FOO KON TAN

Financial Reporting Updates

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Principal Member of HLB International

Welcome to Financial Reporting Updates.

This is your quarterly update on all things relating to International Financial Reporting / Auditing Standards or Financial Reporting / Auditing Standards. We'll bring you up to speed on topical issues, provide comment and points of view and give you a summary of any significant developments.

Our third edition of 2016 starts with some issues of volatile picture for various asset and liabilities classes, development of International Financial Reporting Standards, International Auditing Standards and regulatory matters.

Read this issue to find out:

- **Development of International / Singapore Financial Reporting Standards**
  - IASB / ASC issued Clarifications to IFRS 15 / FRS 115 *Revenue from Contracts with Customers*
  - IASB issued narrow amendments to IFRS 2 *Share-based Payment* - Classification and Measurement of Share-based Payment Transactions
  - ASC issued FRS 116 *Leases*
  - IFRS Convergence - Indonesia
- **International / Singapore Auditing Standards**
  - IAASB issued ISA 810 (Revised) *Engagements to Report on Summary Financial Statements*
  - *ISCA* issued SSA 800 (Revised) *Special Considerations - Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks* and SSA 805 (Revised) *Special Considerations - Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*
  - Communication of Significant Difficulties Encountered during the Audit to Those Charged with Governance
  - ISCA issued Audit Committee Study Report 2015

In addition, we end with **regulatory matters** such as:

- Extending Special Employment Credit
- SGX launches Sustainability Reporting Guide and rule

IASB / ASC issued Clarifications to IFRS 15 / FRS 115 *Revenue from Contracts with Customers*

On 12 April 2016, IASB issued the Clarifications to IFRS *15 Revenue from Contracts with Customers: Issues* while on 8 June 2016, ASC issued the Clarifications to FRS 115 *Revenue from Contract with Customers*.

The amendments clarify how to:

- **Identify a performance obligation (the promise to transfer a good or a service to a customer) in a contract**
  The amendments clarify the guidance for determining when the promises in a contract are 'distinct' goods or services that should be accounted for separately. Identifying performance obligations is fundamental to the application of IFRS 15 / FRS 115 and the IASB / ASC decided to make the same changes as the FASB in order to retain convergence in this important area.

- **Determine whether a company is a principal (the provider of a good or service) or an agent (responsible for arranging for the good or service to be provided)**
  The IASB / ASC has clarified that the principal in an arrangement controls a good or service before it is transferred to a customer. It has also revised the structure of the indicators so that they indicate when the entity is the principal rather than indicate when it is an agent, and eliminated two of the indicators ('the entity's consideration is in the form of a commission' and 'the entity is not exposed to credit risk'). These changes are converged;

- **Determine whether the revenue from granting a licence should be recognised at a point in time or over time.**
  The amendments to the licensing guidance clarify when revenue from a licence of intellectual property (IP) should be

recognised ‘over time’ and when it should be recognised at a ‘point in time’.

The FASB decided to develop a different model, which categorises licences as either ‘functional’ or ‘symbolic’ to determine the accounting treatment. The FASB also provided guidance on the impact of restrictions in licences, accounting for renewals of licences and the pattern of revenue recognition for performance obligations that include a licence.

These differences mean that revenue reported by IFRS / FRS reporters might be different from revenue reported by competitors under US GAAP. This could affect companies that that license IP such as in the media, biotech and software industries. However, it is too soon to know how widespread any differences will be in practice.

The amendments also clarify when to apply the guidance on recognising revenue for licences of intellectual property with fees in the form of a sales- or usage-based royalty. These changes are converged.

In addition to the clarifications, the amendments include two additional reliefs to reduce cost and complexity for a company when it first applies the new Standard.

One expedient allows entities to use hindsight when assessing contract modifications that exist at transition.

The second expedient allows entities applying the full retrospective method to elect not to restate contracts that are completed at the beginning of the earliest period presented. This expedient will not be available to US GAAP reporters.

When are the amendments effective?
The amendments have the same effective date as the Standard, IFRS 15 / FRS 115, i.e. on 1 January 2018.

What is the impact?
The amendments do not change the core principles of IFRS 15 / FRS 115. However, they clarify some of the more complex aspects of the standard. The amendments could be relevant to a broad range of entities and should be considered as management evaluates the impact of IFRS 15 / FRS 115.

The amendments to IFRS 15 / FRS 115 are not in all instances the same as those that the FASB is making to the US standard. In addition to the differences noted above, the FASB has provided an exception for accounting for shipping and handling activities and is further expected to make narrow-scope amendments to the guidance on assessing collectability, presentation of sales-taxes and measuring non-cash consideration.

IFRS 15 / FRS 115 will not include any additional guidance on these topics. The IASB / ASC has in most cases indicated in the Basis for Conclusions where it expects that the differences in wording between the standards will or could result in different conclusions under IFRS / FRS and US GAAP.

IASB issued narrow amendments to IFRS 2 *Share-based Payment* - Classification and Measurement of Share-based Payment Transactions

On 20 June 2016, IASB issued the final amendments to IFRS 2 *Share-Based Payment on the classification and measurement of share-based payment transactions.* The amendments are narrow in scope and address specific areas of classification and measurement.

The three types of arrangement that would be affected are as follows:

Cash-settled share-based payment transactions that include performance conditions
Currently there is no guidance in the extant IFRS 2 on how to measure the fair value of cash-settled share-based payments with vesting or non-vesting conditions. Diversity in practice exists between measuring the liability using the same approach as for equity-settled awards and using full fair value.

Under the amendments, a cash-settled share-based payment would be measured using the same approach as for equity-settled share-based payments - i.e. the modified grant date method.

Hence in measuring the liability: it clarifies that:
- Vesting conditions (service and non-market performance conditions), upon which satisfaction of a cash-settled share-based payment transaction is conditional, are not taken into account when estimating the fair

value of the cash-settled share-based payment at the measurement date. Instead, these are taken into account by adjusting the number of awards included in the measurement of the liability arising from the transaction.
- An entity recognises an amount for the goods or services received during the vesting period. That amount is measured based on the best available estimate of the number of awards that are expected to vest. The entity needs to revise the estimate if subsequent information indicates that the number of awards that are expected to vest differs from previous estimates. On the vesting date, the entity revises the estimate to equal the number of awards that have ultimately vested.
- Market and non-vesting conditions should be taken into account in measuring its fair value
- The number of rights to receive cash would be adjusted to reflect the best estimate of those expected to vest as a result of satisfying service and any non-market performance conditions.
- This amendment would not change the cumulative amount of expenses that is ultimately recognised, because the total consideration for a cash-settled share-based payment is equal to the cash paid on settlement.

A new illustrative example, Example 12A, has also been included in the IG to IFRS 2.

Share-based payments settled net of tax withholdings

In some countries, the company may be obliged to collect or withhold tax related to share-based payment, even though the tax obligation is often a liability of the employee and not the company. A question exists as to whether the portion of the share-based payment that is withheld in these instances should be accounted for as equity-settled or cash-settled.

The amendment clarifies that for classification, a share-based payment transaction with employees is accounted for as equity-settled if:
- The terms of the arrangement permit or require a company to settle the transaction net by withholding a specified portion of the equity instruments to meet the statutory tax withholding requirement (the net settlement feature)
- The entire share-based payment transaction would otherwise be classified as equity-settled if there were no net settlement feature.

A new illustrative example, Example 12B, has also been included in the IG to IFRS 2.

Modification to a share-based payment transaction that changes the classification from cash settled to equity settled

There is no specific guidance in IFRS 2 for cash-settled share payments that are modified. As a result of diversity in practice, the following approach to accounting for a modification to a cash-settled share-based payment that results in its classification changing to equity-settled:
- At the modification date, the liability for the original cash-settled share-based payment would be derecognised, and the equity-settled share-based payment would be measured at its fair value as at the modification date and recognised to the extent that the services have been rendered up to that date
- The difference between the carrying amount of the liability as at the modification date, and the amount recognised in equity as that date, would be recognised in profit or loss immediately.

The amendment also clarifies that if, as a result of the modification, the vesting period is extended or shortened, the application of its requirements must reflect the modified vesting period and that they also apply if the modification occurs after the vesting period.

A new illustrative example, Example 12C, has also been included in the IG to IFRS 2.

Effective date and transition

The effective date of the amendments should be 1 January 2018 and earlier application should be permitted.

As a practical simplification, the amendments can be applied prospectively so that prior periods do not have to be restated. More specifically:
- The amendments relating to the effects of vesting conditions on cash-settled share-based payments and the classification of share-based payments with net settlement features for withholding tax obligations apply to share-based payment transactions that are unvested, or vested but unexercised, at the date that an entity first applies the amendments and to those with a grant date on or after the date of first application of the amendment.
- The amendment relating to the modification of share-based payment transactions from cash-settled to equity-settled only applies to modifications that occur on or after the date that an entity first applies the amendments.

An entity may elect to apply the IFRS 2 amendments retrospectively, subject to the transitional provisions in paragraphs 53–59 of IFRS 2, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, if and only if it is possible without hindsight. If an entity elects retrospective application, it must do so for all three amendments.

Next Steps

The amendments could affect the timing and amount of expense recognised. Companies should consider whether the amendments could result in a change to their accounting for share-based payment transactions.

Careful analysis of net share settlement arrangements will continue to be required to determine whether part of the award should be treated as cash-settled or whether the arrangement is within the scope of this exception and, if so, whether it is appropriate to treat it as equity settled in its entirety.

Entities may also have adopted a policy of spreading any incremental value relating to the vested portion of the award over the remaining (post-modification) vesting period, rather than recognising the difference immediately as at the date of modification. In such cases, entities will need to revise their accounting policy for any modifications made following adoption of the amendment

ASC issued FRS 116 *Leases*

On 30 June 2016, the Accounting Standard Council (ASC) issued FRS 116 *Leases*. FRS 116 *Leases* sets out the principles for the recognition, measurement, presentation and disclosure of leases. The objective is to ensure that lessees and lessors provide relevant information in a manner that faithfully represents those transactions. This information gives a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the entity.

What has changed?

Lessee accounting

FRS 116 *Leases* introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments.

A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities. As a consequence, a lessee recognises depreciation of the right-of-use asset and interest on the lease liability, and also classifies cash repayments of the lease liability into a principal portion and an interest portion and presents them in the statement of cash flows applying FRS 7 *Statement of Cash Flows*.

Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease.

FRS 116 contains disclosure requirements for lessees. Lessees will need to apply judgement in deciding upon the information to disclose to meet the objective of providing a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the lessee.

Lessor accounting

FRS 116 *Leases* substantially carries forward the lessor accounting requirements in FRS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.

FRS 116 *Leases* also requires enhanced disclosures to be provided by lessors that will improve information disclosed about a lessor's risk exposure, particularly to residual value risk.

When is FRS 116 effective?

FRS 116 is effective for annual periods beginning on or after 1 January 2019. Earlier application is permitted for entities that apply FRS 115 *Revenue from Contracts with Customers* at or before the date of initial application of FRS 116.

More detailed changes and illustrative example

You can refer to our Financial Reporting Updates Q2 2016 for detailed changes and illustrative example for lessee accounting.

Next steps

As the final standard is effective from 1 January 2019. This new guidance might require changes to systems, processes and controls. Management will need to assess implications as early as this year to ensure ample time to embrace the change and capture information needed for transition.

IFRS Convergence – Indonesia

On 25 May 2016, the Trustees of the IFRS Foundation, the Indonesia Financial Services Authority (OJK) and the Institute of Indonesia Chartered Accountants (IAI) today announced their intention to deepen cooperation as Indonesia develops its plans to achieve full convergence with IFRS Standards.

IAASB issued ISA 810 (Revised) *Engagements to Report on Summary Financial Statements*

On 24 March 2016, the International Auditing and Assurance Standards Board (IAASB) issued International Standards on Auditing (ISA) no. 810 (Revised), Engagements to Report on Summary Financial Statements respectively.

ISA 810 (Revised) deals with the auditor's responsibilities relating to an engagement to report on summary financial statements derived from financial statements audited in accordance with ISAs by that same auditor.

What are the main changes of ISA 810 (Revised)?

The changes to ISA 810 include:

(a) Amendments to the extant ISA 810 to address the information gap in the auditor's report on the related audited financial statements.

Previously, a material uncertainty related to going concern or an uncorrected material misstatement of other information were required to be addressed in an Emphasis of Matter (EOM) paragraph or an Other Matter (OM) paragraph, respectively, and, in accordance with extant ISA 810.17, would always be required to be highlighted in the auditor's report on the summary financial statements (referred to hereafter as "the ISA 810 report").

ISA 570 (Revised), ISA 706 (Revised) and ISA 720 (Revised) now require separate sections in the auditor's report on the audited financial statements when such circumstances exist (i.e., these matters are no longer addressed using an emphasis of matter or other matters paragraph).

(b) Introducing a new requirement for the ISA 810 report to include a reference to any communication of key audit matters in the auditor's report on the audited financial statements (i.e., limited to requiring a reference to the existence of such communication without needing to describe, repeat or otherwise refer to individual key audit matters).

(c) Presenting the ISA 810 illustrative auditor's reports in a manner consistent with those in ISA 700 (Revised) in terms of the layout and content, including the ordering of elements (for example, the Opinion section is now positioned first) and use of headings.

When is ISA 810 (Revised) effective?

ISA 810 (Revised) will become effective at the same time as the auditor reporting standards addressing general purpose financial statements for engagements to report on summary financial statements for periods ending on or after December 15, 2016.

ISCA issued SSA 800 (Revised) *Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks* and SSA 805 (Revised) *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*

On 27 May 2016, ISCA issued SSA 800 (Revised) *Special Considerations – Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks* and SSA 805 (Revised) *Special Considerations – Audits of Single Financial Statements and Specific Elements, Accounts or Items of a Financial Statement*. The revised standards are based on the International Standard on Auditing (ISA) 800 (Revised) and ISA 805 (Revised) respectively issued by the International Auditing and Assurance Standards Board (IAASB).

What are the key revisions?

Key revisions made to the extant SSA 800 and SSA 805 include:

- Refinements to the requirements and corresponding application material, to be in line with the new concepts established by the new and revised auditor reporting standards, such as (1) communication of key audit matters and (2) a Material Uncertainty Related to Going Concern section.
- New application material relating to going concern, key audit matters, other information and naming of the engagement partner.
- Updated illustrative auditor's reports that:
  - Align with the reporting requirements in SSA 700 (Revised) in terms of the layout and content, including the ordering of elements (for example, the Opinion section is now positioned first), use of headings and terminology; and
  - Include more fulsome descriptions of the circumstances that are assumed for each of the illustrative auditor's reports and indicate the applicability of the auditor reporting enhancements.

What are the conforming amendments?

Conforming amendments have also been made to SSA 700 (Revised) to require the disclosure of the name of the engagement partner in the auditor's reports of all listed entities.

When are the revised standards effective?

The revised standards are effective for audits of financial statements for periods ending on or after 15 December 2016, in line with the effective date of the new and revised auditor reporting standards.

Communication of Significant Difficulties Encountered during the Audit to Those Charged with Governance

The theme of the revised ISA / SSA 260 Communication with Those Charged with Governance is to emphasise the importance of effective two-way communication between the auditor and those who are charged with the governance of the audited entity.

The revised standard provides more guidance on what matters are likely to be of governance interest. In particular, it requires that any significant difficulties encountered during the audit – for example, the unavailability of expected information – be communicated.

Significant matters discussed, or subject to correspondence with management may include such matters as:

- Business conditions affecting the entity, and business plans and strategies that may affect the risks of material misstatement.
- Concerns about management's consultations with other accountants on accounting or auditing matters.
- Discussions or correspondence in connection with the initial or recurring appointment of the auditor regarding accounting practices, the application of auditing standards, or fees for audit or other services.

It also requires the auditor to evaluate whether the two-way communication between the auditor and those charged with governance is adequate for the purposes of the audit. Auditors will need to consider their ability to accept reappointment if they conclude that the level of two-way communication is inadequate for their purposes.

Auditors will need to consider their ability to accept reappointment if they conclude that the level of two-way communication is inadequate for their purposes. The auditor's expectation that communication will be two-way, and that those charged with governance will communicate with the auditor matters they consider relevant to the audit, e.g. strategic decisions that may significantly affect the nature, timing and extent of audit procedures, the suspicion or the detection of fraud, and concerns with the integrity or competence of senior management.

If the two-way communication between the auditor and those charged with governance is not adequate and the situation cannot be resolved, the auditor may take such actions as:

- Modifying the auditor's opinion on the basis of a scope limitation.
- Obtaining legal advice about the consequences of different courses of action.
- Communicating with third parties (e.g. a regulator), or a higher authority in the governance structure that is outside the entity, such as the owners of a business, or the responsible government minister or Parliament in the public sector.
- Withdrawing from the engagement where permitted in the relevant jurisdiction.

When is ISA / SSA 260 effective?

ISA/ SSA 260 (Revised) is effective for audits of financial statements for periods ending on or after December 15, 2016.

ISCA issued Audit Committee Study Report 2015

On 2 June 2016, ISCA issued Audit Committee Study Report 2015. This study is commissioned by the Institute of Singapore Chartered Accountants (ISCA) as part of the on-going knowledge creation by the Corporate Governance Committee of the Institute to obtain information on the compliance with the Singapore Companies Act, the Code of Corporate Governance 2012 (CG Code 2012), the Guidebook for Audit Committees in Singapore - Second Edition (GAC 2014) and the Listing Rules of Singapore Exchange by audit committees (ACs) of listed companies in Singapore.

This report consists of three parts:

- The first part is a review of the empirical literature on ACs with a focus on the attributes of effective ACs.
- The second part profiles the ACs of the listed companies in Singapore in terms of their compliance to the requirements of the Companies Act, the guidelines by the Code of Corporate Governance 2012 (CG Code 2012) and the Guidebook for Audit Committees in Singapore 2014 (GAC 2014), and the Listing Rules of Singapore Exchange.
- The third and final part of this report is a summary of the major issues and views shared by selected chairmen of ACs collated through one-on-one interviews.

Please click here to read the full report.

Extending Special Employment Credit

The Singapore Budget 2016 has announced that the Special Employment Credit (SEC) will be modified and extended for 3 years, to the end of 2019. This will provide employers with a wage offset for workers aged 55 and above earning up to $4,000 a month.

Employers with Singaporean workers aged 65 and above will continue to receive a wage offset of up to 8%. This is in addition to the wage offset of 3% for the re-employment of workers aged 65 and above till the re-employment age is raised in 2017. The SEC will be up to 5% for workers aged 60 to 64 and up to 3% for those aged 55 to 59 (Refer to Table 1 below).

Table 1:
SEC wage offset for working person earning up to S$4,000 per month

Age Group (years)	2017 to 2019
55 to 59	Up to 3% of monthly wage
60 to 64	Up to 5% monthly wage
65 and above	Up to 8% of monthly wage (+ additional 3% until re-employment age is raised)

The current 5-year SEC term ends in 2016, i.e. last SEC payment in March 2017 for work done in July to December 2016. The SEC will be extended for 3 years (viz. 2017 to 2019) to provide a wage-offset to employers hiring Singaporean workers aged 55 and above, and earning up to $4,000. The amount of SEC entitlement depends on two factors:

(i) the number of employees (Singapore workers) on the employer's CPF payroll for work done between January and June 2017 to 2019 and July and December 2017 to 2019

(ii) the salary cost of these employees up to S$4,000, derived from the CPF contributions made for them.

How should employers recognise SEC?

The first SEC will be paid in September of the same year for work done from January and June, and March of the following year for work done from July and December. Accordingly, employers should recognise these credits as income only when it becomes receivable in September 2015 and March 2016 in accordance with FRS 20 paragraph 20 which states:

"A government grant that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs shall be recognised as income of the period in which it becomes receivable."

SGX launches Sustainability Reporting Guide and rule

On 20 June 2016, Singapore Exchange (SGX) introduced sustainability reporting on a "comply or explain" basis.

SGX will invite company CEOs to a briefing for clarity and understanding of the new requirement and organise training for all listed companies to build their reporting capability. SGX consulted on the sustainability reporting requirement at the start of 2016 and received strong support for the "comply or explain" framework. After carefully considering the feedback received, some changes to the Sustainability Reporting Guide and the requirement were made.

What are the main changes?

The main changes are as follows:

- Giving companies up to 12 months from the end of the financial year to publish their first report. This takes effect for any financial year ending on, or after, 31 December 2017.
- Instead of a compliance statement, the Board statement to be included in the report describes the company's sustainability actions.
- The materiality principle will be applied when determining whether an ESG factor should be reported on. Factors like corruption and diversity, if assessed to be immaterial by companies, may be excluded. Companies are however advised to present information on these factors on their websites to satisfy stakeholder interest.

What are the key features of the sustainability reporting requirements?

Key features of the sustainability reporting requirements are:

- Companies have to publish a sustainability report at least once a year, no later than 5 months after the end of each FY.
- The report should describe the sustainability practices with reference to five primary components: material ESG factors; policies, practices and performance; targets; sustainability reporting framework; and the Board statement.
- If a company excludes a primary component, it must describe what it does instead with reasons for doing so. Full details of the sustainability reporting rule and Guide are found here.
- The sustainability report will be based on the principles set out in the Guide which include, among others, providing an accurate and balanced view of the risks and opportunities in a concise manner.
- SGX does not advocate a particular sustainability reporting framework; companies should carefully select an appropriate framework for their business model and industry. Reports do not require external assurance though companies which have been reporting for several years may find it useful to do so.

What are the primary Components of the Sustainability Report – Comply or explain

- Identify environmental, social and governance (ESG) aspects that are material to the business
- Set out policies, practices and performance in relation to material ESG issues identified
- Set performance targets for each material ESG aspect for forthcoming year
- Select a globally-recognised framework to report on ESG matters

The Board has ultimate responsibility over the sustainability process and report.

Where you cannot report on any of the above five primary components, you must state so and explain what you do instead and the reasons for doing so for each.

What can external auditors help listed companies?

Listed companies who have prepared sustainability reports may engage external auditors to conduct independent verification of the reports. Assurance on a sustainability report increases stakeholders' confidence in the accuracy and completeness of the information as well as adds credibility to the report. Assurance also acts as an important feedback mechanism to listed companies in improving the quality of their sustainability reports.

How we can assist

If you need assistance or advice on the above, we are here to assist you.

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