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18 August 2014 <u>By email: commentletters@hkicpa.org.hk and by post</u>

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

Dear Mr. Riley

<u>Invitation to comment on IASB Exposure Draft ED/2014/2 Investment Entities: Applying the Consolidation Exception (Proposed Amendments to IFRS 10 and IAS 28)</u>

Thank you for your letter dated 10 July 2014 inviting the Association's comments on the IASB Exposure Draft of Investment Entities: Applying the Consolidation Exception (Proposed Amendments to IFRS 10 and IAS 28). Our comments on the specific questions raised in the exposure draft are set out in the enclosed annex.

We hope you would find our comments useful. Should you have any questions, please do not hesitate to contact Ms. Caris Wan of the Secretariat at 2521 1855.

Yours sincerely

Eva Wong
Secretary

Enc.

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

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秘書 黃美嫦

Incorporated by Ordinance, Cap. 364
根據條例第364章成立

Annex- Draft comments on ED-Investment Entities: Applying the Consolidation Exception

Question 1— Exemption from preparing consolidated financial statements
The IASB proposes to amend IFRS 10 to confirm that the exemption from preparing consolidated financial statements set out in paragraph 4(a) of IFRS 10 continues to be available to a parent entity that is a subsidiary of an investment entity, even when the investment entity measures its subsidiaries at fair value in accordance with paragraph 31 of IFRS 10. Do you agree with the proposed amendment? Why or why not?

We agree with the proposed amendment. Our support for the proposed amendment is based on the cost benefit consideration as well as the sufficiency of information available to the users of the investment entity's parent's financial statements, as described under paragraphs BC3 and BC4 of the ED.

Question 2— A subsidiary that provides services that relate to the parent's investment activities
The IASB proposes to amend IFRS 10 to clarify the limited situations in which paragraph 32 applies. The IASB proposes that the requirement for an investment entity to consolidate a subsidiary, instead of measuring it at fair value, applies only to those subsidiaries that act as an extension of the operations of the investment entity parent, and do not themselves qualify as investment entities. The main purpose of such a subsidiary is to provide support services that relate to the investment entity's investment activities (which may include providing investment-related services to third parties). Do you agree with the proposed amendment? Why or why not?

We agree with the proposed clarification. Our support is based on the fact that if a subsidiary of an investment entity performs investment related services as an extension of the investment entity parent, such subsidiary would not likely to meet the definition of an investment entity under IFRS 10 which requires such subsidiary's business purpose to be to invest funds solely for returns from capital appreciation.

Question 3—Application of the equity method by a non-investment entity investor to an investment entity investee
The IASB proposes to amend IAS 28 to:
(a) require a non-investment entity investor to retain, when applying the equity method, the fair value measurement applied by an investment entity associate to its interests in subsidiaries; and

(b) clarify that a non-investment entity investor that is a joint venturer in a joint venture that is an investment entity cannot, when applying the equity method, retain the fair value measurement applied by the investment entity joint venture to its interests in subsidiaries. Do you agree with the proposed amendments? Why or why not?

We support the IASB's proposal to retain the fair value measurement applied by an investment entity associate to its interests in subsidiaries when applying the equity method but disagree with the proposal to disallow a non-investment entity investor that is a joint venturer in a joint venture that is an investment entity from retaining the fair value measurement applied by the investment entity joint venture to its interests in subsidiaries when applying the equity method.

Whilst paragraph 33 of IFRS 10 explicitly requires line-by-line consolidation of subsidiaries of a non-investment entity parent, IAS 28 does not contain the same explicit requirement. Paragraph 35 of IAS 28 merely states that "the entity's financial statements shall be prepared using uniform accounting policies for like transactions and events in similar circumstances". Accordingly, it would be logical to follow paragraph 33 of IFRS 10 as the transactions referred to in IFRS 10 are similar to IAS 28 but this will be constrained by the potential practical difficulties associated with unwinding fair value measurements prior to equity accounting.

In paragraphs BC20 – BC21, the IASB justified its proposals for different applications of equity method by explaining that the degree of practical difficulty for an entity in unwinding the fair value measurements is higher when the investee is an associate than if it were a joint venture. The IASB further explained that structuring risks (highlighted in paragraph BC280 of IFRS 10) were higher for an investee that is a joint venture than if it were an associate. On these bases, the IASB felt that it was acceptable for an investment entity associate to retain fair value of its interest in subsidiaries but not for joint ventures. We disagree with both reasons put forward by the IASB because we believe that, in practice, the practical difficulty and structuring risks described are the same regardless of whether the investee is an associate or a joint venture.

In paragraph BC22 of the ED, the IASB notes that there are currently no differences in how IAS 28 is applied to an investment in an associate and a joint venture. Therefore, in the interest of consistency, we do not believe that it is appropriate for the IASB to introduce different applications of equity accounting by a non-investment entity investor in an investment entity associate or joint venture.

For the reasons explained above, we agree with IASB's proposal (a) and disagree with proposal (b).