KPMG
cutting through complexity

FINANCIAL REPORTING MATTERS

MARCH 2015 ISSUE 50 | MICA (P) 117/11/2014

Less than a year after publishing their joint standard on revenue recognition, the International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) are back in standard-setting mode. In their February and March 2015 meetings, the Boards agreed to propose changes to the new standard and in different ways. Find out more about what the decisions could mean for you in this issue.

Credit adjustment for the valuation of derivatives is an area of increasing focus, and most entities do not recognise or calculate these adjustments correctly. In this issue, we highlight the key factors to consider when determining whether credit adjustments are relevant.

Under the Financial Reporting Surveillance Programme (FRSP), the Accounting and Corporate Regulatory Authority (ACRA) has released a Practice Guidance to highlight its areas of review focus for FY2014 financial statements. ACRA's focus areas reflect a number of new Financing Reporting Standards (FRS) and amendments that have come into effect in 2014. ACRA also highlighted significant areas of concerns gathered from the first round of review of the FY 2013 financial statements. What should a director do on receipt of an enquiry letter from ACRA? Which companies are more likely to be selected for review? Read this issue to find out.

Singapore Budget 2015 focuses on building Singapore's future, and takes major steps in four areas – developing our people, investing in innovation and internationalisation, investing in economic and social infrastructure, and strengthening assurance in retirement. In this issue, we give an overview of the key changes in tax measures that affect businesses.

Last but not least, we bring you a roundup of the latest accounting developments on the international front.

Contents

1. IFRS 15 version 1.1?

This article is contributed by:

Reinhard Klemmer
Head of Professional Practice

Chan Yen San
Senior Manager, Professional Practice

In February and March 2015, the IASB and the FASB (the Boards) decided to amend the new revenue standard, IFRS 15/ASC Topic 606 *Revenue from Contracts with Customers*. This decision comes less than a year after the Boards first published the new revenue standard in May 2014.

The Boards have also diverged in their approach with respect to the amendments, each proposing to make different changes to the IFRS and US versions of the standard, with the FASB making more extensive and more detailed changes than the IASB. The FASB has also proposed a number of other amendments that the IASB has decided are not necessary.

In addition, the FASB voted on 1 April 2015 to propose a deferral of the effective date – which is currently 1 January 2017, by one year. The IASB has not made an announcement regarding any decisions to postpone the mandatory effective date. This development clearly confirms that significant time and effort beyond a period of 3 years might be necessary for some companies to properly implement the standard.

Here is how the story goes

The joint Transition Resource Group for Revenue Recognition (TRG) was set up by the Boards at the same time the new standard was published. The TRG's members include auditors, financial statement preparers and users with knowledge and experience of revenue recognition under US GAAP and/or IFRS from various industries and geographies.

The primary focus areas of the TRG are to:

- *solicit, analyse and discuss stakeholder issues arising from implementation of the new standards*

  The TRG will discuss implementation issues about the new revenue standards that are submitted by stakeholders if they give rise to a risk of diversity in practice and are pervasive (i.e. relevant to a wide group of stakeholders). The identity of stakeholders who submit issues will not be made public.

- *inform the Boards about issues arising from the implementation of the new standards,, which will help the Boards determine what, if any, action will be needed to address those issues*:

  The TRG will not issue guidance since it is not empowered to do so under the Boards' due process requirements. However, the TRG may refer an issue to the Boards for clarification if it thinks the guidance in IFRS 15/ASC Topic 606 is unclear, or may recommend that educational material be developed. The Boards will determine what action, if any, will be taken on each issue.

- *provide a public forum for stakeholders to learn about the new standards from others involved with implementation*

  As a resource to stakeholders, agenda items and recordings of TRG meetings will be posted on the Board's website. Additionally, the staff will maintain a log of all submitted issues along with a description of how the issue was addressed. These logs will be made publicly available.

The TRG has met four times – in July 2014, October 2014, January 2015 and March 2015 – and is expected to meet four times annually until 2017 or 2018.

Discussions within the TRG have indicated that stakeholders should be able to understand and apply the new standard. However, in some cases, the discussions have identified potential diversity in practice and these issues were referred to the Boards.

What are the decisions made by the Boards?

The Boards met in February and March 2015 to discuss how to address the issues referred to them by the TRG. The Boards agreed to propose amendments in the following areas:

February's Decisions at a Glance

What is the issue?	IASB decisions	FASB decisions
Licences		
How to determine the nature of an entity's promise in granting a licence?	Clarify the application of the existing criteria for assessing whether licence revenue is recognised over time or at a point in time.	Recharacterise the nature of licences as either functional intellectual property (point-in-time recognition) or symbolic intellectual property (over time recognition).
When does the exception for sales- and usage-based royalties apply?	Clarify that the exception applies whenever the licence is the predominant item to which the royalty relates, and that a single royalty stream should not be split for accounting purposes.	
Does the licences guidance apply when the licence is not distinct?	No action to be taken.	Clarify that in some cases when a licence is not distinct an entity will need to determine its nature in order to appropriately apply the general revenue recognition requirements.
How do contractual restrictions impact the identification of promises?	No action to be taken.	Clarify that contractual restrictions are attributes of the licence and do not affect the identification of the number of promises in the contract.
Identifying performance obligations		
When is a promised good or service 'distinct within the context of the contract'?	Add examples to illustrate the application of the separation guidance.	Add examples to illustrate the application of the separation guidance. Re-articulate the principle of 'separately identifiable'. Align the indicative factors with the re-articulation of separately identifiable.
How to identify promised goods or services?	No action to be taken.	Clarify that materiality is assessed at the contract level when identifying separate performance obligations in the contract.
Should shipping and handling services be accounted for as a promised service?	Perform outreach activities.	Clarify that shipping and handling activities before the transfer of control are fulfillment activities. Add a policy election that allows an entity to consider shipping and handling activities after the transfer of control as fulfillment costs.

For more details, you can download the following publication:

IFRS Newsletter: Revenue – Symbolic Divergence

March Decisions at a Glance

What's the issue?	IASB decisions	FASB decisions
Principal-agent considerations		
How should a company assess whether it is a principal or an agent?	Conduct further research into principal-agent issues to provide clarification on the application of the control principle.	
Presentation of sales taxes		
How should a company present sales taxes?	No action to be taken.	Add a practical expedient under which a company can elect an accounting policy to present sales taxes net.
Collectibility considerations		
How should a company assess collectibility when determining whether a contract exists?	Conduct further research.	Amend the new standard to clarify how to assess collectibility and the meaning of contract termination.
Non-cash consideration		
What is the measurement date for non-cash consideration?	No action to be taken.	Clarify that the fair value of non-cash considerations are measured at the contract inception date.
How is the variable consideration guidance applied to contracts that include non-cash consideration?	No action to be taken.	Clarify that the variable consideration guidance only applies to variability resulting from factors other than the form of the consideration.
Transition to the new standard		
Should further practical expedients be added to the transition options?	Add a practical expedient for contracts that are modified before the date of initial application.	
	Permit companies not to apply the new standard to contracts completed under legacy GAAP when applying the new standard retrospectively.	No action to be taken.
	No action to be taken – exemption already exists under IFRS.	Exempt companies from certain disclosures in the year of adoption of the new standard.

For more details, you can download the following publication:

IFRS Newsletter: Revenue – Problems with principals

In summary

The proposed changes will be released by each Board for public comment. The IASB indicated that it will consider additional changes that may arise at future TRG and Board meetings and release a single exposure draft for comment. However, the FASB is expected to issue an exposure draft on its current proposals shortly. The IASB expects to approve an Exposure Draft at its June 2015 meeting.

With the FASB's tentative decision to postpone the mandatory effective date by one year, the IASB will be under pressure to consider a similar move.

In Singapore, the new standard on revenue recognition was issued as FRS 115 in November 2014. The Accounting Standards Council (ASC) is expected to amend FRS 115 to incorporate changes to IFRS 15 introduced by the IASB including any postponement of the mandatory effective date.

To find out more about the new revenue standard, you can download the following publications:

In the Headlines – May 2014: Revenue a new global standard

First Impressions: Revenue from contracts with customers

Transition to the new revenue standard
What is the best transition option for your business

Issues in-Depth: Revenue from contracts with customers

Impacts on the construction industry of the new revenue standard

Accounting for revenue is changing – Impact on telecommunication companies

New revenue standard - Assessing the impact for power and utilities companies

Accounting for revenue is changing – impact on oil and gas companies

2. Have you factored CVA/DVA into the fair value of derivatives?

This article is contributed by:

Reinhard Klemmer
Head of Professional Practice

Varghese Anthony
Senior Manager, Professional Practice

Many companies frequently utilise derivative financial instruments such as cross-currency swaps, foreign exchange forward contracts and interest rate swaps to hedge exposures to financial risks. These instruments are required by accounting standards to be carried at fair value at each reporting date.

These companies may not always have the necessary expertise when it comes to valuation of derivative financial instruments and are often reliant on the banking counterparty to the transaction to provide the valuation for financial reporting purposes. However, the valuation provided by the banking counterparty rarely incorporates adjustments for credit risks. Such adjustments are required by the accounting standard, FRS 113 *Fair Value Measurements*.

Companies should assess the significance of the valuation adjustments for derivative financial instruments that reflect the banking counterparty's credit risk – i.e. credit valuation adjustment (CVA) – and their own credit risk – i.e. debit valuation adjustment (DVA).

How should companies address this issue? With a qualitative assessment, companies should be able to decide whether a full scale valuation exercise is necessary.

This article highlights some qualitative factors that can be used in an initial assessment to identify those derivative positions for which the potential impact of CVA/DVA on the valuation might be significant. For this group of derivatives, a separate valuation exercise should be performed to quantify the CVA/DVA.

The meaning of CVA and DVA

A feature of most derivatives is that they may change from being an asset to a liability or vice versa – e.g. an interest rate swap or a forward contract – because:

- there may be a mixture of expected net cash inflows and expected net cash outflows for different settlement dates; and
- the amount and direction of cash flows may vary as a result of changes in market underlyings.

Accordingly, an entity considers both its own credit risk and the counterparty's credit risk in the valuation of derivative instruments - if market participants would do so in measuring the fair value of these instruments (see why this is relevant in the next section). 'Credit risk' is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

A valuation adjustment for credit reflects the amount at which such risk is valued by a market participant. The concept behind such an adjustment is straightforward - a bank originating a derivative would distinguish between a credit 'risky' counterparty and a hypothetical credit 'risk-free' counterparty by charging the credit risky counterparty a spread for entering into the contract.

Similarly, if a bank was to sell an existing derivative asset to a market participant, then the market participant would, with other things being equal, pay less for a trade with a risky counterparty than for a trade with a riskless counterparty.

The valuation adjustments to reflect the two-way risk of loss for the counterparty and the reporting entity are commonly referred to as credit valuation adjustments– i.e. those reflecting the counterparty's credit risk – and debit valuation adjustments – i.e. those reflecting the reporting entity's own credit risk.

Although each may be relevant for both derivative assets and liabilities, CVA tends to be most significant for derivative assets and DVA for derivative liabilities. However, for some instruments, such as a purchased option, only one party – the investor in (or purchaser of) the instrument – is exposed to the credit risk of the issuer, as there is no other obligation for the purchaser of the option aside from paying the option premium, usually upfront.

Why does CVA/DVA need to be factored into the fair value of derivatives?

Under FRS 113, the fair value of a financial liability reflects the effect of 'non-performance risk', which is the risk that an entity will not fulfill an obligation. Non-performance risk includes an entity's own credit risk.

The fair value measurement for a liability is based on the price at which it would be transferred to a market participant – assuming that the non-performance risk, including the effect of the entity's own credit risk, remains the same before and after the transfer.

The non-performance risk from an investor's perspective is the CVA and the same risk from an issuer's perspective is the DVA.

In the absence of a quoted market price for the transfer of a liability – as would be the case for an over-the-counter derivative - the liability's fair value is measured from the perspective of a market participant that holds the liability as an asset. This would imply consistency between the calculation of own credit risk adjustments and counterparty credit risk adjustments in measuring derivative assets and liabilities.

Therefore, in principle, and assuming no differences in the unit of account, the credit risk adjustments made in the fair value measurement by both counterparties to the financial instrument should be the same.

The valuation of derivative financial instruments, particularly its credit elements, has been an area of focus for financial reporting since the financial crisis of 2008. Prior to the crisis, it was generally not industry practice to include such credit adjustments due to the presumption that it would be highly unlikely that counterparties would default. Since the crisis, credit risk management has evolved and the potentially significant implications on derivative valuations have generally been recognised.

Another financial reporting implication of these credit adjustments is on hedge accounting, as the effectiveness of the hedging relationship is directly impacted by credit adjustments on the designated hedging instrument – the fair value and the value used for effectiveness computation will be affected. For example, when assessing effectiveness using the hypothetical derivative method in a cash flow hedging relationship, the hypothetical derivative will not factor in the credit risk associated with the derivative hedging instrument counterparty. Therefore, any CVA/DVA in the valuation of the hedging instrument will impact the effectiveness of the hedging relationship.

From the above it is clear that CVA/DVA is a concept required by IFRS to be considered in the fair valuation of derivative financial instruments that could have material financial reporting implications, and therefore warrants regular assessments of the factors that could impact its potential significance.

Factors to consider in the assessment of significance of CVA/DVA

CVA/DVA for derivatives can be calculated for a transaction, single counterparty or portfolio of similar counterparties. But what are the factors that will have the largest impact on any CVA/DVA calculation?

An assessment of the factors below can be used to determine whether there might be a significant impact by CVA/DVA on the valuation of a derivatives portfolio:

Factors to assess	Description
Credit risk	The actual level of own or counterparty credit risk will impact the significance of the CVA/DVA. For example, the credit worthiness of the entity/counterparty represented by the credit ratings, credit spreads, probability of defaults (PDs), financial ratios etc. will directly impact the calculation of CVA/DVA.
Portfolio size	Typically, the larger the portfolio size – i.e. notional amounts and the number of outstanding instruments – the more potentially significant the impact of CVA/DVA on the fair value of the instruments.
Current fair value	Typically, the greater the fair value of the derivatives, the greater the credit risk and hence the credit adjustments in the fair value of the instruments.
Period to Maturity	The longer the duration, the more significant the impact of CVA/DVA on the fair value of the instruments. For example, a three year interest rate swap will have a much lower CVA/DVA compared to a ten year interest rate swap on account of tenor.
Collateral	Generally for a derivative transaction, the higher the level of collateral posted, the lower the level of credit risk adjustment needed.
Derivative netting arrangements	The legal right to set off positions directly impacts the credit exposure and therefore the credit adjustments. For example, the netting terms in a master netting agreement such as an ISDA agreement and an entity's legally enforceable right to set off positions will impact the net exposure.

As the above factors are primarily qualitative in nature, judgment will be required when concluding whether the overall expected impact of CVA/DVA on the valuation of a particular derivative position is material. Each individual relevant qualitative factor needs to be assessed and it is not appropriate to base the conclusion solely on the number of factors pointing in the same direction. If all of the factors point to CVA/DVA not likely to be material, a more detailed analysis will not be necessary.

But a more detailed assessment of these factors may be necessary for financial institutions given the scale and structural complexity of the derivative instruments held. However, most financial institutions would have already considered the impact of CVA and/or DVA particularly considering their potential regulatory implications. Financial institutions typically take the single counterparty or portfolio of single counterparties approach with the CVA/DVA adjustment taking into account:

- derivative netting arrangements;
- risk of future default; and
- collateral

However, in our experience, besides financial institutions, corporates may not always have the necessary expertise when it comes to valuation of derivative financial instruments.

If these companies rely on their banking counterparty on the transaction to provide input for financial reporting purposes, they may need to consider additional steps in order to achieve full compliance with FRS. In such situations, these factors need to be given a greater degree of consideration and external consultation might be helpful - if the conclusion is, based on the assessment, that the CVA/DVA may have a significant impact on the valuation of their derivative financial instruments.

3. Directors, be prepared for ACRA's FY 2014 Financial Reporting Surveillance Programme

This article is contributed by:

Ong Pang Thye
Partner, Head of Audit

Chan Yen San
Senior Manager, Professional Practice

Under the Financial Reporting Surveillance Programme (FRSP), ACRA has released a Practice Guidance to highlight its areas of review focus for FY2014 financial statements. ACRA's focus areas reflect a number of new FRSs and amendments that have come into effect in 2014. They also highlight significant areas of concerns gathered from the first round of review of the FY 2013 financial statements.

What is the Financial Reporting Surveillance Programme?

The FRSP was introduced in 2011 as part of ACRA efforts to ensure that the capital market remains confident in the integrity, transparency and quality of corporate financial reporting.

Under the FRSP, ACRA reviews the financial statements of selected companies for compliance with Singapore Financial Reporting Standards (SFRS). This programme is assisted by a panel of about 30 experienced accounting practitioners from the Institute of Singapore Chartered Accountants (ISCA) under a collaborative arrangement between ACRA and ISCA. Where the reviewers identify any potential non-compliance with SFRS, enquiry letters are sent to the directors to seek clarifications.

What are the areas of review focus for the FY 2014 financial statements that companies' directors can expect?

Annually, ACRA releases a Practice Guidance to highlight its areas of review focus for the year.

This year, ACRA's focus areas reflect a number of new FRSs and amendments that have come into effect in 2014. They also highlight significant areas of concerns gathered from the first round of review of the FY 2013 financial statements.

Directors should therefore pay closer attention to the review focus areas identified by ACRA when authorising the FY 2014 financial statements.

Areas of review focus	Specific points identified by ACRA that directors should consider
1. New consolidation suite of standards	• Application of the control principle • Identification of joint venture and joint operation • Disclosure of the reasons and financial statements effects of the changes in accounting • New disclosures such as summarised financial information of each subsidiary with non-controlling interests that are material to the Group, and of each material associate and joint venture
2. Business acquisitions	• Challenging whether material goodwill arose because the company overpaid for the acquisition or part of the goodwill is attributed to intangible assets (such as know-how, licenses and customer lists) that should be separately recognised • Classification of contingent share consideration (e.g. earn-out shares) as equity or liability
3. Statement of cash flows (SoCF)	• Checking that foreign currency translation reserves arising from translating the financial statements of foreign operations are not included in the SoCF as non-cash adjustments to profits (because these are taken to equity) • Checking that cash flows are appropriately classified into operating, investing and financing based on the underlying nature. For example, inter-company borrowings and deposits placed to acquire investments are likely cash flows from financing/ investing activities
4. Long-life asset value and impairment testing	• Assessing critically management's impairment testing (especially for listed companies whose market capitalisation has fallen significantly below net asset value) and related disclosures
5. Earnings per share (EPS)	• Checking that: (a) the comparative basic and diluted EPS are adjusted to reflect any bonus shares or rights issued during the year; (b) the diluted EPS is adjusted for the effects of all dilutive potential ordinary shares such as share options and contingent share consideration; and (c) ordinary shares issued to pay for business acquisition are included in the weighted average number of shares from the acquisition date.
6. Operating segment	• Questioning if segments identified in the financial statements are inconsistent with those included in the Management Discussion and Analysis sections of the annual report • Obtaining management's clear rationale on aggregating segments, especially those with dissimilar economic characteristics
7. Fair value measurement	• Questioning the basis for categorising the fair value of investment properties and biological assets as Level 2, as the valuation for these assets typically involves many significant unobservable inputs • Ensuring adequate disclosures for fair value measurements under Level 3 with meaningful level of aggregation

Which companies are more likely to be selected for review?

Some companies are more likely to be picked than others. ACRA has designed a risk-based approach in determining the companies to select for review of the financial statements. They will place priority on public and large private companies with:

(a) modified audit opinions as well as audit opinions with emphasis of matter paragraphs, indicating potential non-compliance with Accounting Standards and other requirements of the Act;

(b) significant public interest risks;

(c) operations that require subjective judgement in accounting for its transactions, hence increasing the risk of material misstatement;

(d) changes in listing or trading status (e.g. newly listed, suspended or delisted);

(e) significant changes in key stakeholders including controlling shareholders, directors, management and auditors; and

(f) industries susceptible to accounting changes during the year.

Nevertheless, ACRA may select companies on the basis of other criteria including random sampling.

What should a director do upon receipt of ACRA's enquiry letter?

ACRA expects companies to respond to the queries within three weeks from the date of the enquiry letter. The drafting of responses should start immediately as the turnaround time given by ACRA is relatively short (3 weeks from the date of the letter) and certain information and documents may need to be gathered for submission.

The directors should therefore ensure that management actively supervises the drafting of the responses and that the Company's auditors are notified right away.

Once the responses are drafted, the directors should review the draft responses to ensure that they are comprehensive and adequate. The directors may have to meet the management and the auditors where necessary to understand the issues and discuss the responses.

When reviewing the responses, directors should focus on ensuring that responses adequately explain how the company's accounting and disclosures have complied with the accounting standards. In cases where non-compliances or omissions are based on grounds of immateriality, it is important that the directors understand how materiality has been assessed by the management and that the responses clearly explain the company's basis for evaluating materiality.

Directors should be aware that incomplete or unclear responses, or responses that fail to adequately explain how the company's accounting has complied with the provisions in the accounting standards often lead to follow up letters from ACRA. If the financial reporting breach is very severe, ACRA may request for a physical interview.

Directors should treat this exercise as an opportunity to review and improve the quality of the financial statements of companies under their care. If any deficiencies in the accounting practices or disclosures are identified during the process, steps should be taken to correct the accounting or to enhance the disclosures.

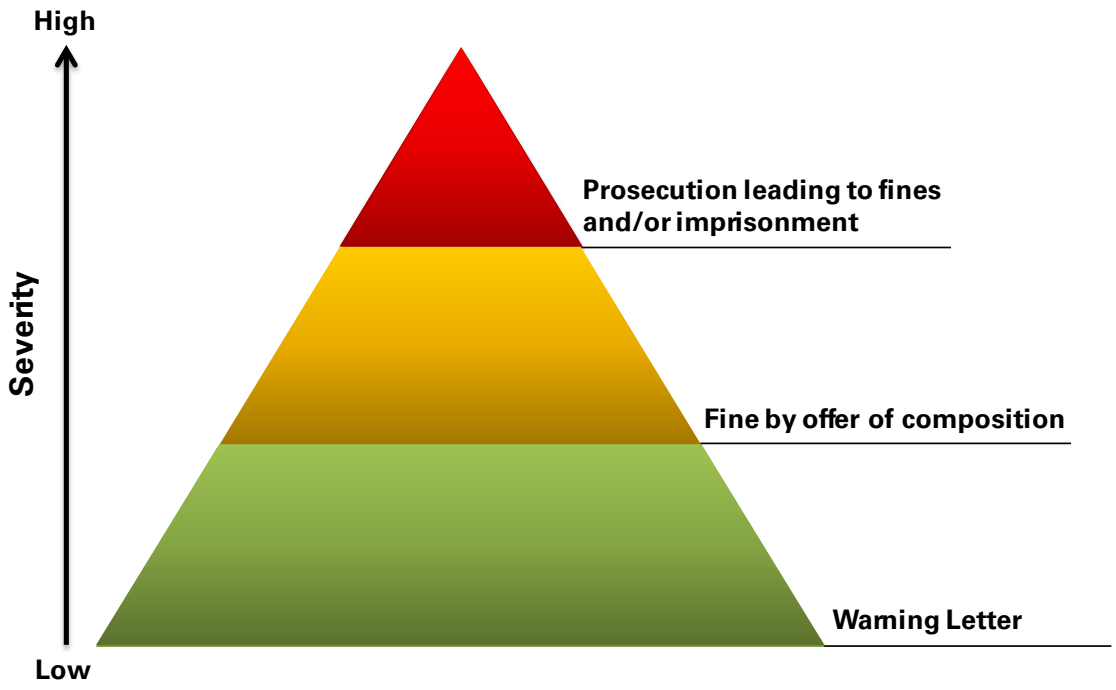
The root causes (e.g. time constraints, lack of skilled resources) for the deficiencies should also be identified so that remedial steps can be taken to prevent future occurrences. Facts discovered during the enquiry may also prompt the need to comprehensively review the accounting practices and disclosures to identify gaps where improvements may be necessary. Engaging an outside accounting expert to provide an independent gap analysis can often be very useful in helping companies identify their blind spots.

What happens when a financial reporting breach is identified?

The enforcement actions that may be taken by ACRA will depend on the severity of the breach.

When the financial reporting breach is considered less serious, ACRA will typically issue a letter advising the company and the directors to make improvements to address the identified financial reporting weaknesses in their future financial statements. This will take in the form of an Advisory letter and is not a regulatory sanction.

When the financial reporting breach is considered more serious, ACRA has the power to impose a range of regulatory sanctions on each individual director who authorised the financial statements based on its assessment of the severity of the breach.



The issuance of a warning letter is considered the least severe of the range of regulatory sanctions. If the financial reporting breach is considered more severe, ACRA may offer to compound the offence by imposing a fine on the directors. In the extreme scenario where the financial reporting breach is considered very severe, ACRA may prosecute the directors which could lead to fines and/or jail sentences.

Directors of listed companies should also take note that if they have been imposed with regulatory sanctions, the listed companies under their care may have to make the necessary announcement if it is considered material information - which is likely to materially affect the share price under the SGX Listing Rules.

Additionally, under the SGX Listing Rules, the director must also declare that he/ she has been subject to regulatory sanctions by the regulatory authority, ACRA, at his next appointment as a director of a listed company.

Directors may find the following guides useful:

- Financial Reporting Practice Guidance No.1 of 2015
Areas of review focus for FY2014 financial statements under the FRSP administered by ACRA.

- Practice Direction No.2 of 2014
Directors' duties in relation to financial reporting and review and sanction process of the FRSP administered by ACRA.

- ACRA & I: Being an effective director
Guidebook sharing experiences, knowledge and practices of audit committee members on corporate governance practices.

- Issue 47 of KPMG Financial Reporting Matters June 2014
Financial Reporting Surveillance Programme Targets Company Directors

- Issue 49 of KPMG Financial Reporting Matters December 2014
Top 5 issues to consider this year-end.

For more timely and topical information to assist in improving your audit committee and financial reporting process, you can refer to our KPMG Audit Committee Institute website.

4. Highlights of Budget 2015 – Tax Measures for Businesses

This article is contributed by:

Chiu Wu Hong
Partner, Corporate Tax

Reinhard Klemmer
Head of Professional Practice

Han Swee Peng
Senior Manager, Corporate Tax

Chua Yun Leng
Senior Manager, Professional Practice

On 23 February 2015, the Deputy Prime Minister and Minister for Finance delivered the Budget Statement. Budget 2015 focuses on building Singapore's future, and takes major steps in four areas – developing our people, investing in innovation and internationalisation, investing in economic and social infrastructure, and strengthening assurance in retirement.

In this section, we provide an overview of the key changes in tax measures that affect businesses.

From the accounting perspective, you should consider these tax changes when computing the amount of current and deferred taxes if your reporting period ends after 23 February 2015.

> "This year's Budget, at the mid-point of our economic restructuring, was an opportune time to take stock of the progress of our productivity and innovation initiatives. We are especially heartened that innovation will be more widely recognised and made more accessible to SMEs. This will position Singapore companies well for regional opportunities and competition with the advent of the ASEAN Economic Community later this year."
>
> Tham Sai Choy, Chairman of KPMG Asia Pacific and Managing Partner at KPMG in Singapore

Income tax measures that affect businesses

Announced in the Singapore Budget 2015, the following tax measures for businesses are aimed at helping businesses cope with rising costs and supporting businesses expanding overseas:

1. Phasing out the Transition Support Package
2. Extending and enhancing the Mergers & Acquisition (M&A) scheme
3. Enhancing the Double Tax Deduction (DTD) for Internationalisation scheme
4. Introducing the International Growth Scheme

Key highlights of these measures are set out below.

1. Phasing out the Transition Support Package

The Transition Support Package, introduced in the Budget 2013 to help businesses restructure, comprises of three components: the Corporate Income Tax (CIT) Rebate, the Wage Credit Scheme (WCS) and Productivity and Innovation Credit (PIC) Bonus. This package, which is due to expire this year, will be phased out gradually in recognition that businesses may need more time to adjust to rising costs as they restructure.

Extending the Corporate Income Tax (CIT) Rebate for YA 2016 and YA 2017

The 30% CIT rebate is extended for YA 2016 and YA 2017, but with a reduced cap of $20,000 (instead of $30,000) per company per YA.

Allowing the PIC Bonus to lapse

The PIC Bonus gives a dollar-for-dollar matching cash bonus for YA 2013 to YA 2015, subject to an overall cap of $15,000 for all three YAs combined. This is given on top of the existing 400% tax deductions/allowances and/or 60% cash payout available under the PIC scheme. As there has been a good take-up of the PIC scheme, the PIC Bonus will be allowed to expire in YA 2015. Businesses will however, continue to benefit from the PIC scheme (which has been extended till YA 2018), and the PIC+ scheme (introduced in the Budget 2014).

For more details on the PIC and PIC+ scheme and the accounting treatment, please refer to the December 2013 and March 2014 issues of KPMG Financial Reporting Matters.

Extending the WCS

Under the WCS, the Government co-funded 40% of the wage increases given between 2013 and 2015 to each Singaporean employee earning a gross monthly wage of $4,000 and below.

As announced in Budget 2015, the WCS will be extended to 2016 and 2017 to give employers more time to adjust to rising wages in the tight labour market. However, the co-funding will be reduced from 40% to 20%. For wage increases given in 2015 which are sustained in 2016 and 2017, employers will continue to receive co-funding at 20% for 2016 and 2017.

For more details on the accounting treatment for the WCS, please refer to the September 2013 issue of KPMG Financial Reporting Matters.

2. Extending and enhancing the M&A scheme

The M&A scheme, which was slated to expire on 31 March 2015, is extended till 31 March 2020 with the following changes taking effect for qualifying acquisitions made from 1 April 2015:

	Current scheme	New scheme
M&A allowance	5% of the value of qualifying acquisitions, with a cap on the allowance of $5 million per YA	25% of the value of qualifying acquisitions, with a cap on the allowance of $5 million per YA
Stamp duty relief on transfer of unlisted shares	Capped at $100 million of qualifying M&A deals (i.e. cap of $200,000 of stamp duty relief per financial year)	Capped at $20 million of qualifying M&A deals (i.e. cap of $40,000 of stamp duty relief per financial year)
Shareholding eligibility tiers	Acquisition of more than 50% ordinary shares (where original holding in target company was 50% or less) or 75% (where original holding between 50% and 75%)	Acquisition of at least 20% ordinary shares (if original holding in target company was less than 20%) or 50% (if original holding was 50% or less)
Step acquisitions	Acquiring company can elect for share acquisitions made during a 12-month period to be consolidated	Consolidation of acquisitions made across 12 months is removed

The M&A allowance rate has increased from 5% to 25%, while the quantum of the cap remained at $5 million. This is aimed at providing more meaningful support for companies, especially SMEs which typically conduct smaller deals. The potential cash tax savings of up to $850,000 (17% x $5 million) is not insignificant and can help Singapore-resident companies bid more competitively against overseas competitors.

To provide Singapore-resident companies more flexibility to grow locally or overseas via strategic partnerships, the shareholding eligibility tiers are revised. The changes will also likely benefit companies venturing into acquisitions for the first time or who want to manage their exposures in emerging markets or unfamiliar territories with minority stakes.

For more details on the accounting treatment for the M&A Scheme, please refer to the December 2011 issue of KPMG Financial Reporting Matters.

3. Enhancing the DTD for Internationalisation scheme

Under the DTD for Internationalisation scheme, businesses may claim a 200% tax deduction on qualifying expenditure incurred on qualifying market expansion and investment development activities, subject to conditions.

The scope of qualifying expenditure is expanded to include qualifying manpower expenses incurred from 1 July 2015 to 31 March 2020 for Singaporeans posted to new overseas entities. The amount of qualifying manpower expenses to enjoy the DTD will be capped at $1 million per approved entity per year. This may help companies defray their internationalisation costs and create more opportunities for Singaporeans to work overseas.

IE Singapore will release further details by May 2015.

4. Introducing the International Growth Scheme

This new scheme will provide a concessionary tax rate of 10% to qualifying Singapore companies for a period up to five years on their incremental income from qualifying activities. The scheme will be administered by IE Singapore with an approval window period from 1 April 2015 to 31 March 2020.

IE Singapore will release further details by May 2015.

> "A high concentration of the tax proposals are skewed towards Singapore businesses. This is a step in the right direction as we groom our businesses from productivity adoption to innovation and internationalisation. These initiatives are critical in encouraging a new generation of businesses to create value and venture abroad."
>
> Tay Hong Beng, Head of Tax, KPMG in Singapore

Other Key Changes for Businesses in Brief

Other measures that have been tweaked to strengthen support for innovation, internationalisation and competitiveness include:

- Extending and/or refining certain existing tax incentives for funds, banks, insurance businesses, designated trusts and maritime businesses to preserve Singapore's competitiveness and promote sustainable growth in the financial services and maritime sectors.
- Extending and enhancing the Temporary Employment Credit and Special Employment Credit to help employers adjust to higher wage costs arising from CPF changes (taking effect from 1 January 2016), and to encourage employers to voluntarily re-employ older workers.
- Recalibrating Foreign Worker Levies (FWL) to encourage firms to hire and retain more productive, higher skilled workers.

In addition, to encourage giving, tax deductions for qualifying donations are enhanced and extended.

Certain incentives (such as approved headquarters incentive, tax concessions on royalties and other payments from approved intellectual property or innovation, and concessionary tax rate on income from offshore leasing of machinery and plant) will be phased out.

More details on the tax changes and new initiatives unveiled in the Budget 2015 are available either on the IRAS website and MOF website.

You may also refer to KPMG Budget 2015 publication for a synopsis of the main objectives and initiatives of the Budget statement for businesses as well as individuals in Singapore.

Accounting impact on 31 December 2014 year-end financial statements

For changes affecting income taxes, under FRS 12 *Income Taxes*, changes in income tax laws and regulations are taken into account in the measurement of current and deferred taxes from the date of substantive enactment of those changes. In Singapore, new tax measures are generally considered substantively enacted on the date of announcement by Singapore Minister for Finance during the Budget Statement.

If your financial year ends on 31 December 2014, the measurement of current and deferred taxes should not take into consideration the effect of the new tax measures introduced in the 2015 Budget Statement.

For other changes, such as levies, and changes in incentives that are accounted for as government grants, the effect of changes is considered when they are effective and applicable.

Accounting impact on interim financial statements ending 31 March 2015

The effect of the new tax measures on the opening current and deferred taxes are recognised immediately in the interim period or as an adjustment to the effective tax rate as appropriate.

Refer to our publication *Insights 11th Edition Chapter (5.9.160 to 190)* for more extensive discussion on the accounting for income tax in the interim financial statements.

5. International developments

More insights and transparency – Enhancing the auditor's report

In response to calls from users for the auditor's report to provide more than a pass/fail opinion, the International Auditing and Assurance Standards Board (IAASB) has issued new requirements on auditor reporting. Without changing the scope of an independent audit, these requirements open the door for the auditor to give users more insight into the audit and improve transparency.

For listed companies, the engagement partner's name will need to be disclosed, as will the 'key audit matters' – i.e. the areas that the auditor worried about and focused on the most during the audit.

The new requirements apply for audits of financial statements for periods ending on or after 15 December 2016. Early application is permitted. Read our In the Headlines to understand more about the changes, why they matter and who will be affected.

> "Introducing descriptions of key audit matters is a significant change in auditor reporting. They provide the means for the auditor to address user demand for more information on the audit."
>
> Larry Bradley
> KPMG's global head of audit

IFRS: New standards

Companies with 31 March 2015 financial year ends will be preparing their annual financial statements considering the consequential effects of newly effective and forthcoming standards. Among others, investment entities will now benefit from the consolidation relief in the newly effective investment entities amendments.

In terms of new developments, clarifications to IAS 1 encourage preparers of financial statements to focus on the bigger picture and on entity-specific information. In addition, subsequent amendments to the new requirements for investment entities address some issues that were identified in early application of the consolidation exception.

Read our In the Headlines – IFRS: New standards for a summary of the newly effective and forthcoming standards.

Accounting for revenue is changing – Assessing the impact on housebuilders

Now that the IASB and FASB have published a new joint standard on revenue recognition, the real work for housebuilders is just beginning. The impact of the new requirements may be felt in areas such as sales of incomplete units or off-plan purchases, contract modifications, warranties and additional disclosures.

The new standard could impact the top line for housebuilders and the related communications with investors. The series of prompts in this publication aim to assist you in your assessment of how your financial reporting, systems and processes will be affected. It also highlights that you will need to engage with investors and other stakeholders to establish expectations of how their key performance indicators or business practices may change as a result of the new standard.

Accounting for revenue is changing – Impact on food, drink and consumer goods companies

The impact of the new joint standard on revenue recognition may be felt across different areas of arrangements with distributors and retailers – e.g. 'slotting fees', trade incentives, warranties, returns and licences. It is important to assess how your financial reporting, systems and processes will be affected, and to engage with your stakeholders to establish expectations of how your key performance indicators or business practices may change.

To help you with these assessments and discussions, we've developed a series of prompts for thinking through what the new requirements could mean for your business.

Accounting for revenue is changing – Assessing the impact on insurance companies

Insurers should not underestimate the impact of the new revenue standard that was published jointly by the IASB and FASB in May 2014. Although the new revenue standard does not apply to insurance contracts, it may apply to other arrangements – such as asset management, insurance broking, pension administration, claims handling or custody services. While the new revenue standard is almost completely converged, due to underlying differences in insurance accounting, the effect on companies reporting under IFRS and US GAAP could be significantly different.

To help you understand the implications, we've developed a series of prompts for thinking through what the new requirements could mean for your business such as whether you have bundled service contracts, non-refundable up-front fees or contracts with variable consideration.

The new revenue standard takes effect in January 2017, although IFRS preparers can choose to apply it earlier. While the effective date may seem a long way off, decisions on when and how to transition to the new revenue standard need to be made soon. An early decision will allow you to develop an efficient implementation plan and inform your key stakeholders.

New revenue standard – Symbolic divergence

Less than a year after publishing their joint standard on revenue recognition, the IASB and the FASB are back in standard-setting mode. In their February 2015 meeting, the Boards agreed to publish proposed amendments to the new standard in the areas of licensing and identifying separate performance obligations. The changes are intended to address implementation issues in a wide variety of industries, including media, pharmaceuticals, software and telecommunications.

Crucially, the FASB proposes making more extensive and more detailed changes than the IASB, though the Boards emphasised that the proposed amendments would represent clarifications to the new standard and are not intended to alter its underlying principles.

The proposed changes will be released for public comment. The Boards may also consider additional changes at future meetings. They plan to discuss the effective date of the new standard in Q2 2015.

Read our IFRS Newsletter: Revenue for more details on the Boards' discussions.

> "It now seems inevitable that the new revenue standard will be amended before it becomes effective – and that different changes will be made to the IFRS and US versions of the standard."
>
> Prabhakar Kalavacherla
> KPMG's global IFRS revenue recognition leader

Problems with principals

The principal-agent guidance in the new revenue standard was the main focus of the March 2015 meeting between the IASB and the FASB. The Boards discussed proposed improvements, but decided that further research was needed before firm decisions could be taken.

However, changes were agreed in other areas – namely collectibility, non-cash consideration and transition. It was the second time in two months that the Boards have agreed to propose changes to the new standard. The FASB also agreed a new practical expedient permitting a company to present sales taxes net.

The proposed changes will be released for public comment. The Boards may also consider additional changes at future meetings. They plan to discuss the effective date of the new standard in Q2 2015.

Read our IFRS Newsletter: Revenue for a summary of recent developments.

> "Once again, the FASB has shown a greater appetite to make detailed changes to the new revenue standard than the IASB."
>
> Prabhakar Kalavacherla
> KPMG's global IFRS revenue recognition leader

The macro hedging project: The latest developments

Feedback on the April 2014 macro hedging discussion paper (DP) expresses concern that the IASB has gone beyond the objective of hedge accounting in the new financial instruments standard (IFRS 9), with calls for a solution that will reflect risk mitigation through a flexible and voluntary hedge accounting model. Respondents broadly agreed that the DP identified the main limitations with current IFRS accounting for dynamic risk management (DRM) activities.

However, they expressed mixed views on whether the portfolio revaluation approach (PRA) would address these limitations. Most respondents seemed to support a project that only addresses accounting mismatches. When commenting on the scope of the PRA, many respondents preferred a scope focused on risk mitigation, rather than a scope focused on DRM, with most respondents supporting optional application of the PRA.

Response to macro hedging proposals, and the impact of IFRS 9 on regulatory capital

At its March 2015 meeting, the IASB completed its analysis of the feedback received. Detailed areas covered include revaluing managed exposures, presentation and disclosures, and applying the portfolio revaluation approach to other risks. Board members also expressed a range of 'bigger picture' views, and seemed to agree that the direction of the project would need to be decided before undertaking section-by-section redeliberations. We expect the overall direction to be determined in future Board meetings. Other topics discussed this quarter include the IASB's new project on the distinction between liabilities and equity, the EU endorsement process for IFRS 9, and disclosures on interests in unconsolidated structured entities.

In The Bank Statement, we review the feedback received on the macro hedging project and consider the Board's possible next steps. We also look at how IFRS 9's expected credit loss model could impact regulatory capital. The size of the impact on a bank's regulatory capital ratios largely depends on which approach the bank uses to calculate credit risk capital requirements. Further changes to regulatory requirements in response to IFRS 9 may also impact regulatory capital.

You may also read the February and March issues of our IFRS Newsletter: Financial Instruments for a summary of recent discussions on the macro hedging project and other financial instrument matters.

Participating contracts: Three key issues

The IASB continues to consider how the general insurance contracts model will accommodate contracts with participating features. This month's education session discussed three key issues.

- Should the contractual service margin (CSM) be adjusted ('unlocked') to reflect changes in an entity's share of underlying items? If so, then how and for which contracts?
- How should the CSM be recognised in profit or loss?
- How should an entity determine interest expense to be presented in profit or loss or, if it is permitted, in other comprehensive income?

For each question, our IFRS Newsletter: Insurance summarises the staff recommendations and discussions with Board members.

> "The staff proposals respond to the concerns of many constituents and may facilitate finalisation of the project."
>
> Joachim Kölschbach
> KPMG's global IFRS insurance leader

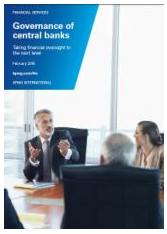
Permission to ballot

In a move that signals their determination to proceed with different lease accounting models, the IASB and the FASB have opted to prepare non-converged ballot drafts of their new standards on lease accounting. In their latest project meetings, the Boards also decided to retain the key elements of their proposed definition of a lease. This will disappoint constituents who were keen to explore alternative approaches.

The Boards have also agreed additional reliefs, including the details of an exemption for 'small-ticket' leases under IFRS and a new transition relief related to the definition of a lease.

The most important outstanding decision is the effective date. However, the Boards expect to issue their respective new standards by the end of 2015. Read our IFRS Newsletter: Leases for a summary of recent developments.

> "After almost ten years of joint work the IASB and the FASB have decided to ballot different lease accounting proposals."
>
> Kimber Bascom
> KPMG's global IFRS leasing standards leader



Taking financial oversight to the next level

Governance has been placed in the spotlight in recent years, driving a clear trend towards improving oversight in many global institutions.

Given their significant public-interest mandate, it is important that central banks lead by example and are at the forefront in adapting to a changing environment. Our publication Governance of Central Banks focuses specifically on financial oversight, one of the key pillars of governance and the most subject to change.

It is aimed at anyone involved in central bank governance, especially board and audit committee members. We identify the characteristics and underlying principles of effective financial oversight, show how some central banks are addressing the challenges and draw attention to emerging issues.

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

This publication has been issued to inform clients of important accounting developments. While we take care to ensure that the information given is correct, the nature of the document is such that details may be omitted which may be relevant to a particular situation or entity. The information contained in this issue of Financial Reporting Matters should therefore not to be taken as a substitute for advice or relied upon as a basis for formulating business decisions. Materials published may only be reproduced with the consent of KPMG LLP.

© 2015 KPMG LLP (Registration No.T08LL1267L), an accounting limited liability partnership registered in Singapore under the Limited Liability Partnership Act (Chapter 163A) and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.