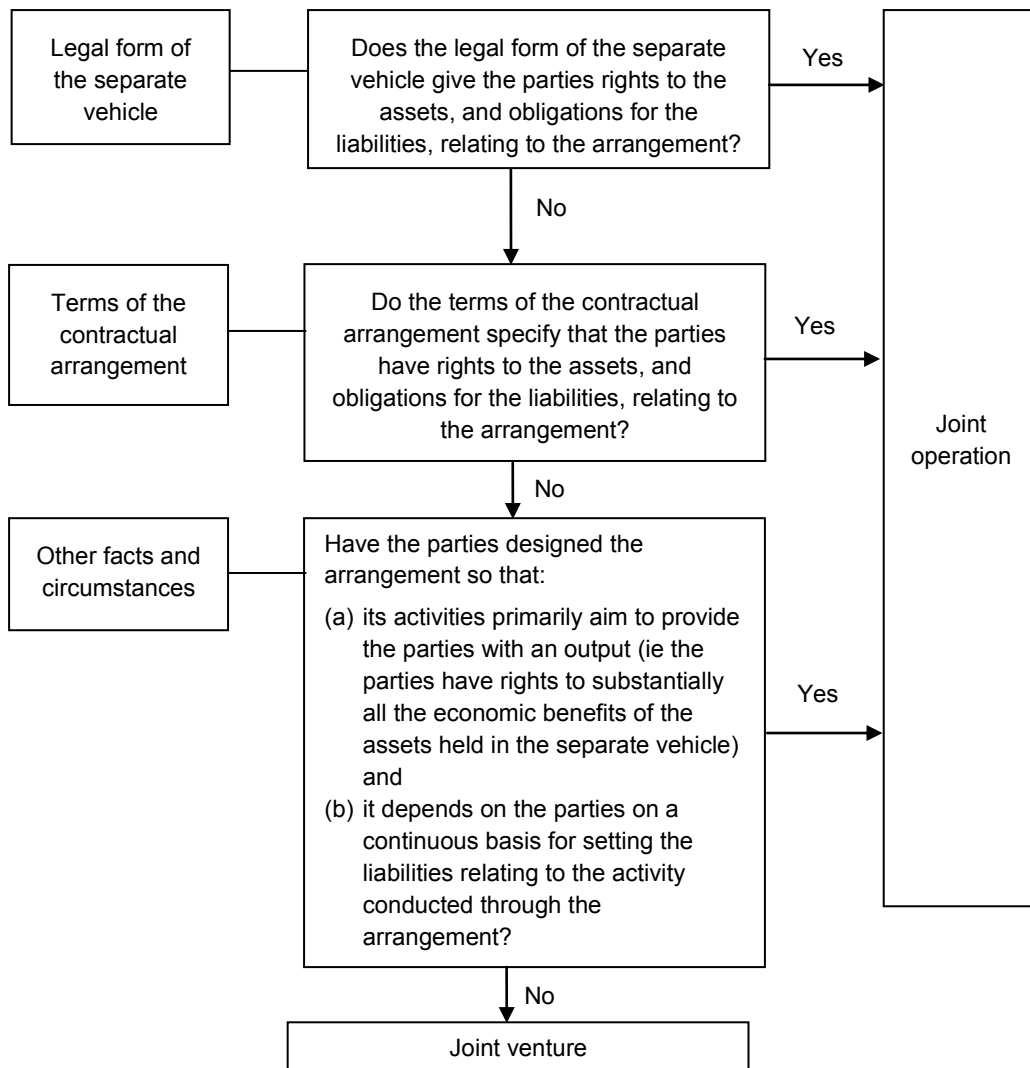
Financial statements of parties to a joint arrangement

Joint operations

- 20 A joint operator shall recognise in relation to its interest in a joint operation:
- (a) its assets, including its share of any assets held jointly;
 - (b) its liabilities, including its share of any liabilities incurred jointly;
 - (c) its revenue from the sale of its share of the output arising from the joint operation;
 - (d) its share of the revenue from the sale of the output by the joint operation; and
 - (e) its expenses, including its share of any expenses incurred jointly.
- 21 A joint operator shall account for the assets, liabilities, revenues and expenses relating to its interest in a joint operation in accordance with the HKFRSs applicable to the particular assets, liabilities, revenues and expenses.
- 21A When an entity acquires an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in HKFRS 3, it shall apply, to the extent of its share in accordance with paragraph 20, all of the principles on business combinations accounting in HKFRS 3, and other HKFRSs, that do not conflict with the guidance in this HKFRS and disclose the information that is required in those HKFRSs in relation to business combinations. This applies to the acquisition of both the initial interest and additional interests in a joint operation in which the activity of the joint operation constitutes a business. The accounting for the acquisition of an interest in such a joint operation is specified in paragraphs B33A–B33D.
- 22 The accounting for transactions such as the sale, contribution or purchase of assets between an entity and a joint operation in which it is a joint operator is specified in paragraphs B34–B37.
- 23 A party that participates in, but does not have joint control of, a joint operation shall also account for its interest in the arrangement in accordance with paragraphs 20–22 if that party has rights to the assets, and obligations for the liabilities, relating to the joint operation. If a party that participates in, but does not have joint control of, a joint operation does not have rights to the assets, and obligations for the liabilities, relating to that joint operation, it shall account for its interest in the joint operation in accordance with the HKFRSs applicable to that interest.

Joint ventures

- 24 A joint venturer shall recognise its interest in a joint venture as an investment and shall account for that investment using the equity method in accordance with HKAS 28 *Investments in Associates and Joint Ventures* unless the entity is exempted from applying the equity method as specified in that standard.
- 25 A party that participates in, but does not have joint control of, a joint venture shall account for its interest in the arrangement in accordance with HKFRS 9 *Financial Instruments*, unless it has significant influence over the joint venture, in which case it shall account for it in accordance with HKAS 28 (as amended in 2011).

Classification of a joint arrangement structured through a separate vehicle**Financial statements of parties to a joint arrangement (paragraphs 21A – 22)****Accounting for acquisitions of interests in joint operations**

B33A When an entity acquires an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in HKFRS 3, it shall apply, to the extent of its share in accordance with paragraph 20, all of the principles on business combinations accounting in HKFRS 3, and other HKFRSs, that do not conflict with the guidance in this HKFRS and disclose the information required by those HKFRSs in relation to business combinations. The principles on business combinations accounting that do not conflict with the guidance in this HKFRS include but are not limited to:

- (a) measuring identifiable assets and liabilities at fair value, other than items for which exceptions are given in HKFRS 3 and other HKFRSs;
- (b) recognising acquisition-related costs as expenses in the periods in which the costs are incurred and the services are received, with the exception that the costs to issue debt or equity securities are recognised in accordance with HKAS 32 *Financial Instruments: Presentation* and HKFRS 9;¹
- (c) recognising deferred tax assets and deferred tax liabilities that arise from the initial recognition of assets or liabilities, except for deferred tax liabilities that arise from the initial recognition of goodwill, as required by HKFRS 3 and HKAS 12 *Income Taxes* for business combinations;
- (d) recognising the excess of the consideration transferred over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed, if any, as goodwill; and
- (e) testing for impairment a cash-generating unit to which goodwill has been allocated at least annually, and whenever there is an indication that the unit may be impaired, as required by HKAS 36 *Impairment of Assets* for goodwill acquired in a business combination.

B33B Paragraphs 21A and B33A also apply to the formation of a joint operation if, and only if, an existing business, as defined in HKFRS 3, is contributed to the joint operation on its formation by one of the parties that participate in the joint operation. However, those paragraphs do not apply to the formation of a joint operation if all of the parties that participate in the joint operation only contribute assets or groups of assets that do not constitute businesses to the joint operation on its formation.

B33C A joint operator might increase its interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in HKFRS 3, by acquiring an additional interest in the joint operation. In such cases, previously held interests in the joint operation are not remeasured if the joint operator retains joint control.

B33D Paragraphs 21A and B33A–B33C do not apply on the acquisition of an interest in a joint operation when the parties sharing joint control, including the entity acquiring the interest in the joint operation, are under the common control of the same ultimate controlling party or parties both before and after the acquisition, and that control is not transitory.

Accounting for sales or contributions of assets to a joint operation

- B34 When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a sale or contribution of assets, it is conducting the transaction with the other parties to the joint operation and, as such, the joint operator shall recognise gains and losses resulting from such a transaction only to the extent of the other parties' interests in the joint operation.
- B35 When such transactions provide evidence of a reduction in the net realisable value of the assets to be sold or contributed to the joint operation, or of an impairment loss of those assets, those losses shall be recognised fully by the joint operator

¹ If an entity applies these amendments but does not yet apply HKFRS 9, the reference in these amendments to HKFRS 9 shall be read as a reference to HKAS 39 *Financial Instruments: Recognition and Measurement*.

Accounting for purchases of assets from a joint operation

- B36 When an entity enters into a transaction with a joint operation in which it is a joint operator, such as a purchase of assets, it shall not recognise its share of the gains and losses until it resells those assets to a third party.
- B37 When such transactions provide evidence of a reduction in the net realisable value of the assets to be purchased or of an impairment loss of those assets, a joint operator shall recognise its share of those losses.

Appendix C

Effective date, transition and withdrawal of other HKFRSs

This appendix is an integral part of the HKFRS and has the same authority as the other parts of the HKFRS.

Effective date

- C1 An entity shall apply this HKFRS for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies this HKFRS earlier, it shall disclose that fact and apply HKFRS 10, HKFRS 12 *Disclosure of Interests in Other Entities*, HKAS 27 (as amended in 2011) and HKAS 28 (as amended in 2011) at the same time.
- C1A *Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance* (Amendments to HKFRS 10, HKFRS 11 and HKFRS 12), issued in July 2012, amended paragraphs C2–C5, C7–C10 and C12 and added paragraphs C1B and C12A–C12B. An entity shall apply those amendments for annual periods beginning on or after 1 January 2013. If an entity applies HKFRS 11 for an earlier period, it shall apply those amendments for that earlier period.
- C1AA *Accounting for Acquisitions of Interests in Joint Operations* (Amendments to HKFRS 11), issued in June 2014, amended the heading after paragraph B33 and added paragraphs 21A, B33A–B33D and C14A and their related headings. An entity shall apply those amendments prospectively in annual periods beginning on or after 1 January 2016. Earlier application is permitted. If an entity applies those amendments in an earlier period it shall disclose that fact.

Transition

- C1B Notwithstanding the requirements of paragraph 28 of HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, when this HKFRS is first applied, an entity need only present the quantitative information required by paragraph 28(f) of HKAS 8 for the annual period immediately preceding the first annual period for which HKFRS 11 is applied (the ‘immediately preceding period’). An entity may also present this information for the current period or for earlier comparative periods, but is not required to do so.

Transition

Joint ventures—transition from proportionate consolidation to the equity method

- C2 When changing from proportionate consolidation to the equity method, an entity shall recognise its investment in the joint venture as at the beginning of the immediately preceding period. That initial investment shall be measured as the aggregate of the carrying amounts of the assets and liabilities that the entity had previously proportionately consolidated, including any goodwill arising from acquisition. If the goodwill previously belonged to a larger cash-generating unit, or to a group of cash-generating units, the entity shall allocate goodwill to the joint venture on the basis of the relative carrying amounts of the joint venture and the cash-generating unit or group of cash-generating units to which it belonged.
- C3 The opening balance of the investment determined in accordance with paragraph C2 is regarded as the deemed cost of the investment at initial recognition. An entity shall apply paragraphs 40–43 of HKAS 28 (as amended in 2011) to the opening balance of the investment to assess whether the investment is impaired and shall recognise any impairment loss as an adjustment to retained earnings at the beginning of the immediately preceding period. The initial recognition exception in paragraphs 15 and 24 of HKAS 12 *Income Taxes* does not apply when the entity recognises an investment in a joint venture resulting from applying the transition requirements for joint ventures that had previously been proportionately consolidated.

- C4 If aggregating all previously proportionately consolidated assets and liabilities results in negative net assets, an entity shall assess whether it has legal or constructive obligations in relation to the negative net assets and, if so, the entity shall recognise the corresponding liability. If the entity concludes that it does not have legal or constructive obligations in relation to the negative net assets, it shall not recognise the corresponding liability but it shall adjust retained earnings at the beginning of the immediately preceding period. The entity shall disclose this fact, along with its cumulative unrecognised share of losses of its joint ventures as at the beginning of the immediately preceding period and at the date at which this HKFRS is first applied.
- C5 An entity shall disclose a breakdown of the assets and liabilities that have been aggregated into the single line investment balance as at the beginning of the immediately preceding period. That disclosure shall be prepared in an aggregated manner for all joint ventures for which an entity applies the transition requirements referred to in paragraphs C2–C6.
- C6 After initial recognition, an entity shall account for its investment in the joint venture using the equity method in accordance with HKAS 28 (as amended in 2011).

Joint operations—transition from the equity method to accounting for assets and liabilities

- C7 When changing from the equity method to accounting for assets and liabilities in respect of its interest in a joint operation, an entity shall, at the beginning of the immediately preceding period, derecognise the investment that was previously accounted for using the equity method and any other items that formed part of the entity's net investment in the arrangement in accordance with paragraph 38 of HKAS 28 (as amended in 2011) and recognise its share of each of the assets and the liabilities in respect of its interest in the joint operation, including any goodwill that might have formed part of the carrying amount of the investment.
- C8 An entity shall determine its interest in the assets and liabilities relating to the joint operation on the basis of its rights and obligations in a specified proportion in accordance with the contractual arrangement. An entity measures the initial carrying amounts of the assets and liabilities by disaggregating them from the carrying amount of the investment at the beginning of the immediately preceding period on the basis of the information used by the entity in applying the equity method.
- C9 Any difference arising from the investment previously accounted for using the equity method together with any other items that formed part of the entity's net investment in the arrangement in accordance with paragraph 38 of HKAS 28 (as amended in 2011), and the net amount of the assets and liabilities, including any goodwill, recognised shall be:
- (a) offset against any goodwill relating to the investment with any remaining difference adjusted against retained earnings at the beginning of the immediately preceding period, if the net amount of the assets and liabilities, including any goodwill, recognised is higher than the investment (and any other items that formed part of the entity's net investment) derecognised.
 - (b) adjusted against retained earnings at the beginning of the immediately preceding period, if the net amount of the assets and liabilities, including any goodwill, recognised is lower than the investment (and any other items that formed part of the entity's net investment) derecognised.

- C10 An entity changing from the equity method to accounting for assets and liabilities shall provide a reconciliation between the investment derecognised, and the assets and liabilities recognised, together with any remaining difference adjusted against retained earnings, at the beginning of the immediately preceding period.
- C11 The initial recognition exception in paragraphs 15 and 24 of HKAS 12 does not apply when the entity recognises assets and liabilities relating to its interest in a joint operation.

Transition provisions in an entity's separate financial statements

- C12 An entity that, in accordance with paragraph 10 of HKAS 27, was previously accounting in its separate financial statements for its interest in a joint operation as an investment at cost or in accordance with HKFRS 9 shall:
- (a) derecognise the investment and recognise the assets and the liabilities in respect of its interest in the joint operation at the amounts determined in accordance with paragraphs C7–C9.
 - (b) provide a reconciliation between the investment derecognised, and the assets and liabilities recognised, together with any remaining difference adjusted in retained earnings, at the beginning of the immediately preceding period.

References to the 'immediately preceding period'

- C12A Notwithstanding the references to the 'immediately preceding period' in paragraphs C2–C12, an entity may also present adjusted comparative information for any earlier periods presented, but is not required to do so. If an entity does present adjusted comparative information for any earlier periods, all references to the 'immediately preceding period' in paragraphs C2–C12 shall be read as the 'earliest adjusted comparative period presented'.
- C12B If an entity presents unadjusted comparative information for any earlier periods, it shall clearly identify the information that has not been adjusted, state that it has been prepared on a different basis, and explain that basis.
- C13 The initial recognition exception in paragraphs 15 and 24 of HKAS 12 does not apply when the entity recognises assets and liabilities relating to its interest in a joint operation in its separate financial statements resulting from applying the transition requirements for joint operations referred to in paragraph C12.

References to HKFRS 9

- C14 If an entity applies this HKFRS but does not yet apply HKFRS 9, any reference to HKFRS 9 shall be read as a reference to HKAS 39 *Financial Instruments: Recognition and Measurement*.

Accounting for acquisitions of interests in joint operations

- C14A *Accounting for Acquisitions of Interests in Joint Operations (Amendments to HKFRS 11)*, issued in June 2014, amended the heading after paragraph B33 and added paragraphs 21A, B33A–B33D, C1AA and their related headings. An entity shall apply those amendments prospectively for acquisitions of interests in joint operations in which the activities of the joint operations constitute businesses, as defined in HKFRS 3, for those acquisitions occurring from the beginning of the first period in which it applies those amendments. Consequently, amounts recognised for acquisitions of interests in joint operations occurring in prior periods shall not be adjusted.

Withdrawal of other HKFRSs

C15 This HKFRS supersedes the following HKFRSs:

- (a) HKAS 31 *Interests in Joint Ventures*; and
- (b) HK(SIC)-Int 13 *Jointly Controlled Entities—Non-Monetary Contributions by Venturers*.

Appendix D

Amendments to other HKFRSs

This appendix sets out amendments to other HKFRSs that are a consequence of issuing HKFRS 11. An entity shall apply the amendments for annual periods beginning on or after 1 January 2013. If an entity applies HKFRS 11 for an earlier period, it shall apply the amendments for that earlier period. Amended paragraphs are shown with new text underlined and deleted text struck through.

The amendments contained in this appendix when this HKFRS was issued in 2011 have been incorporated into the relevant Standards.

Appendix E

Comparison with International Financial Reporting Standards

This comparison appendix, which was prepared in June 2011 and deals only with significant differences in the standards extant, is produced for information only and does not form part of the standards in HKFRS 11.

The International Financial Reporting Standard comparable with HKFRS 11 is IFRS 11 *Joint Arrangements*.

There are no major textual differences between HKFRS 11 and IFRS 11.

*Basis for Conclusions on
Hong Kong Financial Reporting Standard 11*

Joint Arrangements



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Certified Public Accountants
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Basis for Conclusions on IFRS 11 *Joint Arrangements*

HKFRS 11 is based on IFRS 11 *Joint Arrangement*. In approving HKFRS 11, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IFRS 11. Accordingly, there are no significant differences between HKFRS 11 and IFRS 11. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IFRS 11 referred to below generally correspond with those in HKFRS 11.

CONTENTS

	<i>from paragraph</i>
INTRODUCTION	BC1
OBJECTIVE	BC4
The problems with IAS 31	BC7
Improving IAS 31 with the principles of IFRS 11	BC9
SCOPE	BC13
Scope exception	BC15
JOINT ARRANGEMENTS	BC19
Joint control	BC20
TYPES OF JOINT ARRANGEMENT	BC24
FINANCIAL STATEMENTS OF PARTIES TO A JOINT ARRANGEMENT	BC38
Joint operation	BC38
Joint venture	BC41
<u>Accounting for acquisitions of interests in joint operations</u>	<u>BC45A</u>
Transactions between an entity and a joint operation in which that entity is a joint operator and incorporation of SIC-13 into the IFRS	BC46
Reporting interests in joint arrangements in the financial statements of parties that participate in, but do not have joint control of, a joint arrangement	BC48
Joint operation held for sale	BC51
DISCLOSURE	BC52
EFFECTIVE DATE	BC56
TRANSITION	BC60
<u>ACCOUNTING FOR ACQUISITIONS OF INTERESTS IN JOINT OPERATIONS</u>	<u>BC69C</u>
SUMMARY OF MAIN CHANGES FROM ED 9	BC70
COST-BENEFIT CONSIDERATIONS	BC71
APPENDIX	
Amendments to the Basis for Conclusions on other IFRSs	

BC45 The Board does not believe that the elimination of proportionate consolidation will cause a loss of information for users of financial statements. This is because the disclosure requirements in IFRS 12, when compared with IAS 31, will improve the quality of the information provided to users relating to an entity's interest in joint ventures. The disclosure requirements in IFRS 12 will provide users with information about individual joint ventures when those joint ventures are material to the reporting entity. In addition, the Board notes that the summarised financial information required in IFRS 12 results in a higher degree of detail than did IAS 31, which gives users a better basis for assessing the effect on the reporting entity of the activities carried out through joint ventures.

Accounting for acquisitions of interests in joint operations

BC45A The IFRS Interpretations Committee (the Interpretations Committee) reported to the IASB that practice differed in accounting for the acquisition of interests in jointly controlled operations or jointly controlled assets, as specified in IAS 31. In particular, the Interpretations Committee noted diversity in practice if the activity of the jointly controlled operations or jointly controlled assets constitutes a business, as defined in IFRS 3.

BC45B The principal approaches observed in practice were:

- (a) **IFRS 3 approach:** some preparers of IFRS financial statements, when accounting for the acquisition of interests in jointly controlled operations or jointly controlled assets in which the activity constitutes a business, applied IFRS 3 and the guidance on business combinations in other IFRSs. Identifiable assets and liabilities were measured, subject to the exceptions in IFRS 3, at fair value and the residual was recognised as goodwill. Furthermore, transaction costs were not capitalised and deferred taxes were recognised on initial recognition of assets and liabilities. Only guidance on business combinations in IFRS 3 and other IFRSs that was not appropriate for the acquisition of an interest in jointly controlled operations or jointly controlled assets was not applied, for example, the guidance on non-controlling interests.
- (b) **cost approach:** others allocated the total cost of acquiring the interest in the joint operation to the individual identifiable assets on the basis of their relative fair values. Accordingly, any premium paid was allocated to the identifiable assets rather than being recognised as goodwill. Transaction costs were capitalised and deferred taxes were not recognised, because of the initial recognition exceptions in paragraphs 15 and 24 of IAS 12 *Income Taxes*.
- (c) **hybrid approach:** a third group of preparers of IFRS financial statements only applied the principles on business combinations accounting in IFRS 3 and other IFRSs to issues that were not addressed elsewhere in IFRS. Identifiable assets and liabilities were measured at fair value, with exceptions, and the residual was recognised as a separate asset, ie goodwill. Transaction costs, however, were capitalised and contingent liabilities and deferred taxes were not recognised because these issues were considered as being addressed elsewhere in IFRS. Deferred taxes were not recognised, because of the initial recognition exceptions in paragraphs 15 and 24 of IAS 12.

* IFRS 11 *Joint Arrangements* shall be applied for annual periods beginning on or after 1 January 2013. It replaces IAS 31 *Interests in Joint Ventures*.

BC45C The different approaches have led to different accounting outcomes, in particular:

- (a) in accounting for premiums paid in excess of the value of the identifiable net assets;
- (b) in capitalising or expensing acquisition-related costs; and
- (c) in accounting for deferred tax assets and deferred tax liabilities that arise from the initial recognition of assets and liabilities.

BC45D The IASB noted that the diversity in practice resulted from the fact that IAS 31 did not give specific guidance on the accounting for acquisitions of interests in jointly controlled operations or jointly controlled assets, the activity of which constitutes a business, as defined in IFRS 3. The IASB was concerned that this diversity in practice may continue in the accounting for acquisitions of interests in joint operations, as defined in IFRS 11, when the activities of those joint operations constitute businesses. Arrangements that were formerly 'jointly controlled operations' and 'jointly controlled assets' in IAS 31 are joint operations in IFRS 11 (see paragraph BC26). As was the case in IAS 31, a joint operator recognises its (share in the) assets, liabilities, revenue and expenses relating to such arrangements.

BC45E The IASB considered the guidance in current IFRS on the acquisition of an interest in a business. The IASB recognised that the acquisition of an interest in a joint operation does not meet the definition of a business combination in IFRS 3. Nonetheless, the IASB concluded that the most appropriate approach to account for an acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3, is to apply all of the principles on business combinations accounting in IFRS 3 and other IFRSs that do not conflict with the guidance in this IFRS.

BC45F The IASB reached this conclusion because:

- (a) it considers that separate recognition of goodwill, when present, is preferable to allocating premiums to identifiable assets acquired on the basis of relative fair values;
- (b) it thinks that an approach that limits the application of business combinations accounting only to issues that are not addressed elsewhere in IFRS lacks a strong conceptual basis; and
- (c) the guidance in IFRS 3 and other IFRSs on business combinations give a comprehensive and consistent set of accounting principles for the different components of such complex transactions as acquisitions of interests in businesses.

BC45G The IASB also concluded that an entity that is acquiring an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3, shall disclose the relevant information that is specified in IFRS 3 and other IFRSs on business combinations. This is because these requirements are an integral part of the financial reporting about the acquisition of interests in businesses.

BC45H Consequently, the IASB amended IFRS 11 to address the accounting for both the acquisition of an interest in a joint operation in which the activity of the joint operation constitutes a business, as defined in IFRS 3, and the related disclosure requirements, as a means to resolve the diversity in practice.

- BC45I The IASB noted that the fact patterns raised with the Interpretations Committee were limited to circumstances involving a business, as defined in IFRS 3. The IASB noted that IFRS already provides guidance for the acquisition of an interest in an asset or a group of assets that is not a business, as defined in IFRS 3. Consequently, the amendments apply only when an entity acquires an interest in a joint operation in which the activity constitutes a business, as defined in IFRS 3, either on formation of that joint operation or when acquiring an interest in an existing joint operation.
- BC45J The Exposure Draft *Acquisition of an Interest in a Joint Operation* (Proposed amendment to IFRS 11), which was published in December 2012, used the term ‘relevant principles on business combinations accounting in IFRS 3 and other IFRSs’ to describe the principles that have to be applied in accounting for the acquisition of an interest in a joint operation in which the activity constitutes a business. In analysing the comment letters on the Exposure Draft, the IASB noted divergent understanding of what the ‘relevant principles on business combinations accounting in IFRS 3 and other IFRSs’ are, within the context of the proposed amendment.
- BC45K In order to avoid diversity in practice from the application of the term ‘relevant principles on business combinations accounting in IFRS 3 and other IFRSs’, the IASB decided to replace this term with ‘all of the principles on business combinations accounting in IFRS 3 and other IFRSs that do not conflict with the guidance in this IFRS’. In addition, to aid understanding the application guidance includes a non-exhaustive list of five principles related to business combinations accounting in IFRS 3 and other IFRSs that do not conflict with the principles in this IFRS. Four of them relate to the areas in which the Interpretations Committee observed different accounting outcomes from the application of different approaches to the accounting for acquisitions of interests in jointly controlled operations or jointly controlled assets in which the activity constitutes a business (see paragraphs BC45B–BC45C).
- BC45L The IASB also noted that the reference to ‘all of the principles on business combinations accounting in IFRS 3 and other IFRSs’ is ambiguous for acquisitions of additional interests in joint operations that result in the joint operator retaining joint control of the joint operation. It might be understood as a reference to either:
- (a) paragraph 42 of IFRS 3 with the result of remeasuring a previously held interest in a joint operation on the acquisition of an additional interest while retaining joint control; or
 - (b) paragraph 23 of IFRS 10 with the result of not remeasuring a previously held interest in a joint operation on the acquisition of an additional interest while retaining joint control.
- BC45M In order to resolve this ambiguity, the IASB decided to clarify that previously held interests in a joint operation are not remeasured if the joint operator retains joint control. Paragraph 23 of IFRS 10 addresses the accounting for the acquisition of an additional interest in a business that is already controlled by the acquirer. This is the analogous transaction to the acquisition of an interest in a business that is already jointly controlled by the acquirer and will continue to be jointly controlled by it. Paragraph 42 of IFRS 3 instead addresses the acquisition of an interest that results in the acquirer obtaining control over the business. This is the analogous transaction to the acquisition of an interest in a business that results in the acquirer obtaining joint control of the business.
- BC45N The IASB decided to add a scope exclusion for joint operations under common control to the amendments to IFRS 11. The IASB concluded that the amendments to IFRS 11 should not require the application of all of the principles on business combinations accounting for transactions that would be outside the scope of IFRS 3 if control, rather than joint control, would be obtained or retained by the acquirer.

Transactions between an entity and a joint operation in which that entity is a joint operator and incorporation of SIC-13 into the IFRS

- BC46 In its redeliberation of ED 9, the Board noted that the exposure draft was silent on the accounting for transactions between an entity and a joint operation in which that entity is a joint operator. The Board observed that the IFRS did not aim to change the accounting procedures that entities applied when accounting for such transactions in accordance with IAS 31, but it did acknowledge that the IFRS should state what those requirements were.
- BC47 The Board also decided to include the requirements for the accounting for transactions entered into between a joint venturer and a joint venture, including the consensus of SIC-13 *Jointly Controlled Entities—Non-Monetary Contributions by Venturers*, in IAS 28 (as amended in 2011).

Reporting interests in joint arrangements in the financial statements of parties that participate in, but do not have joint control of, a joint arrangement

- BC48 The Board decided to clarify in the IFRS that an arrangement can be a joint arrangement even though not all of its parties have joint control of the arrangement. This was consistent with IAS 31, which defined an ‘investor in a joint venture’ as a party to a joint venture that does not have joint control of that joint venture. The Board noted, however, that relating the term ‘investor’ exclusively to parties with no joint control of the arrangement can be confusing because the parties with joint control of the arrangement are also investors in those arrangements. Accordingly, the Board modified the language in the IFRS to avoid that confusion. However, even though in its redeliberation of ED 9 the Board highlighted that the IFRS establishes recognition and measurement requirements for the parties with joint control of a joint arrangement, the Board decided to address the accounting requirements for parties that participate in, but do not have joint control of, a joint arrangement, to reduce divergence in practice.
- BC49 In relation to parties that participate in, but do not have joint control of, a joint arrangement that is a joint operation, the Board focused its discussions on those parties for which the contractual arrangements specify that they have rights to the assets, and obligations for the liabilities, relating to the joint operation. The Board concluded that, even though those parties are not joint operators, they do have rights and obligations for the assets, liabilities, revenues and expenses relating to the joint operation, which they should recognise in accordance with the terms of the contractual arrangement.

joint operation. The Board concluded that in such a case, an entity should adjust any difference between the net amount of the assets and liabilities recognised and the investment (and any other items that formed part of the entity's net investment in the arrangement) derecognised against retained earnings at the beginning of the earliest period presented.

- BC67 The Board also redeliberated the transition requirements for entities accounting for an interest in a joint operation in its separate financial statements when the entity had previously accounted for this interest at cost or in accordance with IFRS 9. As stated in paragraph BC38, the Board observed that the parties' interests in a joint operation are recognised in their separate financial statements, resulting in no difference between what is recognised in the parties' separate financial statements and in the parties' consolidated financial statements. The Board decided that an entity should adjust any difference between the investment derecognised and the assets and liabilities recognised in respect of the entity's interest in a joint operation against retained earnings at the beginning of the earliest period presented.
- BC68 The Board also considered requiring disclosures to help users of financial statements to understand the consequences of the accounting change from the equity method to accounting for assets and liabilities, and when accounting for an interest in a joint operation in the separate financial statements of an entity when the entity had previously accounted for this interest at cost or in accordance with IFRS 9. The Board decided that in both cases, an entity should provide a reconciliation between the investment derecognised and the breakdown of the assets and liabilities recognised, together with any remaining difference adjusted against retained earnings, at the beginning of the earliest period presented.
- BC69 As stated in paragraph BC57, respondents to the Request for Views also commented on the transition requirements of the IFRSs to be issued in 2011. In relation to the transition requirements relating to the consolidation and joint arrangements IFRSs, the Board noted that the majority of the respondents to the Request for Views had agreed with the tentative decisions that the Board had previously made at the time of the consultation on the transition requirements for those IFRSs.
- BC69A In June 2012, the Board amended the transition guidance in Appendix C to IFRS 10 *Consolidated Financial Statements*. When making those amendments, the Board decided to limit the requirement to present adjusted comparatives to the annual period immediately preceding the date of initial application of IFRS 10. This is consistent with the minimum comparative disclosure requirements contained in IAS 1 *Presentation of Financial Statements* as amended by *Annual Improvements to IFRSs 2009–2011 Cycle* (issued May 2012). Those amendments confirmed that when an entity applies a changed accounting policy retrospectively, it shall present, as a minimum, three statements of financial position (ie 1 January 2012, 31 December 2012 and 31 December 2013 for a calendar-year entity, assuming no early application of this IFRS) and two of each of the other statements (IAS 1 paragraphs 40A–40B). Notwithstanding this requirement, the Board confirmed that an entity is not prohibited from presenting adjusted comparative information for earlier periods. The Board also decided to make similar amendments to the transition guidance in Appendix C to this IFRS and Appendix C to IFRS 12 *Disclosure of Interests in Other Entities* to be consistent with this decision. The Board noted that if all comparative periods are not adjusted then entities should be required to state that fact, clearly identify the information that has not been adjusted, and explain the basis on which it has been prepared.

BC69B The Board also considered the disclosure requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. On the initial application of an IFRS, paragraph 28(f) of IAS 8 requires an entity to disclose, for the current period and for each prior period presented, the amount of any adjustment for each financial statement line item affected. Changes in the accounting for a joint arrangement on transition to IFRS 11 are likely to affect many line items throughout the financial statements. The Board agreed that this requirement would be burdensome for preparers and so agreed to limit the disclosure of the quantitative impact of any changes in the accounting for a joint arrangement to only the annual period immediately preceding the first annual period for which IFRS 11 is applied. An entity may also present this information for the current period or for earlier comparative periods, but is not required to do so.

Accounting for acquisitions of interests in joint operations

BC69C The IASB considered the transition provisions and effective date of the amendments to IFRS 11. The IASB noted that applying all of the principles of business combinations accounting in IFRS 3 and other IFRSs that do not conflict with the guidance in this IFRS to transactions that have previously been accounted for by applying one of the divergent approaches presented in paragraph BC45B might involve the use of hindsight in determining the acquisition-date fair values of the identifiable assets and liabilities that are to be recognised as part of the transaction and in performing the impairment test for goodwill. Consequently, the IASB decided that an entity would apply the amendments to IFRS 11 prospectively for transactions occurring in annual periods beginning on or after 1 January 2016 with early application permitted.

Summary of main changes from ED 9

BC70 The main changes from the exposure draft ED 9 are:

- (a) IFRS 11 applies to all entities that have an interest in a joint arrangement. The scope exception in the exposure draft for venture capital organisations, or mutual funds, unit trusts and similar entities, including investment-linked insurance funds, has been removed and has been recharacterised as an exemption from the requirement to measure investments in joint ventures in accordance with the equity method.
- (b) IFRS 11 replaces the term ‘shared decisions’ introduced by ED 9 with the term ‘joint control’. As in IAS 31, ‘joint control’ is one of the features that, along with the existence of a contractual arrangement, defines ‘joint arrangements’.
- (c) IFRS 11 classifies joint arrangements into two types—‘joint operations’ and ‘joint ventures’. Each type of joint arrangement is aligned with a specific accounting requirement. ED 9 had classified joint arrangements into three types—‘joint operations’, ‘joint assets’ and ‘joint ventures’.

- (d) IFRS 11 provides application requirements to assist entities in the classification of their joint arrangements. The IFRS requires an entity to determine the type of joint arrangement in which it is involved by considering its rights and obligations. In particular, the IFRS requires an entity to give consideration to the structure and legal form of the arrangement, to the terms agreed by the parties in the contractual arrangement and, when relevant, it should also consider other facts and circumstances.
- (e) IFRS 11 clarifies that not all the parties to a joint arrangement need to have joint control for the arrangement to be a joint arrangement. As a result, some of the parties to a joint arrangement might participate in the joint arrangement, but might not have joint control of it.
- (f) The consensus of SIC-13 has been incorporated into IAS 28 (as amended in 2011), and SIC-13 is accordingly withdrawn. ED 9 had proposed to incorporate the consensus of SIC-13 into the standard on joint arrangements.
- (g) The disclosure requirements have been placed in IFRS 12. ED 9 had proposed to incorporate the disclosure requirements for joint arrangements into the standard on joint arrangements.
- (h) IFRS 11 does not require an entity to adjust the differences between the proportionate consolidation method and the equity method retrospectively when an entity changes from proportionate consolidation to the equity method when accounting for its joint ventures. Instead, it requires an entity to recognise its investment in a joint venture as at the beginning of the earliest period presented, by measuring it as the aggregate of the carrying amounts of the assets and liabilities that the entity had previously proportionately consolidated, including any goodwill arising from acquisition. ED 9 had proposed retrospective application of the requirements.

Cost-benefit considerations

- BC71 The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. To attain this objective, the Board seeks to ensure that an IFRS will meet a significant need and that the overall benefits of the resulting information justify the costs of providing it. Although the costs to implement a new IFRS might not be borne evenly, users of financial statements benefit from improvements in financial reporting, thereby facilitating the functioning of markets for capital and credit and the efficient allocation of resources in the economy.
- BC72 The evaluation of costs and benefits is necessarily subjective. In making its judgement, the Board considered the following:
- (a) the costs incurred by preparers of financial statements;
 - (b) the costs incurred by users of financial statements when information is not available;
 - (c) the comparative advantage that preparers have in developing information, compared with the costs that users would incur to develop surrogate information;

(d) the benefit of better economic decision-making as result of improved financial reporting; and

(e) the costs of transition for users, preparers and others.

BC73 The Board concluded that the IFRS benefits preparers and users of financial statements. This is because the accounting for joint arrangements in the IFRS follows a principle-based approach. This approach has allowed the Board to remove the accounting option in IAS 31 so that each type of joint arrangement (ie 'joint operations' and 'joint ventures') is accounted for on a consistent basis. This contributes to enhancing the verifiability, comparability and understandability of these arrangements in entities' financial statements.

BC74 In the IFRS, the accounting for joint arrangements depends on the rights and obligations arising from the arrangement (not exclusively on whether the parties have chosen a particular structure or legal form to carry out their arrangements, or on the consistent application of an accounting policy—proportionate consolidation or equity method). Thus, the IFRS promotes greater comparability by applying the same approach to different joint arrangements.

BC75 The Board believes that basing the accounting on the principles in the IFRS results in enhanced verifiability, comparability and understandability, to the benefit of both preparers and users. First, verifiability and understandability are enhanced because the accounting reflects more faithfully the economic phenomena that it purports to represent (ie an entity's rights and obligations arising from its arrangements), which allows them to be better understood. Second, requiring the same accounting for each type of arrangement will enable entities to account for joint arrangements consistently: arrangements that confer on the parties rights to the assets and obligations for the liabilities are joint operations and arrangements that confer on the parties rights to the net assets are joint ventures. Consistency in the accounting for joint arrangements will help to achieve comparability among financial statements, which will enable users to identify and understand similarities in, and differences between, different arrangements.

BC76 The Board noted that the costs that preparers will have to bear when applying the IFRS to their arrangements are concentrated in the assessment of the type of joint arrangement rather than in the accounting for the arrangements. This is because entities accounting for joint arrangements in accordance with IAS 31 were not required to classify their arrangements on the basis of their rights and obligations arising from the arrangement, but instead on whether the arrangement was structured in an entity. The IFRS will require entities to assess the type of joint arrangement in which they are involved when those arrangements have been structured through a separate vehicle. Even though the classification of the joint arrangements represents an additional assessment that was not required in IAS 31, the application requirements in the IFRS that should assist preparers in the classification of their arrangements are not unduly complex. The Board does not think that the additional assessment that the IFRS will require for the classification of arrangements will result in an undue cost to preparers.

BC77 The Board noted that the IFRS, by comparison with the exposure draft, simplifies the proposals by aligning the types of joint arrangement with the accounting methods. The Board concluded that once an entity has determined the classification of the arrangement, the accounting for the arrangement will follow accounting procedures that have not been modified by the IFRS (ie entities will either account for assets and liabilities or they will account for an investment using the equity method). However, the Board acknowledged that the requirement for joint operations to be accounted for in the same way in the entity's consolidated financial statements as in the entity's

separate financial statements might lead to additional costs to entities in jurisdictions in which separate financial statements are required to be reported in accordance with IFRSs. This is because those requirements might cause entities to perform additional manual procedures such as reconciliations between the statutory accounts and the tax returns, and might require an entity to provide additional explanations of the impact of the changes to, for example, its creditors. Except for these costs and any other costs required on transition, the costs of accounting for joint arrangements once the entities have determined their classification will remain unchanged as a result of the IFRS.

- BC78 The Board concluded that enhanced verifiability, comparability and understandability result in a more faithful representation of joint arrangements in the financial statements of the entities that are involved in such arrangements, and that those benefits outweigh the costs that preparers might incur when implementing the IFRS.

Appendix

Amendments to the Basis for Conclusions on other IFRSs

This appendix contains amendments to the Basis for Conclusions on other IFRSs that are necessary in order to ensure consistency with IFRS 11 and the related amendments to other IFRSs. Amended paragraphs are shown with new text underlined and deleted text struck through.

The amendments contained in this appendix when this IFRS 11 was issued in 2011 have been incorporated into the Basis for Conclusions on the relevant Standards.

Illustrative Examples
Hong Kong Financial Reporting Standard 11

Joint Arrangements



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

CONTENTS

**IFRS 11 *Joint Arrangements*
Illustrative examples**

	<i>from paragraph</i>
1 CONSTRUCTION SERVICES	IE2
2 SHOPPING CENTRE OPERATED JOINTLY	IE9
3 JOINT MANUFACTURING AND DISTRIBUTION OF A PRODUCT	IE14
4 BANK OPERATED JOINTLY	IE29
5 OIL AND GAS EXPLORATION, DEVELOPMENT AND PRODUCTION ACTIVITIES	IE34
6 LIQUEFIED NATURAL GAS ARRANGEMENT	IE44
<u>7 ACCOUNTING FOR ACQUISITIONS OF INTERESTS IN JOINT OPERATIONS IN WHICH THE ACTIVITY CONSTITUTES A BUSINESS</u>	<u>IE53</u>

Example 6 – Liquefied natural gas arrangement

- IE44 Company A owns an undeveloped gas field that contains substantial gas resources. Company A determines that the gas field will be economically viable only if the gas is sold to customers in overseas markets. To do so, a liquefied natural gas (LNG) facility must be built to liquefy the gas so that it can be transported by ship to the overseas markets.
- IE45 Company A enters into a joint arrangement with company B in order to develop and operate the gas field and the LNG facility. Under that arrangement, companies A and B (the parties) agree to contribute the gas field and cash, respectively, to a new separate vehicle, entity C. In exchange for those contributions, the parties each take a 50 per cent ownership interest in entity C. The main feature of entity C's legal form is that it causes the separate vehicle to be considered in its own right (ie the assets and liabilities held in the separate vehicle are the assets and liabilities of the separate vehicle and not the assets and liabilities of the parties).
- IE46 The contractual arrangement between the parties specifies that:
- (a) companies A and B must each appoint two members to the board of entity C. The board of directors must unanimously agree the strategy and investments made by entity C.
 - (b) day-to-day management of the gas field and LNG facility, including development and construction activities, will be undertaken by the staff of company B in accordance with the directions jointly agreed by the parties. Entity C will reimburse B for the costs it incurs in managing the gas field and LNG facility.
 - (c) entity C is liable for taxes and royalties on the production and sale of LNG as well as for other liabilities incurred in the ordinary course of business, such as accounts payable, site restoration and decommissioning liabilities.
 - (d) companies A and B have equal shares in the profit from the activities carried out in the arrangement and, as such, are entitled to equal shares of any dividends distributed by entity C.
- IE47 The contractual arrangement does not specify that either party has rights to the assets, or obligations for the liabilities, of entity C.
- IE48 The board of entity C decides to enter into a financing arrangement with a syndicate of lenders to help fund the development of the gas field and construction of the LNG facility. The estimated total cost of the development and construction is CU1,000 million.*
- IE49 The lending syndicate provides entity C with a CU700 million loan. The arrangement specifies that the syndicate has recourse to companies A and B only if entity C defaults on the loan arrangement during the development of the field and construction of the LNG facility. The lending syndicate agrees that it will not have recourse to companies A and B once the LNG facility is in production because it has assessed that the cash inflows that entity C should generate from LNG sales will be sufficient to meet the loan repayments. Although at this time the lenders have no recourse to companies A and B, the syndicate maintains protection against default by entity C by taking a lien on the LNG facility.

* In ~~this~~ these examples monetary amounts are denominated in 'currency units (CU)'.

Analysis

- IE50 The joint arrangement is carried out through a separate vehicle whose legal form confers separation between the parties and the separate vehicle. The terms of the contractual arrangement do not specify that the parties have rights to the assets, or obligations for the liabilities, of entity C, but they establish that the parties have rights to the net assets of entity C. The recourse nature of the financing arrangement during the development of the gas field and construction of the LNG facility (ie companies A and B providing separate guarantees during this phase) does not, by itself, impose on the parties an obligation for the liabilities of entity C (ie the loan is a liability of entity C). Companies A and B have separate liabilities, which are their guarantees to repay that loan if entity C defaults during the development and construction phase.
- IE51 There are no other facts and circumstances that indicate that the parties have rights to substantially all the economic benefits of the assets of entity C and that the parties have an obligation for the liabilities of entity C. The joint arrangement is a joint venture.
- IE52 The parties recognise their rights to the net assets of entity C as investments and account for them using the equity method.

Example 7—Accounting for acquisitions of interests in joint operations in which the activity constitutes a business

- IE53 Companies A, B and C have joint control of Joint Operation D whose activity constitutes a business, as defined in IFRS 3 *Business Combinations*.
- IE54 Company E acquires company A's 40 per cent ownership interest in Joint Operation D at a cost of CU300 and incurs acquisition-related costs of CU50.
- IE55 The contractual arrangement between the parties that Company E joined as part of the acquisition establishes that Company E's shares in several assets and liabilities differ from its ownership interest in Joint Operation D. The following table sets out Company E's share in the assets and liabilities related to Joint Operation D as established in the contractual arrangement between the parties:

<u>Company E's share in the assets and liabilities related to Joint Operation D</u>	
<u>Property, plant and equipment</u>	<u>48%</u>
<u>Intangible assets (excluding goodwill)</u>	<u>90%</u>
<u>Accounts receivable</u>	<u>40%</u>
<u>Inventory</u>	<u>40%</u>
<u>Retirement benefit obligations</u>	<u>15%</u>
<u>Accounts payable</u>	<u>40%</u>
<u>Contingent liabilities</u>	<u>56%</u>

Analysis

- IE56 Company E recognises in its financial statements its share of the assets and liabilities resulting from the contractual arrangement (see paragraph 20).
- IE57 It applies the principles on business combinations accounting in IFRS 3 and other IFRSs for identifying, recognising, measuring and classifying the assets acquired, and the liabilities assumed, on the acquisition of the interest in Joint Operation D. This is because Company E acquired an interest in a joint operation in which the activity constitutes a business (see paragraph 21A).
- IE58 However, Company E does not apply the principles on business combinations accounting in IFRS 3 and other IFRSs that conflict with the guidance in this IFRS. Consequently, in accordance with paragraph 20, Company E recognises, and therefore measures, in relation to its interest in Joint Operation D, only its share in each of the assets that are jointly held and in each of the liabilities that are incurred jointly, as stated in the contractual arrangement. Company E does not include in its assets and liabilities the shares of the other parties in Joint Operation D.
- IE59 IFRS 3 requires the acquirer to measure the identifiable assets acquired and the liabilities assumed at their acquisition-date fair values with limited exceptions; for example, deferred tax assets and deferred tax liabilities are not measured at fair value but are measured in accordance with IAS 12 *Income Taxes*. Such measurement does not conflict with this IFRS and thus those requirements apply.
- IE60 Consequently, Company E determines the fair value, or other measure specified in IFRS 3, of its share in the identifiable assets and liabilities related to Joint Operation D. The following table sets out the fair value or other measure specified by IFRS 3 of Company E's shares in the identifiable assets and liabilities related to Joint Operation D:

<i>Fair value or other measure specified by IFRS 3 for Company E's shares in the identifiable assets and liabilities of Joint Operation D</i>	
<u>CU</u>	
<u>Property, plant and equipment</u>	<u>138</u>
<u>Intangible assets (excluding goodwill)</u>	<u>72</u>
<u>Accounts receivable</u>	<u>84</u>
<u>Inventory</u>	<u>70</u>
<u>Retirement benefit obligations</u>	<u>(12)</u>
<u>Accounts payable</u>	<u>(48)</u>
<u>Contingent liabilities</u>	<u>(52)</u>
<u>Deferred tax liability</u>	<u>(24)</u>
<u>Net assets</u>	<u>228</u>

IE61 In accordance with IFRS 3, the excess of the consideration transferred over the amount allocated to Company E's shares in the net identifiable assets is recognised as goodwill:

<u>Consideration transferred</u>	<u>CU300</u>
<u>Company E's shares in the identifiable assets and liabilities relating to its interest in the joint operation</u>	<u>CU228</u>
<u>Goodwill</u>	<u>CU72</u>

IE62 Acquisition-related costs of CU50 are not considered to be part of the consideration transferred for the interest in the joint operation. They are recognised as expenses in profit or loss in the period that the costs are incurred and the services are received (see paragraph 53 of IFRS 3).

Example 8—Contributing the right to use know-how to a joint operation in which the activity constitutes a business

IE63 Companies A and B are two companies whose business is the construction of high performance batteries for diverse applications.

IE64 In order to develop batteries for electric vehicles they set up a contractual arrangement (Joint Operation Z) to work together. Companies A and B share joint control of Joint Operation Z. This arrangement is a joint operation in which the activity constitutes a business, as defined in IFRS 3.

IE65 After several years, the joint operators (Companies A and B) concluded that it is feasible to develop a battery for electric vehicles using Material M. However, processing Material M requires specialist know-how and thus far, Material M has only been used in the production of cosmetics.

IE66 In order to get access to existing know-how in processing Material M, Companies A and B arrange for Company C to join as another joint operator by acquiring an interest in Joint Operation Z from Companies A and B and becoming a party to the contractual arrangements.

IE67 Company C's business so far has been solely the development and production of cosmetics. It has long-standing and extensive knowledge in processing Material M.

IE68 In exchange for its share in Joint Operation Z, Company C pays cash to Companies A and B and grants the right to use its know-how in processing Material M for the purposes of Joint Operation Z. In addition, Company C seconded some of its employees who are experienced in processing Material M to Joint Operation Z. However, Company C does not transfer control of the know-how to Companies A and B or Joint Operation Z because it retains all the rights to it. In particular, Company C is entitled to withdraw the right to use its know-how in processing Material M and to withdraw its seconded employees without any restrictions or compensation to Companies A and B or Joint Operation Z if it ceases its participation in Joint Operation Z.

IE69 The fair value of Company C's know-how on the date of the acquisition of the interest in the joint operation is CU1,000. Immediately before the acquisition, the carrying amount of the know-how in the financial statements of Company C was CU300.

Analysis

- IE70 Company C has acquired an interest in Joint Operation Z in which the activity of the joint operation constitutes a business, as defined in IFRS 3.
- IE71 In accounting for the acquisition of its interest in the joint operation, Company C applies all the principles on business combinations accounting in IFRS 3 and other IFRSs that do not conflict with the guidance in this IFRS (see paragraph 21A). Company C therefore recognises in its financial statements its share of the assets and liabilities resulting from the contractual arrangement (see paragraph 20).
- IE72 Company C granted the right to use its know-how in processing Material M to Joint Operation Z as part of joining Joint Operation Z as a joint operator. However, Company C retains control of this right because it is entitled to withdraw the right to use its know-how in processing Material M and to withdraw its seconded employees without any restrictions or any compensation to Companies A and B or Joint Operation Z if it ceases its participation in Joint Operation Z.
- IE73 Consequently, Company C continues to recognise the know-how in processing Material M after the acquisition of the interest in Joint Operation Z because it retains all the rights to it. This means that Company C will continue to recognise the know-how based on its carrying amount of CU300. As a consequence of retaining control of the right to use the know-how that it granted to the joint operation, Company C has granted the right to use the know-how to itself. Consequently, Company C does not remeasure the know-how, and it does not recognise a gain or loss on the grant of the right to use it.



**MEMBERS' HANDBOOK
CONTENTS OF VOLUME III**

(Updated to December 2016)

		<i>Issue/Review date</i>
Preface (Amended)	Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance and Related Services Prouncements	07/12
Glossary (Clarified)	Glossary of Terms Relating to Hong Kong Standards on Quality Control, Auditing, Review, Other Assurance and Related Services	02/15
HONG KONG STANDARDS ON QUALITY CONTROL		
HKSQC 1 (Clarified)	Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements	02/15
HONG KONG FRAMEWORK FOR ASSURANCE ENGAGEMENTS		
Framework (Amended)	Hong Kong Framework for Assurance Engagements	03/14
HONG KONG STANDARDS ON AUDITING		
HKSA 200 – 299	GENERAL PRINCIPLES AND RESPONSIBILITIES	
HKSA 200 (Clarified)	Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Hong Kong Standards on Auditing	02/15
HKSA 200	Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Hong Kong Standards on Auditing	01/16
HKSA 210 (Clarified)	Agreeing The Terms of Audit Engagements	06/14
HKSA 210	Agreeing the Terms of Audit Engagements	08/16
HKSA 220 (Clarified)	Quality Control for an Audit of Financial Statements	02/15
HKSA 220	Quality Control for an Audit of Financial Statements	08/15
HKSA 230 (Clarified)	Audit Documentation	02/15
HKSA 230	Audit Documentation	08/15
HKSA 240 (Clarified)	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements	02/15
HKSA 240	The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements	01/16
HKSA 250 (Clarified)	Consideration of Laws and Regulations in an Audit of Financial Statements	07/10
HKSA 260 (Clarified)	Communication with Those Charged with Governance	02/15
HKSA 260 (Revised)	Communication with Those Charged with Governance	01/16
HKSA 265 (Clarified)	Communicating Deficiencies in Internal Control to Those Charged with Governance and Management	02/15

		<i>Issue/Review date</i>
HKSA 805 (Clarified)	Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement	07/10
HKSA 805 (Revised)	Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement	08/16
HKSA 810 (Clarified)	Engagements to Report on Summary Financial Statements	09/14
HKSA 810 (Revised)	Engagements to Report on Summary Financial Statements	08/16
 HONG KONG STANDARDS ON REVIEW ENGAGEMENTS		
HSRE 2400 (Revised)	Engagements to Review Historical Financial Statements	12/12
HSRE 2410	Review of Interim Financial Information Performed by the Independent Auditor of the Entity	03/08
 HONG KONG STANDARDS ON ASSURANCE ENGAGEMENTS		
HKSAE 3000 (Revised)	Assurance Engagements Other Than Audits or Reviews of Historical Financial Information	02/15
HKSAE 3402	Assurance Reports on Controls at a Service Organization	03/14
HKSAE 3410	Assurance Engagements on Greenhouse Gas Statements	03/14
HKSAE 3420	Assurance Engagements to Report on the Compilation of Pro Forma Financial Information Included in a Prospectus	12/15
 HONG KONG STANDARDS ON INVESTMENT CIRCULAR REPORTING ENGAGEMENTS		
HK SIR 200	Accountants' Reports on Historical Financial Information in Investment Circulars	12/16
HK SIR 400 (Revised)	Comfort Letters and Due Diligence Meetings	12/16
HK SIR 500	Reporting on Profit Forecasts, Statements of Sufficiency of Working Capital and Statements of Indebtedness	12/15
 HONG KONG STANDARDS ON RELATED SERVICES		
HK SRS 4400	Engagements to Perform Agreed-upon Procedures Regarding Financial Information	11/04
HK SRS 4410 (Revised)	Compilation Engagements	07/12
 PRACTICE NOTES		
PN 600.1 (Revised)	Reports by the auditor under the Hong Kong Companies Ordinance (Cap.622)	12/15
PN 600.1 (Revised 2016)	Reports by the auditor under the Hong Kong Companies Ordinance (Cap.622)	08/16
PN 620.2	Communication between the Auditor and the Insurance Authority	02/13
PN 720	Acting as Scrutineer at a General Meeting of a Listed Issuer	07/05
PN 730 (Revised)	Guidance for Auditors Regarding Preliminary Announcements of Annual Results	09/15

HKSIR 200
Issued December 2016

Effective for engagements where the
investment circular is dated on or after 1 July 2017
Early application is permitted

*Hong Kong Standard on
Investment Circular Reporting Engagements 200*

Accountants' Reports on Historical Financial Information in Investment Circulars



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

**HONG KONG STANDARD ON
INVESTMENT CIRCULAR REPORTING ENGAGEMENTS 200**

**ACCOUNTANTS' REPORTS ON
HISTORICAL FINANCIAL INFORMATION IN INVESTMENT CIRCULARS**

(Effective for engagements where the investment circular is dated on or after 1 July 2017)
(Early application is permitted)

CONTENTS

	Paragraphs
Definitions	
Introduction	1-7
Respective Responsibilities of the Directors and the Reporting Accountants	8-11
True and Fair View, for the Purposes of the Accountants' Report.....	12-16
General Professional Considerations	17-22
Planning	23-26
Understanding of the Entity, its Environment and Risk Assessment	27-33
Materiality	34
The Reporting Accountants' Procedures	35-41
Evidence	42-56
Events Occurring up to the Date of the Reporting Accountants' Report.....	57
Events Occurring between the Date of the Reporting Accountants' Report and the Completion Date of the Transaction	58-60
Management Representations	61-67
Working Papers	68-71
Reporting	72-88
Communication with Those Charged with Governance	89
Reporting Accountants' Work for a Dual Listing Exercise	90
Consent	91
 Appendix 1 Example Accountants' Report on Historical Financial Information in Investment Circulars	
Appendix 2 Guidance on conventions commonly used in preparation of Historical Financial Information in Investment Circulars	
Appendix 3 Letter of consent	

Hong Kong Standard on Investment Circular Reporting Engagements (HKSIR) 200, *Accountants' Reports on Historical Financial Information in Investment Circulars* should be read in the context of the *Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* which sets out the application and authority of HKSIRs.

This HKSIR reflects the Listing Rules/GEM Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance that were in effect as at 29 December 2016.

Definitions

The definitions used in this HKSIR are:

- | | | |
|----|-----------------------------------|---|
| a. | Accountants' report: | A report by the reporting accountants included in an investment circular as required by Chapter 4 of the Listing Rules or Chapter 7 of the GEM Rules. |
| b. | Circular: | An announcement or document issued by an issuer for the information or action of holders of any of its securities as required by the Listing Rules/GEM Rules. |
| c. | Consent letter: | A letter whereby the reporting accountants consent to the inclusion in an investment circular of references to their name or the inclusion of any of their reports which are to be published therein in accordance with the Listing Rules/GEM Rules and/or the Companies (Winding Up and Miscellaneous Provisions) Ordinance. |
| d. | GEM Rules: | Rules Governing the Listing of Securities on GEM. |
| e. | GEM: | The Growth Enterprise Market operated by the Stock Exchange. |
| f. | Historical Financial Information: | The financial information as shown in the accountants' report included in the investment circular. |
| g. | HKSA: | Hong Kong Standards on Auditing. |
| h. | Institute or HKICPA: | Hong Kong Institute of Certified Public Accountants. |
| i. | Investment circular: | A document issued by an entity relating to securities and for the information or investment decision of the holders of the entity's securities or other parties, including without limitation a listing document, a prospectus, a circular to shareholders or similar document. |
| j. | Listing Rules: | Rules Governing the Listing of Securities on the Stock Exchange |
| k. | Prospectus: | A document which has the same meaning as in section 2(1) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance. |
| l. | Reporting accountants: | Certified public accountants who are engaged to prepare public reports and letters for inclusion in, or private letters in connection with, an investment circular. Where the context requires, this term includes auditors where they are carrying out a role in connection with an investment circular, other than that of reporting as auditors on financial statements. |
| m. | Securities: | Including but not limited to equity securities and debt securities as defined by the Listing Rules/GEM Rules. |

- n. Sponsor: Any corporation or authorised financial institution, licensed or registered under applicable laws to advise on corporate finance matters and appointed as a sponsor by a new applicant under the Listing Rules / GEM Rules to assist the new applicant with its initial application for listing.
- o. Stock Exchange: The Stock Exchange of Hong Kong Limited.

Introduction

1. In Hong Kong, section 31 to section 33 of Part II of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance, which is effective from 3 March 2014 sets out the requirements for inclusion of an accountants' report in a prospectus. In addition, the Listing Rules and the GEM Rules establish further circumstances where an accountants' report is required to be included in an investment circular. Chapter 4 of the Listing Rules and Chapter 7 of the GEM Rules provide detailed guidance on the preparation of accountants' reports to be included in an investment circular. The purpose of this HKSIR is to establish specific standards and provide guidance for reporting accountants engaged to issue an accountants' report on Historical Financial Information for inclusion in an investment circular.
2. Reporting accountants should also comply with HKSIR 100, *Investment Circulars and Reporting Accountants* when it is finalised and issued by the HKICPA.
3. The nature of the accountants' report is such that the objective of the reporting accountants' exercise does not differ in essence from that of an auditor. The underlying requirement of this HKSIR is that the reporting accountants will, in conducting the work necessary to provide the accountants' report, perform or rely on work that meets those requirements of HKSAAs, or other equivalent auditing standards¹, that are applicable to the reporting accountants' exercise. The reporting accountants apply HKSAAs on the basis set out in this HKSIR in the context of the following:
 - a. the reporting accountants are often reporting on financial information that has been included in, or formed part of, financial statements which have themselves already been subject to audit by an independent auditor; either by the same firm as the reporting accountants or by another firm of auditor. In consequence, there may be available to the reporting accountants a body of independent evidence relating to the Historical Financial Information which would not be available to the auditor examining the financial information for the first time;
 - b. the financial information being examined may relate to accounting periods in circumstances where financial statements for one, and possibly two, subsequent periods have been prepared and audited. These circumstances mean that in assessing risks that may affect the Historical Financial Information in relation to earlier periods the reporting accountants have the benefit of information relating to uncertainties affecting the financial information which would not have been available to auditor auditing the information for the first time; and
 - c. the reporting accountants do not have the statutory reporting responsibilities of auditor (for example there is no requirement to report if proper accounting records have not been kept by the entity). Details of the reporting responsibilities of an auditor under the Hong Kong Companies Ordinance (Cap. 622) are set out in Practice Note 600.1 (Revised), *Reports by the Auditor under the Hong Kong Companies Ordinance (Cap. 622)*.

¹ References hereinafter to HKSAAs should be taken to apply equally to other equivalent auditing standards.

4. This HKSIR provides standards that address those aspects of the reporting accountants' exercise that require the reporting accountants to perform procedures directly, for example risk assessment procedures. It also provides guidance on the application of HKSA's to the reporting accountants' exercise.
5. For the purpose of this HKSIR:
 - a. "Underlying Financial Statements" refers to special purpose audited financial statements prepared solely in connection with the investment circular. Underlying Financial Statements may comprise a single set of special purpose financial statements of the entity, the contents of which are consistent with the Historical Financial Information set out in the investment circular. Alternatively, Underlying Financial Statements may comprise two or more sets of special purpose financial statements at the intermediate holding company level which together form the basis of the Historical Financial Information set out in the investment circular. Underlying Financial Statements and the auditor's report thereon would normally be dated the same date as the accountants' report.
 - b. "Previously Issued Financial Statements" refers to previously issued financial statements of the entity and/or its subsidiaries upon which the Historical Financial Information as shown in the investment circular may in certain circumstances be based. Since they have been issued for a purpose other than in connection with the investment circular, Previously Issued Financial Statements and the auditor's report thereon would be dated earlier than the date of the accountants' report.
 - c. "Historical Financial Statements" refers to the financial statements upon which the Historical Financial Information in the investment circular is based. Historical Financial Statements most commonly take the form of "Underlying Financial Statements". Alternatively, in certain circumstances Historical Financial Statements may take the form of Previously Issued Financial Statements or other unaudited financial information.
 - d. The terms "entity", "Company", "issuer" or "listing applicant" refer to the reporting entity preparing the subject investment circular. In the case of an investment circular prepared for a purpose that involves a proposed acquisition transaction, the term "entity" refers to the subject of the proposed transaction, that is, the target company or target business.

This HKSIR recognises that the reporting accountants may wish to use evidence previously obtained by the auditor who audited the Historical Financial Statements for the relevant period covered by the reporting accountants' exercise. Guidance is provided on the steps that the reporting accountants undertake, including initial planning considerations, in order to assess the suitability of the audit evidence for this purpose.

6. Subject to the considerations set out in this HKSIR, references in the HKSA's to the auditor performing audit procedures or obtaining audit evidence may be read as references to the reporting accountants being satisfied that the procedures have been performed, or the evidence obtained, either by the reporting accountants or auditor.
7. HKSA's are applicable to the reporting accountants' exercise in respect of Historical Financial Information except when the requirement of an HKSA is predicated on a continuing relationship between auditor and the entity being audited, or where the requirement is replaced by the specific nature of the reporting accountants' responsibilities under applicable regulations as discussed in this HKSIR.

Respective Responsibilities of the Directors and the Reporting Accountants

8. The reporting accountants should obtain written acknowledgement from the directors of their responsibility for the Historical Financial Information (see paragraphs 61-67).

9. The directors are responsible for the preparation of the Historical Financial Information which gives for the purposes of the accountants' report a true and fair view for inclusion in investment circulars.
10. Historical Financial Information is based on the records of the entity for the periods reported on. These records reflect the representations and intentions of the management. Matters such as the selection of accounting policies, accounting estimates and valuation judgements form part of the responsibilities of management in compiling a record of its stewardship.
11. It is the reporting accountants' responsibility to form an opinion on the Historical Financial Information and to issue an accountants' report setting out that opinion. The accountants' report should state clearly that the Historical Financial Information (as set out on the relevant pages) forms an integral part of the accountants' report received from the reporting accountants for incorporation in the investment circular.

True and Fair View, for the Purposes of the Accountants' Report

12. The reporting accountants should:
 - a. obtain an understanding of the purpose of the investment circular;
 - b. ascertain which financial reporting framework is required to be used by the applicable regulations and which, if any, conventions commonly used as to the preparation of Historical Financial Information for inclusion in investment circulars are to be applied; and
 - c. consider the appropriateness of the accounting policies used,in order to determine whether the proposed Historical Financial Information is capable of giving a true and fair view, for the purposes of the accountants' report.
13. Certain conventions are commonly used in the preparation of Historical Financial Information in investment circulars. These conventions have been developed to the extent consistent with established accounting principles, to fulfil the criteria set out in the relevant regulations, present the information in an easily analysable form, and give a true and fair view for the purposes of the accountants' report. The Historical Financial Information includes disclosure of any conventions that have been applied in its preparation.
14. Appendix 2 of this HKSIR provides a summary of the conventions commonly used in the preparation of Historical Financial Information in investment circulars. In certain circumstances applying the conventions may result in combined, rather than consolidated, financial information being presented in order to meet the requirement to present financial information that gives a true and fair view, for the purposes of the accountants' report.
15. The directors of the entity are responsible for selecting appropriate accounting policies for the business of the entity. The reporting accountants consider whether the accounting policies adopted in the preparation of the Historical Financial Information are appropriate for the business of the entity and whether such policies are consistent with the applicable financial reporting framework.
16. Where the investment circular involves a proposed acquisition transaction by the issuer, the directors of the issuer are responsible for the contents of the investment circular in which the Historical Financial Information of the target is included, and such information is prepared based on accounting policies materially consistent with those of the issuer. The reporting accountants satisfy themselves that the accounting policies adopted in preparation of the Historical Financial Information of the target are materially consistent with those of the issuer. The reporting accountants also consider whether the policies are consistent with the applicable financial reporting framework.

General Professional Considerations

17. In the conduct of an engagement involving an investment circular, the reporting accountants should comply with the requirements of the Code of Ethics for Professional Accountants issued by the HKICPA.
18. While it is not the responsibility of the reporting accountants to judge the appropriateness, or otherwise, of a proposed transaction, in respect of which they have been engaged, there may be rare circumstances where reporting accountants consider the proposed transaction, or their proposed association with the transaction, to be so inappropriate that the reporting accountants cannot properly commence work or continue to act.
19. The reporting accountants should agree the terms of the engagement with those from whom they accept instructions. All the terms of the engagement should be recorded in writing.
20. Where the evidence used by the reporting accountants includes that contained within the working papers of the auditor, the working papers of the reporting accountants identify the audit working papers reviewed and the nature of the work performed by the auditor. Whilst it is not necessary for the reporting accountants' working papers to replicate all of the detailed findings contained in the auditor's working papers, the reporting accountants document the basis on which the auditor addressed the particular risks identified in the reporting accountants' risk assessment procedures.
21. In considering the requirements of HKSA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements* and HKSA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements* for the auditor to report any matters arising to certain authorities, the reporting accountants will need to assess the effect of these requirements when reporting in terms of the true and fair view, for the purposes of the accountants' report. Where matters arise which may potentially require disclosure by the reporting accountants and the reporting accountants are unsure how to proceed, the reporting accountants should take legal advice.
22. In applying HKSA 240, HKSA 250 and HKSA 260 (Revised), *Communication With Those Charged With Governance*, the reporting accountants consider who, in relation to the investment circular, would be regarded as a person charged with governance. Where the issuer has already formed an audit committee as a subgroup of those charged with governance, the reporting accountants communicate with the audit committee in accordance with the guidance set out in this HKSIR and determine whether they also need to communicate with the governance body, such as the board of directors of the issuer.

Planning

23. The reporting accountants should perform and document risk assessment procedures to support the reporting accountants' exercise.
24. In addition, reporting accountants may consider:
 - a. any modifications to the auditor's report on the Historical Financial Statements and the potential impact on the approach to the reporting accountants' exercise;
 - b. the nature of adjustments to the Historical Financial Statements which the preparer of the Historical Financial Information represents as necessary (for example as a result of correction of errors, achieving consistent accounting policies or changing the applicable financial reporting framework) and the sources of evidence to support the adjustments;
 - c. the interaction with other roles undertaken by the reporting accountants in connection with the transaction;

- d. staffing, including relevant experience and skills linked to investment circular reporting, and sources of consultation;
 - e. liaison with the auditor and arrangements for terms of access to the auditor's working papers, or equivalent evidence if maintained in electronic form;
 - f. the nature and timing of procedures to support any decision to rely on evidence obtained by the auditor;
 - g. whether the financial reporting framework applicable to the Historical Financial Statements is the same as that applicable to the financial information contained in the investment circular;
 - h. whether there are any special circumstances concerning the appointment, resignation or reporting responsibilities of the auditor;
 - i. whether there is evidence of any limitation having been placed on the work of the auditor; and
 - j. whether corrections or adjustments to subsequent financial statements indicate possible inadequacies in the audits of earlier periods.
25. Where the reporting accountants are considering using audit evidence obtained by the auditor as part of the evidence for the reporting accountants' exercise, the reporting accountants should consider the professional qualification, independence and professional competence of the auditor and the quality control systems applied by the audit firm to that engagement.
26. Matters that the reporting accountants consider include:
- a. the integrity and experience of the auditor;
 - b. whether the auditor was required to apply HKSA's or equivalent standards; and
 - c. whether there is any evidence that the auditor has not complied with applicable independence requirements.

Understanding of the Entity, its Environment and Risk Assessment

27. The reporting accountants should obtain an understanding of the entity and its environment, including its internal controls, sufficient to identify and assess the risks of material misstatement of the Historical Financial Information whether due to fraud or error, and sufficient to design and perform further procedures.
28. Such an understanding is ordinarily obtained by:
- a. meeting the directors and management of the entity;
 - b. visiting the entity's premises;
 - c. discussing the financial information and recent results with management;
 - d. applying analytical procedures to the financial information; and
 - e. obtaining from management an understanding of the principal transaction flows, internal controls and reporting arrangements of the business.

29. If this process indicates that there are factors which may give rise to a modification of the reporting accountants' opinion, an emphasis of matter or a material uncertainty related to going concern then such factors are reported immediately to those responsible for the investment circular, usually the directors of the issuer and any other responsible parties, for example, the sponsors in the case of an initial listing application.
30. In considering areas of risk in relation to the periods for which the Historical Financial Information is presented, the reporting accountants have regard to the probability that misstatements in earlier periods, if they exist, are likely to have been detected in subsequent periods. Account is also taken of the fact that other uncertainties, particularly those affecting subjective matters in the Historical Financial Information, may have been resolved with the passage of time.
31. When performing the risk assessment, the reporting accountants should take into account all other relevant work performed in connection with the investment circular.
32. The reporting accountants may be undertaking other relevant work related to the transaction giving rise to the accountants' report. For example, the reporting accountants may have been commissioned to prepare a comfort letter on a statement of sufficiency of working capital.
33. If other relevant work has been performed by another firm, the reporting accountants should request the issuer to provide access to such work. If the reporting accountants are not allowed access to such work, they should consider the implications for their report.

Materiality

34. The reporting accountants determine materiality for the purposes of the reporting accountants' work independently from the auditor who previously audited the Historical Financial Statements, and accordingly the reporting accountants' assessment of materiality may differ from that of the auditor. In determining materiality for the purposes of reporting on Historical Financial Information, regard is had to the context in which the opinion is to be given (which includes the fact that the information may relate to a trend of results over the track record period).

The Reporting Accountants' Procedures

35. The reporting accountants should perform procedures to obtain sufficient appropriate evidence that the work of an auditor which the reporting accountants plan to use is adequate for the reporting accountants' purposes. Where the reporting accountants conclude that the auditor's work is not adequate, or the reporting accountants do not have access to the auditor's working papers, the reporting accountants should perform procedures that compensate for this. The procedures of the auditor and the reporting accountants, taken together, should meet the requirements of HKSA's unless:
 - a. a requirement is not applicable to the reporting accountants' engagement, as discussed in this HKSIR; or
 - b. it is not practicable for the reporting accountants to undertake such procedures.
36. If the reporting accountants decide not to comply with a requirement of HKSA's because it is not practicable for them to undertake such procedures (for example, if there has been a change in an auditing standard during the latest period which requires certain procedures to be carried out at a physical inventory count at the balance sheet date, it may not be practicable for the reporting accountants to undertake such procedures in respect of physical inventory counting for prior periods), they should document the reason for not complying with the requirement and why its omission does not have an impact on their opinion.

37. In approaching the procedures to be performed in response to the assessed risk of material misstatement at the assertion level, the reporting accountants consider the extent to which the procedures that the reporting accountants wish to perform have previously been performed by the auditor. Where such procedures have been performed by the auditor, the reporting accountants may, subject to the considerations discussed in this HKSIR, use the evidence obtained by the auditor from those procedures as part of the reporting accountants' own evidence.
38. Where applicable auditing standards have changed during the period covered by the Historical Financial Information, or it is not practicable for the reporting accountants to undertake procedures that meet the requirements of HKSAAs, the reporting accountants consider the implications for the reporting accountants' exercise, having regard to their risk assessment, including the potential need to perform additional procedures.
39. When the reporting accountants intend to use audit evidence obtained by the auditor, they should evaluate whether the audit procedures performed by the auditor adequately respond to the reporting accountants' assessment of the risks (including significant risks requiring special audit consideration) of material misstatement of the Historical Financial Information to be included in the investment circular.
40. The reporting accountants' procedures should include:
- a. examining material adjustments from the Historical Financial Statements made during the course of preparing the Historical Financial Information and considering whether the adjustments are necessary and whether they have been correctly determined;
 - b. evaluating whether all necessary adjustments to the Historical Financial Statements have been made; and
 - c. comparing the Historical Financial Information to the Historical Financial Statements and assessing whether the information has been accurately extracted therefrom.
41. In certain areas, use of the work of the auditor may be the only practicable means of obtaining the evidence necessary to support the reporting accountants' opinion². The timing of the reporting accountants' own work will inevitably be dictated by the timing of the preparation of the Historical Financial Information and the related investment circular and this may be some time after the end of the periods to which the report relates.

Evidence

42. When the reporting accountants are engaged to prepare an accountants' report, the reporting accountants should obtain sufficient appropriate evidence to express an opinion as to whether the Historical Financial Information presents a true and fair view, for the purposes of the accountants' report.
43. The reporting accountants should evaluate the quality of the audit evidence obtained by the auditor that the reporting accountants intend to rely on. Where the reporting accountants conclude that such audit evidence is either not sufficient or is inappropriate for the purposes of the reporting accountants' exercise, the reporting accountants should obtain evidence directly. The reporting accountants should also obtain evidence directly to the extent that the Historical Financial Information is based on material unaudited financial information. Where the evidence is not available, the reporting accountants should consider the implications for their report.

² For example, procedures which require the reporting accountants to be physically present at a client site at a relevant date (such as attendance at physical inventory counting) will clearly be impossible to perform.

44. Where the Historical Financial Information is derived from audited Historical Financial Statements, the auditor's working papers will frequently be a useful source for the evidence which the reporting accountants may need to provide an opinion on the Historical Financial Information.
45. When audited Historical Financial Statements have been used as the basis for the Historical Financial Information upon which they are reporting, the reporting accountants consider whether applicable HKSAs were complied with by the auditor. The reporting accountants assess the extent to which they are able to rely on the auditor's work and the further evidence they need to support their own opinion. When the Historical Financial Information is not derived from audited Historical Financial Statements the reporting accountants comply with HKSAs in performing their own work to the extent that the reporting accountants judge applicable. In these circumstances much of this work is being done with the benefit of hindsight.
46. The reporting accountants accept evidence in the auditor's working papers as being prima facie truthful and genuine, but in considering that evidence adopt an attitude of professional skepticism, whether the audit working papers were produced by an auditor from the reporting accountants' firm or by the other auditor. However, with respect to audit working papers obtained from their own firm, reporting accountants are more familiar with the detailed quality control procedures that have been applied in the conduct of the audit. The extent to which independent testing of the evidence provided in the auditor's working papers will be necessary is a matter for the reporting accountants' judgement on the basis of the information available at the time, including their assessment of the risks of misstatement.
47. Where the reporting accountants intend to rely on internal controls of the entity, the reporting accountants perform tests of control when unable to rely on the auditor's tests of such internal controls. This is likely to arise when:
 - a. the auditor has not performed tests of those internal controls; or
 - b. the auditor has performed tests of internal controls but the internal controls have subsequently changed.
48. Where relevant information is not available from the audit working papers, the reporting accountants will need to obtain the relevant evidence directly. The audit working papers are unlikely for example, to contain information concerning events after the reporting period up to the date of signing the accountants' report.
49. When the entity's auditor (including former auditor) is not appointed as the reporting accountants, they will be aware that the reporting accountants may need to meet them and obtain access to information contained in the audit files. The auditor is normally prepared to meet with the reporting accountants and make its audit files available in accordance with relevant professional guidance to reporting accountants for the purpose of work under this HKSIR.
50. If access is granted, it would normally be on the basis that the auditor accepts no responsibility or liability to the reporting accountants in connection with the use of the audit working papers by the reporting accountants. Such a basis of access has no effect on the validity or otherwise of auditor's working papers as a source of evidence for the reporting accountants. The reporting accountants use their own judgement in determining whether they can rely on the audit working papers as appropriate evidence. The reporting accountants, however, do not use the conclusions recorded in the auditor's working papers as a substitute for their own judgement.
51. The matters that are considered in the course of planning what reliance might be placed upon the work of the auditor and the degree of independent testing which may be necessary, particularly where the auditor is subject to different regulatory requirements, will normally include:

- a. What is known about the professional qualification and integrity of the auditor?
- b. What auditing standards and requirements apply to the work of the auditor?
- c. Are there any special circumstances concerning the appointment of the auditor and to whom does it report?
- d. Are the reporting accountants able to satisfy themselves that the auditor is independent in all respects?
- e. Has any limitation been placed on the work of the auditor (either in terms of access, time etc., or because of the level of remuneration) or has it been free to decide on the scope and level of its audit tests?
- f. Has the work of the auditor been conducted to an appropriate materiality level?
- g. Has the auditor in fact complied with the basic principles and essential procedures in HKSA's, with which auditor is required to comply in the conduct of any audit (or with equivalent overseas standards)?
- h. Do corrections or adjustments to subsequent financial statements indicate possible inadequacies in the audits of earlier periods?
- i. Was the auditor's report modified?

52. Whether or not the reporting accountants have access to the auditor's working papers, they seek to obtain, either from the directors or from the auditor, copies of management letters sent by the auditor to the entity and copies of any responses to such letters made by the directors.

Evidence from Other Sources

53. Notwithstanding that evidence is to be or has been obtained from an assessment of the auditor's working papers, the reporting accountants will usually seek direct evidence from the entity to be reported on. Such direct evidence is usually obtained from, but is not limited to, the following sources:

- a. by meeting the directors and management of the entity;
- b. by visiting the entity's premises;
- c. from discussing the Historical Financial Information and recent results with management;
- d. from applying analytical procedures to the Historical Financial Information; and
- e. from obtaining an understanding of the principal transaction flows, internal controls and reporting arrangements of the business.

Analytical Procedures

54. Reporting accountants apply analytical procedures at the planning and at the evidence gathering stages of the assignment as well as part of the overall review when completing the assignment. When significant fluctuations or unexpected relationships are identified that are inconsistent with other relevant information, the reporting accountants investigate and obtain explanations. Where practicable, they discuss with management the features and trends of the results during the relevant period.

55. The reporting accountants may be engaged to issue a number of reports and letters related to the securities transaction giving rise to the accountants' report. Evidence obtained as a result of such other work may form part of the basis for the reporting accountants' opinion included in the accountants' report.

Joint Reporting Accountants

56. When joint reporting accountants are appointed the division of work as between them is a matter for agreement. The arrangements between the joint reporting accountants may form part of the engagement letter. Irrespective of any such arrangement, the joint reporting accountants are jointly and severally responsible for the entire accountants' report. Each of the joint reporting accountants participates in the planning of the engagement and they agree upon the scope of work and any changes subsequently found to be necessary thereto. Each of the joint reporting accountants has regard to the considerations set out above in respect of using the work of other auditor in determining the extent to which they are satisfied to rely on the evidence obtained by the other reporting accountants or the extent to which they consider it necessary to carry out their own work, including especially the matters set out in paragraph 51 above. Each of the joint reporting accountants review the work of the other to the extent considered necessary and records the results of that review.

Events Occurring up to the Date of the Reporting Accountants' Report

57. The Underlying Financial Statements and the related auditor's report would normally be dated the same date as the accountants' report. Accordingly, all subsequent events would have already been considered for the purposes of the Underlying Financial Statements. Where the Historical Financial Information is based on Previously Issued Financial Statements or unaudited management accounts, reference is made to the guidance set out in the relevant financial reporting and auditing framework in determining whether adjustment is to be made for events occurring subsequent to the reporting period.

Events Occurring between the Date of the Reporting Accountants' Report and the Completion Date of the Transaction

58. In the period between the date of the reporting accountants' report and the completion date of the transaction, the reporting accountants may become aware of events and other matters which might have caused the reporting accountants to issue a different report or to withhold consent. In such a case, the reporting accountants should discuss the implications of the events or other matters with those responsible for the investment circular and take additional action as appropriate.
59. For the purpose of this HKSIR, after the date of the accountants' report, the reporting accountants have no obligation to perform procedures or make enquiries regarding the investment circular.
60. If, as a result of discussions with those responsible for the investment circular concerning a subsequent event that occurred prior to the completion date of the transaction, the reporting accountants are either uncertain about or disagree with the course of action proposed, the reporting accountants may consider it necessary to take legal advice with respect to an appropriate course of action.

Management Representations

61. The reporting accountants should obtain appropriate written confirmation of representations from the directors of the entity.
62. Written confirmation of representations made by the directors on matters material to the reporting accountants' report should be obtained. These representations also encompass statements or opinions attributed to directors, management, employees or agents of the entity, which are relied upon by the reporting accountants. The directors' representation letter is usually dated the same date as the relevant accountants' report.
63. Representations by the directors of the issuer cannot replace the evidence that the reporting accountants could reasonably expect to be available to support any opinion given, if any. An inability to obtain sufficient and appropriate evidence regarding a matter could represent a limitation of scope even if a representation has been received on the matter.
64. A number of specific representations are required by HKSAAs. Where representations have been obtained by the auditor, subject to the considerations set out in this HKSIR, it may not be necessary for the reporting accountants to seek further representations covering the same matters, other than in relation to the period since the audit opinion relating to the final period included in the Historical Financial Information was given.
65. Representations additional to those pursuant to HKSAAs that the reporting accountants may consider for incorporation in the letter of representation include confirmation from the directors of the entity that (i) they are responsible for the preparation of the Historical Financial Information; (ii) any adjustments made to Historical Financial Statements for the purposes of preparing the Historical Financial Information are necessary; and (iii) such information gives a true and fair view for the purpose of the accountants' report.
66. For listing applications, reporting accountants are required to issue a confirmation (the "Reporting Accountants' Confirmation") to the applicant that no significant adjustment or modification is expected to be made to the draft reports included in the investment circular based on the work done as of the date of the confirmation, when the application proof is submitted. If there are any updates to the financial information after the submission of the application proof, the reporting accountants must also provide a similar confirmation on the updated financial information at the same time the information is submitted to the Stock Exchange. Accordingly, the reporting accountants should obtain, where applicable, the directors' representation letter on the date of the Reporting Accountants' Confirmation to support the issuance of the Reporting Accountants' Confirmation; and obtain additional or updating representation letter(s) when further confirmations are provided and final reports are issued.
67. In connection with the issue of a Reporting Accountants' Confirmation in respect of the draft accountants' report on the Historical Financial Information, the reporting accountants obtain a separate representation from the directors of the entity as of the date of the submission or re-submission of the application proof that:
 - a. no significant adjustment is expected to be made to the draft accountants' report on the Historical Financial Information included in the draft investment circular; and, if applicable,

- b. the stub period comparative financial information³, and the stub period financial information⁴, where appropriate, included in the draft accountants' report is prepared, in all material respects, in accordance with the basis of preparation and presentation as described in the draft accountants' report.

Working Papers

68. The reporting accountants should document matters that are significant in providing evidence that supports the report provided and in providing evidence that the engagement was performed in accordance with this HKSIR. For example, the reporting accountants should record in the working papers their reasoning on all significant matters that require the exercise of judgement, and related conclusions.
69. The information to be recorded in the working papers is a matter of professional judgement since it is neither necessary nor practical to document every matter considered by the reporting accountants. When applying professional judgment in assessing the extent of documentation to be prepared and retained, the reporting accountants may consider what is necessary to provide an understanding of the work performed and the basis of the principal decisions taken to another person, such as reporting accountants, who have no previous experience with the engagement. That other person may, however, only be able to obtain an understanding of detailed aspects of the engagement by discussing them with the reporting accountants who prepared the documentation.
70. A large part of the work performed will often take the form of reading files and documents and discussions with the issuer's management, staff and professional advisers. The working papers of the reporting accountants are designed so as to reflect adequately the nature of these procedures carried out, the evidence examined and the conclusions reached. Therefore, it is not usually necessary for the reporting accountants' working papers to replicate all of the detailed findings contained in the auditor's working papers.
71. As regards the retention of engagement documentation, the reporting accountants should apply policies and procedures to ensure compliance with Hong Kong Standard on Quality Control 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* paragraphs 47 and A60 to A62. For an engagement performed in accordance with this HKSIR, the retention period ordinarily is no shorter than five years from the date of the report issued by the reporting accountants.

Reporting

72. The following standards and guidance are applicable to accountants' reports on Historical Financial Information.

³ The stub period comparative financial information refers to the comparative financial information of a stub period which may or may not form part of the final track record period, which must, as a minimum, be reviewed by the reporting accountants under Hong Kong Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* ("HKSRE 2410") as described in paragraph 79 of this HKSIR.

⁴ The stub period financial information stated above refers to financial information for a current interim period included in an investment circular where the listing applicant submits or plans to submit under the early filing mechanism as set out in the guidance letter issued by The Stock Exchange of Hong Kong Limited "HKEx-GL6-09A - Guidance on the financial information for the trading record period expected in the first draft listing document for listing applications", which must, as a minimum, be reviewed by the reporting accountants under HKSRE 2410. Such stub period is expected to be superseded by an updated and final track record period to be included in the final prospectus. For example, the accountants' report of a December year end Main Board listing applicant which applies early filing may initially include a financial period covering full financial years ended 31 December 2014 and 2015, and a stub period for the nine months ending 30 September, 2016. As the final track record period to be included in the prospectus would cover the full three years ending 31 December 2016, the stub period for the nine months ending 30 September 2016 would be superseded and it must, as a minimum, be reviewed by reporting accountants under HKSRE 2410.

Statement of Responsibility

73. The reporting accountants should distinguish between their responsibilities and those of the directors by including in their report:
- a. a statement that the preparation of the Historical Financial Information is the responsibility of the directors; and
 - b. a statement that the reporting accountants' responsibility is to express an opinion on the Historical Financial Information.

Basis of Opinion

74. The reporting accountants should explain the basis of their opinion by including in their report:
- a. a statement as to their compliance or otherwise with this HKSIR or the reasons for any departure therefrom; and
 - b. a statement that they planned and performed their work so as to obtain reasonable assurance as to whether the Historical Financial Information upon which their opinion is given is free from material misstatement.

Expression of Opinion

75. The accountants' report should contain a clear expression of opinion on the Historical Financial Information.
76. The reporting accountants' opinion is usually expressed in terms of whether the Historical Financial Information gives, for the purpose of the accountants' report, a true and fair view of the financial position, financial performance and cash flows in accordance with the basis of preparation and presentation set out in the notes to the Historical Financial Information that describes, among others, that the preparation of Historical Financial Information is in accordance with the stated accounting policies which conform with Hong Kong Financial Reporting Standards (or other applicable financial reporting framework).
77. The reporting accountants need to be satisfied that the Historical Financial Information adequately describes the applicable financial reporting framework, and makes reference to this in the report.
78. The reporting accountants should apply the principles set out in HKSA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report* and HKSA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report* relating to modified reports. With respect to material uncertainties arising from the adoption of the going concern basis the reporting accountants should apply the principles set out in HKSA 570 (Revised), *Going Concern*.

Review of stub period comparative financial information

79. The Listing Rules/GEM Rules require that the reporting accountants should, as a minimum, carry out a review of any stub period comparative historical financial information in accordance with Hong Kong Standards on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the Institute. The Listing Rules/GEM Rules provide that the stub period comparative financial information may alternatively be audited. The reporting accountants' report following their review or audit of the stub period comparative historical financial information is required to be included within the accountants' report.

Comparatives

80. The reporting accountants are required to express a true and fair opinion on the financial position as at each financial year end and as at any stub period date included in the Historical Financial Information and on the financial performance and cash flows for each of the associated financial years or stub period. The reporting accountants are also required to give a review conclusion on any stub period comparative historical financial information that is presented. The Historical Financial Information upon which the reporting accountants express a true and fair opinion does not constitute "comparative information" as contemplated by HKSA 710, *Comparative Information — Corresponding Figures and Comparative Financial Statements*. However, stub period comparative historical financial information does constitute "comparative information" as contemplated by HKSA 710. Accordingly, HKSA 710 is only applicable to the work of the reporting accountants in respect of stub period comparative information.

Audit qualifications

81. Where the auditor's report(s) on the Historical Financial Statements was qualified on grounds for example of failure to comply with an applicable accounting standard or disagreement over an accounting treatment, it may be possible to make adjustments to the Historical Financial Information so as to avoid a similar qualification in the accountants' report.

Reference to previous audit opinions

82. The reporting accountants' opinion is arrived at independently of any audit opinion previously given by the auditor on the financial statements which form the basis for the financial information to be reported on. It is not part of the reporting accountants' role to explain (where this is the case) why the reporting accountants' opinion differs from the opinion of the auditor. However, the reporting accountants consider the issues leading to previously issued qualifications, if any, the implications for their report and whether any additional work needs to be performed to resolve such issues.

Reference to dividends

83. Section 31(1)(b) of Part II of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance requires disclosure of information about the rates of the dividends, if any, paid by the company in respect of each class of shares in the company in respect of each of the 3 financial years immediately preceding the issue of the prospectus, giving particulars of each such class of shares on which such dividends have been paid and particulars of the cases in which no dividends have been paid in respect of any class of shares in respect of any of those years. This information may be included in the section "Report on matters under the Listing Rules/GEM Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance" or in the notes to the Historical Financial Information as illustrated in Appendix 1 to this HKSIR.

Reference to adjustments

84. Section 42 of Part III of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance requires accountants' reports to either indicate by way of note any adjustments as respects the figures of any profits or losses or assets and liabilities dealt with by the report which appear to the persons making the report necessary or shall make those adjustments and indicate that adjustments have been made. The Listing Rules/GEM Rules also require that the reporting accountants state in their report that the Historical Financial Information is stated after making such adjustments to the Historical Financial Statements as were considered necessary or, alternatively, that in preparing the Historical Financial Information no adjustments to the Historical Financial Statements have been made. More guidance on adjustments is set out in Appendix 2 to this HKSIR.

No Historical Financial Statements

85. Section 31 of Part II of the Third Schedule to the Companies (Winding Up and Miscellaneous Provisions) Ordinance requires that where no financial statements have been made up in respect of any part of the period of three years ending on a date three months before the issue of the prospectus, the accountants' report contains a statement of that fact.
86. Such statement is usually required where the entity, which is the subject of the investment circular, is incorporated shortly before the date of the investment circular.

Date of Accountants' Report

87. The accountants' report is dated on the same date as the investment circular in which it is included or to which it relates.

Example Accountants' Report

88. An example accountants' report on Historical Financial Information in an investment circular is set out in Appendix 1 to this HKSIR.

Communication with Those Charged with Governance

89. Although HKSA 260 (Revised) is written in the context of an audit of financial statements, the reporting accountants may refer to such standard when they communicate with those charged with governance that have a responsibility to oversee the preparation of the Historical Financial Information for investment circulars. The reporting accountants meet and discuss with those charged with governance, such as the audit committee and/ or the board of directors any significant findings on audit and accounting issues, difficulties encountered during the course of their work and other matters as set out in HKSA 260 (Revised). Their communication with those charged with governance may also be in writing.

Reporting Accountants' Work for a Dual Listing Exercise

90. In the situation where an entity offers securities or seeks a listing of its shares on the Stock Exchange and other stock exchange(s) simultaneously and that entity proposes to engage the same reporting accountants to report on the Historical Financial Information in the investment circulars for different stock exchanges, the reporting accountants need to consider whether they would satisfy the requirements in the relevant jurisdiction(s) which include, but are not limited to, their independence and qualification as auditor or reporting accountants under the applicable laws and regulations in the relevant jurisdiction(s), and whether their reports prepared pursuant to this HKSIR would also satisfy the requirements of the relevant exchange(s).

Consent

91. Financial and other information is contained throughout an investment circular and not only in the accountants' report. Whilst the reporting responsibility of the reporting accountants does not extend beyond their own report, reporting accountants should consider the investment circular as a whole. Reporting accountants should be satisfied that nothing contained within the investment circular as a whole is inconsistent with the information in their report, and that all relevant matters which have come to their attention have been properly reflected. In particular, the reporting accountants should take steps to make themselves aware of all the principal issues arising during the drafting of the investment circular. The reporting accountants should give consent where applicable to the publication of the investment circular containing their report only if they are satisfied with the form and context in which their report appears in the published investment circular. Appendix 3 of this HKSIR provides further guidance about the issuance of a letter of consent.

Appendix 1 – Example Accountants' Report on Historical Financial Information in Investment Circulars

Circumstances include the following:

- The Accountants' Report on Historical Financial Information is assumed to be inserted at Appendix I of the investment circular.
- Pages I-1 to I-3 in this example are printed with the reporting accountants' letterhead and continuing pages.

The following is the text of a report set out on pages I-1 to I-[], received from the Company's reporting accountants, ABC & Co., Certified Public Accountants, Hong Kong, for the purpose of incorporation in this investment circular.

APPENDIX I ACCOUNTANTS' REPORT ON HISTORICAL FINANCIAL INFORMATION

Letterhead of reporting accountants

ACCOUNTANTS' REPORT ON HISTORICAL FINANCIAL INFORMATION TO THE DIRECTORS OF XYZ LIMITED AND SPONSORS LIMITED

Introduction

We report on the historical financial information of XYZ Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages [I - 4] to [I - Z], which comprises the [consolidated /combined] statement of financial position¹ as at [respective dates of the reporting periods] and the [consolidated /combined] statements of profit or loss, the [consolidated/combined] statements of comprehensive income, the [consolidated/combined] statements of changes in equity and the [consolidated/combined] statements of cash flows for each of the periods then ended (the "Track Record Period") and a summary of significant accounting policies and other explanatory information (together, the "Historical Financial Information"). The Historical Financial Information set out on pages [I-4] to [I-Z] forms an integral part of this report, which has been prepared for inclusion in the investment circular of the Company dated [] (the "Investment Circular") in connection with the initial listing of shares of the Company on the Main Board of The Stock Exchange of Hong Kong Limited.

Directors' responsibility for the Historical Financial Information

The directors of the Company are responsible for the preparation of Historical Financial Information that gives a true and fair view in accordance with the basis of preparation and presentation set out in Note X to the Historical Financial Information, and for such internal control as the directors determine is necessary to enable the preparation of Historical Financial Information that is free from material misstatement, whether due to fraud or error.

[I - 1]

¹ Terms like "the balance sheets", "the statement of comprehensive income" and "cash flow statements" as set out in Hong Kong Accounting Standard 1 (Revised) Presentation of Financial Statements, may be used as long as they are consistent with the titles of the corresponding statements in the historical financial information.

APPENDIX I
ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

Continuing page of reporting accountants

Reporting accountants' responsibility

Our responsibility is to express an opinion on the Historical Financial Information and to report our opinion to you. We conducted our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 200, *Accountants' Reports on Historical Financial Information in Investment Circulars* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). This standard requires that we comply with ethical standards and plan and perform our work to obtain reasonable assurance about whether the Historical Financial Information is free from material misstatement.

Our work involved performing procedures to obtain evidence about the amounts and disclosures in the Historical Financial Information. The procedures selected depend on the reporting accountants' judgement, including the assessment of risks of material misstatement of the Historical Financial Information, whether due to fraud or error. In making those risk assessments, the reporting accountants consider internal control relevant to the entity's preparation of Historical Financial Information that gives a true and fair view in accordance with the basis of preparation and presentation set out in Note X to the Historical Financial Information in order to design procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Our work also included evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the Historical Financial Information.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion the Historical Financial Information gives, for the purposes of the accountants' report, a true and fair view of [the Company's and] (to insert as appropriate) the Group's financial position as at [respective dates of reporting periods] and of the Group's financial performance and cash flows for the Track Record Period in accordance with the basis of preparation and presentation set out in Note X to the Historical Financial Information.

● ***Review of stub period comparative financial information***

We have reviewed the stub period comparative financial information of the Group which comprises statements of [consolidated/combined] profit or loss, comprehensive income, changes in equity and cash flows for the [x] months ended [date] and other explanatory information (the "Stub Period Comparative Financial Information"). The directors of the Company are responsible for the preparation and presentation of the Stub Period Comparative Financial Information in accordance with the basis of preparation and presentation set out in Note X to the Historical Financial Information. Our responsibility is to express a conclusion on the Stub Period Comparative Financial Information based on our review. We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* issued by the HKICPA. A review consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion. Based on our review, nothing has come to our attention that causes us to believe that the Stub Period Comparative Financial Information, for the purposes of the accountants' report, is not prepared, in all material respects, in accordance with the basis of preparation and presentation set out in Note X to the Historical Financial Information.

[I - 2]

APPENDIX I
ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

Continuing page of reporting accountants

Report on matters under the [Listing Rules/GEM Rules]² and the Companies (Winding Up and Miscellaneous Provisions) Ordinance

Adjustments

[In preparing the Historical Financial Information no adjustments to the Underlying Financial Statements as defined on page I-4 (case 1) have been made. / The Historical Financial Information is stated after making such adjustments to the Underlying Financial Statements as defined on page I-4 (case 2) as were considered necessary. / The Historical Financial Information is stated after making such adjustments to the Historical Financial Statements as defined on page I-4 (case 3) as were considered necessary.]²

Dividends

We refer to note [] to the Historical Financial Information which [contains information about the dividends paid by XYZ Limited in respect of the Track Record Period/ states that no dividends have been paid by XYZ Limited in respect of the Track Record Period].

No historical financial statements for the Company (where applicable)

[No financial statements have been prepared for the Company since its date of incorporation to [the period of three years ending on a date three months before the issue of the investment circular].]

**ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date**

[I - 3]

² Delete whichever is not applicable

APPENDIX I

ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

HISTORICAL FINANCIAL INFORMATION OF THE GROUP

Preparation of Historical Financial Information

Set out below is the Historical Financial Information which forms an integral part of this accountants' report.

Case 1 – Where the Historical Financial Information in the accountants' report is prepared based on a single set of special purpose financial statements of the entity, the following language may be used:

"The financial statements of the Group for the Track Record Period, on which the Historical Financial Information is based, were audited by [name of the firm] in accordance with [the applicable auditing framework] issued by [the relevant standard setting body] ("Underlying Financial Statements")."

Case 2 - Where the Historical Financial Information in the accountants' report is prepared based on two or more sets of special purpose financial statements at the intermediate holding company level, the following language may be used:

"The Historical Financial Information in this report was prepared based on financial statements [and management accounts] of [names of various group entities] for the Track Record Period. The financial statements were audited by [name of firm] in accordance with [the applicable auditing framework] issued by [the relevant standard setting body] ("Underlying Financial Statements")."

Case 3 - Where the Historical Financial Information in the accountants' report is prepared based on Previously Issued Financial Statements or other unaudited financial information, the following language may be used:

"The Historical Financial Information in this report was prepared based on Previously Issued Financial Statements [and management accounts] of [the Group/names of various group entities] for the Track Record Period. The Previously Issued Financial Statements were audited by [name of firm] in accordance with [the applicable auditing framework] issued by [the relevant standard setting body] ("Historical Financial Statements")"

The Historical Financial Information is presented in [HK dollars] and all values are rounded to the nearest thousand (HK\$'000) except when otherwise indicated.

[CONSOLIDATED/COMBINED] STATEMENTS OF PROFIT OR LOSS

[I - 4]

APPENDIX I

ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

[CONSOLIDATED/COMBINED] STATEMENTS OF COMPREHENSIVE INCOME

[I - 5]

APPENDIX I

ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

[CONSOLIDATED/COMBINED] STATEMENTS OF FINANCIAL POSITION

[I - 6]

APPENDIX I

ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

[CONSOLIDATED/COMBINED] STATEMENTS OF CHANGES IN EQUITY

[I - 7]

APPENDIX I

ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

[CONSOLIDATED/COMBINED] STATEMENTS OF CASH FLOWS

[I - 8]

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APPENDIX I
ACCOUNTANTS' REPORT ON
HISTORICAL FINANCIAL INFORMATION

NOTES TO THE FINANCIAL INFORMATION

X. Basis of preparation and presentation of Historical Financial Information

Provide details of the Company and its subsidiaries, group reorganisation and details of business combination under common control where applicable and basis of presentation and conventions applied (e.g.As a result, the Historical Financial Information of the Group has been prepared as if the present group structure had been in place throughout the Track Record Period).

Also, state the fact that the Historical Financial Information has been prepared in accordance with the accounting policies set out in Note Y below which conform with the applicable financial reporting framework.

Y. Significant accounting policies

Z. Other supporting notes as applicable (including information such as audited accounts which have been made up since the end of the last financial period reported on)

[I - Z]

Appendix 2 – Guidance on conventions commonly used in preparation of Historical Financial Information in Investment Circulars

Introduction

1. The purpose of this Appendix is to provide guidance concerning the conventions commonly applied for preparation and presentation of Historical Financial Information for inclusion in investment circulars.
2. The definitions of some of the special terms used in this appendix can be found in "Definitions" of this HKSIR.
3. The directors are responsible for preparing Historical Financial Information for inclusion in investment circulars which gives, for the purposes of the accountants' report, a true and fair view of the financial position of the relevant reporting entity at the end of each reporting period and of the financial performance and cash flows of that relevant reporting entity for each of the periods ending on those dates. In the preparation of the Historical Financial Information, the directors have regard to, and make appropriate disclosure of, accepted conventions which have been developed for the preparation and presentation of Historical Financial Information in investment circulars (including those relating to additional disclosures). These conventions have been developed to assist the directors to fulfil the criteria set out in the relevant regulations, present the information in an easily analysable form, and give a true and fair view for the purposes of the accountants' report.

The conventions are described below.

Basis of preparation and presentation of Historical Financial Information

4. Historical Financial Information for inclusion in an investment circular is most commonly prepared from Underlying Financial Statements without making adjustments. In certain circumstances, Historical Financial Information may be prepared from Previously Issued Financial Statements or from other unaudited financial information, in which case the Historical Financial Information may be presented after making such adjustments as considered necessary. For example, where a group reorganisation is to be completed after the reporting period or upon the adoption of a new or revised financial reporting framework in the final period presented which requires retrospective application, or correction of errors.
5. Information is added to the Historical Financial Information to identify:
 - a. the entity being reported on;
 - b. whether the Historical Financial Information is prepared based on Underlying Financial Statements or based on Previously Issued Financial Statements or from other unaudited financial information;
 - c. the auditor of the Historical Financial Statements throughout the period; and
 - d. whether any financial statements have been prepared for submission to the members for accounting periods later than the last period covered by the report.
6. The entity being reported on should be clearly defined. Accordingly, it may be necessary to give details of the group structure, significant changes during the period, and any reorganisation which has taken place since the date of the last audited financial statements. Where there has been a change in company name during the period or recent times, this should also be explained. If this information is complex and results in a paragraph which is disproportionately long in the context of the introduction section as a whole, it may be appropriate to include it as a separate paragraph elsewhere in the Historical Financial Information. The basis of preparation and presentation of Historical Financial Information

should also be stated in a prominent position where the Historical Financial Information has been prepared as if the present group structure had been in place throughout the track record period.

Adjustments to the Historical Financial Statements

7. The Listing Rules/GEM Rules require the preparation of a "statement of adjustments" by the reporting accountants showing, with reasons, how the audited Historical Financial Statements have been adjusted, to arrive at the figures underlying those included in the accountants' report. Although no particular format is required for the statement, it should be sufficiently detailed to reconcile the figures in the Historical Financial Statements with those in the accountants' report. The preparation of a statement of adjustments satisfies the requirements of paragraph 42 of Part III of the Third Schedule to the Companies (Winding up and Miscellaneous Provisions) Ordinance provided that the figures in the accountants' report are stated as being after making such adjustments as are considered appropriate.
8. Adjustments are made to the Historical Financial Statements in respect of material items in order to:
 - a. present the financial information for the track record period on the basis of consistent, acceptable and appropriately applied accounting policies and financial reporting framework (for example GAAP adjustments where there is a change in financial reporting framework, change in accounting policies and align the accounting policies of the acquiree with that of the acquirer in a business combination); and
 - b. correct material errors; and
 - c. eliminate intra-group balances and transactions where Historical Financial Information has been prepared on a combined basis for a business combination under common control (see paragraph 13 below).
9. Although retrospective adjustments may be made in respect of accounting policies, such adjustments should not be made for accounting estimates. Pursuant to Hong Kong Financial Reporting Standards, the effect of change in an accounting estimate in a later period should only be reflected in that period. Consideration should also be given to any additional disclosure which may be necessary by way of notes.
10. The Historical Financial Information is intended to provide a record of the business as operated and accounted for by the issuer's management. Therefore, it is not appropriate to make notional adjustments to recognise income or expenses or balances in order to make the "track record" more consistent with the entity's expected operations or structure following the transaction. Such adjustments would anticipate future events and are not consistent with the principle that the Historical Financial Information should record the events which actually occurred during the period of the Historical Financial Information.

Legal group not yet formed during the track record period

11. Where the group reorganisation takes place after the end of the track record period and involves a reporting entity acquiring equity interests in companies which, together with the reporting entity, are held under common control, the Historical Financial Information will normally be presented on a combined basis (with eliminations for inter-company transactions and balances).
12. If Historical Financial Information is not presented on a combined basis, separate historical financial information for entities accounting for substantially the whole of the track record period is likely to be required.

Carve outs

13. Where a business has formed part of a larger group ("overall group") during the track record period, but has not been accounted for separately, it may be desirable to present a separate track record (a "carve out") for that business ("carve out business"), derived from the records of the overall group. This approach may be preferable to the alternative approach of presenting the track record of the overall group, with appropriate disclosures of operations discontinuing or not acquired by the reporting entity. Circumstances where a carve out approach might be followed include flotation of businesses in a spin-off of divisions of the overall group.
14. When considering whether it is appropriate to present carve out financial information, the following factors will be relevant:
 - a. The extent to which the carve out business has been separately managed and financially controlled within the overall group; and
 - b. The extent to which it is practicable to identify the historical financial information attributable to the carve out business.
15. Where the omission of the results and assets of those operations not the subject of the transaction concerned would be misleading in the context of the circumstances in which the Historical Financial Information is to be presented, it will generally be appropriate to adopt the approach of presenting financial information on the overall group. Disclosures are made to assist the user to understand the contribution made by the operations not the subject of the transaction concerned. However, each case will need to be assessed on its own facts and circumstances.
16. In preparing the track record for the carve out business, the guidance in paragraphs 13 to 15 of this Appendix will be relevant. The objective will be, so far as possible, to present a historical record reflecting the events which actually occurred in the reporting period. Whilst it may be possible to identify certain transactions and balances which clearly relate to the carve out business, there will often be cases where the accounting records do not differentiate between items which relate to the carve out business and items which relate to the remainder of the overall group's business. Examples include management overheads, funding arrangements and shared assets. The guidance below discusses some of the elements typically encountered in preparing a carve out track record.
17. Clear and comprehensive disclosure in the notes to the Historical Financial Information will normally be needed in the basis of preparation and presentation in order for the nature of the Historical Financial Information to be clearly understood. The description would be expected to give a general indication of the process adopted for the preparation of the Historical Financial Information, and describe any factors which are particularly important to an understanding of the manner in which the information has been prepared.
18. The accounting policies to be adopted in the carve out accounts will need to reflect the requirements relating to the presentation of Historical Financial Information and may differ from those previously adopted. The question of functional currency should also be considered having regard to the economic environment of the carve out business, which may lead to the adoption of a different functional currency from that of the overall group.

Allocations

19. Where transactions or balances are not accounted for within the overall group in a manner which clearly attributes them to the carve out business, it will generally be desirable for a method for allocating the relevant amounts to the carve out business to be identified with a view to providing the fairest approximation to the amounts actually attributable to the carve out business. Any method should be adopted and applied on a rational and consistent basis. It will not, however, be appropriate to make allocations where there is no rational or consistent basis for doing so.

Bases for allocating transactions and balances

20. The appropriate basis for allocating group income and expenditure to a carve out business will vary according to the circumstances. It may, for example, be appropriate to allocate centrally accounted-for human resources costs on the basis of headcount (but account might be taken also of relative levels of staff turnover or other factors which indicate greater or less than average use in deciding whether the approach was in fact appropriate). The costs of a head office accounts department might be allocated by reference to the relevant sizes of the carve out business and remaining group. If other factors suggest that size is not a good indicator – if for example a disproportionate number of the accounting team is engaged in work for one part of the business and not the other – refinements to the approach might be considered appropriate.
21. It is important to recognise that the purpose of the allocation is to attribute an appropriate element of the overall group record to the carve out business. As a consequence, the position shown will frequently not be that which might have existed if the carve out business had been a stand-alone business. The position will be affected by the arrangements which apply to the group as a whole, which are a matter of historical fact and which it is not the purpose of the carve out financial information to alter. Frequently, disclosure will be made accompanying the financial information highlighting that the information presented may not be representative of the position which may prevail after the transaction.
22. Where certain third party receivables and payables of the overall group relates to the carve out business, it may be appropriate to allocate such items to the carve out business during the historical track record period. The basis for such an allocation may be by reference to the terms of the separation agreement. In other cases, the receivables and payables may be treated as part of the carve out business' balance with the overall group. The allocation of interest income/costs relating to the carve out business would be allocated in line with the way in which the related assets and liabilities have been allocated.

Relationship with the remaining group

23. In addition to transactions with "third parties", the results of the business will also include transactions with the part of the overall group which is not part of the carve out business (the "remaining group"). Hence, for example, sales which were previously regarded as "intra group" will need to be re-examined to determine whether they relate to entities within the carve out business or outside it.
24. The remaining group will normally also be regarded as a related party for the purposes of disclosing related party transactions, and it will normally be necessary to identify the extent of the relationships between the carve out business and the remaining group. Balances with the remaining group may have comprised elements of trading balances and short term or long term funding balances, which may or may not be based on contractual arrangements between the remaining group and the carve out business. Balances of a trading nature will normally be presented as an element of debtors or creditors. Balances which are considered to be funding in nature will normally be accounted for according to their general nature and depending on whether there are contractual arrangements governing such balances. Where the balance has the characteristics of financial liabilities, it will be presented in the manner in accordance with the relevant financial reporting framework as such. Where the balance does not meet the definition of financial liabilities under the relevant financial reporting framework, it will be classified as an equity component and be presented in the manner of equity, typically aggregated with the share capital and reserves of companies comprising the carve out business, as "parent company net investment" in the carve out business.
25. Balances with the remaining group may also contain elements of third party debtors or creditors which have been accounted for on behalf of the carve out business by the remaining group. Examples might be VAT costs, payroll taxes, certain customers or suppliers common to the carve out business and the remaining group, and external funding balances. Such elements of the balance with the remaining group would be expected to be reallocated to the appropriate third party captions.

26. Consolidation journals within the overall group accounting records will need to be analysed and, if appropriate, allocated to the carve out business.

Pension costs

27. Where employees of the carve out business participate in a pension scheme relating to the overall group, the track record of the carve out business would reflect the apportioned costs applicable to the carve out business. The accounting implications of any pension surplus/deficit attributable to the carve out business would also normally be expected to be reflected in the track record.

Acquisitions

28. It should be noted that acquisitions previously regarded as insignificant for separate disclosure in the overall group accounts may become sufficiently material to require separate disclosure in the context of the carve out business.

Disposals, non-recurring and exceptional items

29. Non-recurring and exceptional items are generally allocated to the carve out business and accounted for in accordance with the relevant financial reporting framework. The disposals of subsidiaries or a discontinuation of a material section of the business are accounted for and presented in accordance with the requirements in the relevant financial reporting framework.

Taxation

30. Tax charges are generally allocated to the carve out business to reflect the proportion of the overall group charge attributable to the carve out business. The approach will typically involve the aggregation of the tax charges actually incurred by the companies within the carve out business (and will therefore reflect the benefits, reliefs and charges arising as a result of membership of the overall group), after taking account of the tax effects of any adjustments. Where the information relating to the tax charges actually incurred is not available, the tax charge may be recomputed on the basis of the results of the carve out business. The tax rate applied is selected having regard to the tax position of the overall group and might thus include the impact of benefits, reliefs and charges arising as a result of membership of the overall group, to the extent that they would have been available to or imposed upon the carve out business.

Statements of cash flows

31. A statement of cash flows is prepared for the carve out business based on the carve out information. To the extent that the related balances are kept separate for the carve out business, cash flows relating to the carve out business may be specifically allocated to the carve out business. However, where the overall group operates a central cash account, it may not be appropriate to allocate cash flows relating to centrally settled costs to the carve out business.

Investments in subsidiaries, joint ventures and associates

32. The status of an entity in the overall group's accounts (that is, whether it is recorded as a subsidiary, joint venture or associate) may be the result of investments in the relevant entity by more than one group company. If not all the investing companies are to be part of the carve out business, this may mean that the status of the entity in the track record of the carve out business is different from that within the overall group. Additional or new disclosures may therefore be required.

Treatment of other items

33. Dividends are expected to be reflected in the track record of the carve out business where companies within the carve out business have paid dividends to members of the remaining group.
34. In relation to the disclosure of directors' remuneration, it is normal to present information for those individuals who are to be directors of the carve out business or who were employed by the overall group in a capacity equivalent to that of a director of the carve out business. The information disclosed will reflect the salaries and benefits paid in respect of services to the carve out business by any member of the overall group to those individuals (irrespective of whether the individuals were directors or not) during the period covered by the track record. No information is presented for proposed directors of the carve out business who were not employed by the overall group, or for individuals who served as directors of companies within the carve out group but who are not to be directors of the carve out group's holding company following the transaction.
35. A segmental analysis is prepared for the carve out business to reflect the segments which the carve out business has decided to adopt.

Other disclosure conventions

36. In order to meet the disclosure requirements of the Listing Rules/GEM Rules, it may be necessary for certain information which has not previously formed part of an entity's financial reporting information to be incorporated in the Historical Financial Information. For example, additional disclosures are required for emoluments of directors and supervisors and segmental information.
37. In addition, in certain situations the Listing Rules/GEM Rules do not require disclosures in respect of earnings per share, for example, where combined results are presented in accordance with paragraph 4.09 of the Listing Rules/paragraph 7.03(5) of the GEM Rules.

Disclosure of the conventions commonly adopted

38. Where a convention described in this Appendix is applied and its application has a material effect on the financial information or is necessary for an understanding of the basis of preparation and presentation of the Historical Financial Information, it is appropriate to describe the treatment adopted in the basis of preparation and presentation note in the Historical Financial Information.

Appendix 3 – Letter of consent

1. Where the reporting accountants are required to give consent to the inclusion of their public report, or references to their name, in an investment circular the reporting accountants should, before doing so, consider their public report in the form and context in which it appears, or is referred to, in the investment circular as a whole by:
 - a. comparing their public report together with the information being reported on to the other information in the rest of the investment circular and assessing whether the reporting accountants have any cause to believe that such other information is inconsistent with the information being reported on; and
 - b. assessing whether the reporting accountants have any cause to believe that any information in the investment circular which falls within the area of expertise of reporting accountants is misleading.

When the reporting accountants believe information in the investment circular is either inconsistent with their public report, together with the information being reported on, or misleading, the reporting accountants should withhold their consent until the reporting accountants are satisfied that their concerns are unwarranted or until the investment circular has been appropriately amended.

2. The reporting accountants should give consent to the inclusion of any report in an investment circular only when all relevant reports that it has agreed to make, in that investment circular, have been finalized.
3. A requirement for the reporting accountants to consent to the inclusion of their report in an investment circular arises from the Listing Rules/GEM Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance, where a statement or report attributed to an expert (including the reporting accountants) is included in a prospectus or circular issued by a listed company (or by a new applicant for listing). In all such cases there must be a statement that the report is included in the investment circular, in the form and context in which it is included, with the consent of the expert.
4. Whilst the reporting accountants' reporting responsibilities do not extend beyond their report, the process of giving consent involves an awareness of the overall process whereby the investment circular is prepared, and may entail discussions with those responsible for the investment circular as a whole in relation to its contents.
5. In deciding whether to give their consent, the reporting accountants should read the final version of the investment circular with a view to assessing the overall impression given by the investment circular, having regard to the purposes for which it has been prepared, as well as considering whether there are any inconsistencies between their report and the information in the rest of the investment circular. As part of this process the reporting accountants consider whether they have any cause to believe that any information in the investment circular which falls within the area of expertise of the reporting accountants may be misleading such that the reporting accountants would not wish to be associated with it.
6. In cases where an investment circular includes a reference to or reproduction of a report or opinion previously provided by the existing or predecessor auditors, the auditors should assess the appropriateness of issuing a consent letter and perform appropriate procedures such as subsequent event review before issuing the consent letter. They should also state clearly that the consent should not be construed as in any way updating or refreshing the previous issued auditors' report nor do the auditors accept responsibility for such report beyond that owed to those to whom the report was addressed by the auditors at the date of the issue.
7. Consent letters are dated the same date as the relevant investment circular. The Listing Rules/GEM Rules and the Companies (Winding Up and Miscellaneous Provisions) Ordinance require the consent letter to be made available for public inspection. The consent letter may be made available for public inspection in other cases where required by law or regulation. An example consent letter is set out below.

Example Consent Letter

This example is only illustrative and is not intended to be prescriptive as to the form or content of a consent letter.

(Letterhead of the reporting accountants)

(Date)

The Directors
XYZ Limited

Dear Sirs,

We refer to the [prospectus/circular]* dated [date] in connection with [the proposed initial listing of shares of XYZ Limited (the "Company") on the [Main Board/Growth Enterprise Market]* of The Stock Exchange of Hong Kong Limited (the "Prospectus") / the proposed [acquisition of [Name of the acquiree company] / disposal of [Name of the company being disposed] / the proposed debt offering]* by XYZ Limited (the "Company") (the "Circular")]*, a [copy / final proof]* of which is attached and initialled by us on its front cover for the purpose of identification.

Option 1: consent for inclusion of our reports and letters

We hereby consent to the inclusion of our accountants' report dated [date] on the historical financial information for the years ended [dates] and our accountants' report dated [date] on the pro forma financial information for the year ended [date] and our letter dated [date] on the profit forecast for the year ending dated [date] in the Prospectus, and the references to our name in the form and context in which they are included.

Option 2: consent for reproduction/ incorporation by reference of our previous report

We hereby consent to the [reproduction/incorporation by reference]* of our auditor's report dated [date] on the financial statements of the Company for the year ended [date of last audited balance sheet] in the Circular, and the references to our name in the form and context in which they are included.

It should be noted that we have not performed an assurance engagement in accordance with any assurance standard on the financial statements of the Company for any period subsequent to [date of last reported balance sheet]. This consent should not be construed as in any way updating or refreshing the aforementioned auditor's report nor do we accept responsibility for such report beyond that owed to those to whom the report was addressed by us at the date of its issue.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong

* to delete whichever is not appropriate and to describe the transaction of which an investment circular is issued.

HKSIR 400 (Revised)
Issued December 2016

Effective upon issue

*Hong Kong Standard on
Investment Circular Reporting Engagements 400 (Revised)*

Comfort Letters and Due Diligence Meetings



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

**HONG KONG STANDARD ON
INVESTMENT CIRCULAR REPORTING ENGAGEMENTS 400 (REVISED)**

COMFORT LETTERS AND DUE DILIGENCE MEETINGS

(Effective upon issue)

CONTENTS

	Paragraphs
Definitions	
Introduction and Scope	1-13
Comfort Letters	14-58
Due Diligence Meetings	59-68
Cross-Border and International Offerings	69
Effective Date	70
Appendix 1 Example Arrangement Letter Relating to the Issuance of a Comfort Letter and Taking Part in Due Diligence Meetings	
Appendix 2 Example Comfort Letter	
Appendix 3 Example Bring-down Letter	
Appendix 4 Example Issuer's Representation Letter on Subsequent Changes	
Appendix 5A Example Written Oral Due Diligence Acknowledgement	
Appendix 5B Example Master Agreement Regarding Due Diligence Meetings	
Appendix 6 Examples of Questions Commonly Asked in Due Diligence Meetings and Comments on the Reporting Accountants' Response	

Hong Kong Standard on Investment Circular Reporting Engagements (HKSIR) 400 (Revised), *Comfort Letters and Due Diligence Meetings* should be read in the context of the *Amended Preface to the Hong Kong Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* which sets out the application and authority of HKSIRs.

This HKSIR is based on the Listing Rules/GEM Rules, the Takeover Code and the Companies (Winding Up and Miscellaneous Provisions) Ordinance that were in effect as at 29 December 2016.

Definitions

The definitions used in this HKSIR are:

- a. *Bring-down letter:* An abbreviated letter updating the procedures described in a previously issued comfort letter.
- b. *GEM Rules:* Rules Governing the Listing of Securities on the Growth Enterprise Market
- c. *Investment circular:* A document issued by an entity relating to securities and for the information or investment decision of the holders of the entity's securities or other parties, including without limitation a listing document, a prospectus, a circular to shareholders or similar document.
- d. *Issuer:* As defined by the Listing Rules/GEM Rules, an issuer is any company or other legal person any of whose equity or debt securities are the subject of an application for listing or some of whose equity or debt securities are already listed.
- e. *Listing Rules:* Rules Governing the Listing of Securities on the Stock Exchange.
- f. *Prospectus:* A document which has the same meaning as in section 2(1) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance.
- g. *Reporting accountants:* Certified public accountants who are engaged to prepare public reports and letters for inclusion in, or private letters in connection with, an investment circular. Where the context requires, this term includes auditors where they are carrying out a role in connection with an investment circular, other than that of reporting as auditors on financial statements.
- h. *Securities:* Including but not limited to equity securities and debt securities as defined by the Listing Rules/GEM Rules.
- i. *Sponsor:* Any corporation or authorised financial institution, licensed or registered under applicable laws to advise on corporate finance matters and appointed as a sponsor by a new applicant under the Listing Rules / GEM Rules to assist the new applicant with its initial application for listing.
- j. *Stock Exchange:* The Stock Exchange of Hong Kong Limited.
- k. *Takeover Code:* The Codes on Takeovers and Mergers and Share Buy-backs issued by the Securities and Futures Commission.

Introduction and Scope

1. Reporting accountants issuing a comfort letter or taking part in a due diligence meeting with sponsors for an offering of securities in Hong Kong should follow the requirements of this HKSIR. Reporting accountants should also comply with HKSIR 100, *Investment Circulars and Reporting Accountants* when it is finalised and the requirements of the Code of Ethics for Professional Accountants issued by the Hong Kong Institute of Certified Public Accountants (the "Institute" or "HKICPA").
2. The Stock Exchange requires an applicant for listing to appoint a person acceptable to the Stock Exchange for the purpose to act as a "sponsor" to the issuer. The responsibilities of sponsors are set out in the Listing Rules/GEM Rules. These responsibilities, which include the requirement to conduct reasonable due diligence inquiries, are aimed broadly at ensuring that the issuer is suitable to be listed, that the directors understand their obligations both on initial listing and subsequently and that the investment circular complies with the Listing Rules/GEM Rules, is accurate and complete in all material respects and is not misleading.
3. In connection with the issuance of an investment circular by an issuer, reporting accountants may be requested by sponsors to perform procedures to provide comfort in respect of the integrity of certain information disclosed in the investment circular, or to comment on changes in selected financial statement items subsequent to the latest period reported on in the accountants' report. This HKSIR focuses on the issuance of a comfort letter and the participation in a due diligence meeting in these circumstances. Less frequently, these procedures may also be requested by sponsors in relation to other investment circulars prepared by issuers that are already listed. This HKSIR also applies to such letters and due diligence meetings.
4. In certain circumstances, reporting accountants may be engaged by sponsors and / or issuers to undertake a separate engagement to perform procedures other than those described in paragraph 3 above and which are outside the scope of a comfort letter as described by this HKSIR and illustrated in Appendix 2.
5. A due diligence investigation will be undertaken by sponsors to enable them to fulfil their obligations under the Listing Rules/GEM Rules. It is not usually practical for sponsors to carry out such an investigation entirely by themselves, and so they will often ask for professional assistance to provide them with comfort in certain areas outside of the historical financial information. Such assistance may be provided by reporting accountants in the form of a comfort letter and/or agreeing to answer questions at a due diligence meeting. Although the reporting accountants may provide such assistance, the responsibility for the completeness and accuracy of the investment circular, and its compliance with regulatory requirements remains that of the directors of the issuer. There is no statutory or Listing Rules/GEM Rules requirement for reporting accountants to provide a comfort letter covered by this HKSIR to sponsors.
6. Ordinarily, reporting accountants engaged by the issuer to prepare an accountants' report to be included in the investment circular will also be engaged by the issuer to assist sponsors in conducting their due diligence investigation of the issuer's affairs.
7. In providing a comfort letter and/or formulating a response to questions asked by sponsors, reporting accountants should bear in mind four principles underlying this HKSIR:
 - a. Only the sponsors can determine what is sufficient for a reasonable due diligence investigation in connection with their obligations under the Listing Rules/GEM Rules.

- b. The sponsors may rely on any written or oral¹ statement made by reporting accountants to add credibility to the subject matter of the statement; accordingly, any statement needs to be appropriately supported.
 - c. In order to make a statement that is appropriately supported, reporting accountants need to possess adequate knowledge of the subject matter, and to act with due care and an objective state of mind.
 - d. Reporting accountants can properly make a statement only if there is suitable evidence as a basis for reporting on the subject matter.
8. By providing a comfort letter or participating in a due diligence meeting, reporting accountants lend credibility to the information on which their comments are made. Hence it is important that the procedures to be undertaken relate only to matters to which their professional competence is relevant, and are performed in accordance with this HKSIR.
 9. The scope of work in an engagement under this HKSIR encompasses procedures in respect of selected financial information and in respect of subsequent changes in historical financial information included in the investment circular. This work should be planned and performed in accordance with the requirements of this HKSIR and with reference to the principles in other relevant standards issued by the HKICPA. In respect of selected financial and non-financial information, the reporting accountants report the procedures carried out and the findings obtained. Accordingly, in planning and performing this work the reporting accountants should refer to the principles in HKSRS 4400, *Engagements to Perform Agreed-Upon Procedures Regarding Financial Information*. In respect of subsequent changes in historical financial information, it is customary for reporting accountants to provide limited assurance². Accordingly, in planning and performing this work, the reporting accountants should refer to the principles in HKSAE 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* applicable to limited assurance engagements.
 10. Only sponsors can determine the information on which comfort is required and the procedures that will provide the required degree of comfort on that information. Consequently, it is important for reporting accountants, the issuer's management and sponsors to reach an early understanding and agreement as to the sponsors' requirements and the procedures the reporting accountants can properly perform. While responsibility for determining the appropriateness and sufficiency of the procedures required for the sponsors' purposes rests with the sponsors, reporting accountants have a professional responsibility not to be associated with information that they believe, or have reason to believe, is false or misleading.
 11. Reporting accountants, when issuing a comfort letter under this HKSIR may not issue any additional letters or reports under any other standard to sponsors that contain procedures expressly prohibited by this HKSIR.
 12. As explained in paragraphs 3 and 5 above, this HKSIR relates principally to an arrangement among the issuer, the sponsors and the reporting accountants in connection with the sponsors' due diligence responsibilities under the Listing Rules/GEM Rules. In certain circumstances, for example for large public offerings, reporting accountants may be requested to include other parties connected with the investment circular as addressees to the comfort letter. The comfort letter will be provided solely in the context of the due diligence procedures undertaken or procured to be undertaken by the addressees.

¹ Oral statements may only be relied upon on the basis that the reporting accountants shall have no liability in contract or in tort (including negligence) for such oral statements, other than for an oral statement known to be false or misleading when made and made with intent to deceive.

² In a limited assurance engagement, the reporting accountants express their conclusion in the negative form. Accordingly, limited assurance is also commonly referred to as negative assurance.

13. Independent accountants should also follow the guidance in this HKSIR when requested to issue a comfort letter or take part in a due diligence meeting with persons fulfilling a similar role to sponsors in connection with an offering of debt securities. For an offering of debt securities in reliance on Regulation S under the U.S. Securities Act of 1933, as amended ("Regulation S"), an example arrangement letter is included in example 4 of Appendix 1 and an example comfort letter for a Regulation S debt offering is included in example 2 of Appendix 2 to this HKSIR. The example bring down letter in Appendix 3 may also be used, suitably modified with respect to terms such as "sponsor" and "prospectus" and details of the offering.

Comfort Letters

Agreeing the Terms of the Engagement

14. In accordance with the principles in HKSA 210, *Agreeing the Terms of Audit Engagements*, reporting accountants when entering into an arrangement with the issuer and the sponsors to issue a comfort letter should agree the terms of the arrangement with the issuer and sponsors. The terms of the arrangement should be recorded in writing.
15. The terms of the arrangement to issue a comfort letter are recorded in an arrangement letter among the issuer, the sponsors, and the reporting accountants. The arrangement letter documents and confirms the reporting accountants' acceptance of the arrangement, and the scope and nature of the procedures to be performed. It also documents the responsibilities of the issuer and sponsors, and the extent of the reporting accountants' responsibilities to them. The issuer and sponsors being signatories to the letter, also confirm their acceptance of the terms and procedures described therein. The arrangement letter may also include other parties with due diligence obligations as addressees, as indicated in the example arrangement letter included in Appendix 1 to this HKSIR.
16. In any discussion of procedures, reporting accountants should not indicate in any manner that any representations will be able to be provided regarding the sufficiency of the procedures for the sponsors' purposes.
17. Typically, reporting accountants are asked to apply procedures to selected items of a financial nature included in the investment circular and to report the results or factual findings. Such procedures may be applied to, for example, changes in selected financial statement items subsequent to the date of the historical financial information ("subsequent changes"), and specific items of financial or other information included in the investment circular.
18. Reporting accountants may suggest a meeting with management and sponsors, or consultation by telephone or other means, to discuss and agree upon the detailed procedures to be followed in connection with the comfort letter. Only sponsors can determine what is sufficient for their purposes, however, reporting accountants can advise sponsors and management if, for any reason, it is not feasible to perform a requested procedure.
19. Reporting accountants will normally be willing to assist sponsors, but the assistance reporting accountants can provide by way of comfort letters is subject to limitations. One limitation is that reporting accountants can properly report in their professional capacity only on matters to which their professional expertise is substantially relevant. Another limitation is that procedures such as those contemplated in a comfort letter provide reporting accountants with a basis for reporting no more than a list of procedures performed and the findings of those procedures, or providing limited assurance on subsequent changes. Such limited procedures may bring to the sponsors' attention significant matters affecting the financial information, but they do not provide assurance that sponsors will learn of all information that they may wish to know. Because matters concerning the issuer's operations and financial results are the responsibility of management and may not be within the expertise of reporting accountants, they are best communicated to sponsors by management.
20. To ensure a mutual understanding of the procedures to be followed, it is desirable that reporting accountants, after discussing the comfort letter with management and sponsors, furnish both with a draft of the letter they expect to be able to issue, clearly identified as a draft.

Contents of a Comfort Letter

21. The detailed contents of a comfort letter will vary according to the nature of the information in the investment circular and the procedures agreed on by management, sponsors and reporting accountants.
22. At a minimum, a comfort letter should contain the following matters:
 - a. date;
 - b. reporting accountants' address;
 - c. addressees (e.g., the issuer and sponsors, as signatories to the arrangement letter);
 - d. identification of the purpose for which the procedures were performed;
 - e. a statement that the comfort letter is provided pursuant to the terms agreed upon with the addressees in the arrangement letter;
 - f. a statement that reporting accountants comply with the Code of Ethics for Professional Accountants issued by the Hong Kong Institute of Certified Public Accountants;
 - g. a statement that the engagement was performed in accordance with this HKSIR;
 - h. identification of specific financial or non-financial information to which the procedures have been applied;
 - i. a description of the procedures performed and the results or factual findings, including sufficient details of errors and exceptions found;
 - j. when reporting factual findings on agreed-upon-procedures, a statement that the procedures performed do not constitute an assurance engagement in accordance with standards within the Hong Kong Framework for Assurance Engagements and, as such, no assurance is expressed; and when limited assurance is given on subsequent changes, a statement that the procedures performed do not constitute an audit or review in accordance with Hong Kong Standards on Auditing or Hong Kong Standards on Review Engagements issued by the Hong Kong Institute of Certified Public Accountants;
 - k. a statement that the letter is restricted to the addressees of the letter and is to be used only in connection with the stated purpose of the letter; and
 - l. reporting accountants' signature.
23. Sponsors may request reporting accountants to provide a letter reporting the updating of the procedures described in a previously issued comfort letter. This is commonly referred to as a "bring-down" letter. Such a letter should normally be issued at or shortly before the closing date. If more than one letter is requested, it will be necessary to carry out the procedures and enquiries as of the cut-off date for each letter. Comments contained in an earlier letter may, where appropriate, be incorporated by reference in a subsequent letter.
24. An example of a comfort letter and a bring-down letter is included in Appendix 2 and Appendix 3 to this HKSIR.

25. Reporting accountants should have obtained knowledge of the internal controls, policies and procedures before reporting on:
- a. selected financial information;
 - b. non-financial information derived from accounting records; or
 - c. subsequent changes.
26. Reporting accountants may be requested by sponsors to perform procedures and report in the comfort letter on the above kind of information. Reporting accountants report on any such matters only after having obtained knowledge of the issuer's internal controls, policies and procedures as they relate to the preparation of the historical financial information or interim financial information. Knowledge of the issuer's internal controls includes knowledge of the control environment and control systems. Reporting accountants who have reported on an issuer's historical financial information ordinarily should have acquired sufficient knowledge of the issuer's internal controls, policies and procedures as they relate to the preparation of the historical financial information, and may have acquired such knowledge with respect to interim financial information. Reporting accountants who have performed a review in accordance with HKSRE 2400 (Revised), *Engagements to Review Historical Financial Statements* or HKSRE 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity* ordinarily should have acquired such knowledge with respect to the period(s) encompassed by the review. When reporting accountants have not acquired sufficient knowledge of the issuer's internal controls, policies and procedures, additional procedures are performed to obtain the knowledge that is considered necessary to carry out the engagement.
27. It would be inappropriate for reporting accountants to add credibility to information relating to a period without knowledge of the issuer's internal controls, policies and procedures. Reporting accountants should give comfort with respect to periods not covered by an assurance engagement, only after having obtained or updated knowledge of internal controls, policies and procedures for the periods.

Financial and Non-financial Information

28. When reporting accountants provide a comfort letter reporting procedures performed with respect to specific items of financial or quantitative non-financial information in the investment circular:
- a. the comfort letter should:
 - i. specifically identify the information;
 - ii. describe in detail the procedures performed at the request of sponsors; and
 - iii. describe the results of applying the procedures;
 - b. the comfort letter should state that:
 - i. the information has not been the subject of an audit or review engagement performed in accordance with Hong Kong Standards on Auditing or Hong Kong Standards on Review Engagements;
 - ii. reporting accountants make no representation regarding any matter of legal interpretation;
 - iii. reporting accountants make no representation about the adequacy for the sponsors' purposes of the procedures followed;
 - iv. reporting accountants make no representations about the adequacy or completeness of the disclosure; and

- v. the procedures would not necessarily disclose material misstatements or omissions or matters of significance with respect to the comments made; and
 - c. the comfort letter should avoid the use of terms of uncertain meaning (such as general review, limited review, reconcile, test or check) unless the procedures contemplated by these terms are described in the letter.
- 29. When reporting accountants perform procedures with respect to specific items of financial or non-financial information in the investment circular, it is important that the comfort letter be worded so as to minimise the possibility of misinterpretation.
- 30. To avoid ambiguity, it is important that the specific information commented on in the comfort letter be identified by reference to specific captions, tables, page numbers, paragraphs, or sentences. This information may be presented in any one of several ways. Descriptions of the procedures followed and the results obtained may be stated individually for each item of specific information commented on. Alternatively, if the procedures and findings are adequately described, some or all of the descriptions may be grouped or summarised, as long as the applicability of the descriptions to items in the investment circular is clear and the descriptions do not imply that the reporting accountants assume responsibility for the adequacy of the procedures. It may also be appropriate to present a matrix, listing the information and procedures applied to the specific items. Reporting accountants may also choose to identify procedures performed using specific symbols, and identify items to which those procedures have been applied directly on a copy of the applicable pages of the investment circular, which are attached to the comfort letter.
- 31. Reporting accountants should report on financial information contained in the investment circular only when:
 - a. it has been obtained from the issuer's historical financial information, financial statements or accounting records that are subject to the issuer's internal controls, policies and procedures;
 - b. it has been derived directly from such historical financial information, financial statements or accounting records by analysis or computation (for example, percentages or financial ratios); or
 - c. it has been the subject of a separate assurance engagement performed in accordance with Hong Kong Standards on Auditing and Assurance.
- 32. Reporting accountants can agree to report on a procedure such as comparing information contained in an investment circular to a schedule prepared by management, but only if the information in the schedule has been derived from accounting records subject to the issuer's internal controls, policies and procedures of which reporting accountants have knowledge. While responsibility for determining the appropriateness and sufficiency of the procedures required for the sponsors' purposes rests with the sponsors, reporting accountants have a professional responsibility not to be associated with information that they believe, or have reason to believe, is false or misleading.
- 33. Reporting accountants would generally not be in a position to comment on matters primarily involving the exercise of management's business judgment. For example, the causes of changes between periods in gross profit ratios or net income may not necessarily be within the reporting accountants' knowledge and expertise. It would be appropriate for reporting accountants to comment on management's explanation of such changes only if they have obtained the necessary information by performing a separate assurance engagement in accordance with Hong Kong Standards on Auditing and Assurance.
- 34. Reporting accountants should not comment on the appropriateness of allocations made to derive segment information, since the accountants' report would typically encompass that information. In some cases, reporting accountants may be requested to make a statement as to the acceptability of methods of analysis or allocation used in deriving figures not reported in

the segment disclosures in the historical financial information. Whether reporting accountants may properly comment on the methodology applied will depend on the extent to which such allocation is made in, or can be derived directly by analysis or computation from, the issuer's accounting records. In any event, such comments, if made, should make clear that such allocations are to a substantial extent arbitrary, that the method of allocation used is not the only acceptable one, and that other acceptable methods of allocation might produce substantially different results.

Further Guidance Relating to Non-financial Information

35. Reporting accountants should comment only on matters to which their professional competence is relevant.
36. Reporting accountants may be asked to comment on a wide variety of non-financial information, ranging from information taken directly from the historical financial information to information which has no connection with the accounting records of the issuer.
37. Reporting accountants should not comment on information subject to legal interpretation, such as beneficial share ownership or contracts, or on matters such as engineering data or mineral reserves.
38. Any procedures reporting accountants agree to perform on non-financial information would be such as to add a measure of credibility to the information being commented on. Reporting accountants should not comment on matters merely because they happen to be present and are capable of reading, counting, measuring, or performing other functions that might be applicable. In most such cases, sponsors can derive the same degree of comfort with respect to the information by performing the procedures themselves. For reporting accountants to comment in the comfort letter on the performance of such mechanical functions on non-financial information can only add a degree of comfort which is unwarranted and may prove to be misleading.
39. Reporting accountants should comment on quantitative information other than financial information only when:
 - a. it has been obtained from accounting records that are subject to internal controls, policies and procedures of which reporting accountants have knowledge; or
 - b. it has been the subject of a separate assurance engagement performed in accordance with Hong Kong Standards on Auditing and Assurance.
40. Examples of matters on which comment would generally be inappropriate are the proposed use of proceeds of the issue, area of facilities, number of employees (except as related to a given payroll period), backlog information, contingent liabilities, commitments and the classification of assets and liabilities as secured or unsecured.

Subsequent Changes

41. For the change period, the reporting accountants' comments should be solely based on the limited procedures actually performed with respect to that period and that fact should be made clear in the comfort letter.
42. Frequently, reporting accountants are requested to comment on subsequent changes in items in the historical financial information. These changes, which should be restricted to components reported in the historical financial information, may include, for example, changes in share capital, increases in long-term debt, or increases or decreases in other specified financial statement items during a period (the "change period") beginning subsequent to the date and period of the historical financial information, and ending at the cut-off date (being the date to which certain procedures described in the letter are to relate, for example a date three business days before the date of the letter). Reporting accountants may also be requested to address such matters as subsequent changes in the amount of net current assets or net

assets, net sales, and the total and per-share amounts of both profit before taxation and net profit. The comments on subsequent changes should be limited to reporting changes in amounts, and should avoid addressing the reasons for such changes.

43. There may be internal financial statements such as management accounts available for one or more accounting periods following the date of the historical financial information. As a basis for commenting on subsequent changes, reporting accountants should read any such available internal financial statements (including comparative period amounts), and enquire of management as to whether such statements are prepared, in all material respects, on a basis consistent with that of the historical financial information reported on by the reporting accountants in the investment circular.
44. For both the period(s) covered by the available internal financial statements referred to in paragraph 43, and for the period between the date of the historical financial information and the cut-off date, the reporting accountants' procedures with respect to such changes should include reading minutes of meetings of shareholders, directors, and various committees and making inquiries of management relating to the whole of the change period.
45. Usually there will be a period immediately preceding the cut-off date for which complete accounting information is not yet available. Reporting accountants should consider whether it is appropriate to provide comfort with respect to changes, increases or decreases that may have occurred during this period. Frequently it would be possible for the officials consulted to explain the changes in some items (for example, long-term debt and share capital), but not others (for example, revenues and net income). It would be inappropriate for reporting accountants to give comfort if the officials consulted were unable to respond fully to inquiries about changes that may have occurred.
46. Usually a change in an accounting policy made during the change period should be disclosed in the historical financial information. If such disclosure is not made in the historical financial information, reporting accountants should describe the change in the comfort letter.
47. In order that comments on subsequent changes be unambiguous and their determination be within the reporting accountants' expertise, reporting accountants should not refer to "adverse changes" or "material adverse changes", or make similar general statements about developments during the change period.
48. Reporting accountants are sometimes asked to state in the comfort letter that there have been "no adverse changes" or "no material adverse changes", or to make similar general statements about developments during the change period. In order to avoid subjective determinations that are susceptible of misinterpretation, it is important that reporting accountants do not agree to provide such a comment in the comfort letter.
49. When it has come to the reporting accountants' attention that a change, increase or decrease in a financial statement item on which the reporting accountants have been asked to comment has occurred during the change period, all such instances of increase or decrease in the requested items are stated in the comfort letter.
50. Alternatively, when agreed between the parties, if the change, increase or decrease, actual or contemplated, is disclosed in the investment circular, the phrase "except for changes, increases or decreases that the investment circular discloses have occurred or may occur" can be included in the letter. When using this alternative presentation, if the amount of the change, increase or decrease is not disclosed in the investment circular, reporting accountants should note the amount of such change, increase or decrease in the comfort letter.
51. In the context of a comfort letter, an increase (or a decrease) occurs when the amount of a financial statement item at the cut-off date or for the change period (as if financial statements had been prepared at that date and for that period) is more (or less) than the amount of the same item at a specified earlier date or for a specified earlier period.

52. The change period for which reporting accountants provide comfort ends on the cut-off date and ordinarily begins, for balance sheet items, immediately after the date of the last balance sheet in the historical financial information and, for income statement items, immediately after the latest period for which such items are presented in the document.
53. The comparison relates to the entire period and not to portions of that period. For example, a decrease during one part of the period may be offset by an equal or larger increase in another part of the period; however, because there was no decrease for the period as a whole, the comfort letter should not report the decrease occurring during one part of the period.
54. The arrangement letter usually specifies the dates as of which, and periods for which, data at the cut-off date and data for the change period are to be compared. For balance sheet items, the comparison date is normally that of the latest balance sheet included in the historical financial information (that is, immediately prior to the beginning of the change period). For income statement items, the comparison period or periods should ordinarily be the corresponding period of the preceding year, but might be instead or might include in addition any period of corresponding length chosen by sponsors.
55. Whether or not specified in the arrangement letter, the date and period used in comparison should be identified in the comfort letter in both draft and final form so that there is no misunderstanding about the matters being compared and so that sponsors can determine whether the comparison date and period are suitable for the sponsors' purposes.
56. Limited assurance may only be provided on subsequent changes when the financial statements from which the changes are being measured have been subject to an audit or a review in accordance with standards within the Hong Kong Framework for Assurance Engagements. In addition, depending on the particular circumstances applicable to the engagement, reporting accountants may consider it inappropriate to provide limited assurance on subsequent changes. Factors that might be relevant include (but should not be limited to); the period of time since the latest financial information was subject to an assurance engagement, the extent that complete accounting information is not yet available, the extent that the internal financial statements have been prepared on a basis substantially consistent with that of the historical financial information included in the investment circular, and whether factual findings only are being provided in a separate comfort letter for the same transaction (e.g., in respect of an overseas tranche of the offering where a comfort letter is also being issued under a different framework to this HKSIR). Where limited assurance is not provided reporting accountants may instead include in the comfort letter the procedures performed and the factual findings (i.e., in the manner of agreed-upon-procedures), provided that there is an adequate basis to do so.
57. Reporting accountants should obtain written representations from management with respect to changes subsequent to the date of the historical financial information.
58. An illustration of the representations from management is included in Appendix 4 to this HKSIR.

Due Diligence Meetings

59. As part of their due diligence investigation, sponsors frequently request one or more meetings ("due diligence meeting") with the issuer, reporting accountants, and legal counsel, at which the respective parties are requested to respond to specific questions raised by the sponsors. A due diligence meeting provides sponsors with an opportunity to obtain information required to fulfil their responsibilities. The questions asked may relate to the business of the issuer, information contained in the investment circular, the nature of the engagement undertaken by the reporting accountants, financial reporting, corporate governance, and other matters of interest to the sponsors.
60. Before attending a due diligence meeting with sponsors, reporting accountants should establish an understanding and agreement with the issuer's management and sponsors as to the basis on which the reporting accountants attend the due diligence meeting.

61. The terms of the arrangement for the reporting accountants' participation in the due diligence meeting are recorded in the arrangement letter among the issuer, the sponsors and the reporting accountants. However, in the event that the arrangement letter has not been executed prior to the due diligence meeting, the reporting accountants should obtain a written acknowledgement ("written acknowledgement") from the sponsors as to the basis on which the reporting accountants agree to attend the due diligence meeting before the signing of the arrangement letter. An example of such written acknowledgement is set out in Appendix 5A to this HKSIR.
62. Alternatively, the reporting accountants may enter into a master agreement with the sponsor to govern the basis on which the reporting accountants agree to attend the due diligence meeting prior to the execution of the arrangement letter, where the master agreement would apply to the due diligence meeting for each offering of securities for which the master agreement is in effect between the reporting accountants and the sponsor. An example of such master agreement is set out in Appendix 5B.
63. The terms under which the reporting accountants agree to participate in the due diligence meeting should be substantially the same regardless as to whether they are documented in the form of a written acknowledgement for a particular transaction, a master agreement between the reporting accountants and the sponsor, or in a fully executed arrangement letter.
64. Other matters to be agreed on might include management's consent to the reporting accountants' participation, management's undertaking to be represented in the due diligence meeting, and a waiver of normal confidentiality requirements, clearly specifying any limits on the reporting accountants' freedom to speak openly to the sponsors. For example, it should be established whether or not reporting accountants are free to discuss any management letters or internal control letters issued previously.
65. Reporting accountants should normally request, and sponsors may agree to provide in advance of the meeting, a list of the questions addressed to reporting accountants. Reporting accountants may wish to meet with the issuer's management to discuss the intended responses.
66. In a due diligence meeting, the reporting accountants' comments should be confined to matters properly relating to the engagement, including but not limited to:
- a. the nature and duration of the engagement as reporting accountants;
 - b. the reporting accountants' professional standing and experience;
 - c. the scope of the reporting engagements and other professional work in connection with the investment circular;
 - d. the accountants' report and other published reports issued by reporting accountants;
 - e. the reporting accountants' relationship with the issuer's management, directors and audit committee or equivalent;
 - f. the reporting accountants' ability to deliver reports, consents, comfort letters and any other letters or reports in connection with the investment circular; and
 - g. new developments in accounting, or pending accounting changes which have had or may have in future an effect on the issuer's financial statements.
67. Reporting accountants should confine comments in the meeting to matters properly relating to the engagement as reporting accountants and to work undertaken in connection with the investment circular. It is essential that comments be restricted to those that reporting accountants should be prepared to put in writing, and such a communication could be made only if it met the requirements in this HKSIR. Reporting accountants should not comment on

matters primarily involving discussion and analysis of the results of operations and financial position of the issuer, unless this is the subject of a separate assurance engagement performed by the reporting accountants. Reporting accountants should generally decline to answer questions such as questions about the aggressiveness of the issuer's accounting policies or income tax practice, or questions as to the adequacy of the issuer's insurance coverage (except in relation to the fairness of presentation of the historical financial information), or questions on forward-looking statements or on a business plan. Any questions on such matters are properly addressed to the issuer's management, and should be responded to by management.

68. Further guidance as to the manner in which reporting accountants might respond to requests in a due diligence meeting is provided in Appendix 6 to this HKSIR.

Cross-Border and International Offerings

69. When all or part of a securities offering for equity or debt is made overseas, reporting accountants may be requested to perform procedures and provide a separate comfort letter for the purposes of such offerings. In circumstances where there are no relevant standards governing the provision of a comfort letter in the overseas jurisdiction in which the offer is being made, reporting accountants refer to this HKSIR in establishing the scope of work to be performed and the form and content of the comfort letter to the sponsors (or persons fulfilling a similar role to sponsors in the relevant jurisdiction). A commonly encountered example of this is in the case of an international offering in conjunction with a Hong Kong public offering. In addition to providing a comfort letter under this HKSIR for the purposes of the Hong Kong public offering, the reporting accountants are typically requested to provide a separate comfort letter in respect of certain portions of the international offering. In such circumstances, with no requirement to follow any relevant jurisdictional standards, the reporting accountants refer to this HKSIR for the purposes of their comfort letter and due diligence meetings in relation to the relevant international tranche³ (excluding any tranche to be offered in the United States, which will typically be covered by a comfort letter in the style of PCAOB auditing standards (AS) 6101 or AICPA Auditing Standards Board's clarified auditing standard (AU-C 920), as applicable⁴); thereby aligning standards for both the Hong Kong and relevant international portions of the offering.⁵

Effective Date

70. This HKSIR is effective upon issue.

³ For example, to be offered in reliance on Regulation S under the U.S. Securities Act of 1933, as amended.

⁴ For example, to be offered in reliance on Rule 144A under the U.S. Securities Act of 1933, as amended.

⁵ In the context of paragraph 69, it is noted that comfort letters issued in connection with U.S. S.E.C. registered offerings of securities are normally issued following the guidance in PCAOB auditing standards 6101.

Appendix 1

Example Arrangement Letter Relating to the Issuance of a Comfort Letter and Taking Part in Due Diligence Meetings

This arrangement letter has been developed in consultation with stakeholders. The contents of the arrangement letter will vary according to the nature of the information in the investment circular, and the procedures agreed between reporting accountants, sponsors and the issuer.

The examples below refer to an "arrangement letter" which is the terminology more commonly adopted to describe an engagement letter issued in respect to a comfort letter and the taking part in due diligence meetings. They do not cover terms and conditions that relate to the Issuer and reporting accountants only in connection with the engagement, (for example fee arrangements) which would typically be covered by a separate engagement letter between the Issuer and the reporting accountants. Paragraphs 12-14 are appropriate for when limited assurance is provided in relation to subsequent changes. When reporting accountants report on factual findings rather than providing limited assurance the wording should be revised accordingly.

As further explained in paragraph 69 of this HKSIR, where there is also an international offering not covered by relevant jurisdictional standards, reporting accountants shall refer to the requirements of HKSIR 400 (Revised). In practice for such cases, separate comfort letters will often be issued for the international and Hong Kong public offerings (due to, for example, different cut-off dates being applied for each). Separate arrangement letters may also be prepared, or alternatively, where for example the same addressees are applicable for both offerings, a combined letter covering both offerings may be issued. The example arrangement letters below illustrate the following situations: Example 1: a Public Offering in Hong Kong, Example 2: an International Offering in reliance on Regulation S ("Regulation S"), and Example 3: a Public Offering in Hong Kong and an International Offering in reliance on Regulation S (combined approach). Example 4 illustrates a letter with respect to a Debt Offering in reliance on Regulation S.

Example 1 – Public Offering in Hong Kong (letterhead of reporting accountants)

[Date]

To: The Directors, XYZ Limited

Sponsors Limited

[Other Named Addressees and each of the Hong Kong underwriters as defined in the Hong Kong Underwriting Agreement dated [•] (the "Hong Kong Underwriters") that is an Addressee (as defined in Paragraph 3 below)⁶]

Dear Sirs,

Comfort Letter and Other Assistance Relating to the Proposed Listing of XYZ Limited (the "Issuer") on the [Main Board/Growth Enterprise Market] of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange")

Introduction

1. This arrangement letter sets out the scope and limitations of the work to be performed by us, being the reporting accountants of the Issuer, in connection with the issuance of a comfort letter and other assistance in respect of the above transaction, namely the proposed issue in Hong Kong of [•] (the "Issue") which will involve the preparation by the Issuer, and for which the Issuer will be solely responsible, of a prospectus in accordance with the [Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules")]/[Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Rules")] (the "Prospectus"). This arrangement letter is written in the context of the respective roles of the directors of the Issuer, Sponsors Limited (the "Sponsor") and the other Addressees (as defined below) and ourselves, in relation to the Issue. This arrangement letter does not apply to, and shall have no effect on, the rights and obligations of the Issuer, the Addressees or us in relation to the proposed international offering proposed to be conducted (the "International Offering") simultaneously with the Issue in Hong Kong, including any offering in the United States or elsewhere in the world or in connection with any actual or potential proceedings or disputes under U.S. federal or state securities laws relating to the International Offering.
2. The services we will provide in connection with the Issue (the "Services") will comprise:
 - provision of a comfort letter and where applicable, additional or updated comfort letter(s) (addressed to the directors of the Issuer and the Addressees) in connection with the Prospectus (the "Comfort Letter"), and
 - having meetings and discussions with the Addressees and their professional advisers and responding orally or otherwise to questions raised by them in connection with their due diligence regarding the Issue and the Prospectus (the "Other Assistance").

⁶ Named addressees of the arrangement letter and the comfort letter might include the sponsors, global coordinators, bookrunners, lead managers or other managing underwriters. These parties typically enter into the arrangement letter on behalf of the other underwriters of the Hong Kong public offering. It should not be necessary to name such other underwriters in the arrangement letter, since the prospectus and the Hong Kong underwriting agreement will clearly identify them. In certain circumstances, it may be appropriate to address a comfort letter to other parties, in which case such parties would also be appropriate parties to the arrangement letter. Typically, the sponsors and the lead and/or managing underwriters (however named in the underwriting agreement), would be the named addressees of the comfort letter.

Addressees

3. This arrangement letter is addressed to [the Sponsor(s), the Global Coordinator(s) and the Lead Manager(s)] (the "Named Addressees"), and to each of the Hong Kong Underwriters (as defined in the Prospectus) which has agreed (or after the date of this arrangement letter agrees) to participate in the Issue and which has, or prior to the issue of the Comfort Letter will have agreed to be bound by the terms of this arrangement letter, either by having validly authorised one or more of the signatories of this arrangement letter to enter into this arrangement letter on its behalf or validly ratified the entry into this arrangement letter on its behalf. The addressees of this arrangement letter (other than the Issuer) are collectively referred to herein as the "Addressees". By signing and accepting the terms of this arrangement letter, each Named Addressee confirms that it will use reasonable endeavours to obtain prima facie authority from each of the Hong Kong Underwriters authorising it to enter into this arrangement letter on the relevant underwriter's behalf. However, no Named Addressee makes any representation as to whether such prima facie authority actually confers the necessary authority.

Comfort Letter

4. The Comfort Letter and the Other Assistance will be provided to the Issuer for its information only, and to the Addressees solely in the context of the due diligence procedures being undertaken or procured to be undertaken by the Addressees in connection with the offering or sale of the securities in Hong Kong pursuant to the Prospectus, for the purpose of establishing or seeking to establish any defence in such context ("Due Diligence Defence") that the Addressees may wish to advance in any actual or potential court or arbitration proceedings, any investigation, hearing or other proceedings by any regulatory body, or any claim or dispute in respect of the Prospectus or otherwise in connection with the Issue. Accordingly, the Comfort Letter will be addressed to the Addressees for that purpose and neither the Comfort Letter nor the Other Assistance may be relied on by the Addressees for any other purpose. The Addressees are requesting the Comfort Letter in connection with the Issue as one of a number of procedures that the Addressees may use to establish the investigation that they have conducted.
5. Each Named Addressee confirms that it is aware of the due diligence guidance included in the [Listing Rules][GEM Rules], which will be followed.
6. For the avoidance of doubt and subject to the limitations or exclusions which are contained in or referred to in Paragraphs 7, 8, 24 and 30 of this arrangement letter, nothing in this arrangement letter shall preclude any Addressee from obtaining compensation from us in respect of any liability that it may incur to an investor arising out of the Issue or the contents of the Prospectus to the extent that such liability arises because the work undertaken pursuant to this arrangement letter or the Comfort Letter was undertaken negligently, in bad faith or as a result of our fraud or wilful default, it being understood that the foregoing is without prejudice to any defence of contributory negligence that may be available to us.
7. The Comfort Letter issued pursuant to this arrangement letter will be provided in accordance with the standards of the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and will not have been provided in accordance with any other professional standards, including but not limited to those of the American Institute of Certified Public Accountants. Accordingly, the Comfort Letter should not be relied upon in connection with any obligations or responsibilities that the Addressees may have under any legislation, regulations and/or rule of law other than those of Hong Kong and, in the event of any such use in any jurisdiction other than Hong Kong, we accept no responsibility in this regard.
8. Our work and findings shall not in any way constitute advice or recommendations (and we accept no liability in relation to any advice or recommendations) regarding any commercial decisions associated with the Issue, including, in particular, but without limitation, any which may be taken by any Addressee (or any person connected to any Addressee) in the capacity of investor or in providing investment advice to their clients.

9. The Comfort Letter will be provided solely for the Addressees' private information and should not be used for any purpose other than as set out in Paragraph 4. The Comfort Letter may not be referred to in any other document (except that references may be made to its existence in (i) contracts among any of the Issuer, the Addressees and ourselves and (ii) any communications in relation to the Issue among any of the Issuer, the Addressees, the underwriters of the International Offering and ourselves), nor made available to any other party (except that copies may be included in bibles of transaction documents memorialising the Issue).
10. Nothing in Paragraphs 4, 7 or 9 shall prevent the Addressees from disclosing this arrangement letter and the Comfort Letter to the Addressees' professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements the Addressees are complying with, and/or referring to and/or producing the Comfort Letter for any of the purposes set out in Paragraph 4. Except as permitted in the immediately preceding sentence, the Addressees shall first obtain our prior written consent for disclosure of the Comfort Letter to third parties.
11. Other than to those who have, or before the Comfort Letter is issued shall have, validly accepted this arrangement letter, we will not accept any responsibility to any party to whom the Comfort Letter is shown or into whose hands it may come.

Work and Procedures

12. Our work will be conducted in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the HKICPA. Specifically, our work will enable us to report factual findings in relation to selected financial information and to enable us to provide limited assurance on subsequent changes to historical financial information included in the Prospectus. [Procedures undertaken in connection with providing limited assurance on interim financial information will be conducted with reference to Hong Kong Standard on Review Engagements ("HKSRE") 2410.⁷] In other jurisdictions, standards and practices relevant to reporting accountants may be different and may not provide for reporting in the manner contemplated herein. Accordingly, the Comfort Letter should not be relied on as if it had been provided in accordance with the standards and practice of any professional body in any other jurisdiction.
13. Except as specifically stated in our comfort letter we have not performed an audit or review in respect of any financial information relating to the Issuer for any period subsequent to [date of last reported balance sheet] in accordance with Hong Kong Standards on Auditing ("HKSA") or [Hong Kong Standards on Review Engagements ("HKSREs")][HKSREs] issued by the HKICPA. The procedures we will use to perform the work set out in this arrangement letter including those in relation to subsequent changes will not constitute an audit or review made in accordance with HKSA or HKSREs issued by the HKICPA. Furthermore, they will not necessarily reveal matters of significance with respect to any material misstatement of the information referred to below.
14. We will only carry out those procedures expressly provided for in the Comfort Letter. Accordingly, we make no representations as to the sufficiency for the Addressees' purposes of the procedures provided for in the Comfort Letter and, therefore, our responsibility shall be limited to performing the work agreed upon in this arrangement letter and/or recorded in the Comfort Letter with due skill, care and attention. If we were to perform additional procedures or if we were to conduct an audit or review on the financial information of the Issuer in accordance with HKSA or HKSREs issued by the HKICPA, other matters might be reported to the Addressees in the Comfort Letter. The procedures to be performed by us in connection with the Comfort Letter should not be taken to supplant additional inquiries or procedures that may be appropriate in the performance of the Addressees' role under the proposed Issue.

⁷ In certain situations the reporting accountant may be required to perform a review of interim financial information in order to enable negative assurance to be provided on subsequent changes. This sentence should be included where such a review will be undertaken.

15. In relation to the contents of the Prospectus, we will address ourselves solely to such financial and other information in the Prospectus as is identified in the Comfort Letter and we will make no representations as to the adequacy of disclosure in the Prospectus or as to whether any material facts have been omitted by the Issuer. Further, we make no representations regarding any questions of legal interpretation.
16. The procedures that we plan to conduct have been determined by the Named Addressees and agreed by the parties to this arrangement letter, and will be recorded in the Comfort Letter. In carrying out our work pursuant to this arrangement letter, we will rely on the accuracy and completeness of certain information and explanations provided to us during the course of our work and will further request the directors of the Issuer to provide us with written representations concerning the accuracy and completeness of certain information and explanations provided to us for the purpose of our work. The Addressees will therefore understand that the procedures to be carried out by us are not designed to, and are not likely to, reveal fraud, withholding, concealment or misrepresentation by the management of the Issuer or its subsidiaries (the Issuer and its subsidiaries are collectively referred to herein as "the Group"). Notwithstanding the preceding three sentences, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), we will (and are hereby authorised by the Issuer to), as soon as practicable, notify the Issuer and the Named Addressees of this and discuss with them whether further procedures can be designed to seek to resolve the matter. Where such procedures are agreed between us, we will carry them out and amend the Comfort Letter accordingly.
17. Any opinions expressed on financial information outside the context of this arrangement letter were or are expressed solely in the context of the specific terms and conditions governing their preparation. In particular, the terms of this arrangement letter and any action pursuant to it shall be additional to and shall not detract from or change in any way any legal rights which any party to this arrangement letter may otherwise have acquired, whether in contract or in tort, in connection with our reporting on the historical financial information of the Issuer.
18. Save as may be expressly recorded in the Comfort Letter, we do not accept any responsibility for any other reports or letters beyond any responsibility that we owed to those to whom our reports or letters were addressed at the date of their issue.

Contents of the Comfort Letter

19. We will prepare and expect to issue the Comfort Letter addressed to the Issuer and the Addressees on the basis described above. Based upon our present understanding of the Addressees' requirements, we expect to be able to provide the Addressees with the Comfort Letter substantially in the form contained in the Appendix to this arrangement letter, setting out the procedures that we expect to carry out prior to issuing the Comfort Letter.⁸ Execution of this arrangement letter by the Named Addressees will constitute the Addressees' agreement to the scope and extent of such procedures.
20. We would be grateful if the Named Addressees would review the draft comfort letter that we expect to be able to provide the Addressees with and let us have any amendments the Named Addressees propose to the procedures as soon as possible, so that we can provide the Named Addressees with a revised draft for further consideration and approval.
21. Once an advanced draft of the Prospectus is available and the Named Addressees have identified, and we have agreed, the detailed financial information whose extraction or calculation the Named Addressees require to be covered in the Comfort Letter, we will provide the Named Addressees with a further revised draft of the Comfort Letter for approval of its scope prior to finalisation. We would expect to provide such a draft shortly before the draft Prospectus is first submitted to the Hong Kong Stock Exchange.

⁸ Where a draft comfort letter is not appended, briefly explain the procedures to be performed.

22. For the avoidance of doubt, we will not comment on, or otherwise give comfort in relation to, the Issuer's prospects or trading position or, save as expressly stated in the Comfort Letter, comment on or provide any opinion or other conclusion as to the current overall financial position of the Issuer.⁹

Drafts

23. During the course of the arrangement we may show drafts of, or report orally on, the Comfort Letter to the Named Addressees. In so far as any such draft or oral report is inconsistent with the subsequent final Comfort Letter, it will be deemed to be superseded by such final Comfort Letter.

Meetings

24. It will be necessary for us to receive copies of the draft Prospectus as it is produced and it may be necessary for us to attend meetings (including, but not limited to, meetings with the Issuer and its directors and/or employees and the Addressees and their employees, advisers or agents) at which the Prospectus is discussed and drafted or at which other related matters are discussed. We shall answer queries raised at such meetings on an informal basis but the Addressees should neither act nor refrain from acting on the basis of such informal answers unless and until they are confirmed in writing by us, whether in the final Comfort Letter or otherwise. In the absence of such written confirmation we shall have no liability to the Addressees in contract or in tort (including negligence) for our answers other than for an oral statement known to be false or misleading when made and made with intent to deceive.¹⁰ Subject to the above, nothing in this paragraph shall prejudice the Addressees' ability to rely on a non-recourse basis (meaning without any liability on our part except for oral statements known to be false or misleading when made and made with intent to deceive) on any comments we may provide orally, either in the context of establishing or seeking to establish any Due Diligence Defence in connection with any court, arbitral, regulatory or administrative proceedings or otherwise for the purposes of resolving either actual or potential proceedings, investigations, claims or disputes in respect of the Prospectus or otherwise in connection with the Issue.
25. Unless otherwise specifically agreed between the Issuer, the Named Addressees and us, we are authorised by the Issuer to speak to the Addressees and other professional advisers advising on the proposed Issue. In connection with our work pursuant to this arrangement letter, we may release to the Addressees and such other professional advisers any information relating to the Issuer or the Issue, whether confidential or not, and whether obtained during the course of our work or otherwise, and shall not be liable to the Issuer for any use subsequently made of that information. Our partners and staff working on this arrangement shall not be required, expected or deemed to have knowledge of any information known to other partners or staff of our firm but which is not known to those on this arrangement. In addition we shall not be required to make use of or disclose to the Addressees any information which is confidential to another client of our firm.

Timetable

26. Our work will depend upon receiving without undue delay full co-operation from all relevant officials of the Issuer and the Group and their disclosure to us of all accounting records of the Group and all other records and related information (including certain representations) we may need for the purposes of our work. We will endeavour to carry out our work in accordance with a timetable to be agreed between all parties that will satisfy the requirements of the Issue. We intend to provide the Issuer and the Addressees with (1) the Comfort Letter dated the date of the Prospectus relating to the Issue, (2) an additional or updating Comfort Letter on and dated the date of the closing of the Issue (to be delivered at closing of the Issue) and (3) where appropriate, an additional or updating Comfort Letter on and dated the over-allotment option

⁹ If specific procedures and appropriate terms (e.g. as to timing) are agreed between all parties, the reporting accountants may undertake additional work in accordance with HKSIR 400 (Revised).

¹⁰ If specific matters are discussed which the Addressees wish to be able to rely upon in accordance with this arrangement letter, the Issuer and the Named Addressees should arrange for them to be confirmed in writing by reporting accountants. If the reporting accountants are willing to confirm such matters in writing, further work and an extension of the terms of the arrangement are likely to be required.

closing date.¹¹ In connection with the delivery of any new or updating Comfort Letter, we will bring down our work to an agreed cut-off date. We will discuss with the Named Addressees any difficulties we encounter with this arrangement or with meeting the timetable as soon as any problems arise.

Applicable Law and Jurisdiction

27. This arrangement letter shall be governed by, and construed in accordance with, Hong Kong law. The Courts of Hong Kong shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning this arrangement letter, the Comfort Letter or any matter arising from them.

Staffing

28. [Name] will be the partner in charge of the services we will provide. [Name] will act as manager, with the help of [name], calling upon specialist staff as appropriate. We shall use reasonable endeavours to ensure that they are so involved but we may substitute those identified with others of equal or similar skills.

Fees and Certain Other Matters

29. Details of our fees and proposed billing arrangements have been set out in a separate agreement with the Issuer, who will bear the sole responsibility for the payment thereof. Such agreement also sets out certain other matters in relation to the respective rights and responsibilities of the Issuer and us in connection with the services to be performed by us in connection with the issuance of the Comfort Letter.

Other Terms and Conditions

30. In no circumstances shall we be liable, other than in the event of our fraud, bad faith or wilful default, for any loss or damage, of whatsoever nature, arising from information material to our work being withheld or concealed from us or misrepresented to us by the directors, employees, or agents of the Issuer or any other person of whom we may make inquiries unless, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), and we fail to notify the Issuer and the Named Addressees of such conclusion.
31. In the course of providing the Services we, [Accountants] Hong Kong, may, at our discretion, draw on the resource of other entities (whether or not incorporated) which carry on business under a name which includes all or part of the [Accountants] name or is otherwise within (or associated or connected with an entity) or is a correspondent firm of the worldwide network of [Accountants] ("other [Accountants] Firms") and their partners and employees as we deem appropriate, but provision of the Services will remain our responsibility alone.
32. The Addressees agree that the Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) against any other [Accountants] Firm or its personnel in respect of the Services. Any partner or employee of any other [Accountants] Firm who deals with the Addressees in connection with the Services does so solely on our behalf and we are liable for their activities as if they were in all respects our partners or staff.
33. The Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) arising out of or in connection with the Services against any of our employees personally, but this will not limit or exclude any liability we may have for their acts or omissions.

¹¹ In exceptional circumstances, it may also be appropriate to bring down the Comfort Letter to another date. Such arrangements should be discussed on a case-by-case basis.

34. The provisions of paragraphs 31 to 33 of this arrangement letter have been stipulated expressly for the benefit of our employees, and other [Accountants] Firms and their partners and employees (together "Beneficiaries"). The Addressees agree that, each of the Beneficiaries has the right to rely on paragraphs 31 to 34 of this arrangement letter as if they were parties to this arrangement letter. Each of the other [Accountants] Firms which agrees to assist in the provision of the Services does so in reliance on the protections afforded to it by paragraphs 31 to 34 of this arrangement letter, the benefit of which we formally accept on its behalf.

Prohibition on Assignment

35. No party may assign any of its rights in relation to this arrangement letter without the prior written consent of the others against whom the rights may be asserted, save that any Addressee and we may assign any of such rights, or such rights may pass by operation of law, to any successor to all or part of its business without such consent, provided that notice is given to the other signatories to this arrangement letter prior to any step being taken to enforce any rights hereunder.

Third Party Rights

36. Other than as set out in paragraph 34 above, this arrangement letter shall not create or give rise to, nor shall it be intended to create or give rise to, any third party rights and no third party shall have any right to enforce or rely on any provision of this arrangement letter. Save where otherwise stated in paragraph 34 above, the Contracts (Rights of Third Parties) Ordinance (Cap. 623 of the laws of Hong Kong) shall not under any circumstances apply to this arrangement letter. Any rights conferred on third parties by this arrangement letter exclude the right to assign, and their consent is not required to rescind or vary this arrangement letter. For the avoidance of doubt, this paragraph shall not apply to the Addressees or the successors referred to in paragraph 35 above.

Termination

37. Any party to this arrangement letter may at any time terminate this arrangement letter for whatever reason upon written notice to the other parties. In the case of termination by us, notice to the Issuer and the Named Addressees shall be sufficient notice.
38. Termination of this arrangement letter shall be without prejudice to any accrued rights of the parties to this arrangement letter. The provisions of this arrangement letter which expressly or by implication are intended to survive its termination or expiry will survive and continue to bind each party to this arrangement letter.

Internet communication

39. In connection with the Services the parties to this arrangement letter may from time to time communicate with each other electronically. However, the electronic transmission of information cannot be guaranteed to be secure or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use. Accordingly each party to this arrangement letter accepts the limitations of electronic communication, and will use reasonable procedures to check for the then most commonly known viruses before sending information electronically.

Miscellaneous

40. Other than as set out in paragraph 29 above, this arrangement letter and the Appendix to it constitute the entire agreement for the provision of the Services between us to the exclusion of any other express or implied terms, whether expressed orally or in writing, including any conditions, warranties and representations and shall supersede all previous proposals, understandings, contracts, letters of engagement, undertakings, agreements and correspondence regarding the Services. Save as provided in this arrangement letter, no change in the terms of our arrangement with respect to the Services will be effective unless agreed in writing and signed by all parties to this arrangement letter.

41. This arrangement letter may be executed in any number of counterparts, and by the parties on separate counterparts, but shall not be effective until each party has executed and delivered at least one counterpart. Each counterpart shall constitute an original of this arrangement letter, but all the counterparts shall together constitute one and the same instrument.
42. If any term or terms of this arrangement letter shall be held to be invalid, illegal or unenforceable, such term or terms shall be deemed not to form part of this arrangement letter without prejudice to the enforceability of the remaining terms of this arrangement letter, provided always that if any such deletion substantially affects or alters the commercial basis of this arrangement letter, the parties to this arrangement letter will negotiate in good faith to amend and modify them as may be necessary or desirable in the circumstances.
43. Please acknowledge acceptance of the terms of our arrangement by signing and returning the enclosed copy of this arrangement letter.
44. If the Issuer or the Addressees have any questions regarding this arrangement letter please do not hesitate to contact us.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Acknowledgement and Acceptance

We acknowledge receipt of this arrangement letter and agree with the terms of your arrangement set out therein:

Director
for and on behalf of
the board of XYZ Limited

Director
for and on behalf of
Sponsors Limited/ [Named Addressee]
(on its own behalf and on behalf of
each of the Hong Kong Underwriters)

Example 2 – International Offering in reliance on Regulation S

(letterhead of reporting accountants)

[Date]

To: The Directors, XYZ Limited

Lead Manager Limited

[Other Named Addressees and each of the other international underwriters as defined in the International Underwriting Agreement dated [•] (the "International Underwriters") that is an Addressee (as defined in Paragraph 3 below)¹²]

Dear Sirs,

Comfort Letter and Other Assistance Relating to the Proposed International Offering of the Ordinary Shares of XYZ Limited (the "Issuer") in reliance on Regulation S under the U.S. Securities Act of 1933, as amended (the "Securities Act")

Introduction

1. This arrangement letter sets out the scope and limitations of the work to be performed by us, being the reporting accountants of the Issuer, in connection with the issuance of a comfort letter and other assistance in respect of the above transaction, namely the proposed international offering outside of the United States of America in reliance on Regulation S under the Securities Act (the "Regulation S Offering") of [•] (the "Issue") which will involve the preparation by the Issuer, and for which the Issuer will be solely responsible, of an offering memorandum, that may be delivered to investors and utilised by them as a basis for their investment decisions (the "Offering Memorandum"). This arrangement letter is written in the context of the respective roles of the directors of the Issuer, Lead Manager Limited (the "Lead Manager") and the other Addressees (as defined below) and ourselves, in relation to the Issue. This arrangement letter does not apply to, and shall have no effect on, the rights and obligations of the Issuer, the Addressees or us in relation to the proposed public offering in Hong Kong, or any offering in the United States proposed to be conducted simultaneously with the Regulation S Offering.
2. The services we will provide in connection with the Issue (the "Services") will comprise:
 - provision of a comfort letter and where applicable, additional or updated comfort letter(s) (addressed to the directors of the Issuer and the Addressees) in connection with the Offering Memorandum (the "Comfort Letter"), and
 - having meetings and discussions with the Addressees and their professional advisers and responding orally or otherwise to questions raised by them in connection with their due diligence regarding the Issue and the Offering Memorandum (the "Other Assistance").

¹² Named addressees of the arrangement letter and the comfort letter might include the global coordinators, bookrunners, lead managers or other managing underwriters. These parties typically enter into the arrangement letter on behalf of the other underwriters of the Regulation S offering. It should not be necessary to name such other underwriters in the arrangement letter, since the offering memorandum and the international underwriting agreement will clearly identify them. In certain circumstances, it may be appropriate to address a comfort letter to other parties, in which case such parties would also be appropriate parties to the arrangement letter. Typically, the lead and/or managing underwriters (however named in the underwriting agreement), would be the named addressees of the comfort letter.

Addressees

3. This arrangement letter is addressed to [the Global Coordinator(s) and the Lead Manager(s)] (the "Named Addressees"), and to each of the other International Underwriters (as defined in the Offering Memorandum) which has agreed (or after the date of this arrangement letter agrees) to participate in the Issue and which has, or prior to the issue of the Comfort Letter will have agreed to be bound by the terms of this arrangement letter, either by having validly authorised one or more of the signatories of this arrangement letter to enter into this arrangement letter on its behalf or validly ratified the entry into this arrangement letter on its behalf. The addressees of this arrangement letter (other than the Issuer) are collectively referred to herein as the "Addressees". By signing and accepting the terms of this arrangement letter, each Named Addressee confirms that it will use reasonable endeavours to obtain prima facie authority from each of the other International Underwriters authorising it to enter into this arrangement letter as representative of the relevant underwriter. However, no Named Addressee makes any representation as to whether such prima facie authority actually confers the necessary authority.

Comfort Letter

4. The Comfort Letter and the Other Assistance will be provided to the Issuer for its information only, and to the Addressees solely in the context of the due diligence procedures being undertaken or procured to be undertaken by the Addressees in connection with the offering or sale of the securities outside of the United States under Regulation S pursuant to the Offering Memorandum, for the purpose of establishing or seeking to establish any defence in such context ("Due Diligence Defence") that the Addressees may wish to advance in any actual or potential court or arbitration proceedings, any investigation, hearing or other proceedings by any regulatory body, or any claim or dispute in respect of the Offering Memorandum or otherwise in connection with the Issue. Accordingly, the Comfort Letter will be addressed to the Addressees for that purpose and neither the Comfort Letter nor the Other Assistance may be relied on by the Addressees for any other purpose. The Addressees are requesting the Comfort Letter in connection with the Issue as one of a number of procedures that the Addressees may use to establish the investigation that they have conducted.
5. Each Named Addressee confirms that it is aware of the due diligence guidance [issued by *name of framework/organization, e.g., the International Capital Market Association*][included in the [Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited]/[Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited]], which will be followed.
6. For the avoidance of doubt and subject to the limitations or exclusions which are contained in or referred to in Paragraphs 7, 8, 24 and 30 of this arrangement letter, nothing in this arrangement letter shall preclude any Addressee from obtaining compensation from us in respect of any liability that it may incur to an investor arising out of the Issue or the contents of the Offering Memorandum to the extent that such liability arises because the work undertaken pursuant to this arrangement letter or the Comfort Letter was undertaken negligently, in bad faith or as a result of our fraud or wilful default, it being understood that the foregoing is without prejudice to any defence of contributory negligence that may be available to us.
7. The Comfort Letter issued pursuant to this arrangement letter will be provided in accordance with the standards of the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and will not have been provided in accordance with any other professional standards, including but not limited to those of the American Institute of Certified Public Accountants.
8. Our work and findings shall not in any way constitute advice or recommendations (and we accept no liability in relation to any advice or recommendations) regarding any commercial decisions associated with the Issue, including, in particular, but without limitation, any which may be taken by any Addressee (or any person connected to any Addressee) in the capacity of investor or in providing investment advice to their clients.
9. The Comfort Letter will be provided solely for the Addressees' private information and should not be used for any purpose other than as set out in Paragraph 4. The Comfort Letter may not be referred to in any other document (except that references may be made to its existence in (i)

contracts among any of the Issuer, the Addressees and ourselves and (ii) any communications in relation to the Issue among any of the Issuer, the Addressees, the Sponsors of the Hong Kong Public Offering, the International Underwriters and ourselves), nor made available to any other party (except that copies may be included in bibles of transaction documents memorialising the Issue).

10. Nothing in Paragraphs 4, 7 or 9 shall prevent the Addressees from disclosing this arrangement letter and the Comfort Letter to the Addressees' professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements the Addressees are complying with, and/or referring to and/or producing the Comfort Letter for any of the purposes set out in Paragraph 4. Except as permitted in the immediately preceding sentence, the Addressees shall first obtain our prior written consent for disclosure of the Comfort Letter to third parties.
11. Other than to those who have, or before the Comfort Letter is issued shall have, validly accepted this arrangement letter, we will not accept any responsibility to any party to whom the Comfort Letter is shown or into whose hands it may come.

Work and Procedures

12. Our work will be conducted in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the HKICPA. Specifically, our work will enable us to report factual findings in relation to selected financial information and to enable us to provide limited assurance on subsequent changes to historical financial information included in the Offering Memorandum. [Procedures undertaken in connection with providing limited assurance on interim financial information will be conducted with reference to Hong Kong Standard on Review Engagements ("HKSRE") 2410.¹³] In other jurisdictions, standards and practices relevant to reporting accountants may be different and may not provide for reporting in the manner contemplated herein. Accordingly, the Comfort Letter should not be relied on as if it had been provided in accordance with the standards and practice of any professional body in any other jurisdiction.
13. Except as specifically stated in our comfort letter we have not performed an audit or review in respect of any financial information relating to the Issuer for any period subsequent to [date of last reported balance sheet] in accordance with Hong Kong Standards on Auditing ("HKSA") or [Hong Kong Standards on Review Engagements ("HKSREs")][HKSREs] issued by the HKICPA. The procedures we will use to perform the work set out in this arrangement letter including those in relation to subsequent changes will not constitute an audit or review made in accordance with HKSA or HKSREs issued by the HKICPA. Furthermore, they will not necessarily reveal matters of significance with respect to any material misstatement of the information referred to below.
14. We will only carry out those procedures expressly provided for in the Comfort Letter. Accordingly, we make no representations as to the sufficiency for the Addressees' purposes of the procedures provided for in the Comfort Letter and, therefore, our responsibility shall be limited to performing the work agreed upon in this arrangement letter and/or recorded in the Comfort Letter with due skill, care and attention. If we were to perform additional procedures or if we were to conduct an audit or review on the financial information of the Issuer in accordance with HKSA or HKSREs issued by the HKICPA, other matters might be reported to the Addressees in the Comfort Letter. The procedures to be performed by us in connection with the Comfort Letter should not be taken to supplant additional inquiries or procedures that may be appropriate in the performance of the Addressees' role under the proposed Issue.

¹³ In certain situations the reporting accountant may be required to perform a review of interim financial information in order to enable negative assurance to be provided on subsequent changes. This sentence should be included where such a review will be undertaken.

15. In relation to the contents of the Offering Memorandum, we will address ourselves solely to such financial and other information in the Offering Memorandum as is identified in the Comfort Letter and we will make no representations as to the adequacy of disclosure in the Offering Memorandum or as to whether any material facts have been omitted by the Issuer. Further, we make no representations regarding any questions of legal interpretation.
16. The procedures that we plan to conduct have been determined by the Named Addressees and agreed by the parties to this arrangement letter, and will be recorded in the Comfort Letter. In carrying out our work pursuant to this arrangement letter, we will rely on the accuracy and completeness of certain information and explanations provided to us during the course of our work and will further request the directors of the Issuer to provide us with written representations concerning the accuracy and completeness of certain information and explanations provided to us for the purpose of our work. The Addressees will therefore understand that the procedures to be carried out by us are not designed to, and are not likely to, reveal fraud, withholding, concealment or misrepresentation by the management of the Issuer or its subsidiaries (the Issuer and its subsidiaries are collectively referred to herein as "the Group"). Notwithstanding the preceding three sentences, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), we will (and are hereby authorised by the Issuer to), as soon as practicable, notify the Issuer and the Named Addressees of this and discuss with them whether further procedures can be designed to seek to resolve the matter. Where such procedures are agreed between us, we will carry them out and amend the Comfort Letter accordingly.
17. Any opinions expressed on financial information outside the context of this arrangement letter were or are expressed solely in the context of the specific terms and conditions governing their preparation. In particular, the terms of this arrangement letter and any action pursuant to it shall be additional to and shall not detract from or change in any way any legal rights which any party to this arrangement letter may otherwise have acquired, whether in contract or in tort, in connection with our reporting on the historical financial information of the Issuer.
18. Save as may be expressly recorded in the Comfort Letter, we do not accept any responsibility for any other reports or letters beyond any responsibility that we owed to those to whom our reports or letters were addressed at the date of their issue.

Contents of the Comfort Letter

19. We will prepare and expect to issue the Comfort Letter addressed to the Issuer and the Addressees on the basis described above. Based upon our present understanding of the Addressees' requirements, we expect to be able to provide the Addressees with the Comfort Letter substantially in the form contained in the Appendix to this arrangement letter, setting out the procedures that we expect to carry out prior to issuing the Comfort Letter.¹⁴ Execution of this arrangement letter by the Named Addressees will constitute the Addressees' agreement to the scope and extent of such procedures.
20. We would be grateful if the Named Addressees would review the draft comfort letter that we expect to be able to provide the Addressees with and let us have any amendments the Named Addressees propose to the procedures as soon as possible, so that we can provide the Named Addressees with a revised draft for further consideration and approval.
21. Once an advanced draft of the Offering Memorandum is available and the Named Addressees have identified, and we have agreed, the detailed financial information whose extraction or calculation the Named Addressees require to be covered in the Comfort Letter, we will provide the Named Addressees with a further revised draft of the Comfort Letter for approval of its scope prior to finalisation.

¹⁴ Where a draft comfort letter is not appended, briefly explain the procedures to be performed.

22. For the avoidance of doubt, we will not comment on, or otherwise give comfort in relation to, the Issuer's prospects or trading position or, save as expressly stated in the Comfort Letter, comment on or provide any opinion or other conclusion as to the current overall financial position of the Issuer.¹⁵

Drafts

23. During the course of the arrangement we may show drafts of, or report orally on, the Comfort Letter to the Named Addressees. In so far as any such draft or oral report is inconsistent with the subsequent final Comfort Letter, it will be deemed to be superseded by such final Comfort Letter.

Meetings

24. It will be necessary for us to receive copies of the draft Offering Memorandum as it is produced and it may be necessary for us to attend meetings (including, but not limited to, meetings with the Issuer and its directors and/or employees and the Addressees and their employees, advisers or agents) at which the Offering Memorandum is discussed and drafted or at which other related matters are discussed. We shall answer queries raised at such meetings on an informal basis but the Addressees should neither act nor refrain from acting on the basis of such informal answers unless and until they are confirmed in writing by us, whether in the final Comfort Letter or otherwise. In the absence of such written confirmation we shall have no liability to the Addressees in contract or in tort (including negligence) for our answers other than for an oral statement known to be false or misleading when made and made with intent to deceive.¹⁶ Subject to the above, nothing in this paragraph shall prejudice the Addressees' ability to rely on a non-recourse basis (meaning without any liability on our part except for oral statements known to be false or misleading when made and made with intent to deceive) on any comments we may provide orally, either in the context of establishing or seeking to establish any Due Diligence Defence in connection with any court, arbitral, regulatory or administrative proceedings or otherwise for the purposes of resolving either actual or potential proceedings, investigations, claims or disputes in respect of the Offering Memorandum or otherwise in connection with the Issue.
25. Unless otherwise specifically agreed between the Issuer, the Named Addressees and us, we are authorised by the Issuer to speak to the Addressees and other professional advisers advising on the proposed Issue. In connection with our work pursuant to this arrangement letter, we may release to the Addressees and such other professional advisers any information relating to the Issuer or the Issue, whether confidential or not, and whether obtained during the course of our work or otherwise, and shall not be liable to the Issuer for any use subsequently made of that information. Our partners and staff working on this arrangement shall not be required, expected or deemed to have knowledge of any information known to other partners or staff of our firm but which is not known to those on this arrangement. In addition we shall not be required to make use of or disclose to the Addressees any information which is confidential to another client of our firm.

Timetable

26. Our work will depend upon receiving without undue delay full co-operation from all relevant officials of the Issuer and the Group and their disclosure to us of all accounting records of the Group and all other records and related information (including certain representations) we may need for the purposes of our work. We will endeavour to carry out our work in accordance with a timetable to be agreed between all parties that will satisfy the requirements of the Issue. We intend to provide the Issuer and the Addressees with (1) the Comfort Letter dated the date of the Offering Memorandum relating to the Issue, (2) an additional or updating Comfort Letter on and dated the date of the closing of the Issue (to be delivered at closing of the Issue) and (3) where appropriate, an additional or updating Comfort Letter on and dated the over-allotment

¹⁵ If specific procedures and appropriate terms (e.g. as to timing) are agreed between all parties, the reporting accountants may undertake additional work in accordance with HKSIR 400 (Revised).

¹⁶ If specific matters are discussed which the Addressees wish to be able to rely upon in accordance with this arrangement letter, the Issuer and the Named Addressees should arrange for them to be confirmed in writing by reporting accountants. If the reporting accountants are willing to confirm such matters in writing, further work and an extension of the terms of the arrangement are likely to be required.

option closing date.¹⁷ In connection with the delivery of any new or updating Comfort Letter, we will bring down our work to an agreed cut-off date. We will discuss with the Named Addressees any difficulties we encounter with this arrangement or with meeting the timetable as soon as any problems arise.

Applicable Law and Jurisdiction

27. This arrangement letter shall be governed by, and construed in accordance with, Hong Kong law. The Courts of Hong Kong shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning this arrangement letter, the Comfort Letter or any matter arising from them.

Staffing

28. [Name] will be the partner in charge of the services we will provide. [Name] will act as manager, with the help of [name], calling upon specialist staff as appropriate. We shall use reasonable endeavours to ensure that they are so involved but we may substitute those identified with others of equal or similar skills.

Fees and Certain Other Matters

29. Details of our fees and proposed billing arrangements have been set out in a separate agreement with the Issuer, who will bear the sole responsibility for the payment thereof. Such agreement also sets out certain other matters in relation to the respective rights and responsibilities of the Issuer and us in connection with the services to be performed by us in connection with the issuance of the Comfort Letter.

Other Terms and Conditions

30. In no circumstances shall we be liable, other than in the event of our fraud, bad faith or wilful default, for any loss or damage, of whatsoever nature, arising from information material to our work being withheld or concealed from us or misrepresented to us by the directors, employees, or agents of the Issuer or any other person of whom we may make inquiries unless, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), and we fail to notify the Issuer and the Named Addressees of such conclusion.
31. In the course of providing the Services we, [Accountants] Hong Kong, may, at our discretion, draw on the resource of other entities (whether or not incorporated) which carry on business under a name which includes all or part of the [Accountants] name or is otherwise within (or associated or connected with an entity) or is a correspondent firm of the worldwide network of [Accountants] ("other [Accountants] Firms") and their partners and employees as we deem appropriate, but provision of the Services will remain our responsibility alone.
32. The Addressees agree that the Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) against any other [Accountants] Firm or its personnel in respect of the Services. Any partner or employee of any other [Accountants] Firm who deals with the Addressees in connection with the Services does so solely on our behalf and we are liable for their activities as if they were in all respects our partners or staff.
33. The Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) arising out of or in connection with the Services against any of our employees personally, but this will not limit or exclude any liability we may have for their acts or omissions.

¹⁷ In exceptional circumstances, it may also be appropriate to bring down the Comfort Letter to another date. Such arrangements should be discussed on a case-by-case basis.

34. The provisions of paragraphs 31 to 33 of this arrangement letter have been stipulated expressly for the benefit of our employees, and other [Accountants] Firms and their partners and employees (together "Beneficiaries"). The Addressees agree that, each of the Beneficiaries has the right to rely on paragraphs 31 to 34 of this arrangement letter as if they were parties to this arrangement letter. Each of the other [Accountants] Firms which agrees to assist in the provision of the Services does so in reliance on the protections afforded to it by paragraphs 31 to 34 of this arrangement letter, the benefit of which we formally accept on its behalf.

Prohibition on Assignment

35. No party may assign any of its rights in relation to this arrangement letter without the prior written consent of the others against whom the rights may be asserted, save that any Addressee and we may assign any of such rights, or such rights may pass by operation of law, to any successor to all or part of its business without such consent, provided that notice is given to the other signatories to this arrangement letter prior to any step being taken to enforce any rights hereunder.

Third Party Rights

36. Other than as set out in paragraph 34 above, this arrangement letter shall not create or give rise to, nor shall it be intended to create or give rise to, any third party rights and no third party shall have any right to enforce or rely on any provision of this arrangement letter. Save where otherwise stated in paragraph 34 above, the Contracts (Rights of Third Parties) Ordinance (Cap. 623 of the laws of Hong Kong) shall not under any circumstances apply to this arrangement letter. Any rights conferred on third parties by this arrangement letter exclude the right to assign, and their consent is not required to rescind or vary this arrangement letter. For the avoidance of doubt, this paragraph shall not apply to the Addressees or the successors referred to in paragraph 35 above.

Termination

37. Any party to this arrangement letter may at any time terminate this arrangement letter for whatever reason upon written notice to the other parties. In the case of termination by us, notice to the Issuer and the Named Addressees shall be sufficient notice.
38. Termination of this arrangement letter shall be without prejudice to any accrued rights of the parties to this arrangement letter. The provisions of this arrangement letter which expressly or by implication are intended to survive its termination or expiry will survive and continue to bind each party to this arrangement letter.

Internet communication

39. In connection with the Services the parties to this arrangement letter may from time to time communicate with each other electronically. However, the electronic transmission of information cannot be guaranteed to be secure or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use. Accordingly each party to this arrangement letter accepts the limitations of electronic communication, and will use reasonable procedures to check for the then most commonly known viruses before sending information electronically.

Miscellaneous

40. Other than as set out in paragraph 29 above, this arrangement letter and the Appendix to it constitute the entire agreement for the provision of the Services between us to the exclusion of any other express or implied terms, whether expressed orally or in writing, including any conditions, warranties and representations and shall supersede all previous proposals, understandings, contracts, letters of engagement, undertakings, agreements and correspondence regarding the Services. Save as provided in this arrangement letter, no change in the terms of our arrangement with respect to the Services will be effective unless agreed in writing and signed by all parties to this arrangement letter.

41. This arrangement letter may be executed in any number of counterparts, and by the parties on separate counterparts, but shall not be effective until each party has executed and delivered at least one counterpart. Each counterpart shall constitute an original of this arrangement letter, but all the counterparts shall together constitute one and the same instrument.
42. If any term or terms of this arrangement letter shall be held to be invalid, illegal or unenforceable, such term or terms shall be deemed not to form part of this arrangement letter without prejudice to the enforceability of the remaining terms of this arrangement letter, provided always that if any such deletion substantially affects or alters the commercial basis of this arrangement letter, the parties to this arrangement letter will negotiate in good faith to amend and modify them as may be necessary or desirable in the circumstances.
43. Please acknowledge acceptance of the terms of our arrangement by signing and returning the enclosed copy of this arrangement letter.
44. If the Issuer or the Addressees have any questions regarding this arrangement letter please do not hesitate to contact us.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Acknowledgement and Acceptance

We acknowledge receipt of this arrangement letter and agree with the terms of your arrangement set out therein:

Director
for and on behalf of
the board of XYZ Limited

Director
for and on behalf of
Lead Manager Limited/ [Named Addressee]
(on its own behalf and as representative
of each of the other International Underwriters)

Example 3 – Public Offering in Hong Kong and an International Offering in reliance on Regulation S (combined approach)

(letterhead of reporting accountants)

[Date]

To: The Directors, XYZ Limited

Sponsors Limited/Lead Manager Limited

[Other Named Addressees and each of the Hong Kong and international underwriters as defined in the respective Hong Kong and International Underwriting Agreements dated [•] (the "Hong Kong and International Underwriters") that is an Addressee (as defined in Paragraph 3 below)¹⁸

Dear Sirs,

Comfort Letter and Other Assistance Relating to the Proposed Listing of XYZ Limited (the "Issuer") on the [Main Board/Growth Enterprise Market] of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange") and Relating to the Proposed Offering of the Ordinary Shares of the Issuer in reliance on Regulation S under the U.S. Securities Act of 1933, as amended ("the Securities Act")

Introduction

1. This arrangement letter sets out the scope and limitations of the work to be performed by us, being the reporting accountants of the Issuer, in connection with the issuance of a comfort letter[(s)] and other assistance in respect of the above transaction, namely the proposed issue in Hong Kong (the "Hong Kong Public Offering") and outside of the United States of America in reliance on Regulation S under the Securities Act (the "Regulation S Offering") of [•] (collectively the "Issue") which will involve the preparation by the Issuer, and for which the Issuer will be solely responsible, in the case of the Hong Kong Public Offering, of a prospectus in accordance with the [Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules")]/[Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Rules")] and in the case of the Regulation S Offering, of an offering memorandum, that may be delivered to investors and utilised by them as a basis for their investment decisions (hereinafter each referred to in this letter as the "Offering Document"). This arrangement letter is written in the context of the respective roles of the directors of the Issuer, Sponsors Limited / Lead Manager Limited and the other Addressees (as defined below) and ourselves, in relation to the Issue. This arrangement letter does not apply to, and shall have no effect on, the rights and obligations of the Issuer, the Addressees or us in relation to any offering in the United States proposed to be conducted simultaneously with the Issue.

¹⁸ Named addressees of the arrangement letter and the comfort letter might include the sponsors, global coordinators, bookrunners, lead managers or other managing underwriters. These parties typically enter into the arrangement letter on behalf of the other underwriters of the Hong Kong public and Regulation S offerings. It should not be necessary to name such other underwriters in the arrangement letter, since the offering document and the Hong Kong and international underwriting agreements will clearly identify them. In certain circumstances, it may be appropriate to address a comfort letter to other parties, in which case such parties would also be appropriate parties to the arrangement letter. Typically, the sponsors and the lead and/or managing underwriters (however named in the underwriting agreements), would be the named addressees of the comfort letter.

2. The services we will provide in connection with the Issue (the "Services") will comprise:
 - provision of a comfort letter and where applicable, additional or updated comfort letter(s) [for each of the Hong Kong Public Offering and the Regulation S Offering] (addressed to the directors of the Issuer and the Addressees) in connection with the Offering Document (the "Comfort Letter"), and
 - having meetings and discussions with the Addressees and their professional advisers and responding orally or otherwise to questions raised by them in connection with their due diligence regarding the Issue and the Offering Document (the "Other Assistance").

Addressees

3. This arrangement letter is addressed to [the Sponsor(s), the Global Coordinator(s) and the Lead Manager(s)] (the "Named Addressees"), and to each of the Hong Kong and the International Underwriters (as defined in the Offering Document) which has agreed (or after the date of this arrangement letter agrees) to participate in the Issue and which has, or prior to the issue of the Comfort Letter will have agreed to be bound by the terms of this arrangement letter, either by having validly authorised one or more of the signatories of this arrangement letter to enter into this arrangement letter on its behalf or validly ratified the entry into this arrangement letter on its behalf. The addressees of this arrangement letter (other than the Issuer) are collectively referred to herein as the "Addressees". By signing and accepting the terms of this arrangement letter, each Named Addressee confirms that it will use reasonable endeavours to obtain prima facie authority from each of the Hong Kong and the International Underwriters authorising it to enter into this arrangement letter as representative of the relevant underwriter. However, no Named Addressee makes any representation as to whether such prima facie authority actually confers the necessary authority.

Comfort Letter

4. The Comfort Letter and the Other Assistance will be provided to the Issuer for its information only, and to the Addressees solely in the context of the due diligence procedures being undertaken or procured to be undertaken by the Addressees in connection with the offering or sale of the securities in Hong Kong and outside of the United States under Regulation S pursuant to the Offering Document, for the purpose of establishing or seeking to establish any defence in such context ("Due Diligence Defence") that the Addressees may wish to advance in any actual or potential court or arbitration proceedings, any investigation, hearing or other proceedings by any regulatory body, or any claim or dispute in respect of the Offering Document or otherwise in connection with the Issue. Accordingly, the Comfort Letter will be addressed to the Addressees for that purpose and neither the Comfort Letter nor the Other Assistance may be relied on by the Addressees for any other purpose. The Addressees are requesting the Comfort Letter in connection with the Issue as one of a number of procedures that the Addressees may use to establish the investigation that they have conducted.
5. Each Named Addressee confirms that it is aware of the due diligence guidance included in the [Listing Rules][GEM Rules] [and in respect of the International Offering the due diligence guidance issued by [*name of framework/organization, e.g., the International Capital Market Association*]], which will be followed.
6. For the avoidance of doubt and subject to the limitations or exclusions which are contained in or referred to in Paragraphs 7, 8, 24 and 30 of this arrangement letter, nothing in this arrangement letter shall preclude any Addressee from obtaining compensation from us in respect of any liability that it may incur to an investor arising out of the Issue or the contents of the Offering Document to the extent that such liability arises because the work undertaken pursuant to this arrangement letter or the Comfort Letter was undertaken negligently, in bad faith or as a result of our fraud or wilful default, it being understood that the foregoing is without prejudice to any defence of contributory negligence that may be available to us.

7. The Comfort Letter issued pursuant to this arrangement letter will be provided in accordance with the standards of the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and will not have been provided in accordance with any other professional standards, including but not limited to those of the American Institute of Certified Public Accountants.
8. Our work and findings shall not in any way constitute advice or recommendations (and we accept no liability in relation to any advice or recommendations) regarding any commercial decisions associated with the Issue, including, in particular, but without limitation, any which may be taken by any Addressee (or any person connected to any Addressee) in the capacity of investor or in providing investment advice to their clients.
9. The Comfort Letter will be provided solely for the Addressees' private information and should not be used for any purpose other than as set out in Paragraph 4. The Comfort Letter may not be referred to in any other document (except that references may be made to its existence in (i) contracts among any of the Issuer, the Addressees and ourselves and (ii) any communications in relation to the Issue among any of the Issuer, the Addressees and ourselves), nor made available to any other party (except that copies may be included in bibles of transaction documents memorialising the Issue).
10. Nothing in Paragraphs 4, 7 or 9 shall prevent the Addressees from disclosing this arrangement letter and the Comfort Letter to the Addressees' professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements the Addressees are complying with, and/or referring to and/or producing the Comfort Letter for any of the purposes set out in Paragraph 4. Except as permitted in the immediately preceding sentence, the Addressees shall first obtain our prior written consent for disclosure of the Comfort Letter to third parties.
11. Other than to those who have, or before the Comfort Letter is issued shall have, validly accepted this arrangement letter, we will not accept any responsibility to any party to whom the Comfort Letter is shown or into whose hands it may come.

Work and Procedures

12. Our work will be conducted in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the HKICPA. Specifically, our work will enable us to report factual findings in relation to selected financial information and to enable us to provide limited assurance on subsequent changes to historical financial information included in the Offering Document. [Procedures undertaken in connection with providing limited assurance on interim financial information will be conducted with reference to Hong Kong Standard on Review Engagements ("HKSRE") 2410.¹⁹] In other jurisdictions, standards and practices relevant to reporting accountants may be different and may not provide for reporting in the manner contemplated herein. Accordingly, the Comfort Letter should not be relied on as if it had been provided in accordance with the standards and practice of any professional body in any other jurisdiction.
13. Except as specifically stated in our comfort letter we have not performed an audit or review in respect of any financial information relating to the Issuer for any period subsequent to [date of last reported balance sheet] in accordance with Hong Kong Standards on Auditing ("HKSA") or [Hong Kong Standards on Review Engagements ("HKSREs")][HKSREs] issued by the HKICPA. The procedures we will use to perform the work set out in this arrangement letter including those in relation to subsequent changes will not constitute an audit or review made in accordance with HKSA or HKSREs issued by the HKICPA. Furthermore, they will not necessarily reveal matters of significance with respect to any material misstatement of the information referred to below.

¹⁹ In certain situations the reporting accountant may be required to perform a review of interim financial information in order to enable negative assurance to be provided on subsequent changes. This sentence should be included where such a review will be undertaken.

14. We will only carry out those procedures expressly provided for in the Comfort Letter. Accordingly, we make no representations as to the sufficiency for the Addressees' purposes of the procedures provided for in the Comfort Letter and, therefore, our responsibility shall be limited to performing the work agreed upon in this arrangement letter and/or recorded in the Comfort Letter with due skill, care and attention. If we were to perform additional procedures or if we were to conduct an audit or review on the financial information of the Issuer in accordance with HKSA's or HKSREs issued by the HKICPA, other matters might be reported to the Addressees in the Comfort Letter. The procedures to be performed by us in connection with the Comfort Letter should not be taken to supplant additional inquiries or procedures that may be appropriate in the performance of the Addressees' role under the proposed Issue.
15. In relation to the contents of the Offering Document, we will address ourselves solely to such financial and other information in the Offering Document as is identified in the Comfort Letter and we will make no representations as to the adequacy of disclosure in the Offering Document or as to whether any material facts have been omitted by the Issuer. Further, we make no representations regarding any questions of legal interpretation.
16. The procedures that we plan to conduct have been determined by the Named Addressees and agreed by the parties to this arrangement letter, and will be recorded in the Comfort Letter. In carrying out our work pursuant to this arrangement letter, we will rely on the accuracy and completeness of certain information and explanations provided to us during the course of our work and will further request the directors of the Issuer to provide us with written representations concerning the accuracy and completeness of certain information and explanations provided to us for the purpose of our work. The Addressees will therefore understand that the procedures to be carried out by us are not designed to, and are not likely to, reveal fraud, withholding, concealment or misrepresentation by the management of the Issuer or its subsidiaries (the Issuer and its subsidiaries are collectively referred to herein as "the Group"). Notwithstanding the preceding three sentences, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), we will (and are hereby authorised by the Issuer to), as soon as practicable, notify the Issuer and the Named Addressees of this and discuss with them whether further procedures can be designed to seek to resolve the matter. Where such procedures are agreed between us, we will carry them out and amend the Comfort Letter accordingly.
17. Any opinions expressed on financial information outside the context of this arrangement letter were or are expressed solely in the context of the specific terms and conditions governing their preparation. In particular, the terms of this arrangement letter and any action pursuant to it shall be additional to and shall not detract from or change in any way any legal rights which any party to this arrangement letter may otherwise have acquired, whether in contract or in tort, in connection with our reporting on the historical financial information of the Issuer.
18. Save as may be expressly recorded in the Comfort Letter, we do not accept any responsibility for any other reports or letters beyond any responsibility that we owed to those to whom our reports or letters were addressed at the date of their issue.

Contents of the Comfort Letter

19. We will prepare and expect to issue the Comfort Letter addressed to the Issuer and the Addressees on the basis described above. Based upon our present understanding of the Addressees' requirements, we expect to be able to provide the Addressees with the Comfort Letter substantially in the form contained in the Appendix to this arrangement letter, setting out the procedures that we expect to carry out prior to issuing the Comfort Letter.²⁰ Execution of this arrangement letter by the Named Addressees will constitute the Addressees' agreement to the scope and extent of such procedures.

²⁰ Where a draft comfort letter is not appended, briefly explain the procedures to be performed.

20. We would be grateful if the Named Addressees would review the draft comfort letter that we expect to be able to provide the Addressees with and let us have any amendments the Named Addressees propose to the procedures as soon as possible, so that we can provide the Named Addressees with a revised draft for further consideration and approval.
21. Once an advanced draft of the Offering Document is available and the Named Addressees have identified, and we have agreed, the detailed financial information whose extraction or calculation the Named Addressees require to be covered in the Comfort Letter, we will provide the Named Addressees with a further revised draft of the Comfort Letter for approval of its scope prior to finalisation.
22. For the avoidance of doubt, we will not comment on, or otherwise give comfort in relation to, the Issuer's prospects or trading position or, save as expressly stated in the Comfort Letter, comment on or provide any opinion or other conclusion as to the current overall financial position of the Issuer.²¹

Drafts

23. During the course of the arrangement we may show drafts of, or report orally on, the Comfort Letter to the Named Addressees. In so far as any such draft or oral report is inconsistent with the subsequent final Comfort Letter, it will be deemed to be superseded by such final Comfort Letter.

Meetings

24. It will be necessary for us to receive copies of the draft Offering Document as it is produced and it may be necessary for us to attend meetings (including, but not limited to, meetings with the Issuer and its directors and/or employees and the Addressees and their employees, advisers or agents) at which the Offering Document(s) is discussed and drafted or at which other related matters are discussed. We shall answer queries raised at such meetings on an informal basis but the Addressees should neither act nor refrain from acting on the basis of such informal answers unless and until they are confirmed in writing by us, whether in the final Comfort Letter(s) or otherwise. In the absence of such written confirmation we shall have no liability to the Addressees in contract or in tort (including negligence) for our answers other than for an oral statement known to be false or misleading when made and made with intent to deceive.²² Subject to the above, nothing in this paragraph shall prejudice the Addressees' ability to rely on a non-recourse basis (meaning without any liability on our part except for oral statements known to be false or misleading when made and made with intent to deceive) on any comments we may provide orally, either in the context of establishing or seeking to establish any Due Diligence Defence in connection with any court, arbitral, regulatory or administrative proceedings or otherwise for the purposes of resolving either actual or potential proceedings, investigations, claims or disputes in respect of the Offering Document or otherwise in connection with the Issue.
25. Unless otherwise specifically agreed between the Issuer, the Named Addressees and us, we are authorised by the Issuer to speak to the Addressees and other professional advisers advising on the proposed Issue. In connection with our work pursuant to this arrangement letter, we may release to the Addressees and such other professional advisers any information relating to the Issuer or the Issue, whether confidential or not, and whether obtained during the course of our work or otherwise, and shall not be liable to the Issuer for any use subsequently made of that information. Our partners and staff working on this arrangement shall not be required, expected or deemed to have knowledge of any information known to other partners or staff of our firm but which is not known to those on this arrangement. In addition we shall not be required to make use of or disclose to the Addressees any information which is confidential to another client of our firm.

²¹ If specific procedures and appropriate terms (e.g. as to timing) are agreed between all parties, the reporting accountants may undertake additional work in accordance with HKSIR 400 (Revised).

²² If specific matters are discussed which the Addressees wish to be able to rely upon in accordance with this arrangement letter, the Issuer and the Named Addressees should arrange for them to be confirmed in writing by reporting accountants. If the reporting accountants are willing to confirm such matters in writing, further work and an extension of the terms of the arrangement are likely to be required.

Timetable

26. Our work will depend upon receiving without undue delay full co-operation from all relevant officials of the Issuer and the Group and their disclosure to us of all accounting records of the Group and all other records and related information (including certain representations) we may need for the purposes of our work. We will endeavour to carry out our work in accordance with a timetable to be agreed between all parties that will satisfy the requirements of the Issue. We intend to provide the Issuer and the Addressees with (1) Comfort Letters dated the date of the Offering Documents relating to the Issues, (2) additional or updating Comfort Letters on and dated the date of the closing of the Issues (to be delivered at closing of each Issue) and (3) where appropriate, an additional or updating Comfort Letter on and dated the over-allotment option closing date of the Regulation S Offering.²³ In connection with the delivery of any new or updating Comfort Letter, we will bring down our work to an agreed cut-off date. We will discuss with the Named Addressees any difficulties we encounter with this arrangement or with meeting the timetable as soon as any problems arise.

Applicable Law and Jurisdiction

27. This arrangement letter shall be governed by, and construed in accordance with, Hong Kong law. The Courts of Hong Kong shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning this arrangement letter, the Comfort Letter or any matter arising from them.

Staffing

28. [Name] will be the partner in charge of the services we will provide. [Name] will act as manager, with the help of [name], calling upon specialist staff as appropriate. We shall use reasonable endeavours to ensure that they are so involved but we may substitute those identified with others of equal or similar skills.

Fees and Certain Other Matters

29. Details of our fees and proposed billing arrangements have been set out in a separate agreement with the Issuer, who will bear the sole responsibility for the payment thereof. Such agreement also sets out certain other matters in relation to the respective rights and responsibilities of the Issuer and us in connection with the services to be performed by us in connection with the issuance of the Comfort Letter.

Other Terms and Conditions

30. In no circumstances shall we be liable, other than in the event of our fraud, bad faith or wilful default, for any loss or damage, of whatsoever nature, arising from information material to our work being withheld or concealed from us or misrepresented to us by the directors, employees, or agents of the Issuer or any other person of whom we may make inquiries unless, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), and we fail to notify the Issuer and the Named Addressees of such conclusion.
31. In the course of providing the Services we, [Accountants] Hong Kong, may, at our discretion, draw on the resource of other entities (whether or not incorporated) which carry on business under a name which includes all or part of the [Accountants] name or is otherwise within (or associated or connected with an entity) or is a correspondent firm of the worldwide network of [Accountants] ("other [Accountants] Firms") and their partners and employees as we deem appropriate, but provision of the Services will remain our responsibility alone.

²³ In exceptional circumstances, it may also be appropriate to bring down the Comfort Letter to another date. Such arrangements should be discussed on a case-by-case basis.

32. The Addressees agree that the Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) against any other [Accountants] Firm or its personnel in respect of the Services. Any partner or employee of any other [Accountants] Firm who deals with the Addressees in connection with the Services does so solely on our behalf and we are liable for their activities as if they were in all respects our partners or staff.
33. The Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) arising out of or in connection with the Services against any of our employees personally, but this will not limit or exclude any liability we may have for their acts or omissions.
34. The provisions of paragraphs 31 to 33 of this arrangement letter have been stipulated expressly for the benefit of our employees, and other [Accountants] Firms and their partners and employees (together "Beneficiaries"). The Addressees agree that, each of the Beneficiaries has the right to rely on paragraphs 31 to 34 of this arrangement letter as if they were parties to this arrangement letter. Each of the other [Accountants] Firms which agrees to assist in the provision of the Services does so in reliance on the protections afforded to it by paragraphs 31 to 34 of this arrangement letter, the benefit of which we formally accept on its behalf.

Prohibition on Assignment

35. No party may assign any of its rights in relation to this arrangement letter without the prior written consent of the others against whom the rights may be asserted, save that any Addressee and we may assign any of such rights, or such rights may pass by operation of law, to any successor to all or part of its business without such consent, provided that notice is given to the other signatories to this arrangement letter prior to any step being taken to enforce any rights hereunder.

Third Party Rights

36. Other than as set out in paragraph 34 above, this arrangement letter shall not create or give rise to, nor shall it be intended to create or give rise to, any third party rights and no third party shall have any right to enforce or rely on any provision of this arrangement letter. Save where otherwise stated in paragraph 34 above, the Contracts (Rights of Third Parties) Ordinance (Cap. 623 of the laws of Hong Kong) shall not under any circumstances apply to this arrangement letter. Any rights conferred on third parties by this arrangement letter exclude the right to assign, and their consent is not required to rescind or vary this arrangement letter. For the avoidance of doubt, this paragraph shall not apply to the Addressees or the successors referred to in paragraph 35 above.

Termination

37. Any party to this arrangement letter may at any time terminate this arrangement letter for whatever reason upon written notice to the other parties. In the case of termination by us, notice to the Issuer and the Named Addressees shall be sufficient notice.
38. Termination of this arrangement letter shall be without prejudice to any accrued rights of the parties to this arrangement letter. The provisions of this arrangement letter which expressly or by implication are intended to survive its termination or expiry will survive and continue to bind each party to this arrangement letter.

Internet communication

39. In connection with the Services the parties to this arrangement letter may from time to time communicate with each other electronically. However, the electronic transmission of information cannot be guaranteed to be secure or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use. Accordingly each party to this arrangement letter accepts the limitations of electronic communication, and will use reasonable procedures to check for the then most commonly known viruses before sending information electronically.

Miscellaneous

40. Other than as set out in paragraph 29 above, this arrangement letter and the Appendix to it constitute the entire agreement for the provision of the Services between us to the exclusion of any other express or implied terms, whether expressed orally or in writing, including any conditions, warranties and representations and shall supersede all previous proposals, understandings, contracts, letters of engagement, undertakings, agreements and correspondence regarding the Services. Save as provided in this arrangement letter, no change in the terms of our arrangement with respect to the Services will be effective unless agreed in writing and signed by all parties to this arrangement letter.
41. This arrangement letter may be executed in any number of counterparts, and by the parties on separate counterparts, but shall not be effective until each party has executed and delivered at least one counterpart. Each counterpart shall constitute an original of this arrangement letter, but all the counterparts shall together constitute one and the same instrument.
42. If any term or terms of this arrangement letter shall be held to be invalid, illegal or unenforceable, such term or terms shall be deemed not to form part of this arrangement letter without prejudice to the enforceability of the remaining terms of this arrangement letter, provided always that if any such deletion substantially affects or alters the commercial basis of this arrangement letter, the parties to this arrangement letter will negotiate in good faith to amend and modify them as may be necessary or desirable in the circumstances.
43. Please acknowledge acceptance of the terms of our arrangement by signing and returning the enclosed copy of this arrangement letter.
44. If the Issuer or the Addressees have any questions regarding this arrangement letter please do not hesitate to contact us.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Acknowledgement and Acceptance

We acknowledge receipt of this arrangement letter and agree with the terms of your arrangement set out therein:

Director
for and on behalf of
the board of XYZ Limited

Director
for and on behalf of
Sponsors Limited/Lead Manager Limited
[Named Addressee]
(on its own behalf and as representative of
each of the Hong Kong and other International
Underwriters)

Example 4 – Debt Offering in reliance on Regulation S

(letterhead of Independent accountants)

[Date]

To: The Directors, XYZ Limited [and ABC Limited]

Lead Manager Limited

[Other Named Addressees and each of the other joint lead managers and managers as defined in the Subscription Agreement dated [•] (the "Managers") that is an Addressee (as defined in Paragraph 3 below)²⁴]

Dear Sirs,

Comfort Letter and Other Assistance Relating to the Proposed Offering of [x] (the "Notes") of XYZ Limited (the "Company") [guaranteed by ABC Limited (the "Guarantor")] in reliance on Regulation S under the U.S. Securities Act of 1933, as amended (the "Securities Act")

Introduction

1. This arrangement letter sets out the scope and limitations of the work to be performed by us, in connection with the issuance of a comfort letter and other assistance in respect of the above transaction, namely the proposed international offering outside of the United States of America in reliance on Regulation S under the Securities Act (the "Regulation S Offering") of the Notes (the "Issue") which will involve the preparation by the Company, and for which the Company will be solely responsible, of an offering circular, [in accordance with the Listing Rules of [relevant] Stock Exchange or other Listing Authority] (the "Offering Circular"). This arrangement letter is written in the context of the respective roles of the directors of the Company,[the directors of the Guarantor,] Lead Manager Limited (the "Lead Manager") and the other Addressees (as defined below) and ourselves, in relation to the Issue. This arrangement letter does not apply to, and shall have no effect on, the rights and obligations of the Company, [the Guarantor,] the Addressees or us in relation to any offering in the United States not otherwise pursuant to the Regulation S Offering.
2. The services we will provide in connection with the Issue (the "Services") will comprise:
 - provision of a comfort letter and where applicable, additional or updated comfort letter(s) (addressed to the directors of the Company,[the directors of the Guarantor] and the Addressees) in connection with the Offering Circular (the "Comfort Letter"), and
 - having meetings and discussions with the Addressees and their professional advisers and responding orally or otherwise to questions raised by them in connection with their due diligence regarding the Issue and the Offering Circular (the "Other Assistance").

²⁴ Named addressees of the arrangement letter and the comfort letter might include the global coordinators, bookrunners, lead managers or other underwriters. These parties typically enter into the arrangement letter on behalf of the other underwriters of the Regulation S offering. It should not be necessary to name such other underwriters in the arrangement letter, since the offering circular and the subscription agreement will clearly identify them. In certain circumstances, it may be appropriate to address a comfort letter to other parties, in which case such parties would also be appropriate parties to the arrangement letter. Typically, the lead and/or other underwriters (however named in the subscription agreement), would be the named addressees of the comfort letter.

Addressees

3. This arrangement letter is addressed to [the Global Coordinator(s) and the Lead Manager(s)] (the "Named Addressees"), and to each of the other Managers (as defined in the Offering Circular) which has agreed (or after the date of this arrangement letter agrees) to participate in the Issue and which has, or prior to the issue of the Comfort Letter will have agreed to be bound by the terms of this arrangement letter, either by having validly authorised one or more of the signatories of this arrangement letter to enter into this arrangement letter on its behalf or validly ratified the entry into this arrangement letter on its behalf. The addressees of this arrangement letter (other than the Company [and the Guarantor]) are collectively referred to herein as the "Addressees". By signing and accepting the terms of this arrangement letter, each Named Addressee confirms that it will use reasonable endeavours to obtain prima facie authority from each of the other Managers authorising it to enter into this arrangement letter as representative of the relevant Manager. However, no Named Addressee makes any representation as to whether such prima facie authority actually confers the necessary authority.

Comfort Letter

4. The Comfort Letter and the Other Assistance will be provided to the Company [and the Guarantor] for [its/their] information only, and to the Addressees solely in the context of the due diligence procedures being undertaken or procured to be undertaken by the Addressees in connection with the offering or sale of the securities outside of the United States under Regulation S pursuant to the Offering Circular, for the purpose of establishing or seeking to establish any defence in such context ("Due Diligence Defence") that the Addressees may wish to advance in any actual or potential court or arbitration proceedings, any investigation, hearing or other proceedings by any regulatory body, or any claim or dispute in respect of the Offering Circular or otherwise in connection with the Issue. Accordingly, the Comfort Letter will be addressed to the Addressees for that purpose and neither the Comfort Letter nor the Other Assistance may be relied on by the Addressees for any other purpose. The Addressees are requesting the Comfort Letter in connection with the Issue as one of a number of procedures that the Addressees may use to establish the investigation that they have conducted.
5. Each Named Addressee confirms that it is aware of the guidance related to due diligence issued by the International Capital Market Association, which will be followed.
6. For the avoidance of doubt and subject to the limitations or exclusions which are contained in or referred to in Paragraphs 7, 8, 24 and 30 of this arrangement letter, nothing in this arrangement letter shall preclude any Addressee from obtaining compensation from us in respect of any liability that it may incur to an investor arising out of the Issue or the contents of the Offering Circular to the extent that such liability arises because the work undertaken pursuant to this arrangement letter or the Comfort Letter was undertaken negligently, in bad faith or as a result of our fraud or wilful default, it being understood that the foregoing is without prejudice to any defence of contributory negligence that may be available to us.
7. The Comfort Letter issued pursuant to this arrangement letter will be provided in accordance with the standards of the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and will not have been provided in accordance with any other professional standards, including but not limited to those of the American Institute of Certified Public Accountants.
8. Our work and findings shall not in any way constitute advice or recommendations (and we accept no liability in relation to any advice or recommendations) regarding any commercial decisions associated with the Issue, including, in particular, but without limitation, any which may be taken by any Addressee (or any person connected to any Addressee) in the capacity of investor or in providing investment advice to their clients.
9. The Comfort Letter will be provided solely for the Addressees' private information and should not be used for any purpose other than as set out in Paragraph 4. The Comfort Letter may not be referred to in any other document (except that references may be made to its existence in (i) contracts among any of the Company [and the Guarantor], the Addressees and ourselves and (ii) any communications in relation to the Issue among any of the Company[, the Guarantor], the Addressees, the Managers and ourselves), nor made available to any other party (except that

copies may be included in bibles of transaction documents memorialising the Issue).

10. Nothing in Paragraphs 4, 7 or 9 shall prevent the Addressees from disclosing this arrangement letter and the Comfort Letter to the Addressees' professional advisers or as may be required by law, regulation or court order or the rules or requirements of a regulatory body or stock exchange whose requirements the Addressees are complying with, and/or referring to and/or producing the Comfort Letter for any of the purposes set out in Paragraph 4. Except as permitted in the immediately preceding sentence, the Addressees shall first obtain our prior written consent for disclosure of the Comfort Letter to third parties.
11. Other than to those who have, or before the Comfort Letter is issued shall have, validly accepted this arrangement letter, we will not accept any responsibility to any party to whom the Comfort Letter is shown or into whose hands it may come.

Work and Procedures

12. Our work will be conducted in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the HKICPA. Specifically, our work will enable us to report factual findings in relation to selected financial information and to enable us to provide limited assurance on subsequent changes to historical financial information included in the Offering Circular. [Procedures undertaken in connection with providing limited assurance on interim financial statements will be conducted with reference to Hong Kong Standard on Review Engagements ("HKSRE") 2410.²⁵] In other jurisdictions, standards and practices relevant to our work may be different and may not provide for reporting in the manner contemplated herein. Accordingly, the Comfort Letter should not be relied on as if it had been provided in accordance with the standards and practice of any professional body in any other jurisdiction.
13. Except as specifically stated in our comfort letter we have not performed an audit or review in respect of any financial statements relating to the [Company/Guarantor] for any period subsequent to [date of last reported balance sheet] in accordance with Hong Kong Standards on Auditing ("HKSA") or [Hong Kong Standards on Review Engagements ("HKSREs")][HKSREs] issued by the HKICPA. The procedures we will use to perform the work set out in this arrangement letter including those in relation to subsequent changes will not constitute an audit or review made in accordance with HKSA or HKSREs issued by the HKICPA. Furthermore, they will not necessarily reveal matters of significance with respect to any material misstatement of the information referred to below.
14. We will only carry out those procedures expressly provided for in the Comfort Letter. Accordingly, we make no representations as to the sufficiency for the Addressees' purposes of the procedures provided for in the Comfort Letter and, therefore, our responsibility shall be limited to performing the work agreed upon in this arrangement letter and/or recorded in the Comfort Letter with due skill, care and attention. If we were to perform additional procedures or if we were to conduct an audit or review on the financial statements of the [Company/Guarantor] in accordance with HKSA or HKSREs issued by the HKICPA, other matters might be reported to the Addressees in the Comfort Letter. The procedures to be performed by us in connection with the Comfort Letter should not be taken to supplant additional inquiries or procedures that may be appropriate in the performance of the Addressees' role under the proposed Issue.
15. In relation to the contents of the Offering Circular, we will address ourselves solely to such financial and other information in the Offering Circular as is identified in the Comfort Letter and we will make no representations as to the adequacy of disclosure in the Offering Circular or as to whether any material facts have been omitted by the Company. Further, we make no representations regarding any questions of legal interpretation.
16. The procedures that we plan to conduct have been determined by the Named Addressees and agreed by the parties to this arrangement letter, and will be recorded in the Comfort Letter. In carrying out our work pursuant to this arrangement letter, we will rely

²⁵ In certain situations independent accountants may be required to perform a review of interim financial statements in order to enable negative assurance to be provided on subsequent changes. This sentence should be included where such a review will be undertaken.

on the accuracy and completeness of certain information and explanations provided to us during the course of our work and will further request the directors of the [Company/Guarantor] to provide us with written representations concerning the accuracy and completeness of certain information and explanations provided to us for the purpose of our work. The Addressees will therefore understand that the procedures to be carried out by us are not designed to, and are not likely to, reveal fraud, withholding, concealment or misrepresentation by the management of the [Company or its subsidiaries (the Company and its subsidiaries are collectively referred to herein as "the Group")] [Company, the Guarantor or its subsidiaries (the Guarantor and its subsidiaries are collectively referred to herein as "the Group")]. Notwithstanding the preceding three sentences, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), we will (and are hereby authorised by the Company [and the Guarantor] to), as soon as practicable, notify the Company[, the Guarantor] and the Named Addressees of this and discuss with them whether further procedures can be designed to seek to resolve the matter. Where such procedures are agreed between us, we will carry them out and amend the Comfort Letter accordingly.

17. Any opinions expressed on financial information outside the context of this arrangement letter were or are expressed solely in the context of the specific terms and conditions governing their preparation. In particular, the terms of this arrangement letter and any action pursuant to it shall be additional to and shall not detract from or change in any way any legal rights which any party to this arrangement letter may otherwise have acquired, whether in contract or in tort, in connection with our reporting on the historical financial information of the [Company/Guarantor].
18. Save as may be expressly recorded in the Comfort Letter, we do not accept any responsibility for any other reports or letters beyond any responsibility that we owed to those to whom our reports or letters were addressed at the date of their issue.

Contents of the Comfort Letter

19. We will prepare and expect to issue the Comfort Letter addressed to the Company [, the Guarantor] and the Addressees on the basis described above. Based upon our present understanding of the Addressees' requirements, we expect to be able to provide the Addressees with the Comfort Letter substantially in the form contained in the Appendix to this arrangement letter, setting out the procedures that we expect to carry out prior to issuing the Comfort Letter.²⁶ Execution of this arrangement letter by the Named Addressees will constitute the Addressees' agreement to the scope and extent of such procedures.
20. We would be grateful if the Named Addressees would review the draft comfort letter that we expect to be able to provide the Addressees with and let us have any amendments the Named Addressees propose to the procedures as soon as possible, so that we can provide the Named Addressees with a revised draft for further consideration and approval.
21. Once an advanced draft of the Offering Circular is available and the Named Addressees have identified, and we have agreed, the detailed financial information whose extraction or calculation the Named Addressees require to be covered in the Comfort Letter, we will provide the Named Addressees with a further revised draft of the Comfort Letter for approval of its scope prior to finalisation.

²⁶ Where a draft comfort letter is not appended, briefly explain the procedures to be performed.

22. For the avoidance of doubt, we will not comment on, or otherwise give comfort in relation to, the [Company's/Guarantor's] prospects or trading position or, save as expressly stated in the Comfort Letter, comment on or provide any opinion or other conclusion as to the current overall financial position of the [Company/Guarantor].²⁷

Drafts

23. During the course of the arrangement we may show drafts of, or report orally on, the Comfort Letter to the Named Addressees. In so far as any such draft or oral report is inconsistent with the subsequent final Comfort Letter, it will be deemed to be superseded by such final Comfort Letter.

Meetings

24. It will be necessary for us to receive copies of the draft Offering Circular as it is produced and it may be necessary for us to attend meetings (including, but not limited to, meetings with the Company[, the Guarantor] and [its/their] directors and/or employees and the Addressees and their employees, advisers or agents) at which the Offering Circular is discussed and drafted or at which other related matters are discussed. We shall answer queries raised at such meetings on an informal basis but the Addressees should neither act nor refrain from acting on the basis of such informal answers unless and until they are confirmed in writing by us, whether in the final Comfort Letter or otherwise. In the absence of such written confirmation we shall have no liability to the Addressees in contract or in tort (including negligence) for our answers other than for an oral statement known to be false or misleading when made and made with intent to deceive.²⁸ Subject to the above, nothing in this paragraph shall prejudice the Addressees' ability to rely on a non-recourse basis (meaning without any liability on our part except for oral statements known to be false or misleading when made and made with intent to deceive) on any comments we may provide orally, either in the context of establishing or seeking to establish any Due Diligence Defence in connection with any court, arbitral, regulatory or administrative proceedings or otherwise for the purposes of resolving either actual or potential proceedings, investigations, claims or disputes in respect of the Offering Circular or otherwise in connection with the Issue.
25. Unless otherwise specifically agreed between the Company[, the Guarantor], the Named Addressees and us, we are authorised by the Company [and the Guarantor] to speak to the Addressees and other professional advisers advising on the proposed Issue. In connection with our work pursuant to this arrangement letter, we may release to the Addressees and such other professional advisers any information relating to the Company [and the Guarantor] or the Issue, whether confidential or not, and whether obtained during the course of our work or otherwise, and shall not be liable to the Company [or the Guarantor] for any use subsequently made of that information. Our partners and staff working on this arrangement shall not be required, expected or deemed to have knowledge of any information known to other partners or staff of our firm but which is not known to those on this arrangement. In addition we shall not be required to make use of or disclose to the Addressees any information which is confidential to another client of our firm.

Timetable

26. Our work will depend upon receiving without undue delay full co-operation from all relevant officials of the Company[, the Guarantor] and the Group and their disclosure to us of all accounting records of the Group and all other records and related information (including certain representations) we may need for the purposes of our work. We will endeavour to carry out our work in accordance with a timetable to be agreed between all parties that will satisfy the requirements of the Issue. We intend to provide the Company[, the Guarantor] and the Addressees with (1) the Comfort Letter dated the date of the Offering Circular relating to the Issue, (2) an additional or updating Comfort Letter on and dated the date of the closing of the

²⁷ If specific procedures and appropriate terms (e.g. as to timing) are agreed between all parties, the independent accountants may undertake additional work in accordance with HKSIR 400 (Revised).

²⁸ If specific matters are discussed which the Addressees wish to be able to rely upon in accordance with this arrangement letter, the Issuer and the Named Addressees should arrange for them to be confirmed in writing by the independent accountants. If the independent accountants are willing to confirm such matters in writing, further work and an extension of the terms of the arrangement are likely to be required.

Issue (to be delivered at closing of the Issue) and (3) where appropriate, an additional or updating Comfort Letter on and dated the over-allotment option closing date.²⁹ In connection with the delivery of any new or updating Comfort Letter, we will bring down our work to an agreed cut-off date. We will discuss with the Named Addressees any difficulties we encounter with this arrangement or with meeting the timetable as soon as any problems arise.

Applicable Law and Jurisdiction

27. This arrangement letter shall be governed by, and construed in accordance with, Hong Kong law. The Courts of Hong Kong shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning this arrangement letter, the Comfort Letter or any matter arising from them.

Staffing

28. [Name] will be the partner in charge of the services we will provide. [Name] will act as manager, with the help of [name], calling upon specialist staff as appropriate. We shall use reasonable endeavours to ensure that they are so involved but we may substitute those identified with others of equal or similar skills.

Fees and Certain Other Matters

29. Details of our fees and proposed billing arrangements have been set out in a separate agreement with the Company [and the Guarantor], who will bear the sole responsibility for the payment thereof. Such agreement also sets out certain other matters in relation to the respective rights and responsibilities of the Company[, the Guarantor] and us in connection with the services to be performed by us in connection with the issuance of the Comfort Letter.

Other Terms and Conditions

30. In no circumstances shall we be liable, other than in the event of our fraud, bad faith or wilful default, for any loss or damage, of whatsoever nature, arising from information material to our work being withheld or concealed from us or misrepresented to us by the directors, employees, or agents of the Company[, the Guarantor] or any other person of whom we may make inquiries unless, if in carrying out the procedures agreed under this arrangement letter, and solely as a result of information provided to us which we are required to consider or do consider, we conclude that there has been fraud, withholding, concealment or misrepresentation (or otherwise we conclude that any such information contains an inconsistency which clearly indicates that there may have been such a fraud, withholding, concealment or misrepresentation), and we fail to notify the Company[, the Guarantor] and the Named Addressees of such conclusion.
31. In the course of providing the Services we, [Accountants] Hong Kong, may, at our discretion, draw on the resource of other entities (whether or not incorporated) which carry on business under a name which includes all or part of the [Accountants] name or is otherwise within (or associated or connected with an entity) or is a correspondent firm of the worldwide network of [Accountants] ("other [Accountants] Firms") and their partners and employees as we deem appropriate, but provision of the Services will remain our responsibility alone.
32. The Addressees agree that the Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) against any other [Accountants] Firm or its personnel in respect of the Services. Any partner or employee of any other [Accountants] Firm who deals with the Addressees in connection with the Services does so solely on our behalf and we are liable for their activities as if they were in all respects our partners or staff.
33. The Addressees will not bring any claim (whether in contract, tort (including negligence) or otherwise) arising out of or in connection with the Services against any of our employees personally, but this will not limit or exclude any liability we may have for their acts or omissions.

²⁹ In exceptional circumstances, it may also be appropriate to bring down the Comfort Letter to another date. Such arrangements should be discussed on a case-by-case basis.

34. The provisions of paragraphs 31 to 33 of this arrangement letter have been stipulated expressly for the benefit of our employees, and other [Accountants] Firms and their partners and employees (together "Beneficiaries"). The Addressees agree that, each of the Beneficiaries has the right to rely on paragraphs 31 to 34 of this arrangement letter as if they were parties to this arrangement letter. Each of the other [Accountants] Firms which agrees to assist in the provision of the Services does so in reliance on the protections afforded to it by paragraphs 31 to 34 of this arrangement letter, the benefit of which we formally accept on its behalf.

Prohibition on Assignment

35. No party may assign any of its rights in relation to this arrangement letter without the prior written consent of the others against whom the rights may be asserted, save that any Addressee and we may assign any of such rights, or such rights may pass by operation of law, to any successor to all or part of its business without such consent, provided that notice is given to the other signatories to this arrangement letter prior to any step being taken to enforce any rights hereunder.

Third Party Rights

36. Other than as set out in paragraph 34 above, this arrangement letter shall not create or give rise to, nor shall it be intended to create or give rise to, any third party rights and no third party shall have any right to enforce or rely on any provision of this arrangement letter. Save where otherwise stated in paragraph 34 above, the Contracts (Rights of Third Parties) Ordinance (Cap. 623 of the laws of Hong Kong) shall not under any circumstances apply to this arrangement letter. Any rights conferred on third parties by this arrangement letter exclude the right to assign, and their consent is not required to rescind or vary this arrangement letter. For the avoidance of doubt, this paragraph shall not apply to the Addressees or the successors referred to in paragraph 35 above.

Termination

37. Any party to this arrangement letter may at any time terminate this arrangement letter for whatever reason upon written notice to the other parties. In the case of termination by us, notice to the Company[, the Guarantor] and the Named Addressees shall be sufficient notice.
38. Termination of this arrangement letter shall be without prejudice to any accrued rights of the parties to this arrangement letter. The provisions of this arrangement letter which expressly or by implication are intended to survive its termination or expiry will survive and continue to bind each party to this arrangement letter.

Internet communication

39. In connection with the Services the parties to this arrangement letter may from time to time communicate with each other electronically. However, the electronic transmission of information cannot be guaranteed to be secure or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use. Accordingly each party to this arrangement letter accepts the limitations of electronic communication, and will use reasonable procedures to check for the then most commonly known viruses before sending information electronically.

Miscellaneous

40. Other than as set out in paragraph 29 above, this arrangement letter and the Appendix to it constitute the entire agreement for the provision of the Services between us to the exclusion of any other express or implied terms, whether expressed orally or in writing, including any conditions, warranties and representations and shall supersede all previous proposals, understandings, contracts, letters of engagement, undertakings, agreements and correspondence regarding the Services. Save as provided in this arrangement letter, no change in the terms of our arrangement with respect to the Services will be effective unless agreed in writing and signed by all parties to this arrangement letter.

41. This arrangement letter may be executed in any number of counterparts, and by the parties on separate counterparts, but shall not be effective until each party has executed and delivered at least one counterpart. Each counterpart shall constitute an original of this arrangement letter, but all the counterparts shall together constitute one and the same instrument.
42. If any term or terms of this arrangement letter shall be held to be invalid, illegal or unenforceable, such term or terms shall be deemed not to form part of this arrangement letter without prejudice to the enforceability of the remaining terms of this arrangement letter, provided always that if any such deletion substantially affects or alters the commercial basis of this arrangement letter, the parties to this arrangement letter will negotiate in good faith to amend and modify them as may be necessary or desirable in the circumstances.
43. Please acknowledge acceptance of the terms of our arrangement by signing and returning the enclosed copy of this arrangement letter.
44. If the Company[, the Guarantor] or the Addressees have any questions regarding this arrangement letter please do not hesitate to contact us.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Acknowledgement and Acceptance

We acknowledge receipt of this arrangement letter and agree with the terms of your arrangement set out therein:

Director
for and on behalf of
the board of XYZ Limited [and ABC Limited]

Director
for and on behalf of
Lead Manager Limited/ [Named Addressee]
(on its own behalf and as representative
of each of the other Managers)

Appendix 2

Example Comfort Letter

The following example comfort letters are provided for illustrative purposes only. They are intended to be used only as a guide to the possible form and content of a comfort letter that reporting accountants may wish to provide, and are not intended to suggest standard wording to be used in any particular set of circumstances. The contents of the comfort letter will vary according to the nature of the information in the investment circular, and the procedures agreed between reporting accountants, sponsors, and the issuer. When preparing a comfort letter, reporting accountants will need to ensure that the letter meets the requirements of this HKSIR.

As further explained in paragraph 69 of this HKSIR, where there is an international equity or debt offering not covered by relevant jurisdictional standards, reporting accountants refer to the requirements of HKSIR 400 (Revised). In practice, due for example, to different cut-off dates being applied to the procedures in respect of subsequent changes for the respective international and Hong Kong public offerings, it will often be the case that for practical purposes more than one comfort letter is issued for certain transactions. Example 1 illustrates a letter with respect to the Hong Kong public offering. Where a separate comfort letter is issued for the international offering the text below should be tailored as appropriate. In general, other than for certain specific textural differences reflecting for example, the terminology often used for an international offering and different cut-off dates, it is not expected that there would be significant differences between the comfort letters. Example 2 illustrates a letter with respect to a Debt Offering in reliance on Regulation S.

Example 1 – Hong Kong Public Equity Offering

(letterhead of reporting accountants)

Date

To: The Directors, XYZ Limited
[Address]

Sponsors Limited
[Address]

[Other Named Addressee]³⁰
[Address]

[and each of the Hong Kong Underwriters as defined in the Hong Kong Underwriting Agreement dated [•] (the "Hong Kong Underwriters") identified below as an Addressee]³⁰

Dear Sirs,

Proposed Listing of [XYZ Limited] (the "Issuer") on the [Main Board/Growth Enterprise Market] of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange")

This letter is written to you pursuant to the terms agreed between us in our arrangement letter dated [date] (the "Arrangement Letter"). Our engagement to prepare this letter has been performed in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

This letter is addressed to [insert the names of each Named Addressee] and to each of the Hong Kong Underwriters that is an "Addressee" as defined in paragraph 3 of the Arrangement Letter and to the directors of the Issuer. Other than to those who have validly accepted the Arrangement Letter, we will not accept any responsibility to any party to whom this letter is shown or into whose hands it may come.

We confirm that we are independent with respect to the Issuer in accordance with the requirements of the Code of Ethics for Professional Accountants issued by the HKICPA.

Selected Financial Information

For the purposes of this letter, we have read the items that you have identified as indicated on the attached extract of the prospectus (attached as Appendix 1) of the Issuer and have performed the following procedures, which were applied as indicated by the letters explained below:³¹

- A Compared the amount or percentage to, or recalculated the amount and/or percentage from, the corresponding amount or percentage appearing in the historical financial information of the Issuer [and its subsidiaries ("the Group")] for the years ended 31 December 20X2, 31 December 20X3 and 31 December 20X4 and [periods ended [insert stub period balance sheet date] and [insert comparative stub period balance sheet date] as set out on pages [] to [] of the prospectus (the "Historical Financial Information"), as applicable, and found them to be in agreement.

³⁰ Refer to Example 1, footnote 6, in Appendix 1 to this HKSIR.

³¹ The purpose of the procedures described in this section is to compare amounts and to state whether such amounts are found to be in agreement or to recompute calculations and to state whether or not these were found to be arithmetically accurate.

- B Compared the amount or percentage to the corresponding amount or percentage appearing on a schedule prepared by the management of the Issuer and found the amount or percentage to be in agreement. Management of the Issuer has represented to us that the information on the schedule was derived from the regularly maintained accounting records of the [Issuer][Group] and was subject to the [Issuer's][Group's] internal controls over financial reporting. [We compared the amounts shown on the schedule prepared by the management of the Issuer with the accounting records and found such amounts to be in agreement.]
- C Recalculated the amount, percentage or ratio based on the information in the same sentence, paragraph or table and found them to be arithmetically accurate.
- D Recalculated the [United States dollar] amount based on the corresponding [*reporting currency*] amount and the rate of US\$[x] to [x] as specified on page [x] in the prospectus and found them to be arithmetically accurate. However, we make no comment as to the appropriateness of such rate or whether the [*reporting currency*] could have been, or could be, converted into [United States dollars] at that rate.
- E [Recalculated the amounts under "As Adjusted" in the "Capitalization [and Indebtedness]" section of the Offering memorandum based on the assumptions specified on page [x] of the Offering Memorandum and found them to be arithmetically accurate. However, we make no comment as to the reasonableness or appropriateness of those assumptions or as to the ultimate amount or use of proceeds or the appropriateness of the financial reporting presentation.³²]

For the purposes of reporting our findings, in those instances in which one or more of the compared or recalculated amounts (including percentages and ratios) stated were rounded to some degree, we have nevertheless stated that we found the compared or recalculated amounts to be in agreement or arithmetically accurate if differences are attributable to rounding.

We make no representations regarding questions of legal interpretation or regarding the sufficiency for your purposes of the aforementioned procedures; also, such procedures do not constitute an assurance engagement performed in accordance with Hong Kong Standards on Auditing ("HKSA"), Hong Kong Standards on Review Engagements ("HKSREs"), Hong Kong Standards on Assurance Engagements [or other Hong Kong Standards on Investment Circular Reporting Engagements] issued by the HKICPA, and therefore would not necessarily reveal any material misstatement of the amounts, percentages or ratios identified above. Further, we have addressed ourselves solely to the foregoing data in the prospectus and we make no representations regarding the adequacy of disclosures or regarding whether any material facts have been omitted.

³² This procedure is only applicable for an international equity offering (hence the reference to an "Offering Memorandum" as opposed to a prospectus) and should only be performed and reported on if all of the information required to recalculate the amounts under "As Adjusted" are set out on the specified page in the Offering Memorandum. In an actual comfort letter in respect of an international equity offering, other conforming changes to the introductory paragraphs and other parts of the letter would be required reflecting, for example, the different terminology used for an international offering.

Changes in Financial Position^{33,34}

For the purpose of this letter, we have [also] performed the following limited procedures:

- (1) We have:
- (a) read the minutes of meetings of shareholders and the board of directors of the Issuer [and its subsidiaries] held since [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus], as set out in minute books at 22 May 20X5 (the "Cut-off Date") [(together with/excluding³⁵ the papers referred to in the minutes)], which the directors have advised us are complete; and
 - (b) read the unaudited management accounts of the [Issuer/Group] for the [four] month[s] ended 30 April 20X5 (the "April 20X5 Management Accounts") [(which the directors have advised us are the most recent management accounts available)] [(as agreed with you)³⁶] and the corresponding unaudited management accounts for the previous year (the "April 20X4 Management Accounts").

Our objective in reading the documents referred to in paragraphs 1(a) and (b) above is to identify those matters which in our view, might, *prima facie*, be expected to impact the figures and changes set out in paragraph (3) below.

- (2) We have made inquiries of [certain officials of the Issuer/*name of officials*] with responsibility for financial and accounting matters (the "Persons Responsible for Financial and Accounting Matters") as to whether:

³³ For the purpose of this example comfort letter limited assurance is provided in respect to the changes in financial position, rather than reporting accountant reporting in the form of agreed-upon-procedures. Should the form of agreed-upon-procedures be adopted, paragraphs (5) and (7) would be revised by reporting the factual findings obtained, for example the final sentence of paragraph (7) may be deleted and paragraph (5) may be revised to read:

We enquired of the Persons Responsible for Financial and Accounting Matters whether:

- (a) at 30 April 20X5 there were any decreases in [the issued share capital, cash and cash equivalents, net current assets or total current assets or increases in long-term debt or total current liabilities] of the [Group] as compared with the corresponding amounts as at [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] in the Historical Financial Information; and
- (b) in the period from [1 January] 20X5 to 30 April 20X5 there were any decreases in [turnover or profit before taxation or increases in net interest expense, or depreciation of fixed assets] of the Group, as compared to the corresponding period in the preceding year as shown in the April 20X4 Management Accounts.

Those Persons Responsible for Financial and Accounting Matters stated that there was no such increase or decrease except that the April 20X5 Management Accounts showed a [decrease/increase] in [insert line items] as compared with [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] and a [decrease/increase] in [insert line items] as compared with the [4] months ended 30 April 20X4, as set out in Appendix 2.

³⁴ Where the reporting accountants agree to perform a review of subsequent interim financial information not included in the prospectus for the purpose of providing limited assurance on subsequent changes, this may be referred to in the section headed "Changes in Financial Position" and any other corresponding changes made to the comfort letter as applicable. For example, the following language may be added to record the fact that the review was performed and the conclusion arising from that review:

For the purposes of this letter, with respect to the three-month period ended 31 March 20X5, we have performed procedures with reference to HKSRE 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*, on the unaudited condensed statement of financial position of the Group as of 31 March 20X5, and the related unaudited condensed statements of comprehensive income, changes in equity and cash flows for the three-month period ended 31 March 20X5, attached to this comfort letter as Appendix 3.

Nothing came to our attention as a result of the foregoing procedures that caused us to believe that any material modification should be made to the unaudited condensed financial information described in the paragraph above and attached to this comfort letter as appendix 3, for them to be in conformity with [Hong Kong][International] Accounting Standard 34 "Interim Financial Reporting".

³⁵ Where practicable, on appropriate terms and provided sufficient time is available, the accountants may agree to review the papers referred to in the minutes.

³⁶ This wording would apply in circumstances where the Reporting Accountants and the Sponsors are aware of the date of the latest management accounts, but it is agreed that management accounts as of and for an earlier period are to be referred to in this letter.

- (a) those matters identified by us in the course of the work undertaken pursuant to paragraph (1) above have been reflected in the April 20X5 Management Accounts upon which the amounts and changes referred to in paragraph (3) below are based; and
- (b) the April 20X5 Management Accounts have been prepared and presented on a basis consistent with the accounting policies normally adopted by the Group and applied in preparing the Historical Financial Information.
- (3) We have compared the amounts shown in the schedule included in Appendix 2 to this letter prepared by the management of the Issuer (the "Schedule"), relating to [turnover, profit before taxation, net interest expense, depreciation of fixed assets, issued share capital, borrowings due after more than one year ("long-term debt"), cash and cash equivalents, net current assets, total current assets and total current liabilities], to the April 20X5 Management Accounts, April 20X4 Management Accounts or the Historical Financial Information as appropriate and found them to be in agreement. We have recalculated the changes set out in the Schedule and found them to be arithmetically accurate.
- (4) The procedures described in paragraphs (1) to (3) above do not constitute an audit [or review] in accordance with HKSAAs [or HKSREs] issued by the HKICPA. Nor do they provide any assurance that the April 20X5 Management Accounts have been prepared on a basis consistent with the April 20X4 Management Accounts, that such management accounts have been prepared in a reliable manner or that either have been prepared on a basis consistent with the Historical Financial Information. Consequently, our procedures would not necessarily reveal matters of significance with respect to the comments made in the following paragraphs and we make no representations as to the sufficiency for your purposes of any such procedures.
- (5) In respect of the foregoing procedures nothing has come to our attention that causes us to believe that:
- (a) at 30 April 20X5 there were any decreases in [the issued share capital, cash and cash equivalents, net current assets or total current assets] or [increases in long-term debt or total current liabilities] of the [Group] as compared with the corresponding amounts as at [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] in the Historical Financial Information; and
- (b) in the period from [1 January] 20X5 to 30 April 20X5 there were any decreases in [turnover or profit before taxation or increases in net interest expense, or depreciation of fixed assets] of the Group, as compared to the corresponding period in the preceding year as shown in the April 20X4 Management Accounts.
- except that the April 20X5 Management Accounts showed a [decrease/increase] in [insert line items] as compared with [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] and a [decrease/increase] in [insert line items] as compared with the [4] months ended 30 April 20X5, as set out in Appendix 2.³⁷
- (6) Since [the directors have advised us that no management accounts have been prepared up to any date subsequent to 30 April 20X5][we have agreed with you to read the unaudited management accounts for the [four] month[s] ended 30 April 20X5], the procedures carried out by us with respect to changes in financial statement items³⁸ of the [Issuer/Group] after 30 April 20X5 have of necessity been even more limited than those carried out for the period up to that date. Up to the Cut-off Date (our work did not extend to the period from the Cut-off Date to the date of this letter), we have made inquiries of the Persons Responsible for Financial and Accounting Matters as to:

³⁷ Line items described as exceptions here should not be listed in 5(a) or (b).

³⁸ Reporting accountants should consider the guidance in paragraph 45 in determining the appropriateness of which specific line items to provide comfort.

- (a) whether there has been any decrease in [issued share capital, cash and cash equivalents, net current assets or total current assets] or increase in [long term debt or total current liabilities] of the [Group] at the Cut-off Date as compared with the corresponding amounts shown at [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] in the Historical Financial Information; and
- (b) whether for the period from [1 January 20X5] up to the Cut-off Date there have been any decreases in [turnover or profit before taxation], or increases in [net interest expense or depreciation of fixed assets] of the [Group] as compared with the corresponding period in the preceding year.
- (7) The persons responsible for financial and accounting matters advised us that they were not aware of any increase in [long term debt, total current liabilities, net interest expense or depreciation of fixed assets] or decrease in any of the other listed items described in paragraph (6)(a) or (b) above except that [as at the Cut-off Date as compared with [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] [there was an [increase][decrease] in [*state line items*]]/[for the period from 1 [January 20X5] to the Cut-off Date as compared with the corresponding period in the previous year there was an [increase][decrease] in [*state line items*]]. On the basis of the responses to these inquiries and our reading of the minutes as described in paragraph (1) above, [except for all instances of increases or decreases advised by the Persons Responsible for Financial and Accounting Matters as set out above], nothing has come to our attention that causes us to believe that there was any such increase or decrease.
- (8) We have not performed an audit in respect of any historical financial information of the Issuer or the Group as of any date or for any period subsequent to [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus] in accordance with HKSAs issued by the HKICPA. Therefore we are unable to and do not express any opinion on the financial position, results of operations or cash flows of the Issuer [or the Group] as of any date or for any period subsequent to [31 December 20X4 or such later reported stub period balance sheet date included in the prospectus].

This letter is solely for your information and to assist the Addressees in conducting and documenting their due diligence investigation of the affairs of the [Issuer/Group] in connection with the issue of new shares covered by the prospectus and except as permitted in the Arrangement Letter, it is not to be used, circulated, quoted, or otherwise referred to for any other purpose, nor is to be filed with or referred to in whole or in part in the prospectus or any other document.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Enclosures: Appendix 1 - Extract of prospectus
Appendix 2 - Schedule prepared by the Issuer's management
[Appendix 3 – Unaudited condensed consolidated financial statements for the period ended [*insert interim balance sheet date reviewed*] and [*insert corresponding date in prior year*]

Example 2 – Debt Offering in reliance on Regulation S

(letterhead of independent accountants)

Date

To: The Directors, [XYZ Limited and ABC Limited]
[Address]

[Lead Manager Limited]
[Address]

[Other Named Addressee]³⁹
[Address]

[and each of the joint lead managers and managers as defined in the Subscription Agreement dated [x] (the "Managers") identified below as an Addressee]³⁹

Dear Sirs,

Proposed Issue (the "Issue") of [x] (the "Notes") by [XYZ Limited] (the "Company") [and guaranteed by [ABC Limited] (the "Guarantor")]

This letter is written to you pursuant to the terms agreed between us in our arrangement letter dated [date] (the "Arrangement Letter"). Our engagement to prepare this letter has been performed in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), *Comfort Letters and Due Diligence Meetings* issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

This letter is addressed to [insert the names of each Named Addressee] and to each of the Managers that is an "Addressee" as defined in paragraph 3 of the Arrangement Letter and to the directors of the Company [and the Guarantor]. Other than to those who have validly accepted the Arrangement Letter, we will not accept any responsibility to any party to whom this letter is shown or into whose hands it may come.

We confirm that we are independent with respect to the Company [and the Guarantor] in accordance with the requirements of the Code of Ethics for Professional Accountants issued by the HKICPA.

On pages [x to x], the offering circular of the Company with respect to the Notes dated 20[x] (the "Offering Circular") sets out certain financial statements as at and for the [three] years ended 31 December 20X2, 20X3 and 20X4 (the "Historical Financial Statements") [and the [six] months ended 30 June 20X4 and 20X5] (the "Interim Financial Statements") of the [Company/Guarantor] and its subsidiaries (the "Group"). We have read this information and have compared it with that shown in the published audited consolidated financial statements as at and for the [three] years ended 31 December 20X2, 20X3 and 20X4 [and the published unaudited consolidated interim financial statements as at and for the [six] months ended 30 June 20X4 and 20X5] of the [Company/Guarantor]. We confirm that these financial statements have been found to be in agreement with the published audited consolidated financial statements for the relevant years [or, as the case may be, the published unaudited consolidated interim financial statements for such period]. [We did not conduct a review of such interim financial statements in accordance with the standards and guidance issued by the [HKICPA] or any professional body in any other jurisdiction].

³⁹ Refer to Example 4, footnote 24, in Appendix 1 to this HKSIR.

Selected Financial Information

For the purposes of this letter, we have read the items that you have identified as indicated on the attached extract of the Offering Circular (attached as Appendix 1) and have performed the following procedures, which were applied as indicated by the letters explained below⁴⁰:

- A Compared the amount or percentage to, or recalculated the amount and/or percentage from, the corresponding amount or percentage appearing in the Historical Financial Statements [or the Interim Financial Statements] as set out in the Offering Circular, as applicable, and found them to be in agreement.
- B Compared the amount or percentage to the corresponding amount or percentage appearing on a schedule prepared by the management of the [Company/Guarantor] and found the amount or percentage to be in agreement. The management of the [Company/Guarantor] has represented to us that the information in the schedule was derived from the regularly maintained accounting records of the Group and was subject to the [Company's/Guarantor's] internal controls over financial reporting. [We compared the amounts shown on the schedule prepared by the management of the [Company/Guarantor] with the accounting records of the Group and found such amounts to be in agreement.]
- C Recalculated the amount, percentage or ratio based on the information in the same sentence, paragraph or table and found them to be arithmetically accurate.
- D Recalculated the [United States dollar] amount based on the corresponding [*reporting currency*] amount and the rate of US\$[x] to [x] as specified on page [] in the Offering Circular and found them to be arithmetically accurate. However, we make no comment as to the appropriateness of such rate or whether the [*reporting currency*] could have been, or could be, converted into [United States dollars] at that rate.
- E Recalculated the amounts under "As Adjusted" in the "Capitalization [and Indebtedness]" section of the Offering Circular based on the assumptions specified on page [x] of the Offering Circular and found them to be arithmetically accurate. However, we make no comment as to the reasonableness or appropriateness of those assumptions or as to the ultimate amount or use of proceeds or the appropriateness of the financial reporting presentation.⁴¹

For the purposes of reporting our findings, in those instances in which one or more of the compared or recalculated amounts (including percentages and ratios) stated were rounded to some degree, we have nevertheless stated that we found the compared or recalculated amounts to be in agreement or arithmetically accurate if differences are attributable to rounding.

We make no representations regarding questions of legal interpretation or regarding the sufficiency for your purposes of the aforementioned procedures; also, such procedures do not constitute an assurance engagement performed in accordance with Hong Kong Standards on Auditing ("HKSAAs"), Hong Kong Standards on Review Engagements ("HKSREs"), Hong Kong Standards on Assurance Engagements [or other Hong Kong Standards on Investment Circular Reporting Engagements] issued by the HKICPA, and therefore would not necessarily reveal any material misstatement of the amounts, percentages or ratios identified above. Further, we have addressed ourselves solely to the foregoing data in the Offering Circular and we make no representations regarding the adequacy of disclosures or regarding whether any material facts have been omitted.

⁴⁰ The purpose of the procedures described in this section is to compare amounts and to state whether such amounts are found to be in agreement or to recompute calculations and to state whether or not these were found to be arithmetically accurate.

⁴¹ This procedure should only be performed and reported on if all of the information required to recalculate the amounts under "As Adjusted" are set out on the specified page in the Offering Circular.

Changes in Financial Position^{42, 43}

For the purpose of this letter, we have [also] performed the following limited procedures:

- (1) We have:
- (a) read the minutes of meetings of shareholders and the board of directors of the [Company/Guarantor] [and its subsidiaries] held since 31 December 20X4, as set out in minute books at 22 July 20X5 (the "Cut-off Date") [(together with/excluding⁴⁴ the papers referred to in the minutes)], which the directors have advised us are complete; and
 - (b) read the unaudited consolidated management accounts of the [Company/Guarantor] for the [one/seven] months ended 31 July 20X5 (the "July 20X5 Management Accounts") [(which the directors have advised us are the most recent management accounts available)][(as agreed with you)⁴⁵] and the corresponding unaudited consolidated management accounts for the previous year (the "July 20X4 Management Accounts").

Our objective in reading the documents referred to in paragraphs 1(a) and (b) above is to identify those matters which in our view, might, *prima facie*, be expected to impact the figures and changes set out in paragraph (3) below.

- (2) We have made inquiries of [certain officials of the Company/Guarantor/*name of officials*] with responsibility for financial and accounting matters (the "Persons Responsible for Financial and

⁴² For the purpose of this example comfort letter limited assurance is provided in respect to the changes in financial position, rather than reporting in the form of agreed-upon-procedures. Should the form of agreed-upon-procedures be adopted, paragraphs (5) and (7) would be revised by reporting the factual findings obtained, for example the final sentence of paragraph (7) may be deleted and paragraph (5) may be revised to read:

We enquired of the Persons Responsible for Financial and Accounting Matters whether:

- (a) at 31 July 20X5 there were any decreases in [the issued share capital, cash and cash equivalents, net current assets or total current assets or increases in long-term debt or total current liabilities] of the [Group] as compared with the corresponding amounts as at [31 December 20X4/30 June 20X5] in the [Historical Financial Statements/Interim Financial Statements] included in the Offering Circular; and
- (b) in the period from 1 [January/July] 20X5 to 31 July 20X5 there were any decreases in [turnover or profit before taxation or increases in net interest expense, or depreciation of fixed assets] of the [Group], as compared to the corresponding period in the preceding year as shown in the July 20X4 Management Accounts.

Those Persons Responsible for Financial and Accounting Matters stated that there was no such increase or decrease except that the July 20X5 Management Accounts showed a [decrease/increase] in [insert line items] as compared with [31 December 20X4/30 June 20X5] in the [Historical Financial Statements/Interim Financial Statements] included in the Offering Circular and a [decrease/increase] in [insert line items] as compared with the [1/7] months ended 31 July 20X4, as set out in Appendix 2.

⁴³ Where the independent accountants agree to perform a review of Interim Financial Statements included in the Offering Circular, or subsequent interim financial information not included in the Offering Circular for the purpose of providing limited assurance on subsequent changes, this may be referred to in the section headed "Changes in Financial Position" and any other corresponding changes made to the comfort letter as applicable. For example, the following language may be added to record the fact that the review was performed and the conclusion arising from that review:

For the purposes of this letter, with respect to the six-month period ended 30 June 20X5, we have performed procedures with reference to HKSRE 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*, on the unaudited condensed consolidated statement of financial position of the Group as of 30 June 20X5, and the related unaudited condensed consolidated statements of comprehensive income, changes in equity and cash flows for the six-month period ended 30 June 20X5[, attached as Appendix 3 to this comfort letter].

Nothing came to our attention as a result of the foregoing procedures that caused us to believe that any material modification should be made to the unaudited condensed consolidated financial statements described in the paragraph above and attached to this comfort letter as Appendix 3, for them to be in conformity with [Hong Kong][International] Accounting Standard 34 "Interim Financial Reporting".

⁴⁴ Where practicable, on appropriate terms and provided sufficient time is available, the independent accountants may agree to review the papers referred to in the minutes.

⁴⁵ This wording would apply in circumstances where the independent accountants and the Lead Managers are aware of the date of the latest management accounts, but it is agreed that management accounts as of and for an earlier period are to be referred to in this letter.

Accounting Matters") as to whether:

- (a) those matters identified by us in the course of the work undertaken pursuant to paragraph (1) above have been reflected in the July 20X5 Management Accounts upon which the amounts and changes referred to in paragraph (3) below are based; and
 - (b) the July 20X5 Management Accounts have been prepared and presented on a basis consistent with the accounting policies normally adopted by the Group and applied in preparing the 31 December 20X4 audited consolidated financial statements.
- (3) We have compared the amounts shown in the schedule included in Appendix 2 to this letter prepared by the management of the [Company/Guarantor] (the "Schedule"), relating to [turnover, profit before taxation, net interest expense, depreciation of fixed assets, issued share capital, borrowings due after more than one year ("long-term debt"), cash and cash equivalents net current assets, total current assets and total current liabilities], to the July 20X5 Management Accounts, July 20X4 Management Accounts or the 31 December 20X4 audited consolidated financial statements as appropriate and found them to be in agreement. We have recalculated the changes set out in the Schedule and found them to be arithmetically accurate.
- (4) The procedures described in paragraphs (1) to (3) above do not constitute an audit [or review] in accordance with HKSAAs [or HKSREs] issued by the HKICPA. Nor do they provide any assurance that the July 20X5 Management Accounts have been prepared on a basis consistent with the July 20X4 Management Accounts, that such management accounts have been prepared in a reliable manner or that either have been prepared on a basis consistent with the 31 December 20X4 audited consolidated financial statements. Consequently, our procedures would not necessarily reveal matters of significance with respect to the comments made in the following paragraphs and we make no representations as to the sufficiency for your purposes of any such procedures.
- (5) In respect of the foregoing procedures nothing has come to our attention that causes us to believe that:
- (a) at 31 July 20X5 there were any decreases in [the issued share capital, cash and cash equivalents, net current assets or total current assets] or increases in [long-term debt or total current liabilities] of the [Group] as compared with the corresponding amounts as at [31 December 20X4/30 June 20X5] in the [Historical Financial Statements/Interim Financial Statements] included in the Offering Circular; and
 - (b) in the period from 1 [January/July] 20X5 to 31 July 20X5 there were any decreases in [turnover or profit before taxation] or increases in [net interest expense, or depreciation of fixed assets] of the [Group], as compared to the corresponding period in the preceding year as shown in the July 20X4 Management Accounts;

except that the July 20X5 Management Accounts showed a [decrease/increase] in [*insert line items*] as compared with [31 December 20X4/30 June 20X5] and a [decrease/increase] in [*insert line items*] as compared with the [one/seven] months ended 31 July 20X5, as set out in Appendix 2.⁴⁶

- (6) Since [the directors have advised us that no management accounts have been prepared up to any date subsequent to 31 July 20X5][we have agreed with you to read the unaudited management accounts for the [one/seven] months ended 31 July 20X5], the procedures carried out by us with respect to changes in financial statement items⁴⁷ of the [Company/Guarantor] after 31 July 20X5 have of necessity been even more limited than those carried out for the period up to that date. Up to the Cut-off Date (our work did not extend to the period from the Cut-off Date to the date of this letter), we have made inquiries of the Persons Responsible for

⁴⁶ Line items described as exceptions here should not be listed in 5(a) or (b).

⁴⁷ Independent accountants should consider the guidance in paragraph 45 in determining the appropriateness of which specific line items to provide comfort.

Financial and Accounting Matters as to:

- (a) whether there have been any decreases in [issued share capital, cash and cash equivalents, net current assets or total current assets] or increases in [long term debt or total current liabilities] of the [Group] at the Cut-off Date as compared with the corresponding amounts shown at [31 December 20X4/30 June 20X5] in the [Historical Financial Statements/Interim Financial Statements] included in the Offering Circular; and
 - (b) whether for the period from 1 [January/July] 20X5 up to the Cut-off Date there have been any decreases in [turnover or profit before taxation], or increases in [net interest expense or depreciation of fixed assets] of the [Group] as compared with the corresponding period in the preceding year.
- (7) The Persons Responsible for Financial and Accounting Matters advised us that they were not aware of any increase in [long term debt, total current liabilities, net interest expense or depreciation of fixed assets] or decrease in any of the other listed items described in paragraph (6)(a) or (b) above except that [as at the Cut-off Date as compared with [31 December 20X4/30 June 20X5] [there was an [increase][decrease] in [*state line items*]]/[for the period from 1 [January/July] to the Cut-off Date as compared with the corresponding period in the previous year there was an [increase][decrease] in [*state line items*]]. On the basis of the responses to these inquiries and our reading of the minutes as described in paragraph (1) above, [except for all instances of increases or decreases advised by the Persons Responsible for Financial and Accounting Matters as set out above] nothing has come to our attention that causes us to believe that there was any such increase or decrease.
- (8) We have not performed an audit in respect of any historical financial statements of the [Company/Guarantor] or the Group as of any date or for any period subsequent to 31 December 20X4 in accordance with HKSA's issued by the HKICPA or the standards of any other professional body in any other jurisdiction. Therefore, we are unable to and do not express any opinion on the financial position, results of operations or cash flows of the [Company/Guarantor] or the Group as of any date or for any period subsequent to 31 December 20X4.

This letter is solely for your information and to assist the Addressees in conducting and documenting their due diligence investigation of the affairs of the [Company/Group] in connection with the Issue covered by the Offering Circular and except as permitted in the Arrangement Letter, it is not to be used, circulated, quoted, or otherwise referred to for any other purpose, nor is to be filed with or referred to in whole or in part in the Offering Circular or any other document.

Yours faithfully,

ABC & Co.
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Enclosures: Appendix 1 – Extract of Offering Circular
Appendix 2 - Schedule prepared by the [Company's/Guarantor's] management
[Appendix 3 – Unaudited condensed consolidated financial statements for the period ended [*insert interim balance sheet date reviewed*] and [*insert corresponding date in prior year*]

Appendix 3

Example Bring-down Letter

The following example bring-down letter (that can be used for either a debt or equity offering as appropriate) is provided for illustrative purposes only. It is intended to be used only as a guide to the possible form and content of a bring-down letter that reporting accountants may wish to provide, and is not intended to suggest standard wording to be used in any particular set of circumstances. The contents of the bring-down letter will vary according to the nature of the information in the investment circular, and the procedures agreed between reporting accountants, sponsors, and the issuer. When preparing a bring-down letter, reporting accountants will need to ensure that the letter meets the requirements of this HKSIR.

Date

To: The Directors, [XYZ Limited and ABC Limited]

[Sponsors Limited/Lead Managers]
[Address]

[Other Named Addressee]⁴⁸
[Address]

[Each of the [Hong Kong underwriters/Managers] identified below as an Addressee]⁴⁸

Dear Sirs:

We refer to our letter of [date of previous comfort letter] relating to the [prospectus/Offering Circular] of XYZ Limited (the ("Company"/"Issuer") dated [date] prepared in connection with the [public] offering of [description of security] of the [Company/Issuer]. We reaffirm as of the date hereof (and as though made on the date hereof) all statements made in that letter except that, for purposes of this letter:

1. the reading of minutes described in item 1(a) of that letter has been carried out through [x] 20X5 (the "New Cut-off Date");
2. the references to the unaudited management accounts for the [x] months ended [date] 20X5 and April 20X4, in items 1(b), 2, and 3 and paragraph 4 of that letter are changed to the unaudited management accounts for the [x] months ended [date] 20X5 and [month] 20X4 respectively. [The Directors of the [Company/Issuer] have advised us that no such financial statements as of any date or for any period subsequent to [date] 20X5 were available];
3. the references to [date] 20X5, the period from [date] 20X5 to [date] 20X5 and [date] 20X4 in item 5 of that letter are changed to [date] 20X5, the period from [date] 20X5 to [date] 20X5 and [month] 20X4 respectively; and
4. the references to [date] 20X5 and the cut-off date in item 6 of that letter are changed to [date] 20X5, and the New Cut-Off date respectively.

[Or where no management accounts have been prepared since those referred to in the Comfort Letter, item 2 is replaced as follows and items 3 and 4 deleted :

2. the inquiries covered in item 6 of that letter have been carried out to the New Cut-Off date.]

⁴⁸ Refer to Appendix 1.

5. Our work did not extend to the period from [date] 20X5 to [the closing date] inclusive.

This letter is addressed to [*insert the names of each Named Addressee*] and to each of the [Hong Kong underwriters/Managers] that is an "Addressee" as defined in paragraph 3 of the Arrangement Letter and to the directors of the Company [and the Guarantor]. Other than to those who have validly accepted the Arrangement Letter, we will not accept any responsibility to any party to whom this letter is shown or into whose hands it may come.

This letter is solely for your information and to assist the Addressees in conducting and documenting their due diligence investigation of the affairs of the [Issuer][Group] in connection with the [*describe offering*] covered by the [prospectus/Offering Circular] and except as permitted in the Arrangement Letter it is not to be used, circulated, quoted, or otherwise referred to for any other purpose, nor is to be filed, with or referred to in whole or in part in the [prospectus/Offering Circular] or any other document.

Yours faithfully,

ABC & Co
Certified Public Accountants (Practising) [or Certified Public Accountants]
Hong Kong
Date

Appendix 4

Example Issuer's Representation Letter on Subsequent Changes

The following example representation letter is provided for illustrative purposes only. It is intended to be used only as a guide to the possible form and content of a representation letter, and is not intended to suggest standard wording to be used in any particular set of circumstances.

Where a bring-down letter is provided on subsequent changes, the Issuers representations in respect to matters covered in that letter should also be obtained⁴⁹.

(letterhead of the Issuer)

Date

To [Name of reporting accountants]

Dear Sirs

Proposed Listing of XYZ Limited on the [Main Board/Growth Enterprise Market] of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange")

In connection with the proposed listing of XYZ Limited, we certify to the best of our knowledge and belief that during the period from 31 December 20X4 to date, no events have occurred which have a material effect on the historical financial information or which should be disclosed in order to keep those information from being misleading^{50, 51}.

With respect to the unaudited management accounts as at 30 April 20X5 and 20X4 and for the four-month periods ended 30 April 20X5 and 20X4, we certify to the best of our knowledge and belief that:

- a. such management accounts were prepared in accordance with accounting policies and practices consistent in all material respects with those followed in the preparation of the historical financial information contained in the Prospectus, except as set forth in the Prospectus;
- b. such management accounts present fairly the information purported to be shown thereby;
- c. no material adjustment of such management accounts is required and no adjustments other than those necessary for fair presentation of the results for those periods have been reflected therein.

Also to the best of our knowledge and belief, except in all instances for changes that the Prospectus discloses have occurred or may occur:

- d. at 22 May 20X5 there has been no decrease in the issued share capital, net current assets or total current assets or increase in long-term debt or total current liabilities of the Group, as compared with amounts shown in the 31 December 20X4 balance sheet of the historical financial information;

⁴⁹ Not illustrated in this HKSIR.

⁵⁰ Any exception should be spelled out in the letter

⁵¹ Where the reporting accountants perform a review of interim financial information in order to provide negative assurance on subsequent changes, representations in respect of the interim financial information are also obtained. These representations are not illustrated in this example letter.

COMFORT LETTERS AND DUE DILIGENCE MEETINGS

- e. for the period 1 January 20X5 to 22 May 20X5 there has been no decrease, as compared with the corresponding period in the preceding year, in turnover, profit before taxation or increase in net interest expense or depreciation of fixed assets.

Further, we confirm that:

- f. no audited financial statements of the Group are available as at any date or for any period subsequent to 31 December 20X4, and no management accounts are available as at any date or for any period subsequent to 30 April 20X5;
- g. the minutes of all meetings of the shareholders and the board of directors are entered up to 15 May 20X5 in the minute books, and no such meetings have been held since that date.
- h. We confirm that we are solely responsible for the information in the schedules referred to in tick mark B under the section heading "Selected Financial Information" of your comfort letter dated [Letter Date], with respect to the Prospectus, and that the information was derived from the Group's regularly maintained accounting records and subject to the Group's internal controls over financial reporting.

Yours faithfully

For and on behalf of XYZ Limited

[name]
Managing Director

[name]
Finance Director

Appendix 5A

Example Written Oral Due Diligence Acknowledgement

In accordance with paragraph 61 of this HKSIR, before attending a due diligence meeting, reporting accountants should establish a written understanding and agreement as to the terms of the engagement with the issuer and the sponsor(s), manager(s) or, as the case may be, arranger(s)/dealer(s) (and, if applicable, other parties who have due diligence obligations and who will be a "named addressee" of the arrangement letter) as to the basis on which the reporting accountants agree to attend the due diligence meeting. This can be achieved by having the arrangement letter signed and executed prior to the due diligence meeting or having a master agreement with the relevant financial intermediaries (see Appendix 5B for an example of such master agreement). However, in the event that the arrangement letter has not been executed and the due diligence meeting transaction is not otherwise governed by a master agreement, the reporting accountants should obtain a written acknowledgement from the sponsor(s), manager(s) or, as the case may be, arranger(s)/dealer(s) and, if applicable, each of the other named addressees of the arrangement letter, as to the basis on which the reporting accountants agree to attend the due diligence meeting before the signing of the arrangement letter. Reporting accountants are reminded that this written acknowledgement does not replace the execution of the arrangement letter which may be at a later date after the due diligence meeting.

An example of such acknowledgement is as follows:

[Legal name of institution], as the [sponsor]/[manager]/[arranger]/[dealer] of the proposed [[initial public offering]/[programme establishment] of [XYZ Limited] (the "[Proposed Offering]/[Programme Establishment]"), acknowledges that:

- (i) we are aware of the due diligence guidance [included in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited which will be followed by us in connection with the [Proposed Offering]/[Programme Establishment]] / [issued by the International Capital Market Association from time to time, which will be followed by us in connection with the [Proposed Offering]/[Programme Establishment];
- (ii) the oral due diligence discussions that involve [Reporting Accountants] in connection with the [Proposed Offering]/[Programme Establishment] are those contemplated by paragraph 24 of the form of arrangement letter set out in Appendix 1 of Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised) (the "HKSIR400 AL Form") and will be governed by the terms of such paragraph 24 (with therein [legal name of institution] referred to as "the Addressee" and [Reporting Accountants] referred to as "we, our and us");
- (iii) if we decide to proceed with and participate in the [Proposed Offering]/[Programme Establishment], the arrangement letter to be entered into between [XYZ Limited], us and [Reporting Accountants] in connection with the [Proposed Offering]/[Programme Establishment] (the "Arrangement Letter") will be based on the HKSIR400 AL Form, with those amendments agreed by the parties thereto as necessary to reflect the particulars of the [Proposed Offering]/[Programme Establishment].

This acknowledgment will be superseded by the Arrangement Letter upon the signing of the Arrangement Letter.

Appendix 5B

Example Master Agreement Regarding Due Diligence Meetings

This agreement has been developed in consultation with stakeholders. As explained in paragraph 62 of this HKSIR, reporting accountants may enter into a master agreement with the sponsor(s), manager(s) or, as the case may be, arranger(s)/dealer(s) (and, if applicable, other parties who have due diligence obligations and who will be a "named addressee" of the arrangement letter) to govern the basis on which the reporting accountants agree to attend the due diligence meeting prior to the execution of the arrangement letter. Execution of this master agreement, however, does not replace the requisite execution of the arrangement letter among the issuer, the reporting accountants and the relevant financial intermediaries. Reporting accountants are reminded to adopt appropriate means to satisfy themselves that proper master agreements are executed with the financial intermediaries attending the due diligence meeting. In instances where no master agreement is in place for some or all of the financial intermediaries attending the due diligence meeting, reporting accountants may consider the use of a written acknowledgement as explained in paragraph 61 of this HKSIR from the relevant financial intermediaries as appropriate.

This Agreement only applies in the context of reporting accountants issuing a comfort letter or taking part in a due diligence meeting with sponsors, global coordinators, bookrunners, lead managers or other managing underwriters for an offering of securities under the Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised), Comfort Letters and Due Diligence Meetings issued by the Hong Kong Institute of Certified Public Accountants.

Agreement Regarding Oral Due Diligence

THIS AGREEMENT is between the undersigned manager (the "**Manager**") who may act as sponsor, global coordinator, bookrunner, lead manager and/or manager and the undersigned accounting firm, including its partners, principals, employees and subcontractors, collectively, (the "**Accounting Firm**"), and is made as of the date set forth above the signature blocks below (the "**Effective Date**").

Section 1. Agreement regarding discussions.

- (a) The Manager and the Accounting Firm each agrees that the standards on Due Diligence Meetings set out in paragraphs 59-68 of the Hong Kong Standard on Investment Circular Reporting Engagements 400 (Revised) ("**HKSIR 400**") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") apply to oral due diligence discussions between the Manager and the Accounting Firm occurring on or after the Effective Date and until the termination of this Agreement, in each offering of securities *provided, however*, that (i) this Agreement shall not apply if either party gives written notice to the other party prior to the commencement of oral due diligence discussions for a specific offering that the Agreement shall not apply to those oral discussions for that offering, or (ii) this Agreement shall cease to apply when the parties enter into an arrangement letter for a specific offering substantially in the form provided as Appendix I of HKSIR 400 (or as otherwise agreed between the Manager and the Accounting Firm). Except to the extent the context requires otherwise, expressions defined in HKSIR 400 shall have the same meanings in this Agreement.
- (b) In consideration for the Accounting Firm orally responding to questions from the Manager in the course of due diligence, the Manager agrees that the Accounting Firm shall have no liability to the Manager in contract or in tort (including negligence) for its oral answers to such questions other than for an oral statement known to be false or misleading when made and made with intent to deceive. Subject to the above, nothing in this paragraph shall prejudice the Manager's ability to rely on a non-recourse basis (meaning without any liability on the Accounting Firm's part except for oral statements known to be false or misleading when made and made with intent to deceive) on any comments the Accounting Firm may provide orally, either in the context of establishing or seeking to establish any due diligence defence in connection with any court, arbitral, regulatory or administrative proceedings or otherwise for the purposes of resolving either actual or potential proceedings, investigations, claims or disputes in respect of any offering circular prepared in

connection with an issuance of securities or otherwise in connection with any issuance of securities. This paragraph does not otherwise affect any claim or defense that the parties may have vis-à-vis against each other based on statements or conduct other than in oral due diligence discussions. This paragraph also does not (i) affect any claim or defense that the parties have vis-à-vis against third parties, or (ii) affect the ability of the Manager to use or refer to the Accounting Firm's oral statements in asserting claims against or defending against claims by third parties.

Section 2. Termination.

Either party may terminate this Agreement at any time with immediate effect upon written notice to the other party. Any such termination shall be prospective only and shall not apply to any discussions that have occurred prior to such termination, as to which this Agreement shall remain in full force and effect.

Section 3. Notices.

Any notice hereunder by one party shall be sent to the other at its address set forth below its signature to this Agreement. Any notice shall be effective when received.

Section 4. Counterparts.

This Agreement may be executed in counterparts, which together shall be considered one original.

Section 5. Severability.

If any provision of this Agreement is found by a court to be unenforceable, such provision shall not affect the other provisions, but such unenforceable provision shall be deemed modified to the extent necessary to render it enforceable, preserving to the fullest extent permissible the intent of the parties set forth herein.

Section 6. Governing Law.

This Agreement shall be governed by and construed in accordance with the laws of Hong Kong. The Courts of Hong Kong shall have exclusive jurisdiction in relation to any claim, dispute or difference concerning this Agreement or any matter arising from it.

Section 7.

A person or entity that is not a party to this Agreement shall have no right to enforce any of its terms under the Contracts (Rights of Third Parties) Ordinance (Cap. 623, Laws of Hong Kong).

[Signature Page Follows]

IN WITNESS WHEREOF, the parties have executed this Agreement as of the Effective Date set forth below.

Effective Date: [●] 2016

Manager:

Accounting Firm:

By: _____

By: _____

Name:

Name:

Title:

Title:

Address for Notices:

Address for Notices:

- **Attention:**
- **Facsimile:**
- **Telephone:**

- **Attention:**
- **Facsimile:**
- **Telephone:**

Appendix 6

Examples of Questions Commonly Asked in Due Diligence Meetings and Comments on the Reporting Accountants' Response

The following examples are to be read in conjunction with paragraphs 59 – 68 of HKSIR 400 (Revised).

Usually, the reporting accountants' response to questions asked by the sponsor in a due diligence meeting can be brief. The comments on the questions cited below are more detailed than the responses that would usually be required, and are intended as general guidance about matters the reporting accountants would normally consider in determining a response. The comments are not intended as illustrations of the answer that would be appropriate in every situation.

- A. Questions the reporting accountants are usually able to answer (A1-A13)
 - B. Questions to which the reporting accountants are unable to respond in the terms in which they are asked (B1-B5)
 - C. Questions properly addressed to management (C1-C3)
- A. Questions the reporting accountants are usually able to answer (A1-A13)**

Following are a number of questions to which the reporting accountants are usually able to respond, with comments as to the response that might be appropriate.

Question A1 How long have you (or your firm) been the reporting accountants (or auditor) of the issuer?

Response considerations This question demands a factual answer.

Question A2 Describe the nature and scope of your examination of the issuer's historical financial information included in the investment circular. Were any limitations imposed upon the scope of your examination by management of the issuer or others?

Response considerations The reporting accountants would make it clear that the examination covered only the historical financial information for the dates and periods referred to in the accountants' report.

The scope of an examination is set out in the accountants' report:

- An examination is conducted in accordance with [Hong Kong Standard on Investment Circular Reporting Engagements 200 (HKSIR 200)], which requires that the reporting accountants plan and perform the examination to obtain reasonable assurance whether the historical financial information is free of material misstatement.
- An examination includes examining, on a test basis, evidence supporting the amounts and disclosures in the historical financial information.
- An examination also includes assessing the accounting policies used and significant estimates made by management.

In the normal case, the scope of the examination would enable the reporting accountants to express an opinion without reservation on the historical financial information. If there was any limitation imposed on the scope of the examination, the matter would be dealt with in the accountants' report.

The reporting accountants might be willing to describe the examination procedures performed on certain financial information elements in forming an opinion on the historical financial information as a whole; however, the reporting accountants would make it clear that no assurance is provided on these specific items beyond that conveyed by the historical financial information.

Question A3 **Management has provided us with a list of pending litigation, commitments, contingent liabilities, guarantees, and any indebtedness or other off-balance sheet items (a list would be provided to the reporting accountants). In the course of your examination, did you discuss with management or otherwise identify any other items of the same type not included on this list that exceed (an amount provided by the sponsor)?**

Response considerations The reporting accountants could reply that, based on the procedures performed, including discussions with management, no other items of the types mentioned were identified, or discuss any such items that were so identified. The reporting accountants may wish to point out that reporting accountants must rely to a large extent on management, and sometimes on legal counsel, in identifying outstanding contingencies.

If the reporting accountants wish to ensure that the sponsor understands the procedures reporting accountants apply to contingencies, commitments and other such items, the procedures that are performed in gathering evidence to determine whether any such contingent items require accrual or disclosure in the historical financial information could be outlined, such as:

- review of the issuer's written summary of known and threatened claims;
- discussion with management of contingencies, commitments, and other obligations;
- discussion with the issuer's general counsel of all litigation and threatened litigation of which the issuer is aware, including litigation and claims or threatened claims covered by insurance;
- search for unrecorded liabilities by a review of disbursements subsequent to period-end and open invoices;
- receipt of written confirmation of obligations from third parties such as banks and lenders;
- receipt of written representations from management;
- review of events which have occurred between the date of the historical financial information and the date of the accountants' report; and
- review of accounting treatment and disclosure in the historical financial information.

Question A4 **Management has informed us that it does not plan to change any of the significant accounting policies as set forth in note 1 to the historical financial information of the issuer. Has management informed you, or had any discussions with you, regarding any change in the accounting policies?**

Response considerations The reporting accountants may properly respond to these questions. If the reporting accountants are aware of any recent or pending changes in accounting standards or regulatory requirements that would make a change in the issuer's accounting policies necessary or desirable in the future, attention would be drawn to such recommendations or requirements.

Question A5 **Management has informed us that it does not plan to have any material potential write-downs in the current year. Has management informed you, or had any discussions with you, regarding any potential write-downs in connection with the examination of historical financial information?**

Response considerations Normally the reporting accountants can answer this question without difficulty. The reporting accountants may wish to convey to the sponsor that reporting accountants and management usually have an ongoing dialogue with respect to potential future issues, and may choose to identify some of the accounting matters on which discussions have taken place.

The reporting accountants may also wish to refer the sponsor to any measurement uncertainty disclosures in the historical financial information, in particular any disclosures regarding historical financial information items where there is a reasonable possibility that the recognized amount of the historical financial information item could change by a material amount in the near term.

Question A6 **Management has informed us that it is not aware of any facts that would give rise to any unusual items appearing in the issuer's historical financial information. Has management informed you, or had any discussions with you, regarding any such items?**

Response considerations The reporting accountants can answer this question without difficulty. However, unusual items do not have a precise meaning in accounting terms. To avoid misunderstanding, it is therefore important that the sponsor define what is meant by "unusual" items.

Question A7 **How often do you meet with the issuer's audit committee or board of directors, and what are the procedures at and nature of such meetings?**

Response considerations The reporting accountants would describe the frequency of meetings with the audit committee and, if applicable, the board of directors.

Meetings with the audit committee would generally encompass a review and approval by the committee of the reporting accountants' examination plan and discussion of accounting and financial presentation issues. The committee would generally meet to review the historical financial information and recommend its approval by the board of directors. The reporting accountants would indicate whether meetings of the committee were held at the request of the committee or the reporting accountants.

Meetings with the board are likely to be less common, and would generally be related to a special assignment undertaken by the reporting accountants, such as delivering a special report, or discussing financing alternatives.

Question A8 **Do you have full and open access to all materials which you consider necessary to enable you to perform your examination?**

Response considerations It would be expected that the reporting accountants would have full and open access to all necessary materials.

Question A9 **Discuss your relationship with the issuer's management. Have you had any disagreements with management that have not been resolved to your satisfaction?**

Response considerations Generally the reporting accountants would be in a position to state that management was cooperative, and provided all of the information and explanations that the reporting accountants required. The reporting accountants may choose to point out that in the course of normal communications with the issuer, the reporting accountants frequently meet with management to discuss emerging accounting issues, and have always been able to resolve the issues with senior management satisfactorily. Otherwise, the reporting accountants would have included a reservation in the accountants' report.

Question A10 **Have there been any significant weaknesses in internal control that you have identified during the course of your examination of the historical financial information that were communicated to the audit committee or management committee that, to the best of your knowledge, have not been acted upon by management?**

Response considerations The reporting accountants would state whether or not significant weaknesses in internal control have been reported to the issuer, and might identify the areas of weakness. In the course of the engagement related to the investment circular, the reporting accountants will have updated knowledge of the internal controls, and may be in a position to comment on changes that have been effected since the time when the weaknesses were reported. However, the question of management's actions would properly be addressed to, and answered by, management. The reporting accountants are not normally in a position to comment

on the effectiveness of any action that has been taken by management to address the internal control weaknesses that have been reported.

In responding to this question, the reporting accountants may also wish to outline the limited nature of the review of internal controls in connection with the examination of the historical financial information, to ensure that there is no misunderstanding by the sponsor of the nature and extent of the reporting accountants' review of internal controls and the type of weakness that the reporting accountants would consider to be "significant".

Question A11 **Other than as disclosed in the investment circular, are you aware of any related party transactions involving the issuer that require disclosure in the historical financial information under HKFRSs?**

Response considerations The reporting accountants will likely be able to answer this question in the negative, but should be concerned about any possible related party transactions subsequent to the most recent balance sheet date that would require financial statement disclosure in the track record period.

If the reporting accountants wish to be sure that the sponsor understands the procedures reporting accountants apply to identify significant related party transactions, the procedures applied may be outlined, such as the following:

- preparation of a list of directors, officers and related entities, to be consulted by audit staff when they are reviewing the issuer's transactions;
- receipt of written representations from management regarding related party transactions; and
- review of material contracts entered into during the track record period.

Question A12 **Please discuss the most significant areas of audit risk you have encountered in respect of the issuer and how you gained comfort in these areas.**

Response considerations The reporting accountants might identify the most critical audit areas and issues discussed with the audit committee in the years and periods covered by the historical financial information. However, it is important that the reporting accountants explain that the assessment of audit risk is concerned with the fairness of presentation of the historical financial information in accordance with generally accepted accounting principles, and should not be taken to provide comfort on individual elements within the historical financial information, or on the absence of other significant business risks which, because of their nature, were not considered by the reporting accountants to constitute areas of significant audit risk.

Question A13 **Is there anything of which you are aware that would inhibit your delivery, in accordance with HKSIRs, and the terms of your engagement, of an unqualified report on the historical financial information, consent letters, and the comfort letter to the sponsor?**

Response considerations The reporting accountants would be careful to explain any development (such as a delay in the issuer's providing necessary information, or an unresolved problem regarding disclosure in the investment circular) which might delay the completion of the reporting accountants' work.

B. Questions to which the reporting accountants are unable to respond in the terms in which they are asked (B1-B5)

The sponsor may ask questions to which the reporting accountants are unable to respond in the terms in which they are asked. In such circumstances, the reporting accountants may wish to respond by explaining the reasons why they are unable to provide the information requested. Some examples of these types of questions, together with a commentary on how the reporting accountants might respond to the question, are set out below.

Question B1 **Based on your reading of the prospectus, do you have any reason to believe that it is not fairly presented? (Or, Are you aware of any other matters that should be disclosed in the prospectus? Or, Are there any other questions that we should have asked in completing our due diligence investigation?)**

Response considerations There is no accepted standard by which the reporting accountants can judge whether a prospectus is fairly presented. Professional standards require that the reporting accountants read the prospectus with a view to assessing the overall impression given by the document, having regard to the purposes for which it has been prepared, as well as considering whether there are any inconsistencies between their report and the information in the rest of the document.

These procedures would not necessarily disclose material misstatements or omissions in the information included in the investment circular. Accordingly, except for the historical financial information included in the prospectus, the reporting accountants are not in a position to make any representations as to completeness or adequacy of disclosures in the prospectus.

The sponsor applies many other considerations in forming an opinion as to what constitutes a fair presentation, but the reporting accountants have no way of knowing what would be of interest to the sponsor. As well, a great deal of the information in a prospectus (and, perhaps, significant omissions) is outside of the knowledge of the reporting accountants.

Question B2 **Are you aware of any matters that may directly or indirectly affect the value of the securities offered under the prospectus?**

Response considerations The reporting accountants are not competent to express a view as to matters that may affect the value of securities. This subject is within the province of a securities dealer such as an underwriter.

Question B3 **Are provisions for losses (e.g., bad debts, inventory obsolescence) adequate?**

Response considerations An examination is designed to assess the presentation of the historical financial information as a whole, and not to provide assurance on individual financial information items. The reporting accountants determine materiality by reference to the historical financial information taken as a whole. The only appropriate answer to the question is that the reporting accountants would not have given an opinion without reservation if in the reporting accountants' opinion the historical financial information did not give a true and fair view. The reporting accountants may be willing to describe the examination procedures performed in order to conclude on the adequacy of loss provisions in the context of the examination of the historical financial information as a whole.

Question B4 **Are the accounting policies and methods used by the issuer appropriate? Please comment on the general fairness (adequacy) of the issuer's accounting policies and the presentation of its historical financial information. Are these accounting policies consistent with the majority of enterprises in the same business as the issuer? Would you describe the financial reporting policies of the issuer as conservative/liberal relative to other companies in the industry?**

Response considerations Assuming that the reporting accountants have expressed an opinion without reservation on the issuer's historical financial information, it would ordinarily be possible to confirm that the accounting policies and methods used by the issuer are appropriate.

The reporting accountants would advise the sponsor that management has the responsibility for the accurate recording of transactions and the preparation of historical financial information in accordance with generally accepted accounting principles. This responsibility includes the selection and application of accounting policies. An examination of the historical financial information does not relieve management of its responsibilities. The reporting accountants may make suggestions as to the form or content of the historical financial information, and ensure that the accounting principles and policies are in accordance with generally accepted accounting principles; however, the reporting accountants are not required to assess the preferability of an accounting principle or method when acceptable alternatives exist. The reporting accountants would also consider discussing the alternative accounting policies available under generally accepted accounting principles, generally, and in the issuer's industry.

From time to time, the reporting accountants may discuss with the audit committee the quality of various accounting policies, and express a view as to the relative merits of differing methods. The reporting accountants may wish to refer to these discussions. However, in dealing with a third party such as a sponsor, the reporting accountants would be very cautious about answering any question about the relative conservatism of the issuer's accounting policies, as any answer is likely to be based on the reporting accountants' personal experience, and not on any generally accepted criteria.

Question B5 **What was the extent of your involvement in the preparation of the historical financial information and the other financial information in the investment circular?**

Response considerations The responsibility for the preparation of historical financial information, and also of investment circulars, rests with management of the entity. It is the reporting accountants' responsibility to perform an examination of the historical financial information prepared by management.

C. Questions properly addressed to management (C1-C3)

The sponsor may ask questions that are properly addressed to management, rather than the reporting accountants.

Question C1 **Is the historical financial information for the periods contained in the prospectus of the issuer accurate in all material respects?**

Response considerations The reporting accountants would remind the sponsor that the historical financial information is the responsibility of the issuer's management and that this question is best answered by management. The reporting accountants would explain that the responsibility as reporting accountants is to express an opinion on the historical financial information based on an examination. As noted in the accountants' report, it is the reporting accountants' opinion that the historical financial information included in the investment circular gives a true and fair view of the financial position of the company as at (dates) and the results of its operations and its cash flows for the years then ended.

Question C2 What is the reason for the increase / decrease in (certain historical financial information items) in 20X5 as compared to 20X4?

Response considerations The reporting accountants' responsibility is to form an opinion as to whether the historical financial information gives a true and fair view. A change in the recorded amount of an asset, liability, revenue or expense item from period to period is normally the result of numerous transactions. Management has the responsibility of operating the business, has first-hand knowledge of these transactions, and is in a position to analyse changes. Therefore, any questions as to the reasons for a change in a historical financial information item would be addressed to management, and responded to by management. The reporting accountants could comment on management's response only if a separate assurance engagement was carried out on the matters in question.

Question C3 Please provide us with an assessment (comment on the adequacy) of the Company's internal control systems. Are you satisfied that internal controls are in place to prepare adequate financial information? Have you relied upon internal controls in performing your examination?

Response considerations The reporting accountants would advise the sponsor that this question can only be answered by the issuer's management, because responsibility for ensuring the adequacy of internal control is part of the issuer's management's overall responsibility.

The reporting accountants may respond by stating that management's internal control objectives go beyond financial information objectives. Internal controls relevant to the examination comprise those policies and procedures established and maintained by management that relate to specific financial information assertions.

The reporting accountants would explain that the reporting accountants have a responsibility to obtain a sufficient understanding of internal control to plan the examination. This understanding includes knowledge about the design of policies and procedures and whether they have been implemented, but does not extend to evaluating the operating effectiveness of these policies and procedures. The reporting accountants only evaluate, and test, those internal controls on which it is planned to rely on during the examination. Accordingly, an opinion in an accountants' report provides no assurance as to the efficiency or effectiveness with which operations, including internal controls, have been conducted.

The reporting accountants may then wish to discuss the approach adopted in performing the examination including reliance on internal controls. The reporting accountants may also wish to point out that these controls would not normally include all of the controls over the preparation of the historical financial information; accordingly, the reporting accountants are not in a position to provide any assurance regarding such controls.

Notwithstanding this, the reporting accountants would consider informing the sponsor as to any significant weaknesses in the issuer's internal control structure which were reported to management.