

Financial Reporting Matters

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INTERNATIONAL DEVELOPMENTS

On the international front, the IASB has issued its clarifications to IFRS 15 *Revenue from Contracts with Customers*. Now that the IASB has issued the clarifications, we have the final version of IFRS 15 that IFRS preparers will be required to apply by 2018. Companies that have yet made a start can confidently begin to implement.



Stepped up enforcement actions for AGM and annual report breaches

Since 2015, Accounting and Corporate Regulatory Authority (ACRA) has stepped up its enforcement actions for breaching the statutory requirements to hold an annual general meeting (AGM) and to file an annual return (AR) under the Companies Act (the Act).

Directors should remember that the statutory requirements include all companies irrespective of size (including single asset holding companies) or business purpose.

Specific attention should be given to listed companies to hold an AGM in a timely manner. For companies with financial year ending 31 December, AGMs have to be held before the end of April as the financial statements presented will otherwise be outdated and in violation of the statutory requirements.

Common breaches of statutory requirements

A director of a Singapore-incorporated company has to comply with specified statutory obligations under the Act. These obligations are applicable to all companies incorporated in Singapore. It does not matter whether the company is active or dormant or whether the paid up capital is large or small.

ACRA has identified the following as the three most common breaches either by companies and / or their directors for which enforcement actions will be taken:

Companies Act Section	Statutory requirements	Breach by
Section 175(1)	A company and its directors must hold an AGM every calendar year and not more than 15 months from the previous AGM. If the company is newly incorporated, it has to hold its AGM within 18 months from its date of incorporation.	Both company and director
Section 197(1b)	After a company has held its AGM, it has to file the AR within one month via Bizfile, ACRA's online filing and information retrieval system.	Both company and director
Section 201(1)	For listed companies, the financial statements laid at the AGM by the directors must not be more than four months old. For non-listed companies, the financial statements laid at the AGM by the directors must not be more than six months old.	Director

Source: ACRA website

Enforcement actions by ACRA

1. Penalties and/or composition fines

ACRA may offer companies and / or directors who breach the above statutory obligations an opportunity to pay a composition sum, instead of facing a prosecution per breach. Separately, a late lodgement fee will be imposed at time of lodgement for each AR that is lodged late.

When the AR is lodged online, the date the financial statements are made up to and laid at the AGM and the date the AGM is held for laying the financial statements are required to be provided. With these two dates, the online system will ascertain if the company and / or directors are in breach. The composition sum and late lodgement fees are as follows with effect from 1 December 2015:

- (a) A flat penalty of \$300 for the late filing of AR regardless of the length of default;
- (b) A composition sum of \$300 for holding the AGM later; and
- (c) A composition sum of \$300 for laying out-of-date financial statements at the AGM.

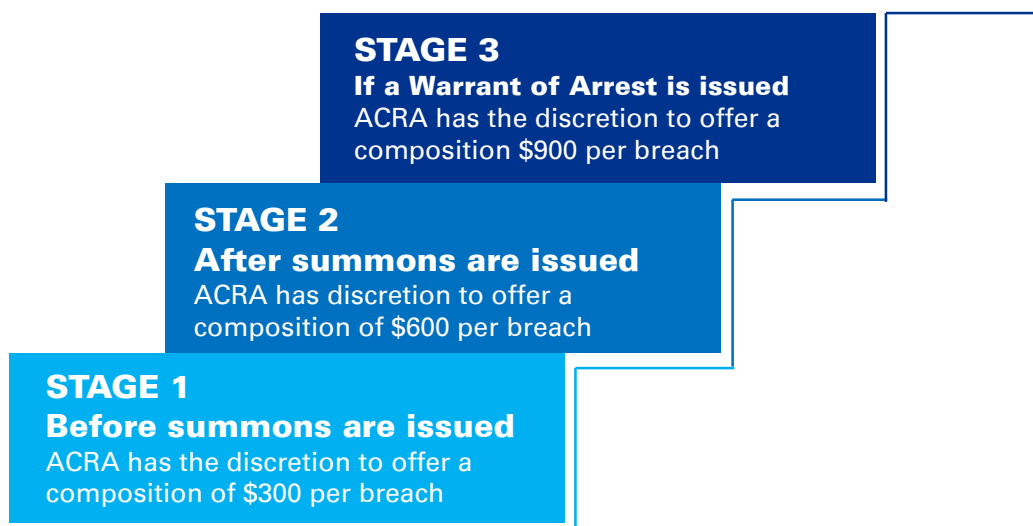
The penalty for late filing and composition sum for holding the AGM late are imposed against the company. However, the composition sum for laying out-of-date financial statements is imposed against the director. This is stage 1 of the 3-tier composition regime that ACRA has implemented.

When the breaches are not rectify, ACRA will issue summons against the directors to answer to the breaches under stage 2 of the 3-tier composition regime. ACRA may offer a composition sum of \$600 for each breach.

When the directors fail to attend Court to answer to the charges, a Warrant of Arrest is issued under stage 3 of the 3-tier composition regime. ACRA may offer a composition sum of \$900 for each breach.

The following diagram depicts ACRA's new 3-tier composition for failure to hold AGM or to file AR:

3-Tier Composition for: Failure to hold AGM and Failure to File AR



*Note: ACRA has the discretion not to offer composition and to take enforcement action against all or any of the company's officers.
Source: ACRA*

With the new enforcement regime, directors are encouraged to be more aware of the timeline to hold AGMs and to file ARs on time. If in doubt, directors can consult their legal counsel or corporate secretary.

2. Prosecution

ACRA will consider prosecuting the directors in Court if:

- (a) they fail to register and attend the Directors Compliance Programme (DCP) after ACRA writes to them to offer them a chance to attend the DCP (only first time offenders are eligible); or
- (b) they fail to compound the offences when offered a chance; or
- (c) ACRA is not prepared to let the directors compound due to the facts of the case.

The purpose of the DCP is to strengthen the directors' knowledge about their statutory obligations. Directors who attend the DCP and rectify their breaches will not be prosecuted by ACRA for the offences committed.

3. Disqualification or debarment

Starting 2016, ACRA also has the enforcement power to disqualify / debar a director or a company secretary in the following situations:

- A director who has at least three of his companies struck off within a period of five years will be disqualified from acting as director, or to take part in the management of any company for a period of five years commencing after the date on which the third company is struck off. For the avoidance of doubt, the striking off of the three companies are initiated by the Registrar and does not include voluntary applications for striking off.
- A director or a company secretary who is in default of a relevant requirement in the Act for a continuous period of 3 months or more may face a debarment order from the Registrar preventing him from taking on new appointments as director or company secretary of other companies.

References:

[ACRA: An overview of the common offences and prosecutions and penalties for companies under the Companies Act, Cap 50](#)

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Budget 2016 - Measures for Businesses

On 24 March 2016, Minister for Finance delivered the Budget statement. Budget 2016 seeks to transform our economy through enterprise and innovation, and to build a more caring and resilient society. In this article, we provide an overview of the key tax measures that will 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 24 March 2016.



"The continued emphasis on innovation in this year's Budget helps to prepare Singapore for the future. As other countries also move up the value chain, having an efficient and educated workforce, with their capabilities harnessed through enterprises with strong market positions, will enable Singapore's economy to stay competitive and relevant in a globalised world."

THAM SAI CHOY
Chairman of KPMG's Asia Pacific Region
and Managing Partner,
KPMG in Singapore

Income tax measures for businesses

In view of the current economic conditions, Budget 2016 announced calibrated measures to address challenges faced by small-medium enterprises (SMEs) while supporting businesses to innovate and continue restructuring. Key measures are:

1. Raising the Corporate Income Tax (CIT) Rebate for Year of Assessment (YA) 2016 and YA 2017
2. Introducing a new Automation Support Package
3. Enhancing the Mergers & Acquisitions (M&A) Scheme
4. Enhancing the Writing-Down Allowance (WDA) Claims for Intellectual Property Rights (IPRs)

As a move to shift away from broad-based support for business to more targeted measures, the cash payout rate under the Productivity and Innovation Credit (PIC) scheme will be lowered from 60% to 40% for qualifying expenditure incurred from 1 August 2016. The PIC scheme will expire after YA 2018.

Key highlights of these measures are set out below.

1. Raising the CIT Rebate for YA 2016 and YA 2017

To help companies, especially SMEs, the CIT rebate will be raised from 30% to 50% of tax payable for YA 2016 and YA 2017, subject to a cap of \$20,000 rebate per YA.

“The increase in the corporate tax rebate largely benefits small-medium enterprises (SMEs) who are paying tax. Start-ups who are making losses will not be able to enjoy the benefits. In fact, the reduction in PIC cash pay-out may be a let-down for start-ups who have invested in PIC initiatives and are cash-strapped.”

ANNA LOW,
Tax Partner at KPMG in Singapore



2. Introducing a new Automation Support Package

This new scheme aims to support firms that are looking to scale-up their automation efforts and comprises four components:

- Investment Allowance of 100% on approved capital expenditure (net of grants) capped at \$10 million per qualifying project;
- Capability Development Grant to support the roll-out or scaling up of automation projects at up to 50% of qualifying costs, with a maximum grant of \$1 million;
- Improve access to equipment loans under SPRING Singapore’s Local Enterprise Finance Scheme (LEFS) by enhancing the government’s risk-share with participating financial institutions from 50% to 70% for qualifying projects undertaken by SMEs. This LEFS will also be expanded to cover equipment loans for non-SMEs at 50% risk-share.

In addition, to support viable SMEs that may have cash flow concerns or wish to expand, a SME Working Capital Loan scheme is introduced, for loans of up to \$300,000 per SME. Funds can be used for working capital or for automation and upgrading of factory and equipment. Under this SME Working Capital Loan scheme, the Government will co-share 50% of default risk with participating financial institutions.

- International Enterprise (IE) Singapore and SPRING Singapore will partner businesses where appropriate to access overseas markets.

The example below illustrates how a local medium-sized company can benefit from the Capability Development Grant and LEFS.

Local medium-sized food manufacturing Company A engaged a system integrator to look into automating its manufacturing process and paid the system integrator a consultancy and installation fee of \$200,000. Company A further invested \$1.8 million to purchase three robotic arms and a conveyor belt system that integrates the packing and palletising process.

Under the new Automation Support Package, Company A will receive:

- a Capability Development Grant of \$1 million, defraying \$100,000 of consultancy and installation fee (50% x \$200,000), and \$900,000 for the cost of capital investments (50% x \$1.8 million); and
- 100% investment allowance on the remaining capital investment of \$900,000 on the robotic arms and the conveyor belt system, which will translate to \$153,000 of tax savings (17% corporate tax rate x \$900,000).

Company A can also obtain financing for the purchase of equipment from financial institutions that are participating in the enhanced LEFS. Company A will have a better chance of securing a competitive loan since the Government's risk-share has been increased from 50% to 70% for SMEs.

With the capacity to scale production, Company A can also tap on IE Singapore's schemes, such as the Market Readiness Assistance and Global Company Partnership, in order to go overseas. (More details are available at [IE Singapore](#)).

1. Enhancing the M&A Scheme

Under the current M&A Scheme, a qualifying Singapore company can claim a tax allowance for 25% of the cost of acquisition (capped at \$20 million), for qualifying share purchases. To support more M&A activities, the cap on consideration available for the M&A allowance and stamp duty relief will be increased to \$40 million of consideration paid per year for qualifying M&A deals made 1 April 2016 to 31 March 2020¹. This increase doubles the M&A allowance claims amount from \$5 million to \$10 million for acquisitions of at least \$40 million. This translates into potential tax savings of \$1.7 million (17% corporate tax rate x \$10 million), which is not insignificant and can help Singapore-resident companies bid competitively against overseas competitors. As for the stamp duty relief, doubling the cap means that a stamp duty relief of up to \$80,000 (instead of \$40,000) can be enjoyed for qualifying M&A deals.

¹ Qualifying M&A deals during this period (amongst other conditions) are those that result in the acquiring company owning:

1. at least 20% of the ordinary shares of the target company if the acquiring company owns less than 20% of the ordinary shares of the target company before the date of the share acquisition; or
2. more than 50% of the ordinary shares of the target company if the acquiring company owns no more than 50% of the ordinary shares of the target company before the date of the share acquisition.

For details on the other qualifying conditions, please refer to the [IRAS website](#).

IRAS will release further details by June 2016. For more details on the M&A scheme and the accounting treatment, please refer to the [March 2015](#) issue and the [December 2011](#) issue of KPMG Financial Reporting Matters respectively.

2. Enhancing the WDA Claims for IPRs

Under the current rules, companies and partnerships can submit a Workforce Development Agency (WDA) claim on the acquisition cost of qualifying IPRs over a period of five years. The election, which is irrevocable, must be made at the point of submitting the tax return of the YA relating to the basis period in which the qualifying cost is first incurred. This change will apply to qualifying IPR acquisitions made within the basis periods for YA 2017 to YA 2020.

As an anti-avoidance measure, IRAS has introduced specific provisions to adjust the acquisition/ disposal price of the IPR to the open market value for purposes of computing WDA to be allowed or balancing charge to be computed. This change will apply to acquisitions, sales, transfers or assignments of IPRs that are made from 25 March 2016.

“The flexibility to claim writing-down allowances on the acquisition cost of Intellectual Property (IPs) over a longer period will help companies to take full advantage of foreign tax credits on foreign royalty income arising out of such IPs.

Previously, these were often lost due to higher amount of claims squeezed over a fixed period of five years. While we do not have a “Patent Box” regime yet, tweaks like this go a long way in encouraging companies to bring IPs to Singapore as these help to minimise the tax impact.”

AJAY SANGANERIA,
Tax Partner,
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 the upfront certainty of non-taxation of gains on disposal of equity investments for another five years until 31 May 2022 to provide upfront certainty to companies for their corporate restructuring. The existing scheme parameters that the divesting company’s minimum shareholding of 20% of the divesting company and ownership for a period of at least 24 months from the date of disposal remain.
- Extending the Double Tax Deduction (DTD) for Internationalisation scheme for another four years until 31 March 2020. This covers qualifying expenditure incurred on activities such as overseas business development, investment study trips and missions, and participation in overseas trade fairs up to \$100,000 of the expenses of these activities will automatically qualify for DTD. For other qualifying activities or those exceeding \$100,000, companies may apply to IE Singapore for approval. To encourage SMEs to internationalise, the government will also provide assistance such as Global Company Partnership and Market Readiness Assistance programmes.

- Enhancing the Land Intensification Allowance (LIA) to encourage higher industrial land productivity.
- Extending and/or refining certain existing tax incentives to enhance activities in the areas of finance and treasury, insurance, global trading and maritime sector so as to strengthen Singapore's competitiveness.
- Extending the Special Employment Credit (SEC) for another three years until 31 December 2019 to provide employers with a wage offset for workers aged 55 and above and earning up to \$4,000 a month. The extended SEC will be tiered (i.e. up to 3%, 5% or 8% of wages) by employee age. Extending the SEC and increasing foreign worker levies and limiting the quotas, will encourage employers to hire and retain older workers and have a more productive and higher skilled workforce.
- Deferring the foreign worker levy increases for one year for the marine and process sectors in view of challenging business conditions and the reduction in the number of work permit holders in these sectors.

More details on the tax changes and new initiatives unveiled in Budget 2016 are available on the [IRAS website](#) and [MOF website](#).



You may also refer to [KPMG Budget 2016 publication](#) for more insights.



Accounting impact on 31 December 2015 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 these changes. In Singapore, new tax measures are generally considered substantively enacted on the date of the Budget announcement by Singapore Minister for Finance during the Budget Statement.

If your financial year ends on 31 December 2015, the measurement of current and deferred taxes should not take into consideration the effect of the new tax measures introduced in the 2016 Budget Statement. However, if the tax changes arising from the new tax measures are material to the financial statements, a description of the new measures and an estimate of their financial effect shall be disclosed as a subsequent event.

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

Accounting impact on interim financial statements ended 31 March 2016

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 12th Edition Chapter (5.9.160 to 190) which provides an extensive discussion on the accounting for income tax in the interim financial statements.

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IFRS 16 *Leases*

On 13 January 2016, the IASB issued the much anticipated and highly controversial lease accounting standard, IFRS 16. Consistent with the original goal of the IASB, under the new standard most leases will be treated on-balance sheet for lessees.

IFRS 16 will affect industry sectors that leases 'big-ticket' items such as properties, manufacturing facilities, vessels, and aircrafts the most.

The changes will fundamentally alter the impact of leases on lessees' income statement and balance sheet – the current divide between finance and operating leases is removed, along with the off-balance sheet treatment for lessees in the latter. IFRS 16 introduces a single on-balance sheet lease accounting model for lessees that is similar to current finance lease accounting.

IFRS 16 largely preserved the accounting for lessors other than enhanced disclosures about their risk exposures, in particular residual value risk. Lessors continue to assess whether an arrangement is an operating or a finance lease by using criteria similar to the current lease classification test.

This article will focus on the accounting of leases under IFRS 16 from the lessees' perspective and how the new standard will affect a lessee.

The new standard is effective from 1 January 2019, but given the scale of the upcoming changes on financial instruments, leases, revenue and IFRS 1 convergence for listed companies, companies may like to take action now.



"All companies that lease major assets for use in their business will see an increase in reported assets and liabilities. This will affect a wide variety of sectors, from airlines that lease aircraft to retailers that lease stores. The larger the lease portfolio, the greater the impact on key reporting metrics."

KIMBER BASCOM
KPMG's global IFRS leasing standards leader

Effective date

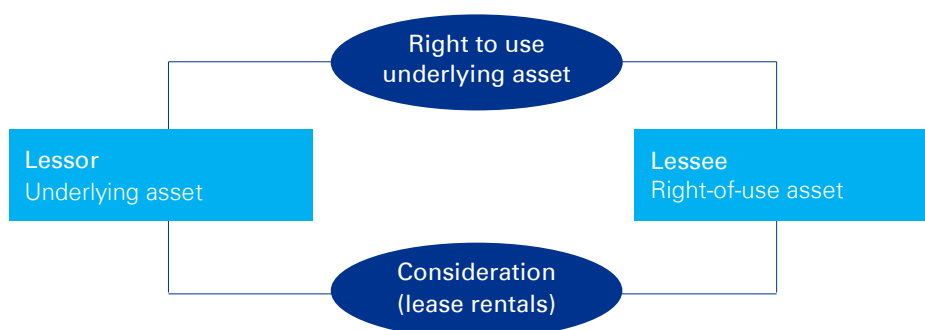
The standard is effective for financial years beginning on or after 1 January 2019. As of the date of this issue, the Singapore Accounting Standards Council is expected to issue the equivalent standard in Singapore in the near future.

Key impacts

- Companies leasing properties and other high-value assets, such as ships, aircrafts and other transport assets will see large increases in reported liabilities.
- The standard need not be applied to low value leases even if large volumes of such items are leased.
- Lessee and lessor accounting is not symmetrical. The standard introduces a single on-balance sheet accounting model for lessees but largely preserves current lessor accounting practice (i.e. lessors continue to classify leases as finance and operating leases).
- Total lease expense will be front-loaded even when cash rentals are constant.
- New estimates and judgements are required to identify, classify and measure leases.
- Key judgements are reassessed and lease balances may need to be remeasured at each reporting date, introducing more volatility into the balance sheet.
- IFRS 16 requires full retrospective or modified retrospective application when it becomes effective.

Identifying a lease

IFRS 16 defines a 'lease' as a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.



A lease will exist when both of the following conditions are met:

- fulfillment of a contract depends on the use of an identified asset; and
- the contract conveys the right to control the use of the identified asset for a period of time in exchange for consideration – i.e. the customer is able to direct the use of the asset or direct others to operate the asset, and obtains substantially all the economic benefits from its use throughout the term of the contract.

Identifying whether an agreement is, or contains a lease will be a key judgement when implementing the standard, particularly for lessees. The new definition of leases is, in effect, a new bright-line between treating the contract on-balance sheet (leases under the standard) and off-balance sheet (service contracts under the revenue recognition standard).

Here are two examples to illustrate the new definition of leases.

Example 1: Shipping contract A

Customer C enters into a two-year contract with Supplier S to transport cargo by sea from Singapore to Rotterdam. The ship to be used for transport is explicitly specified in the contract and S has no substitution rights over the ship. C did not design the ship.

The cargo will occupy all of the ship's capacity during the voyage. The contract specifies the cargo to be transported and the pick-up and delivery dates.

S operates and maintains the ship, and is responsible for safe passage of the cargo on board. C is prohibited from operating the ship itself, and from hiring another party to do so.

This is *not* a lease.

C has the right to gain all of the economic benefits from the use of the ship over the period of use. This is because C's cargo will occupy all of the ship's capacity, preventing other parties from obtaining significant economic benefits from use of the ship.

However, C does not have the right to direct the use of the ship because it does not have the right to direct how and for what purpose the ship is used for.

- The relevant decisions regarding how and for what purpose the ship is used are predetermined – i.e. carrying specific cargo from Singapore to Rotterdam within a specified timeframe.
- C does not have the right to change how and for what purpose the ship is used.
- C does not have the right to operate the ship and did not design it.
- C has the same rights as any regular customer.

Example 2: Shipping contract B

Customer C enters into a contract with Supplier S for the use of a specified ship for five years. The ship to be used for transport is explicitly specified in the contract and S does not have substitution rights. C decides whether and what cargo will be transported, and which ports to visit and when, throughout the five-year period.

C is prohibited from sailing the ship into waters at high risk of piracy, and from carrying explosive materials. S operates and maintains the ship and is responsible for safe passage of the cargo on board. C is prohibited from operating the ship itself, and from hiring another party to do so.

This is a lease.

C has the right to gain all of the economic benefits from use of the ship since it has exclusive use of the ship during the five-year period.

C also has the right to direct the use of the ship because it makes relevant decisions about how and for what purpose the ship is used throughout the period – i.e. it decides whether, where and when the ship sails, as well as the cargo it will transport.

The restrictions over not sailing in dangerous waters or transporting dangerous cargo are protective rights that define C's right to use the ship.

Example 2 is typical of a time charter arrangement in the shipping industry. Part of the contract meets the definition of a lease under the standard as it conveys the right to control the use of the vessel (an identified asset) for a period of time. Part of the contract also includes ship management and crew support services which is a service contract and does not fall under lease accounting.

Although the standard allows a lessee to account for the entire contract on-balance sheet as a practical expedient, separating between the two components will be advantageous as the service portion will be treated off-balance sheet.

How will this affect you?

You will need to revisit all of your existing agreements to assess whether they are, or contain, a lease. This exercise will require new judgements to be made in many cases.

As a result of the re-assessment, contracts that are currently under lease accounting may not be under the new standard, while contracts that are currently not under lease accounting may be considered under the standard's definition. This adds complexity in particular on transition.

A number of arrangements, for example, some power purchase agreements that are identified as leases under *IFRIC 4 Determining whether an Arrangement contains a Lease* may not be leases under the new standard. This is because the standard's approach to control has a greater focus on the purchaser's ability to control the use of the underlying asset than IFRIC 4. Similar considerations may arise for other output off-take and outsourcing contracts.

Significant practical expedients for lessees

Significant practical expedients are provided in the standard to ease the pressure on application of the lease definition and reduce compliance burden. Notably, leases of low value items (e.g. items that have a value of less than USD5,000 when new) and leases with a term of less than 12 months are typically exempted from the standard.

How will this affect you?

These exemptions will likely capture leases that are high in volume but low in value such as leases of IT equipment like laptops, mobile phones, basic printers or copiers or office furniture.

The exemption can be applied even if the effect is material in aggregate. These exemptions will permit a lessee to account for qualifying leases in the same manner as existing operating leases.

Lessee Accounting

IFRS 16 requires lessees to account for leases on-balance sheet by recognising a Right-of-Use (RoU) asset and a lease liability.

Statement of financial position	Statement of profit or loss	Profile of total lease expense
RoU asset	Depreciation of RoU asset	Front-loaded
Lease liability	(operating expense) Interest expense on lease liability (finance expense)	

Initial measurement

IFRS 16 requires that the lessee initially measures its lease liability at the present value of the future lease payments. Future lease payments include fixed or in-substance fixed lease payments and certain variable lease payments that depend on an index or rate. Usage or revenue-based variable payments are excluded from the lease liability. In addition, future lease payments will also take into account assumptions on lease term, residual value guarantees, purchase options, term option penalties, among others. These cash flows are then discounted using the rate that the lessor charges the lessee, or if it cannot be determined, the lessee's incremental borrowing rate.

On the other hand, the RoU asset is initially measured at cost, which equals:

- the lease liability, and
- any initial direct costs, and
- any pre-paid lease payments, and
- any restoration provision, without
- any lease incentives received.

Companies will have to exercise significant judgement in measuring the lease liability and RoU asset. For example, for an office space lease of five years with an extension option of three years, the lessee's conclusion on whether it has a significant economic incentive to exercise the option will have a significant impact on the amount of liability and RoU asset to be recognised at the inception of the lease.

How will this affect you?

Companies that are lessees in a lease arrangement will be significantly impacted by IFRS 16 as most of the contracts will now need to be recognised on-balance sheet. Key performance ratios (e.g. debt/equity ratios, tangible asset ratios) are likely to be affected and consequently the ability to satisfy debt covenants or any other balance sheet-based Key Performance Indicators (KPIs). If you are currently negotiating debt arrangements, you may wish to seek flexibility in determining the appropriate debt covenants to minimise the impact of the standard when it becomes effective.

Subsequent measurement

Lease Liability

After initial recognition, the lessee will measure its lease liability at amortised cost using the effective interest rate method. A lessee is required to reassess key judgements previously taken. If there is a change, the entity may need to remeasure the lease liability each time it reports.

RoU Asset

After initial recognition, the lessee will measure the RoU asset at cost less accumulated depreciation and accumulated impairment losses, or alternatively under the IAS 16 Property, Plant and Equipment revaluation model or in the case of an investment property, the *IAS 40 Investment Property* fair value model, if applicable.

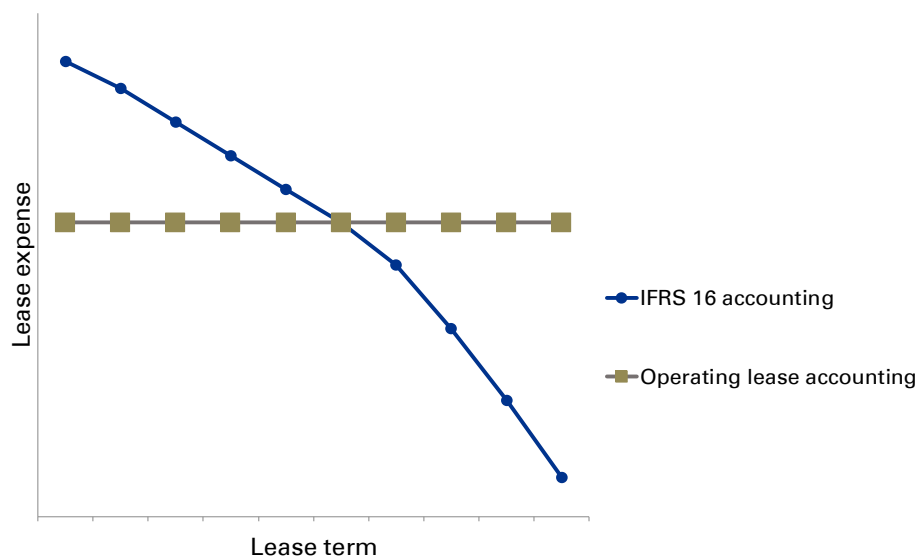
Lessees will also adjust the carrying amount of the RoU asset for remeasurement of lease liability.

The RoU asset will be depreciated on a straight-line basis, unless another systematic basis is more representative, over the shorter of the lease term and the useful life of the ROU asset.

RoU assets will be subject to the impairment requirements of *IAS 36 Impairment of Assets*.

How will this affect you?

Bringing operating leases on-balance sheet changes the profit or loss account of lessees. Currently, operating lease expenses are charged to the profit or loss account on a straight-line basis over the life of the lease. From 2019, leases will be accounted for as if the company had borrowed funds to purchase the RoU asset. This results in higher interest expense in early years than in later years, similar to any amortising debt. This means that total expense in the profit or loss account will be front-loaded.



The reassessment requirements will increase balance sheet volatility for lessees. At each reporting date, the reassessment may result in an increase or decrease of balance sheet size, making it less predictable.

Lessor Accounting

Lessor accounting remains similar to the current requirements. However, there are a number of changes in the details of lessor accounting. For example, lessors are required to apply the new definition of leases in IFRS 16.

How will this affect you?

Lessor and lessee accounting models are not consistent. In cases of inter-company leases, the group are required to keep track at consolidation and eliminate the RoU asset and the lease liability to avoid double counting.

Lessors will also need to revisit all existing agreements to assess whether they are, or contain, a lease. More importantly, lessees may reach out to you to restructure the agreements in light of the upcoming change in accounting that will impact them.

Multiple transition options

Both lessor and lessee are required to retrospectively apply IFRS 16's requirements upon application. However, IFRS 16 provides an option for a modified retrospective approach and certain practical expedients.

How will this affect you?

Applying the standard for the first time might be a time consuming and costly process for many companies. You are required to gather key inputs for nearly all leases, especially for those leases that are currently classified as operating leases under IAS 17.

You should evaluate whether you have sufficient resources available to identify and record data from all lease agreements in a timely manner upon transition to the proposed standard.

What to do next?

Given that IFRS 16 may potentially affect many companies, we recommend that you familiarise with the detailed requirements of the standard through trainings / education programs and start thinking about the potential impact the standard will have by performing a high-level impact assessment. Due to the retrospective application requirements, long term leases entered into today may have an impact on future financial statements when the standard becomes effective.

Tax implications

Under existing tax principles, the lessee can claim deductions for the operating lease payments as and when the expenses are incurred (i.e. liability must be crystallised in quantum and in law). However, with IFRS 16, the accounting treatment deviates from tax principles. If tax principles are unchanged, tax adjustments will have to be made to deduct only the contractual lease payments. Depreciation and interest charged to the profit or loss account will not be tax deductible.

Companies may also need to consider the impact on deferred taxation if there are differences between the carrying amount of the RoU asset and lease liability and the tax base. It remains to be seen if IRAS will align the tax treatment with the accounting treatment when the standard becomes effective.

Your next steps

Planning your implementation project for the new leases standard will take cost, effort and time. To assess your readiness, refer to the [IFRS 16 Readiness Questionnaire](#).

You can download the following KPMG publication to find out more about the new leases standard.



[First Impressions: IFRS 16 Leases](#)
[A more transparent balance sheet](#)

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How does the new Revenue Standard, FRS 115, affect construction margins?

For companies in the construction industry, while there has been a lot of focus on whether the adoption of the new revenue standard FRS 115 *Revenue from Contracts with Customers* will impact the top line, there has been less focus on how FRS 115 might impact contract cost accounting and contract margin.

Such companies will often find that applying the new revenue standard to a traditional construction contract will result in a revenue accounting outcome broadly similar to the current percentage-of-completion (POC) method. However, companies may be surprised that new concepts on contract cost accounting may result in a volatile contract margin over the life cycle of a typical contract.

One notable change for contract cost accounting is that FRS 115 costs are generally expensed and there is no automatic link between revenue and cost. This means that the approach under FRS 11 Construction Contracts of using a balance sheet true-up to create a consistent margin over the life of the contract may change under the new standard.

FRS 11 consistent margin approach versus FRS 115 cost incurred approach

We illustrate the impact arising from the change with an example below.

Example

Contract price: \$1,320

Contract margin: 20%

Output measure: POC is 28% based on survey work completed to date

Input measure: POC is 30% based on cost-to-cost method

	\$'000	\$'000	\$'000
	Actual cost	Cost-to-complete	Total budgeted cost
Materials/labour	110	290	400
Sub-contractor	110	290	400
Overhead	97	158	255
	317	738	1,055

Revenue to be recognised

	FRS 11	FRS 11	FRS 115	FRS 115
	Output measure	Input measure	Output measure	Input measure
POC	28%	30%	28%	30%
Revenue \$'000	370	396	370	396
Cost of sale \$'000	(295)	(317)	(317)	(317)
Contract Margin \$'000	75	79	53	79
Contract margin %	20%	20%	14%	20%

Under FRS 11, both contract revenue and contract costs that are accounted for using the POC method are recognised with reference to the stage of completion. Examples of acceptable methods are contract cost incurred to date as a percentage of forecast cost (cost-to-cost method), survey of work performed and physical completion.

Under FRS 115, revenue is recognised using a measure depicting performance using an input or an output measure (diagram 1). A contractor applying the input measure excludes the effect of inputs that do not depict its performance in transferring control of goods or services to customer (e.g. unexpected amounts of wasted materials, labour and any uninstalled materials).

Costs on the other hand, are expensed as incurred unless they qualify to be capitalised as an asset under another standard (e.g. inventory, property, plant and equipment) or they relate to incremental cost to obtain the contract or future performance. This assessment is not affected by whether an entity chooses an input or output measure to measure progress.

INPUT METHOD

- Contract cost incurred to date as a percentage of total forecast cost
- Time elapsed
- Labour hours expended
- Machine hours used

OR

OUTPUT METHOD

- Survey of work completed to date
- Appraisals of results achieved
- Milestones reached
- Time elapsed

Diagram 1

Implications

From the above example, under FRS 115, an input measure using the cost-to-cost method will most likely result in an outcome similar to FRS 11 (using the same cost-to-cost measure) and provide a stable margin. On the other hand, if an output measure is used, it may result in a more volatile margin because there is no direct linkage between the costs being expensed and the output measure used to determine revenue. (Illustration 2)

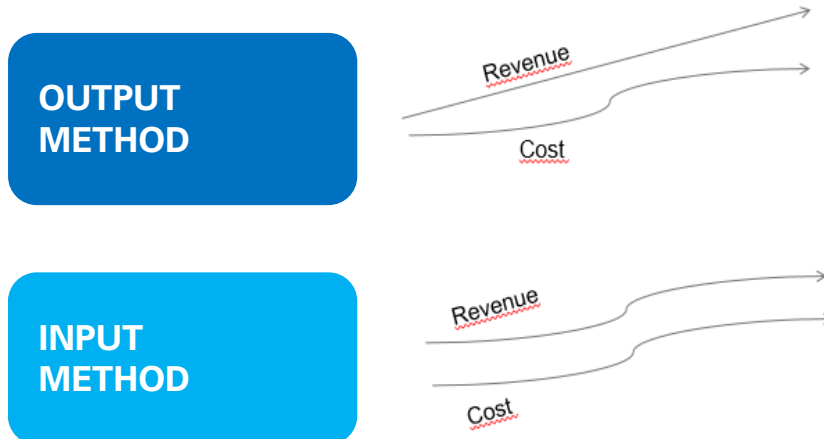


Diagram 2

If progress is based on surveys (output method), revenue may be consistent throughout the stages. However, costs may be higher in the early stages of construction and consequently the margin in the early stages may be much lower than the later stages. Conversely, if an input measure based on cost-to-cost method is used, higher revenue will be recognised at the earlier stage when the higher costs are incurred and therefore the margin will be more stable.

Under the new standard, construction companies that previously recognised revenue and costs with reference to the stage of completion which falls under the 'output' measure or other input measures (except cost-to-cost) need to carefully consider how this might impact their bottom line. Specifically, they need to consider if changing to the cost-to-cost method might result in a better reflection of their performance under the contract and the margin earned.

Cost accounting- what can be capitalised and what can be precluded?

FRS 115 also introduced the following new concepts for cost recognition which may change current accounting for pre-contract costs, work-in-progress and provision for loss-making contracts (i.e. foreseeable losses):-

1. **Costs that cannot be capitalised are expensed as incurred. Costs can be capitalised only if they qualify to be capitalised as an asset under another standard (e.g. inventory, property, plant and equipment) or they relate to incremental cost to obtain a contract (e.g. bonus or sale commission on winning a contract) and future performance.**

The main costs for construction contracts are staff costs, material costs and depreciation costs. Sophisticated systems may be required to determine how to segregate costs between those relating to "future performance" and those that need to be "expensed off directly to P&L". In addition, it is not uncommon for costs to be incurred for variation orders before they are "approved". The determination of whether these costs should be expensed off or if some portion of it can be capitalised depends on "future performance" or a separate performance obligation and the ability to track capitalisable cost are key considerations under the new standard.

2. **Costs that are not incurred (e.g. risk contingencies, warranties) are recognised if they qualify as a provision under FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*.**
3. **Losses on loss-making contracts are provided for under FRS 37 only if considered onerous. The measurement of the provision may change from FRS 11.**

Construction companies need to identify all costs incurred throughout the life cycle of the construction contract and review if the cost accounting is still appropriate under FRS 115 and assess the potential impact on adoption of the new standard.

Given that most construction contracts are long-term, it is critical to start the process now as a contract signed today may still be "open" when FRS 115 becomes effective in January 2018. In addition, it is also important to understand that the transition options are available, including the impact on the comparative period, and ensure that open contracts are restructured in advance if required.

Effective date and transition

FRS 115 is effective for annual reporting periods beginning on or after 1 January 2018. For Singapore-incorporated companies listed on the Singapore Exchange, transition to FRS 115 will coincide with the beginning of the first reporting period under a new reporting framework identical to the IFRS. Listed companies will need to take note that the application of IFRS 1 will effectively remove one of the transition approaches in FRS 115 – the cumulative effect approach.

Consequently, these companies will have to show comparatives for 2017. In order to do so, their systems will have to be in place by 1 January 2017 (7 months away for companies with December year-ends) to ensure that the information for FY 2017 are captured appropriately under FRS 115.

To understand more about the transition options, refer to our publication on [Transition to the New Revenue Standard and Issues In-Depth \(September 2014\) – Chapter 13 and 14.](#)

In addition, you may access these publications for more information on the new revenue standard.



[Impacts on the construction industry of the new revenue standard](#)



[Financial Reporting Matters, December 2014, Issue 49](#)

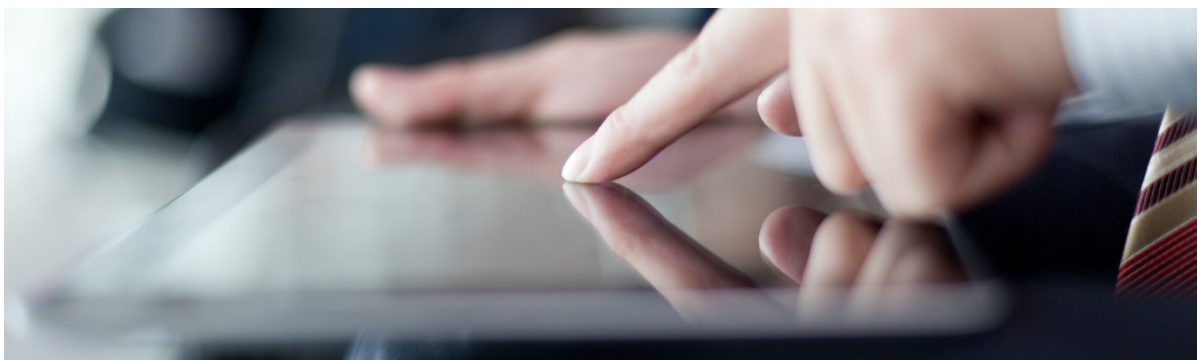
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International Developments



New revenue recognition standard – It’s time to engage

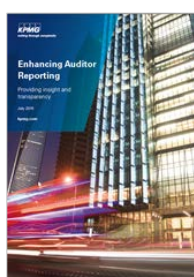
Now that the IASB has issued its clarifications to IFRS 15, we have the final version of the standard that IFRS preparers will be required to apply by 2018. No further amendments are expected. Therefore, companies that have not made a start can confidently begin to implement.

Our [article](#) provides a high-level summary and the [First Impressions](#) has been fully revised and updated to provide a digestible introduction to the clarified version of IFRS 15, highlighting key impacts and potential next steps. We will also release a second edition of our Issues In-Depth guide in the coming weeks.

“If you haven’t yet engaged with IFRS 15, then it’s time to assess the extent of the impact, so that you can address the wider business implications – and meet the expectations of your stakeholders and regulators.”

BRIAN O’DONOVAN

KPMG’s global IFRS revenue recognition deputy leader



Enhancing the value of audit – What next?

In a world where demand for transparency and disclosure continues to grow, sound corporate reporting and a quality audit remain essential.

A global debate is ongoing about how corporate reporting – and the audit profession – need to evolve in order to continue to meet growing demands. KPMG is adding to this debate through a series of Value of Audit roundtables, in which investors, audit committees and other stakeholders exchange views as to how these changes may take shape.

With respect to audit, innovations are already taking place. For example, new-style audit reports are already being produced in several jurisdictions, focused on sharing better insight and based on recently issued international standards. In the countries that have already gone live with the new requirements, the response has been positive – especially from investors. And although implementation dates vary by country, all stakeholders have an interest in planning now for what is to come.

For more specific information on the new-style audit report, download your copy of [Enhancing auditor reporting: Providing insight and transparency](#). For insight on some of the pressing issues facing the audit model and profession today, visit our global [Value of Audit website](#).

“I have always felt that we, as auditors, had more insight that we could share with investors. The new international auditor reporting requirements give us the opportunity to do just that.”

BILL O’MARA

KPMG’s International Global Head of Audit



Looking at ways to improve IAS 32

As part of its ongoing discussions on financial instruments with characteristics of equity, the Board has continued to consider the three approaches identified as potential ways of improving IAS 32 Financial Instruments: Presentation.

At its February 2016 meeting, the Board highlighted the need to further explore presentation options as a means of addressing the shortcomings of a binary classification approach. It also considered claims with conditional alternative settlement outcomes.

The next step for the project will be to further develop the approaches discussed so that the Board can form a preliminary view on its preferred approach.

Read our [IFRS Newsletter: Financial Instruments](#) for a summary of these recent developments.

“The latest Board discussions have highlighted the need to further explore presentation options as a means to address the shortcomings of a binary classification approach.”

CHRIS SPALL

KPMG’s Global IFRS Financial Instruments Leader



Revised criteria for deferring IFRS 9

More companies will be able to benefit from the temporary exemption from applying IFRS 9 *Financial Instruments*, thanks to decisions taken by the IASB this month.

The Board has responded to feedback by agreeing to broader qualifying criteria for the temporary exemption. It has also confirmed aspects of the overlay approach and amended some disclosures, which may enhance comparability between entities.

The IASB is on track to publish its final amendments to IFRS 4 *Insurance Contracts* in September 2016.

For a detailed discussion of these developments, read [Issue 53](#) of our IFRS Newsletter: Insurance. Previous issues can be found on our [Newsletters](#) page.



Banks – IFRS 9 implementation challenges

Banks' efforts on implementing IFRS 9 Financial Instruments shows that determining classification is not as straightforward as they may have initially expected. The classification and measurement phase is closely related to the impairment phase, and banks have to work on both phases together.

This quarter's newsletter shares lessons learned in the field. It also discusses the changing requirements of Pillar 3 of the Basel Framework and the increasing focus of the regulators on comparability of disclosures between Pillar 3, financial statements and other public disclosures.

Read our [IFRS Newsletter: The Bank Statement](#) for a summary of recent developments.

“Many banks started their IFRS 9 implementation projects by focusing on specific accounting issues known to be challenging, and did not focus sufficiently on the broader impact of adopting the standard.”

GERD STRAUB and GUDRUN HARTIG
Accounting Advisory Services, KPMG in Germany



Banks – Your essential year-end guide

Our *Guide to annual financial statements – Illustrative disclosures for banks* has been updated to reflect early application of IFRS 9 *Financial Instruments*. As with other complex standards, the interpretation of IFRS 9's requirements is subject to ongoing discussions. This guide does not intend to pre-empt this process, but aims to help banks implement IFRS 9, by guiding them through the decision-making process needed to prepare the required disclosures.

This guide illustrates example disclosures for the early adoption of IFRS 9 and of consequential amendments to other standards, which are required to be adopted at the same time. Apart from that, it reflects IFRSs in issue at 31 December 2015 that are required to be applied by an entity with an annual period beginning on 1 January 2015.

Download your copy of [the guide](#).



Insurance - New standard set for balloting

The International Accounting Standards Board (IASB) has instructed staff to begin the balloting process for the forthcoming insurance contracts standard, paving the way for the final standard to be issued around the end of 2016.

In the meantime, the IASB will decide on the effective date and complete targeted external reviews to ensure that the wording in the standard is interpreted consistently with the Board's objectives.

Companies should begin assessing the potential impact on their business and closely follow issues that may arise during the balloting process.

Read our [web article](#) to find out more, and our [visual guide](#) to -prepare your companies for the forthcoming insurance contracts standard.

“Now is the time for entities to begin assessing the impact the new insurance contracts standard will have on their key performance indicators and processes.”

JOACHIM KÖLSCHBACH
KPMG's Global IFRS Insurance Leader



KPMG supports transitional relief for insurers on IFRS 9

We support the IASB's efforts to address the differing effective dates of IFRS 9 Financial Instruments and the forthcoming insurance contracts standard.

In our view, the Board's proposals to amend IFRS 4 Insurance Contracts represent a targeted and proportionate response to concerns raised by constituents. In addition, we think that more insurers can benefit from the temporary exemption from applying IFRS 9 if certain improvements – such as modifications to the predominance criteria – are made.

Download our [comment letter](#) to understand KPMG's position.

To find out more, read our [web article](#) and the accompanying SlideShare presentation.

For a more detailed analysis, [download our New on the Horizon: Insurance amendments.](#)



Direction set for IFRS 4 amendments

At the March 2016 meeting, the IASB outlined its plans for finalising its proposed amendments to IFRS 4 Insurance Contracts and started redeliberations.

The Board discussed the feedback received on its exposure draft addressing concerns about the differing effective dates of IFRS 9 Financial Instruments and the forthcoming insurance contracts standard.

It confirmed that both the temporary exemption from applying IFRS 9 and the overlay approach will be retained as options. It also confirmed that eligibility for the temporary exemption will be assessed at the reporting entity level and that it will have a fixed expiry date.

Its discussions will continue in April and May, and the final amendments to IFRS 4 are currently expected to be published in September.

Read our [IFRS Newsletter: Insurance](#) for a summary of recent developments.

“Confirmation of an optional temporary exemption at the reporting entity level will allow eligible ‘pure’ insurance entities to postpone application of IFRS 9.”

JOACHIM KÖLSCHBACH
KPMG’s Global IFRS Insurance Leader



Clearer accounting for deferred tax assets

During the financial crisis, a question arose on the accounting for deferred tax assets.

Can a deferred tax asset be recognised for an unrealised loss on a debt instrument for which the holder ultimately expects to collect the contractual amount?

The IASB’s recent amendments to IAS 12 Income Taxes clarify that the answer is ‘yes’, if certain conditions are met.

While the initial question may have been relatively narrow, the amendments address a much broader area of accounting for deferred tax assets in general, including the question of how to determine future taxable profit for the recognition test.

The amendments are effective for annual periods beginning on or after 1 January 2017. The impact on your clients’ financial statements will depend on their tax environment and how they currently account for deferred taxes.

Read our [web article](#) to find out more.

“Stemming from a relatively narrow question about deferred taxes on unrealised losses on debt instruments, the amendments address a much broader area of accounting for deferred tax assets in general, including the question of how to determine future taxable profit for the recognition test.”

SANEL TOMLINSON
KPMG in China



KPMG supports accounting for uncertain tax positions proposals

We support the IASB's [proposals](#) to bring clarity to the accounting for uncertain income tax treatments and believe that they should be expanded to include the related interest and penalties.

Further clarifications are also necessary to support consistent application of the proposals, including areas relating to the collective assessments of uncertain tax treatments, events after the end of the reporting period and the definition of the term 'probable'.

Download our [comment letter](#) to understand KPMG's position. Read our [web article](#) and the accompanying [SlideShare presentation](#) to find out more.

"While we welcome the greater clarity and transparency, this is a sensitive issue that has generated much controversy. We urge you to read the proposals and participate in the debate."

SANEL TOMLINSON
KPMG in China



Disclosure on changes in financing liabilities

[IAS 7 Statement of Cash Flows](#) has been amended as part of the IASB's broader [disclosure initiative](#) to improve presentation and disclosure in financial statements.

For some time, investors have been calling for more disclosures on net debt, a term not defined in IFRS. The Board has responded by requiring disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes.

Read our [web article](#) to find out more.

"While we welcome another step towards more valuable disclosures for users, the question remains whether these narrow-scope amendments will result in more relevant information about an entity's cash dynamics, on a consistent and comparable basis."

GABRIELA KEGALJ
KPMG's Global IFRS Presentation Deputy Leader



Newly effective standards at a glance

Our summary of newly effective and forthcoming standards for March 2016 year ends is now available.

There are five summary sheets based on the four most common financial year ends. Each one links to our insight on the new requirements.


The summary of newly effective standards is available all year-round and updated whenever a relevant pronouncement is issued. You may access our summaries via our [IFRS: New standards](#) web page when you need to look up information for your financial year end.

IFRS 16 Readiness Questionnaire

Planning your implementation project will take time and care. However, it might be worth asking yourself a few simple questions now – just to get a feel for the scale of the challenge ahead...



Topic	Questions and comments	<input checked="" type="checkbox"/>
Lease Definition	Do you know which of your transactions are, or contain, leases?	<input type="checkbox"/>
	Will you elect to grandfather the lease definition for existing contracts on transition?	<input type="checkbox"/>
	<ul style="list-style-type: none"> • In many cases, lease definition will be obvious, and a transaction that is a lease today will be a lease in 2019. However, there are significant changes in lease definition that will affect many common transactions – e.g. power purchase agreements and transport agreements. • There is also a big decision to be made on transition – will you spend the time and cost necessary to reassess your existing transactions and thereby exclude some existing transactions from lease accounting, or grandfather existing arrangements and apply the new definition only to new arrangements? 	
Lease Data	Do you have a database of all of your leases?	<input type="checkbox"/>
	Do you have the systems and processes necessary to calculate lease assets and liabilities?	<input type="checkbox"/>
	Are your current disclosures of operating lease commitments complete and accurate?	<input type="checkbox"/>
	<ul style="list-style-type: none"> • Some companies have databases that capture all of their lease data – but this isn't true for everyone. Now is the time to begin to assess whether your current systems have the information necessary to apply the new standard. • The operating lease commitments note may not always be the top priority in a busy reporting season. Now is the time to check that it includes all of the leases that you will soon be bringing on-balance sheet, so that there are no surprises on transition. 	
Debt Covenants	Will application of the new standard impact your debt and other covenants?	<input type="checkbox"/>
	<ul style="list-style-type: none"> • Many financial agreements feature covenants that are applied on a 'frozen GAAP' basis – that is, a change in accounting policy won't affect the covenant test. But this isn't true in all cases. • Given the scale of accounting change – with new standards on financial instruments, leases and revenue to be applied in 2018–19 – it's time to double-check, to identify any covenants that you may wish to renegotiate before the standard becomes effective. 	

Topic	Questions and comments	
Sale-and-leaseback	<p data-bbox="373 282 1254 344">Do you understand the impact of the new standard on your sale-and-leaseback transactions?</p> <ul data-bbox="373 383 1254 757" style="list-style-type: none"> <li data-bbox="373 383 1254 445">• Most companies and users know that the new leases standard eliminates sale-and-leaseback as an off-balance sheet proposition. <li data-bbox="373 461 1254 524">• But there's more than one way in which a sale-and-leaseback can come back on-balance sheet. <li data-bbox="373 539 1254 571">• If the transaction is a true sale under IFRS 15, then it comes <li data-bbox="373 586 1254 649">• on-balance sheet like a current sale-and-finance leaseback – i.e. with the liability measured at cost. <li data-bbox="373 665 1254 757">• If the transaction is not a sale under IFRS 15, then it comes on-balance sheet as a financing under IFRS 9, which may require ongoing remeasurement at fair value through profit or loss. 	<input type="checkbox"/>
Financial ratios	<p data-bbox="373 792 1254 855">Do you understand the impact of the new standard on your financial ratios, KPIs etc?</p> <p data-bbox="373 893 1254 981">Will optional exemptions, such as those for short-term leases and leases of low-value items, have a material impact on your financial statements?</p> <ul data-bbox="373 1019 1254 1514" style="list-style-type: none"> <li data-bbox="373 1019 1254 1081">• Most companies and users know that the new standard brings more leases on-balance sheet, increasing gearing etc. <li data-bbox="373 1097 1254 1514">• But what about other effects? <ul data-bbox="400 1135 1254 1514" style="list-style-type: none"> <li data-bbox="400 1135 1254 1223">- Detailed modelling may be required to predict the impact of the front-loaded total lease expense in moving from operating lease accounting to the ROU model. <li data-bbox="400 1238 1254 1326">- The geography of the profit or loss account will change, as operating lease expense is replaced by depreciation/ amortisation of the ROU asset and interest expense. <li data-bbox="400 1341 1254 1404">- Will you redefine non-GAAP measures such as EBITDA to reflect the new lease model? <li data-bbox="400 1420 1254 1451">- How will you present variable lease payments? <li data-bbox="400 1467 1254 1514">- Do you know what impact the optional exemptions will have on your KPIs? Have you decided which ones to elect? 	<input type="checkbox"/>
Transition options	<p data-bbox="373 1550 1254 1581">Have you thought about how to transition to the new standard?</p> <ul data-bbox="373 1619 1254 1879" style="list-style-type: none"> <li data-bbox="373 1619 1254 1879">• The new standard will offer a wide range of transition options, featuring many practical expedients. One key question is whether to apply the standard: <ul data-bbox="400 1720 1254 1879" style="list-style-type: none"> <li data-bbox="400 1720 1254 1783">- retrospectively, which may require additional cost and effort but will result in greater consistency in comparative periods; or <li data-bbox="400 1798 1254 1879">- as a 'big bang' on the date of initial application, which will require less historical information but may impact your trend data for many years to come. 	<input type="checkbox"/>

Source: *First Impressions: IFRS 16 Leases, A more transparent balance sheet* by KPMG International

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.

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