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

Our Ref.: C/FRSC

By e-mail CommentLetters@iasb.org and by post

2 May 2007

Mr. Jeff Singleton
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Mr. Singleton,

IASB Exposure Draft: Proposed Amendments to IFRS 1 *First-Time Adoption of International Financial Reporting Standards – Cost of an Investment in a Subsidiary*

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.

In general, we support allowing a parent to use a deemed cost to measure its investment in subsidiaries when it first adopts IFRSs. However, we have some concerns about the proposals as to whether these amendments will reduce the burden on preparers on first-time adoption of IFRSs. Further details of our concerns are set out in our responses to your questions in the Appendix to this letter.

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

Yours sincerely,

Patricia McBride
Executive Director

PM/EC/al

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APPENDIX

Hong Kong Institute of CPAs

Comments on the IASB Exposure Draft
Proposed amendments to IFRS 1 First-Time *Adoption of International Financial Reporting Standards – Cost of an Investment in a Subsidiary*

Question 1

This Exposure Draft proposes to allow a parent, at its date of transition to IFRSs, to use a deemed cost for an investment in a subsidiary. The deemed cost would be determined using either the carrying amount of the net assets of the subsidiary, or its fair value, at that date. Is this appropriate? If not, why?

In principle, we agree that the use of a deemed cost on transition to IFRS should be permitted, as this is consistent with the practical relief granted in other respects, for example, with respect to the carrying value of property, plant and equipment and business combinations at the date of transition. However, we have the following concerns with respect to the proposed measures of deemed cost for investments in subsidiaries.

We consider that for a group which has intermediate parents, the effort in preparing sub-group consolidations to determine the net asset position of a subsidiary at the date of the ultimate parent's transition to IFRSs could be significant. In addition, deeming "cost" to be based on a subsidiary's IFRS net assets would not necessarily reflect goodwill and other intangible assets in existence at the date of acquisition, even though these would generally have been a key driver in determining actual cost.

We would also note that, while appreciating that the option to use the fair value of the investment as the deemed cost of an investment in a subsidiary at the parent's date of transition to IFRSs may provide more useful information to users than the other two options, we doubt whether this option will be used in practice in view of the associated costs (staff time, external resources required) and difficulties (valuation complexities, re-creation of data, subjective estimations) of applying this measure. This option also bears little conceptual relationship to determining cost at the date of acquisition under IAS 27.37(a).

Conceptually, therefore, neither of the proposed measures bears a close relationship to determining cost at the date of acquisition under IAS 27.37(a), nor do they appear to offer much relief in cost-benefit terms. By contrast, the carrying amount under previous GAAP will generally bear a conceptual relationship to the actual cost as would be determined under IAS 27.37(a) and is straightforward to determine. Furthermore, it would be more consistent with the concessions and requirements relating to business combinations as set out in appendix B to IFRS 1.

We therefore recommend that the Board allows parent companies to regard the carrying amount of the investment based on the previous GAAP to be the deemed cost on transition to IFRS.

In addition, we consider that, as for measuring the cost of an investment in a subsidiary, entities may face the same difficulties on first-time adoption of IFRSs of measuring in the separate financial statements of an investor the cost of an investment in an associate or a jointly controlled entity. We therefore suggest that the scope of the

proposed amendment should be extended to the cost of an investment in an associate and a jointly controlled entity.

Question 2

This Exposure Draft proposes a simplified approach to determining the pre-acquisition accumulated profits of a subsidiary for the purpose of the cost method in IAS 27. Is this appropriate? If not, why?

We are not convinced that the proposal concerning re-determining the pre-acquisition profits at the date of transition is either necessary or fair. In the case where a parent measures an investment in a subsidiary using a deemed cost in accordance with the proposal in the Exposure Draft, the proposal of treating the subsidiary's accumulated profits under IFRSs at the date of transition as pre-acquisition accumulated profits could potentially block the distribution of post-acquisition accumulated profits, when there may have been no corresponding increase in the carrying value of the subsidiary on transition (for example, where the original cost of the subsidiary included a significant premium over identifiable net assets, which have since increased due to post acquisition profits). We therefore suggest the Board to further consider providing an option to allow the use of the pre-acquisition accumulated profits determined under the previous GAAP. We consider that the current rules in IAS 36 concerning impairment are sufficient to address any concerns that the investment may be over-stated if dividends are subsequently recognised as income.