

# HKFRSs / IFRSs UPDATE

2010/04

24 May 2010

## IMPROVEMENTS TO HKFRSs 2010

### Background

*Improvements to HKFRSs 2010* 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.

In particular, the IASB extended the scope of paragraph D8 to IFRS 1 *First-time Adoption of International Financial Reporting Standards* for the use of the deemed cost exemption for an event-driven fair value. In some jurisdictions, local law requires an entity to revalue its assets and liabilities to fair value for a privatisation or initial public offering (IPO) and to treat the revalued amounts as deemed cost for the entity's previous GAAP. Before the amendment made in May 2010, if that revaluation occurred after the entity's date of transition to IFRSs, the entity could not have used that revaluation as deemed cost for IFRSs. Therefore, the entity would have had to prepare two sets of measurements for its assets and liabilities – one to comply with IFRSs, and one to comply with local law. The IASB considered this unduly onerous. Therefore, the IASB amended paragraph D8 to allow an entity to recognise an event-driven fair value measurement as deemed cost when the event occurs, provided that this is during the periods covered by its first IFRS financial statements. In addition, the IASB concluded that the same relief should apply to an entity that adopted IFRSs in periods before the effective date of IFRS 1 or applied IFRS 1 in a previous period, provided the measurement date is within the period covered by its first IFRS financial statements.

### STATUS

Final

### EFFECTIVE DATE

Annual periods beginning on/after 1 July 2010 or 1 January 2011

### ACCOUNTING IMPACT

May be significant

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

HKFRS	Subject of amendment
HKFRS 1 <i>First-time Adoption of Hong Kong Financial Reporting Standards</i>	Accounting policy changes in the year of adoption
	Revaluation basis as deemed cost
	Use of deemed cost for operations subject to rate regulation
HKFRS 3 <i>Business Combinations</i>	Transition requirements for contingent consideration from a business combination that occurred before the effective date of the revised HKFRS
	Measurement of non-controlling interests
	Un-replaced and voluntarily replaced share-based payment awards
HKFRS 7 <i>Financial Instruments: Disclosures</i>	Clarifications of disclosures
HKAS 1 <i>Presentation of Financial Statements</i>	Clarification of statement of changes in equity
HKAS 27 <i>Consolidated and Separate Financial Statements</i>	Transition requirements for amendments made as a result of HKAS 27 (as amended in 2008) to HKAS 21, HKAS 28 and HKAS 31
HKAS 34 <i>Interim Financial Reporting</i>	Significant events and transactions
HK (IFRIC)-Int 13 <i>Customer Loyalty Programmes</i>	Fair value of award credits

While some of the amendments are minor, it is possible that some, particularly those relating to the measurement of non-controlling interest and the use of deemed cost for operations subject to rate regulated activities, will have a significant effect on financial statements. Consequently the effect of the amendments should be analysed carefully by those entities that have adopted, or plan to adopt, HKFRSs.

The effective date of each of the amendments, and their transitional arrangements, are included below.

## Amendments

### HKFRS 1 *First-time Adoption of Hong Kong Financial Reporting Standards*

**Issue:** *Changes in accounting policies during an entity's year of adoption of HKFRSs*

If a first-time adopter changes its accounting policies or its use of exemptions in HKFRS 1 after the date of its first interim financial report prepared in accordance with HKAS 34, but before the issue of its first annual HKFRS financial statements, the reconciliations between previous GAAP and HKFRSs are required to be updated. The requirements of HKAS 8 do not apply.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

**Issue:** *Use of revalued amount as deemed cost*

Some GAAPs permit an event driven fair value (being a remeasurement to fair value of some or all assets and liabilities on an event such as a privatisation or public offering) to be established as a deemed cost. The amendment extends the relief available under HKFRS 1, to permit a first-time adopter to use that event driven fair value as deemed cost under HKFRSs, from measurements which are carried out at or before transition date to measurements that are carried out between the date of transition and the end of the entity's first annual HKFRS reporting period.

As an example, if an entity chooses to use an event driven fair value as deemed cost under HKFRS for an asset where the measurement date is after its date of transition to HKFRS but before the end of the entity's first annual HKFRS reporting period, an adjustment will be made to equity as at the measurement date. During the period from transition date to the measurement date, historical cost or other amounts permitted by HKFRS are presented. The HKICPA agrees with the IASB's decision to reject an approach of 'working back' from the measurement date to a deemed cost at the date of transition, on the basis that this would require the use of hindsight and would result in a carrying amount at transition date that was neither historical cost nor fair value.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

**Issue:** *Deemed cost for assets used in operations subject to rate regulation*

The amendment permits a first-time adopter to use its previous GAAP carrying amount of property, plant and equipment and intangible assets that are, or were previously, used in operations subject to rate regulation as deemed cost at the date of transition to HKFRS. This election is available on an individual asset basis.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

### **HKFRS 3 Business Combinations**

**Issue:** *Transition – contingent consideration balances arising from business combinations that took place prior to the adoption of HKFRS 3 (2008)*

HKFRS 3 (2008) included a consequential amendment to HKAS 39 that brought contingent consideration balances within the scope of that standard. This means that instead of changes in the amount of contingent consideration being accounted for as an adjustment to the cost of the original business combination, they are now accounted for in accordance with HKAS 39 and recognised in profit or loss. The amendment clarifies that the change in scope of HKAS 39 is applied to business combinations on a prospective basis, meaning that where a business combination took place before the date of adoption of HKFRS 3 (2008), changes in contingent consideration are accounted for as an adjustment to the cost of the original business combination.

Effective date and transition: Annual periods beginning on/after 1 July 2010, with earlier application permitted.

**Issue:** *Measurement of Non-Controlling Interest (NCI)*

The amendment clarifies that the option to measure NCI at either fair value, or the proportionate share of the acquisition date fair value of the acquiree's identifiable net assets that are recognised by the acquirer, applies only to instruments that give the NCI a present ownership interest and entitle the holder to a proportionate share of net assets in the event of liquidation. All other components of NCI are measured at their acquisition date fair value, unless another measurement is required by HKFRS.

This amendment has been made to ensure that certain components of NCI are not measured at zero. For example, if a share-based payment transaction is classified as equity, it is measured in accordance with HKFRS 2 *Share-based Payment*. Another example is a preference share that represents NCI, being an equity instrument, with its holder being entitled to a return of the initial amount subscribed on liquidation. The NCI that relates to the preference shares is measured at fair value.

Effective date and transition: Annual periods commencing on/after 1 July 2010, with earlier application permitted. On adoption, to be applied prospectively from the date on which HKFRS 3 (2008) was first applied.

**Issue:** *Share-based payment transactions of an acquiree that are either not replaced on a business combination, or are voluntarily replaced.*

The current requirement for an acquirer to measure share-based payment awards that it issues to replace existing awards of an acquiree at the acquisition date, in accordance with HKFRS 2 is extended. This means that existing share-based payment awards of an acquiree that are not replaced in a business combination are also measured by the acquirer in accordance with HKFRS 2 at the acquisition date. If the awards have vested at the acquisition date, they are accounted for as part of NCI in the acquiree. If the awards have not vested at the acquisition date, they are accounted for as if the acquisition date was the grant date.

An acquirer may exchange its own share-based payment awards for awards held by employees of the acquiree. The current requirement to account for that exchange as a modification of the existing arrangement, where the acquirer is obliged to replace the existing awards, is retained with the amount calculated in accordance with HKFRS 2 being allocated between the cost of the business combination and post acquisition services. The amendment extends this to cover replacement awards where the acquirer is not obliged to replace the existing awards, but chooses to voluntarily.

In some cases, existing share-based payment awards in an acquiree expire as a result of a business combination. In those circumstances, if the acquirer replaces those awards voluntarily, the entire fair value of those replacement awards calculated in accordance with HKFRS 2 is accounted for as a post acquisition remuneration expense.

Effective date and transition: Annual periods commencing on/after 1 July 2010, with earlier application permitted. On adoption, to be applied prospectively from the date on which HKFRS 3 (2008) was first applied.

## **HKFRS 7 Financial Instruments: Disclosures**

### *Issue: Clarification of disclosure requirements*

The amendment clarifies quantitative disclosure requirements for risks arising from financial instruments, and encourages accompanying narrative disclosures if the concentration of risk is not apparent from the quantitative disclosures.

The requirements for disclosures of credit risk, including collateral held, are clarified and reduced, with the carrying amount of assets that would have been past due or impaired unless they had been renegotiated no longer needing to be disclosed.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

## **HKAS 1 Presentation of Financial Statements**

### *Issue: Presentation of changes in equity*

The amendment clarifies that the analysis of items of Other Comprehensive Income may be shown in either the (primary) statement of changes in equity, or in the notes to the financial statements.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

## **HKAS 27 Consolidated and Separate Financial Statements – consequential amendments to HKAS 21 The Effects of Changes in Foreign Exchange Rates, HKAS 28 Investments in Associates and HKAS 31 Interests in Joint Ventures**

### *Issue: Transitional requirements for consequential amendments*

The amendments to HKAS 21, HKAS 28 and HKAS 31 clarify that the amendments made to these standards as a consequence of HKAS 27 (revised 2008) are to be applied prospectively from the date of adoption of that standard (annual periods beginning on/after 1 July 2009 with earlier application permitted). As exceptions, paragraph 35 of HKAS 28 and paragraph 46 of HKAS 31, which relate to accounting in the separate financial statements of the investor, are applied retrospectively.

Effective date and transition: Annual periods beginning on/after 1 July 2010, with earlier application permitted.

## **HKAS 34 Interim Financial Reporting**

### *Issue: Content of an interim financial report – significant events and transactions*

The amendments emphasise that disclosure about significant transactions and events is required to update relevant information presented in the most recent annual financial report.

HKAS 34 is made more specific about events and transactions for which disclosure is required, and guidance has been added covering the application of the requirements for financial instruments.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

## **HK(IFRIC)-Int 13 Customer Loyalty Programmes**

### *Issue: Fair value of award credits*

The amendment clarifies that the fair value of award credits includes consideration of the amount of discounts or incentives that would otherwise be offered to customers who have not earned award credits from an initial sale.

Effective date and transition: Annual periods beginning on/after 1 January 2011, with earlier application permitted.

## **BDO's support and assistance on HKFRSs**

For any support and assistance on HKFRSs, please talk to your usual BDO contact or Stephen Chan, Partner and Head of Technical & Training at +852 2853 5820 or email [StephenChan@bdo.com.hk](mailto:StephenChan@bdo.com.hk)

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