



Room 525, 5/F., Prince's Building, Central, Hong Kong
Telephone: 2521 1160, 2521 1169 Facsimile: 2868 5035
Email: info@hkab.org.hk Web: www.hkab.org.hk

香港中環太子大廈5樓525室
電話：2521 1160, 2521 1169 圖文傳真：2868 5035
電郵：info@hkab.org.hk 網址：www.hkab.org.hk

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By post and email: commentletters@hkicpa.org.hk

Mr. Simon Riley
Director, Standard Setting
Hong Kong Institute of Certified Public Accountants
37th Floor, Wu Chung House
213 Queen's Road East
Wanchai
Hong Kong

Dear Mr. Riley

IASB's Discussion Paper on Review of the Conceptual Framework for Financial Reporting

We refer to your letter dated 4 October 2013 inviting our comments on the International Accounting Standards Board's Discussion Paper on Review of the Conceptual Framework for Financial Reporting.

Our comments on the specific questions raised in the discussion paper are attached. Should you have any questions, please do not hesitate to contact our Assistant Manager, Mr. Timothy Tam, at 2526 6080.

Yours sincerely

Boey Wong
Secretary

Enc.

Chairman Standard Chartered Bank (Hong Kong) Ltd
Vice Chairmen Bank of China (Hong Kong) Ltd
The Hongkong and Shanghai Banking Corporation Ltd
Secretary Boey Wong

主席 渣打銀行（香港）有限公司
副主席 中國銀行（香港）有限公司
香港上海匯豐銀行有限公司
秘書 黃凱儀

**Responses of the Hong Kong Association of Banks (“HKAB”) to Specific Questions
in the International Accounting Standards Board’s Discussion Paper of
Conceptual Framework for Financial Reporting**

Section 1 Introduction

Question 1

Paragraphs 1.25–1.33 of the set out the proposed purpose and status of the Conceptual Framework. The IASB’s preliminary views are that:

*(a) the primary purpose of the revised Conceptual Framework is to assist the IASB by identifying concepts that it will use consistently when developing and revising IFRSs; and
(b) in rare cases, in order to meet the overall objective of financial reporting, the IASB may decide to issue a new or revised Standard that conflicts with an aspect of the Conceptual Framework. If this happens the IASB would describe the departure from the Conceptual Framework, and the reasons for that departure, in the Basis for Conclusions on that Standard.*

Do you agree with these preliminary views? Why or why not?

We generally agree with the proposal (a) on the purpose of the Conceptual Framework (“CF”). However, we do not see benefit of limiting the use of a certain parts of CF by IASB only per paragraph 1.29. The preparers and users of IFRS look to CF where there is no IFRS that directly address a particular transaction to understand and interpret IFRS. As to (b), we would like IASB to identify the existing conflicts and further provide explanations.

Section 2 Elements of financial statements

Question 2

The definitions of an asset and a liability are discussed in paragraphs 2.6–2.16 of the DP. The IASB proposes the following definitions:

*(a) an asset is a present economic resource controlled by the entity as a result of past events.
(b) a liability is a present obligation of the entity to transfer an economic resource as a result of past events.
(c) an economic resource is a right, or other source of value, that is capable of producing economic benefits.*

Do you agree with these definitions? Why or why not? If you do not agree, what changes do you suggest, and why?

We generally agree. See the comment on Question 3 below.

Question 3

Whether uncertainty should play any role in the definitions of an asset and a liability, and in the recognition criteria for assets and liabilities, is discussed in paragraphs 2.17–2.36 of the DP. The IASB’s preliminary views are that:

- (a) the definitions of assets and liabilities should not retain the notion that an inflow or outflow is ‘expected’. An asset must be capable of producing economic benefits. A liability must be capable of resulting in a transfer of economic resources.*
- (b) the Conceptual Framework should not set a probability threshold for the rare cases in which it is uncertain whether an asset or a liability exists. If there could be significant uncertainty about whether a particular type of asset or liability exists, the IASB would decide how to deal with that uncertainty when it develops or revises a Standard on that type of asset or liability.*
- (c) the recognition criteria should not retain the existing reference to probability.*

Do you agree? Why or why not? If you do not agree, what do you suggest, and why?

We generally agree. The probability threshold should not be included in the definitions of assets and liabilities. Further guidance on the probability should be made a part of recognition criteria in corresponding asset or liability Standards. We do believe the recognition criteria should retain the reference to probability. However, CF should provide further guidance to explain when a recognition is not likely due to uncertainty that is “significant”.

Question 4

Elements for the statement(s) of profit or loss and OCI (income and expense), statement of cash flows (cash receipts and cash payments) and statement of changes in equity (contributions to equity, distributions of equity and transfers between classes of equity) are briefly discussed in paragraphs 2.37–2.52 of the Discussion Paper.

Do you have any comments on these items? Would it be helpful for the Conceptual Framework to identify them as elements of financial statements?

We have no comments.

Section 3 Additional guidance to support the asset and liability definitions

Question 5

Constructive obligations are discussed in paragraphs 3.39–3.62 of the DP. The discussion considers the possibility of narrowing the definition of a liability to include only obligations that are enforceable by legal or equivalent means. However, the IASB tentatively favours retaining the existing definition, which encompasses both legal and constructive obligations – and adding more guidance to help distinguish constructive obligations from

economic compulsion. The guidance would clarify the matters listed in paragraph 3.50 of the DP.

Do you agree with this preliminary view? Why or why not?

We agree that IASB should retain the existing definition of liability. The current definition which includes both legal and constructive obligations has been consistently used and we see no significant benefit from further expansion or refinement of the definition.

Question 6

The meaning of ‘present’ in the definition of a liability is discussed in paragraphs 3.63–3.97 of the DP. A present obligation arises from past events. An obligation can be viewed as having arisen from past events if the amount of the liability will be determined by reference to benefits received, or activities conducted, by the entity before the end of the reporting period. However, it is unclear whether such past events are sufficient to create a present obligation if any requirement to transfer an economic resource remains conditional on the entity’s future actions. Three different views on which the IASB could develop guidance for the Conceptual Framework are put forward:

- (a) View 1: a present obligation must have arisen from past events and be strictly unconditional. An entity does not have a present obligation if it could, at least in theory, avoid the transfer through its future actions.*
- (b) View 2: a present obligation must have arisen from past events and be practically unconditional. An obligation is practically unconditional if the entity does not have the practical ability to avoid the transfer through its future actions.*
- (c) View 3: a present obligation must have arisen from past events, but may be conditional on the entity’s future actions.*

The IASB has tentatively rejected View 1. However, it has not reached a preliminary view in favour of View 2 or View 3.

Which of these views (or any other view on when a present obligation comes into existence) do you support? Please give reasons.

We support View 2. We believe View 3 would create wider diversity in application due to the ambiguity. View 2, however, should be expanded to provide further guidance to identify the types of condition that an entity could avoid so that we could identify the situations when “obligations that depend on an entity’s future actions” arise.

Question 7

Do you have comments on any of the other guidance proposed in this section of the DP to support the asset and liability definitions?

We have no further comments.

Section 4 Recognition and derecognition

Question 8

Paragraphs 4.1–4.27 of the DP discuss recognition criteria. In the IASB’s preliminary view, an entity should recognise all its assets and liabilities, unless the IASB decides when developing or revising a particular standard that an entity need not, or should not, recognise an asset or a liability because:

- (a) recognising the asset (or the liability) would provide users of financial statements with information that is not relevant, or is not sufficiently relevant to justify the cost; or*
- (b) no measure of the asset (or the liability) would result in a faithful representation of both the asset (or the liability) and the changes in the asset (or the liability), even if all necessary descriptions and explanations are disclosed.*

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We agree based on the view expressed in (b).

Question 9

In the IASB’s preliminary view, as set out in paragraphs 4.28–4.51 of the, an entity should derecognise an asset or a liability when it no longer meets the recognition criteria. (This is the control approach described in paragraph 4.36(a)). However, if the entity retains a component of an asset or a liability, the IASB should determine when developing or revising particular Standards how the entity would best portray the changes that resulted from the transaction. Possible approaches include:

- (a) enhanced disclosure;*
- (b) presenting any rights or obligations retained on a line item different from the line item that was used for the original rights or obligations, to highlight the greater concentration of risk; or*
- (c) continuing to recognise the original asset or liability and treating the proceeds received or paid for the transfer as a loan received or granted.*

Do you agree? Why or why not? If you do not agree, what changes do you suggest, and why?

We agree that an asset or a liability should be derecognised when it no longer meets the recognition criteria. We also agree that when an entity retains a component of an asset or a liability, further guidance should be provided by the IASB through issuance of new or revised Standards. Further guidance should also be provided to distinguish modification from derecognition of asset or liability.

Section 5 Definition of equity and distinction between liabilities and equity instruments

Question 10

The definition of equity, the measurement and presentation of different classes of equity, and how to distinguish liabilities from equity instruments are discussed in paragraphs 5.1-5.59 of the DP. In the IASB's preliminary view:

(a) the Conceptual Framework should retain the existing definition of equity as the residual interest in the assets of the entity after deducting all its liabilities.

(b) the Conceptual Framework should state that the IASB should use the definition of a liability to distinguish liabilities from equity instruments. Two consequences of this are:

(i) obligations to issue equity instruments are not liabilities; and

(ii) obligations that will arise only on liquidation of the reporting entity are not liabilities (see paragraph 3.89(a) of the DP).

(c) an entity should:

(i) at the end of each reporting period update the measure of each class of equity claim. The IASB would determine when developing or revising particular Standards whether that measure would be a direct measure or an allocation of total equity.

(ii) recognise updates to those measures in the statement of changes in equity as a transfer of wealth between classes of equity claim.

(d) if an entity has issued no equity instruments, it may be appropriate to treat the most subordinated class of instruments as if it were an equity claim, with suitable disclosure. Identifying whether to use such an approach, and if so, when, would still be a decision for the IASB to take in developing or revising particular Standards.

Do you agree? Why or why not? If you do not agree, what changes do you suggest and why?

We agree with the proposals which will provide clarity and ensure consistent application to distinguish equity from liabilities.

Section 6 Measurement

Question 11

How the objective of financial reporting and the qualitative characteristics of useful financial information affect measurement is discussed in paragraphs 6.6–6.35 of the DP. The IASB's preliminary views are that:

(a) the objective of measurement is to contribute to the faithful representation of relevant information about:

(i) the resources of the entity, claims against the entity and changes in resources and claims; and

(ii) how efficiently and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.

(b) a single measurement basis for all assets and liabilities may not provide the most relevant information for users of financial statements;

(c) when selecting the measurement to use for a particular item, the IASB should consider what information that measurement will produce in both the statement of financial position and the statement(s) of profit or loss and OCI;

(d) the relevance of a particular measurement will depend on how investors, creditors and other lenders are likely to assess how an asset or a liability of that type will contribute to future cash flows. Consequently, the selection of a measurement:

(i) for a particular asset should depend on how that asset contributes to future cash flows; and

(ii) for a particular liability should depend on how the entity will settle or fulfil that liability.

(e) the number of different measurements used should be the smallest number necessary to provide relevant information. Unnecessary measurement changes should be avoided and necessary measurement changes should be explained; and

(f) the benefits of a particular measurement to users of financial statements need to be sufficient to justify the cost.

Do you agree with these preliminary views? Why or why not? If you disagree, what alternative approach to deciding how to measure an asset or a liability would you support?

We agree with the preliminary views that CF to provide guidance on the measurement and define object of measurement, because it is fundamental.

Question 12

The IASB's preliminary views set out in Question 11 have implications for the subsequent measurement of assets, as discussed in paragraphs 6.73 – 6.96 of the DP. The IASB's preliminary views are that:

(a) if assets contribute indirectly to future cash flows through use or are used in combination with other assets to generate cash flows, cost-based measurements normally provide information that is more relevant and understandable than current market prices.

(b) if assets contribute directly to future cash flows by being sold, a current exit price is likely to be relevant.

(c) if financial assets have insignificant variability in contractual cash flows, and are held for collection, a cost-based measurement is likely to provide relevant information.

(d) if an entity charges for the use of assets, the relevance of a particular measure of those assets will depend on the significance of the individual asset to the entity.

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

We agree with the preliminary views and proposed guidance, because it will provide further clarity.

Question 13

The implications of the IASB's preliminary views for the subsequent measurement of liabilities are discussed in paragraphs 6.97–6.109 of the DP. The IASB's preliminary views are that:

- (a) cash-flow-based measurements are likely to be the only viable measurement for liabilities without stated terms.*
- (b) a cost-based measurement will normally provide the most relevant information about:
 - (i) liabilities that will be settled according to their terms; and*
 - (ii) contractual obligations for services (performance obligations).**
- (c) current market prices are likely to provide the most relevant information about liabilities that will be transferred.*

Do you agree with these preliminary views and the proposed guidance in these paragraphs? Why or why not? If you disagree, please describe what alternative approach you would support.

We agree with the preliminary views and proposed guidance which provide further clarity.

Question 14

Paragraph 6.19 of the DP states the IASB's preliminary view that for some financial assets and financial liabilities (for example, derivatives), basing measurement on the way in which the asset contributes to future cash flows, or the way in which the liability is settled or fulfilled, may not provide information that is useful when assessing prospects for future cash flows. For example, cost-based information about financial assets that are held for collection or financial liabilities that are settled according to their terms may not provide information that is useful when assessing prospects for future cash flows:

- (a) if the ultimate cash flows are not closely linked to the original cost;*
- (b) if, because of significant variability in contractual cash flows, cost-based measurement techniques may not work because they would be unable to simply allocate interest payments over the life of such financial assets or financial liabilities; or*
- (c) if changes in market factors have a disproportionate effect on the value of the asset or the liability (i.e. the asset or the liability is highly leveraged).*

Do you agree with this preliminary view? Why or why not?

We agree with the preliminary view which provides guidance on the use of market price which could be more appropriate measurement method over the cost.

Question 15

Do you have any further comments on the discussion of measurement in this section?

We have no further comments.

Section 7 Presentation and disclosure

Question 16

This section sets out the IASB's preliminary views about the scope and content of presentation and disclosure guidance that should be included in the Conceptual Framework. In developing its preliminary views, the IASB has been influenced by two main factors:

(a) the primary purpose of the Conceptual Framework, which is to assist the IASB in developing and revising Standards (see Section 1); and

(b) other work that the IASB intends to undertake in the area of disclosure (see paragraphs 7.6–7.8 of the DP), including:

(i) a research project involving IAS 1, IAS 7 and IAS 8, as well as a review of feedback received on the Financial Statement Presentation project;

(ii) amendments to IAS 1; and

(iii) additional guidance or education material on materiality.

Within this context, do you agree with the IASB's preliminary views about the scope and content of guidance that should be included in the Conceptual Framework on:

(a) presentation in the primary financial statements, including:

(i) what the primary financial statements are;

(ii) the objective of primary financial statements;

(iii) classification and aggregation;

(iv) offsetting; and

(v) the relationship between primary financial statements.

(b) disclosure in the notes to the financial statements, including:

(i) the objective of the notes to the financial statements; and

(ii) the scope of the notes to the financial statements, including the types of information and disclosures that are relevant to meet the objective of the notes to the financial statements, forward-looking information and comparative information.

Why or why not? If you think additional guidance is needed, please specify what additional guidance on presentation and disclosure should be included in the Conceptual Framework.

We agree with the preliminary views. The scope and content of presentation and disclosure are all very important concepts for preparation of financial statements, and therefore should be a part of CF.

Question 17

Paragraph 7.45 of the DP describes the IASB's preliminary view that the concept of materiality is clearly described in the existing Conceptual Framework. Consequently, the IASB does not propose to amend, or add to, the guidance in the Conceptual Framework on materiality. However, the IASB is considering developing additional guidance or education material on materiality outside of the Conceptual Framework project.

Do you agree with this approach? Why or why not?

We agree with this approach, as the existing CF's definition of materiality is sufficient and when needed accounting standards could be revised or developed to provide more detailed guidance.

Question 18

The form of disclosure requirements, including the IASB's preliminary view that it should consider the communication principles in paragraph 7.50 of the DP when it develops or amends disclosure guidance in IFRSs, is discussed in paragraphs 7.48–7.52 of the DP.

Do you agree that communication principles should be part of the Conceptual Framework? Why or why not?

If you agree they should be included, do you agree with the communication principles proposed? Why or why not?

We agree that the communication principles should be part of CF to provide a clear objective for disclosure and presentation.

Section 8 Presentation in the statement of comprehensive income-profit of loss and other comprehensive income

Question 19

The IASB's preliminary view that the Conceptual Framework should require a total or subtotal for profit or loss is discussed in paragraphs 8.19–8.22.

Do you agree with this preliminary view? Why or why not? If you do not agree do you think that the IASB should still be able to require a total or subtotal profit or loss when developing or revising particular Standards?

We agree with the preliminary view that a total or subtotal for profit or loss should be presented, because the profit or loss is the pervasive and key benchmark that the users of financial statements use.

Question 20

The IASB's preliminary view that the Conceptual Framework should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss; i.e. recycled, is discussed in paragraphs 8.23–8.26 of the DP.

Do you agree with this preliminary view? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss?

Why or why not?

If you do not agree, how would you address cash flow hedge accounting?

We agree with the preliminary view expressed in View 2B which permits or requires at least some items previously recognised in OCI to profit or loss, unless recycling would not provide relevant information, because an entity's performance should eventually be reflected in profit or loss which is the key performance measure. Thus, we do not agree with View 1 which prohibits recycling. Further, adoption of View 2A would create inconsistency from the current IFRS.

Question 21

In this Discussion Paper, two approaches are explored that describe which items could be included in the OCI: a narrow approach (Approach 2A described in paragraphs 8.40–8.78 of the DP) and a broad approach (Approach 2B described in paragraphs 8.79-8.94 of the DP).

Which of these approaches do you support, and why?

If you support a different approach, please describe that approach why do you believe it is preferable to the approaches described in this Discussion Paper.

We support the Approach 2B per Question 20 above. CF should provide broader guidance and when needed accounting standards could be revised or developed to provide more detailed guidance.

Section 9 Other issues

Question 22

Paragraphs 9.2–9.22 of the address the chapters of the existing Conceptual Framework that were published in 2010 and how those chapters treat the concepts of stewardship, reliability and prudence. The IASB will make changes to those chapters if work on the rest of the Conceptual Framework highlights areas that need clarifying or amending. However, the IASB does not intend to fundamentally reconsider the content of those chapters.

Do you agree with this approach? Please explain your reasons.

If you believe that the IASB should consider changes to those chapters (including how those chapters treat the concepts of stewardship, reliability and prudence), please explain those changes and the reasons for them, and please explain as precisely as possible how they would affect the rest of the Conceptual Framework.

We agree with the IASB's approach not to change the previous CF, because it went through much due diligence when it was drafted and it still sufficiently conveys the fundamental principles.

The use of the business model concept in financial reporting

Question 23

The business model concept is discussed in paragraphs 9.23–9.34. This DP does not define the business model concept. However, the IASB’s preliminary view is that financial statements can be made more relevant if the IASB considers, when developing or revising particular Standards, how an entity conducts its business activities.

Do you think that the IASB should use the business model concept when it develops or revises particular Standards? Why or why not?

If you agree, in which areas do you think that the business model concept would be helpful?

Should the IASB define ‘business model’? Why or why not? If you think that ‘business model’ should be defined, how would you define it?

We agree that the business model concept should be part of CF, because how a reporting entity conducts its business affects many areas of accounting standards such as measurements, consolidation, presentations, and disclosures.

Unit of account

Question 24

The unit of account is discussed in paragraphs 9.35–9.41. The IASB’s preliminary view is that the unit of account will normally be decided when the IASB develops or revises particular Standards and that, in selecting a unit of account, the IASB should consider the qualitative characteristics of useful financial information.

Do you agree? Why or why not?

We agree with the proposal to leave the selection of a unit of account with the IASB, because the unit of account should be considered in conjunction with each Standard where relevant.

Going Concern

Question 25

Going concern is discussed in paragraphs 9.42–9.44 of the DP. The IASB has identified three situations in which the going concern assumption is relevant (when measuring assets and liabilities, when identifying liabilities and when disclosing information about the entity).

Are there any other situations where the going concern assumption might be relevant?

We are not aware of other situations.

Capital maintenance

Question 26

Capital maintenance is discussed in paragraphs 9.45–9.54 of the DP. The IASB plans to include the existing descriptions and the discussion of capital maintenance concepts in the revised Conceptual Framework largely unchanged until such time as a new or revised Standard on accounting for high inflation indicates a need for change.

Do you agree? Why or why not? Please explain your reasons.

We agree with the IASB to defer revision or refinement until it is needed, because we have not encountered high inflation issues.