

## Meeting Summary

### Discussion on HKICPA Request for Information: PIR of AG 5

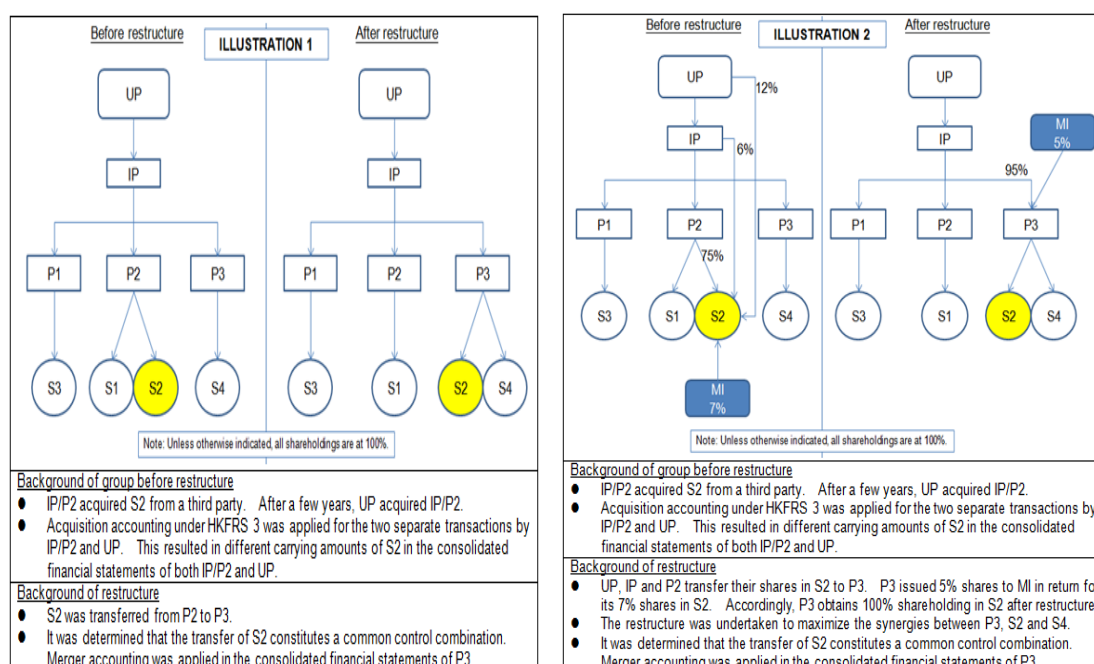
**Date:** 19 September 2016

**Venue:** Pacific Place, Admiralty

**Participant:**

Ghee Chong Peh, Former sell-side analyst with 20 years of experience in Citigroup, UBS and BNP Paribas as a sell-side analyst covering commodity companies regionally and also other sectors including China consumer electronics, technology and property.

**In a group reorganization such as Illustration 1 and 2 below, should entity P3 consolidate entity S2 using its fair values or existing book values from UP/IP?**



1. Mr. Peh's view is book values are generally meaningless for investors, as they are historical numbers. In his experience, equity analysts would prefer to see the fair values of any acquisitions regardless of whether common control acquisitions or external acquisitions. Therefore the carrying values of S2 regardless of whether they are from an immediate parent or ultimate parent are not relevant.
2. Accordingly, as an investor he typically requests the reporting and parent entity for a valuation of the entity being acquired, if the valuation is not recent. Fair value would help investors assess what the current market value is, as well as acting as a basis for predicting future income/cash generating ability. He also emphasizes that fair value is important, because what is relevant to investors is what you can get for the business tomorrow.
3. Investors also typically look for a 'lower cost to the dollar'—the latest fair value as

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it would help them assess if they are paying an appropriate price, or receiving good value for their investment. Hence, an investor's main risk is overstatement rather than understatement.

4. However, Mr. Peh understands that in some cases, there may be no 'real economic substance' in a reorganization. Hence, he commented that if there is perceived change in the value of the whole group by more than 20%, he would require/request fair value at least on the assets that are not already stated at fair value.
5. Mr. Peh noted that depending on the volatility of the industry, there should also be a valuation. Industries such as real estate, technology or mining for example can fluctuate quite a lot from year to year. Hence, he suggests that it is advisable for the assets of these types of companies to be revalued.
6. Mr. Peh also commented that disclosing the fair value of the acquired entity may be sufficient but the basis and assumptions of the valuation must also be disclosed. Key characteristics of the acquired entity should also be disclosed. For example, if the acquired entity is in the real estate industry; then the location of the property, rental mix and rental forecast should be disclosed.

#### **Is this restatement of comparatives as if the current group structure had always existed useful to investors?**

7. Mr. Peh understands the concerns that preparers have in relation to cost and time for the restatement of comparative financial information.
8. However, he notes that restating comparatives is useful for investor analysts, as they would have a basis of comparison. Otherwise, it would be difficult for historical trend analysis and to have a consistent basis for forecasting future performance.
9. On balance, he suggests making restatement optional for preparers. This is because for small private companies, the cost of restating comparatives may exceed the benefits of preparing them for tax purposes only.
10. Mr. Peh also emphasizes that making restatement optional (or voluntary) for preparers works, as there is a check and balance. If users of the financial statements (whether listed or private) want restated comparatives, they will voice their requests. His theory is that if companies do not provide a requested information, investors will not end up investing in it.
11. Finally, he thinks there could be a threshold on whether or not the comparatives are restated, for example, if the acquisition is material (i.e. larger than 10%-15% of net assets/profits).

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#### **How should minority interests be presented in the financial statements before and after a group reorganization?**

12. Mr. Peh commented that the minority interest which represents the legal structure is more relevant.