Professional and Technical News at a glance

HKSA TechWatch

Hong Kong Society of Accountants 香港會計師公會

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This is the Ninth Issue of TechWatch, a publication designed to alert members to topics and issues that impact on accountants and their working environment. We welcome your comments and feedback. Comments and suggestions on TechWatch should be addressed to Ms. Winnie Cheung, Senior Director, Professional & Technical Development, Hong Kong Society of Accountants (email:<commentletters@hksa.org.hk>).

This issue (and all back issues) is available online at the Society's website <http://www.hksa.org.hk/professionaltechnical/techwatch/>.

If you would prefer to receive future issues electronically via email or in hard copy format, you may register or alter your option online at the Members Only section of HKSA web page under "Personal Profile - Publications Preferences". If you have any questions, please contact Karen Moy, Administrative Officer, Professional & Technical Department at <karen_moy@hksa.org.hk> or tel: 2287 7089.

Headlines Of This Issue

Accounting & Financial Reporting

Hong Kong Framework For The Preparation And Presentation Of Financial Statements To Converge With International Framework - ED Issued

The Financial Accounting Standards Committee (FASC) has released an Exposure Draft of a Proposed Revised Framework for the Preparation and Presentation of Financial Statements (HK Framework). Comments on this Exposure Draft are requested by 15 November 2002.

With the HKSA's standards setting due process, the FASC has a mandate to achieve convergence with International Accounting Standards Board (IASB) Standards. The FASC's objective in issuing this Exposure Draft is to bring about the convergence of the HK Framework with the IASB Framework.

The significant amendments to the present version of the HK Framework, proposed in the Exposure Draft, are to:

- ✔ Widen the scope of the HK Framework to cover "general purpose financial statements" rather than solely "true and fair view financial statements";
- ✔ Recognise that a wide range of users place reliance on financial statements for making economic decisions;
- ✔ Eliminate textual differences that presently exist between the HK

Framework and the IASB Framework; and

- ✔ Include within the purpose of the Framework the fact that the Framework assists the HKSA Council in developing accounting standards

The paper version of the Exposure Draft was released on 20 September 2002. A copy of the Exposure Draft and the FASC's Invitation to Comment have also been posted on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/accounting/exposuredraft/frameworki2c.pdf>.

New Accounting Standard - SSAP 36, Agriculture

The HKSA has issued SSAP 36, Agriculture. The new SSAP is in all material respects verbatim with the equivalent International Accounting Standard, IAS 41, Agriculture, and will become effective for financial statements covering periods beginning on or after 1 January 2004 with earlier application encouraged.

SSAP 36 introduces a fair value model to agriculture accounting. This is a major shift away from the traditional cost model widely applied in primary industry and largely explains the extended lead-in time before the new Statement becomes effective.

SSAP 36 will particularly impact those agricultural activities where the income-producing biological assets are expected to have economic lives that stretch beyond one accounting period. This will be the case for both "consumable biological assets", such as a tree that will be logged, and for "bearer biological assets", such as a grape vine that bears fruit but which itself will not eventually become agricultural produce. By contrast, in the case of an annual crop of wheat, for example, when the cultivated plants would typically have a useful life that does not extend beyond the next balance sheet date, the introduction of the fair value model should not have such a major impact.

An article on the new SSAP will be published in the October 2002 edition of the Hong Kong Accountant.

The SSAP, which is largely unchanged from the text proposed in the exposure draft, will be published in a forthcoming Members' Handbook Update and on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/publications> (under "Online Members' Handbook" and "Volume II-A").

HKSA Commentary On The IASB's ED Of Proposed Improvements To The International Accounting Standards

The HKSA has sent a comment letter to the IASB in response to the IASB's invitation to comment on its Exposure Draft of Proposed Revisions to the International Accounting Standards.

During the Consultation period of the Exposure Draft, HKSA received 16 letters from local commentators. The HKSA commentary reflected many of these comments.

A copy of the comment letter has been posted on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/accounting/submissions/>.

HKSA Defers A Proposed Revision Of Hong Kong's Investment Property Accounting Standard

In a press release issued on 4 October 2002, the HKSA announced that a proposed revision to Hong Kong's investment property accounting standard (SSAP 13) would be delayed.

The delay is necessitated in part because a number of property companies had recently expressed significant concerns with the proposed convergence of SSAP 13 with the equivalent international standard, IAS 40. Commentators were concerned primarily about the impact on reported earnings if the fair value model in IAS 40 (which requires all changes in fair value to be reported through the income statement) were adopted in Hong Kong. The commentators' concerns were expressed in response to the FASC's invitation to comment on the IASB's proposed improvements to IAS and their comment letters have been posted on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/accounting/rm/>.

While the HKSA's policy is to converge Hong Kong's accounting standards with those issued by the IASB, it is worthwhile to note that the IASB is revisiting the whole area of how changes in fair value should be reported in the financial statements and significant change appears in the offing. Until the FASC has a better understanding of the IASB's proposals in this regard, further consideration of a proposed revision to the investment property standard will be deferred.

The press release is available for viewing on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/accounting/pressrelease/>.

FASC Meeting - 11 September 2002

The FASC met on 11 September 2002 and discussed the following items:

- ✔ Deposit-taking, Lending and Securities Activities - the IASB's proposed revision of IAS 30
- ✔ ED/Interpretation 19, "Intangible Assets - Website Costs"
- ✔ The Committee's draft comment letter on the IASB's Exposure Draft of Proposed Improvements to International Accounting Standards

A copy of the meeting summary is attached to this issue of TechWatch. The meeting summary has also been posted on the HKSA website at: <http://www.hksa.org.hk/professionaltechnical/accounting/fascupdate/>.

Audit & Assurance

Revised SAS 610 "Communications Of Audit Matters With Those Charged With Governance"

SAS 610 has been revised to adopt the ISA term "those charged with governance" instead of "directors or management".

The revised SAS, now titled "Communications of audit matters with those charged with governance" is identical to the equivalent ISA. The revisions made were mainly textual and accordingly, no exposure draft was issued.

Report By Auditors On Voluntary Revocation Of Authorization Of An Authorized Institution

The Hong Kong Monetary Authority (HKMA) usually requires an authorized institution (AI) to provide a report of factual findings by its auditors concerning its balance sheet, third party deposit liabilities, contingent liabilities and outstanding commitments, when applying for voluntary revocation of authorization. In response to members' concern about the uncertainty of the reporting framework, the HKSA entered into discussion with the HKMA early this year with the view to defining the HKMA's requirements and the appropriate type of opinion that would be given by auditors.

The HKSA's proposed "Example report of factual findings in relation to application for voluntary revocation of authorization of an authorized institution", which is prepared in accordance with SAS 710 "Engagements to perform agreed-upon procedures regarding financial information", has been accepted by the HKMA. The agreed-upon procedures to be carried out by auditors are set out in the Example Report, a copy of which is attached in the Appendices.

Ethics

Hong Kong Code Of Ethics Exposure Draft Released For 2 Months Consultation

The HKSA has released an Exposure Draft (ED) of proposed Hong Kong Code of Ethics for consultation until 15 December 2002. The proposed Hong Kong Code of Ethics is closely modelled on the Code of Ethics for Professional Accountants issued by the International Federation of Accountants (IFAC).

Comments on all aspects of the ED are welcome. Specific comments are requested on the appropriateness of:

- a move to a conceptual framework approach to auditors' independence such that auditors are required to exercise professional judgement, rather than follow certain prescriptive rules, to identify and evaluate threats to independence, and to apply safeguards to reduce the threats to an acceptable level in order to preserve their independence;

- the inclusion of examples of specific circumstances and relationships that may create threats to independence; and
- further liberalisation of the existing practice promotion rules, which is consistent with the latest developments in the UK, US, Australia and Canada, by removing the restrictions on cold calling, direct mailing, distribution of leaflets, promotional gifts and other items, and making references to fees or scale charges in promotional material, provided that such promotion aims at informing the public in an objective manner and is decent, honest, truthful and in good taste.

Annex 1 to ED is the proposed Statement of Policy of Council which sets out the authority of the proposed Hong Kong Code of Ethics and the disciplinary provisions in the Professional Accountants Ordinance for the failure to comply with the ethical requirements. The Hong Kong Code of Ethics will be applicable to both members and registered students of the HKSA.

On the finalisation of the proposed Hong Kong Code of Ethics, a majority of the existing Statements of Professional Ethics (PES) will be withdrawn, and the remaining PES, being additional local guidance on the application of the Hong Kong Code of Ethics, will be updated to become Additional Guidance. Details of the disposition of the existing PES are set out in Part 4 of the Preface to the Exposure Draft.

The ED has been posted on the HKSA's website at:<http://www.hksa.org.hk/professionaltechnical/ethics/exposuredraft/code_of_ethics.pdf>.

Legislation & Government Initiatives

Proposed Company Law Amendments To Introduce Single Member/Director Companies etc.

The Companies (Amendment) Bill 2002 is primarily a technical piece of legislation, which seeks to implement an initial batch of 17 of the recommendations of the Standing Committee on Company Law Reform (SCCLR). These include provisions aimed at enhancing shareholder protection, updating requirements regarding directorships and providing for one member, one-director companies, as previously reported in Techwatch (Issue No.3).

The Bill can be accessed at the LegCo website at <http://www.legco.gov.hk/yr01-02/english/bills/brief/b43_brf.pdf>.

While in general support of most of the proposals contained in the Bill, the Society, in its recent submission on the Bill to LegCo, raised a few issues on certain provisions:-

- Clause 54 proposes to make directors automatically liable for the acts of their alternates where there are no provisions to the contrary in the articles. The Society did not express total support for this and suggests that this should not apply where in practice the director has no say in the appointment of a particular alternate and no control over his actions.
- Clause 58 proposes to extend the prohibitions on a company making a loan to a director under section 157H of the Ordinance to cover quasi-loans and credit transactions. The prohibition would include an arms' length transaction or transactions with a director in the course of its normal business, if the value of the transaction(s) exceeded $500,000. The Society questioned the imposition of an arbitrary ceiling and suggested that instead a link should be made between the ceiling on permissible transactions with directors and the size of transactions that a company normally carries out as part of its business.

- Clause 63, which replaces section 161B of the Ordinance, requires accounts to contain particulars of every transaction in relation to loans to officers. This was considered to be potentially very onerous. It is instead suggested that items of similar nature should be able to be disclosed in aggregate, as under SSAP 2.120 on Related Party Disclosures.

In addition to the provisions currently contained in the Bill, it is proposed that the opportunity also be taken to amend s22 of the Ordinance further, in relation to the situation where a company name is the same or too like an existing name. The Society is of the view that the current 12-month period for the Registrar of Companies to require a change of name is too short to prevent abuses by, for example, registering a dormant company with a similar name to an existing company. As the new company would be inactive, the similarity in names would not necessarily come to light during the relevant period. It is suggested therefore that the period during which the Registrar may order a change be extended to, say, 5 years.

The Society's submission on the Bill may be accessed at <http://www.hksa.org.hk/professionaltechnical/whatsnew/docs/021010.pdf>.

Extension Of International Anti-money Laundering Recommendations Creates Unreasonable Expectation On Accountants' Role

The Financial Action Task Force on Money Laundering (FATF) is an international governmental anti-money laundering organisation, which is currently chaired by the Hong Kong Government in the person of the Commissioner for Narcotics. As an international anti-money laundering standard, the FATF's Forty Recommendations (40Rs) have been implemented by countries in all parts of the world.

At present the 40Rs apply primarily to financial institutions, including banks and "non-bank" financial operations such as remittance agents. They relate to such matters as customer identification and due diligence (extending also to identification of ultimate beneficial owners), including record keeping, reporting of suspicious transactions and regulation and supervision of entities subject to the 40Rs. The 40Rs may be accessed at the FATF website at <http://www.fatf-gafi.org/40Recs_en.htm>.

In 2001, the FATF decided to commence a review of the 40Rs by a consultation process at both national and international levels.

In the "Consultation Paper on the Review of the FATF Forty Recommendations", which was issued internationally, the FATF has proposed to extend 40Rs' application to a number of categories of non-financial businesses and professions, including the accountancy profession. The Consultation Paper may be accessed at <http://www.fatf-gafi.org/pdf/Review40_en.pdf>.

In its submission on the Consultation Paper, the Society has expressed the view that the Recommendations (in particular Rs 10-21 and 26-29) dealing with customer identification, due diligence etc. should apply only to those directly in the front-line in relation to financial transactions, either receiving or handling monies on a regular basis, such as financial institutions, or those acting as financial intermediaries other than on an infrequent or incidental basis. If the status quo is to be changed, then external accountants should be covered by the 40Rs only where they are acting as financial intermediaries, and not when they are performing other services, such as the statutory audit function.

The Society has also expressed the view in its submission that it does not support the proposals in the Consultation Paper for external auditors of gambling entities other than casinos and real estate agents and dealers in high value goods, to be required as part of their annual audit of such entities to have to report on the entity's anti-money laundering controls. We consider that this would represent an extension of the scope of the annual audit of financial statements and as such it would exacerbate the growing concern in the profession over the "expectation gap" between the public perception and the reality regarding the role and function of auditors and the statutory audit, and the proper scope of audit. However, this would not preclude the employment of external accountants to carry out a separate assurance engagement on the clients' anti-money laundering system.

The Society's submission may be accessed at its website at <http://www.hksa.org.hk/professionaltechnical/whatsnew/docs/020930.pdf>.

Accountants In Business

Special Half-day Forum For Accountants In Business (AIBs) - 9 November 2002 "AIBs 'Post-Enron' - On A Mission To Reassure & Excel"

The Society's Financial Management Committee (FMC) is organising a CPD forum for accountants working in the business sector (AIBs) to take stock of certain key issues in the "Post-Enron" climate. The forum will take place on the morning of Saturday, 9 November 2002 at the Marriott Hotel.

Following damaging events that have taken place in the US corporate sector (Enron, WorldCom, Tyco, etc.) and the aftermath of these, the FMC believes that it is a good time to review events and to consider what if anything needs to be done, from the perspective of AIBs, to ensure that similar things do not happen here.

The forum's opening addresses will deal with issues such as how accountants can add value to the role of independent non-executive directors and whether CEOs and CFOs should be held more accountable for the appropriateness of financial statements. This will be followed by panel sessions dealing with the key areas of - Business Ethics, Corporate Governance and Accounting Standards.

The full programme rundown can be accessed at <http://www.hksa.org.hk> (see the "What's New" column). Register now to guarantee your place!

Corporate Governance

HKSA Best Corporate Governance Disclosure Awards Reached Final Judging Stage

By the entry deadline date of 30 August 2002, 120 annual reports had been entered in this year's Best Corporate Governance Disclosure Awards (BCGDA) competition, including 33 Hang Seng Index (HSI)-constituent companies and 87 non-HSI companies and public sector/not-for-profit corporations.

As in the previous two years, Awards will be presented in three categories, namely (1) HSI constituents, (2) Non-HSI listed companies and (3) Public sector/not-for-profit organisations. This year, for the first time, the competition will also feature a Significant Improvement Award to be presented to the company/organisation whose disclosures, in the opinion of the judges, reflect the greatest improvement. This is in keeping with one of the main aims of the annual BCGDA competition which is to encourage the development of better corporate governance practices in Hong Kong.

The Review Panel has now completed its review of the annual reports of all entrants and has submitted a short-list in each category for final judging by the panel of distinguished judges, based on the results of the Compliance and Quality Review exercises.

The Judging Panel is now in the process of assessing the short-listed annual reports, from which the Panel will determine the Diamond, Platinum and Gold Award winners in each entry category as well as the Significant Improvement Award winner.

The results of the Awards will be announced in a press conference in mid-November and the Awards presentation ceremony will be held at the

16th World Congress of Accountants Gala Dinner on the evening of 19 November 2002. A prominent guest will be invited to present the Awards.

Information Technology

Update On Inland Revenue's Proposal To Facilitate Password And Telephone Filing Of Tax Returns

In TechWatch Issue No. 2 (January 2002), members were informed about the introduction into LegCo of the Inland Revenue (Amendment) (No. 2) Bill 2001. The Bill aims to amend the Inland Revenue Ordinance (IRO) so as (a) to provide the necessary legal framework for the use of passwords, as an alternative to digital signatures, under the Government's ESD Scheme, for electronic filing of certain types of individual and property tax returns; and (b) to provide for telephone filing of simple returns.

After the Bill was gazetted in November 2001, the Society expressed doubts about various matters, primarily the following:

(a) the overall legislative framework (principally the decision to not to amend the Electronic Transactions Ordinance (ETO) instead of or as well as the IRO);

(b) the system design, operation and security supporting the use of passwords (e.g. issues of authentication of the sender and integrity of documents sent);

(c) legal responsibilities and liabilities (e.g. equating in law the use of a password to signing a return and the related questions of non-repudiation and responsibility for discrepancies); and

(d) concepts and terminology (such as the appropriateness of referring to "affixing" a password to a tax return and passwords having to be "approved" by the IRD).

Although, in the course of exchanges of correspondence and a meeting between the Society and the Inland Revenue Department (IRD), some reassurance was given by the IRD on technical matters, such as the security and integrity of the particular system proposed by the IRD for transmission of data, and the ability of the system to minimise the risk of breaches, the Society continues to have concerns about certain aspects of the Bill.

Our principal reservations relate to the interface of the Bill with the ETO; the lack of guarantees in the Bill prescribing the technical and legal infrastructure to support the proposed new form of e-filing and the proposal to treat the submission of a tax return through the use of a password as the legal equivalent of signing a return. Representatives of the Society attended a Bills Committee meeting on 23 October 2002 to convey these concerns.

The Society's submission dated 20 September 2002 to the LegCo Bills Committee, highlighting the main issues that have not been fully addressed by the IRD, may be accessed at <http://www.hksa.org.hk/professionaltechnical/whatsnew/docs/020920.pdf>.

Online Government Search Services

Members may wish to note that on-line Government search services are now available under the ESDLife website at <http://www.esdlife.com/e_public/eng/default.asp>. The business applications, which entail no additional service charges for users, include the following items:

- Enquiries on Business Registration Numbers and Information;
- Searches for Bankruptcy and Compulsory Winding-up records;
- Purchases of Government publications and periodicals; and
- Applications for Certificate of Vehicle Particulars.

Taxation

Update On Proposed Changes To Anti-avoidance Provisions Relating To Deduction Of Interest Expenses

Introduced in late 2000, the Inland Revenue (Amendment) Bill 2000 (now the Inland Revenue (Amendment) Bill 2002) ("IR(A)Bill") gave rise to concerns on the part of the Society and various other professional and industry bodies over clause 5 (covering section 15 Inland Revenue Ordinance (IRO)), which appeared to extend the reach of the royalty provisions in a way that was inconsistent with the rules on "source" of profits under the Hong Kong tax regime, and, more particularly, clause 6 (covering sections 16(2)(d), (e) and (f) of the IRO), i.e. the anti-avoidance provisions relating to deduction of interest expenses. The Society previously issued two submissions on the Bill, in December 2000 and June 2001 respectively.

The Inland Revenue Department (IRD) was subsequently asked by the Bills Committee to address the concerns of professional and industry bodies. As a result, the IRD has recently consulted interested parties, including the Society, on certain draft Committee Stage Amendments (CSAs) to the IR(A)Bill prior to submitting them to the Bills Committee.

While the CSAs deal with certain of the points raised in our previous submissions, they have not addressed all the concerns expressed by the Society and other bodies. In particular the CSAs now provide, in relation to section 16(2) of the IRO, that the interest payable on debentures or other marketable instruments (referred to collectively as "debentures") will not be entirely disqualified from being deducted as an expense by the issue of the debentures when any of the debenture holders is an associate of the issuer. Instead the Bill as amended will provide for a reduced deduction according to a prescribed formula that takes into account inter alia the period during which the debentures are held by a connected party and the amount of principal outstanding on them.

Similar apportionment arrangements are proposed where money is borrowed and arrangements are in place whereby interest on the borrowings is payable either directly or indirectly to the borrower, or a person other than the lender who is connected with the borrower and who is not an "excepted person". At the same time, a more discretionary form of apportionment is provided for in relation to situations where borrowings are secured or guaranteed by a deposit or loan made with or to any person by the borrower or an associate of the borrower.

However, the draft CSAs are complex and somewhat opaque, and they give rise to several new issues of concern and further areas of uncertainty that need to be clarified. In addition, they do not deal at all with the question of the apparent conflict of the proposed changes to the royalty provisions, contained in section 15 of the IRO, with the territorial basis of the Hong Kong tax system. As such, we have also reiterated our concerns regarding Clause 5 of the Bill.

The Society's submission to the IRD may be accessed at its website at <http://www.hksa.org.hk/professionaltechnical/whatsnew/docs/020918.pdf>.

Corporate Restructuring & Insolvency

HKSA Commentary On The Role Of The Official Receiver's Office

The Society has submitted its comments on the Review of the Role of the Official Receiver's Office (ORO) Consultation Paper released by the Financial Services Bureau. As reported in TechWatch (Issue No.8), the consultation paper aimed to review the existing role of the ORO in the provision of insolvency administration services, identify what future role ORO should play, and the changes that should be made to the present modus operandi of ORO in the light of its future role. It contains a number of recommendations regarding the administration of insolvency cases, regulation and supervision of private sector insolvency practitioners (PIPs), investigation of potential misconduct and offences, enforcement of insolvency legislation, and the financing and administration of the ORO. The consultation paper may be accessed at the Government website at <http://www.info.gov.hk/fstb/fsb/consult/index.htm>.

The key points of the Society's submission are as follows:

1. The ORO has an important role to play in the oversight, monitoring and review of the legal and regulatory framework for insolvencies in Hong Kong. This is considered to be an area in relation to which more attention should be given.
2. Both corporate compulsory and personal insolvency work should be contracted out to the private sector, such that the ORO could focus more of its efforts on investigations and enforcement in relation to possible breaches of insolvency law or misappropriation of assets, working closely with other authorities such as the Commercial Crime Bureau, the Independent Commission Against Corruption and the Department of Justice. It needs to be adequately resourced for this role.
3. In order to strengthen the ORO's hand in this respect, and to send a clear message to the business community and the general public, that directors will not with impunity be able to deplete the assets of a company before it is put into liquidation, the Society expressed its support for legislation on insolvent trading, which forms part of the Companies (Corporate Rescue) Bill (subject to the qualifications regarding the extension of liability to employees below director level that we expressed in relation to the Bill). It also supports widening the range of offences prosecuted and increasing the severity of the penalties that are imposed on delinquent directors in terms of fines and the length of disqualification orders. Further, the penalties for failure to maintain books and records or to assist liquidators with their investigations should also be increased.
4. As regards the future of insolvency case administration, the consultation paper proposes that views should be sought on the possibility of introducing a "cab rank" system, under which any PIPs who wish to handle compulsory liquidations must register on a court roll and they are then obliged to take whatever cases are allocated to them on a roster basis. Practitioners consider that more information is required as to how such a system would work in Hong Kong, e.g. if the proposal were to involve putting all summary and non-summary cases through the system, there would have to be an objective measure of the suitability of candidates for such a cab rank, as it would include jobs of substantially different sizes. Given the lack of remunerative cases in Hong Kong, such a system would only be commercially viable if it were to be properly funded.
5. The introduction of a system of licensing of PIPs is a desirable long-term goal to ensure the maintenance of high standards within the insolvency profession and to encourage the development of a good local base of young skilled practitioners in Hong Kong. However, the Society acknowledges that there are practical and market-related issues that would first need to be addressed. In the meanwhile, the existing administrative authorisation (Panel A) scheme should continue and the Society is willing to work closely with the ORO to help improve the scheme.
6. The ORO, as a government department, should assume a more direct role in supporting duly-appointed PIPs on cross-border insolvency matters involving the Mainland or other jurisdictions, especially in relation to voluntary liquidation cases.
7. The ORO needs to be adequately funded but the existing means of funding are inappropriate and inequitable, and alternative means should be found to cover

the department's costs. However, given that the ORO provides what are largely non-remunerative public service functions (e.g. liquidator of last resort, oversight of the insolvency regime) and that its future role should, in the Society's view, emphasise on investigation and enforcement, no specific cost-recovery targets should be set.

The submission can be accessed at the Society's website at <http://www.hksa.org.hk/professionaltechnical/whatsnew/index.php>.

Risk Management

HKSA PII Master Policy

Readers will note from the recent issue of the HKSA PII Master Policy Bulletin that the Policy is due for renewal on 1 December 2002. The Society's appointed brokers Aon Hong Kong Limited and Windsor Professional Indemnity Insurance Limited are currently finalizing the renewals terms with the insurance companies with the aim to minimizing the changes to premiums and policy terms given the current tight market conditions. The renewal terms will be announced once they are finalized, which is expected soon.

The Bulletin also covered topics on "Receivers Owe No Duty of Care" and "Members' Questions Answered".

The Bulletin has been posted on the HKSA's website at <http://www.hksa.org.hk/publications/bulletins/pii/pii8.pdf>.

Members Ask...

Comparison Between Hong Kong Accounting Standards And GAAP In Other Jurisdictions

A frequently asked question from members is whether the HKSA publishes any material to identify and/or illustrate the differences between Hong Kong SSAPs and accounting standards applying in other jurisdictions.

Consistent with the HKSA's policy to converge Hong Kong SSAPs with the International Accounting Standards Board's Standards, the HKSA does publish in each SSAP a comparison between the SSAP and the corresponding IAS.

The HKSA does not publish comparisons of Hong Kong SSAPs with accounting standards applying in other jurisdictions. The accounting standards applying in many jurisdictions are, however, compared with the IASB's standards, for example on the IFAD website, http://www.ifad.net, in their publication, GAAP 2001. But readers may note that this comparison may not necessarily be current because of changes to accounting standards both in Hong Kong, the IASB and in

Comment Key Dates

Date	Subject
31 October 2002	Consultation Paper on a Proposed Framework for Differential Reporting, which has been posted on the HKSA website at: <http://www.hksa.org.hk/professionaltechnical/accounting/exposuredraft/consultation_paper.pdf>.
15 November 2002	Exposure Draft (ED) of a Proposed Revised Framework for the Preparation and Presentation of Financial Statements, which has been posted on the HKSA website at: <http://www.hksa.org.hk/professionaltechnical/accounting/exposuredraft/frameworki2c.pdf>.
15 December 2002	Exposure Draft of Proposed HKSA Code of Ethics, which has been posted on the HKSA website at: <http://www.hksa.org.hk/professionaltechnical/ethics/exposuredraft/code_of_ethics.pdf>.
Please send comments to <commentletters@hksa.org.hk>	

other jurisdictions subsequent to publication date.

There is a high degree of convergence between Hong Kong SSAPs and the IASB's Standards. On the basis that differences between SSAPs and the IASB's Standards are relatively few in number, the best method to determine the differences between SSAPs and the accounting standards applying in another jurisdiction would firstly be to obtain a comparison between that other jurisdiction's accounting standards and the IASB's Standards (for example, by reference to the IFAD website and/or publications obtainable from major international accounting firms) and, secondly, to make the minor necessary adjustments to reflect differences between the SSAPs and the IASB's Standards, as identified in the SSAPs themselves.

Please note that the answers above are given in accordance with the HKSA Staff Policy on Handling Technical Queries, which is available for reference on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/policy/techqs.pdf>

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The HKSA Professional and Technical Department is headed by Ms. Winnie Cheung, Senior Director. Section heads of the Professional and Technical Department are:

Mr. Simon Riley, Deputy Director (Accounting)

Mr. Stephen Chan, Deputy Director (Assurance)

Mr. Peter Tisman, Deputy Director (Business & Practice)

Hong Kong Society of Accountants

4th Floor, Tower Two, Lippo Centre, 89 Queensway, Hong Kong

Tel: (852)2287 7228 Fax: (852)2865 6776

*E-mail: **hksa@hksa.org.hk***

*Website: **http://www.hksa.org.hk***

*Comments may be submitted to HKSA by e-mail to <**commentletters@hksa.org.hk**>.*

Financial Accounting Standards Committee
Meeting summary - September 2002

The Society's Financial Accounting Standards Committee (Committee) met on 11 September 2002 and discussed the following items:

- ✔ Deposit-taking, Lending and Securities Activities - the IASB's proposed revision of IAS 30
- ✔ ED/Interpretation 19, "Intangible Assets - Website Costs"
- ✔ The Committee's draft comment letter on the IASB's Exposure Draft of Proposed Improvements to International Accounting Standards

Deposit-taking, Lending and Securities Activities

The Committee considered latest developments in the IASB's project, "Deposit-taking, Lending and Securities Activities".

The IASB's project had previously been referred to as "Activities of Financial Institutions: Disclosures and Presentation" but, while the change in project title would appear to be more consistent with the activity-based focus of the proposed standard (rather than one focussed on a particular category of entity), the project scope continues to be the development of a new IFRS to replace IAS 30, *Disclosures in Financial Statements of Banks and Similar Financial Institutions.*

The current IAS 30 applies on an "enterprise basis" and is limited to banks and similar financial institutions one of whose principal activities is to take deposits and borrow with the objective of lending and investing and which are within the scope of banking or similar legislation.

At present there is no Hong Kong SSAP equivalent to IAS 30 but a number of financial reporting disclosure requirements broadly equivalent to IAS 30 are specified by the Hong Kong Monetary Authority (HKMA) in the Supervisory Policy Manual, Module FD-1, "Financial Disclosure by Locally Authorised Institutions" (FD-1).

These requirements, however, apply only to those entities under the HKMA's regulatory jurisdiction and not necessarily to all entities that engage in deposit-taking and lending activities and which prepare financial statements in accordance with Hong Kong SSAPs.

A proposed new IFRS on deposit-taking, lending and securities activities would primarily be a disclosure-based standard (as is the present IAS 30) but would apply to any entity that takes deposits, grants credit or provides other financing or investment services, whether or not those are part of the enterprise's primary activities. The standard would apply solely in respect of such activities.

The IASB's project - and eventually a Hong Kong SSAP that is converged with the revised IAS 30 - will affect, among others:

- ✔ Banks and other financial institutions (whether or not regulated and supervised as banks) that:
  - take deposits,
  - grant credit,
  - provide other lending or financing services, or
  - provide securities investment services; and
- ✔ Consolidated financial statements that include at least one subsidiary that is a bank or similar financial institution, even if the parent company is not a bank or similar financial institution.

The main proposals under consideration by the IASB centre on:

1. The elimination of redundant requirements in IAS 30. IAS 30 has largely been unchanged since it was first approved in 1990. Since then a number of standards, most notably the standards on financial instruments, have guidance on matters such as the offsetting of assets and liabilities, disclosures about fair values, maturities of assets and liabilities and concentrations of credit risk;
2. Bringing the existing requirements up to date, in response to developments in the deposit-taking and lending industry; and
3. Enhancement of disclosures that supplement the balance sheet and income statement and those that provide information on risk exposure, including asset quality and capital adequacy.

To date the IASB has arrived at tentative conclusions in the following specific areas:

- Fixed reporting formats should not be prescribed but, rather, certain minimum line items on the face of the balance sheet and income statement and note disclosures should be required in respect of an entity's deposit-taking and lending activity. This is especially relevant when an entity or a consolidated group also undertakes business of an unrelated nature. Coordination with the IASB's Reporting Performance project would also be necessary.
- Disclosure should be required about the composition of financial assets and financial liabilities and items of revenue and expense arising from deposit-taking and lending activities. In particular, when an entity undertakes a securities activity for which it has fiduciary responsibilities (for example, handling customer or client funds on trust) - and such funds are appropriately excluded from the entity's balance sheet - a note disclosure would be required of the aggregate amount of such funds held in trust.
- Disclosure of narrative information and quantitative data about risk management policies and the entity’s exposure to credit risk, liquidity risk and cash flow interest rate (price) risk should be provided within the scope of the financial statements (rather than as part of the Management Discussion and Analysis section of an annual report) and such requirements should be both consistent with and supplementary to the requirements of IAS 32.
- Disclosure of information about the entity's solvency risk and operational risks - specifically in relation to deposit-taking and lending activities - may be more appropriately provided outside of the financial statements.

The Committee noted that the HKMA had recently issued a consultation draft revision to its requirements on Financial Disclosure by Locally Incorporated Authorised Institutions (AI) (available at: <http://www.info.gov.hk/hkma/eng/bank/spma/attach/FD-1-C.pdf)> and noted the following proposed new paragraphs on corporate governance:

> *3.2.1 AIs should include a statement on the extent of compliance with the guideline CG-1 “Corporate Governance of Locally Incorporated Authorized Institutions” issued by the HKMA and the reason for any non-compliance. In cases of full compliance throughout the financial year, a general statement to that effect should be made. In case of partial compliance, the statement should specify the details of, and reasons for, the non-compliance.*
>
> *3.2.2 AIs should disclose the roles, functions and compositions of key specialised committees established under the Board of Directors. Typical specialised committees include the Executive Committee, Credit Committee, Asset and Liability Committee and Audit Committee.*

3.2.3 AIs are encouraged to disclose the major areas or topics reviewed and discussed by the Audit Committee during the financial year.

The Committee noted that it was unclear from the IASB's project information supplied thus far as to whether they are considering adding in corporate governance disclosure requirements into the ED. The Committee agreed to approach the IASB to bring to their attention the HKMA's proposed new disclosure requirements and to gauge whether the IASB are considering including corporate governance disclosures in their ED.

The IASB's project timetable currently is to issue an Exposure Draft in the 1st quarter of 2003 and finalise a Standard in the 2nd half of 2003. The Committee tentatively agreed in principle to issue an Invitation to Comment on the IASB's exposure draft when that is published.

<u>ED/Interpretation 19, "Intangible Assets - Website Costs"</u>

The FASC considered comment letters received in respect of the Exposure Draft Interpretation 19, "Intangible Assets - Website Costs". Comment letters were received from:

✔ The DTC Association

✔ Hong Kong Monetary Authority

✔ Hong Kong Institute of Vocational Education

✔ K T Yeung & Co CPAs

On consideration of the comments raised, the Committee determined to recommend to the HKSA Council approval of the Interpretation unamended from the exposure draft and that the Interpretation become effective from the date of Council's approval. The comment letters will be made available on the HKSA website.

<u>The Committee's draft comment letter on the IASB's Exposure Draft of Proposed Improvements to International Accounting Standards</u>

The FASC considered comment letters received from the following, in response to the Committee's Invitation to Comment on the IASB's Exposure Draft of Proposed Improvements to the International Accounting Standards:

✔ ACCA

✔ Argos

✔ Au Yuet Shan

✔ Chan, Suzanne

✔ Ernst & Young

✔ Hang Lung Properties Limited

✔ Hong Kong Monetary Authority

✔ Hysan Development Co. Ltd.

✔ KPMG

✔ New World Development Company Limited

✔ PricewaterhouseCoopers

✔ Sun Hung Kai Properties Ltd

✔ The DTC Association

✔ The Hong Kong Institute of Surveyors

✔ The Real Estate Developers Association of Hong Kong

✔ Yu Tai Tei

The comment letters, which will be made available on the HKSA website, raised substantive points in relation to the proposals contained in the IASB's exposure draft and the specific areas for comment raised in the FASC's Invitation to Comment.

The Committee finalised its consideration of a comment letter in response to the IASB's exposure draft and agreed to make the comment letter available on the HKSA website at <http://www.hksa.org.hk/professionaltechnical/accounting/submissions/>.

Date of Next Meeting

The Committee's next meeting is scheduled to be held on 16 October 2002.

This meeting summary is provided for the information and convenience of those who wish to follow the Committee's deliberations. All conclusions reported are tentative and may be changed at future meetings.

The IASB publishes summaries of its meetings and projects. These can be found on the IASB's website at <http://www.iasb.org.uk>.

The Committee welcomes comments on its technical agenda. Please e-mail us at <commentletters@hksa.org.hk>.

EXAMPLE REPORT OF FACTUAL FINDINGS IN RELATION TO APPLICATION FOR VOLUNTARY REVOCATION OF AUTHORIZATION OF AN AUTHORIZED INSTITUTION

(Issued by the HKSA after consultation with the HKMA)

(Letterhead of the auditors)

The Board of Directors

(ABC Ltd.)

(address)

(Date)

Dear Sirs

Report of factual findings in relation to (ABC Ltd.)'s application for voluntary revocation of its authorization as a (deposit-taking company/restricted licence bank/bank)*

In accordance with your letter of instruction dated (date), a copy of which is attached, we have performed the procedures below with respect to (ABC Ltd.) ("Institution"). Our engagement was conducted in accordance with Statement of Auditing Standards 710 "Engagements to perform agreed-upon procedures regarding financial information" issued by the Hong Kong Society of Accountants ("HKSA"). The procedures were performed solely for the purpose of assisting you in satisfying the requirements stated in the letter dated (date) from the Hong Kong Monetary Authority ("HKMA") in relation to the Institution's application for voluntary revocation of the authorization as a (deposit-taking company/restricted licence bank/bank)*. The procedures are summarized as follows:

1. We inspected the general ledger and customer deposit records of the Institution to ascertain whether there were any third party deposit liabilities recorded as at (date).
2. We obtained the attached balance sheet as at (date) which was prepared by the management of the Institution, and compared it to the books and records.
3. We obtained the attached summary of contingent liabilities and outstanding commitments as at (date) which was prepared by the management of the Institution, and compared it to the books and records.
4. With respect to (1) - (3) above, we also:
   a. obtained and reviewed the minutes of the Board of Directors for the period from (date) to (date) ("Board Minutes"); and
   b. obtained a representation letter from the Board of Directors ("Representation Letter").

We report our findings as follows:

a. With respect to item 1, we found there were no third party deposit liabilities outstanding in the books of the Institution as at (date), and this was consistent with the information in the Board Minutes and the Representation Letter.

b. With respect to item 2, we found the attached balance sheet as at (date) was in agreement with the Institution's books and records, and was consistent with the information in the Board Minutes and the Representation Letter.

c. With respect to item 3, we found the attached summary of contingent liabilities and outstanding commitments as at (date) was in agreement with the Institution's books and records, and was consistent with the information in the Board Minutes and the Representation Letter.

Because the above procedures do not constitute either an audit or a review made in accordance with Statements of Auditing Standards issued by the HKSA, we do not express any assurance on the Institution's balance sheet, third party deposit liabilities, contingent liabilities and commitments as at (date).

Had we performed additional procedures or had we performed an audit or review of the financial statements in accordance with Statements of Auditing Standards issued by the HKSA, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report. It relates only to the items specified above and does not extend to any financial statements of the Institution, taken as a whole.

This report is intended for filing with the HKMA. We have no objection that a copy of this report is given by the HKMA to the Financial Secretary of the HKSAR Government for the purpose of section 22(1) of the Banking Ordinance. Except for the foregoing, this report should not be used for any other purpose.

Yours faithfully

Certified Public Accountants

* Delete as appropriate

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