



創於 1913 年
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香港華人會計師公會

The Society of Chinese Accountants & Auditors

(在香港註冊成立之有限公司)
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2008

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30 September 2008

Mr. Steve Ong
Deputy Director, Standard Setting Department,
Hong Kong Institute of Certified Public Accountants (the 'Institute'),
37/F Wu Chung House,
213 Queen's Road East,
Wan Chai,
Hong Kong

BY:

Dear Steve,

Consultations on (i) Financial Reporting by Private Companies and (ii) Exposure Draft of Proposed Amendments to Small and Medium-Size Entity Financial Reporting Framework and Standards (SME-FRF & SME-FRS) to cover Group Accounts and Cash Flow Statements

Thank you for your letters dated 12 June 2008 and 16 June 2008 inviting us to give our comments on the captioned matters. On behalf of the Society and our members, I would like to extend our sincere thanks to the Institute and its highly capable teams in working hard for the benefits of the accountancy profession in Hong Kong as a whole.

In response to the above, Our Society has conducted a Members' Forum on 24 September 2008 for our members to express their views on the impact of the captioned matters. I now append below our responses and comments relating to these two consultation documents for your kind consideration.

I Financial Reporting by Private Companies

During our Members' Forum, almost all of the attendees (over 120 in number) voted for 2 tiers of financial reporting framework retaining the existing full Hong Kong Financial Reporting Standards ("HKFRSs") and Hong Kong SME-FRF and SME-FRS with certain relaxations to allow more larger private companies qualified to apply.

Our reasons for not supporting the proposed introduction of a large private company reporting framework are as follows:

(a) As auditors

- (i) Most of our staff and us have already got cognizant of the existing two financial reporting frameworks, which have been in place for more than three years.

The new reporting framework would mean unnecessary and non-productive cost to be incurred in training for our clients and our own staff in order to cope with the new requirements. For most small and medium size practitioners, these costs will need to be borne by the practitioners themselves.



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(ii) A new set of audit programme will also need to be established which would incur too much expense and delay in our part. One can look at the Institute's Audit Practice Manual, which is still not yet updated to take into account the recent changes in HKFRSs, which have already been effective for the current year.

(iii) We have to incur cost of engaging more qualified professionals or outside expertise for the compliance with the various reporting requirements under the three reporting frameworks. This will create undue hardship when the entire profession is suffering from severe shortages of staff.

(iv) The introduction and use of three sets of reporting standards may lead to unwarranted disputes with our clients in their choices of reporting framework.

(b) As preparers

(i) The massive changes in reporting standards in the past few years have already led to chaos amongst the preparers. One only needs to look at the error made by a well known listed company recently to understand the havoc facing the preparers. The addition of another tier of reporting framework within such a short period will create more work and confusion to the business community and investors of Hong Kong.

(ii) Additional cost of engaging qualified professionals or outside expertise is required to prepare their financial statements.

(iii) It is already difficult for preparers to keep track of the ever changing requirements of two sets of accounting standards. With the introduction of another set of reporting standards, they need to put in additional long hours in order to keep abreast of the latest development of this new reporting framework also.

(c) As users

(i) The new reporting framework will cause confusion to the users and the public as by now, the Inland Revenue Department, the owners of the entities and most of the financial institutions have just familiarised themselves with the existing two reporting frameworks to a certain extent and the financial statements prepared under either of these two financial reporting standards are widely accepted by them.

(ii) In cases where private companies having sophisticated transactions such as derivatives and/or share-based payments



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etc, the users can always request for additional information if and when necessary without the need of adopting a new reporting framework which they may have to incur more time and costs to learn.

- (iii) It seemed that the cost of providing the additional information to users of the financial statements prepared under the new reporting framework might outweigh the benefits obtained.

II Exposure Draft of Proposed Amendments to SME-FRF & SME-FRS to cover Group Accounts and Cash Flow Statements

During our Members' Forum, the majority of participants agreed that the existing SME-FRF & SME-FRS should be expanded as a means to providing larger private companies with a simpler reporting option.

Our suggestions are summarised as follows:

- (a) There should be no size test requirement for a single private company incorporated in Hong Kong in applying SME-FRF & SME-FRS. The present criteria should continue without any changes.
- (b) Size test should only be required for an overseas company or a small private group of companies, regardless of whether they are incorporated in Hong Kong or elsewhere, which needs to prepare consolidated financial statements under the proposed Section 19 "Consolidated Financial Statements" of the SME-FRS.
- (c) Size test on a private group should be set on an accumulated basis depending on the number of subsidiaries and the total amount of annual revenue, total amount of assets and number of employees capped at a certain figure.
- (d) The exemptions for not presenting consolidated financial statements under the proposed Section 19.2 of the SME-FRS should be expanded to include those private companies without a parent and their members are also the directors managing the companies.
- (e) We agreed that at the company level the investments in associates and interests in jointly controlled entities ("JCEs") should be accounted for using the cost model under Section 6 of the SME-FRS. However if the consolidated financial statements need to be prepared under the proposed Section 19.2 of SME-FRS, the investments in associates and interests in JCEs should be accounted for using the equity method based on the accounting treatments and disclosure requirements similar to those of Pre-2005 Statements of Standard Accounting Practice ("SSAPs") such as; SSAP 10 "Accounting for investments in associates" and SSAP 21



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"Accounting for interests in joint ventures" etc, with which most of us are familiar.

- (f) The difference between the reporting date of the subsidiary, associate or JCE and that of the parent shall be no more than three months which is in line with the requirement set under the relevant HKFRSs for easy to follow.
- (g) There should be exemptions for not preparing cash flow statement in preparing a complete set of financial statements for a single private company under the proposed Section 22 of the SME-FRS such as:
 - (i) Its members are also the directors managing the company; or
 - (ii) With the unanimous consent of all its members.
- (h) If a cash flow statement is required, we agreed that either the direct method or the indirect method could be used for reporting cash flows from operating activities.

III Other comments

Although we admit that there may be some advantages in developing a new set of financial reporting framework for certain large private companies planning for flotation in a couple of years or larger private companies that are subsidiaries of a group applying HKFRSs, as their figures can be included in the group's consolidated financial statements without further adjustments; however the new set of financial reporting framework will provide little benefit to most of the private companies that do not fall into either of those two categories. Therefore we propose that private companies in Hong Kong could continue to elect to apply either HKFRSs or the expanded SME-FRS only.

If the Institute wishes to introduce a new and simpler reporting framework for larger private companies due to whatever reasons, such new reporting framework should have the following characteristics:

- (a) stable and not subject to changes for at least five years;
- (b) simple to understand and easy to follow; and
- (c) specially developed for the Hong Kong environment and focusing on matters commonly undertaken by larger private companies in Hong Kong.

In this connection, this new reporting framework should be established by streaming down from the full HKFRSs with reduced disclosures such as:

- (i) HKAS 12 "Income Taxes" may not be required as the information may be of little value to majority of users of the financial statements;



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(ii) HKFRS 7 "Financial Instruments: Disclosures" and the Amendment to HKAS 1, "Presentation of financial Statements: Capital disclosures" may not be required as the information required to be disclosed is meaningless and not useful to majority of users of the financial statements; and

(iii) One of the exemption criteria for not presenting consolidated financial statements which requires the ultimate or any intermediate parent of the entity to produce consolidated financial statements available for public use under HKFRSs or IFRSs should be removed.

However it is suggested that larger private companies should be allowed to decide which financial reporting frameworks to be selected in order to suit the needs of their stakeholders of the financial statements in case the Institute goes for the three tiers of financial reporting framework.

We hope that you would agree to our suggestions and would be happy to discuss with you in more details on any of our responses and suggestions. Should you require further clarifications, please feel free to contact me.

Yours sincerely,

Yeung Chi Wai, Edwin
President