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Dear Sir/Madam

**COMMENTS ON EXPOSURE DRAFT (“ED”) OF A PROPOSED SSAP,
AGRICULTURE**

We have been engaging in the audit of agricultural enterprises since 2001 and are willing to comment on the ED of a proposed SSAP on Agriculture, which was issued by the Financial Accounting Standards Committee of Hong Kong Society of Accountants (“HKSA”). The terms in this letter are consistent with those used by the ED.

(1) Cost of a biological asset

Paragraph 30 of the ED states that presumption can be rebutted only on initial recognition for a biological asset for which market-determined prices or values are not available and for which alternative estimates of fair value are determined to be clearly unreliable, that biological asset should be measured at its cost less any accumulated depreciation and any accumulated impairment losses. However, the ED does not specify clearly what should be included in the cost under the following circumstances:

(a) Costs varied due to reproduction of animals

If the agriculture enterprise involved in the development of animals (e.g. a distinct species of calf) which may not have an objective fair value depending on the success of the development, the measurement of cost of the biological asset by its breeding cost may result in doubts for any additional cost incurred if the adult animal gives birth to infant animals. We suggest this item should be clarified in the proposed SSAP and examples to be provided to avoid any doubts.

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(b) **Costs incurred for genetic agriculture product development**

If an agriculture enterprise involved in the development of genetic products through animal or plant farming, the objective fair value of the animals may depend on the success of the development. The accounting treatment for research and development costs stated in SSAP 29 Intangible Assets may apply. We suggest this should be clearly specified or referenced in the proposed SSAP and examples to be provided.

(2) **Disclosure of valuer's information**

Paragraph 47 requires the disclosure of the methods and significant assumptions applied in determining the fair value of each group of agricultural produce at the point of harvest and each group of biological assets.

However, the proposed SSAP does not require the disclosure whether the fair values have been determined in accordance with an independent valuation or directors' valuation and, where the fair values have been determined in accordance with an independent valuation, the name(s) of the firm(s) which made that valuation. We consider this should be included in the disclosure requirement of the proposed SSAP to enable the users' understanding of the fair value determination.

(3) **Value of agricultural produce may be overstated**

Paragraph 30 and 31 allow the biological asset to be measured at its cost less any accumulated depreciation and any accumulated impairment losses only at its initial recognition for a biological asset and paragraph 32 requires the biological asset to be valued at the fair value less estimated point-of-sale costs in other cases.

We consider some agricultural produces may have uncertainty to determine the fair values for their biological assets and the values estimated may be significantly higher than the costs. If we allow them to value the biological assets at their so called "fair values" and recognise the gain before the disposal has actually taken place, the results may be easily manipulated.

We recommend the proposed SSAP should allow the value of the agricultural produce to be stated at the lower of cost less accumulated depreciation & impairment loss and fair values at the balance sheet date to be consistent with the principle of prudence.

(4) Transition arrangement

Paragraph 59 mentions this statement does not establish any specific transitional provisions and the adoption of this statement is accounted for in accordance with SSAP 2. Paragraph 45 and 48 of SSAP 2 requires a change in accounting policy to be applied retrospectively unless the amount of any resulting adjustment that relates to prior periods is not reasonably determinable. The change in accounting policy should be applied prospectively when the amount of the adjustment to the opening balance of retained earnings required cannot be reasonably determined.

We consider this may cause significant effort to establish the fair values of the biological assets and the agricultural produce at the balance sheet dates of the respective prior years. It could be time consuming and incurring lots of costs and sometimes may even be impracticable.

We suggest the proposed SSAP to specify the adjustments which could be made prospectively in the first year of adoption of the proposed SSAP instead of having the retrospective effect.

(5) Scope of the Statement

Paragraph 12 requires a biological asset should be measured on initial recognition and at each balance sheet date at its fair value less estimated point-of-sale costs. Paragraph 26 further requires a gain or loss arising on initial recognition of a biological asset at fair value less estimated point-of-sale costs and from a change in fair value less estimated point-of-sale costs of a biological asset should be included in net profit or loss for the period in which it arises.

We consider the disclosing of the carrying amount of the biological asset at each balance sheet date based on its fair value less estimated point-of-sale cost already enable users to understand the change in fair value of the biological asset at each reporting balance sheet date, there is no need to require the biological asset to recognise the gain at each point of harvest.

Moreover, if the enterprises have frequent harvest times for different biological assets (e.g. different crops) throughout the year, which is quite common in an agricultural business, they may incur significant effort and cost or even be impractical to obtain the fair values of their crops at each harvest time.

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We suggest the proposed SSAP to grant exemptions to allow the enterprises to reflect the change in fair values of their biological assets only at the reporting date instead of at each harvest time so as to save resources but achieve the same results.

(6) Treatment of unrealised gain or loss after harvesting

Paragraph 26 requires a gain or loss arising from a change in fair value less estimated point-of-sale costs of a biological asset should be included in net profit or loss for the period in which it arises. However, paragraph 3 mentions clearly after the harvest point, SSAP 22 Inventories will be applied. Paragraph 5 of SSAP 22 requires inventories to be measured at the lower of cost and net realisable value. The different treatments may cause confusion under the following circumstance.

For example, an enterprise is engaged in fruit tree growing business, assuming that the harvest time is on 30/12/2002 and reporting date is on 31/12/2002 with the following financial information:

(A) Initial cost of a tree (assuming the change in fair value of the tree at 31/12/2002 is immaterial)	10
(B) Breeding cost of tree up to harvest	90
(C) Fair value of fruit at point of harvest on 30/12/2002	250
(D) Net realisable value of fruit at balance sheet date on 31/12/2002	

According to the proposed ED, at harvest time (30/12/2002), the tree should be valued at fair value and unrealised gain should be recorded at (C – B)

But at the balance sheet date on 31/12/2002, even though the fruit is still on the tree, it needed to be recorded according to SSAP 22 and booked at the lower of cost and net realisable value, which is comparing the lower of (B) and (D). 90

It seems that on one hand we recognised the unrealised gain of fruit at HK\$160 on 30/12/2002 but we have to immediately write down the fruit from \$250 to \$90 on 31/12/2002 simply because of the adoption of different SSAP regardless of the actual value of assets.



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We consider the financial results between the harvest time and year end date may fluctuate significantly and cause confusion. The matter can be relieved by this proposed SSAP if it allows the carrying amounts of the biological assets to be stated at the lower of cost and fair value in the balance sheet or even the gain or loss not to be recognised at the point of harvest but only at the year end date for the change in fair values of the biological assets.

We hope HKSA will consider the above comments in finalising the proposed SSAP. Should you have any questions please do not hesitate to contact Ms Pammy Fung at 2894 6820 or Mr Edmund Li at 2894 6895 in our office.

Yours faithfully
For and on behalf of
Charles Chan, Ip & Fung CPA Ltd.

A handwritten signature in black ink that reads 'Charles Chan' in a cursive script.

Charles Chan
Managing Director