Certified Public Accountants
香港會計師公會

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By e-mail and by post

Our Ref.: C/FRSC

International Accounting Standards Board,
30 Cannon Street,
London EC4M 6XH,
United Kingdom.

Attention: Mr. Alan Teixeira, Senior Project Manager

Dear Sirs,

Comment Letter
IASB Exposure Drafts of Proposed Amendments to:
(a) IFRS 3 *Business Combinations*
(b) IAS 27 *Consolidated and Separate Financial Statements*
(c) IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and IAS 19 *Employee Benefits*

The Hong Kong Institute of CPAs welcomes the opportunity to provide you with our comments on the captioned Exposure Drafts. Our responses to the questions raised in these Exposure Drafts are set out in the attached Appendix to this letter.

In general, we consider that the proposed amendments in these Exposure Drafts are technically sound. However, we are concerned about the practicability of some of the proposals, in particular their measurement aspects.

In respect of the proposed amendments to IFRS 3 and IAS 27, we believe that, without robust guidance or framework on valuing an entity or a business, the requirement for the acquirer to measure the fair value of the acquiree, as a whole, as of the acquisition date would, in many cases, become a mechanical exercise. This might result in meaningless, if not misleading, figures (particularly, the measured of total goodwill) being reported in the financial statements. In order to prevent this undesirable outcome, we suggest that IASB work with the valuation profession to develop a robust methodology for valuing an entity or a business before proceeding with the model proposed in these Exposure Drafts.

In respect of the proposed amendments to IAS 37, we consider that applying the conditional and unconditional obligations model in practice could be subjective and problematic. We are also doubtful that unconditional obligations (sometimes referred to as stand ready obligations) can, except in extremely rare cases, be measured reliably given that observable market data is unlikely to be available. If the IASB decides to go ahead with its proposals, we recommend that:

(1) more robust guidance on when an unconditional obligation exists and how to measure such obligation should be included in the final Standards; and

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(2) instead of including a note about measurement, the actual working of the measurement of the unconditional obligation should be specified in the relevant examples in the appendix to the final Standards.

Until further guidance is in place, we would expect that entities would have to rely on the proposed exemption for not recognising the unconditional obligation because it cannot be measured reliably but disclose the information required more often than in extremely rare cases as suggested in the proposed Standard.

In respect of the proposed amendments to IAS 19, we consider that there are some inconsistencies between the proposals under IAS 37 concerning an unconditional obligation and the proposals under IAS 19 concerning termination benefits (see our response to Question 2 relating to IAS 19). We therefore suggest that the IASB should consider these identified inconsistencies and either make appropriate changes to the relevant proposal or explain in the Basis for Conclusions on IAS 19 how they reconcile the identified inconsistencies.

If you have any questions on our comments, please do not hesitate to contact the undersigned at schan@hkicpa.org.hk.

Yours faithfully,

Stephen Chan
Executive Director

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APPENDIX

HONG KONG INSTITUTE OF CPAs' RESPONSES TO THE QUESTIONS RAISED IN THE EXPOSURE DRAFTS

IFRS 3 *Business Combinations*

Question 1—Are the objective and the definition of a business combination appropriate for accounting for all business combinations? If not, for which business combinations are they not appropriate, why would you make an exception, and what alternative do you suggest?

We generally consider the objective and the definition of a business combination appropriate for accounting for all business combinations.

However, we are concerned about the continuing scope exclusion of business combinations involving entities and businesses under common control, given the prevalence of these transactions in practice. We consider that there is a great demand in the market for guidance on such and urge the IASB to assign a high priority to this project. We also encourage the IASB to clarify whether forming a non-operating company to acquire control over another entity meets the definition of a business combination and, if not, how such transactions should be recognized.

Question 2—Are the definition of a business and the additional guidance appropriate and sufficient for determining whether the assets acquired and the liabilities assumed constitute a business? If not, how would you propose to modify or clarify the definition or additional guidance?

We consider the definition of a business and the additional guidance appropriate and sufficient. However, we support the provision of any additional guidance that provides clarity and promotes consistency in practice.

Question 3—In a business combination in which the acquirer holds less than 100 per cent of the equity interests of the acquiree at the acquisition date, is it appropriate to recognise 100 per cent of the acquisition-date fair value of the acquiree, including 100 per cent of the values of identifiable assets acquired, liabilities assumed and goodwill, which would include the goodwill attributable to the non-controlling interest? If not, what alternative do you propose and why?

We consider that it is theoretically correct to recognise 100 percent of the acquisition-date fair value of the acquiree, including 100 per cent of the values of identifiable assets acquired, liabilities assumed and goodwill, which would include the goodwill attributable to the non-controlling interest in a business combination in which the acquirer holds less than 100 per cent of the equity interests of the acquiree at the acquisition date. However, we see difficulties in practice in determining the full fair value of the acquiree where less than 100% is acquired. Without any robust guidance or framework on how to value an entity or a business (see also our comments on question 4 below), we believe that this requirement could become an mechanical exercise and might result in meaningless figures for goodwill being reported in the financial statements.

Question 4—Do paragraphs A8-A26 in conjunction with Appendix E provide sufficient guidance for measuring the fair value of an acquiree? If not, what additional guidance is needed?

No. We do not consider the guidance sufficient. The examples provided deal with straight forward situations and do not address the more complex situations that preparers encounter in practice. For example, we note the development of the practices behind acquisition accounting in China and the resultant difficulties in identifying fair values of the businesses acquired.

We therefore suggest the Board working with the valuation profession to develop more robust guidance on the basis on which the full fair value of the acquiree should be determined so that preparers of the financial statements can have a clear framework to follow when dealing with more difficult situations.

Question 5—Is the acquisition-date fair value of the consideration transferred in exchange for the acquirer's interest in the acquiree the best evidence of the fair value of that interest? If not, which forms of consideration should be measured on a date other than the acquisition date, when should they be measured, and why?

We agree that the acquisition date fair value of the consideration transferred in exchange for control is the best evidence of the fair value of the interest acquired at that date.

Question 6—Is the accounting for contingent consideration after the acquisition date appropriate? If not, what alternative do you propose and why?

We consider that the accounting for contingent consideration after the acquisition date appropriate.

Question 7—Do you agree that the costs that the acquirer incurs in connection with a business combination are not assets and should be excluded from the measurement of the consideration transferred for the acquiree? If not, why?

We agree that the costs that the acquirer incurs in connection with a business combination are not assets in their own right and are not part of the consideration for the acquisition. We therefore consider that they should be excluded from the measurement of the consideration. This is consistent with the fair value treatment of the consideration transferred.

Question 8—Do you believe that these proposed changes to the accounting for business combinations are appropriate? If not, which changes do you believe are inappropriate, why, and what alternatives do you propose?

We consider that the proposed changes to the accounting for business combinations are technically appropriate. However, we see difficulties in determining the fair value of individual contingencies. We recommend that the revised Standard require note disclosure where measurement is not sufficiently reliable for an item to be recognised.

Question 9—Do you believe that these exceptions to the fair value measurement principle are appropriate? Are there any exceptions you would eliminate or add? If so, which ones and why?

We agree that the exceptions to the fair value principle are appropriate at this time. We urge the IASB to revise the Standards containing the exceptions so that acquisitions can be recognised at fair value in the future and differences between fair value and carrying amounts can be excluded from goodwill.

Question 10—Is it appropriate for the acquirer to recognise in profit or loss any gain or loss on previously acquired non-controlling equity investments on the date it obtains control of the acquiree? If not, what alternative do you propose and why?

We consider that it is appropriate for the acquirer to recognise in profit or loss any gain or loss on previously acquired non-controlling equity investments on the date it obtains control of the acquiree.

Question 11—Do you agree with the proposed accounting for business combinations in which the consideration transferred for the acquirer's interest in the acquiree is less than the fair value of that interest? If not, what alternative do you propose and why?

We agree with the proposed accounting for business combinations in which the consideration transferred for the acquirer's interest in the acquiree is less than the fair value of that interest.

Question 12—Do you believe that there are circumstances in which the amount of an overpayment could be measured reliably at the acquisition date? If so, in what circumstances?

We are not aware of any circumstances under which amount of overpayment could be measured reliably.

Question 13—Do you agree that comparative information for prior periods presented in financial statements should be adjusted for the effects of measurement period adjustments? If not, what alternative do you propose and why?

We agree that comparative information for prior periods presented in financial statements should be adjusted for the effects of measurement period adjustments for the purpose of enhancing the comparability of the financial statements.

Question 14—Do you believe that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price or any assets acquired and liabilities assumed or incurred are not part of the exchange for the acquiree? If not, what other guidance is needed?

We consider that the guidance provided is sufficient for making the assessment of whether any portion of the transaction price or any assets acquired and liabilities assumed or incurred are not part of the exchange for the acquiree. However, we welcome any further guidance that provides clarity and promotes consistency in practice.

Question 15—Do you agree with the disclosure objectives and the minimum disclosure requirements? If not, how would you propose amending the objectives or what disclosure requirements would you propose adding or deleting, and why?

We agree with the disclosure objectives and the minimum disclosure requirements.

Question 16—Do you believe that an intangible asset that is identifiable can always be measured with sufficient reliability to be recognised separately from goodwill? If not, why? Do you have any examples of an intangible asset that arises from legal or contractual rights and has both of the following characteristics:

(a) the intangible asset cannot be sold, transferred, licensed, rented, or exchanged individually or in combination with a related contract, asset, or liability; and

(b) cash flows that the intangible asset generates are inextricably linked with the cash flows that the business generates as a whole?

We are not aware of any circumstances where an intangible asset that is identifiable cannot be measured with sufficient reliability to be recognised separately from goodwill.

Question 17—Do you agree that any changes in an acquirer's deferred tax benefits that become recognisable because of the business combination are not part of the fair value of the acquiree and should be accounted for separately from the business combination? If not, why?

We agree that any changes in an acquirer's deferred tax benefits that become recognisable because of the business combination are not part of the fair value of the acquiree and should be accounted for separately from the business combination.

Question 18—Do you believe it is appropriate for the IASB and the FASB to retain those disclosure differences? If not, which of the differences should be eliminated, if any, and how should this be achieved?

We consider that the disclosures should be harmonized to the extent possible, subject to the requirements of other standards that are not currently being reconsidered by the Boards.

Question 19—Do you find the bold type-plain type style of the Exposure Draft helpful? If not, why? Are there any paragraphs you believe should be in bold type, but are in plain type, or vice versa?

We found the style of the Exposure Draft helpful and generally consistent with the format of recent International Financial Reporting Standards.