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Mr. Steve Ong
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Hong Kong Institute of Certified Public Accountants
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Wanchai, Hong Kong

Dear Steve,

IFRS Foundation Paper for Public Consultation – Status of Trustee's Strategy Review ("Consultation Paper")

I refer to your letter dated 17 December 2010 on the above to our Mr. Mark Dickens which has been passed to me for my attention.

We have completed our review of the Consultation Paper and are pleased to be given the opportunity to comment on the IFRS Foundation Strategy Review ("Review"). The objective of the Review is to help the IFRS Foundation formulate its strategy to achieve its ultimate objective of a single, high quality set of global accounting standards. We believe the objective of the Foundation should be phrased sufficiently broad to cover the need to consider the impact of the standards on the financial stability of the capital markets and the countries or economies that use the standards.

We believe high quality financial information should be relevant, reliable, and prudent and show a faithful representation of the transactions undertaken by a reporting entity. Quality accounting standards play a key element in maintaining financial market stability as accounting standards influence human behaviour. It would be unrealistic to believe that accounting standards setting can be isolated and divorced from politics and economic consequences.

We have significant concerns that the new standards that are currently being produced are too complex for lay readers as well as professionals to understand, and too costly for preparers to implement. We believe some proposals, such as the recent exposure draft on lease accounting, would not produce better information to enable users of financial statements make informed economic decisions. We also believe that the wider use of fair value and the recognition of fair value changes either in the profit and loss statement or statement of other comprehensive income does not improve financial statements reliability and usefulness but in fact contributes to making financial statements less

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relevant and reliable, and we believe in some cases non-auditable. Moreover, recognition of fair values facilitates the easier manipulation of the financial position and performance of reporting entities which in turn may lead to financial instability which is not in the long term interests of investors, financial markets and economies as a whole.

In order to achieve its objective, we suggest that the IFRS Foundation revisit as a matter of urgency the Conceptual Framework which should include the key considerations of going concern, prudence and financial stability. In particular, it should seriously re-consider whether the focus of accounting should be to account for actual transactions that have occurred rather than adopting its current position which appears to be a focus on the re-measurement of assets and liabilities subsequent to their initial recognition. The substance of fair value accounting is the recognition of hypothetical transactions with hypothetical parties and at hypothetical values at a reporting period end date. Although we believe that fair value information is useful, we believe a fair value gain or loss should not be recognised unless it is supported by an actual exchange or settlement of goods and services by the reporting entity with another party. Until an actual transaction has occurred, fair value information should only be provided by way of a note disclosure so that readers of financial statements can question management why certain actions have not been taken.

Our detailed comments including strategic issues that should be considered by the IFRS Foundation are discussed further below.

Conceptual Framework

We have stressed many times in our comment letters that the IASB should refrain from making any substantial changes to individual standards until completion of the review of the Conceptual Framework. We believe the Conceptual Framework should be the core benchmark for the development of specific accounting standards as this will ensure consistency of the specific standards to a single cohesive body of key underlying concepts and principles for financial reporting. We would point out that recently released discussion papers and exposure drafts introduce conflicting concepts and principles. This leads to confusion and results in the development of incoherent rule-based standards rather than principle-based standards. A recent example is the Lease project where we have questioned the conceptual basis for recognising "rights-of-use" as an asset and recognising "future obligations" as a liability.

In October 2010 the IASB issued a request for views on the timing for implementing new or amended IFRSs and acknowledged the fact that the volume of proposed amendments to IFRSs would be a burden to stakeholders. We also note that the development of the Conceptual Framework has been delayed. We believe the IFRS Foundation should seriously re-consider its and the IASB's priorities and approach to setting accounting standards.

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Inappropriate priorities and timetable in the IASB work plan

We understand the IASB and FASB wish to issue a converged financial instrument standard by June 2011. Although we would accept that there should be a targeted timeline for the development and completion of new or revised standards, we believe that there should be flexibility on timing. If issues are more complex than originally estimated, the target completion date should be deferred.

We believe that the release of high quality and well thought-out standards should be the first priority and primary concern of the IFRS Foundation, including the IASB. Quality should not be sacrificed for quantity or the timing in issuing new standards.

The IAS 39 replacement project is being introduced in phases. The Lease project is also being rushed and has focused primarily on the accounting by lessees rather than fully considering the issues from both the lessee and lessor's point of view. We do not agree with these approaches as it is unclear whether the proposals will result in a coherent conceptually consistent overall picture when reporting such transactions. We believe rushed or inadequately field tested standards will only result in future revisions resulting in both costs to preparers and confusion to users of financial statements. Moreover, potential successive and substantive changes to the standards are likely to arise leading to added costs and confusion.

Preparers, auditors and users of financial statements are currently struggling to digest the changes and understanding the impact of the numerous fundamental changes to the current requirements, including new proposals on financial instruments, revenue recognition, liability measurement and leases. We believe that the IASB's work plan strategy should include regular impact assessments of its proposals throughout the life of each project to fully understand the possible impact on a micro-level as well as a macro-level; that is, at the reporting entity level as well as its possible impact on the financial stability of the capital markets as a whole.

Transparency on responses to comments received from constituents

Although the IASB has steps to consider the comments received on discussion papers and exposure drafts, we are troubled that concerns from constituents sometimes do not appear to be fully and properly addressed.

For example, we do not believe that financial liabilities should be re-measured at their fair values after their initial recognition and we understand that many other constituents expressed the same view. In particular, the recognition of a gain from a decline in the credit quality of an entity's own liabilities is counter-intuitive and unrealistic, and also results in the reporting entity recognising a lesser liability than the amount due and payable. In response to this issue IFRS 9, published in November 2010, requires the fair value change due to changes in an entity's own credit risk to be recognised directly in

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other comprehensive income. We are not convinced by the IASB's solution as the real issue is a conceptual issue of what is a liability and how it should be measured, not just a presentation issue.

We believe that considerable time and effort is spent by stakeholders to prepare and submit comment letters to the IASB and the IASB should consider ways to improve the transparency and the thoroughness in dealing with contrary views.

Field testing

We also believe that the IASB should undertake thorough field testing of its proposed standards before they are issued as standards. Such an approach is adopted by the motor vehicle industry to ensure that new vehicles will actually work as designed and are useful and safe. We believe a similar approach should be adopted by the IASB in the development of accounting standards given their wider implications as they affect a larger number of stakeholders as well as the financial stability of the capital markets and the economies that adopt the standards. Thorough field testing by the IASB should ensure that the full implications of the proposed standard are understood and so that the IASB has sufficient evidence that if the standard is to be released the standard is worthwhile and workable in practice. For example, we believe that the cost of implementing some proposals, such as the proposals on the Lease project will be substantial but the information produced will fail to provide sufficient benefits and useful information to readers of financial statements.

Voting benchmark

Currently the approval of a new or revised standard only requires nine votes out of the 15 IASB members. We believe a 40% dissenting vote indicates that there is legitimate cause for concern that the standard is in some way deficient or weak. The IFRS Foundation may wish to consider whether a higher percentage supporting vote should be introduced.

Strategic issues

We believe that accounting standards development undertaken by the IFRS Foundation plays a crucial role. The responsibility extends beyond the micro-level of a reporting entity as the impact of accounting standards affect the human behaviour of preparers, users of financial statements and other stakeholders. Accounting standards inevitably have a significant impact on the financial stability of capital markets as well as economies as a whole. We believe that financial stability requirements should be a consideration in developing standards and believe that the concept of prudence was an element in addressing this issue. Unfortunately its importance is being downplayed in recent accounting literature. We strongly believe that the Conceptual Framework review should be the IASB's first priority and the development of detailed standards can then follow.

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We believe that given the objective of the IFRS Foundation is to develop globally accepted accounting standards, it needs to recognise that countries will be at different stages of development and may have different perspectives to issues. As a global organisation, we believe the Foundation needs greater transparency and representation on its governing board. The work of the IFRS Foundation is currently focused on standard setting. We believe that to provide feedback on the practical aspects of its standards, it should also introduce a separate Compliance and Monitoring function to identify practical issues encountered in implementation and use. This would also assist in identifying issues needed to be considered by the IFRIC or the IASB.

To enable the IFRS Foundation to be a truly global organisation which requires it to be also concerned with financial stability, we believe that it requires more public funding and support from governments. Although this may lead to political pressure, we believe that this already exists and is inevitable for any entity that has a global responsibility. Public funding will lead to issues on independence and this needs to be properly managed. However we believe that a wider source of financing will result in ensuring that the IFRS Foundation has adequate resources to do its work effectively. This includes the ability to thoroughly field test new and revised standards across a broad spectrum of countries before they are introduced, which to-date appears to have been a low priority.

We hope that the above comments are useful.

Yours sincerely,
For and on behalf of
The Stock Exchange of Hong Kong Limited



Colin Chau
Senior Vice President
Listing Division

CC/ESA/el

c.c. Mr. Mark Dickens – Head of Listing

