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FINANCIAL REPORTING MATTERS

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A new standard on joint arrangements, FRS 111, comes into effect 1 January 2014. What key questions should you be asking as you prepare for the transition?

In May 2013, the FASB and the IASB issued the controversial lease accounting proposal for a second round of public comments. The revised proposal is a watered-down version of the original issued in 2010 and contain concessions for property leases. How will the proposed changes impact tenants and landlords?

The Wage Credit Scheme, announced during Singapore Budget 2013, is part of a three-year Transition Support Package within the Government's Quality Growth Programme. What are the key features of the scheme and how do you estimate and report the amount of entitlement in your interim and annual financial statements?

On the international front, various boards are seeking comments on standards including the IASB Conceptual Framework, the IAASB exposure draft on improving the auditor's report, and the IASB and the FASB exposure draft on insurance contracts. Read the section on International developments to find out more.

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MANDATORY XBRL FILING TAKES EFFECT ON 2 DECEMBER 2013

In August 2013, ACRA released the finalised XBRL filing requirements and the new XBRL tool, BizFinX.

Singapore-incorporated companies are required to file a full set of financial statements in XBRL from **2 December 2013.**

If you *need help making sense of the new requirements and converting or mapping your financial statements to the new XBRL taxonomy, speak to your KPMG contact today or email us at xbrl@kpmg.com.sg*

1. Getting ready for transition: FRS 111 Joint Arrangements

This article is contributed by:

Lee Sze Yeng
Partner, Audit

Chan Yen San
Senior Manager, Professional Practice

If you are party to a joint arrangement such as a joint marketing or a joint sourcing arrangement, it is important that you familiarise yourself with and prepare for the transition to FRS 111, a new standard on joint arrangements.

FRS 111, which comes into effect on 1 January 2014, may impact you if you have:

- a joint arrangement accounted for as a jointly controlled entity under current accounting standard
- a joint arrangement structured as a partnership
- a joint arrangement structured through a separate legal entity such as an incorporated company
- a commitment to purchase goods or services from the jointly-controlled entity

Old arrangements, new challenges

If you are party to an arrangement in which you have joint control, you should note that there is a new standard on joint arrangements on the horizon, FRS 111. This new standard comes into effect on 1 January 2014. Have you completed your analysis of what it means for your accounting?

The new standard is challenging as it no longer relies solely on the legal form of the arrangement. Instead, there are a series of steps to the analysis and many factors to potentially consider, all of which require time and resources.

You will need to conduct an analysis of what FRS111 means for your accounting. Once your analysis of the joint arrangements is completed, the related disclosure standard, FRS 112 *Disclosure of Interests in Other Entities*, presents challenges of its own and may require additional data collection, too.

These additional disclosures in FRS 112 are all on a gross basis, that is, 100 percent of the arrangement assets and liabilities. It is not based on your percentage interest in the joint ventures and some of this information may not be readily available under your current processes and systems.

Details of the new proposals are available in our September 2012 issue of financial reporting matters

In this article, we list four key questions you should consider as you prepare for transition to FRS 111.

1. Do you have a joint arrangement accounted for as a jointly controlled entity under current accounting standard?

The accounting policy choice under the old standard (equity accounting or proportionate consolidation) for jointly controlled entities has been removed.

Under FRS 111, a jointly-controlled entity could be:

- a joint venture for which equity accounting is applied; or
- a joint operation for which line-by-line accounting of the underlying assets and liabilities is applied.

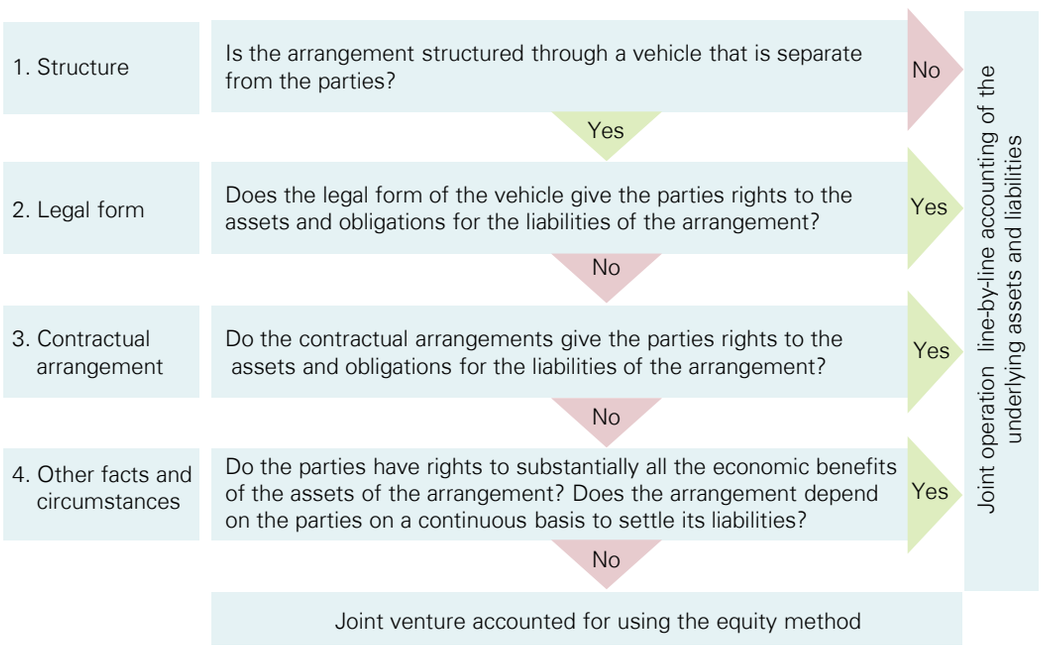
The new standard drives the accounting through a series of tests to determine who has rights to the assets and obligations for the liabilities of the arrangement. It is important to note that the accounting is no longer driven by the legal form of the arrangement.

We expect many, although not all, jointly controlled entities under the current accounting standard to be classified as joint ventures under FRS 111.

Nonetheless, all joint arrangements will need to be re-assessed in the transition to FRS 111.

The following diagram is a summary of the series of tests to be applied when classifying a joint arrangement.

Diagram 1



Under the new standard, if you need to apply the equity method to an interest that is currently proportionately consolidated, the current gross reporting of related assets, liabilities and transactions will appear on a one-line basis going forward. This will notably decrease your revenue, gross assets and gross liabilities.

Conversely, if you currently apply the equity method to an interest that is determined to be a joint operation under FRS 111, you will be required to gross up your reporting of the related assets, liabilities and transactions.

The example below illustrates the two accounting methods in a 50% - 50% joint arrangement.

Joint arrangement (Partner A: 50%/Partner B: 50%)					
	Joint arrangement	Joint venture equity accounting		Joint operation[1] line-by-line accounting	
		Partner A	Partner B	Partner A	Partner B
	100%	50%	50%	50%	50%
Balance sheet					
Investment properties	1,000			500	500
Cash	500			250	250
Inventories	500			250	250
Other assets	500			250	250
Total assets	2,500			1,250	1,250
Debt	(800)			(400)	(400)
Other liabilities	(200)			(100)	(100)
Total liabilities	(1,000)			(500)	(500)
Net assets	**1,500**	**750**	**750**	**750**	**750**
Income statement					
Revenue	800			400	400
Cost of sales	(500)			(250)	(250)
Gross profit	300			150	150
Expenses	(100)			(50)	(50)
Finance costs	(40)			(20)	(20)
Net profit before tax	160			80	80
Taxation	(20)			(10)	(10)
Net profit after tax	**140**	**70**	**70**	**70**	**70**

2. Do you have a joint arrangement structured as a partnership?

Partnerships are commonly used as vehicles for joint arrangements.

By current accounting standard, all partnerships are classified as jointly controlled entities based on their structure as a separate vehicle. Therefore, there is a choice of using either the equity method or proportionate consolidation. In the separate financial statements of the investor, they are typically accounted for at cost less impairment.

Under the new standard, if you have a joint arrangement structured through a partnership, you will need to first consider whether the partnership has a separate legal personality. If the partnership does not have a separate legal personality (i.e. the legal structure does not confer separation of rights and obligations between the partners and the partnership), it is a joint operation under FRS 111.

In Singapore, a General Partnership registered under the Business Registration Act (Chapter 32) is not a separate legal entity. A General Partnership cannot own property in its name. Its partners have unlimited liability and are personally liable for the partnership's debts and losses incurred by other partners.

In the Singapore context, if you are a partner with joint control in a General Partnership, you will have to account for your interest in the General Partnership as a joint operation.

As a partner, you will have to account for your share of the underlying assets and liabilities of the partnership. This will be on a line-by-line basis as determined and specified in the contractual arrangement. It may be the same as your ownership interest.

[1] Assuming the rights to the underlying assets, the obligations for the underlying liabilities, revenue and expenses are shared in proportion to the joint venture interest.

This accounting is similar in effect to proportionate consolidation and is applied to the separate financial statements of the partner as well as the consolidated financial statements.

If you are exempted from consolidation and have been accounting for your interests in such partnerships at cost less impairment (separate financial statements) or using the equity-method, you will need to collate the information necessary for the line-by-line accounting under the new standard.

In contrast to a General Partnership, a Limited Liability Partnership (LLP) that is governed under the Limited Liability Partnerships Act (Chapter 163A) is a separate legal entity from its partners.

In Singapore, an LLP can own a property in its name and partners of a LLP have limited liability. Partners are also not personally liable for the LLP's debts and losses incurred by other partners.

If you are a partner with joint control in a Singapore LLP, your interest will more likely than not be accounted for as a joint venture under the new standard (i.e. equity accounting), given that the whole purpose of using a LLP structure instead of a General Partnership structure is to enjoy the benefits of separate legal status. Nonetheless, under FRS 111 you will still have to perform further assessment under test 3 and test 4 (see Diagram 1) to determine the appropriate accounting, whether as a joint venture or a joint operation.

If you are a partner in foreign partnerships, you will have to carefully assess the respective legal framework in the foreign jurisdictions as there will likely be differences from the framework in Singapore.

3. Do you have a joint arrangement structured through a separate legal entity such as an incorporated company?

By the new standard, a joint arrangement not structured through a separate legal entity is always a joint operation. However, the accounting outcome is less obvious if your joint arrangement is structured through a separate legal entity such as an incorporated company or a Singapore LLP.

You will need to further consider whether there is any agreement between you and your partners that might pierce through the corporate veil, thus conveying the rights to the assets and obligations for the liabilities of the separate legal entity to you and your partners.

Guarantees provided by you and your partners to the creditors of the separate legal entity generally do not lead to you and your partners having the primary obligation for the liabilities of the arrangement. Hence, a guarantee will not, by itself, result in joint operation accounting.

Based on our experience, assessing the implications of the agreements vis-à-vis the relevant laws and contractual terms can be time-consuming and may require the input of legal professionals. Hence, you should start your assessment earlier rather than later.

4. Do you have a commitment to purchase goods or services from the jointly controlled entity?

The final test in the series of tests is the consideration of 'other facts and circumstances' (see Diagram 1).

This test is particularly relevant when the activities of the joint arrangement are primarily to provide output to you and your partners. For example, when you and your partners are committed to purchase goods or services from the arrangement by entering into off-take agreements, or the arrangement provides services to your business such as a joint marketing arrangement.

To illustrate this, let us assume that you and your partners invested in a jointly controlled entity. In this joint arrangement, you and your partners are contractually committed to purchase all of the production in the arrangement. It will be at a price that covers all production costs; and any cash shortages will be financed by you and your partners in proportion to the ownership interests. In this example, the jointly controlled entity is a joint operation, because:

(1) you and your partners have committed to purchase all of the production manufactured and therefore have rights to substantially all the economic benefits of the assets; and

(2) you and your partners have an obligation for the liabilities of the manufacturing arrangement because there is exclusive dependence on the parties to generate cash flows and to cover any cash shortages.

Other important facts and circumstances to consider include liquidity and financing arrangements, transfer pricing and the level of output sold to you and your partners as compared to third parties.

The above discussion shows that the analysis is more holistic but it is also more complex and highly judgemental under the new requirements.

2. Radical changes to lease accounting – what does it mean to tenants and landlords?

This article is contributed by:

Lo Mun Wai
Partner, Audit

Chan Yen San
Senior Manager, Professional Practice

In May 2013, the FASB and the IASB (the Boards) issued the controversial lease accounting proposal for a second round of public comments. The revised proposal is a watered-down version of the original proposal issued in 2010 and has numerous concessions for leases of property.

Details of the new proposals are available in our June 2013 issue of financial reporting matters.

A notable change from the original proposal is that most property leases will be accounted for using a model that is different from most non-property leases.

How will the revised proposal affect you?

Tenants: On-balance sheet accounting for all tenants with operating leases, unless the maximum possible lease period is 12 months or less

From the tenants' perspective, the revised proposal will radically change today's lease accounting. It removes the current divide between operating and finance leases, and brings most leases onto your balance sheet.

Under the current accounting standard, leases of office, retail or industrial space are off-balance sheet items if they are operating leases.

With the revised proposal, tenants will be required to recognise a right-of-use (ROU) asset and a corresponding lease liability for the expected future lease payments on-balance sheet for most leases. This is similar to how we currently account for finance lease.

As a tenant, if you are granted an option to extend the lease or an early termination option, you will have to include the estimated lease payments during the secondary lease period in the measurement of the lease liability. Accounting for lease liability in this manner applies if you have a significant economic incentive to extend the lease or not to exercise the termination option.

The revised proposal allows short-term leases to continue to stay off your balance sheet as a practical expedient. Short-term leases are defined as those that do not contain a purchase option and have a maximum possible lease term, including any optional secondary lease period of 12 months or less.

Since most leases in Singapore are for lease periods of two years or more, you will likely show higher assets and liabilities under the revised proposal.

As a tenant, you should assess the effects arising from the revised proposal. The impact on your leverage ratio may be significant and loan covenants may be breached.

This is also an opportunity for you to review your real estate needs and evaluate carefully the different options available (such as buy, re-contract for shorter lease term, incorporate more turnover rents (see below on "No change to accounting for turnover rents") so as to optimise your balance sheet.

An early start will give you the much needed time to get your people, systems and processes ready for the revised proposal.

Tenants: Preservation of straight-line expense recognition for most tenants with operating leases

The revised proposal introduces a dual model for lease classification. You will need to classify the leases into either Type A or Type B leases.

As a tenant, you will recognise lease expense on a straight-line basis in the income statement if the lease is classified as a Type B lease.

A property (i.e. land and/or building) lease is presumed to be a Type B lease unless:
(a) the lease term is for the major part of the remaining economic life of the underlying asset; or
(b) the present value of the lease payments accounts for substantially all of the fair value of the underlying asset.

If the underlying asset contains both land and building, the remaining economic life of the building is used as the basis for determining the classification of the lease.

Leases that do not qualify as Type B leases are classified as Type A leases. If you have Type A leases, you will present the amortisation of the ROU asset and the interest on lease liability as separate expenses in the income statement. This may result in the front-loading of expenses.

Under the revised proposal, property leases currently classified as operating leases will likely fall under Type B leases while those currently classified as finance leases (e.g. 99 years and 999 years leasehold properties) will likely be Type A leases.

Hence, the good news for tenants is that straight-line expense recognition will be preserved for most property leases. This is similar to how operating lease expense is recognised today.

In Singapore, full payment is usually made upfront for leasehold properties (e.g. 99 years or 999 years), which are also likely Type A leases. For such leases, the expense profile will continue to be a straight-line under the revised proposal as they are outright purchases of leasehold interests. If external borrowings are taken to finance the acquisition, you will have additional interest expense arising from the loan that could be front-loaded.

The preservation of straight-line expense recognition under Type B leases for property interests held under operating leases today is certainly welcomed by the real estate industry.

It is noteworthy that the revised proposal distinguishes between property and non-property leases and provides more stringent criteria for classification of non-property leases as Type B leases.

Under the revised proposal, most non-property leases (e.g. equipment) are likely to be classified as Type A leases.

The Boards, however, may face difficulty in getting widespread support for the differing classification criteria for property and non-property leases.

Tenants: No change to accounting for turnover rents

In addition to preserving the straight-line expense recognition, the revised proposal reversed the original decision to include estimated turnover rents in the measurement of lease liability and ROU asset.

Unless the turnover rents are in-substance fixed lease payments, they are recognised as they are paid under the revised proposal, similar to current practice.

Excluding turnover rents will reduce complexity in the measurement process, and keep the ROU asset and the corresponding lease liability lower than they would have been under the original proposal.

Tenants: On-balance sheet accounting for leaseback component in a sale and operating leaseback transaction

If you are a property owner contemplating a sale and leaseback transaction with the aim of downsizing your balance sheet, you may wish to reconsider the transaction in light of the revised proposal.

Today, a sale with an at-market operating leaseback will result in off-balance sheet accounting. Under the revised proposal, the leaseback component will be on-balance sheet unless it is a short-term lease as defined in the standard (i.e. one that does not contain a purchase option and has a maximum possible lease term, including any optional secondary lease period of 12 months or less).

Tenants: Ability to identify and measure the costs of services and reimbursable costs embedded in lease rate will reduce the size of lease liabilities

For many short-term commercial property leases, the landlord may provide certain services such as centralised air-conditioning, building repair and maintenance, building security and exterior cleaning as part of the lease arrangement. It is also common for the landlord to require certain costs and taxes related to the leased property such as insurance premium and property taxes to be reimbursed by the tenant.

If the costs of services and reimbursable costs are embedded in the lease rate, the revised proposal allows non-lease elements to be separated from the lease elements as set out in the table below. If separated, the service elements and reimbursable costs will be off-balance sheet and recognised when incurred.

Scenario	Allocation method
1) When the purchase price (PP) or selling price (SP) of each component is an observable stand-alone price[1]	Separate and allocate based on a relative standalone price basis
2) When the PP/SP of one or more, but not all, components are observable stand-alone prices	Separate and allocate using residual method
3) When no observable stand-alone prices for any of the components in the arrangement are available	No separation. All elements are treated as leases

Under the current accounting standard, the identification and split between the lease and non-lease elements may not be important in the case of an operating lease as both elements are off-balance sheet.

However, with the revised proposal, it will be advantageous for you to clearly identify the pricing of the property lease, costs of services and other reimbursable costs. If you are not able to clearly identify the stand-alone price of at least one element, the whole arrangement will be treated as a lease. The lease, the services and the reimbursable costs will be on-balance sheet.

[1] An 'observable stand-alone price' is a price that the lessor or similar supplier charges for a similar lease, good, or service component on a stand-alone basis.

Landlords: Most aspects of current accounting will continue

If you are a landlord, you are required to apply the same lease classification test as a tenant under the dual model which categorises each lease into either a Type A or a Type B lease.

The classification of a lease as a Type A or Type B lease is important as the accounting differs significantly.

Under the revised proposal, a property (i.e. land and/or building) lease is presumed to be a Type B lease unless:

(a) the lease term is for the major part of the remaining economic life of the underlying asset; or
(b) the present value of the lease payments accounts for substantially all of the fair value of the underlying asset.

If the underlying asset contains both land and building, the remaining economic life of the building is used as the basis for determining the classification of the lease. In some cases, the economic life of the land and the building may differ significantly.

As a landlord of Type B leases, you will follow an accounting model similar to that of operating lease accounting today. What this means is that you will continue to recognise the underlying asset and record the lease income generally on a straight-line basis over the lease term.

As a landlord of Type A leases, you will derecognise the underlying asset and recognise:
- a lease receivable, representing your right to receive lease payments; and
- a residual asset, representing your interest in the underlying asset at the end of the lease term.

Under the revised proposal, property leases that are currently classified as operating leases will likely be classified as Type B leases. Property leases that are finance leases today (e.g. 99 years and 999 years leasehold properties) will likely be classified as Type A leases.

Hence, as a landlord, unless you have Type A leases, most aspects of current accounting will continue under the revised proposal.

While substantial effort is still needed to reassess existing leases, the more important consideration is whether the leasing behaviour of your customers (the tenants) will change due to the revised proposal.

Your tenants may be evaluating their options now and you should take this opportunity to engage them early in the process so that you can reshape your business strategies to cater to their changing needs.

Landlords: Lease classification may change over the life of the property

The classification criterion for property leases into Type A or Type B leases requires a comparison of the lease term with the remaining economic life of the building. This may cause certain leases (new lease or modified lease) of an older building to be classified as Type A leases. For example, a 12-year lease of a building will likely constitute a major part of the remaining economic life of a building with 15 years left.

Landlords: Estimating the value of the residual asset in a Type A lease can be challenging

If you have carved out a 99-year leasehold interest from your freehold land for sale, such leases will likely be classified as Type A leases under the revised proposal.

In a Type A lease, you are required to derecognise the underlying asset and recognise a lease receivable for future lease payments discounted using the rate that you charge the purchaser of the leasehold interest, and a residual asset.

The residual asset is initially measured as:

- the present value of the estimated residual value at the end of the lease term, discounted using the rate that you charge the purchaser of the leasehold interest; and adjusted for
- the present value of expected variable lease payments and unearned profit arising on lease commencement.

You will have to subsequently accrete the residual asset to the estimated residual value at the end of the lease term using the rate you charged the purchaser of the lease. In addition, you will have to test the residual asset for impairment under FRS 36 *Impairment of Assets*.

The residual asset arising from such long-term leases typically relate to the reversionary interest in freehold land. Estimating the expected land value at the end of a long lease term of 99 years or 999 years maybe a challenging task in a volatile property market.

Landlords: Subleases

If you are an intermediate lessor, you will have to account for the head lease using the lessee accounting model and the sublease separately, using the lessor accounting model in the revised proposal.

When classifying the sublease as a Type A or Type B lease, you will have to make the assessment with reference to the underlying property and not the leasehold interest arising from the head lease.

The head lease and the sublease will be accounted for as two separate transactions, both with reference to the underlying property. Your balance sheet will be grossed up with the ROU asset and lease liability arising from the head lease if the sublease is classified as a Type B lease.

When accounting for the sublease as a Type B lease, you will not derecognise the ROU asset arising from the head lease. Instead, the lease income from the sublease is recorded generally on a straight-line basis over the lease term.

Landlords: More investment properties on the landlord's balance sheet

As an intermediate lessor, head leases of property that meet the definition of an investment property (e.g. if the property under the head lease is subleased out to earn rental income) must be accounted for under FRS 40 *Investment Property*.

If you are accounting for investment properties using the fair value model under FRS 40, the ROU assets arising from the head leases have to be measured at fair value.

If you are accounting for investment properties using the cost model under FRS 40, you will need to estimate and disclose the fair value of the ROU assets in the financial statements.

The proposal to require all leases of investment property to be accounted for under FRS 40 represents a change to the scope of FRS 40. According to the existing standard, property interests classified as operating leases can be accounted for on a property-by-property basis under either FRS 40 or FRS 17.

Tenants and Landlords: Property yield can be used if the rate implicit in the lease is not available

The rate the landlord charges tenants is used to discount the lease payments. Unlike the current FRS 17, in the absence of the rate implicit in the lease, the property yield can be used to represent the rate the landlord charges tenants.

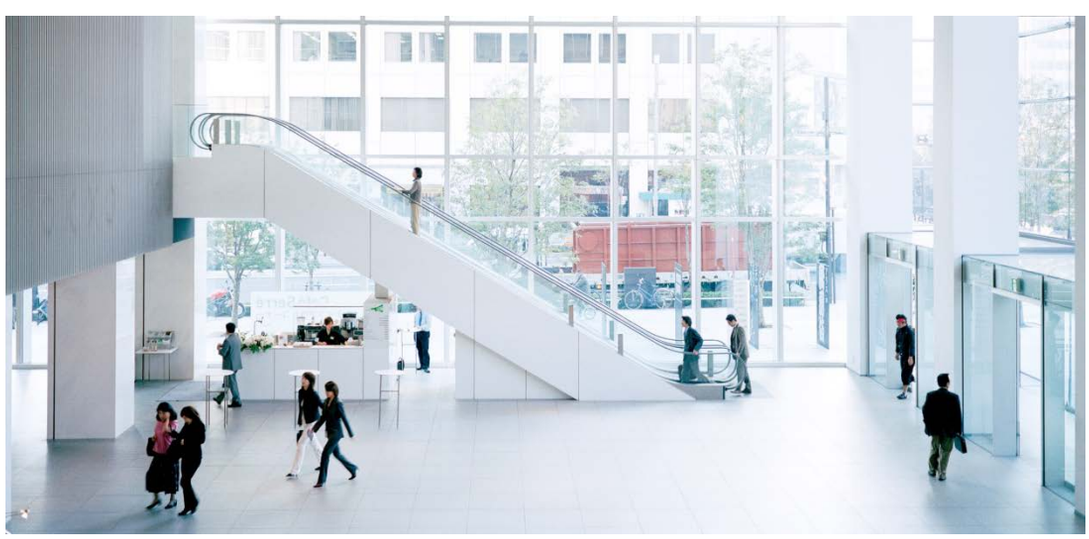
As a tenant, you can use your incremental borrowing rate if the rate your landlord charges you is not readily determinable.

Property yield is one of the inputs often used by property valuers when they appraise the value of a property. This is especially useful in situations where the rate implicit in the lease is not available.

Different valuers use different assumptions and have different ways of calculating the yield. The approaches can be highly subjective and judgemental.

Next Step

At the date of closure of the comment period, the Boards received more than 600 comment letters on the lease proposal. This shows how controversial the proposed changes are. As of now, it remains to be seen how much more compromises are required before the Boards can accomplish their goal of bringing all leases on-balance sheet.



3. Wage credit scheme – How should you account for your entitlement?

This article is contributed by:

Reinhard Klemmer
Partner, Professional Practice

Lim Li Peng
Partner, Corporate Tax

Yip Yong Syn
Senior Manager, Professional Practice

Tan Ter Cheah
Director, Corporate Tax

Under the Wage Credit Scheme announced during the Singapore Budget 2013, the Government will co-fund 40 percent of the increase (of at least $50) in gross monthly wages of Singaporean employees.

An eligible employer who qualifies for the wage credit scheme will receive the payout automatically from the Government. The first payout is expected to be made in March 2014.

If the wage credit is received before the issuance of the financial statements, you can use the actual receipt to account for the wage credit in the financial statements. In situations where the wage credit has not been received, you will have to estimate the amount of wage credit and record the estimated entitlement in the financial statements.

In this article, we explain the key features of the wage credit scheme so as to assist you in estimating and reporting the amount of entitlement in your interim and annual financial statements.

What is the Wage Credit Scheme?

The Wage Credit Scheme (WCS) is a government effort to co-fund wage increases of Singaporean employees. Under this scheme, the Government will co-fund 40 percent of the increase (of at least $50) in gross monthly wages of Singaporean employees.

This co-funding is limited to the portion of wage increase given to employees earning gross monthly wages of up to $4,000, and will cover wage increases that are given between 2013 and 2015.

In other words, once an employee's gross monthly wage exceeds $4,000, the portion of the wage increase that brings the gross monthly wage above $4,000 will not be eligible for co-funding under WCS.

This co-funding will be given until 2015, as long as the wage increases (of at least $50) is sustained.

Illustrative Example – Calculating gross monthly wages
Adapted from *"FAQs on the Wage Credit Scheme"* by the IRAS.

Suppose Company X hires an eligible Singaporean employee from January 2012 to December 2014. The company pays the employee as follows:

	2012	2013	2014
Basic monthly wage	$1,000	$1,100	$1,100
Monthly food allowance	$100	$100	$100
Annual bonus payable in December	$2,400	$3,000	$3,000

The amount of wage credit is dependent on the extent of increase in the Gross Monthly Wage of the employee in 2013 and 2014.

How is 'Gross Monthly Wage' derived?

Gross monthly wage is the total wages paid by the employer to the employee in the calendar year, divided by the number of months in which Central Provident fund (CPF) contributions were made.

The amount of 'total wages' is derived from the monthly employer's CPF contributions based on the allowances and payments for which contributions to CPF are required (which include the basic salary, overtime pay, commissions and bonuses).

What is the employee's gross monthly wage for each of the calendar year from 2012 to 2014?

	2012	2013	2014
Number of months on Company X's payroll **(A)**	12	12	12
Basic monthly wage **(B)**	$1,000	$1,100	$1,100
Monthly food allowance **(C)**	$100	$100	$100
Annual bonus paid in December **(D)**	$2,400	$3,000	$3,000
Total wages **(E) = A*(B+C)+D**	$13,440	$17,400	$17,400
Employee's gross monthly wage **E / A**	**$1,300**	**$1,450**	**$1,450**

How much wage credits can Company X receive from the Government?

The wage credit is limited to the portion of wage increase given to the employee earning gross monthly wages of up to $4,000, and will cover wage increases that are given between 2013 and 2015. The wage credits for Company X are calculated as follows:

	2012	2013	2014
Employee's gross monthly wage	**$1,300**	**$1,450**	**$1,450**
Gross monthly wage increase from previous year **(F)**	n/a	$150	$0
		2013	2014
Wage credits to be paid to employer **(40%*F*A)**		$720	$720

While there is no increase in gross monthly wage in 2014, the company will continue to receive wage credits as the wage increase given in 2013 is sustained in 2014.

When will employers receive the wage credit?

The wage credits will be paid automatically to eligible employers by March of the following year. The first payout under WCS is expected to be made at the end of March 2014, while the last payout will be at the end of March 2016.

In the above example, the wage credit for 2013 is expected to be paid to Company X in March 2014 and 2014 wage credits in March 2015.

Which employers are eligible for WCS?

All employers, other than those on the exclusion list below, would qualify for wage credits if all of the following conditions are fulfilled:

(i) Employer gave at least a $50 increase in gross monthly wage to Singaporean employees who earn up to $4,000.
(ii) Employer made CPF contributions for at least 3 months in the year of the wage increase for these employees.
(iii) Employees who received the wage increase must have received CPF contributions for at least three months from one employer in the preceding year.

Employers on the exclusion list are as follows:

(a) Local government agencies, including organs of state, ministries and departments, statutory boards
(b) Government and government-aided schools
(c) People's Association services and grassroots units
(d) High Commissions, embassies, trade offices, consulates
(e) Unregistered foreign entities
(f) Foreign military units
(g) Representative offices of foreign companies, foreign government agencies, foreign trade associations/ foreign chambers/ foreign non-profit organisations
(h) Entities which pay CPF but are not registered in Singapore.

Who are the eligible employees under WCS?

Eligible employees are Singaporean employees who earn less than $4,000 gross monthly wages and receive employer CPF contributions.

There is no age cap for coverage under WCS. Employees may work on a full-time or part-time basis, or are permanent or contract staff.

The following individuals, however, do not qualify as employees under WCS:

- Sole proprietors and partners (i.e. of general partnerships/ limited liability partnerships/ limited partnerships)
- Employees who are also shareholders and directors (as defined in the Companies Act) of the employer company
- Self-employed individuals (including commission agents, taxi-drivers, owners of professional practices).

Accounting for wage credit scheme

The wage credit is a transfer of resources from the government to entities in return for meeting stipulated conditions relating to their operating activities. This wage credit falls within the scope of FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance*.

Under FRS 20, the wage credit is recognised as a government grant when there is reasonable assurance that the conditions under the WCS will be complied with, and that the amount will be received.

This will generally be the case if the employer is eligible for WCS and has remunerated eligible employees during the calendar year.

How should Company X account for the wage credit in its annual financial statements for the year ending 31 December 2013?

Illustrative Example – Accounting for wage credit in the annual financial statements for the year ending 31 December 2013

As at 31 December 2013, Company X would have met all qualifying conditions for its 2013 wage credit. Hence, there will be reasonable assurance that it will receive the $720 wage credit in March 2014. Accordingly, as at 31 December 2013, Company X will record the following in respect of the 2013 wage credit:

Dr Government grant receivable $720
  Cr Other income or staff costs $720*

** Assuming Company X recognises all staff costs as expenses when incurred.*

Company X does not record the 2014 wage credit in its 31 December 2013 financial statements because it is unlikely for there to be reasonable assurance that the conditions under WCS will be complied with as the employee has not rendered any services and may resign from Company X in 2014.

How should Company X account for the wage credit in its interim financial statements for the period ended 30 September 2013?

Illustrative Example – Accounting for wage credit in the interim financial statements for the period ended 30 September 2013

When preparing its interim financial statements, Company X has to exercise judgement when assessing whether there is reasonable assurance that the qualifying conditions will be met.

In applying the judgement, the approaches mentioned below may be applied. The chosen approach should be applied consistently to similar facts and circumstances from period to period.

Table 1

	2012	2013 - Approach 1	2013 – Approach 2
Number of months on Company X's payroll **(A)**	12	9	9
Basic monthly wage **(B)**	$1,000	$1,100	$1,100
Monthly food allowance **(C)**	$100	$100	$100
Annual (or pro-rated) bonus paid/payable in December **(D)**	$2,400	-	$2,250
Total wages **(E) = (B+C)*A+D**	$13,440	$10,800	$13,050
Employee's gross monthly wage **E / A**	**$1,300**	**$1,200**	**$1,450**

Approach 1

Company X assesses monthly wage increase based on actual wages paid during the period ended 30 September 2013. Based on actual wages paid, the gross monthly wage for 2013 year-to-date will be $1,200 compared to the gross monthly wage for 2012 of $1,300 (see Table 1).

As there is no actual monthly wage increase as at 30 September 2013, Company X considers that there is no reasonable assurance that it can comply with the qualifying criteria since it is not reasonably assured that the employee will continue employment with Company X until December 2013 (when the bonus is paid). Company X hence does not recognise any government grant receivable as at 30 September 2013.

Approach 2

Company X assesses monthly wage increase based on accrued wages during the period ended 30 September 2013. Based on accrued wages, the gross monthly wage as at 30 September 2013 will be $1,450, assuming bonus of $3,000 is recognised as pro-rated (see Table 1). Compared to the gross monthly wage for 2012 of $1,300, there is an accrued gross monthly wage increase of $150 as at 30 September 2013.

Consistent with its basis for accruing pro-rated bonus as at 30 September 2013, Company X considers there to be reasonable assurance the employee will continue employment with Company X until December 2013 (when the bonus is paid).

Hence, Company X recognises government grant receivable as at 30 September 2013, as follows:

Dr Government grant receivable $540 (40%*$150*9 months)
Cr Other income or staff costs $540*

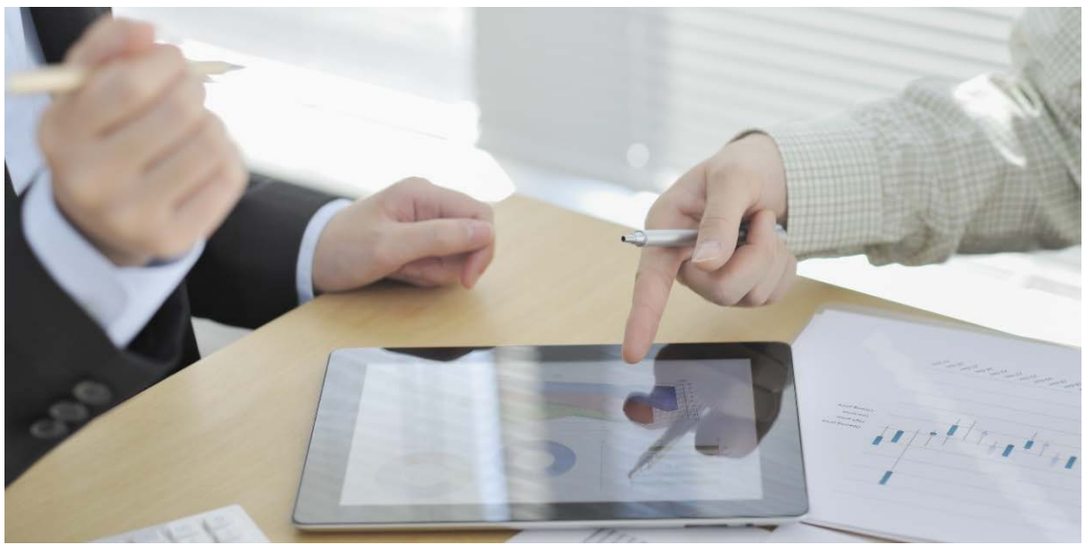
** Assuming Company X recognises all staff costs as expenses when incurred.*

When to recognise the wage credit in profit or loss?

Government grants shall be recognised in profit or loss on a systematic basis over the periods for which the entity recognises as expenses, the related costs the grants are intended to compensate. In the above example, the grants are recognised immediately in profit or loss as they relate to expenses already incurred.

To the extent that the staff costs have been capitalised as part of an asset (other than assets measured at fair value with changes therein recognised in profit or loss), the related wage credit should be deferred and recognised in profit or loss as the asset is depreciated or amortised or when the asset is derecognised.

For assets measured at fair value less costs to sell and for other assets measured at fair value with changes therein recognised in profit or loss, the wage credit should be recognised in profit or loss only when the conditions under WCS are fulfilled.



How do you present the wage credit in the financial statements?

Where the staff costs are recognised in profit or loss as incurred, the wage credit can be presented as a reduction of staff costs or as other income. The presentation format, once chosen, has to be applied consistently to similar government grants.

Where the staff costs have been capitalised as part of an asset (other than assets measured at fair value with changes therein recognised in profit or loss), the following two approaches are acceptable. The presentation format, once chosen, has to be applied consistently to similar government grants.

Approach 1: Gross presentation

Under this approach, the wage credit is initially recognised in the statement of financial position as deferred income, and subsequently amortised to profit or loss over the useful life of the asset. The entity chooses an accounting policy, to present such grants either as other income or as a reduction in the related expense. This policy has to be applied consistently.

Approach 2: Net presentation

Under this approach, the wage credit is initially deducted against the carrying amount of the asset. This results in reduction in depreciation or amortisation expense over the useful life of the asset.

Is the wage credit taxable?

The wage credit is taxable in the hands of the employers.

From the accounting perspective, employers will have to recognise any associated income taxes payable when the wage credit is recognised.

4. International developments

Unique opportunity to shape the future

In the aftermath of the global financial crisis, there has been much discussion about whether global accounting standards are still fit for purpose.

On 18 July 2013, the IASB published a discussion paper in response to long-standing calls to review its Conceptual Framework which is essential to developing high-quality, principles-based standards. The calls for review came amidst more recent concerns such as the growing complexity in financial reporting.

While it may not have the immediacy of other proposals, the consultation will have a long-term influence on the direction of accounting. It will help shape the fundamental principles for developing robust and consistent global standards.

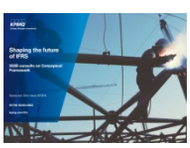
The consultation focuses on some fundamental questions, which the IASB believes have created challenges in setting standards, including:

- What is an asset and what is a liability?
- When should they be recorded on or taken off the balance sheet?
- How should they be measured?
- Should an item of income or expense be recorded above or below the bottom line?

This is an opportunity for stakeholders from every part of the financial reporting chain to offer their views to the IASB.

Comments are due to the IASB by 14 January 2014, and the comment period for the ASC ends on 1 November 2013.

For details, refer to:



In the Headlines – Sep 2013: Shaping the future of IFRS

> "This IASB consultation is timely (as it) addresses concerns that have been expressed about the IFRS in recent times, including the growing complexity in financial reporting. Questions have also been raised about fundamental issues such as the stewardship role of financial statements, the extent of fair value accounting in IFRS and what 'performance' actually means. It is vital that stakeholders from every part of the financial reporting chain around the world provide input to the IASB. We must not miss this opportunity."
>
> Mark Vaessen
> Global IFRS Network Leader and Partner at KPMG in the UK

Enhancing the value of auditor reporting

For some time now, users of financial statements have been calling for the auditor's report to include insights gained during the audit of financial statements.

In the December 2012 issue of FRM, we discussed how key proposals in the IAASB's report *Invitation to Comment: Improving the Auditors' Report (ITC)*, published on 22 June 2012, affect the interactions between the preparers of financial statements and their auditors.

For details, refer to:

In the Headlines – July 2013: Enhancing the value of auditor reporting

Following the ITC and other public consultations as well as stakeholder outreach and international research, the IAASB released an exposure draft on 25 July 2013. The IAASB's aim is to significantly expand the content of the auditor's report, beyond a simple pass/fail assessment, so that it provides information about the audit to users.

The exposure draft includes a new proposed International Standard on Auditing (ISA) titled *Communicating Key Audit Matters in the Independent Auditor's Report*. This proposed ISA directs auditors of financial statements of listed entities to communicate in their report those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements.

Among other enhancements, the IAASB has also proposed that auditors include specific statements about going concern in their reports and to make an explicit statement about the auditor's independence from the audited entity. In addition, the name of the engagement partner must be disclosed in the auditor's report. The exposure draft includes example reports that illustrate the application of the proposed new and revised ISAs under various circumstances.

Comments are due to the IAASB by 22 November 2013.

> "We expect (that) the proposed new and revised standards will result in substantive changes to how auditors contemplate and approach communication to users of their reports — the beneficiaries of a financial statement audit. These changes are critical to the perceived value of the financial statement audit and thus to the continued relevance of the auditing profession."
>
> Prof. Arnold Schilder
> Chairman of the IAASB

The IASB completes post-implementation review of IFRS 8 *Operating Segments*

The IASB announced the completion of its post-implementation review of IFRS 8 *Operating Segments*.

The review finds the Standard to be generally functioning as anticipated. The limited areas where further investigation is warranted will be subject to liaison with the FASB, and will be considered within the context of the convergence with US GAAP achieved by IFRS 8.

Areas for potential improvements and amendments include:

- the concept and identification of a chief operating decision maker (CODM);
- application guidance on reconciliations required in the standard;
- disclosures when there are changes to basis of segmentation;
- additional disclosures of certain defined line items to allow investors to calculate their own sub-totals for operating results or cash flows;
- additional guidance for aggregating operating segments; and
- segment by segment reconciliations.

> "Post-implementation reviews are an important step in our due process as they provide a mechanism to make sure our Standards are working as intended. This first review shows us that overall IFRS 8 achieved its objectives, although the report has highlighted some areas to the IASB where further targeted improvements could be made."
>
> Hans Hoogervorst
> Chairman of the IASB

The IASB begins the post-implementation review of IFRS 3 *Business Combinations*

The IASB has begun its post-implementation review of IFRS 3 *Business Combinations*. The IASB has confirmed that this post-implementation review will look at the changes introduced in 2004 and 2008, including changes to the presentation of consolidated financial statements that were made at the same time.

The review will be carried out in two phases. In Phase I, the IASB will undertake targeted outreach to identify areas where entities encountered implementation problems or unexpected costs with IFRS 3. It will also review academic and other studies about the application of the Standard. The issues identified during this phase will be included in a Request for Information (RFI), which will be published for public comment. In Phase II, the IASB will undertake extensive outreach and analyse the public comments received in response to the RFI. The aim is to learn about experiences in applying the Standard and how investors and others use the results it produces. At the end of the post-implementation review, the IASB will publish a Feedback Statement with the main findings and the steps it plans to take, if any, as a result of the review.

> "We remain committed to undertaking post-implementation reviews of new Standards and major amendments to ensure they are working as intended. We want to make sure that IFRS 3 is being implemented on a consistent basis and to understand any unintended consequences arising from its introduction."
>
> Hans Hoogervorst
> Chairman of the IASB

Collecting their thoughts

The IASB and the FASB are working to finalise a new revenue standard for publication later this year. In July 2013, they discussed some key application issues identified during the drafting process. These include the implications of doubts about collectability and the application of the revenue constraint to the measurement of revenue. The Boards reaffirmed their previous decisions in these areas, each of which will require entities to exercise significant judgement.

In preparation for the launch of the new revenue standard, the Boards announced the formation of a joint transition resource group. This group will be responsible for identifying interpretative issues as entities work to implement the new requirements.

> "The Boards reaffirmed areas that would require a significant amount of judgement to apply the new revenue standard and announced plans for a new group that will identify interpretative issues."
>
> Phil Dowad
> Global IFRS Revenue Recognition Leader and Partner at KPMG Canada

For details, refer to

IFRS Newsletter – Revenue Issue 10

Some welcome relief for banks, but implementation challenges ahead

The banking industry recently welcomed two developments in hedge accounting. The first is the IASB's provision of a limited-scope relief for a widespread issue resulting from derivative novations. The second is the decision to allow an accounting policy choice over which general hedging model to use once IFRS 9 *Financial Instruments* becomes effective.

However, with only months left before issuing their first financial statements under IFRS 13 *Fair Value Measurement*, banks face a number of implementation challenges. The magnitude of these challenges are largely dependent on a bank's existing approach under IAS 39/IFRS 9, the nature of the business and the financial instruments held. It will be important for banks to monitor evolving practice in complicated areas and areas with only limited guidance available.

Meanwhile, high on the agenda for many banks, is the need to identify crossovers and synergies between the IASB's proposals on expected credit losses and the credit risk parameters in the Basel capital framework.

For details, refer to

IFRS Newsletter – Banking Issue 10

> "With only months to go before issuing their first annual reports under IFRS 13, banks will need to address implementation issues, particularly in areas where there is limited guidance or where industry practice is still developing."
>
> Mahesh Narayanasami
> Partner, Advisory Services, KPMG in Canada

Going forward – Progress made in financial instruments projects

The September 2013 meetings proved productive for the IASB's and FASB's financial instruments projects, as the Boards reached a number of decisions on classification and measurement, and the impairment of financial assets.

The IASB made progress in refining the contractual cash flows assessment for financial assets, although some differences of view with the FASB emerged. The Boards reached tentative decisions on the meanings of 'principal' and 'interest', contingent features, and prepayment and extension features.

The IASB also moved forward with clarifications to its proposed impairment model, reaching tentative decisions on assessing increases in credit risk and the definition of 'default'. It also agreed to look at future possibilities for convergence with the FASB.

KPMG IFRS Newsletter, "Financial Instruments", highlights IASB discussions in September 2013 on the financial instruments (IAS 39 replacement) project, and key project milestones and timeline for completion.

For details, refer to

IFRS Newsletter – Financial Instruments Issue 15

> "The IASB made progress in refining the contractual cash flows assessment for financial assets, but some differences of view with the FASB emerged. The IASB also moved forward with clarifications to its proposed impairment model."
>
> Andrew Vials
> Global IFRS Financial Instruments Leader and Partner at KPMG in the UK

Leases proposals – Assessing the impact on banks

For details, refer to

New on the Horizon – Leases for banks

Major changes to lease accounting proposed by the IASB and the FASB in May 2013 were big news for the banking sector.

While it is apparent that the proposals may have significant implications in some areas – particularly compliance with capital and other regulatory requirements – it remains unclear how banks would apply certain aspects of the proposals.

KPMG report, Leases for Banks, looks at the potential impact of the revised proposals on banks, discusses whether previous concerns expressed by banks have been addressed and highlights new issues relevant to banks.

Highlights:

- The new lease accounting proposals may have a significant impact on a bank's compliance with capital and other regulatory requirements.
- The proposed dual model and new lease classification test may impede comparability.
- The proposals may affect the covenant arrangements of customers with significant lease commitments, and the complexity of the proposals could impact leasing business in general.
- The exclusion of some sale and leaseback transactions from the lease proposals could increase volatility in profit or loss.
- The future tax treatment of leases is uncertain in some jurisdictions as tax authorities consider the proposals.

> "The revised lease proposals will affect banks in their capacity as lessees and in their capacity as lessors. Banks will also need to assess the effect of the proposals on their customers. The impacts could be far-reaching."
>
> Colin Martin
> Partner, Banking Accounting Advisory Services, KPMG in the UK

A new world for insurance

For details, refer to

New on the Horizon – Insurance contracts

The IASB and the FASB issued their exposure drafts on insurance contracts in June 2013, marking a major step forward in the implementation of a common insurance reporting framework across much of the world.

The proposals apply to all insurance contracts, including certain financial guarantees rather than insurance entities, and to investment contracts with a discretionary participation feature issued by insurance companies.

The exposure drafts introduce a revised current value measurement model which would go some of the way towards addressing concerns over increased volatility in profit or loss. They also introduce a new presentation approach which would significantly change the way insurers – especially life insurers – report performance.

The proposals are likely to have a profound impact across an organisation, affecting asset-liability management and decisions over product design, features and pricing. Capital management and regulatory requirements may also be affected in some jurisdictions. The new data collection and retention requirements could necessitate systems upgrades, increased demand for resources and additional training.

Comments are due to the IASB and the FASB by 25 October 2013.

> "This looks set to be the biggest ever financial reporting change for most insurers. The extent of change would be far-reaching, and there is no question that insurers' financial statements would look very different compared to today. If insurers start planning now, the wave of change could open up opportunities for synergies in areas such as data collection, modelling capability and investment in systems and resources. The bottom line is that the technical aspects of the proposals would need to be made operational."
>
> Lau Kam Yuen
> Head of Insurance Practice and Partner at KPMG in Singapore

Common abbreviations

ASC	Accounting Standards Council in Singapore
ACRA	Accounting and Corporate Regulatory Authority
CPF	Central Provident Fund
DP	Discussion Paper
ED	Exposure Draft
FASB	U.S. Financial Accounting Standards Board
FSP	FASB Staff Position
FRS	Singapore Financial Reporting Standard
GAAP	Generally Accepted Accounting Principles
IAS	International Accounting Standard
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
ISCA	Institute of Singapore Chartered Accountants
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard
INT FRS	Interpretation of Financial Reporting Standard
IRAS	Inland Revenue Authority of Singapore
LM	Listing Manual of the Singapore Exchange
MAS	Monetary Authority of Singapore
MOF	Ministry of Finance
PCAOB	Public Company Accounting Oversight Board
REIT	Real Estate Investment Trust
SGX	Singapore Exchange
XBRL	eXtensible Business Reporting Language

Note: All values in this publication are in Singapore Dollars, unless otherwise stated.

Contact us

Reinhard Klemmer
Partner, Professional Practice
T: +65 6213 2333
E: rklemmer2@kpmg.com.sg

KPMG LLP
16 Raffles Quay #22-00
Hong Leong Building
Singapore 048581
T: +65 6213 3388
F: +65 6225 0984

kpmg.com.sg