1 December 2016

Director, Standard Setting
Hong Kong Institute of Certified Public Accountants
37/F, Wu Chung House
213 Queen's Road East
Wanchai
Hong Kong

Dear Christina Ng,

Comments on the "Request for Information on Post-implementation Review of Accounting Guideline 5 – *Merger Accounting for Common Control Combinations*"

Upon your request in the letter sent to us on 9 August 2016, I am writing to give our comments on the captioned Request for Information of the Hong Kong Institute of Certified Public Accountants (HKICPA).

A copy of the comments on the Request for Information is enclosed.

Thank you.

Yours faithfully,

Alan Chan
Financial Accounting Director

Encl.

Comments to the questions:

Q1 (a):
We are the preparers of financial statements and have experienced a few times with accounting for common control combinations in recent years.

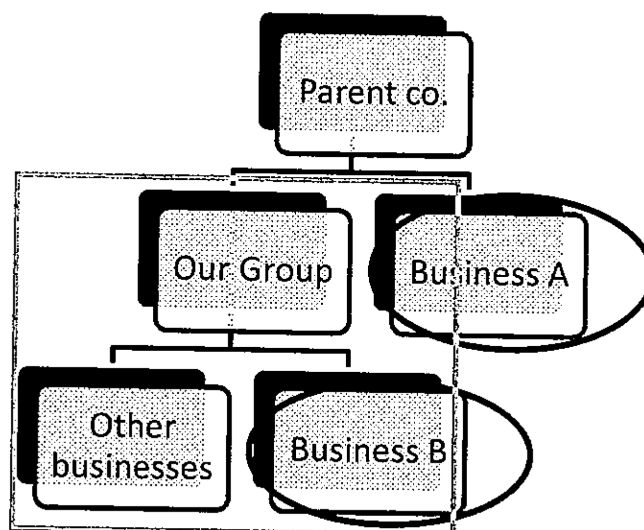
Q1 (b):
(i) The principal activities of our Group are retail, beer, food, beverage, property investments and logistics.
(ii) We prepare financial statements under HKFRS.
(iii) We have encountered a few common control combination transactions in recent years.

Q1 (c):
Not applicable.

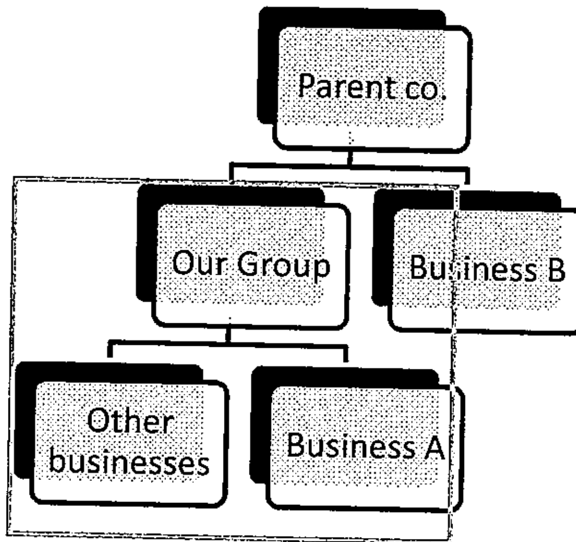
Q2 (a):
The nature and purpose of the common control combination transactions that we encountered is an internal group restructuring following a change in the Group's management structure.

We had encountered a common control combination transaction which business swap. This is an exchange of our Group's business with another business owned by our holding company. We also encountered another common control combination which is a group reorganisation that a new holding company is set up to hold the in the old holding company and subsidiaries which used to be held by the old holding company. The old holding company spin off certain businesses to the new holding company. Therefore, the new holding company is just a continuation of the old holding company in substance.

1. **Business Swap:**
   Before business swap:

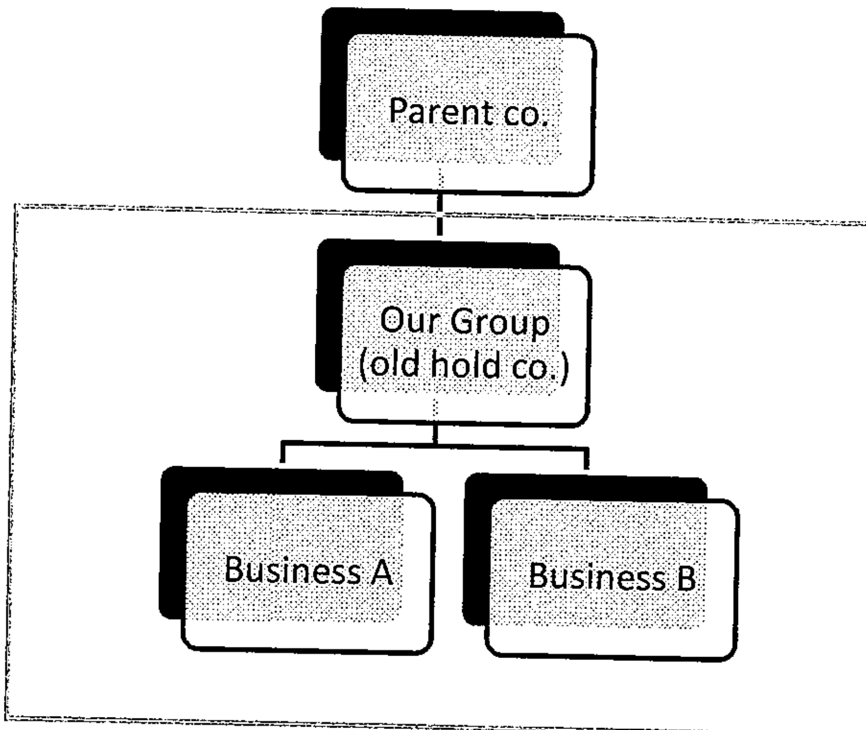


After business swap:

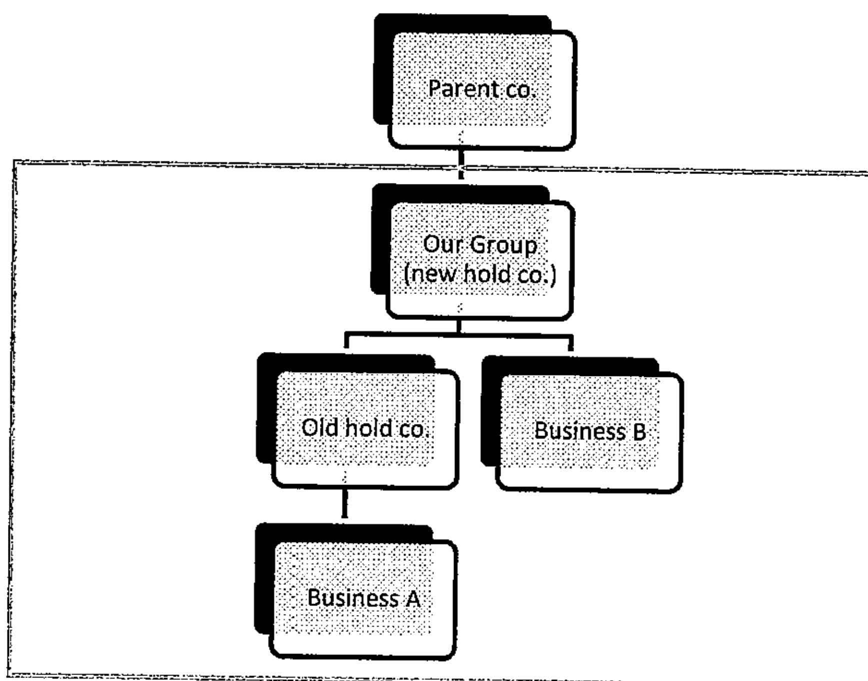


2. **Group restructuring:**

Before restructuring:



After restructuring:



Two different types of accounting method have been applied for the above two transactions. Please refer to information in Q2(b) below for details.

Q2 (b)

Restructuring accounting, similar to merger accounting under AG5, but without restating the comparatives before the combination date has been selected to use for the Business Swap transaction, while merger accounting with comparatives restatement, similar to AG5, has been selected to use for the reorganisation transaction. The reasons to select restructuring accounting or merger accounting is to avoid unnecessary valuation on combination date and easier consolidation by using the sub-consolidation of our Group directly in the holding company's perspective. No restatement is applied for the business swap as it is sensitive for a listed company to have prior year restatements, and it would incur significant time cost to prepare restatement involving entities not under our Group's control previously. Restatement is applied for the reorganisation as the setting up of new holding company is a continuation of the old holding company and the historical financial information of the old Group could be directly applied as the comparatives of the new Group without spending significant time cost for preparation.

Q3 (a)

These principles and procedures are just basic and unclear for application in details.

Illustrative examples for walkthrough procedures showing the journal entries and impact on financial statements (P/L, B/S, CF, SCE, disclosure) should be shown.

For example:

- Should the consideration paid to parent be presented as financing activities, considered that it is a kind of distribution to owner, since it is a reduction of merger reserve; or presented as investing activities, considered that it is an acquisition cost of the subsidiary?
- Illustrative example in AG5 should also include a preparation of cashflow statement and statement of changes in equity.
- Please illustrate the impact on the financial statements, including P/L, B/S, CF and SCE, if the date of under common control is in the middle of the previous year.
- Equity should include the post-acquisition reserve of the combined entity even if the date of under common control is later than the acquisition date of the combined entity from parent's perspective.
- Please give clear guidance on whether or when the consideration paid should be booked as fair value or book value.
- Under a business swap with parent company, i.e. exchange of business/ subsidiary between parent company and the reporting entity, should the consideration paid measured as book value of NAV of subsidiary disposed or fair value? Any other accounting issue in application of AG5 regarding this type of transactions?

Q3 (b)

The main challenges are:

- Difficult to obtain the related financial information, including comparatives and consolidation adjustments, of the combined subsidiary from the parent company.
- If the combined subsidiary is only a part of the acquired group in parent company's perspective, it is difficult to separate and extract the consolidation adjustment and related goodwill details related to the transferred subsidiary.

Q3 (c)

We have identified IP as the 'controlling party' when applying AG5 in the consolidated financial statements of P3. Our main consideration is that it is easier to get access to the financial information of S2 from IP, instead of ultimate holding company. Also, the financial statements of our Group is submitted to IP (immediate parent) instead of UP (ultimate parent) directly, therefore using book value of S2 in IP's perspective is more relevant. In our case, there should be no difference of S2's book value in IP's or UP's perspective.

Q3 (d)

As mentioned above, if the combined subsidiary is only a part of the acquired group in parent company's perspective, it is difficult to separate and extract the consolidation adjustment and related goodwill details related to the transferred subsidiary. Lots of time is required for communication and investigation when obtaining the related financial information and adjustments from the immediate parent. To obtain information from ultimate parent would be more difficult and time consuming.

Q3 (e)

Not applicable.

Q3 (f)
Not applicable.

Q4 (a)
Principles and example of minority interests should specify whether the minority interests should be calculated based on parent's perspective before combination date or on reporting entity's perspective after the combination date.

Also, please give clear illustration on how the change in minority interests as at combination date should be presented in the statement of changes in equity.

Q4 (b)
We did not have material challenges on accounting for minority interests.

Q4 (c)
Following the logic of illustrative example in AG5 and Illustration 2 in this RfI:

(i) Minority interests ("MI") for S2 in B/S of P3 as at the current year end date: 0%. MI for S2 in B/S of P3 as at the prior year end date: 19%

(ii) MI for S2 in P/L of P3 for current year: 0% after date of combination and 19% before date of combination. MI for S2 in P/L of P3 for prior year: 19%

The consideration is that reporting entity's consolidated financial statements are submitted to the immediate parent in our case, therefore IP's MI% is used for MI calculation prior to date of combination.

Q4 (d)
Not applicable.

Q4 (e)
Not applicable.

Q5 (a)
The main challenge in presenting comparatives is that the financial information of the combined subsidiary prior to the date of combination is difficult to obtain from parent company. It is more difficult if the transferred subsidiary is only a part of the sub-group originally acquired by the parent.

Q5 (b)
Not applicable.

Q6 (a)
In our case of "Business Swap", i.e. acquisition of fellow subsidiary from parent company and disposal of subsidiary to parent company happened at the same time, the consideration paid to parent for the acquired entity is partly shares of the subsidiary disposed and partly cash. In our case of reorganisation, the consideration was paid in

cash.

Q6 (b)
We have accounted for the consideration paid for the "Business Swap" transaction using book value of NAV of disposed subsidiary as at disposal date plus the amount paid in cash, while the comparatives are not restated prior to the date of combination. The difference between the acquiree and the disposal companies was charged or credited to equity. For the case of reorganisation, the consideration was paid in cash, and thus is not reflected in comparative years or be eliminated in the year of reorganisation.

Q7 (a)
No significant challenge in preparing, auditing or enforcing the disclosures required by AG5 is expected.

Q7 (b)
The practical challenges we would foresee in applying additional disclosures similar to those in HKFRS 3 and/or those suggested in Q7 (b) para. (i) to (k) would be fair value measurement of the net assets of the acquired entity, as the valuation is costly and unnecessary for business combination under common control.

Q7 (c)
Not applicable.

Q7 (d)
Not applicable.

Q8 (a)
AG5 is a cost saving method for preparers of financial statements as the fair value of the acquired entity is not required to be ascertained.

Q8 (b)
AG5 have resulted in additional significant time cost on separating and extracting the GAAP and consolidation adjustments of the acquired entity from the parent's consolidated financial statements, especially when the acquired entity is only a part of parent's sub-group. Also, increased time cost and difficulties are faced by auditors on auditing the comparatives prior to the combination date.

Q8 (c)
No effect on the terms or structure of the combination is expected.

Q8 (d)
More general guidance and illustrative example is preferred for preparation of cash flow statement, statement of changes in equity and disclosures.