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

MEMBERS' HANDBOOK

Update No. 64

(Issued May 2009)

This Update contains:

- Improvements to HKFRSs 2009
- Editorial changes

Document Reference and Title	*Instructions*	*Explanations*
VOLUME II		
Contents of Volume II	Discard the existing pages i to iii and replace with the new pages i to iii.	Revised contents pages
HONG KONG ACCOUNTING STANDARDS (HKAS)		
HKAS 1 (Revised) *Presentation of Financial Statements*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 7 *Cash Flow Statements*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 17 *Leases*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 18 *Revenue*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 36 *Impairment of Assets*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 38 *Intangible Assets*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKAS 39 *Financial Instruments: Recognition and Measurement*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note

HONG KONG FINANCIAL REPORTING STANDARDS (HKFRS)

HKFRS 1 (Revised) *First-time Adoption of Hong Kong Financial Reporting Standards* (Implementation Guidance)	Replace page 30 with revised page 30.	Editorial changes
HKFRS 2 *Share-based Payment*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HKFRS 8 *Operating Segments*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
Improvements to HKFRSs 2009	Insert these pages after *Improvements to HKFRSs 2008* issued in October 2008	Improvements to HKFRSs 2009 – Note

HONG KONG (IFRIC) INTERPRETATIONS (HK(IFRIC)-Int)

HK(IFRIC)-Int 9 *Reassessment of Embedded Derivatives*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note
HK(IFRIC)-Int 16 *Hedges of a Net Investment in a Foreign Operation*	Replace cover page with revised cover page.	Improvements to HKFRSs 2009 – Note

Note:

BACKGROUND ABOUT *IMPROVEMENTS TO HKFRSs 2009*:

Improvements to HKFRSs 2009 sets out a collection of amendments to HKFRSs which is issued in response to the International Accounting Standards Board's (IASB) annual improvements project to make necessary, but non-urgent, amendments to IFRSs that will not be included as part of another major project. By presenting the amendments in a single document rather than as a series of piecemeal changes, the IASB aims to ease the burden of change for all concerned.

Unless otherwise specified, the amendments are effective for annual periods beginning on or after 1 January 2010, although entities are permitted to adopt them earlier.

The following table lists the HKFRSs and topics addressed by the amendments.

HKFRS	**Subject of amendment**
HKFRS 2 *Share-based Payment*	Scope of HKFRS 2 and revised HKFRS 3
HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*	Disclosures of non-current assets (or disposal groups) classified as held for sale or discontinued operations

HKFRS 8 *Operating Segments*	Disclosure of information about segment assets
HKAS 1 *Presentation of Financial Statements*	Current/non-current classification of convertible instruments
HKAS 7 *Statement of Cash Flows*	Classification of expenditures on unrecognised assets
HKAS 17 *Leases*	Classification of leases of land and buildings
HKAS 18 *Revenue*	Determining whether an entity is acting as a principal or as an agent
HKAS 36 *Impairment of Assets*	Unit of accounting for goodwill impairment test
HKAS 38 *Intangible Assets*	Additional consequential amendments arising from revised HKFRS 3
	Measuring the fair value of an intangible asset acquired in a business combination
HKAS 39 *Financial Instruments: Recognition and Measurement*	Treating loan prepayment penalties as closely related embedded derivatives
	Scope exemption for business combination contracts
	Cash flow hedge accounting
HK(IFRIC)-Int 9 *Reassessment of Embedded Derivatives*	Scope of HK(IFRIC)-Int 9 and revised HKFRS 3
HK(IFRIC)-Int 16 *Hedges of a Net Investment in a Foreign Operation*	Amendment to the restriction on the entity that can hold hedging instruments

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MEMBERS' HANDBOOK
CONTENTS OF VOLUME II

(Updated to May 2009)

HKAS 1 (Revised)
Revised ~~October 2008~~May 2009

Effective for annual periods
beginning on or after 1 January 2009*

Hong Kong Accounting Standard 1 (Revised)

Presentation of Financial Statements

* (a) HKAS 1 (Revised) is applicable for annual periods beginning on or after 1 January 2009. Earlier application is permitted. HKAS 1 (Revised) supersedes HKAS 1 issued in 2004, as amended in 2005.

  (b) An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.

  (c) An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 January 2010.

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Hong Kong Accounting Standard 7

Cash Flow Statements

(a)	An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.
(b)	An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 January 2010.

Hong Kong Accounting Standard 17

Leases

An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 January 2010.

Hong Kong Accounting Standard 18

Revenue

(a)	An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.
(b)	Appendix to HKAS 18 *Revenue* was amended by *Improvements to HKFRSs 2009* issued in May 2009.

Hong Kong Accounting Standard 36

Impairment of Assets

(a) An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.

(b) An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 prospectively for annual periods beginning on or after 1 January 2010.

Hong Kong Accounting Standard 38

Intangible Assets

(a)	An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.
(b)	An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 prospectively for annual periods beginning on or after 1 July 2009.

Hong Kong Accounting Standard 39

Financial Instruments: Recognition and Measurement

(a) The related amendments to HKAS 39 and HKFRS 7 on *Reclassification of Financial Assets* are set out in Appendix D of this HKAS 39 issued in October 2008. Appendix D also includes a further amendment, *Reclassification of Financial Assets—Effective Date and Transition* issued in December 2008, clarifying the effective date and transition requirements of those earlier amendments. An entity shall apply those amendments on or after 1 July 2008.

(b) An entity shall apply amendments resulting from *Improvements to HKFRSs* issued in October 2008 for annual periods beginning on or after 1 January 2009.

(c) The related amendment to HKAS 39 on *Eligible Hedged Items* is set out in Appendix E of this HKAS 39 issued in November 2008. An entity shall apply this amendment retrospectively for annual periods beginning on or after 1 July 2009.

(d) An entity shall apply amendments resulting from HKFRS 1 (Revised) *First-time Adoption of Hong Kong Financial Reporting Standards* issued in December 2008 for annual periods beginning on or after 1 July 2009.

(e) An entity shall apply amendments to HK(IFRIC)-Int 9 and HKAS 39 on *Embedded Derivatives* issued in March 2009 for annual periods ending on or after 30 June 2009.

(f) HKAS 39 was amended by *Improvements to HKFRSs 2009* issued in May 2009. Effective date and transition of the amendments are contained in paragraphs 103K and 108C of the Standard.

…continued

IG Example 11 Reconciliation of equity and total comprehensive income

4 A restructuring provision of CU250 was recognised in accordance with previous GAAP at 1 January 20X4, but did not qualify for recognition in accordance with HKFRSs until the year ended 31 December 20X4. This increases administrative expenses for 20X4 in accordance with HKFRSs.

5 Adjustments 1–4 above lead to a reduction of CU128 in deferred tax expense.

6 Available-for-sale financial assets carried at fair value in accordance with HKFRSs increased in value by CU180 during 20X4. They were carried at cost in accordance with previous GAAP. The entity sold available-for-sale financial assets during the year, recognising a gain of CU40 in profit or loss. Of that realised gain CU30 had been included in the revaluation ~~reserve~~surplus as at 1 January 20X4 and is reclassified from revaluation ~~reserve~~surplus to profit or loss (as a reclassification adjustment).

7 The fair value of forward foreign exchange contracts that are effective hedges of forecast transactions decreased by CU40 during 20X4.

8 Adjustments 6 and 7 above lead to an increase of CU29 in deferred tax expense.

Explanation of material adjustments to the statement of cash flows for 20X4:

Income taxes of CU133 paid during 20X4 are classified as operating cash flows in accordance with HKFRSs, but were included in a separate category of tax cash flows in accordance with previous GAAP. There are no other material differences between the statement of cash flows presented in accordance with HKFRSs and the statement of cash flows presented in accordance with previous GAAP.

HKFRS 2 *Share-based Payment*

IG64 A first-time adopter is encouraged, but not required, to apply HKFRS 2 *Share-based Payment* to equity instruments that were granted after 7 November 2002 that vested before the later of (a) the date of transition to HKFRSs and (b) 1 January 2005.

IG65 For example, if an entity's date of transition to HKFRSs is 1 January 2004, the entity applies HKFRS 2 to shares, share options or other equity instruments that were granted after 7 November 2002 and had not yet vested at 1 January 2005. Conversely, if an entity's date of transition to HKFRSs is 1 January 2010, the entity applies HKFRS 2 to shares, share options or other equity instruments that were granted after 7 November 2002 and had not yet vested at 1 January 2010.

[Paragraphs IG66–IG200 reserved for possible guidance on future standards]

Hong Kong (IFRIC) Interpretations

HK(IFRIC)-Int 1 *Changes in Existing Decommissioning, Restoration and Similar Liabilities*

IG201 HKAS 16 requires the cost of an item of property, plant and equipment to include the initial estimate of the costs of dismantling and removing the asset and restoring the site on which it is located. HKAS 37 requires the liability, both initially and subsequently, to be measured at the amount required to settle the present obligation at the end of the reporting period, reflecting a current market-based discount rate.

Hong Kong Financial Reporting Standard 2

Share-based Payment

An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 July 2009.

Hong Kong Financial Reporting Standard 5

Non-current Assets Held for Sale and Discontinued Operations

(a) This HKFRS is amended as a result of the adoption of *Improvements to HKFRSs* issued in October 2008. An entity shall apply the amendments contained in Part I of *Improvements to HKFRSs* for annual periods beginning on or after 1 July 2009, and amendments contained in Part II for annual periods beginning on or after 1 January 2009.

(b) An entity shall apply amendments resulting from HK(IFRIC) Int-17 *Distributions of Non-cash Assets to Owners* issued in December 2008 for annual periods beginning on or after 1 July 2009.

(c) An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 prospectively for annual periods beginning on or after 1 January 2010.

HKFRS 8
~~Issued March 2007~~Revised May 2009

Effective for annual periods beginning on or after 1 January 2009

Hong Kong Financial Reporting Standard 8

Operating Segments

An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 January 2010.

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Hong Kong Financial Reporting Standard

Improvements to HKFRSs 2009

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Contents

Improvements to HKFRSs

Introduction

This document sets out amendments to Hong Kong Financial Reporting Standards (HKFRSs) and the related Bases for Conclusions and guidance made in response to the International Accounting Standards Board's (IASB) annual improvements project.

The amendments result from proposals that were contained in exposure drafts of proposed amendments to International Financial Reporting Standards (IFRSs) published in October 2007, August 2008 and January 2009.

The annual improvements project provides a vehicle for making non-urgent but necessary amendments to HKFRSs.

The effective date of each amendment is included in the HKFRS affected.

HKFRSs addressed

The following table shows the topics addressed by these amendments.

HKFRS	**Subject of amendment**
HKFRS 2 *Share-based Payment*	Scope of HKFRS 2 and revised HKFRS 3
HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*	Disclosures of non-current assets (or disposal groups) classified as held for sale or discontinued operations
HKFRS 8 *Operating Segments*	Disclosure of information about segment assets
HKAS 1 *Presentation of Financial Statements*	Current/non-current classification of convertible instruments
HKAS 7 *Statement of Cash Flows*	Classification of expenditures on unrecognised assets
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HKAS 18 *Revenue*	Determining whether an entity is acting as a principal or as an agent
HKAS 36 *Impairment of Assets*	Unit of accounting for goodwill impairment test
HKAS 38 *Intangible Assets*	Additional consequential amendments arising from revised HKFRS 3
	Measuring the fair value of an intangible asset acquired in a business combination
HKAS 39 *Financial Instruments: Recognition and Measurement*	Treating loan prepayment penalties as closely related embedded derivatives
	Scope exemption for business combination contracts
	Cash flow hedge accounting
HK(IFRIC)-Int 9 *Reassessment of Embedded Derivatives*	Scope of HK(IFRIC)-Int 9 and revised HKFRS 3
HK(IFRIC)-Int 16 *Hedges of a Net Investment in a Foreign Operation*	Amendment to the restriction on the entity that can hold hedging instruments

Amendment to HKFRS 2 *Share-based Payment*

Paragraphs 5 and 61 are amended (new text is underlined and deleted text is struck through).

Scope

5 As noted in paragraph 2, this HKFRS … However, an entity shall not apply this HKFRS to transactions in which the entity acquires goods as part of the net assets acquired in a business combination ~~to which~~ as defined by HKFRS 3 *Business Combinations* (as revised in 2008) ~~applies~~, in a combination of entities or businesses under common control as described in paragraphs B1–B4 of HKFRS 3, or the contribution of a business on the formation of a joint venture as defined by HKAS 31 *Interests in Joint Ventures*. Hence, equity instruments issued … (and therefore within the scope of this HKFRS).

Effective date

61 HKFRS 3 (as revised in 2008) and *Improvements to HKFRSs* issued in May 2009 amended paragraph 5. An entity shall apply those ~~that~~ amendments for annual periods beginning on or after 1 July 2009. Earlier application is permitted. If an entity applies HKFRS 3 (revised 2008) for an earlier period, the amendments shall also be applied for that earlier period.

Amendment to Basis for Conclusions on HKFRS 2 *Share-based Payment*

Paragraphs BC24A–BC24D are added.

Transactions within the scope of IFRS 3 *Business Combinations*

BC24A IFRS 3 (as revised in 2008) changed the definition of a business combination. The previous definition of a business combination was 'the bringing together of separate entities or businesses into one reporting entity'. The revised definition of a business combination is 'a transaction or other event in which an acquirer obtains control of one or more businesses'.

BC24B The Board was advised that the changes to that definition caused the accounting for the contribution of a business in exchange for shares issued on formation of a joint venture by the venturers to be within the scope of IFRS 2. The Board noted that common control transactions may also be within the scope of IFRS 2 depending on which level of the group reporting entity is assessing the combination.

BC24C The Board noted that during the development of revised IFRS 3 it did not discuss whether it intended IFRS 2 to apply to these types of transactions. The Board also noted that the reason for excluding common control transactions and the accounting by a joint venture upon its formation from the scope of revised IFRS 3 was to give the Board more time to consider the relevant accounting issues. When the Board revised IFRS 3, it did not intend to change existing practice by bringing such transactions within the scope of IFRS 2, which does not specifically address them.

BC24D Accordingly, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraph 5 of IFRS 2 to confirm that the contribution of a business on the formation of a joint venture and common control transactions are not within the scope of IFRS 2.

Amendment to HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*

Paragraphs 5B and 44E are added.

Scope

5B This HKFRS specifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations. Disclosures in other HKFRSs do not apply to such assets (or disposal groups) unless those HKFRSs require:

(a) specific disclosures in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations; or

(b) disclosures about measurement of assets and liabilities within a disposal group that are not within the scope of the measurement requirement of HKFRS 5 and such disclosures are not already provided in the other notes to the financial statements.

Additional disclosures about non-current assets (or disposal groups) classified as held for sale or discontinued operations may be necessary to comply with the general requirements of HKAS 1, in particular paragraphs 15 and 125 of that Standard.

Effective date

44E Paragraph 5B was added by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment prospectively for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

Amendment to Basis for Conclusions on HKFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*

Paragraphs BC14A–BC14E are added.

Scope of the IFRS

BC14A The Board identified a need to clarify the disclosure requirements for non-current assets (or disposal groups) classified as held for sale or discontinued operations in accordance with IFRS 5. Some believed that IFRS 5 and other IFRSs that specifically refer to non-current assets (or disposal groups) classified as held for sale or discontinued operations set out all the disclosures required in respect of those assets or operations. Others believed that all disclosures required by IFRSs whose scope does not specifically exclude non-current assets (or disposal groups) classified as held for sale or discontinued operations apply to such assets (or disposal groups).

BC14B The Board noted that paragraph 30 of IFRS 5 requires an entity to 'present and disclose information that enables users of the financial statements to evaluate the financial effects of discontinued operations and disposals of non-current assets (or disposal groups).' Paragraph BC17 below states that 'the Board concluded that providing information about assets and groups of assets and liabilities to be disposed of is of benefit to users of financial statements. Such information should assist users in assessing the timing, amount and uncertainty of future cash flows.'

BC14C The Board noted that some IFRSs other than IFRS 5 require specific disclosures for non-current assets (or disposal groups) classified as held for sale or discontinued operations. For instance, paragraph 68 of IAS 33 *Earnings per Share* requires an entity to disclose the amount per share for discontinued operations. The Board also noted that the requirements of IAS 1 on fair presentation and materiality also apply to such assets (or disposal groups).

BC14D The Board also noted that when a disposal group includes assets and liabilities that are not within the scope of the measurement requirements of IFRS 5, disclosures about measurement of those assets and liabilities are normally provided in the other notes to the financial statements and do not need to be repeated, unless they better enable users of the financial statements to evaluate the financial effects of discontinued operations and disposals of non-current assets (or disposal groups).

BC14E Consequently, in *Improvements to IFRSs* issued in April 2009, the Board clarified that IFRS 5 and other IFRSs that specifically refer to non-current assets (or disposal groups) classified as held for sale or discontinued operations set out all the disclosures required in respect of those assets or operations. Additional disclosures about non-current assets (or disposal groups) classified as held for sale may be necessary to comply with the general requirements of IAS 1, in particular paragraphs 15 and 125 of that Standard.

Amendment to HKFRS 8 *Operating Segments*

Paragraphs 23 and 36 are amended (new text is underlined and deleted text is struck through). Paragraph 35A is added.

Disclosure

Information about profit or loss, assets and liabilities

23 An entity shall report a measure of profit or loss ~~and total assets~~ for each reportable segment. An entity shall report a measure of <u>total assets and</u> liabilities for each reportable segment if such ~~an~~ amount<u>s</u> ~~is~~ <u>are</u> regularly provided to the chief operating decision maker. An entity shall also disclose the following about each reportable segment if the specified amounts are included in the measure of segment profit or loss reviewed by the chief operating decision maker~~,~~ or are otherwise regularly provided to the chief operating decision maker~~,~~ even if not included in that measure of segment profit or loss:

(a) revenues from external customers;

(b) …

Transition and effective date

35A Paragraph 23 was amended by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

36 Segment information for prior years that is reported as comparative information for the initial year of application <u>(including application of the amendment to paragraph 23 made in May 2009)</u> shall be restated to conform to the requirements of this HKFRS, unless the necessary information is not available and the cost to develop it would be excessive.

Amendment to Basis for Conclusions on HKFRS 8 *Operating Segments*

In the Basis for Conclusions on HKFRS 8, paragraph BC35 is deleted (new text is underlined and deleted text is struck through) and a footnote and paragraph BC35A are added.

Aspects of the management approach

Information about segment assets

BC35 ~~The Board noted that requiring disclosure of a measure of segment assets only when such a measure is reviewed by the chief operating decision maker would create divergence from SFAS 131. The Board also supported a minimum disclosure of segment profit or loss and segment assets. The Board therefore concluded that measures of segment profit or loss and total segment assets should be disclosed for all segments regardless of whether those measures are reviewed by the chief operating decision maker.~~*

BC35A After IFRS 8 was issued, the Board was informed that the reasons originally set out in paragraph BC35 contradict long-standing interpretations published in the US for the application of SFAS 131 and create an unintended difference from practice in the US under SFAS 131. After reconsideration and discussion of the interaction between the disclosure and measurement requirements in the IFRS (paragraphs 23 and 25), the Board concluded that those reasons no longer reflected its thinking. Therefore, the Board amended paragraph 23 by *Improvements to IFRSs* issued in April 2009 to clarify that a measure of segment assets should be disclosed only if that amount is regularly provided to the chief operating decision maker.

* Paragraph BC35 was deleted and paragraph BC35A added as a consequence of *Improvements to IFRSs* issued in April 2009.

Dissenting opinions on IFRS 8

Dissent of Stephen Cooper from the amendment issued in April 2009

DO1 Mr Cooper dissents from the amendment to IFRS 8 *Operating Segments* made by *Improvements to IFRSs* issued in April 2009.

DO2 In his view the changes are unnecessary considering that the provisions in the *Framework* regarding materiality already enable a reporting entity not to disclose segment assets when those assets are small relative to segment profit and not relevant to the understanding of the business. Mr Cooper believes that allowing a reporting entity not to disclose segment assets merely because this is not reported to the chief operating decision maker weakens IFRS 8, and may result in segment assets not being disclosed even when they are important to understanding the performance and financial position of that business.

Amendment to HKAS 1 *Presentation of Financial Statements*

Paragraph 69 is amended (new text is underlined and deleted text is struck through). Paragraph 139D is added.

Structure and content

Statement of financial position

Current liabilities

69 An entity shall classify a liability as current when:

(a) it expects to settle the liability in its normal operating cycle;

(b) it holds the liability primarily for the purpose of trading;

(c) the liability is due to be settled within twelve months after the reporting period; or

(d) ~~the entity~~ <u>it</u> does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period <u>(see paragraph 73). Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification</u>.

An entity shall classify all other liabilities as non-current.

Transition and effective date

139D Paragraph 69 was amended by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

Amendment to Basis for Conclusions on HKAS 1 *Presentation of Financial Statements*

In the Basis for Conclusions on HKAS 1, a heading and paragraphs BC38E–BC38I are added.

Statement of financial position

Classification of the liability component of a convertible instrument (paragraph 69)

BC38E As part of its improvements project in 2007, the Board considered the classification of the liability component of a convertible instrument as current or non-current. Paragraph 69(d) of IAS 1 states that when an entity does not have an unconditional right to defer settlement of a liability for at least twelve months after the reporting period, the liability should be classified as current. According to the *Framework*, conversion of a liability into equity is a form of settlement.

BC38F The application of these requirements means that if the conversion option can be exercised by the holder at any time, the liability component would be classified as current. This classification would be required even if the entity would not be required to settle unconverted instruments with cash or other assets for more than twelve months after the reporting period.

BC38G IAS 1 and the *Framework* state that information about the liquidity and solvency positions of an entity is useful to users. The terms 'liquidity' and 'solvency' are associated with the availability of cash to an entity. Issuing equity does not result in an outflow of cash or other assets of the entity.

BC38H The Board concluded that classifying the liability on the basis of the requirements to transfer cash or other assets rather than on settlement better reflects the liquidity and solvency position of an entity, and therefore it decided to amend IAS 1 accordingly.

BC38I The Board discussed the comments received in response to its exposure draft of proposed *Improvements to IFRSs* published in 2007 and noted that some respondents were concerned that the proposal in the exposure draft would apply to all liabilities, not just those that are components of convertible instruments as originally contemplated in the exposure draft. Consequently, in *Improvements to IFRSs* issued in April 2009, the Board amended the proposed wording to clarify that the amendment applies only to the classification of a liability that can, at the option of the counterparty, be settled by the issue of the entity's equity instruments.

Amendment to HKAS 7 *Statement of Cash Flows*

The rubric is amended (new text is underlined and deleted text is struck through).

Hong Kong Accounting Standard 7 *Statement of Cash Flows* (HKAS 7) is set out in paragraphs 1–~~55~~56. All the paragraphs have equal authority. HKAS 7 should be read in the context of its objective and the Basis for Conclusions, the *Preface* …

Paragraph 16 is amended (new text is underlined) and paragraph 56 is added.

Presentation of a statement of cash flows

Investing activities

16 The separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which expenditures have been made for resources intended to generate future income and cash flows. Only expenditures that result in a recognised asset in the statement of financial position are eligible for classification as investing activities. Examples of cash flows arising from investing activities are:

(a) ...

Effective date

56 Paragraph 16 was amended by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

Addition of Basis for Conclusions on HKAS 7 *Statement of Cash Flows*

A Basis for Conclusions on HKAS 7 containing paragraphs BC1–BC8 is added.

Basis for Conclusions on HKAS 7 *Statement of Cash Flows*

This Basis for Conclusions accompanies, but is not part of, HKAS 7.

HKAS 7 is based on IAS 7 *Statement of Cash Flows.* In approving HKAS 7, the Council of the Hong Kong Institute of Certified Public Accountants considered and agreed with the IASB's Basis for Conclusions on IAS 7. Accordingly, there are no significant differences between HKAS 7 and IAS 7. The IASB's Basis for Conclusions is reproduced below. The paragraph numbers of IAS 7 referred to below generally correspond with those in HKAS 7.

BC1 This Basis for Conclusions summarises the considerations of the International Accounting Standards Board in reaching its conclusions on amending IAS 7 *Statement of Cash Flows* as part of *Improvements to IFRSs* issued in April 2009. Individual Board members gave greater weight to some factors than to others.

BC2 IAS 7 was developed by the International Accounting Standards Committee in 1992 and was not accompanied by a Basis for Conclusions. This Basis refers to clarification of guidance on classification of cash flows from investing activities.

Classification of expenditures on unrecognised assets

BC3 In 2008 the International Financial Reporting Interpretations Committee (IFRIC) reported to the Board that practice differed for the classification of cash flows for expenditures incurred with the objective of generating future cash flows when those expenditures are not recognised as assets in accordance with IFRSs. Some entities classified such expenditures as cash flows from operating activities and others classified them as investing activities. Examples of such expenditures are those for exploration and evaluation activities, which IFRS 6 *Exploration for and Evaluation of Mineral Resources* permits to be recognised as either an asset or an expense depending on the entity's previous accounting policies for those expenditures. Expenditures on advertising and promotional activities, staff training, and research and development could also raise the same issue.

BC4 The IFRIC decided not to add this issue to its agenda but recommended that the Board should amend IAS 7 to state explicitly that only an expenditure that results in a recognised asset can be classified as a cash flow from investing activity.

BC5 In 2008, as part of its annual improvements project, the Board considered the principles in IAS 7, specifically guidance on the treatment of such expenditures in the statement of cash flows. The Board noted that even though paragraphs 14 and 16 of IAS 7 appear to be clear that only expenditure that results in the recognition of an asset should be classified as cash flows from investing activities, the wording is not definitive in this respect. Some might have misinterpreted the reference in paragraph 11 of IAS 7 for an entity to assess classification by activity that is most appropriate to its business to imply that the assessment is an accounting policy choice.

BC6 Consequently, in *Improvements in IFRSs* issued in April 2009, the Board removed the potential misinterpretation by amending paragraph 16 of IAS 7 to state explicitly that only an expenditure that results in a recognised asset can be classified as a cash flow from investing activities.

BC7 The Board concluded that this amendment better aligns the classification of cash flows from investing activities in the statement of cash flows and the presentation of recognised assets in the statement of financial position, reduces divergence in practice and, therefore, results in financial statements that are easier for users to understand.

BC8 The Board also amended the Basis for Conclusions on IFRS 6 to clarify the Board's view that the exemption in IFRS 6 applies only to recognition and measurement of exploration and evaluation assets, not to the classification of related expenditures in the statement of cash flows, for the same reasons set out in paragraph BC7.

Appendix to Amendment to HKAS 7

Amendment to Basis for Conclusions on HKFRS 6 *Exploration for and Evaluation of Mineral Resources*

Paragraphs BC23A and BC23B are added.

Recognition of exploration and evaluation assets

Temporary exemption from IAS 8 paragraphs 11 and 12

BC23A In 2008, as part of its annual improvements project, the Board considered the guidance on the treatment in IAS 7 *Statement of Cash Flows* of some types of expenditures incurred with the objective of generating future cash flows when those expenditures are not recognised as assets in accordance with IFRSs. Some entities classify such expenditures as cash flows from operating activities and others classify them as investing activities. Examples of such expenditures are those for exploration and evaluation activities, which can be recognised according to IFRS 6 as either an asset or an expense.*

BC23B The Board noted that the exemption in IFRS 6 applies only to recognition and measurement of exploration and evaluation assets, not to the classification of related expenditures in the statement of cash flows. Consequently, the Board amended paragraph 16 of IAS 7 to state that only an expenditure that results in a recognised asset can be classified as a cash flow from investing activities.

* Paragraphs BC23A and BC23B were added as a consequence of an amendment to IAS 7 included in *Improvements to IFRSs* issued in April 2009.

Amendment to HKAS 17 *Leases*

Paragraphs 14 and 15 are deleted (new text is underlined and deleted text is struck through).
Paragraphs 15A, 68A and 69A are added.

Classification of leases

14 [Deleted] ~~Leases of land and of buildings are classified as operating or finance leases in the same way as leases of other assets. However, a characteristic of land is that it normally has an indefinite economic life and, if title is not expected to pass to the lessee by the end of the lease term, the lessee normally does not receive substantially all of the risks and rewards incidental to ownership, in which case the lease of land will be an operating lease. A payment made on entering into or acquiring a leasehold that is accounted for as an operating lease represents prepaid lease payments that are amortised over the lease term in accordance with the pattern of benefits provided.~~

15 [Deleted] ~~The land and buildings elements of a lease of land and buildings are considered separately for the purposes of lease classification. If title to both elements is expected to pass to the lessee by the end of the lease term, both elements are classified as a finance lease, whether analysed as one lease or as two leases, unless it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership of one or both elements. When the land has an indefinite economic life, the land element is normally classified as an operating lease unless title is expected to pass to the lessee by the end of the lease term, in accordance with paragraph 14. The buildings element is classified as a finance or operating lease in accordance with paragraphs 7–13.~~

15A When a lease includes both land and buildings elements, an entity assesses the classification of each element as a finance or an operating lease separately in accordance with paragraphs 7–13. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.

Transitional provisions

68A An entity shall reassess the classification of land elements of unexpired leases at the date it adopts the amendments referred to in paragraph 69A on the basis of information existing at the inception of those leases. It shall recognise a lease newly classified as a finance lease retrospectively in accordance with HKAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, if an entity does not have the information necessary to apply the amendments retrospectively, it shall:

(a) apply the amendments to those leases on the basis of the facts and circumstances existing on the date it adopts the amendments; and

(b) recognise the asset and liability related to a land lease newly classified as a finance lease at their fair values on that date; any difference between those fair values is recognised in retained earnings.

Effective date

69A Paragraphs 14 and 15 were deleted, and paragraphs 15A and 68A were added as part of *Improvements to HKFRSs* issued in May 2009. An entity shall apply those amendments for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

Amendment to Basis for Conclusions on HKAS 17 *Leases*

Before paragraph BC4, the heading is amended and paragraphs BC4, BC5 and BC8 are amended (new text is underlined). After paragraph BC8, a heading, a footnote and paragraphs BC8A–BC8F are added.

Classification of leases—leases of land and buildings <u>(2003 amendment)</u>

BC4 Paragraph 14 of the Standard required a lease of land with an indefinite economic life to be normally classified as an operating lease, unless title is expected to pass to the lessee by the end of the lease term. The previous version of IAS 17 <u>(as amended in 2000)</u> was not explicit about how to classify a lease of land and buildings.

BC5 This is a matter of concern in countries where property rights are obtained under long-term leases and the substance of those leases differs little from buying a property. Therefore, the Board decided to deal with this matter in its Improvements project <u>in 2001</u> and not to defer its resolution until the more fundamental project on leases was completed.

BC8 The Board also discussed a third approach, namely whether to delete the requirement (in paragraph 14 of the Standard) normally to classify a lease of land as an operating lease when title does not pass at the end of the lease and to require such a lease to be classified as a finance lease when all other conditions for finance lease classification in the Standard are met. The Board noted that such an accounting treatment would conflict with the criteria for lease classification in the Standard, which are based on the extent to which the risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. Indeed, land normally has an indefinite economic life and hence there are significant risks and rewards associated with the land at the end of the lease term, which do not pass to the lessee. Therefore, the Board rejected this approach <u>when issuing the amendments to IAS 17 in December 2003</u>.

Land element in long-term leases (2009 amendment)*

* Paragraphs BC8A–BC8F were added as a consequence of amendments to IAS 17 made by *Improvements to IFRSs* issued in April 2009.

BC8A As part of its annual improvements project in 2007, the Board reconsidered the decisions it made in 2003, specifically the perceived inconsistency between the general lease classification guidance in paragraphs 7–13 and the specific lease classification guidance in paragraphs 14 and 15 related to long-term leases of land and buildings. The Board concluded that the guidance in paragraphs 14 and 15 might lead to a conclusion on the classification of land leases that does not reflect the substance of the transaction.

BC8B For example, consider a 999-year lease of land and buildings. In this situation, significant risks and rewards associated with the land during the lease term would have been transferred to the lessee despite there being no transfer of title.

BC8C The Board noted that the lessee in leases of this type will typically be in a position economically similar to an entity that purchased the land and buildings. The present value of the residual value of the property in a lease with a term of several decades would be negligible. The Board concluded that the accounting for the land element as a finance lease in such circumstances would be consistent with the economic position of the lessee.

BC8D The Board noted that this amendment reversed the decision it made in amending IAS 17 in December 2003. The Board also noted that the amendment differed from the International Financial Reporting Interpretations Committee's agenda decision in March 2006 based on the IAS 17 guidance that such long-term leases of land would be classified as an operating lease unless title or significant risks and rewards of ownership passed to the lessee, irrespective of the term of the lease. However, the Board believed that this change improves the accounting for leases by removing a rule and an exception to the general principles applicable to the classification of leases.

BC8E Some respondents to the exposure draft proposing this amendment agreed with the direction of this proposal but suggested that it should be incorporated into the Board's project on leases. The Board acknowledged that the project on leases is expected to produce a standard in 2011. However, the Board decided to issue the amendment now because of the improvement in accounting for leases that would result and the significance of this issue in countries in which property rights are obtained under long-term leases. Therefore, the Board decided to remove this potential inconsistency by deleting the guidance in paragraphs 14 and 15.

BC8F Some respondents raised concerns about the proposed requirement to apply the amendment retrospectively. The land and buildings elements of a long-term finance lease may have different amortisation bases. Accordingly, entities must obtain relative fair values even when both elements are classified as finance leases. The Board noted that this information should already be available because entities would have had to obtain it to adopt the 2003 amendment to IAS 17 that required the split between land and buildings elements for the purposes of lease classification. However, the Board acknowledged that the fair values at the inception of the leases might not be available in some situations. The Board noted that determining the fair value of the land element at the inception of long-term leases in these instances would require the use of hindsight and might not achieve comparability. Accordingly, the Board decided not to require retrospective application when the necessary information is not available. The Board also rejected prospective application of the amendment because the land element in existing long-term leases would be accounted for inconsistently. Therefore, the Board decided to adopt the modified retrospective transition requirement in paragraph 68A of IAS 17.

Dissenting opinion

Dissent of James J Leisenring from the amendment issued in April 2009

DO1 Mr Leisenring dissents from the amendment to IAS 17 *Leases* made by *Improvements to IFRSs* issued in April 2009.

DO2 Mr Leisenring believes that the amendment inappropriately permits an accounting that does not reflect the economic position of the lessee. In his view, land normally has an indefinite economic life, unlike other properties with finite useful lives. Therefore, it is not the lessee's land at the end of the lease even if the lease term is 999 years. He does not believe that a lessee is in a position economically similar to the purchaser of the land. Any appreciation in the land value does not accrue to the lessee at the termination of the lease. Furthermore, it is unclear how long the lease term must be for the Board to conclude that a lessee and a purchaser are in the same economic position.

DO3 This amendment also reverses the decision the Board made in amending IAS 17 in December 2003 and creates a divergence from US generally accepted accounting principles. Mr Leisenring agrees with some respondents that it is best to incorporate this amendment into the Board's broader project on lease accounting.

Amendment to Appendix to HKAS 18 *Revenue*

After example 20, a heading and example 21 are added.

Recognition and measurement

21 *Determining whether an entity is acting as a principal or as an agent (2009 amendment).*

Paragraph 8 states that 'in an agency relationship, the gross inflows of economic benefits include amounts collected on behalf of the principal and which do not result in increases in equity for the entity. The amounts collected on behalf of the principal are not revenue. Instead, revenue is the amount of commission.' Determining whether an entity is acting as a principal or as an agent requires judgement and consideration of all relevant facts and circumstances.

An entity is acting as a principal when it has exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. Features that indicate that an entity is acting as a principal include:

(a) the entity has the primary responsibility for providing the goods or services to the customer or for fulfilling the order, for example by being responsible for the acceptability of the products or services ordered or purchased by the customer;

(b) the entity has inventory risk before or after the customer order, during shipping or on return;

(c) the entity has latitude in establishing prices, either directly or indirectly, for example by providing additional goods or services; and

(d) the entity bears the customer's credit risk for the amount receivable from the customer.

An entity is acting as an agent when it does not have exposure to the significant risks and rewards associated with the sale of goods or the rendering of services. One feature indicating that an entity is acting as an agent is that the amount the entity earns is predetermined, being either a fixed fee per transaction or a stated percentage of the amount billed to the customer.

Amendment to HKAS 36 *Impairment of Assets*

Paragraph 80 is amended (new text is underlined and deleted text is struck through) and paragraph 140E is added.

Cash-generating units and goodwill

Recoverable amount and carrying amount of a cash-generating unit

Goodwill

Allocating goodwill to cash-generating units

80 For the purpose of impairment testing, goodwill acquired in a business combination shall, from the acquisition date, be allocated to each of the acquirer's cash-generating units, or groups of cash-generating units, that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated shall:

(a) represent the lowest level within the entity at which the goodwill is monitored for internal management purposes; and

(b) not be larger than an operating segment ~~determined in accordance with~~ as defined by paragraph 5 of HKFRS 8 *Operating Segments* before aggregation.

Transitional provisions and effective date

140E *Improvements to HKFRSs* issued in May 2009 amended paragraph 80(b). An entity shall apply that amendment prospectively for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

Amendment to Basis for Conclusions on HKAS 36 *Impairment of Assets*

In the Basis for Conclusions on HKAS 36, paragraphs BC150B and BC228A and its heading are added.

Allocating goodwill to cash-generating units (paragraphs 80–87)

BC150B Entities adopting IFRS 8 must reconsider the allocation of goodwill to cash-generating units because of the definition of operating segment introduced by IFRS 8. That definition affects the determination of the largest unit permitted by paragraph 80 of IAS 36 for testing goodwill for impairment. In 2008 the Board was made aware that divergent views had developed regarding the largest unit permitted by IAS 36 for impairment testing of goodwill. One view was that the unit is the operating segment level as defined in paragraph 5 of IFRS 8 *before* the aggregation permitted by paragraph 12 of IFRS 8. The other view was that the unit is the operating segment level as defined in paragraph 5 of IFRS 8 *after* the aggregation permitted by paragraph 12 of IFRS 8. The Board noted that the lowest level of the entity at which management monitors goodwill as required in paragraph 80(a) is the same as the lowest level of operating segments at which the chief operating decision maker regularly reviews operating results as defined in IFRS 8. The Board also noted that the linkage of the entity's goodwill monitoring level with the entity's internal reporting level is intentional, as described in paragraph BC140. The Board noted that aggregating operating segments for goodwill impairment testing into a unit larger than the level at which goodwill is monitored contradicts the rationale underlying IAS 36, as set out in paragraphs BC145–BC150. In addition, meeting the aggregation criteria of similar economic characteristics permitted in IFRS 8 does not automatically result in groups of cash-generating units that are expected to benefit from the synergies of allocated goodwill. Similarly, the aggregated segments do not necessarily represent business operations that are economically interdependent or work in concert to recover the goodwill being assessed for impairment. Therefore, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraph 80(b) to state that the required unit for goodwill impairment in IAS 36 is not larger than the operating segment level as defined in paragraph 5 of IFRS 8 before the permitted aggregation.

Transitional provisions (paragraphs 138–140)

Transitional provision for *Improvements to IFRSs* (2009)

BC228A The Board considered the transition provisions and effective date of the amendment to paragraph 80(b). The Board noted that the assessment of goodwill impairment might involve the use of hindsight in determining the fair values of the cash-generating units at the end of a past reporting period. Considering practicability, the Board decided that the effective date should be for annual periods beginning on or after 1 January 2010 although the Board noted that the effective date of IFRS 8 is 1 January 2009. Therefore, the Board decided that an entity should apply the amendment to paragraph 80(b) made by *Improvements to IFRSs* issued in April 2009 prospectively for annual periods beginning on or after 1 January 2010.

Amendment to HKAS 38 *Intangible Assets*

Paragraphs 36, 37, 40, 41 and 130C are amended (new text is underlined and deleted text is struck through) and paragraph 130E is added.

Recognition and measurement

Acquisition as part of a business combination

Measuring the fair value of an intangible asset acquired in a business combination

36 An intangible asset acquired in a business combination might be separable, but only together with a related contract, identifiable ~~tangible or intangible~~ asset or liability. ~~For example, a magazine's publishing title might not be able to be sold separately from a related subscriber database, or a trademark for natural spring water might relate to a particular spring and could not be sold separately from the spring.~~ In such cases, the acquirer recognises the intangible ~~group of~~ asset~~s as a single asset~~ separately from goodwill ~~if the individual fair values of the assets in the group are not reliably measurable~~, but together with the related item.

37 ~~Similarly, the terms 'brand' and 'brand name' are often used as synonyms for trademarks and other marks. However, the former are general marketing terms that are typically used to refer to a group of complementary assets such as a trademark (or service mark) and its related trade name, formulas, recipes and technological expertise.~~ The acquirer may recognise~~s~~ a group of complementary intangible assets as a single asset ~~a group of complementary intangible assets comprising a brand if the individual fair values of the complementary assets are not reliably measurable. If the individual fair values of the complementary assets are reliably measurable, an acquirer may recognise them as a single asset~~ provided the individual assets in the group have similar useful lives. For example, the terms 'brand' and 'brand name' are often used as synonyms for trademarks and other marks. However, the former are general marketing terms that are typically used to refer to a group of complementary assets such as a trademark (or service mark) and its related trade name, formulas, recipes and technological expertise.

40 If no active market exists for an intangible asset, its fair value is the amount that the entity would have paid for the asset, at the acquisition date, in an arm's length transaction between knowledgeable and willing parties, on the basis of the best information available. In determining this amount, an entity considers the outcome of recent transactions for similar assets. For example, an entity may apply multiples reflecting current market transactions to factors that drive the profitability of the asset (such as revenue, operating profit or earnings before interest, tax, depreciation and amortisation).

41 Entities that are ~~regularly~~ involved in the purchase and sale of ~~unique~~ intangible assets may have developed techniques for estimating their fair values indirectly. These techniques may be used for initial measurement of an intangible asset acquired in a business combination if their objective is to estimate fair value and if they reflect current transactions and practices in the industry to which the asset belongs. These techniques include, for example ~~when appropriate~~:

(a) discounting estimated future net cash flows from the asset; or

~~(a)~~(b) ~~applying multiples reflecting current market transactions to indicators that drive the profitability of the asset (such as revenue, market shares and operating profit) or to the royalty stream that could be obtained from licensing the intangible asset to~~ estimating the costs the entity avoids by owning the intangible asset and not needing:

(i) to license it from another party in an arm's length transaction (as in the 'relief from royalty' approach, using discounted net cash flows); or

(ii) to recreate or replace it (as in the cost approach).~~; or~~

~~(b) discounting estimated future net cash flows from the asset.~~

Transitional provisions and effective date

130C HKFRS 3 (as revised in 2008) amended paragraphs 12, 33–35, 68, 69, 94 and 130, deleted paragraphs 38 and 129 and added paragraph 115A. *Improvements to HKFRSs* issued in May 2009 amended paragraphs 36 and 37. An entity shall apply those amendments prospectively for annual periods beginning on or after 1 July 2009. Therefore, amounts recognised for intangible assets and goodwill in prior business combinations shall not be adjusted. If an entity applies HKFRS 3 (revised 2008) for an earlier period, it shall apply the amendments ~~shall also be applied~~ for that earlier period and disclose that fact.

130E *Improvements to HKFRSs* issued in May 2009 amended paragraphs 40 and 41. An entity shall apply those amendments prospectively for annual periods beginning on or after 1 July 2009. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

Amendment to Basis for Conclusions on HKAS 38 *Intangible Assets*

Paragraphs BC19C and BC19D are added.

Criteria for initial recognition

Acquisition as part of a business combination (paragraphs 33–38)

Reliability of measurement recognition criterion

BC19C When the Board developed IFRS 3 (as revised in 2008), it decided that if an intangible asset acquired in a business combination is separable or arises from contractual or other legal rights, sufficient information exists to measure the fair value of the asset reliably. The Board made related amendments to IAS 38 to reflect that decision. However, the Board identified additional amendments that were needed to reflect clearly its decisions on the accounting for intangible assets acquired in a business combination. Consequently, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraphs 36 and 37 of IAS 38 to clarify the Board's intentions.

BC19D Additionally, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraphs 40 and 41 of IAS 38 to clarify the description of valuation techniques commonly used to measure intangible assets at fair value when assets are not traded in an active market. The Board also decided that the amendments should be applied prospectively because retrospective application might require some entities to remeasure fair values associated with previous transactions. The Board does not think this is appropriate because the remeasurement might involve the use of hindsight in those circumstances.

Amendment to HKAS 39 *Financial Instruments: Recognition and Measurement*

Paragraphs 2(g), 80, 97, 100 and 108C are amended (new text is underlined and deleted text is struck through) and paragraph 103K is added.

Scope

2 **This Standard shall be applied by all entities to all types of financial instruments except:**

(a) ...

(g) <u>any forward</u> contract~~s~~ between an acquirer and a ~~vendor in a business combination~~ <u>selling shareholder</u> to buy or sell an acquiree <u>that will result in a business combination</u> at a future <u>acquisition</u> date<u>. The term of the forward contract should not exceed a reasonable period normally necessary to obtain any required approvals and to complete the transaction.</u>

(h) …

Hedging

Hedged items

Qualifying items

80 For hedge accounting purposes, only assets, liabilities, firm commitments or highly probable forecast transactions that involve a party external to the entity can be designated as hedged items. It follows that hedge accounting can be applied to transactions between entities ~~or segments~~ in the same group only in the individual or separate financial statements of those entities ~~or segments~~ and not in the consolidated financial statements of the group. As an exception …

Hedge accounting

Cash flow hedges

97 **If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gains or losses that were recognised in other comprehensive income in accordance with paragraph 95 shall be reclassified from equity to profit or loss as a reclassification adjustment (see HKAS 1 (as revised in 2007)) in the same period or periods during which the <u>hedged forecast cash flows</u> ~~asset acquired or liability assumed~~ affect~~s~~ profit or loss (such as in the periods that interest income or interest expense is recognised). However, if an entity expects that all or a portion of a loss recognised in other comprehensive income will not be recovered in one or more future periods, it shall reclassify into profit or loss <u>as a reclassification adjustment</u> the amount that is not expected to be recovered.**

100 **For cash flow hedges other than those covered by paragraphs 97 and 98, amounts that had been recognised in other comprehensive income shall be reclassified from equity to profit or loss as a reclassification adjustment (see HKAS 1 (revised 2007)) in the same period or periods during which the hedged forecast <u>cash flows</u> ~~transaction~~ affect~~s~~ profit or loss (for example, when a forecast sale occurs).**

Effective date and transition

103K *Improvements to HKFRSs* issued in May 2009 amended paragraphs 2(g), 97, 100 and AG30(g). An entity shall apply the amendments to paragraphs 2(g), 97 and 100 prospectively to all unexpired contracts for annual periods beginning on or after 1 January 2010. An entity shall apply the amendment to paragraph AG30(g) for annual periods beginning on or after 1 January 2010. Earlier application is permitted. If an entity applies the amendment for an earlier period it shall disclose that fact.

108C Paragraphs 9, 73 and AG8 were amended and paragraph 50A added by *Improvements to HKFRSs* issued in October 2008. Paragraph 80 was amended by *Improvements to HKFRSs* issued in May 2009. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. An entity shall apply the amendments in paragraphs 9 and 50A as of the date and in the manner it applied the 2005 amendments described in paragraph 105A. Earlier application of all the amendments is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

Amendment to application guidance on HKAS 39 *Financial Instruments: Recognition and Measurement*

Paragraph AG30(g) is amended (new text is underlined and deleted text is struck through).

Embedded derivatives (paragraphs 10–13)

AG30 The economic characteristics and risks of an embedded derivative are not closely related to the host contract (paragraph 11(a)) in the following examples. In these examples, assuming the conditions in paragraph 11(b) and (c) are met, an entity accounts for the embedded derivative separately from the host contract.

…

(g) A call, put, or prepayment option embedded in a host debt contract or host insurance contract is not closely related to the host contract unless:

(i) the option's exercise price is approximately equal on each exercise date to the amortised cost of the host debt instrument or the carrying amount of the host insurance contract; or~~.~~

(ii) the exercise price of a prepayment option reimburses the lender for an amount up to the approximate present value of lost interest for the remaining term of the host contract. Lost interest is the product of the principal amount prepaid multiplied by the interest rate differential. The interest rate differential is the excess of the effective interest rate of the host contract over the effective interest rate the entity would receive at the prepayment date if it reinvested the principal amount prepaid in a similar contract for the remaining term of the host contract.

~~From the perspective of the issuer of a convertible debt instrument with an embedded call or put option feature, t~~The assessment of whether the call or put option is closely related to the host debt contract is made before separating the equity element of a convertible debt instrument in accordance with ~~under~~ HKAS 32.

(h) ...

Amendment to Basis for Conclusions on HKAS 39 *Financial Instruments: Recognition and Measurement*

A heading, paragraphs BC24A–BC24E, a heading and paragraphs BC40B, BC40C and BC161A–BC161G are added. Paragraphs BC165, BC172 and BC172A are amended (new text is underlined and deleted text is struck through).

Scope

Business combination forward contracts

BC24A The Board was advised that there was diversity in practice regarding the application of the exemption in paragraph 2(g) of IAS 39. Paragraph 2(g) applies to particular contracts associated with a business combination and results in those contracts not being accounted for as derivatives while, for example, necessary regulatory and legal processes are being completed.

BC24B As part of the *Improvements to IFRSs* issued in April 2009, the Board concluded that paragraph 2(g) should be restricted to forward contracts between an acquirer and a selling shareholder to buy or sell an acquiree in a business combination at a future acquisition date and should not apply to option contracts, whether or not currently exercisable, that on exercise will result in control of an entity.

BC24C The Board concluded that the purpose of paragraph 2(g) is to exempt from the provisions of IAS 39 contracts for business combinations that are firmly committed to be completed. Once the business combination is consummated, the entity follows the requirements of IFRS 3. Paragraph 2(g) applies only when completion of the business combination is not dependent on further actions of either party (and only the passage of a normal period of time is required). Option contracts allow one party to control the occurrence or non-occurrence of future events depending on whether the option is exercised.

BC24D Several respondents to the exposure draft expressed the view that the proposed amendment should also apply to contracts to acquire investments in associates, referring to paragraph 20 of IAS 28. However, the acquisition of an interest in an associate represents the acquisition of a financial instrument. The acquisition of an interest in an associate does not represent an acquisition of a business with subsequent consolidation of the constituent net assets. The Board noted that paragraph 20 of IAS 28 explains only the methodology used to account for investments in associates. This should not be taken to imply that the principles for business combinations and consolidations can be applied by analogy to accounting for investments in associates and joint ventures. The Board concluded that paragraph 2(g) should not be applied by analogy to contracts to acquire investments in associates and similar transactions. This conclusion is consistent with the conclusion the Board reached regarding impairment losses on investments in associates as noted in the *Improvements to IFRSs* issued in May 2008 and stated in paragraph BC27 of the Basis for Conclusions on IAS 28.

BC24E Some respondents to the exposure draft raised concerns about the proposed transition requirement . The Board noted that determining the fair value of a currently outstanding contract when its inception was before the effective date of this amendment would require the use of hindsight and might not achieve comparability. Accordingly, the Board decided not to require retrospective application. The Board also rejected applying the amendment prospectively only to new contracts entered into after the effective date because that would create a lack of comparability between contracts outstanding as of the effective date and contracts entered into after the effective date. Therefore, the Board concluded that the amendment to paragraph 2(g) should be applied prospectively to all unexpired contracts for annual periods beginning on or after 1 January 2010.

Embedded derivatives

Embedded prepayment penalties (paragraph AG30(g))

BC40B The Board identified an apparent inconsistency in the guidance in IAS 39. The inconsistency related to embedded prepayment options in which the exercise price represented a penalty for early repayment (ie prepayment) of the loan. The inconsistency related to whether these are considered closely related to the loan.

BC40C The Board decided to remove this inconsistency by amending paragraph AG30(g). The amendment makes an exception to the examples in paragraph AG30(g) of embedded derivatives that are not closely related to the underlying. This exception is in respect of prepayment options, the exercise prices of which compensate the lender for the loss of interest income because the loan was prepaid. This exception is conditional on the exercise price compensating the lender for loss of interest by reducing the economic loss from reinvestment risk.

Hedging

BC161A If a hedged forecast transaction results in the recognition of a financial asset or a financial liability, paragraph 97 of IAS 39 required the associated gains or losses on hedging instruments to be reclassified from equity to profit or loss as a reclassification adjustment in the same period or periods during which the hedged item affects profit or loss (such as in the periods that interest income or interest expense is recognised).

BC161B The Board was informed that there was uncertainty about how paragraph 97 should be applied when the designated cash flow exposure being hedged differs from the financial instrument arising from the hedged forecast cash flows.

BC161C The example below illustrates the issue:

> An entity applies the guidance in the answer to Question F.6.2 of the guidance on implementing IAS 39. On 1 January 20X0 the entity designates forecast cash flows for the risk of variability arising from changes in interest rates. Those forecast cash flows arise from the repricing of existing financial instruments and are scheduled for 1 April 20X0. The entity is exposed to variability in cash flows for the three-month period beginning on 1 April 20X0 attributable to changes in interest rate risk that occur from 1 January 20X0 to 31 March 20X0.
>
> The occurrence of the forecast cash flows is deemed to be highly probable and all the other relevant hedge accounting criteria are met.
>
> The financial instrument that results from the hedged forecast cash flows is a five-year interest-bearing instrument.

BC161D Paragraph 97 required the gains or losses on the hedging instrument to be reclassified from equity to profit or loss as a reclassification adjustment in the same period or periods during which the asset acquired or liability assumed affected profit or loss. The financial instrument that was recognised is a five-year instrument that will affect profit or loss for five years. The wording in paragraph 97 suggested that the gains or losses should be reclassified over five years, even though the cash flows designated as the hedged item were hedged for the effects of interest rate changes over only a three-month period.

BC161E The Board believes that the wording of paragraph 97 did not reflect the underlying rationale in hedge accounting, ie that the gains or losses on the hedging instrument should offset the gains or losses on the hedged item, and the offset should be reflected in profit or loss by way of reclassification adjustments.

BC161F The Board believes that in the example set out above the gains or losses should be reclassified over a period of three months beginning on 1 April 20X0, and not over a period of five years beginning on 1 April 20X0.

BC161G Consequently, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraph 97 of IAS 39 to clarify that the gains or losses on the hedged instrument should be reclassified from equity to profit or loss during the period that the hedged forecast cash flows affect profit or loss. The Board also decided that to avoid similar confusion paragraph 100 of IAS 39 should be amended to be consistent with paragraph 97.

Hedging using internal contracts

BC165 IAS 39 does not preclude entities from using internal contracts as a risk management tool, or as a tracking device in applying hedge accounting for external contracts that hedge external positions. Furthermore, IAS 39 permits hedge accounting to be applied to transactions between entities in the same group ~~or between segments~~ in the *separate reporting* of those entities ~~or segments~~. However, IAS 39 does not permit hedge accounting for transactions between entities in the same group in consolidated financial statements. The reason is the fundamental requirement of consolidation that the accounting effects of internal contracts should be eliminated in consolidated financial statements, including any internally generated gains or losses. Designating internal contracts as hedging instruments could result in non-elimination of internal gains and losses and have other accounting effects. The Exposure Draft did not propose any change in this area.

BC172 The Board also decided to clarify that IAS 39 does not preclude hedge accounting for transactions between entities in the same group ~~or transactions between segments~~ in individual or separate financial statements of those entities ~~or reporting segments~~ because they are not internal to the entity (ie the individual entity ~~or segment~~).

BC172A Previously, paragraph<u>s</u> 73 <u>and 80</u> referred to the need for hedging instruments to involve a party external to the reporting entity. In doing so, ~~it~~ <u>they</u> used a segment as an example of a reporting entity. However, IFRS 8 *Operating Segments* requires disclosure of information that is reported to the chief operating decision maker even if this is on a non-IFRS basis. Therefore, the two IFRSs appeared to conflict. In *Improvements to IFRSs* issued in May 2008 <u>and April 2009</u>, the Board removed from paragraph<u>s</u> 73 <u>and 80</u> references to the designation of hedging instruments at the segment level.

Amendment to guidance on implementing HKAS 39 *Financial Instruments: Recognition and Measurement*

The answer to Question F.6.2 is amended (new text is underlined and deleted text is struck through).

F.6.2 Hedge accounting considerations when interest rate risk is managed on a net basis

Issue (j) – For cash flow hedges, if a derivative is used to manage a net exposure to interest rate risk and the derivative is designated as a cash flow hedge of forecast interest cash flows or portions of them on a gross basis, does the occurrence of the hedged forecast transaction give rise to an asset or liability that will result in a portion of the hedging gains and losses that were recognised in other comprehensive income remaining in equity?

No. In the hedging relationship described in Issue (c) above, the hedged item is a group of forecast transactions consisting of interest cash flows in specified future periods. The hedged forecast transactions do not result in the recognition of assets or liabilities and the effect of interest rate changes that are designated as being hedged is recognised in profit or loss in the period in which the forecast transactions occur. Although this is not relevant for the types of hedges described here, if instead the derivative is designated as a hedge of a forecast purchase of a financial asset or issue of a financial liability, the associated gains or losses that were recognised in other comprehensive income are reclassified from equity to profit or loss in the same period or periods during which the ~~asset acquired or liability incurred~~ <u>hedged forecast cash flows</u> affect~~s~~ profit or loss (such as in the periods that interest expenses are recognised). However, if an entity expects at any time that all or a portion of a loss recognised in other comprehensive income will not be recovered in one or more future periods, it shall reclassify immediately from equity to profit or loss the amount that is not expected to be recovered.

Amendment to HK(IFRIC)-Int 9 *Reassessment of Embedded Derivatives*

In the rubric, 'paragraphs 1–9' is amended to 'paragraphs 1–11'.

Paragraph 5 is amended (new text is underlined and deleted text is struck through) and paragraph 11 is added.

Scope

5 This interpretation does not ~~address the acquisition of contracts with embedded derivatives in~~ apply to embedded derivatives in contracts acquired in:

(a) a business combination (as defined in HKFRS 3 *Business Combinations* (as revised in 2008));

(b) a combination of entities or businesses under common control as described in paragraphs B1–B4 of HKFRS 3 (revised 2008); or

(c) the formation of a joint venture as defined in HKAS 31 *Interests in Joint Ventures*

~~n~~or their possible reassessment at the date of acquisition.*

Effective date and transition

11 Paragraph 5 was amended by *Improvements to HKFRSs* issued in May 2009. An entity shall apply that amendment prospectively for annual periods beginning on or after 1 July 2009. If an entity applies HKFRS 3 (as revised in 2008) for an earlier period, it shall apply the amendment for that earlier period and disclose that fact.

* HKFRS 3 (as revised in 2008) addresses the acquisition of contracts with embedded derivatives in a business combination.

Amendment to the Basis for Conclusions on HK(IFRIC)-Int 9 *Reassessment of Embedded Derivatives*

Paragraphs BC5A–BC5D are added.

Introduction

BC5A In 2009 the International Accounting Standards Board observed that the changes to the definition of a business combination in the revisions to IFRS 3 *Business Combinations* (as revised in 2008) caused the accounting for the formation of a joint venture by the venturer to be within the scope of IFRIC 9. Similarly, the Board noted that common control transactions might raise the same issue depending on which level of the group reporting entity is assessing the combination.

BC5B The Board observed that during the development of the revised IFRS 3, it did not discuss whether it intended IFRIC 9 to apply to those types of transactions. The Board did not intend to change existing practice by including such transactions within the scope of IFRIC 9. Accordingly, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraph 5 of IFRIC 9 to clarify that IFRIC 9 does not apply to embedded derivatives in contracts acquired in a combination between entities or businesses under common control or the formation of a joint venture.

BC5C Some respondents to the exposure draft *Post-implementation Revisions to IFRIC Interpretations* issued in January 2009 expressed the view that investments in associates should also be excluded from the scope of IFRIC 9. Respondents noted that paragraphs 20–23 of IAS 28 *Investments in Associates* state that the concepts underlying the procedures used in accounting for the acquisition of a subsidiary are also adopted in accounting for the acquisition of an investment in an associate.

BC5D In its redeliberations, the Board confirmed its previous decision that no scope exemption in IFRIC 9 was needed for investments in associates. However, in response to the comments received, the Board noted that reassessment of embedded derivatives in contracts held by an associate is not required by IFRIC 9 in any event. The investment in the associate is the asset the investor controls and recognises, not the underlying assets and liabilities of the associate.

Amendment to HK(IFRIC) Interpretation 16 *Hedges of a Net Investment in a Foreign Operation*

Paragraphs 14 and 18 are amended (new text is underlined and deleted text is struck through).

Conclusions

Where the hedging instrument can be held

14 A derivative or a non-derivative instrument (or a combination of derivative and non-derivative instruments) may be designated as a hedging instrument in a hedge of a net investment in a foreign operation. The hedging instrument(s) may be held by any entity or entities within the group ~~(except the foreign operation that itself is being hedged)~~, as long as the designation, documentation and effectiveness requirements of HKAS 39 paragraph 88 that relate to a net investment hedge are satisfied. In particular, the hedging strategy of the group should be clearly documented because of the possibility of different designations at different levels of the group.

Effective date

18 An entity shall apply this Interpretation for annual periods beginning on or after 1 October 2008. <u>An entity shall apply the amendment to paragraph 14 made by *Improvements to HKFRSs* issued in May 2009 for annual periods beginning on or after 1 July 2009.</u> Earlier application <u>of both</u> is permitted. If an entity applies this Interpretation for a period beginning before 1 October 2008, <u>or the amendment to paragraph 14 before 1 July 2009,</u> it shall disclose that fact.

Amendment to Basis for Conclusions on HK(IFRIC) Interpretation 16 *Hedges of a Net Investment in a Foreign Operation*

Paragraph BC24 is deleted (new text is underlined and deleted text is struck through). A footnote, paragraphs BC24A–BC24D, a heading and paragraph BC40A are added.

Consensus

Hedging instrument

Location of the hedging instrument (paragraph 14) and assessment of hedge effectiveness (paragraph 15)

BC24 ~~The IFRIC concluded that the foreign operation being hedged could not hold the hedging instrument because that instrument would be part of, and denominated in the same currency as, the net investment it was intended to hedge. In this circumstance, hedge accounting is unnecessary. The foreign exchange differences between the parent's functional currency and both the hedging instrument and the functional currency of the net investment will automatically be included in the group's foreign currency translation reserve as part of the consolidation process. The balance of the discussion in this Basis for Conclusions does not repeat this restriction.~~ *

* Paragraph BC24 was deleted and paragraphs BC24A–BC24D and paragraph BC40A added as a consequence of *Improvements to IFRSs* issued in April 2009.

BC24A Paragraph 14 of IFRIC 16 originally stated that the hedging instrument could not be held by the foreign operation whose net investment was being hedged. The restriction was included in draft Interpretation D22 (from which IFRIC 16 was developed) and attracted little comment from respondents. As originally explained in paragraph BC24, the IFRIC concluded, as part of its redeliberations, that the restriction was appropriate because the foreign exchange differences between the parent's functional currency and both the hedging instrument and the functional currency of the net investment would automatically be included in the group's foreign currency translation reserve as part of the consolidation process.

BC24B After IFRIC 16 was issued, it was brought to the attention of the International Accounting Standards Board that this conclusion was not correct. Without hedge accounting, part of the foreign exchange difference arising from the hedging instrument would be included in consolidated profit or loss. Therefore, in *Improvements to IFRSs* issued in April 2009, the Board amended paragraph 14 of IFRIC 16 to remove the restriction on the entity that can hold hedging instruments and deleted paragraph BC24.

BC24C Some respondents to the exposure draft *Post-implementation Revisions to IFRIC Interpretations* (ED/2009/1) agreed that a parent entity should be able to use a derivative held by the foreign operation being hedged as a hedge of the net investment in that foreign operation. However, those respondents recommended that the amendment should apply only to derivative instruments held by the foreign operation being hedged. They asserted that a non-derivative financial instrument would be an effective hedge of the net investment only if it were issued by the foreign operation in its own functional currency and this would have no foreign currency impact on the profit or loss of the consolidated group. Consequently, they thought that the rationale described in paragraph BC24B to support the amendment did not apply to non-derivative instruments.

BC24D In its redeliberations, the Board confirmed its previous decision that the amendment should not be restricted to derivative instruments. The Board noted that paragraphs AG13–AG15 of IFRIC 16 illustrate that a non-derivative instrument held by the foreign operation does not need to be considered to be part of the parent's net investment. As a result, even if it is denominated in the foreign operation's functional currency a non-derivative instrument could still affect the profit or loss of the consolidated group. Consequently, although it could be argued that the amendment was not required to permit non-derivative instruments to be designated as hedges, the Board decided that the proposal should not be changed.

Effective date of amended paragraph 14

BC40A The Board amended paragraph 14 in April 2009. In ED/2009/01 the Board proposed that the amendment should be effective for annual periods beginning on or after 1 October 2008, at the same time as IFRIC 16. Respondents to the exposure draft were concerned that permitting application before the amendment was issued might imply that an entity could designate hedge relationships retrospectively, contrary to the requirements of IAS 39. Consequently, the Board decided that an entity should apply the amendment to paragraph 14 made in April 2009 for annual periods beginning on or after 1 July 2009. The Board also decided to permit early application but noted that early application is possible only if the designation, documentation and effectiveness requirements of paragraph 88 of IAS 39 and of IFRIC 16 are satisfied at the application date.

Effective for annual periods
beginning on or after 1 June 2006

HK(IFRIC) Interpretation 9

Reassessment of Embedded Derivatives

(a)	An entity shall apply amendments to HK(IFRIC)-Int 9 and HKAS 39 on *Embedded Derivatives* issued in March 2009 for annual periods ending on or after 30 June 2009.
(b)	An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 prospectively for annual periods beginning on or after 1 July 2009.

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Effective for annual periods
beginning on or after 1 October 2008

HK(IFRIC) Interpretation 16

Hedges of a Net Investment in a Foreign Operation

An entity shall apply amendments resulting from *Improvements to HKFRSs 2009* issued in May 2009 for annual periods beginning on or after 1 July 2009.

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