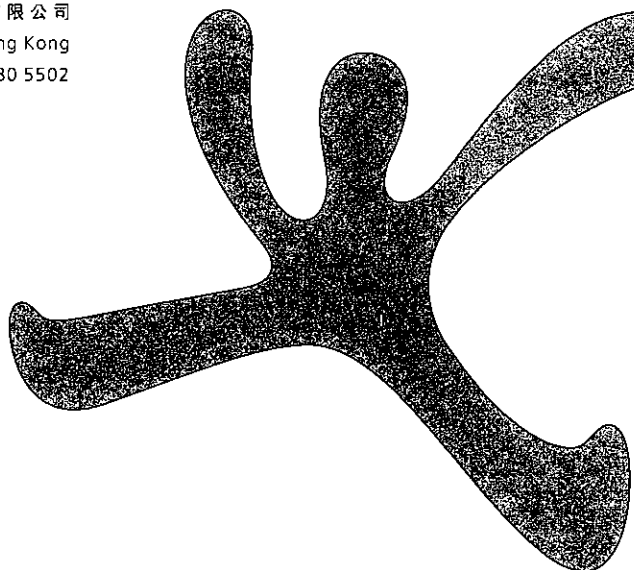


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15 August 2013

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

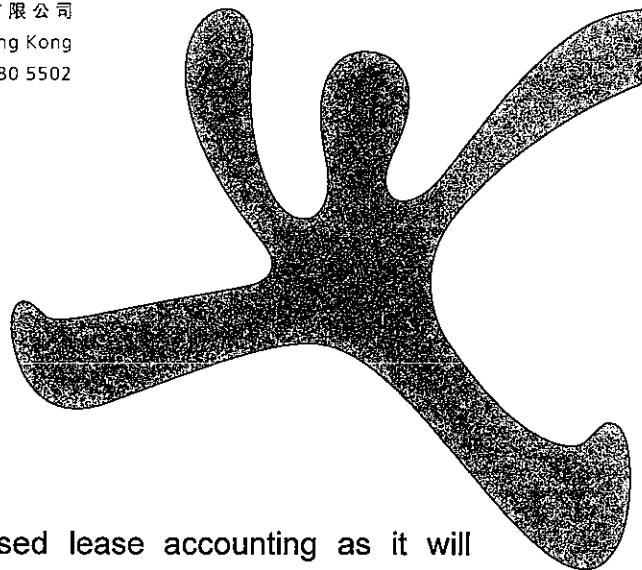
Dear Mr Simon Riley,

Re: Comment on Revised Exposure Draft Lease ("RED") published jointly by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB)

With regard to the subject matter, we would like to take this opportunity to advise our comments on the revised exposure draft.

Fairwood has been operating as fast food chains in Hong Kong for over forty years. We are currently running over 140 outlets located in Hong Kong and Mainland China. Like most retailers in Hong Kong, most of our stores are rented under the definition of operating lease as stipulated in the accounting standard applicable in Hong Kong.

According to the current accounting standard on operating lease, the lessee is not required to recognize future lease commitment on the balance sheet. Such accounting standard has been adopted as usual practice in the market for a long time. Though the RED is more comprehensive, it is noted that it causes significant change on the treatment and presentation of lease accounting on the financial statements, which put much pressure on the enterprises for preparation. In this connection, we hope to share our major concerns for the proposed RED.



Burden and costs

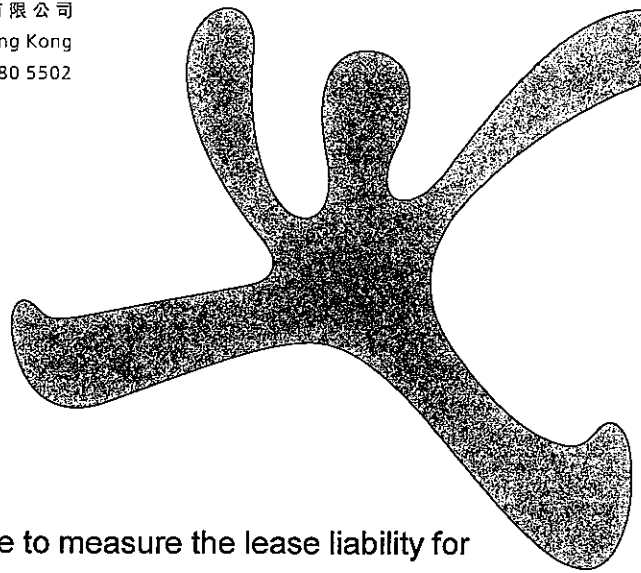
Firstly, we object the implementation of revised lease accounting as it will definitely impose a lot of workload on us. Due to the uniqueness of the tenancy agreement, we have to take much effort to scrutinize each individual lease agreement separately. Currently, there are over hundreds of leases being executed, including leased properties, signboards and storerooms. Although the RED permits the lessees to have a choice on the method of recognition of a lease under 12-month period or over 12-month period, most of the lease agreements are still recognized as over-12-month leases. In view of the scope of work, it is very difficult for us to justify that the benefits of the RED outweighs the efforts and time costs for ensuring the compliance.

Secondly, in addition to the initial recognition, we have to reassess the existing lease terms annually that it would consume us a lot of effort in order to ensure our compliance.

Thirdly, as the RED requires that the "Right-of-use" and "Lease liability" must be reflected in the balance sheet, it is undoubted that the financial ratios will be changed which requires us to reset the bank covenants with our bankers. Subsequent measurement and monitoring of such bank covenants will definitely be very difficult that requires longer time in comparison with the existing policy. As a consequence, there would be increment in the audit fee as it takes auditors an extra amount of time to review the terms.

Type B leases

As a retailer, our leases are likely to be categorized under Type B. Given the existing guidance, the changes will be reflected in the balance sheet by increasing the asset side of "right-of-use" and the liability side of "lease payment". In general, the lease amortization is a straight line method for Type B lease and the amount is same as the previous model. We envisage the change is an uneconomical treat to the preparers and most users could only understand it after studying the notes to the financial statements.



Variable lease payment

At the commencement of the lease, lessees have to measure the lease liability for the variable lease payments which is dependent on an index or a rate (such as the Consumer Price Index or a market interest rate). Initially measured using the index or rate at the commencement date and variable lease payments are in-substance the fixed payments. In practice, it is very time consuming to find an appropriate rate as the definition of "in-substance" is unclear.

Reassessment

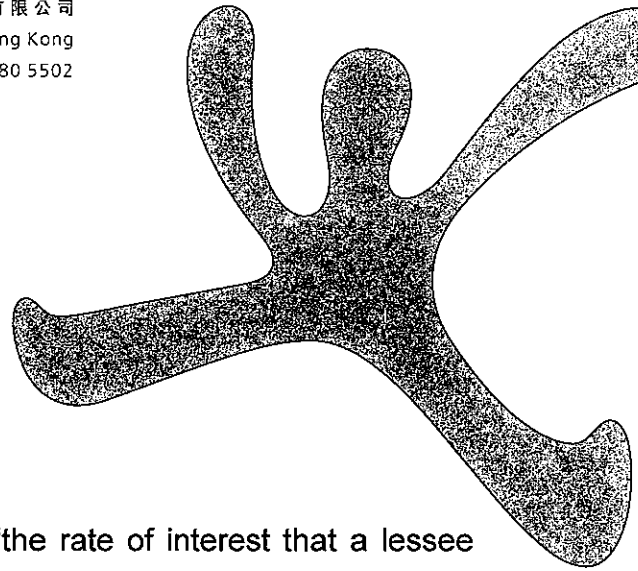
A lessee shall reassess the discount rate if there is a change in any of the following factors, unless the possibility of change was reflected in determining the discount rate at the commencement date:

- (a) the lease term;
- (b) relevant factors that result in the lessee having or no longer having a significant economic incentive to exercise an option to purchase the underlying asset; or
- (c) a reference interest rate which is a basis for determining the variable lease payments

Such extensive reassessment works make our Company very difficult to justify from the economic point of view.

Optional lease term

The RED requires the lessee to include the variable term when there is significant economic incentive for option period. Such works will be quite a burden to retailers. We recommend the removal of inclusion of the option term to avoid subjective judgment because some terms and conditions shown in the rental agreement, such as the amount of the lease payment under the option term, is only stated as "not under the open market value", is common to us. We cannot reliably predict future lease payment in the inception of lease which will create ambiguity to the preparers.



Incremental borrowing rate

The incremental borrowing rate is defined as “the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment.” We believe that it is impracticable to find such a rate from our bankers as our business involves a number of leased properties. Moreover, the incremental borrowing rate is also affected by the extend of leverage the borrowers will provide to banks. More guidance on how to identify the incremental borrowing rate is prominently required. Alternatively, adoption of a risk-free rate may make it much easier to be assessed and understood.

Conclusion

In short, the implementation of the RED may cause problem of interpretation and result in a lack of comparability of the financial statements across the industries. We would be grateful if your Board could review upon taking into consideration of our comments so that a much simplified and practical approach could be provided to the retailers

Yours faithfully,

Margaret Mak
Chief Financial Officer