香港地產建設商會
THE REAL ESTATE DEVELOPERS ASSOCIATION OF HONG KONG
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6 September 2004

Mr. Simon Riley
Technical Director (Financial Reporting)
Hong Kong Society of Accountants
4/F, Tower Two, Lippo Centre
89 Queensway
Hong Kong

Dear Mr Riley

We refer to the circular issued by the Hong Kong Society of Accountants on 16 June 2004. We respect the HKSA's initiative in the proposed convergence of Hong Kong Accounting Standards with International Accounting Standards. However, as the HKSA is aware, we have very serious concerns about the proposed introduction of IAS 40 (to be known as HKAS 40 in Hong Kong).

Revaluation surpluses/deficits

We consider that the proposed requirement to include surpluses and deficits arising on the revaluation of investment properties within the profit and loss account is flawed, for the following reasons:

1. It would combine realised and unrealised profits and losses within the income statement. This would be a major change in conventional understanding of the profit and loss account and is likely to be misleading and confusing for investors.
2. It introduces an element of volatility into reported profit that is unwarranted and is inconsistent with the steady, long-term nature of realised income from the investment property business.
3. The potential for large fluctuations in profit is likely to lead to difficulty and confusion in meeting the profits test outlined in the Listing Rules in relation to discloseable transactions.
4. It is inconsistent with the treatment of financial assets allowed under IAS 39, where valuation gains and losses are permitted through equity.

The HKSA itself has consistently opposed the introduction of IAS 40 under the current reporting framework.

1. In 1999, when IAS 40 was released as an exposure draft (E64), the HKSA's submission to the International Accounting Standards Committee (as it was then called) expressed concern that recognising changes in the fair value of investment properties in net profit or loss would "confuse the reader, may not be meaningful and is unlikely to present a true and fair view".

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2. At that time the HKSA noted discussions within the international accounting community on the presentation of comprehensive income, and proposed that it would be premature to require changes in the fair value of investment properties in income until there was a resolution of this issue.
3. In 2002, after consultation in Hong Kong on the proposed introduction of IAS 40, the HKSA again concluded that it would "defer further consideration to the investment property accounting standard until such time as we have a better understanding of the IASB's proposals with regard to reporting fair value changes in the financial statements".
4. In June 2004, announcing the current consultation, the HKSA stated: "We appreciate that there is not total support for the proposed overhaul of the investment property accounting standards from the entire property company sector. Property companies have argued that income statement volatility will confuse users of their financial statements and create undue fluctuations in share price. We disagree on both counts." This comment contradicts the HKSA's stated position in 1999, whilst the HKSA's action in bringing IAS 40 forward once more for public consultation is contrary to the course it outlined in both 1999 and 2002. The IASB's project on the reporting of comprehensive income is still active, and the conclusion reached by the HKSA in 2002 remains valid.

We are extremely concerned that the HKSA now appears to reverse its position and to be prepared to disregard its own views on the problems with IAS 40. The conclusions reached by the HKSA through due process and consultation in 1999 and 2002 are in danger of being swept away in an excess of enthusiasm for convergence. The HKSA must be accountable for its past decisions, and we urge that HKAS 40 be withdrawn from the convergence project until such time as the IASB has resolved the issues relating to the reporting of comprehensive income.

As an alternative, if the HKSA ultimately determines that convergence should proceed with effect from 1 January 2005, and that therefore Hong Kong must adopt HKAS 40 with effect from that date, we recommend that HKAS 40 be amended so as to allow revaluation surpluses and deficits to be taken through equity, rather than through the profit and loss account. This approach would be consistent with that adopted by the IASB for IAS 39, in relation to financial assets, and is therefore conceptually justified.

Yours sincerely

Louis Loong
Secretary General

cc: Mr. Roger Best
Mr. Paul Winkelmann