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From: Hau, Yee Mann [mailto:Hau.Yee-Mann@sc.com]
Sent: Friday, April 03, 2009 10:33 AM
To: P.T. Comment Letter
Cc: Razvi, Saleem; Yee, Charles; hkab.scb@standardchartered.com; Li, Frenda Wing Yan
Subject: FW: Request of Hong Kong Institute of Certified Public Accountants (HKICPA) for Input to Questions Raised by Financial Crisis Advisory Group - Please reply to HKICPA by 30 March 2009 (09/068)

Dear Mr Ong

Please find attached our comments on the questions raised by the Financial Crisis Advisory Group.

Regards
Yee Mann Hau
Head of Reporting
Standard Chartered Bank (Hong Kong) Ltd

Q1 From your perspective, where has general purpose financial reporting helped identify issues of concern during the financial crisis? Where has it not helped, or even possibly created unnecessary concerns? Please be as specific as possible in your answers.

We consider that fair value accounting in general could provide a better picture of the financial position of a reporting entity. However, there is not enough guidance on how to determine the fair value of financial instruments in an illiquid market or under crisis. Different valuation models and assumptions have been employed by different entities which have created difficulties when comparing results. Further guidance is required on how to determine the impact of liquidity on fair value.

Also, we consider that the inclusion of gains or losses from fair value changes in a reporting entity's own credit standing in the entity's profit and loss is appropriate only if they buy back their own debt and trade the liability.

Furthermore, it appears that the existing reporting requirements have failed to explain the reason why a lot of financial institutions recently have to provide financial supports to (or even buy-back) the SPE or the assets that they previously de-recognized in their financial statements. The current criteria for derecognition/consolidation of assets and liabilities and SPEs should be reviewed to take in to account reputational risks as well.

Q2 If prudential regulators were to require 'through-the-cycle' or 'dynamic' loan provisions1 that differ from the current IFRS or US GAAP requirements, how should general purpose financial statements best reflect the difference: (1) recognition in profit or loss (earnings); (2) recognition in other comprehensive income; (3) appropriation of equity outside of comprehensive income; (4) footnote disclosure only; (5) some other means; or (6) not at all? Please explain how your answer would promote transparency for investors and other resource providers.

We consider that the through-the-cycle or dynamic provision should be recognized in the Pnl as a separate item on the face of the Pnl with a disclosure note to analyze the movement etc. It does not make sense for the provision to be recognized in other comprehensive income as most analysts/investors focus primarily on the Pnl.

Q3 Some FCAG members have indicated that they believe issues surrounding accounting for off-balance items such as securitisations and other structured entities have been far more contributory to the financial crisis than issues surrounding fair value (including mark-to-market) accounting. Do you agree, and how can we best improve IFRS and US GAAP in that area?

As mentioned in Q1, we consider that the existing reporting requirements in some circumstances have failed to reflect the economic substance (i.e. risks and rewards) of the SPE and other off-balance sheet items in a reporting entity's financial statements. We believe that the failure to capture some off balance sheet instruments in financial statements have misled some investors, creditors and regulators to assess the risks and financial positions of some reporting entities.

Q4 Most constituents agree that the current mixed attributes model for accounting and reporting of financial instruments under IFRS and US GAAP is overly complex and otherwise suboptimal. Some constituents (mainly investors) support reporting all financial instruments at fair value. Others support a refined mixed attributes model. Which approach do you support and why? If you support a refined mixed attributes model, what should that look like, and why, and do you view that as an interim step toward full fair value or as an end goal? Whichever approach you support, what improvements, if any, to fair value accounting do you believe are essential prerequisites to your end goal?

We support a refined mixed attributed model as the end goal. We consider that loans and receivables and most of the liabilities (e.g. deposits from customers) should continue to be stated at amortized cost unless they are designated at fair value with a sound justification. The rationale behind this is that these instruments are normally held to maturity and it may be difficult for the reporting entity to realize the unrealized gain / loss if there is no secondary market or if it is not their intention to do so under their business model (e.g. a traditional retail bank is to manage the on-going credit risks, interest rate and liquidity gaps of their assets and liabilities, instead of the fair values). However, we support that the fair value information of these instruments should be provided as a disclosure requirement in the financial statements.

For those financial instruments which are fair value accounted, we consider that further guidance is required on valuation techniques including additional guidance for determining the impact of liquidity on fair value and due consideration of appropriate reserves (e.g. liquidity reserve, model reserve and basis risk reserve) to avoid over-reliance on the fair value deduced from valuation models. Also, detailed disclosures in the financial statements are required in order to enable the investors to assess the quality and uncertainty of the fair value information and the Pnl implication.

Q5 What criteria should accounting standard-setters consider in balancing the need for resolving an 'emergency issue' on a timely basis and the need for active engagement from constituents through due process to help ensure high quality standards that are broadly accepted?

We consider that the accounting standard-setters should still consult with constituents before they issue an accounting standard (even for an amendment) although they could reduce the turnaround time by shortening the consultation period, otherwise, it will create a lot of confusion to the market participants (e.g. the market noise arising from the amendment on IAS39 – reclassification in Oct 2008).

Q6 Are there financial crisis-related issues that the IASB2 or the FASB have indicated they will be addressing that you believe are better addressed in combination with, or alternatively by, other organisations3? If so, which issues and why, and which organisations?

Q7 Is there any other input that you'd like to convey to the FCAG?