

SSAP 20, Related Party Disclosures

Background

SSAP 20 came into effect for financial statements covering periods beginning on or after 1 October 1997.

Questions and answers on SSAP 20 appear below.

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Disclaimer

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Feedback welcomed

We welcome your comments and feedback. Comments and suggestions on the material in this document should be addressed to Mr. Simon Riley, Deputy Director – Accounting, Hong Kong Society of Accountants, e-mail: commentletters@hksa.org.hk.

Relevant links

SSAP 20..... http://www.hksa.org.hk/professionaltechnical/pronouncements/handbook/volume2a/2_120.htm

Summary of SSAP 20..... <http://www.hksa.org.hk/professionaltechnical/accounting/standards/ssap20.pdf>

Exposure Draft of a proposed revision of SSAP 20 (included in the “Improvements ED issued in 2002”
..... <http://www.hksa.org.hk/professionaltechnical/accounting/exposuredraft/edimprovements.pdf>

..... <http://www.hksa.org.hk/professionaltechnical/accounting/exposuredraft/02-imp-ed.pdf> (refer IAS 24)

HKSA Financial Reporting home page <http://www.hksa.org.hk/professionaltechnical/accounting/>

Reference materials page <http://www.hksa.org.hk/professionaltechnical/accounting/rm>

SSAP 20.05-1 Determining whether one party is considered to be related to another***Q: How does SSAP 20 determine that one party is related to another?***

A: Under SSAP 20 paragraph 5, “parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence.”

For the purpose of SSAP 20:

“Control” is the ownership, directly or indirectly, of more than one half of the voting power of an entity, or a substantial interest in voting power and the power to direct, by statute or agreement, the financial and operating policies of the management of the entity; and

“Significant influence” is the participation in the financial and operating policy decisions of an entity, but not control of those policies. Significant influence may be exercised in several ways, usually by representation on the board of directors but also by, for example, participation in the policy making process, material intercompany transactions, interchange of managerial personnel or dependence on technical information. Significant influence may be gained by share ownership, statute or agreement. With share ownership, significant influence is presumed in accordance with the definition contained in SSAP 10 “Accounting for Investments in Associates”.

Subject to the proviso (*) below, the SSAP deals specifically with the following related party relationships:

- (a) Entities that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting entity (this includes holding companies, subsidiaries and fellow subsidiaries);
- (b) Joint ventures and associated companies of the reporting entity, and entity that, directly or indirectly, have significant influence over or are under common significant influence with the reporting entity;
- (c) Individuals owning, directly or indirectly, an interest in the voting power of the reporting entity that gives them control or significant influence over the entity, and close members of the family of any such individual (close members of the family of an individual are those that may be expected to influence, or be influenced by, that person in their dealings with the entity);
- (d) Key management personnel of the reporting entity and its holding companies, and close members of the family of such individuals. Key management personnel are those persons that have authority and responsibility for planning, directing and controlling the activities of an entity (in the case of a company, this would include directors and officers); and
- (e) Entities over which any person described in (c) or (d) above are able to exercise control or significant influence. This includes entities owned by directors or major shareholders of the reporting entity and entities that have a member of key management in common with the reporting entity;

* The following are deemed not to be related parties:

- ✓ Two entities solely on the basis that they have one or more non-executive directors (or equivalent persons in an unincorporated entity) in common, so long as those directors do not have significant influence to be able to affect the policies of both entities in their mutual dealings);

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- ✓ Providers of finance, trade unions, public utilities, government departments and agencies, in the course of their normal dealings with an entity by virtue only of those dealings (although they may circumscribe the freedom of action of an entity or participate in its decision-making process); and
 - ✓ A single customer, supplier, franchiser, distributor, or general agent with whom an entity transacts significant volume of business merely by virtue of the resulting economic dependence.

The fact that there may or may not be transactions between two parties during a given period of time is not relevant to determining whether two parties are related for the purposes of SSAP 20.

Example

To illustrate the definition in SSAP 20 paragraph 5, let us assume that:

- ✓ Entity X, the “reporting entity”, prepares its financial statements in accordance with Hong Kong SSAPs; and
- ✓ Entity Y (a company, a natural person, etc.) has an ownership interest in Entity X.

For X’ s financial statements, the following are deemed under SSAP 20 to be a related party of X:

- ✓ Entity Y – but only when Entity X would be regarded under the SSAPs (either directly or through one or more intermediate entities) as a subsidiary (under SSAP 32), joint venture (under SSAP 21) or associate (under SSAP 10) of Entity Y.

In such a case where Y is a related party then all other subsidiaries, joint ventures or associates of Entity Y will also be deemed to a related party of X.

- ✓ Persons described in (c), (d) and (e) above.

To illustrate further, Entity Y has a controlling interest in Entity X (either directly or indirectly through one or more subsidiaries). X is therefore a subsidiary of Y. Y also owns 35% of Entity Z and, because Y does not have outright or shared control but rather exercises significant influence over Z, Z is accounted for as an associate in Y’ s financial statements. X and Z are related parties by virtue of Y having both significant influence over Z and control over X.