SUMMARY OF MEETING WITH SMALL AND MEDIUM-SIZED PRACTITIONERS

Request for Information on Post-implementation Review: Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (SME Standard)

Date: 22 January 2019

Time: 14:00 – 15:00

Venue: HKICPA VIP Room, 37/F Wu Chung House, Wanchai

Present:

Edmund Wong, Patrick Wong C.P.A. Limited

Webster Ng, Webster Ng & Co.

Anthony Wong, Standard Setting, HKICPA

1. Edmund and Webster provided their feedback on the questions in the Request for Information on the post-implementation review (PIR) of the SME Standard (see paragraphs 2 to 14 below).

Extract of Question 1 in the Request for Information
(a) *Please tell us about your role with respect to financial reporting (for example, preparer of financial statements, auditor, regulator, academic, accounting professional body, or user of financial statements and, if so, the type of user) and your experience in applying the SME Standard.* (b) *If you are a preparer, we would like to know the following:* (i) *Which standard(s) are applied in preparing your company or group financial statements (for example, SME Standard, HKFRS for Private Entities or HKFRS)?* (ii) *Why you are applying the respective standard(s) mentioned in question 1(b)(i)?* (iii) *(If relevant) How many sets of financial statements are prepared within your group?*

2. Edmund and Webster are practitioners from accounting firms. Their clients mainly use the SME Standard or HKFRS to prepare their financial statements.

Extract of Question 2 in the Request for Information
(a) *(This question is for lessors) As the SME Standard currently does not include accounting requirements for lessors, how have you accounted for leases?* (b) *Do you support adding accounting requirements for lessors to the SME Standard? Why, or why not?*

3. Edmund and Webster supported adding accounting requirements for lessors to

the SME Standard and this is consistent with the views of targeted stakeholders[1] in the first phase of the PIR. They commented that, applying paragraph 2.1[2] of the SME Standard, most SME lessors account for operating lease rental income and adjust for the rent free period (if any) on a straight-line basis over the lease term.

Extract of Question 3 in the Request for Information	
(a)	*Have you been impacted by the SME Standard which currently does not explicitly allow or include a 'presentation currency' concept as in HKAS 21?*
(b)	*Do you support adding the 'presentation currency' concept to the SME Standard? Why, or why not?*

4. Edmund and Webster observed that, applying paragraph 2.1, SMEs select an accounting policy based on the 'presentation currency' concept in the HKAS 21 *The Effects of Changes in Foreign Exchange Rates* if they have operations that are based outside of Hong Kong but report Hong Kong dollars as their reporting currency. They supported adding the 'presentation currency' concept to the SME Standard to avoid confusion from the absence of requirements and this is consistent with the views of targeted stakeholders in the first phase of the PIR.

Extract of Question 4 in the Request for Information	
(a)	*Have you been impacted by the SME Standard which currently does not include accounting and/or disclosure requirements for derivatives?*
(b)	*Do you support adding accounting and/or disclosure requirements for derivatives to the SME Standard? Why, or why not?*
(c)	*Are there other accounting and/or disclosure requirements that are not currently in the SME Standard with which you have experienced issues? Please provide sufficient details and explains about the items you encountered issues in accounting and why accounting and/or disclosure requirements are necessary.*

5. Edmund and Webster observed that most SMEs are applying paragraph 2.1 of the SME Standard and section 6 *Investments* to account for derivatives. They did not support fair value accounting and disclosure requirements for derivatives because this would be a departure from the cost-based approach adopted in the SME Standard and would require SMEs to incur significant cost. This view is consistent with the views of targeted stakeholders in the first phase of the PIR.

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1 The first phase of the PIR was targeted outreach with the Financial Reporting Standards Committee's SME Standard Advisory Panel and a few other interested parties, including other auditors from small and medium-sized accounting firms and users of financial statements.

2 According to paragraph 2.1 of the SME Standard, "Management should use its judgment in developing an accounting policy resulting in information that is relevant to the needs of users of the financial statements and is reliable in nature. Management should select and apply an entity's accounting policies so that the financial statements comply with all the requirements of the SME-FRS and are consistent with the historical cost convention."

6. Edmund and Webster questioned the need for disclosure requirements about the terms of derivatives contracts because the financial statements are prepared mainly for tax reporting purposes. The Inland Revenue Department only focuses on adjusting items in a profits tax computation to evaluate whether the assessable profit is computed based on the Inland Revenue Ordinance. In addition, they commented that although banks use the financial statements they can request additional financial information (such as derivatives and embedded derivatives, which currently may be off-balance sheet) from management for their credit assessment. Hence, they considered the required disclosures may impose additional burden on most of the SMEs and SMPs while it only fulfills the needs of a particular group of users (ie the banks). This is not consistent with the views of targeted stakeholders in the first phase of the PIR.

Extract of Question 5 in the Request for Information
Have you experienced difficulties in applying the disclosure requirements in paragraph 19.16 of the SME Standard? If yes, please explain in detail.

7. Edmund and Webster observed their clients had not experienced difficulties in applying the disclosure requirements in paragraph 19.16 of the SME Standard. They agreed with permitting the financial information of subsidiaries excluded from consolidation to be presented on an aggregated basis because the subsidiaries are not material to the group. This is consistent with the views of targeted stakeholders in the first phase of the PIR. They considered the existing disclosure requirement is straightforward. They expected additional cost will be incurred to maintain workings for disclosure if is the financial information of subsidiaries is presented in aggregated basis.

8. Edmund and Webster supported clarifying that the disclosure requirements in paragraphs 19.16(b), (c), (d) and (g) might not be applicable for company-level financial statements and would apply to consolidated financial statements only. This is consistent with the views of targeted stakeholders in the first phase of the PIR.

Extract of Question 6 in the Request for Information
Have you experienced challenges in restating comparative information of property, plant, equipment, intangible asset or any other financial statement item when an entity transitioned from a different reporting framework to the SME Standard? If yes, please explain in detail.

9. Edmund and Webster observed their clients experienced significant difficulties in locating the historical cost information and restating comparative information for property, plant, equipment and intangible assets when transitioning from a different reporting framework to the SME Standard in the absence of transitional provisions. They agreed that transition could be facilitated by allowing an entity to use the carrying amount of the property, plant, equipment, investment property or intangible asset under the previous reporting framework at the date of transition as the item's deemed cost on transition. This view is consistent with the views of targeted stakeholders in the first phase of the PIR.

Extract of Question 7 in the Request for Information
Have you experienced difficulties with or have any other comments about applying a useful life of five years for goodwill accounting? If yes, please explain in detail.

10. Edmund and Webster observed their clients did not experienced difficulties in applying a useful life of five years for goodwill accounting. He considered that a five year amortisation period is reasonable because it is the average payback period of investments in Hong Kong. Hence, they did not consider there is a need to change the rebuttable presumption of 5 years to 10 years to align with paragraph 19.23 of the *HKFRS for Private Entities*. This is not consistent with the views of targeted stakeholders in the first phase of the PIR who would like to change to a rebuttable presumption of 10 years to limit the transitional adjustments if the entity is converting from the SME Standard to the *HKFRS for Private Entities*.

Extract of Question 8 in the Request for Information
Would you recommend clarifying/simplifying other accounting requirements of the SME Standard? Please explain the requirements you propose to be clarified/simplified and why it is necessary.

11. Edmund and Webster did not provide any other recommendations for clarifying/simplifying other accounting requirements of the SME Standard.

Extract of Question 9 in the Request for Information	
(a)	*Have you experienced any other challenges or benefits when applying the SME Standard? If you are a user of financial reports prepared under the SME Standard, have you experienced any challenges or benefits with such reports? Please explain in detail, for example, whether you found a predominantly cost-based measurement reporting useful?*
(b)	*Do you have other comments, including feedback on the HKICPA's PIR process?*

12. Edmund and Webster have not experienced any other challenges or benefits when applying the SME Standard.

13. Edmund and Webster support the HKICPA's PIR process and agreed that the SME Standard should be reviewed every five years unless there is a change in regulatory requirements (e.g. Companies Ordinance).

Extract of Question 10 in the Request for Information
Do you have comments on the FRSC's approach to wait for a review of implementation experience of the major new HKFRS standards before considering whether to introduce the relevant new requirements into the SME Standard? Please explain why and when is an appropriate time, if you disagree with the FRSC's decision.

14. Edmund and Webster agreed with the FRSC's approach to wait for a review of implementation experience of the major new HKFRS standards before considering whether to introduce the relevant new requirements into the SME Standard.