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

Our Ref.: C/FRSC

Sent electronically through the IASB Website (www.iasb.org)

25 May 2007

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

IASB Exposure Draft of *Proposed Amendments to IAS 24 Related Party Disclosures – State-controlled Entities and the Definition of a Related Party*

The Hong Kong Institute of CPAs is the only body authorised by law to promulgate financial reporting, auditing and ethical standards for professional accountants in Hong Kong. We welcome the opportunity to provide you with our comments on the captioned Exposure Draft. Our responses to the questions raised in your Exposure Draft are set out in the Appendix for your consideration.

We fully support the proposed amendments to eliminate the disclosure requirements for some entities that are related only because they are either controlled or significantly influenced by the state. We agree that eliminating the disclosure requirements under those circumstances will enable preparers and users of financial statements to focus on the substance of those related party relationships that are likely to affect the financial statements. We highly appreciate the Board's effort in speeding up the process of exposing the proposed amendments, which deal with an issue that is very important to Hong Kong, Mainland China and jurisdictions which have a high proportion of government business units in their economy.

In addition, we generally consider that the proposed amendments in the definition of a related party would help removing inconsistencies in the extant Standard.

If you have any questions on our comments, please do not hesitate to contact me at patricia@hkicpa.org.hk.

Yours faithfully,

Patricia McBride
Executive Director

PM/EC/al

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Hong Kong Institute of CPAs

Comments on the IASB Exposure Draft
Proposed Amendments to IAS 24 Related Party Disclosures
– State-controlled Entities and the Definition of a Related Party

Question 1

(a) Do you agree with the proposal to provide, in the circumstances described in this exposure draft, an exemption for entities controlled or significantly influenced by the state? If not, why? What would you propose instead and why?

We agree with the proposal to provide an exemption from the disclosure requirements of paragraph 17 of IAS 24 for reporting entities that are controlled or significantly influenced by a state in relation to transactions with other entities controlled or significantly influenced by that state where there are no indicators that the reporting entity influenced, or was influenced by, that entity.

We agree that the cost of meeting the extant requirements in IAS 24 for entities controlled or significantly influenced by the state is not always offset by the benefit of increased information for users of financial statements. Eliminating requirements that produce information that is often of high volume and little value will therefore enable preparers and users of financial statements to focus on those related party relationships that are likely to affect the financial statements.

(b) Do you agree (i) that an indicator approach is an appropriate method for identifying when the exemption should be provided for entities controlled or significantly influenced by the state; and (ii) that the proposed indicators are appropriate? If not, why? What would you propose instead and why?

(i) We agree that an indicator approach is an appropriate method as it provides guidance to an entity to identify whether or not influence exists. It is consistent with the principles-based approach adopted by IFRSs and allows management to exercise judgement when applying the exemption. However, we question whether the Board intended that the existence of an indicator should automatically result in the exemption from the disclosure requirements in paragraph 17 not being available, or whether it should only trigger an assessment of whether sufficient influence exists. The current wording in paragraph 17A(b) would imply the former.

In our view, it is the existence, or non-existence, of indicators of **significant** influence between the parties which should determine whether the exemption in paragraph 17A can be taken advantage of. We therefore consider that paragraph 17A(b) should be modified as follows: “there are no indicators that the reporting entity **significantly** influenced or was **significantly** influenced by that entity”.

We further note that the proposals do not clarify whether the indicator approach should be applied each period or whether entities should be considered related parties in all future periods once a related party relationship has been determined for one period. We recommend that paragraph 17A clarifies that the assessment is made on a period-by-period basis, for example by adding “during the period” to the end of paragraph 17A(b). Comparatives should also be adjusted if the entity is a related party during the period but not in the previous period.

(ii) In respect of the proposed indicators in paragraph 17B,

- transacting business at non-market rates (otherwise than by way of regulation) implies that non-market rates would not indicate influence on the entity if they are a result of regulation. Regulation of non-market rates might indicate that the state has influenced the transaction. We suggest that the reference to regulation be extended to “regulation applicable generally”.

- the meaning of sharing of resources is not clear. For example, a state-controlled entity might use public services such as public security, fire and health services in the same way as other state-controlled entities. We recommend that this be clarified as sharing of resources that are not public goods.

- engaging in economically significant transactions with each other requires further elaboration since entities that engage in economically significant transactions with each other can still be transacting in the ordinary course of business. Therefore, they should not automatically be treated as related parties for the purpose of disclosures under IAS 24. We recommend that this indicator be moved to paragraph 17C as a factor that needs to be considered when assessing whether influence exists between entities instead of including it in paragraph 17B which indicates that influence always exists in such circumstances.

- the paragraph is written as if the indicators provided are an exhaustive list. We recommend that this be stated in more general form as “including the following items”.

In respect of paragraph 17C,

- the paragraph refers to "direction or compulsion". These words imply only control rather than influence or control. We suggest that the wording be amended to describe influence in addition to control.

- the paragraph includes "...the presence of common members on the boards of the reporting entity and the other entity..." as an indicator of influence. The presence of common members on the board of the entity's parent is also likely to indicate influence. We suggest amending this sentence to state: "...the presence of common members on the board of the reporting entity (or a parent) and the other entity."

Question 2

(a) The definition of a related party in IAS 24 does not include, for a subsidiary's individual or separate financial statements, an associate of the subsidiary's controlling investor. The Board has decided that it should be included, and thus proposes to amend the definition of a related party. The Board similarly proposes that when the investor is a person, entities that are either significantly influenced or controlled by that person are to be treated as related to each other. Do you agree with this proposed amendment? If not, why? What would you propose instead and why?

We agree with the proposal. There is likely to be influence over the transactions between an associate and a subsidiary of that associate's significant investor due to the existence of a common owner.

(b) IAS 24 does not define associates of an entity as related parties. However, when a person has significant influence over an entity and a close member of the family of that person has significant influence over another entity, IAS 24 defines those two entities as related parties. The Board proposes to align the definition for both types of ownership by excluding from the definition of a related party an entity that is significantly influenced by a person and an entity that is significantly influenced by a close member of the family of that person. Do you agree with the proposed amendment? If not, why? What would you propose instead and why?

We agree with the proposal as we agree that, where the entities are related simply because one entity is subject to significant influence through a person and another entity is subject to significant influence through a close member of the family of that person, such a relationship is generally too distant for the purposes of disclosure under IAS 24.

This has the effect of omitting certain parties that potentially may have a relationship that is similar to a related party relationship as defined. Where such a relationship exists and influences a specific transaction, we recommend that the revised IAS 24 should note that disclosure of that transaction is necessary to give a true and fair view.

(c) IAS 24 defines any entity over which a member of the key management personnel of the reporting entity has control, joint control or significant influence, or in which the member holds significant voting power, as related to the reporting entity. However, the converse is not true. Thus, when the entity that a person controls, jointly controls or significantly influences, or in which the person has significant voting power, is the reporting entity and that person is a member of the key management personnel of another entity, that other entity is not defined as related to the reporting entity. The Board proposes to remove this inconsistency by expanding the definition to encompass both situations. Do you agree with the proposed amendment? If not, why? What would you propose instead and why?

We agree that the inconsistency should be removed. However, we do not support the proposed extension of the definition of related party to cover certain relationships involving only common significant influence by a member of "key management personnel" as set out in paragraphs 9(b)(vi) and 9(b)(vii) of the revised definition.

Paragraph 9(b)(vi) and (vii) have the effect of deeming two entities to be related if a member of key management personnel of one of the entities has significant influence over the other. In our opinion, an individual member of a key management team of a reporting entity generally could be viewed as having no more than significant influence over that entity. This proposal therefore is inconsistent with the Board's proposal to clarify that two associates are not deemed to be related to each other simply because they are both significantly influenced by the same investor. We therefore do not support the proposals to extend the definition of related party in this way, particularly in respect of the proposals in paragraph 9(b)(vii).

(d) Do you agree with the proposal to clarify the definition of a related party? Does the wording proposed capture the same set of related parties as IAS 24 at present (except for the amendments described in (a) – (c) above)? Do you agree that the proposed wording improves the definition of a related party? If not, why? What would you propose instead and why?

We agree with the proposal to clarify the definition of a related party.

Question 3

Do you agree with the proposal to clarify the definition of a related party transaction? If not, why? What changes would you propose and why?

We agree with the proposal to clarify the definition of a related party transaction. The amendments clarify that disclosures are required for transactions between the reporting entity and its related parties rather than transactions between two of an entity's related parties.

Question 4

Do you have any other comments on the proposals?

Timing of finalisation of the proposed amendments

We urge the Board to expedite the finalisation of the proposed amendments so that they can be available for entities to early adopt for reporting periods ending on 31 December 2007.

Disclosure requirement under IFRS 8 Operating Segments

Paragraph 34 of IFRS 8 requires disclosure when revenue arising from a single customer is greater than 10%, and states that "a group of entities known to a reporting entity to be under common control shall be considered a single customer, and a government (national, state, provincial, territorial, local or foreign) and entities known to the reporting entity to be under the control of that government shall be considered a single customer."

We are concerned that the application of this requirement in IFRS 8 by any entities with significant or diverse operations in Mainland China will lead to the same data gathering, information overload and cost-benefit concerns as led to the issue of this Exposure Draft amending IAS 24. In our view, it is neither practicable nor meaningful to regard all state-owned entities as a single customer in a country where state control over commercial enterprises is pervasive. We therefore request that the Board reconsiders the current disclosure requirements of IFRS 8.34, for the same reasons that prompted the Board to propose relief from disclosure under proposed paragraph 17A of IAS 24.

Guidance for comparatives

The proposed amendment does not provide guidance for comparatives. For example, a state-controlled entity may be a related party in the current year, but not in the previous year based on the indicator approach. Does IAS 24 require the previous year's transactions to be disclosed as related party transactions in the comparative information? We believe this should be clarified in the amendment.

Reference to joint ventures or joint control

The Introduction and the Basis of Conclusion refer only to associates and significant influence and there is no reference to joint ventures or joint control. We suggest that the references be clarified to include joint ventures and joint control.

Use of the term "significant voting power"

The term "significant voting power" in (b)(vi) & (vii) is retained from the existing Standard. We recommend that this be deleted (as being part of determination of significant influence) or further explained.