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

TechWatch News at a glance

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TechWatch updates you on technical developments in financial reporting, auditing, regulation and business. The Institute welcomes your comment, emailed to < commentletters@hkicpa.org.hk >. Click here for past issues.

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Steve Ong (Editor), Selene Ho, Winnie Chan, Katherine Leung, Ben Lo

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Peter Tisman (Editor), Elena Chai, Mary Lam, Sharon Yeung

Financial Reporting, Auditing and Ethics

New!

1. The Revised Code of Ethics Seminar

The Institute issued the Revised Code of Ethics for Professional Accountants ("Revised Code") in June 2010, which is effective from 1 January 2011. The Revised Code maintains the principles-based approach and covers guidance on accepting payment in an agent-principal relationship under the Prevention of Bribery Ordinance.

The Institute will hold the Revised Code of Ethics Seminar in conjunction with the ICAC on 15 March 2011. A Senior Community Relations Officer of the ICAC Regional Office (Hong Kong East) will also talk on Professional Ethics – The Best Defence Against Corruption.

To secure seats, please register early by completing the **registration form**.

2. Financial Reporting and Auditing Alert – Issue 14

The Institute issued **Financial Reporting and Auditing Alert – Issue 14** ("Alert") in relation to the preparation of accounting records and financial statements for an audit client.

The Alert makes reference to the recent court judgment on a disciplinary action by the Institute and the Revised Code which is effective on 1 January 2011.

The Revised Code is based on the principle of "threats and safeguards". Auditors are required to assess potential threats to independence and, where possible, implement safeguards to eliminate or reduce the threat to an acceptable level.

Members are assured that the Revised Code and the law does continue to allow members to provide accounting services, to their audit clients upon certain conditions being satisfied.

To help members, the Alert sets out the latest requirements and guidance in the Revised Code.

Members are reminded that when providing services in relation to preparation of accounting records and financial statements to audit clients that are not public interest entities, it is necessary to evaluate the significance of any threat created and employ appropriate safeguards.

For audit clients that are public interest entities, the Revised Code recognizes that more stringent requirements are necessary and a firm shall not provide accounting and bookkeeping services, except in emergency situations.

Financial Reporting

3. FRSC Minutes

This **FRSC minutes** on 11 January 2011 covers:

- HKICPA Accounting Bulletin 4 *Guidance on the Determination of Realized Profits and Losses in the Context of Distributions under the Hong Kong Companies Ordinance*
- HK Interpretation 5 *Presentation of Financial Statements – Classification by the Borrower of a Term Loan that Contains a Repayment on Demand Clause*
- HKFRS for Private Entities and SME-FRF & FRS
- IFRS Practice Statement on Management Commentary
- Business Combination under Common Control
- IFRS Interpretations Committee Review
- IASB ED of Hedge Accounting
- Comparison between HKFRSs and IFRSs as at 1 January 2011

4. Invitation to Comment on Consultation Documents

(i) IASB Supplement to ED of *Financial Instruments: Impairment*

The Institute has issued an **Invitation to Comment** on IASB Supplement to ED of *Financial Instruments: Impairment,* with comments requested by **9 March 2011**.

At present, IFRSs and US generally accepted accounting principles ("GAAP") account for credit losses using an incurred loss model, which requires evidence of a loss (known as a trigger event) before financial assets can be written down. The IASB and the Financial Accounting Standards Board ("the boards") have proposed moving to an expected loss model that provides a more forward-looking approach to how credit losses are accounted for, which they believe better reflects the economics of lending decisions.

The proposals are published as a supplement to an exposure draft published by the IASB in November 2009, and a separate FASB exposure draft published in May 2010. Those exposure drafts outlined different methods to account for credit impairment. Since then, the boards have worked to align their approaches. In doing so, they have sought to take account of responses to the original exposure drafts and recommendations made by the Expert Advisory Panel ("EAP"), an external group of risk management experts tasked with considering the operational consequences of applying an expected loss model as well as responses to the FASB proposal.

A summary prepared by the IASB on the ED is set out in the Appendix to the Invitation to Comment.

(ii) IFRS Foundation Monitoring Board Paper for Public Consultation – Consultative Report on the Review of the IFRS Foundation's Governance

The Institute has issued an **Invitation to Comment** on IFRS Foundation Monitoring Board Paper for Public Consultation – Consultative Report on the Review of the IFRS Foundation's Governance, with comments requested by **18 March 2011**.

The Monitoring Board review's fundamental question is whether the current governance structure effectively promotes the standard-setter's primary mission of setting high quality, globally accepted standards as set forth in the Constitution of the IFRS Foundation, and whether the standard-setter is appropriately independent yet accountable. The primary focus of the review is institutional aspects relating to governance, in particular the composition and the respective responsibilities and roles of the Monitoring Board, Trustees and IASB.

The Monitoring Board plans to organize public meetings with stakeholders in Asia, Europe and the Americas during this consultation period to enhance involvement of stakeholders in the review project. Thereafter, an action plan for implementation of the proposals will be developed and published by early in the third quarter of 2011.

(iii) IASB ED of *Offsetting Financial Assets and Financial Liabilities*

The Institute has issued an **Invitation to Comment** on IASB ED of *Offsetting Financial Assets and Financial Liabilities,* with comments requested by **7 April 2011**.

At present, the circumstances when financial assets and financial liabilities may be presented in an entity's statement of financial position as a single net amount, or as two gross amounts, differs depending on whether the entity reports using IFRSs or US GAAP.

The accounting differences result in the single largest quantitative difference in reported numbers in statements of financial position prepared in accordance with IFRSs or US GAAP. This reduces the comparability of financial statements, and is especially prominent in the presentation of derivative assets and derivative liabilities by financial institutions. As a result, users and preparers of financial statements have asked the IASB and the US Financial Accounting Standards Board to find a common solution for offsetting those items. Proposing a common solution is also consistent with requests from the G20 and the Financial Stability Board.

The boards are proposing that offsetting should apply only when the right of set-off is enforceable at all times, including in default and bankruptcy, and the ability to exercise this right is unconditional, that is, it does not depend on a future event. The entities involved must intend to settle the amounts due with a single payment or simultaneously. Provided all of these requirements are met, offsetting would be required. The proposals would amend IFRSs and US GAAP and eliminate several industry-specific netting practices.

A summary prepared by the IASB on the ED is set out in the Appendix to the Invitation to Comment.

(iv) SME Implementation Group Draft Question and Answer on Use of IFRS for SMEs in Parent's Separate Financial Statements

The Institute has issued an **Invitation to Comment** on SME Implementation Group ("SMEIG") Draft Question and Answer ("Q&A") on Use of IFRS for SMEs in Parent's Separate Financial Statements, with comments requested by **28 March 2011**.

The Institute has adopted the IFRS for SMEs in Hong Kong with some local modifications, in the form of HKFRS for Private Entities, as a reporting option for private companies which have no public accountability.

The draft Q&A (2011/01) addresses whether a parent entity that itself does not have public accountability may present its separate financial statements in accordance with the IFRS for SMEs if it is part of a group that is required (or elects) to present consolidated financial statements in accordance with full IFRSs. The Q&As issued by the SMEIG are intended to provide non-mandatory and timely guidance on specific accounting questions that are being raised with the SMEIG by users implementing the IFRS for SMEs.

5. Institute Comments on IASB Request for Views on Effective Dates and Transition Methods

The Institute made a **submission** to IASB Request for Views on Effective Dates and Transition Methods and the Institute generally supports the sequential approach to implementing the new standards. The Institute believes it would be necessary for the IASB to distinguish between two groups of standards based on their complexity of application and impact on financial reporting:

- Group 1 - Revenue from Contracts with Customers, Leases, Insurance Contracts, Financial Instruments, and Fair Value Measurements

  It is believed that the changes that may be introduced by these standards may have a pervasive impact on financial statements of a wide range of different entities and/or require extensive system changes to capture the necessary information at the point of each relevant transaction. Given their scopes of application are closely related, the Institute considers these projects should be effective simultaneously and entities should be given a sufficient lead time to implement them. The Institute recommends that the mandatory effective date should be no earlier than 1 January 2015.

- Group 2 - Consolidation, Joint Arrangements, Post-Employment Benefit and Presentation of Other Comprehensive Income

The Institute believes that the proposed IFRSs on Consolidations and Joint Arrangements could also have a pervasive impact on financial statements; however, the impact of consolidation or non-consolidation can be more easily described and quantified. Consequently, the Institute would not object to these two IFRSs be effective before those in Group 1 but their effective dates should be the same.

The other proposed IFRSs would represent more contained changes to financial statements. The Institute would not object to the effective date of these standards being before 1 January 2015, on a case-by-case basis.

Audit & Assurance

6. Institute Comments on IAASB Proposed Amendments to the Preface and Proposed IAPS 1000

The Institute made a **submission** to IAASB Proposed Amendments to the *Preface to the International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements* ("Preface") and Proposed IAPS 1000 *Special Considerations in Auditing Complex Financial Instruments*. The Institute supports the proposed plan to clarify the status and authority of the IAPS in the proposed Preface and withdrawal of existing IAPSs. In addition, it is believed that the proposed IAPS 1000 provides guidance on the audit considerations as well as providing educational information.

International Meetings

7. International Accounting Standards Board

The IASB met on 1-2 February, 15-18 February 2011, and discussed the following topics:

- Consolidation and joint arrangements
- Cross-cutting issues
- Financial instruments: impairment
- Insurance contracts
- Leases
- Post-employment benefits
- Revenue recognition

Click to view the IASB Update on the meetings on **1-2 February** and **15-18 February**. The IASB next meets in March 2011.

8. IFRS Interpretations Committee

The IFRS Interpretations Committee next meets in March 2011. Click **here** for the next meeting's details.

9. International Auditing and Assurance Standards Board

The IAASB next meets in March 2011. Click **here** for the next meeting's details and previous meeting summary.

10. International Ethics Standards Board for Accountants

The IESBA next meets in June 2011. Click **here** for the next meeting's details and previous meeting summary.

Useful Resources

11. Publications

The following are publications on various topics:

(i) Revised Code of Ethics:

- **Staff Q & A** by the IESBA

(ii) Leases of land:

- **IFRS Practice issues** by KPMG

(iii) Wave of accounting change:

- **IFRS/HKFRS news** by PwC

Comment Due Dates

9 March 2011: IASB Supplement to ED of *Financial Instruments: Impairment*

14 March 2011: IFAC's IAASB Consultation Paper on *Proposed Strategy and Work Program for 2012-2014*

18 March 2011: IFRS Foundation Monitoring Board Paper for Public Consultation – Consultative Report on the Review of the IFRS Foundation's Governance

28 March 2011: SME Implementation Group Draft Question and Answer on Use of IFRS for SMEs in Parent's Separate Financial Statements

7 April 2011: IASB ED of *Offsetting Financial Assets and Financial Liabilities*

21 April 2011: IAASB ED on Proposed ISRE 2400 (Revised) *Engagements to Review Historical Financial Statements*

3 May 2011: IAASB DP on *The Evolving Nature of Financial Reporting: Disclosure and its Audit Implications*

20 May 2011: IAASB ED on Proposed ISAE 3410 *Assurance Engagements on Greenhouse Gas Statements*

Specialist Practices, Business Members and Advocacy

Corporate Finance

12. Government to Legislate on Disclosure of Price Sensitive Information

On 11 February 2011, the government **released** consultation **conclusions** on legislative proposals for price sensitive information ("PSI") disclosures, announcing that it would implement a statutory PSI disclosure regime to encourage a continuous disclosure culture among listed corporations and to enhance market transparency and quality. A set of **FAQs** on the statutory PSI disclosure regime has also been published.

Under the statutory regime, a listed corporation has to disclose PSI to the public as soon as reasonably practicable after the PSI (to be referred to as "inside information") has come to its knowledge. The Securities and Futures Commission ("SFC") will be the enforcement authority and the Market Misconduct Tribunal ("MMT") will determine whether a breach of the PSI disclosure requirement has occurred. The law will also empower the SFC to conduct investigations into suspected breaches and provide for alleged breaches to be heard by an independent tribunal.

"Safe harbours", which aim to safeguard the legitimate interests of listed corporations in keeping certain types of information confidential, such as trade secrets or information about incomplete negotiations, will be set out in the law. A new provision will be added to the effect that where a piece of information has been leaked, and a safe harbour becomes irrelevant, it will be a defence for the corporation to prove that it has taken reasonable measures to monitor the confidentiality and it has made disclosure as soon as reasonably practicable when it becomes aware of the leak.

In line with the objective of cultivating a continuous disclosure culture, and to improve corporate governance, in addition to the proposed range of civil remedies, the MMT will be empowered to order an officer or a director to undergo training, or to order a listed corporation to appoint an independent professional adviser to review its compliance procedure or advise on compliance matters.

At the same time, the SFC published **consultation conclusions** on the draft guidelines on disclosure of "inside information" (the term used to define PSI), which seeks to assist listed corporations to comply with the statutory obligation by providing guidance on the interpretation of inside information, and explaining the application of safe harbours.

The government aims at introducing a bill into the Legislative Council ("LegCo") in the 2010/11 legislative year to codify the disclosure requirements in the Securities and Futures Ordinance (Cap. 571) ("SFO"). The SFC guidelines will be finalized in the light of the consultation conclusions and the text of the bill, and will be published when the legislation is settled.

See the Institute's **submission**, reported in **TechWatch no. 94** (item 16).

13. SFC to Refine Evidential Requirements for Proving Professional Investor Status

On 23 February 2011, the SFC **released** a set of **conclusions** drawn from a public consultation, announcing that it would proceed to refine the requirements for determining whether a person qualifies as a high-net-worth professional investor under the Securities and Futures (Professional Investor) Rules ("PI Rules"), including:

(i) to adopt a principles-based approach so that firms may use methods that are appropriate in the circumstances to satisfy themselves that an investor meets the relevant assets or portfolio threshold at the relevant date to qualify as a professional investor;

(ii) to preserve the existing methods set out in sections 3(a) to 3(c) of the current PI Rules to enable firms to continue with the existing practices; and

(iii) to extend the application of section 3(d) of the existing PI Rules to all three types of high-net-worth professional investors under sections 3(a)-(c), namely, trust corporations, individuals and corporations/partnerships. So, any corporation, which is wholly-owned by one or more trust corporations, individuals or corporations/partnerships, where each of the owners qualifies as a professional investor under sections 3(a)-(c) of the PI Rules, will qualify as a professional investor.

In its **submission**, the Institute expressed some reservations about the practical aspects of the proposal, as reported in **TechWatch no. 98** (item 21(iii)).

14. Credit Rating Agencies in Hong Kong to be Regulated

The government plans to add "provision of credit rating services" as a new type of regulated activity under the SFO, in order to create a regulatory regime for credit rating agencies operating in Hong Kong. Under the regulatory regime, both corporate credit rating agencies in Hong Kong and their individual rating analysts will need to be licensed and will be subject to the general obligations common to all persons licensed or registered under the SFO.

In this connection, the **Securities and Futures Ordinance (Amendment of Schedule 5) Notice 2011** and the **Securities and Futures (Financial Resources) (Amendment) Rules 2011** were published in the gazette on 18 February 2011. The notice adds "Type 10: providing credit rating services" to Schedule 5 to SFO and definitions for "credit ratings", "debt securities", "preferred securities" and "providing credit rating services". The rules stipulate capital requirements for Type 10 licensed corporations and related matters.

The notice and rules were tabled before the LegCo on 23 February 2011, and they will come into operation on 1 June 2011.

SFC will produce a new code of conduct for persons providing credit rating services to help ensure that the credit ratings are independent, objective and of appropriate quality.

Taxation

15. Annual Meeting with the Inland Revenue Department

The annual meeting between representatives of the Institute's Taxation Committee and the Inland Revenue Department ("IRD") took place on 11 February 2011. Among the items discussed at the meeting, the following filing deadlines are highlighted for immediate attention.

The IRD confirmed the following due dates for lodging profits tax returns for the year of assessment 2010/11:

Accounting date	Extended due date	Further extended due date (for electronic filing)
"N" Code	3-May-11 (no extension)	17-May-11
"D" Code	15-Aug-11	29-Aug-11
"M" Code	15-Nov-11	29-Nov-11
"M" Code (current year loss cases)	31-Jan-12	31-Jan-12

16. 2011-12 Budget Speech

The **budget speech** was delivered on 23 February 2011. The Institute issued its **budget proposals** in January. In a **press release** responding to the budget speech, the Institute noted some positive measures announced by the government, including:

- accepting the Institute's recommendation to **increase by 20 percent the dependants' allowances for parents, grandparents and children**; and
- initiatives in education and more support for vulnerable groups, such as the elderly, disabled, new immigrants and ethnic minorities,

while also pointing to areas where more should be done. These included:

- inflation-linked retail bonds, which aim to tackle inflation by paying inflation-based interest. The total amount made available in the bond programme should be increased;
- housing concerns. The Institute's proposals – home rental tax deduction, property-inflation-adjusted stamp duty rates, and a stamp duty exemption for first-time buyers for properties for self-use, costing up to $6 million, would have given quicker help to the younger people and middle class families. However, the government's proposed changes to land supply will take longer to have any effect on the market;
- $6,000 injection into MPF accounts should have been targeted at lower and middle-income groups;
- lack of tax measures to enhance Hong Kong's international competitiveness, while competitors make use of their tax systems to attract new business. For example, there were insufficient measures to reinforce Hong Kong's pillar and new industries, including financial services, innovation and technology, and regional operations. The Institute's call to lower taxes for small companies with gross revenue of less than $2 million was also not accepted; and
- measures to clean up the environment were lacking, e.g. the Institute's proposed tax breaks for green buildings and higher road taxes for polluting vehicles.

17. Useful links from the IRD

The following are useful links from the IRD:

- **Information on business registration e-application and new application forms**
- **Advance ruling case no. 44 relating to Inland Revenue Ordinance, sections 14 and 20(2)**
- **Departmental interpretation and practice notes 5 (DIPN) (Revised) which has been revised mainly to include "environmental protection facilities"**
- **Stamp office interpretation and practice notes 2 on relief for stock borrowing and lending transactions, which has been revised**
- **Double taxation agreements with Ireland and Hungary came into effect on 10 and 23 February 2011 respectively**

Legislation & Other Initiatives

18. Companies Registry Update

The Companies Registry's website has been updated, as follows:

- The content of the '"Electronic Services" → "**Electronic Submission of Information**" section
- The following new information pamphlets can be downloaded from the "Publications and Press Releases" → "**Information Pamphlets**" section:
  - **Obligations after Company and Business Registration**
  - **Requirements for Documents Delivered in the Form of Electronic Records**
- Old versions (July 2008) of the following specified forms have been removed from the "Public Forms" → "**Specified Forms**" section:
  - NC1 – Incorporation Form (Company limited by shares)
  - NC1G – Incorporation Form (Company not limited by shares)
- A revised "**Guide on Communications by a Company to Another Person Other than the Registrar**" has been uploaded under the "Publications and Press Releases" → "**Memorandum Notes/Guidelines**" section

19. Combating Money Laundering/Terrorist Financing

Members should note the following notices in relation to combating money laundering/terrorist financing:

- **Government notice 632**: A list of relevant persons specified under the United Nations Sanctions (Côte d'Ivoire) Regulation. The regulation was made under the United Nations Sanctions Ordinance that was published as **legal notice 9 of 2011** in the gazette.
- Legal notice **10** and **11**: The United Nations Sanctions (Arms Embargoes) Regulation (Repeal) Regulation and the United Nations Sanctions (Sierra Leone) (Immigration Control) Regulation (Repeal) Regulation were made under the United Nations Sanctions Ordinance.
- **US executive order 13224**: Changes to the list relating to "Blocking property and prohibiting transactions with persons who commit, threaten to commit or support terrorism".

For more background information on the current law in Hong Kong relating to anti-money laundering, see the Institute's **Legal Bulletin 1**, "Requirements on anti-money laundering, anti-terrorist financing and related matters".

Useful Resources

20. Library Resources

Featured titles and **new books** of high reference value for members are now available. In addition, members can **login** to the **e-Library** and access e-journals and e-books on a wide range of business subjects.

21. Other Publications

The following articles/publications on topical issues may be of interest to members:

(i) In February 2011, HKEx published:

- **presentation materials** on Mixed Media Offer
- **findings** of its Cash Market Transaction Survey 2009/10
- a **listing decision** on whether a contractual right to acquire a company's interest in a joint venture was an "option" under Chapter 14 of the Listing Rules (LD2-2011)
- **report** on IPO applications, delisting and suspensions (as at 28 February 2011)

(ii) In February 2011, SFC published:

- **Quarterly Report** for October to December 2010

(iii) Articles on corporate governance by Deloitte:

- **Today's boards have a role to play in building employee trust**
- **The tech-intelligent board: priorities for tech-savvy directors as they oversee IT risk and strategy**
- **Implications of the SEC's evolving agenda on corporate governance**

(iv) **Money laundering – card tricks** from GAA Accounting/Canadian Institute of Chartered Accountants