



## TechWatch 52

The latest standards  
and technical  
developments

### ► Financial reporting

#### **Handbook update 37 – new HK(IFRIC) Interpretation 11**

Update 37 encloses new HK(IFRIC) Interpretation 11 *HKFRS 2 – Group and Treasury Share Transactions*, which is effective for annual periods beginning on or after 1 March 2007.

HK(IFRIC)-Int 11 is converged with the equivalent IFRIC interpretation. It addresses the question of how to apply HKFRS 2 *Share-based Payment* to share-based payment arrangements involving an entity's own equity instruments or the equity instruments of another entity in the same group.

It requires a share-based payment arrangement in which an entity receives goods or services as consideration for its own equity instruments to be accounted for as an equity-settled share-based payment transaction, regardless of how the equity instruments needed for the transaction are obtained. It also provides guidance on whether share-based payment arrangements, in which suppliers of goods or services of an entity are provided with equity instruments of the entity's parent, should be accounted for as cash-settled or equity-settled in the entity's financial statements.

### ► Audit and assurance

#### **Audit of licensed corporations and associated entities of intermediaries**

The Institute's expert panel on securities issued audit issues questions and answers on the audit of licensed corporations and associated entities of intermediaries in January 2007. The Q&As should be read in the light of the Institute's Practice Note 820 *The Audit of Licensed Corporations and Associated Entities of Intermediaries*.

Topics covered in the Q&As include:

- Features of the HKSA's issued since the issuance of Practice Note 820 in February 2004.
- A sample unqualified audit report effective for auditor's reports dated on or after 31 December 2006.

#### **Invitation to comment on IAASB EDs**

The Institute has issued an invitation to comment on a number of International Auditing and Assurance Standards Board (IAASB) exposure drafts, in two parts:

**Part A:** ISA 230 (Redrafted) *Audit Documentation*, ISA 560 (Redrafted) *Subsequent Events*, ISA 610 (Redrafted) *The Auditor's Consideration of the*

*Internal Audit Function* and ISA 720 (Redrafted) *The Auditor's Responsibility in Relation to Other Information in Documents Containing Audited Financial Statements*, with comments requested by **16 March 2007**.

**Part B:** ISA 540 (Revised and Redrafted) *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures* and ISA 580 (Revised and Redrafted) *Written Representations*, with comments requested by **16 April 2007**.

The explanatory memorandum to exposure drafts provides background information and explanation of the proposed ISAs. The IAASB's intentions in developing the revisions to the ISAs are:

- Proposed ISAs 230, 560, 610 and 720 are redrafted to provide clearer requirements and easy-to-understand application guidance, with no changes proposed to the requirements in the standards.
- Proposed ISA 540, which combines the extant ISA 540 and ISA 545 *Auditing Fair Value Measurements and Disclosures*, is revised to reinforce best practices and cause the auditor to give appropriate attention to areas of accounting judgment, such as assumptions, and to possible bias.
- Proposed ISA 580 is revised to improve the quality and appropriateness of written representations sought by the auditor and, in particular, to deal with concerns about whether auditors may overrely on representations at the expense of other evidence.

## ► Ethics

### **Invitation to comment on IESBA ED on auditor independence requirements**

The Institute has issued an invitation to comment on the IFAC International Ethics Standards Board for Accountants exposure draft on auditor independence requirements, with comments requested by **16 April 2007**.

The exposure draft proposes to update and strengthen the auditor independence requirements contained in the IFAC Code of Ethics for Professional Accountants (the code). The explanatory memorandum to the exposure draft provides background information and explanation of the proposed modifications to the code.

## ► Taxation

### **2007 annual meeting with the commissioner of Inland Revenue**

Representatives of the Institute met the commissioner of Inland Revenue and members of her staff on 26 January 2007. The minutes of the meeting are being prepared and will be published as a Tax Bulletin. Some urgent matters that could be released prior to the publication of the Tax Bulletin are:

- Filing deadlines for the 2006-07 tax returns.
- DIPN 15 (revised) – part B: leasing arrangements.
- Commercial and industrial building allowance.
- Declaration of due representation in the application for block extension.

## ► International meeting

### **IASB and FASB round tables**

Two IASB and FASB round tables were held on 16 and 17 January 2007 in Hong Kong and were attended by 20 participants from Hong Kong, the mainland, Australia, Japan, Singapore, Korea and Malaysia.

The round tables provided an opportunity to deliberate on the suitable methods of measurement. Most participants preferred a mixture of measurement basis comprising of historical cost, amortized cost, fair values, present value and replacement cost. They were satisfied with fair value for investments as long as fair values could be measured reliably.

*Extracts from TechWatch 52. The entire publication is available as a PDF on the Institute's website.*

### **Quick link**

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# Let's get



*This column is dedicated to answering questions submitted by members regarding Institute standards*

**Q.** I am a small practitioner and one of my clients is a securities broker. I understand the Institute issued Practice Note 820 *The Audit of Licensed Corporations and Associated Entities of Intermediaries* in February 2004 to assist auditors to develop an approach to the audit of financial statements of licensed corporations and associated entities of intermediaries. Has the Institute issued any further guidance since then?

**A.** The Institute's expert group of members on securities will be updating Practice Note 820 this year. The target for completion is by the end of 2007. The existing Practice Note is still relevant as the guidance was written specifically for the securities industry.

However, practitioners should note that the Hong Kong Standards on Auditing (HKSA) requirements, issued in February 2004, are more rigorous and robust. Practitioners are required to consider all HKSA to identify which standards are applicable to the circumstances surrounding their audits of licensed corporations and associated entities of intermediaries.

An audit issues Q&As on the audit of licensed corporations and associated entities of intermediaries was issued on 19 January 2007, which sets out further guidance. The document is available online at [www.hkicpa.org.hk/professionaltechnical/assurance/rm/EPS\\_0701.pdf](http://www.hkicpa.org.hk/professionaltechnical/assurance/rm/EPS_0701.pdf) and includes an example unqualified auditor's report based on HKSA 700 *The Independent Auditor's Report on a Complete Set of General Purpose Financial Statements*, effective for an auditor's report of a licensed corporation dated on or after 31 December 2006.

*Please note that the answers only address general issues and provide general guidance, and do not constitute professional or legal advice. You need to base your decisions on frameworks, standards and other documents approved by the Council of the Institute, after taking account of your specific circumstances.*

# technical

## Members helping members

*Do you want to help your fellow members? Try answering this question from a member and send an email to [hkicpa@hkicpa.org.hk](mailto:hkicpa@hkicpa.org.hk). Answers received by 21 March will be considered for inclusion in the May issue of A Plus.*

This month's question:

**Q.** I've noted from the Members' Handbook Volume I that Professional Ethics Statements 1.200 to 1.292 were superseded by the Code of Ethics for Professional Accountants when it became effective on 30 June 2006. However, it appears there is no section in the Code of Ethics similar to Professional Ethics Statement 1.209 *Management Consulting Services*.

Could you let me know whether I can still refer to Professional Ethics Statement 1.209 for management consulting services or has such services been addressed in the Code of Ethics?

Here is the answer to the question we asked members to help with in the January edition of *A Plus*:

**Q.** I am preparing the financial statements for my company and its one subsidiary. The subsidiary is 90 percent owned by my company.

I have agreed with my friend who owns the remaining 10 percent of shares that I will let him run the company and that I will just appoint a nominee director to the board of

directors. This means that I will not control the company on a day-to-day basis. I have been told that as I do not control the company, I do not have to prepare consolidated financial statements. I plan to treat the company as an associate because the agreement with my friend lets me tell him what I would like him to do, and so I have significant influence.

Is this correct, or should I treat the company as a joint venture as my friend and I have agreed to share control?

**A.** HKAS 27 *Consolidated and Separate Financial Statements* defines control as being "the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities." HKAS 27 defines a subsidiary as being an entity that is controlled by another entity. HKAS 27 further notes that control is presumed to exist when the parent owns more than half of the voting power of another entity, which applies in your case.

You still have the **power** to govern your subsidiary despite allowing your friend to run it on a day-to-day basis. Your decision to cede some of your rights to control the company to your friend does not mean that you do not have the **power** and ability to govern the subsidiary. You could change your mind tomorrow and elect to exercise your powers or you could

continue leaving your friend to run the subsidiary. You could also change your mind and replace your nominee director. Holding 90 percent of the votes of the company lets you elect most, if not all, of the directors to the board of directors at any time that you decide to do so.

There is nothing that prevents you from exercising control at any time in the future when you decide that you want to manage the subsidiary rather than leave it to your friend. You control the subsidiary and you have to prepare consolidated financial statements that include your subsidiary.

You could only consider whether or not you are dealing with an associate or a joint venture where you do not have control. However, this clearly doesn't apply to your case.

*You can submit questions on technical issues by sending an email to [hkicpa@hkicpa.org.hk](mailto:hkicpa@hkicpa.org.hk). The standard setting team will answer these questions in accordance with the policy on handling members' technical questions which is posted on the Institute's website.*