

HKAS 17 & 40 and Interpretation

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Examples and Cases
for Discussion

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HKAS 17 – Leases

Example

Entity A

- paid a land premium to lease a land from the HKSAR government for 50 years

- then, constructed a building on the land for own use

10 years later, Entity B “acquired” the interest of the land and building for own use

Assuming Entity B “acquired” the property at HK\$20 million and

- A similar land has a fair value of \$12M
- Construction cost of a similar building is \$4M

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HKAS 17 – Leases

Example

Entity A

- paid a land premium to lease a land from the HKSAR government for 50 years

- then, constructed a building on the land for own use

10 years later, Entity B “acquired” the interest of the land and building for own use

Assuming Entity B “acquired” the property at HK\$20 million

An independent surveyor reported that:

- The fair value of the building elements based on depreciated replacement cost is HK\$6 million
- The residual amount of HK\$14 million is the fair value of the land elements

Please comment.

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Leases – HK Interpretation 4

Example

- Entity ABC has a property bought in 1980 and it is located in Cheung Sha Wan.
- According to the land search, the lease term with the HK SAR government should expire in 30 June 1997.
- Based on SSAP 14 and 17, the land and building had been depreciated over 50 years previously.
- Please discuss the implication under HKAS 17.

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Leases – HK Interpretation 4

Example

- Based on the information in the previous example, an auditor issued a letter to ABC as follows:

Dear Raymond

- For the amortisation issue we discussed, I confirmed with our partner for the estimated useful life of the land element only. We consider that the estimated useful life of the land should be 2047 but it should not be 1997. Therefore, the land cost should be amortised until 2047.
- Our judgement is based on the HKSA's the accounting guideline issued on 1990s for the treatment of land title in the new Kowloon area. In fact, the land use right should have been already automatically extended to 2047.
- If we are in doubt, we may further consult HKICPA for their view. I think this is benefit to you and to us.

Yours sincerely

Thomas

- After receiving the above letter, Raymond approached you for comment.

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HK(IFRIC) Interpretations 4

Example

- Entity OB contracted with a toy manufacturer, Jedi China Inc.
- The contract required Jedi to use its plastic machine, Premium Toy No.1, to produce and deliver 20,000 sets of premium toys to Entity OB.
- If the toys can be produced with the same quality, Jedi can choose to produce the toys by using other machine not specified in the contract.
- Is it a lease under HKAS 17?



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HK(IFRIC) Interpretations 4

Example

- ABC signed a contract with UX to supply minimum quantity of electricity needed in its production process for 10 years.
- UX builds a power generator adjacent to ABC's plant to produce the electricity and maintains ownership and control over it. The contract terms include:
 - The generator is explicitly identified in the arrangement.
 - UX has a right to supply the generator's electricity to other customers but ABC has the ability to control physical access to the generator
 - UX is responsible for repairs, maintenance, and capital expenditures and must stand ready to deliver a minimum quantity of electricity each month.



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Example

- As stated in the previous example, ABC signed a contract with UX to supply minimum quantity of electricity needed in its production process for 10 years.
- UX builds a power generator adjacent to ABC's plant to produce the electricity and maintains ownership and control over it. In addition to the terms stated in the previous example, the contract terms also include:
 - UX is responsible for repairs, maintenance, and capital expenditures and must stand ready to deliver a minimum quantity of gas each month.
 - Each month, ABC will pay
 - a fixed capacity charge (irrespective of whether it takes any electricity from the generator) and
 - a variable charge based on actual production taken (incl. the generator's actual energy costs, which amount to about 90% of the generator's total variable costs).



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HKAS 40 – Investment Property

Example

How do we account for the following property?

- Owner-occupied property
- Property (completed or under development) intended for sale in the ordinary course of business
- Property being constructed or developed for third parties
- Property leased out under finance lease
- Property that is being constructed or developed for future use as investment property
- How's the classification for existing investment property being redeveloped for continued future use as investment property?

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HKAS 40 – Investment Property

Case



Accounting policy (2004/05) on buildings:

- The cost of construction of **the Duke of Windsor Social Service Building** “the Building” has been written down to a nominal value of HK\$1.
- The Council hires out meeting rooms and auditorium in the Building to third parties and lease out some portion of usable floor area to certain bodies approved by the Government.
- Income derived from hiring meeting rooms and auditorium and leasing out usable floor area have been accounted for in the statement of operations as hiring fees, rental and management fee income.

Point for consideration:

- Fulfil the definition of investment property?
- Generate passive cash flow or owner-occupied?
- Separable under HKAS 40? If not, significant portion for rental?

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HKAS 40 – Investment Property

Example

Can the following freehold properties be classified as investment property in individual level and in consolidation?

Individual

Consolidation

- Parent A's property leased to Subsidiary B
- Subsidiary C's property leased to Parent D
- Subsidiary E's property leased to Subsidiary F
- Parent G's property leased to Associate H