Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Our Ref.: C/FRSC

Sent electronically through the IASB Website (www.iasb.org)

6 March 2008

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

IASB Exposure Draft of Proposed Amendments to IFRS 1 *First-Time Adoption of International Financial Reporting Standards* and IAS 27 *Consolidated and Separate Financial Statements* – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate

The Hong Kong Institute of CPAs is the only body authorised by law to promulgate financial reporting, auditing and ethical standards for professional accountants in Hong Kong. We welcome the opportunity to provide you with our comments on the captioned Exposure Draft. Our responses to the questions raised in your Exposure Draft are set out in the Appendix for your consideration.

We would like to take this opportunity to express our appreciation in relation to the changes made by the IASB to the original exposure draft regarding the proposals to allow an entity to choose the previous GAAP carrying amount of the investment as a deemed cost for an investment in a subsidiary at the entity's date of transition to IFRSs and to extend its application to associates and jointly controlled entities. We consider that these changes have taken into account the comments made by us in our previous submission made in May 2007.

However, we have particular concerns regarding (a) the proposed requirement for an investor to recognise as income dividend received from a subsidiary, jointly controlled entity or associate and the consequential requirement to test the related investments for impairment and (b) the drafting of proposed paragraph 37A of IAS 27 for new parent formations:

(a) Whilst we agree with the proposal that dividends received from a subsidiary, jointly controlled entity or associate accounted for at cost should be recognised as income, we are concerned that the requirement to test the related investments for impairment in every case of a dividend being received is excessive. We recommend that investors should only be required to perform an impairment test when they consider the receipt of the dividend is an indication of impairment of the investment under paragraph 9 of IAS 36 *Impairment of Assets.* We do not support this proposal to add "receipt of dividend from a subsidiary, jointly controlled entity or an associate accounted for at cost in separate financial statements" to paragraph 10 of IAS 36 as being a circumstance in which the recoverable amount needs to be estimated irrespective of whether there are any other indications of impairment.

37th Floor, Wu Chung House,
213 Queen's Road East, Wanchai, Hong Kong
香港灣仔皇后大道東213號胡忠大廈37樓
Tel電話: (852) 2287 7228
Fax傳真: (852) 2865 6776
(852) 2865 6603
Website網址: www.hkicpa.org.hk
Email電郵: hkicpa@hkicpa.org.hk

Hong Kong Institute of
Certified Public Accountants
香港會計師公會

(b) In respect of the proposal related to the new parent formations, we support the proposal for the cost of a new parent to be measured using the carrying amount of assets and liabilities in the separate financial statements of an existing entity. However, we believe that the Board should consider whether other measurement bases might also be appropriate for entities under common control.

If you have any questions on our comments, please do not hesitate to contact me at patricia@hkicpa.org.hk.

Yours sincerely,

Patricia McBride
Executive Director

PM/WC/ac

APPENDIX

Hong Kong Institute of CPAs

Comments on the IASB Exposure Draft
Proposed Amendments to IFRS 1 *First-Time Adoption of International Financial Reporting Standards* and IAS 27 *Consolidated and Separate Financial Statements* – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate

Question 1 - Do you agree with the two deemed cost options as they are described in this exposure draft? If not, why?

We agree with the proposed two deemed cost options whereby an entity may choose as the deemed cost either the fair value or the previous GAAP carrying amount of the investment at the entity's date of transition to IFRSs. The proposed changes to the original exposure draft are in line with our earlier submission.

Question 2 - Do you agree with the proposal to allow the deemed cost option for investments in jointly controlled entities and associates? If not, why?

We agree to extend the deemed cost option to associates and jointly controlled entities. The proposal is in line with our earlier submission.

Question 3 - Do you agree with the proposal to delete the definition of the cost method from IAS 27? If not, why?

We agree with the proposal to delete the definition of the cost method from IAS 27 as this will now avoid the judgement needed in distinguishing between dividends from the pre-acquisition and post-acquisition retained earnings.

Question 4 - Do you agree with the proposed requirement for an investor to recognise as income dividends received from a subsidiary, jointly controlled entity or associate and the consequential requirement to test the related investment for impairment? If not, why?

We agree that dividends received from a subsidiary, jointly controlled entity or associate should be recognised as income, but we do not agree with the consequential requirement to test the related investment for impairment if such a requirement is set out under paragraph 10 of IAS 36 such that "receipt of dividend from a subsidiary, jointly controlled entity or an associate accounted for at cost in separate financial statements" is always considered a circumstance in which the recoverable amount needs to be estimated irrespective of whether there are any other indications of impairment. While we can appreciate the concern that once the pre-acquisition/ post-acquisition distinction is removed, the distribution of dividends may potentially be paid from pre-acquisition profits which may result in impairment of the investment, we consider the requirement as currently drafted is burdensome, especially to those entities who receive dividends regularly.

We recommend that a more appropriate approach would be to require the preparers to consider whether the receipt of the dividend is an indication of impairment of the investment and only if so would they then need to perform a test for impairment as required by paragraph 9 of IAS 36 *Impairment of Assets.*

Question 5 – Do you agree with the proposed requirement that, in applying paragraph 37(a) of IAS 27, a new parent should measure cost using the carrying amounts of the existing entity? If not, why?

We support the proposal for the cost of a new parent to be measured using the carrying amount of assets and liabilities in the separate financial statements of an existing entity. We agree with the Board that the formation of a new parent is a unique form of transaction, which has no substantive impact on relative ownership interests, cash flows or equity, assets and liabilities of the group. However, we believe that the Board should consider whether other measurement bases may be more appropriate for entities under common control, as set out below.

The creation of a new holding company ("newco") as part of a group reorganisation is a very common occurrence in Hong Kong and China; the newco is often established as a precursor to a listing of the newco's securities in an Initial Public Offering. The group to be listed may be owned by a group of individuals prior to the reorganisation, or by another corporate entity. Accordingly, the newco may in some cases be formed as the ultimate parent of the existing group, while in others it may become an intermediate holding company that is interposed within an existing chain or companies, or added on top of a number of companies under common control. While in some of these situations the Board's proposal of "pushing up" the carrying amounts of assets and liabilities in the subsidiary's (or subsidiaries') financial statements may be appropriate, we believe that in other situations involving common control combinations a "push-down" form of accounting based upon the carrying amount of the existing investment in subsidiaries in the newco's parent's separate financial statements may be more appropriate.

We are aware that the IASB has added the question of accounting for common control transactions to its agenda and is at the early stages of establishing a project agenda. We are also mindful of the fact that the role of separate financial statements within a larger group, and therefore the accounting principles to be adopted in such financial statements, is also an area of current debate. We therefore consider it important that any new rules in these areas take care not to pre-empt the conclusions of such research and debate.

Therefore, while we support the proposal for the cost of a new parent to be measured using the carrying amount of assets and liabilities in the separate financial statements of an existing entity for pragmatic reasons, given the early stages of the project to consider the appropriate accounting treatments for common control combinations, we do not consider that it is appropriate to mandate, at this time, that all formations of parent entities should follow the requirements set out in the proposed new paragraph 37A of IAS 27.

We believe instead that where common control exists the cost of a new parent (for example parent entities interposed between two existing entities in a group) should be permitted to apply either the form of push-up accounting mandated in paragraph 37A, or a form of push down accounting with reference to amounts reported by the immediate parent of the new entity. As an alternative, the Board should explicitly state in IAS 27 that the scope exclusions which exist in IFRS 3 for common control combinations also apply to IAS 27.

Question 6 – Do you agree that prospective application of the proposed amendments to IFRS 1 and IAS 27 is appropriate? If not, why?

We agree with the proposal to apply the proposed amendments to IFRS 1 and IAS 27 prospectively. However, we would welcome an option allowing companies a choice of retrospective (from a given date) application of the proposed amendments. This would allow entities that adopted IFRS prior to the issue of this pronouncement to benefit from the relaxation. Given the implications for dividend traps for new parent which were recorded at fair value in the past, we believe that a choice of retrospective application would be preferable.