

In this year-end issue, we highlight the recent changes in financial reporting standards and other key developments that have an impact on financial reporting. These include fair value discussions during the IASB and FASB round-tables. Companies should start preparing for these changes immediately if they have not already done so. Developments in corporate governance, the filing of financial statements in XBRL, the proposed changes to the SGX Listing Manual and some international developments are also covered.

Contents

- Accounting issues under current economic conditions..... 2
- Changes in legislation and best practices
 - Singapore Exchange Matters.. 4
 - Changes to Singapore income tax..... 5
 - New business vehicle – Limited Partnership..... 5
 - Filing of financial statements in XBRL..... 6
- Overview of 2008 changes to financial reporting standards..... 8
- Improvements to FRSs..... 15
- Amendments to FRS 101 and FRS 27 - *Cost of investment in a subsidiary, jointly controlled entity and associate*..... 19
- Amendments to FRS 32 and FRS 1 - *Puttable financial instruments and Obligations Arising on Liquidation*..... 21
- INT FRS 116 *Hedge of a net investment in a foreign operation*..... 24
- International developments..... 29

The credit crisis that started in the United States has now affected the real economy. The focus is now on questions over the likely length and depth of the recession, and the adverse effects on many companies in fundamental areas including the availability of funds, consumer demand and the evaluation of the value of investments and other assets.

Subsequent to our Credit Crisis Special Report issued in November 2008, the IASB and the FASB have held three public round-table discussions to identify financial reporting issues highlighted by the global financial crisis. We discuss the salient points raised at these discussions as many of the issues identified are also relevant to companies in Singapore.

The IASB has a number of specific projects on financial instruments on hand in response to the credit crisis. However, these projects will take time to complete. Therefore, for the immediate December 2008 financial statements, entities should consider how to disclose the nature and extent of risks arising from financial instruments, the reasonable changes in risk variables in the sensitivity analysis, the estimation uncertainties and whether impairment losses exist under current economic conditions. For non-financial instruments, impairment loss issues are also relevant for many entities.

It is perhaps timely that the industry-led Audit Committee Guidance Committee (ACGC) has issued a detailed set of guidelines to help audit committee (AC) members discharge their responsibilities according to best practices. This will effectively raise the bar on corporate governance best practices for ACs in Singapore.

Many new or revised financial reporting standards and interpretations will become effective for annual financial periods commencing on or after 1 January 2009. Looking at the volume and extent of the changes, we believe that most companies are likely to need more time to prepare for them. Companies should start preparing for the changes immediately if they have not already done so.

A. Accounting issues under current economic conditions

Refer to *Financial Reporting Matters November 2008 – Credit Crisis Special Report* for details

In our November 2008 special issue of *Financial Reporting Matters – Credit Crisis Special Report*, we discussed the key steps taken by the IASB in response to the credit crisis. We also summarised the "Common Principles to Guide Financial Market Reform" and the "Action Plan" to implement the 'Common Principles' agreed at the meeting of the G20 leaders in Washington on 15 November 2008.

The report included a summary of the key guidance issued by the IASB on fair value accounting, in addition to our comments on the following topics:

- Guidance on Fair Value in Inactive Markets
- Reclassifications of Financial Assets
- Improving Disclosures about Fair Value and Liquidity Risks

The Common Principles and agreed actions towards strengthening transparency and accountability will significantly affect the agendas of the IASB and set financial reporting trends in the near future.

IASB and FASB public round-table discussions

Refer to *IFRS Briefing Sheet – Issue 116* for details

Subsequent to our write-up in November 2008, the IASB and the FASB (the Boards) have held three public round-table discussions to identify the financial reporting issues highlighted by the global financial crisis. The round tables are intended to help the Boards identify any accounting issues that may require immediate attention to improve financial reporting and help enhance investor confidence in the financial markets.

The insights gained at the round tables will form the inputs for a high-level advisory group of senior leaders with a broad international experience of financial markets. This group was established to assist the boards in responding to the crisis in an internationally co-ordinated manner.

The three public round-table discussions were held in:

- (1) London, England on 14 November 2008;
- (2) Norwalk, United States on 25 November; and
- (3) Tokyo, Japan on 3 December 2008.

Many of the issues discussed at the public round-table discussion in London are equally relevant to entities in Asia, including Singapore. Participants at the round table meetings included a wide range of stakeholders, including regulatory bodies, preparers, auditors, and users of financial statements. There are various views, not necessarily consistent, on how to take things forward. Some of the more salient points discussed at these round-table discussions are:

General consensus

Participants generally agreed that further changes to existing standards should be subject to due process and approached jointly by the Boards.

Any significant proposals to amend the recognition and measurement requirements is unlikely to affect reporting periods ending in December 2008.

The views expressed indicate a need for greater transparency and some entities may choose make voluntary disclosures pending changes to financial reporting standards.

Impairment – triggers and measurement

Available for sale equity securities

Some participants stated they had difficulty in identifying impairment triggers, and that there seems to be a divergence in practice on the interpretation and application of the “significant or prolonged” criteria in IFRSs. Those participants believe that the market price for a share is not necessarily indicative of its underlying economic value. They believe that judgement should be exercised to evaluate the economics of the investee rather than being required to recognise an impairment loss whenever there is a significant decline in market price.

Other participants argued that as a market price for a share represents objective information, it is the most appropriate indicator to use when determining whether a security is impaired. They felt that if management believes that a market price is not indicative of the underlying value of an investment, then it still should measure the asset based on the market price but should provide additional disclosures explaining its view.

Our comments:

It should be noted that FRS 39 *Financial Instruments: Recognition and Measurement* currently states that the best evidence of fair value is quoted prices in an active market. However, if a market is deemed to be inactive or forced sale transactions are considered to have occurred, the use of a valuation technique may be appropriate after having assessed all relevant facts and circumstances. A valuation technique might incorporate both observable market data and unobservable inputs. Disclosure of the valuation techniques used is important to meet the objective of helping users understand the techniques used and the judgements made in measuring fair value. An example of this may be where management believes that the underlying economic value is not reflected in the share price.

Available for sale debt securities

Some participants suggested that the presentation of impairment losses could be split between those resulting from credit deterioration (to be recognised in the income statement) and those related to market movements (to be recognised directly in equity as other comprehensive income).

Our comments:

Separating impairment losses between credit and other factors, such as interest or liquidity, may be difficult.

Fair value considerations

Some participants stated that there is difficulty in measuring fair value when there are no observable market prices, and requested further application guidance.

The Boards’ representatives reaffirmed their view that observable market data is the best measure of fair value. They further stated that implied market data is preferable even if the data is old or for a similar transaction. Management should use this observable data and if necessary, make additional assumptions to derive their best estimate of a fair value.

Our comments:

The IASB has issued an ED on Improving Disclosures about Financial Instruments, which proposes that entities disclose fair value measurements using a three-level fair value hierarchy that reflects the significance of the inputs used in measuring fair values.

Entities may want to voluntarily disclose the information as proposed in the ED in their 31 December 2008 financial statements. This is particularly relevant where fair values are measured using valuation techniques for which any significant input is not based on observable market data.

B. Changes in legislation and best practices

Singapore Exchange Matters

Audit Committee Guidance Committee (ACGC) issues guidebook

Refer to our publication "*Summary of the Audit Committee Guidance Committee Guidelines*" for details

The ACGC was established on 15 January 2008 by the Monetary Authority of Singapore (MAS), ACRA and the SGX in an effort to promote and strengthen good corporate governance practices of listed companies in Singapore.

On 30 October 2008, the ACGC released the ACGC guidebook which provided greater direction and practical guidance to audit committees in the following key areas:

- (1) Audit committee composition; and
- (2) Roles and responsibilities of an audit committee (AC)
 - Internal controls
 - Risk management
 - Internal audit
 - Financial reporting
 - External audit
 - Other duties and responsibilities

The guidebook was developed with extensive industry input, sought through dialogue sessions, focus groups and a survey of audit committee members. In addition to the 'frequently asked questions' section which is featured throughout the various sections in the guidebook, it also incorporates case studies, and appendices of sample templates and other detailed guidance notes, drawing from useful real-life examples.

The guidebook is not a new rulebook and does not prescribe additional standards. However, it can be expected that audit committees will increasingly discharge their duties and responsibilities in line with the practical guidance of good corporate governance given in the guidebook. This will effectively raise the bar on corporate governance best practices for ACs in Singapore.

To support ACs in Singapore, KPMG has launched the KPMG Audit Committee Institute (ACI). The ACI in Singapore is an extension of KPMG's Global ACI network, established in over 28 countries worldwide. The primary objective of the ACI is to share "best and good practices" in the business community and how best AC members can work effectively in discharging their responsibilities.

The ACI's initiatives will include roundtables or forum discussions, chair forums, and educational seminars, publications, and periodic distribution of time-sensitive information. Refer to the website www.kpmg.com.sg/aci for details.

SGX introduces new rules on "Watch-List"

Effective: 1 March 2008

On 1 March 2008, the SGX's new rules on the "Watch-List", as set out in the new Part V of Chapter 13 of the SGX-ST Listing Manual came into effect. The "Watch-List" aims to encourage market transparency by alerting investors to the financial developments of listed companies on the Mainboard which have been placed on the Watch-List.

Listed companies will be placed on the "Watch-list" if they:

- a. Register pre-tax losses for three consecutive financial years; and
- b. Have an average daily market capitalisation of less than S\$40 million over the last 120 market days.

Rule 1312 of the Listing Manual further provides that a Listed Company must immediately announce this fact upon recording a pre-tax loss for the third consecutive financial year.

Trading in the "Watch-List" companies will continue as usual. However, companies that do not satisfy the criteria for removal from the "Watch-List" within 24 months will face delisting from the SGX. The SGX will review the "Watch-List" every quarter.

SGX issues consultation paper on proposed amendments to the listing rules

Comment closed: 7 August 2008

In July 2008, the SGX issued a consultation paper on the proposed amendments to the Listing Rules. The proposed changes arise from one of the more extensive annual rule reviews, and focus on two primary areas:

- (1) Widening the range of companies and product types listed on the SGX; and
- (2) Changes to existing rules to enable better disclosure.

Key proposals to enhance disclosure of material information include:

- (a) Requiring an issuer which has been granted a rule waiver by the SGX to **announce the details of such waiver granted**, the reasons for seeking the waiver and the conditions (if any) imposed by the Exchange;
- (b) Requiring an issuer which intends to **issue shares, company warrants or other convertible securities for cash to disclose the types of investors** being targeted or excluded. In addition, the issuer will be required to disclose the percentage of placement proceeds allocated for each stated use; and
- (c) Requiring disclosure of **additional information where an issuer intends to acquire businesses or assets where profit guarantees are provided** by the vendor.

SGX has yet to issue the final amendments to the listing rules resulting from the consultation exercise.

Changes to Singapore Income Tax

Refer to KPMG Tax Special (February 2008) and KPMG publication – Budget 2008 for details

On 15 February 2008, changes to income tax matters were announced during the 2008 Budget Speech. These changes are summarised in the KPMG Tax Special published in February 2008. However, they are not expected to have a significant impact on the accounting for current and deferred tax for most entities.

Proposed new business vehicle – Limited Partnership

Proposed new business vehicle – Limited Partnership

On 18 November 2008, the Limited Partnerships Bill 2008 (the Bill) was tabled in Parliament and read for the second time. The Bill seeks to introduce a new business structure called the Limited Partnership.

A limited partnership (LP) is a structure consisting of at least one general partner and one limited partner. A general partner has management control and is liable for all debts and obligations of the LP incurred. A limited partner will only be liable for the debts and obligations of the LP up to the amount of his agreed contribution, but cannot participate in management. An individual or a corporation may be a general partner.

The LP is expected to be an attractive structure for persons who wish to conduct business as investors but do not wish to take an active role in the management of the business, and would prefer to entrust the management of the business to persons who have the sufficient confidence to assume unlimited liability. The LP structure is more often suitable for private equity and investment fund businesses.

Filing of Financial Statements in XBRL

Background

Refer to *Financial Reporting Matters – December 2007 and June 2008* for details

Developments on eXtensible Business Reporting Language (XBRL)

For filings performed on or after 1 November 2007, most Singapore incorporated companies are required to file their financial statements in XBRL under the two filing options below:

Option A – Full XBRL: Filing the entire set of financial statements in XBRL format;

Option B – Partial XBRL: Filing only the balance sheet, income statement and certain information (denoted by a red asterisk) in XBRL format. If a company adopts this option, it must also file a PDF copy of its financial statements.

Entities which are exempted from filing XBRL financial statements (excluded categories) can continue with the old practice of filing a PDF copy of the audited financial statements approved at the Annual General Meeting (AGM).

Extension of filing options and waiver of penalties

On 29 October 2008, ACRA announced that all filing options, including Option B, will continue to be available until further notice. For non-listed companies filing under Option A, ACRA is continuing to extend the deadline, without imposing penalty charges, to one month from:

- The time the full XBRL financial statements are presented at the AGM; or
- The date the Annual Return is required by law to be filed.

Changes to Option A from 29 October 2008

Effective 29 October 2008, and to encourage more companies to prepare and file under Option A, companies are no longer required to table the Full XBRL financial statements prepared using FS Manager at the AGM when they opt to file under Option A. This is allowed provided that the set of financial statements tabled at the AGM is **identical in content** to the Full XBRL set of financial statements.

ACRA takes the view that "**identical in content**" includes the following scenarios:

- (1) The financial terminologies used in the AGM copy of the financial statements are identical with the ACRA Taxonomy data elements terminologies (e.g. Property, Plant and Equipment, Total);
- (2) The financial statements presented at the AGM is identical to the PDF copy of the Full XBRL financial statements prepared subsequently using FS Manager.

Implementation issues in the second year

As highlighted in Financial Reporting Matters in June 2008, there are many implementation issues when using FS Manager to prepare XBRL financial statements. Many of these issues are still applicable. In addition, we have also identified some other practical issues arising in the second year of implementation:

- Rolling forward of prior period's balances
- Changing from Option B to Option A in the second year

Rolling forward of prior period's balances

Where a set of XBRL financial statements was filed in the first year of implementation, FS Manager is able to generate a new set of XBRL financial statements under the same filing option for the second year with the prior period's information populated.

However, this roll-forward option is only available to authorised users when they access FS Manager to create a new set of XBRL financial statements using their "SingPass" login on BizFile. Upon creation, they will be prompted to retrieve the information from the prior period's XBRL financial statements.

Suggested approach

Preparers should ensure that they **engage their authorised users to create and save a new set of XBRL financial statements in XML format** before they can proceed to input the information for the current financial year or period.

Changing from Option B to Option A in the second year

For the second year of implementation, some companies may decide on a change. They may decide to file under Option A instead of filing under Option B. Under Option A, the Full XBRL financial statements is required including comparative information.

Suggested approach

In addition to rolling-forward the prior period's XBRL financial statements, preparers need to key in the current period's information and all other required comparative information required under Option A.

Public consultation on 'Revisions to ACRA Taxonomy'

Comment closed: 12 December 2008

The ASC has adopted the revised FRS 1, which is applicable to companies and effective for annual periods beginning on or after 1 January 2009, with early adoption permitted. This will affect the format and content of the primary financial statements to be filed in Singapore.

On 13 October 2008, ACRA launched a consultation paper to gather views on:

- The revisions to the current ACRA taxonomy to incorporate the revised FRS 1 requirements; and
- The possible revisions to the preparation and filing requirements for financial statements in XBRL in Singapore.

C. Overview of 2008 Changes in Financial Reporting Standards

We have approached the end of the three-year 'stable period' where the IASB announced that it will not require the application of new IFRS under development or major amendments to existing standards before 1 January 2009.

As of 12 December 2008, *seven* new or revised FRSs and *two* interpretations have been issued. These will be effective on or after 1 January 2009.

Companies in Singapore need to look beyond financial reporting standards which are already effective since they need to prepare for the implementation of many new and revised FRSs that will come into effect in 2009. We summarise the new and revised FRSs and their interpretations below.

New FRSs effective for annual financial periods beginning from 1 January 2008

FRS 107 *Financial Instruments: Disclosures* and Amendments to FRS 1 *Presentation of Financial Statements – Capital Disclosures*

Effective: Annual periods beginning from 1 January 2007 (listed companies) and 1 January 2008 (all other companies)

Refer to *Financial Reporting Matters – April 2006* and September 2007 for details

FRS 107 will apply to common financial instruments, including cash, trade receivables and payables, and borrowings. Examples of the risks associated with these financial instruments are:

- Credit risk from trade receivables;
- Liquidity risk arising from the ability to pay trade payables; and
- Market risks, such as interest rate risk from floating rate borrowings and foreign currency exchange rate risk from trade receivables and payables.

FRS 107 has introduced some new disclosures – in particular, sensitivity analysis for market risk to which a company is exposed at the balance sheet date. KPMG in Singapore recently posted the *Singapore Illustrative Financial Statements 2008* on its website which incorporates example disclosures required by FRS 107, as well as other changes for financial year 2008.

Amendments to FRS 39 and FRS 107 – *Reclassification of Financial Assets*

Effective: 1 July 2008

Refer to *Financial Reporting Matters November 2008 – Credit Crisis Special Report* and IFRS Briefing Sheet – Issue 113 for details

On 13 October 2008, the IASB issued amendments to IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 7 *Financial Instruments: Disclosures*. The amendments permit reclassification of certain financial assets to allow the financial assets can be measured at amortised cost, rather than at fair value. The disclosure requirements imposed are quite onerous and will be applied until the instruments are derecognised. Subsequent to reclassification, the usual impairment loss tests will be applied.

ASC has issued the equivalent amendments in Singapore on 30 October 2008 with the same effective dates and transition requirements.

The amendments are applicable on or after July 2008 and no reclassification should be applied retrospectively before July 2008. For reclassifications made on or after November 2008, it should take effect only from the date the reclassification is made.

The amendments mainly deal with reclassifications of:

- Loans and receivables: to be reclassified from the 'held for trading' or 'available for sale' categories if the entity has the intent and ability to hold the financial asset for the foreseeable future.
- Other financial assets: to allow non-derivative financial assets classified as held for trading to be reclassified in rare circumstances.

The amended standards do not define rare circumstances but the IASB notes in the accompanying Basis for Conclusions that "*rare circumstances arise from a single event that is unusual and highly unlikely to recur in the near term.*" An accompanying IASB press release stated that "*the deterioration of the world's financial markets that has occurred during the third quarter of this year is a possible example of rare circumstances cited in these IFRS amendments and therefore justifies its immediate publication*".

INT FRS 111 FRS 102 Group and Treasury Share Transactions

Effective: Annual periods beginning from 1 March 2007

Refer to *IFRS Briefing Sheet* - Issue 57 for details.

One potential change from the current practice arising from INT FRS 111 is when a subsidiary grants rights to equity instruments (for example, share options) of any of its parents to its own employees. In such a situation, INT FRS 111 would require the subsidiary to account for the transaction as a cash-settled arrangement. Currently, such a transaction could be classified as equity-settled or cash-settled arrangement, depending on the subsidiary's accounting policy.

Such a transaction is classified as cash-settled irrespective of how the subsidiary obtains the equity instruments to satisfy its obligations to employees (e.g. by entering into an agreement with the parent company to provide the shares). This is a separate transaction from its transactions with employees.

INT FRS 112 Service Concession Arrangements

Effective: Annual periods beginning from 1 January 2008

Refer to *IFRS Briefing Sheet* - Issue 59 for details.

Service concession arrangements are arrangements whereby a government or other body grants contracts for the supply of public services - such as roads, energy distribution, prisons or hospitals - to private operators.

This interpretation covers public-to-private service concession arrangements in which the public sector controls or regulates the services provided with the infrastructure and their prices, and controls any significant residual interest in the infrastructure.

The main change from the current practice is that the private operator would not recognise any property, plant or equipment throughout the life of the arrangement. Instead, the operator recognises an intangible asset if its right to receive cash is dependent upon usage of the infrastructure, or a financial asset if its right to receive cash is not so dependent.

INT FRS 114 FRS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirement and their Interaction

Effective: Annual periods beginning from 1 January 2008

Refer to *IFRS Briefing Sheet* - Issue 71 for details.

This interpretation clarifies when refunds or reductions in future contributions in relation to defined benefit assets should be regarded as available, and provides guidance on the impact of minimum funding requirements (MFR) on such assets. It also addresses when a MFR might give rise to a liability.

This interpretation is not expected to apply to most of the Singapore companies providing post-employment benefits solely under a defined contribution scheme, such as the Central Provident Fund Scheme.

New FRSs effective for annual financial periods beginning from 1 January 2009

Revised FRS 1 *Presentation of Financial Statements*

Effective: Annual periods beginning from 1 January 2009

Refer to *Financial Reporting Matters* – September 2008 for details.

This revised FRS 1 supercedes the current version of FRS 1 and introduces 'total comprehensive income' (changes in equity during a period, other than those changes resulting from transactions with owners in their capacity as owners).

Another significant change is that an opening statement of financial position (formerly the balance sheet) is required at the beginning of the earliest comparative period following a change in accounting policy, the correction of an error or the reclassification of items in the financial statements. Accordingly, an entity is likely to be required to present its balance sheets for three years, instead of the current two years, when many new or revised standards come into effect from 1 January 2009.

FRS 23 (revised) *Borrowing Costs*

Effective: Annual periods beginning from 1 January 2009

Refer to *Financial Reporting Matters* – March 2008 for details

The revised standard requires that an entity capitalises borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the total cost of that asset. It also removes the option for immediately recognising all borrowing costs as an expense.

On first time adoption of the revised standard, the revision is to be applied prospectively from the effective date.

FRS 108 *Operating Segments*

Effective: Annual periods beginning from 1 January 2009

Refer to *Financial Reporting Matters* – March 2008 for details

FRS 108 replaces FRS 14 *Segment Reporting*. FRS 108 will require all entities within its scope to adopt the 'management approach' in reporting the financial performance of its operating segments, based on the same segment information as used by top management. Consequently, the segment information disclosed aims to provide the reader with insight into how top management manages the entity's operations.

FRS 108 also requires the amount of each segment item reported to be the measure which is reported internally. This is irrespective of the basis of preparation for the financial statements.

This 'management approach' differs from FRS 14, which currently requires the disclosure of two sets of segments, based on a disaggregation of information contained in the financial statements.

Improvements to FRSs for 2008

Effective: Generally for annual periods beginning from 1 January 2009

Refer to Section D of this publication for details

Improvements to FRSs for 2008 contains 35 amendments to 20 FRSs involving non-urgent but necessary amendments to FRSs. The improvements focus on areas of inconsistency in FRSs or where clarification of wording is required. It is divided into two parts:

Part I: Includes 24 amendments that result in accounting changes for presentation, recognition or measurement purposes.

Part II: Includes 11 terminology or editorial amendments that are expected to have either no or only minimal effects on accounting.

Amendments to FRS 101 *First-time Adoption of Financial Reporting Standards, and FRS 27 Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*

Effective: Annual periods beginning from 1 January 2009

Refer to Section E of this publication for details.

The amendments to FRS 101 is not applicable to a Singapore entity which has always been applying FRS.

The amendments to FRS 27 relates to the company's separate financial statements, and:

1. Eliminates the requirement to distinguish between pre-acquisition and post-acquisition dividends; all dividends received from a subsidiary, jointly controlled entity or associate will be recognised as income.
2. Requires an investor to assess whether there is an indicator of impairment when dividend income is received.
3. Provides new guidance on determining the cost of investment on formation of a new parent in specific situations.

Amendments to FRS 102 *Share-based Payment – Vesting Conditions and Cancellations*

Effective: Annual periods beginning from 1 January 2009

Refer to *Financial Reporting Matters – September 2008* for details.

The original definition of vesting conditions in FRS 102 (2004) described them as including service and performance conditions. However, it was unclear how other conditions related to share-based payment arrangements should be treated.

Examples include:

- Requirement for an employee to contribute to an employee share purchase plan (ESPP).
- Requirement for an employee to hold shares of an entity for a specified period in order to be eligible for participation in a share-based payment grant.

In the amendments, conditions other than service or performance conditions, are considered as non-vesting conditions.

Non-vesting conditions must be taken into account in measuring the grant date fair value of the share-based payment. In addition, if employees fulfil the service conditions, then the entity will recognise the grant date fair value of the share-based payment. This is even if the employee does not become entitled to the share-based payment due to the failure to meet a non-vesting condition.

Amendments to FRS 32 and FRS 1 – *Puttable Financial Instruments and Obligations Arising on Liquidation*

Effective: Annual periods beginning from 1 January 2009

Refer to Section F of this publication for details.

The amendment allows certain instruments that would normally be classified as liabilities to be classified as equity if they meet certain conditions. The amendments cover two categories of instruments issued by an entity:

- A puttable financial instrument; or
- A financial instrument that is puttable only on liquidation.

The amendments define a 'puttable instrument' as "...a financial instrument that gives the holder the right to put the instrument back to the issuer for cash or another financial asset or is automatically put back to the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder."

Entities which are likely to be able to classify the units that they issue as equity includes real estate investment trusts, unit trusts, business trusts and investment funds.

FRS 39 *Financial Instruments: Recognition and Measurement (Issue of additional Application Guidance on Eligible Hedged Items)*

Effective: Annual periods beginning from 1 July 2009

Refer to IFRS Briefing Sheet – Issue 100 for details.

Additional Application Guidance has been issued to clarify how the existing principles underlying hedge accounting should be applied in two particular situations:

- (a) A one-sided risk in a hedged item, and
- (b) Inflation in a financial hedged item.

INT FRS 113 *Customer Loyalty Programmes*

Effective: Annual periods beginning from 1 July 2008

Refer to *Financial Reporting Matters* – June 2008 for details

This interpretation addresses the accounting for customer loyalty programme award credits granted as part of sales transactions. INT FRS 113 requires that customer loyalty programmes be accounted for by using a 'multi-element' approach. Under this approach, the consideration received from a sales transaction is separated into two identifiable components:

1. The goods or services delivered; and
2. The award credits which may be redeemed in the future

The portion allocated to the award credits is measured and based on the fair value of the points to the customer. It is deferred and recognised in income as and when the entity has fulfilled its obligations with respect to the redemption of the award credits.

INT FRS 116 *Hedges of a Net Investment in a Foreign Operation*

Effective: Annual periods beginning from 1 October 2008

Refer to Section G of this publication for details

INT FRS 116 applies to an entity which hedges the foreign currency risk arising from its net investments in foreign operations. For example, by taking out borrowings in the same currency as the functional currency of the foreign operation.

Key requirements of the interpretation are that it:

- Does not permit hedge accounting on foreign exchange differences arising between the functional currency of the foreign operation and the presentation currency of the parent entity's consolidated financial statements;
- Requires the foreign currency exposure resulting from the net investment in a foreign operation to be hedged only once in the consolidated financial statements; and
- Allows the hedging instrument to be held by any entity within the group, other than in the foreign operation that is being hedged.

Recently issued IFRSs not yet adopted in Singapore

IFRIC 15 *Agreements for the Construction of Real Estate*

Effective: Annual periods beginning from 1 January 2009

Refer to IFRS Briefing Sheet – Issue 97 for details.

Entities which undertake real estate development may enter into agreements with buyers before construction has been completed. IFRIC 15 provides guidance on when revenue should be recognised. IFRIC 15 requires *retrospective* application. Earlier application is permitted.

When IFRIC 15 is adopted in Singapore, real estate developers will need to determine whether contracts with customers are construction contracts (IAS 11), contracts for the rendering of services (IAS 18) or contracts for the sale of goods (IAS 18).

Contracts with periods of over one year to completion are likely to use either the 'Percentage of Completion' method or the 'Completion of Contract' method for revenue recognition. The main criteria is whether the contract transfers control and the significant risks and rewards of ownership continuously to the buyer or at a single point in time. The different types of agreements for construction which can exist, the different circumstances, and the different laws in Singapore will mean that each type of contract will need to be considered individually.

Revised standard IFRS 3 *Business Combinations* (2008) and amended standard IAS 27 *Consolidated and Separate Financial Statements* (2008)

Effective: Annual periods beginning from 1 July 2009

Refer to IFRS Briefing Sheet – Issue 81 for details.

IFRS 3 (2008) is the outcome of the second phase of the IASB and the FASB business combinations joint project. This phase reconsidered the application of acquisition accounting for business combinations.

The main changes from IFRS 3 (2004) are that the:

- Contingent consideration payable for the acquisition should be measured at fair value at the acquisition date.
- Acquirer can elect to measure any non-controlling interest (NCI, previously termed 'minority interest'):
 - at fair value at the acquisition date, or
 - at its proportionate interest in the fair value of the identifiable assets and liabilities of the acquiree (consistent with current treatment).
- Transaction costs incurred by the acquirer in connection with the business combination are expensed as incurred.

The main changes from IAS 27 (2003) are as follows:

- In a step acquisition, the identifiable assets and liabilities of the acquiree are recognised at fair value when control is obtained, with any adjustment recognised in profit or loss.
- Acquisitions of additional NCI after control is obtained, and disposals, of equity interests while retaining control are accounted for as equity transactions.
- A transaction resulting in a loss of control results in a gain or loss being recognised in profit or loss.

Singapore is expected to issue the interpretation with the same effective date.

IFRIC 17 *Distributions of Non-cash Assets to Owners*

Effective: Annual periods beginning from 1 July 2009

Refer to IFRS Briefing Sheet – Issue 115 for details

On 27 November 2008, IFRIC 17 was issued to standardise the accounting for distributions of non-cash assets to owners. Before IFRIC 17, such dividend payable could be recognised at the carrying amount or fair value of the assets to be distributed.

The interpretation clarifies that an entity should measure the dividend payable at the fair value of the net assets to be distributed, and recognise the difference between the dividend paid and the carrying amount of the net assets distributed in profit or loss.

Singapore is expected to issue the interpretation with the same effective date.

Public consultations of ASC

ASC's public consultation on differential reporting framework for Small and Medium Sized Entities (SMEs)

Deadline for public comment ended on 30 June 2008

All Singapore-incorporated companies, regardless of size or level of public interest in them, are currently required to prepare their financial statements in accordance with FRSs issued by the ASC.

Refer to Financial Reporting Matters – June 2008 for details

In May 2008, the ASC published a consultation paper which proposed to allow SMEs to adopt a simpler financial reporting framework.

The reporting framework proposed for SMEs in the consultation paper is the equivalent of the IFRS for Private Entities, which is expected to be issued by the IASB in the first quarter of 2009.

In the consultation paper, the taskforce proposes that a company would qualify as an SME if it satisfies two of the following three criteria:

- (1) Net assets do not exceed \$15 million
- (2) Annual turnover does not exceed \$15 million
- (3) The average number of employees does not exceed 200

The results of this consultation paper is expected to be important in deciding whether Singapore adopts the IFRS for Private Entities and the threshold for companies to apply this proposed standard.

ASC's public consultation on draft accounting and reporting requirements for Charities and Institutions of Public Character (IPC)

Deadline for public comment ended on 7 September 2008

In August 2008, ASC published a consultation paper to gather views on the draft accounting proposals and reporting requirements for charities. The proposals in the consultation are applicable to all charities and IPCs regardless of their legal constitution.

The main proposals in the consultation paper are:

- Large charities and large IPCs will be defined as those with annual income or expenditure exceeding \$10 million for two immediate preceding years.
- Large charities and large IPCs will be required to comply with all FRSs except FRS 1. FRS 1 will be substituted by the presentation format proposed in Annex B to the consultation paper.
- Non-Large charities and non-large IPCs will be required to follow simplified Charity Accounting Standards to be developed by the Committee for Charities.
- All charities and IPCs will be required to disclose additional pertinent information in their annual reports such as the structure, governance and management of the charity, its achievements and performance, its reserves management policy, its investment policy and details of funds held on behalf of others.

D. Improvements to FRSs

In October 2008, the ASC issued the *Improvements to FRSs for 2008*. It is Singapore's equivalent of the IASB's *Improvement to IFRSs for 2008*.

The IASB adopted an annual process to deal with non-urgent but necessary amendments to IFRSs (the 'annual improvements project'). *Improvements to IFRSs for 2008* is the result of its first annual improvements project. It consists of amendments to IFRSs focusing on areas of inconsistency in IFRSs or where clarification of wording was needed. Improvements are accumulated throughout the year and processed collectively annually in a single publication.

Generally, the amendments are effective beginning on or after 1 January 2009, with one exception, which will be effective 1 July 2009. Different transitional provisions will apply when companies will adopt the amendments.

Improvements to FRSs for 2008 contains 35 amendments to 20 standards and is divided into two parts:

- **Part I:** Includes 24 amendments that result in accounting changes for presentation, recognition or measurement purposes; and
- **Part II:** Includes 11 terminology or editorial amendments which the IASB expects to have either no or only minimal effects on accounting.

In this section of the publication, we discuss certain key amendments within Part I of the *Improvements to FRSs for 2008* that we considered to have more significant impact and wider relevance.

Please refer to *IFRS Briefing Sheet Issue 94* for a full summary on all 35 amendments.

FRS 105 *Non-current Assets Held for Sale and Discontinued Operations*

- Plan to sell the controlling interest in a subsidiary

The amendment:

If an entity is committed to a sale plan involving the loss of control of a subsidiary, then it would classify all of that subsidiary's assets and liabilities as held for sale, subject to meeting the criteria in FRS 105.

Reason for the amendment:

The loss of control of a subsidiary is considered to be a significant economic event that changes the nature of an investment from parent-subsidiary to investor-investee relationship.

Potential accounting implication:

This amendment includes transactions where there is a partial disposal of the subsidiary and where a non-controlling interest is retained by the entity.

For example, if an entity announces the disposal of 70 percent of its interest in a wholly-owned subsidiary, all the assets and liabilities of the subsidiary would be classified and accounted for as a disposal group held for sale, and FRS 105 would apply from the time the criteria are met up to the actual disposal of the 70 percent interest.

FRS 1 *Presentation of Financial Statements*

- Current / non-current classification of derivatives

The amendment:

FRS 1 was clarified to indicate that derivatives which are held primarily for trading should be presented as current regardless of its maturity date. Derivatives which are not held for trading purposes should be presented as current or non-current on the basis of its settlement.

Reason for the amendment:

Previously, FRS 1 seemed to imply that all derivatives classified as held for trading under FRS 39 had to be classified as current, even though they are not held for the purpose of trading.

Potential accounting implication:

An entity needs to consider the terms and intention of derivatives held, in order to classify them appropriately as current or non-current.

For example, an entity holds a foreign exchange contract, and the terms of the contract requires gross-settlement in two years time. The entity did not designate the foreign exchange contract as a hedging instruments for purpose of applying hedge accounting under FRS 39. The entity expects to hold the contract until the settlement date. The fair value of the foreign exchange contracts would therefore be classified as non-current.

FRS 16 *Property, Plant and Equipment*

- Sale of assets held for rental

The amendment:

For assets which are rented and then subsequently sold on a routine basis, the proceeds from the sale of such assets would be recognised as revenue in the ordinary course of business. Such assets would be transferred to inventories at their carrying amount when they cease to be rented and are to be sold.

In the cash flow statements, cash flows to acquire or manufacture such assets and the cash receipts from the renting and subsequent sale of such assets are cash flows from operating activities.

Reason for the amendment:

Previously, all entities are prohibited from recognising the proceeds from sale of property, plant and equipments as part of revenue. Instead, only the net gain/loss is recognised in 'other income'.

Potential accounting implication:

The change only applies to entities whose business model is to rent the assets and then sell those assets in the course of ordinary activities with the sales occurring on a regular basis. Industries that may be affected include car rental, aircraft manufacturing, heavy equipment, shipping and the property industry.

An entity should determine whether if the rental and subsequent sale of the rental assets are part of its ordinary activities before applying the amendments. Factors that could be considered include:

- The business model of the entity relies on leasing and selling the assets,
- A structure is in place to facilitate the sales; and
- An active market exists for the second-hand assets.

FRS 20 Accounting for Government Grants and Disclosure of Government Assistance

- Government loans with a below-market rate of interest

The amendment:

FRS 20 clarifies that the benefit of a loan with a below-market rate of interest received from a government is treated as government grant and is recognised and measured in accordance with FRS 39.

Reason for the amendment:

Previously, FRS 20 did not require interest to be imputed on low or interest-free loans from government although FRS 39 required that all financial instruments are measured at fair value at initial recognition. FRS 20 was not consistent with FRS 39 in this respect.

Potential accounting implication:

In Singapore, the government agency SPRING offers a Local Enterprise Finance Scheme (LEFS) mainly to SMEs, where the SMEs can enjoy easier access to funds at a lower interest rate.

An entity which receives loan under such scheme would need to account for the difference between the amount received from the government and the fair value of the liability as a government grant. Thus, the income would be recognised on a systematic basis, using the effective interest method, generally over the period of the loan.

FRS 28 Investment in Associates

- Impairment of investment in associates

The amendment:

FRS 28 was amended to clarify that:

- An impairment loss on an investment in an associate is not allocated to any asset, including goodwill, which forms part of the carrying amount of the investment in the associate; and
- Any reversal of a previously recognised impairment loss is recognised to the extent that the recoverable amount of the investment in the associate subsequently increases.

Reason for the amendment:

Before the amendment, it was unclear whether impairment losses against an investment in associate is required to be allocated to the underlying assets, including goodwill. It was also unclear whether those impairment losses recognised could be reversed subsequently when the recoverable amount increases. FRS 36 *Impairment of Assets* prohibits reversal of impairment loss recognised for goodwill.

Potential accounting implication:

In situations where an entity had recognised impairment losses on its investments in associates, the impairment loss can be reversed in subsequent reporting periods when there is a change in the estimates used that resulted in an increase in the recoverable amount.

The amount of reversal need not consider the goodwill element arising on acquisition of the investment in associates.

FRS 38 *Intangible Assets*

- Advertising and promotional activities

The amendment:

FRS 38 was amended to clarify the meaning of “recognising expense when incurred” for advertising and promotional activities. An expense is recognised when the entity has the right to access those goods in the case of goods and when the entity receives those services in the case of services.

The amendment also clarifies that catalogues are considered to be a form of advertising and promotional activities.

Reason for the amendment:

It was unclear when expenditure on advertising and promotional activities should be recognised. Some believed that such expense should be recognised when the entity receives the goods or services that it would be used to develop or communicate the advertisement or promotion. Others believed that an entity should recognise an expense when the advertisement or promotion was delivered to its customers or potential customers.

Potential accounting implication:

For example, an entity spent \$2 million on a new advertising campaign promoting its new brand, new look and new service. The advertising firm delivered the print and television advertisements to the entity on 15 December 2008. These advertisements will be printed and aired in 2009.

The advertising and promotion expense would be recognised in 2008, when the entity has access to the related goods and services relating to the print and television advertisements.

FRS 40 *Investment Property*

- Property under construction or development for future use as investment property

The amendment:

FRS 40 was amended to include property under construction or development for future use as investment property in its definition of ‘investment property’.

In addition, if an entity’s policy is to measure investment property at fair value, but the entity is unable to reliably measure its fair value during the construction or development stage, then the entity would be permitted to measure the investment property at cost until construction or development is completed.

Reason for the amendment:

Previously, a property acquired for construction or development for future use as an investment property was accounted for under FRS 16 *Property, Plant and Equipment*. This treatment is inconsistent with an existing investment property that is being redeveloped, which remained to be accounted for in FRS 40 *Investment Property*.

Potential accounting implication:

An entity purchasing a property for construction or redevelopment for future use as an investment property would account for the property as follows:

- Fair value gains on the property under construction would now be reflected in profit or loss, rather than directly in equity, and
- The entity would not be able to defer fair value gains on investment property under construction until completion by adopting a cost policy for investment property under construction, and a fair value policy for investment property. Instead, if a fair value policy was adopted for investment property, only investment property under construction for which fair value could not be reliably measured would be measured at cost.

E. Amendments to FRS 101 *First-time Adoption of Financial Reporting Standards* and FRS 27 *Consolidated and Separate Financial Statements – Cost of Investment in a Subsidiary, Jointly-controlled entity and Associates*

In October 2008, the ASC issued the amendments to FRS 101 *First-time Adoption of Financial Reporting Standards* and FRS 27 *Consolidated and Separate Financial Statements*.

FRS 101 applies only to the financial statements of an entity in the first year of adoption of FRSs. So far as existing preparers under FRSs are concerned, the amendments to FRS 101 would not be relevant. Therefore, we will only discuss the amendments to FRS 27 in this section of the *Financial Reporting Matters*.

What is the scope of the amendments?

When preparing separate (i.e. 'company-level') financial statements, entities are allowed to make an accounting policy choice under FRS 27 to measure the investments in subsidiaries, jointly-controlled entities and associates:

- At cost (less impairment, if any); or
- At fair value in accordance with FRS 39

Typically, entities choose the cost method as it is a simpler method. There are two amendments to FRS 27 and these amendments apply only when an investor has chosen to measure the investments at cost.

Amended FRS 27 allows all dividends received to be recognised as income.

The **first amendment to FRS 27** is the elimination of the current requirement to distinguish between dividends which come from the investee's pre-acquisition profits and those which come from the investee's post-acquisition profits.

After the amendments, all dividends received from a subsidiary, jointly controlled entity or associate will be recognised as income.

To reduce the concern that this full income recognition approach could lead to the over-statement of the investment balance, FRS 36 *Impairment of assets* has been amended to require an investor to assess whether there is an indicator of impairment when dividend income is received.

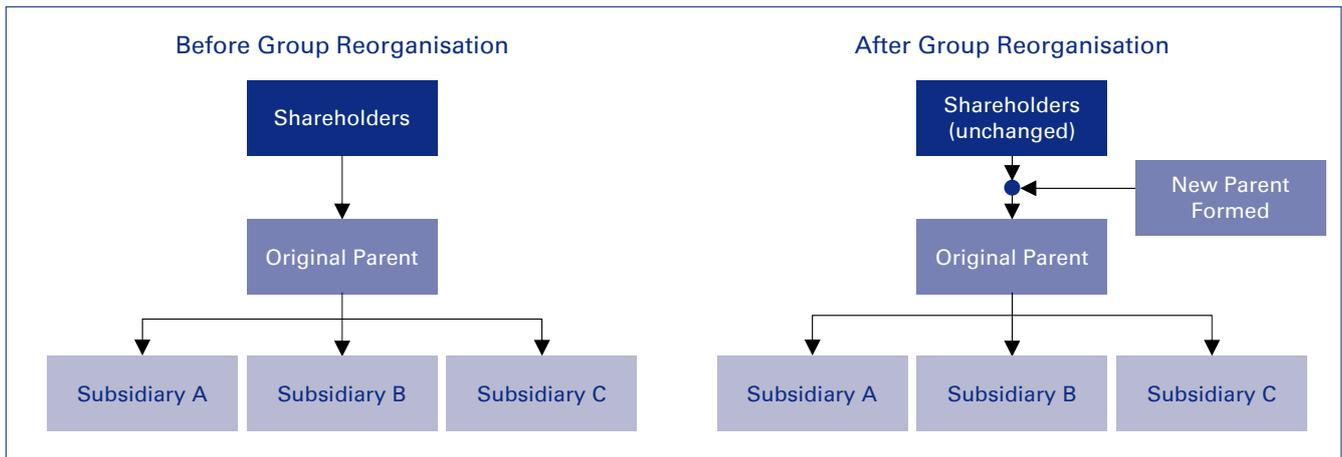
The receipt of dividend income is deemed to be an indicator of impairment when either:

- The carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial statements of the investee's net assets (including any goodwill); or
- The dividend exceeds the total comprehensive income of the subsidiary, jointly controlled entity or associate in the period that the dividend is declared.

In situations where the investment is assessed to be impaired, dividends received should still be presented as a gross amount with any associated impairment loss presented separately.

Amended FRS 27 provides guidance on the cost of investment to be recorded in a newly formed parent.

The **second amendment to FRS 27** provides new guidance on determining the cost of investment on the formation of a new parent in the following structure, provided the reorganisation meets certain conditions.



The conditions which need to be met are:

- The new parent entity issues equity instruments as consideration in the reorganisation;
- There is no change in the group's assets or liabilities as a result of the reorganisation; and
- There is no change in the interest of the shareholder, either absolute or relative to one another, as a result of the reorganisation.

If the reorganisation meets the conditions specified above, the cost of investment of the new parent's investment in the original parent should be measured based on its share of the carrying value of the original parent's equity shown in the separate financial statements of the original parent at the date of the reorganisation.

The above guidance is also applicable if the new parent acquires the shares of an entity which is not a parent (i.e. it does not have any subsidiaries). In such cases, all references above to the acquired 'original parent' should be read as being to the acquired 'original entity'.

What is the effective date and what are the transitional provisions?

The two amendments to FRS 27 are effective for annual periods beginning on or after 1 January 2009. Earlier application is permitted.

The first amendment to FRS 27 concerning dividend recognition should be applied prospectively.

The second amendment to FRS 27 concerning the formation of a new parent in a group reorganisation may be applied prospectively or retrospectively.

If an entity applies the requirements for the formation of a new parent prior to the effective date, then all later such reorganisations should be restated.

- The only identical feature required is the obligation for the issuing entity to deliver to the holder a pro-rata share of its net assets on liquidation
- If a component of an instrument puttable *only* on liquidation meets the definition of a liability (other than the right on liquidation), the component will be recognised separately as a financial liability. The instrument will be presented as a compound financial instrument (e.g. *ordinary shares issued by a 100 years life entity with fixed non-discretionary dividends for the first five years after issuance would be presented as a compound financial instrument*).
- Any cash flows paid to the holder during the life of the instrument will reduce the amount ultimately payable on liquidation.

F. Amendments to FRS 32 *Financial Instruments: Presentation and FRS 1 Presentation of Financial Statements - Puttable Financial Instruments and Obligations Arising on Liquidation*

Why was FRS 32 amended?

All entities require some form of long-term financing. Sources of financing typically come from issuance of shares and bonds or bank borrowings.

FRS 32 *Financial Instruments: Presentation* requires long-term financing received by an entity to be classified as equity or liability.

The general principle under FRS 32 is that if an entity cannot avoid repayment of the financing received, the instrument will be classified as liability.

Ordinary members' contributions ('ordinary shares') are generally classified as equity. However, under FRS 32 some entities classify their ordinary shares as liabilities.

There are two broad reasons for such liability classification:

1. Entities such as co-operatives, partnerships or investment funds, might be required by law to redeem the ordinary shares issued if the holders of such instruments request for redemption. These types of shares are usually issued by unlisted entities to provide a liquidity mechanism for the holders.
2. Some entities may be required to be liquidated after a fixed period of time in accordance with the law or their constituting documents. They are commonly referred to as limited life entities.

These ordinary shares are known as puttable financial instruments and are currently classified as liabilities as the issuing entities cannot avoid redemption of the shares.

In the case of a limited life entity, redemption is in fact, certain to occur.

The liability classification applies even if the shares belong to a class of instruments which are subordinated to all other classes of instruments issued by the entity and represent the residual claim to the net assets of the entity (*on liquidation, the shareholders are paid only after all other creditors are paid*).

The FRS 32 classification rules do not reflect economic reality because the holders are in fact the owners of the entity but they are reflected as creditors. Hence, the amendments were made.

Amended FRS 32 allows equity classification for the most subordinated class of puttable financial instruments if specified conditions are met

In August 2008, the ASC issued the amendments to FRS 32 to provide conditional exemption from the liability classification for the following two types of financial instruments:

1. Financial instruments puttable before liquidation; and
2. Obligations arising on liquidation (*financial instruments puttable only on liquidation*).

The amendments to FRS 32 are very much rule-based and a short-term solution to the issue and therefore:

- The amendments *cannot* be applied by analogy to other instruments; and
- The exemption should only be applied when accounting for instruments under FRS 1 *Presentation of Financial Statements*, FRS 32, FRS 39 *Financial Instruments: Recognition and Measurement* and FRS 107 *Financial Instruments: Disclosures*. Consequently, the scope exemption should not be applied when accounting for instruments under other FRSs (e.g. under FRS 102 *Share-based Payment*).

Which entities will be affected?

The amendments will only be relevant to entities whose ordinary members' contributions are currently classified as liabilities (*some co-operatives, partnerships, business trusts, unit trusts, real estate investment trusts and investment funds*) because only the most subordinated class of puttable financial instruments are eligible for the exemption.

The amendments will not be relevant to companies incorporated under the Companies Act as their ordinary share capital, which represent the most subordinated interest in these companies, are already classified as equity.

What are the specified conditions?

The table below summarises the specified conditions that must be met for puttable financial instruments to be classified as equity:

	Conditions	Puttable before liquidation	Puttable <i>only</i> on liquidation
i	The holder is entitled to a pro rata share of the entity's net assets in the event of the entity's liquidation.	✓	✓
ii	The instrument belongs to the most subordinated class of instruments issued by the entity.	✓	✓
iii	All financial instruments in this most subordinated class of instruments have identical features.	✓ <i>(none of the instrument holders in that class can have preferential terms or conditions)</i>	✓ (Note a)
iv	The instrument must not have any other characteristic that would meet the definition of a financial liability other than the put option.	✓ <i>(ordinary shares puttable throughout its life at fair value with fixed non-discretionary dividends will fail this criteria)</i>	Not applicable (Note b)
v	The total expected cash flows attributable to the instrument over its life should be based substantially on: - the profit or loss; - the change in the recognised net assets; or - the change in the fair value of the recognised and unrecognised net assets of the entity. <i>(Profit or loss and the change in recognised net assets need to be measured in accordance with FRSs.)</i>	✓	Not applicable (Note c)

- (a) The only identical feature required is the obligation for the issuing entity to deliver to the holder a pro-rata share of its net assets on liquidation
- (b) If a component of an instrument puttable *only* on liquidation meets the definition of a liability (other than the right on liquidation), the component will be recognised separately as a financial liability. The instrument will be presented as a compound financial instrument (*e.g. ordinary shares issued by a 100 years life entity with fixed non-discretionary dividends for the first five years after issuance would be presented as a compound financial instrument*).
- (c) Any cash flows paid to the holder during the life of the instrument will reduce the amount ultimately payable on liquidation.

To ensure that the rights and obligations arising from the puttable financial instruments are substantive, the issuer must not have any other financial instrument or contract:

- That has a term equivalent to (v) above; and
- That has the effect of substantially restricting or fixing the residual return to the puttable financial instrument holders.

Amended FRS 32 requires continuous monitoring of the classification of puttable financial instruments

An entity should classify a puttable financial instrument as equity from the date the financial instrument and the issuing entity meet the specified conditions.

When an instrument is reclassified from financial liability to equity, the equity instrument is measured at the *carrying amount* of the financial liability at the date of reclassification.

Conversely, a puttable financial instrument should be reclassified from equity to liability from the date when either it or the capital structure of the issuing entity fails to meet all the specified conditions.

When an instrument is reclassified from equity to liability, the liability should be measured at the instrument's *fair value* (the present value of redemption value) at the date of reclassification.

Any difference between the carrying value of the equity instrument and the financial liability at the date of reclassification should be recognised in equity.

A change in the liability/equity classification of an instrument is usually triggered by issuance/redemption of a new/existing class of instruments that is subordinated to the existing instruments.

An entity has to continuously monitor the effect of an issuance of a new class of instruments and redemption of an existing class of instruments on the classification of the puttable financial instruments.

What are the disclosures requirements?

The disclosure requirements in FRS 107 will not apply to equity-classified puttable financial instruments. Instead, entities are required to provide the necessary disclosures under FRS 1.

FRS 1 has also been amended to introduce the following additional disclosure requirements specific to these instruments:

- If an entity has reclassified the instruments covered under these amendments between financial liabilities and equity, then the amount, the timing and the reason for the reclassification must be disclosed.
- For puttable instruments which are classified as equity instruments:
 - Summary quantitative data about the amount classified as equity;
 - The entity's objectives, policies and processes for managing its obligation to repurchase or redeem such instruments; and
 - The expected cash outflow on redemption or repurchase and how this amount was determined.
- For a limited life entity, information regarding the length of its life.

When is an entity required to apply the amendments?

The amendments outlined above are effective for annual periods beginning on or after 1 January 2009. Early adoption is permitted.

Entities are required to restate comparatives of the earliest prior periods presented in the financial statements as the amendments are to be applied retrospectively.

A limited transitional relief is available where entities are not required to retrospectively split a compound instrument, when the liability component is no longer outstanding.

G. INT FRS 116 *Hedges of a Net Investment in a Foreign Operation*

What is a hedge of a net investment in a foreign operation?

Many companies carry out activities in foreign countries by setting up a branch or a subsidiary, investing in an associate or entering into joint ventures with foreign partners.

Under FRS 21 *The effects of changes in foreign exchange rates*, these are known as foreign operations.

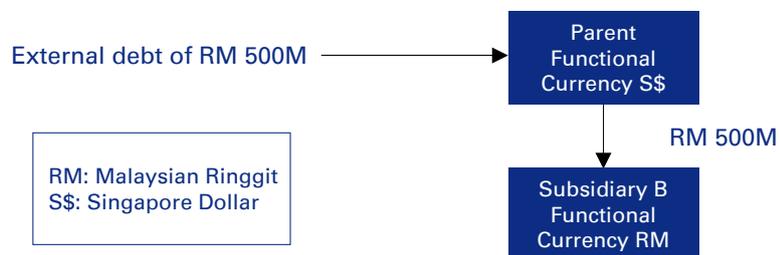
Investments in foreign operations will give rise to foreign currency exposures within the group.

Many groups often seek to hedge such risks by using financial instruments. For example, by taking out borrowings in the same currency as the functional currency of the foreign operation.

If the special rules on hedge accounting under FRS 39 *Financial Instruments: Recognition and Measurement* were not in place, the hedging relationship will not be portrayed in the consolidated financial statements of the group prepared using the normal accounting rules.

Let us look at the example below:

The group structure consists of a parent company (Parent) and a wholly-owned subsidiary B. Each entity has a different functional currency. The monetary amount shown represents the net investment in respect of B. Parent presents its consolidated financial statements in S\$.



Under FRS 21, B's net assets are translated at the closing exchange rate and the exchange difference arising from translating the net assets at the closing exchange rate versus the exchange rate at the beginning of the period is recorded in other comprehensive income (*in the Foreign Currency Translation Reserve or FCTR*) in the consolidated financial statements of the Parent.

The FCTR is reclassified to profit or loss on disposal of B.

The external debt, being a foreign currency monetary liability, is also translated at closing exchange rate under the requirements of FRS 21. However, the exchange difference arising on translation of the debt is recorded in profit or loss.

Although Parent is effectively hedged against any adverse movement in RM against S\$ (*the exchange difference arising from the foreign currency debt will offset the exchange difference arising from the net investment in B*), this hedging relationship is not reflected in the financial statements which follow the normal accounting rules.

Existing hedge accounting rules are set out in FRS 39. These rules give an entity the choice to reflecting the hedging relationship in the financial statements in which the net assets of the foreign operation are included. This can be by way of consolidation, proportionate consolidation and equity method accounting ('net investment hedging model').

To qualify for hedge accounting, Parent must ensure that:

- The hedging relationship is documented at inception;
- The hedge is expected to be highly effective;
- Effectiveness must be reliably measurable; and
- The hedge must remain highly effective during the whole period of the hedge.

To achieve hedge effectiveness:

- The foreign currency debt and the net investment should be denominated in the same currency or denominated in currencies that move in correlation with each other; and
- The exchange difference arising from the foreign currency debt can offset the exchange difference arising from the net investment within a range of 80 percent to 125 percent.

In the above example, if Parent applies the *net investment hedging model* under FRS 39 in its consolidated financial statements, the exchange difference arising on translation of the foreign currency debt would be reversed to FCTR if the hedging relationship is effective.

The cumulative amount of exchange differences on the foreign currency debt deferred in FCTR would be reclassified to profit or loss only on disposal of B.

What are the practical issues?

FRS 39 contains very little guidance on accounting for a net investment hedge. In practice, many issues arise and there is diversity and uncertainty in practice.

In September 2008, ASC issued INT FRS 116 *Hedges of a Net Investment in a Foreign Operation* to provide clarity on the following questions:

(i) What is the hedged risk?

- Is the hedged risk the difference between the functional currency of the foreign operation and
 - The functional currency of the parent entity; or
 - Also the presentation currency of the group?
- If the parent holds the foreign operation through intermediate holding entities, does the hedged risk include:
 - Only the difference between functional currency of the foreign operation and the functional currency of the immediate holding entity; or
 - Also the differences between functional currency of the foreign operation and the functional currency of the ultimate holding entity/other intermediate holding entities?

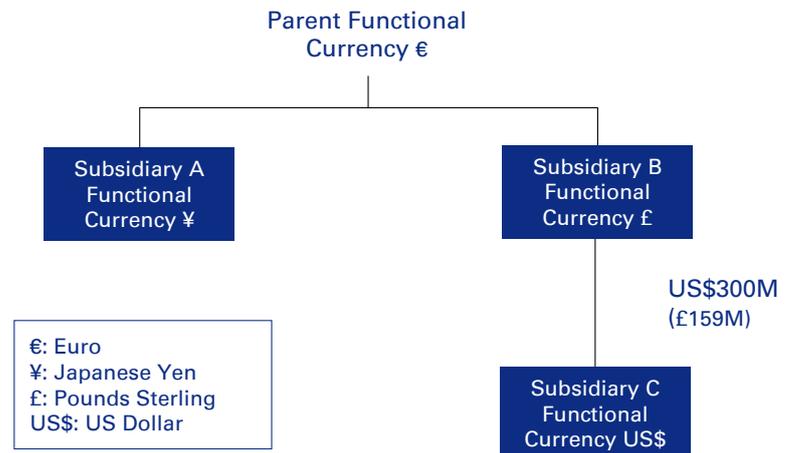
(ii) Which entity within a group can hold the hedging instrument (for example, a foreign currency loan) if hedge accounting is to be applied?

(iv) If the entity holding the hedging instrument has a different functional currency from the Parent hedging the risk, how should the Parent determine hedge effectiveness?

(v) What amount(s) should be reclassified from equity to profit or loss upon disposal of the foreign operation?

The following example can be found in the Application Guidance (AG) to INT FRS 116 and is used here to illustrate the concepts in INT FRS 116.

The group structure consists of a Parent and wholly-owned subsidiaries which are foreign operations (A, B and C). Each entity has a different functional currency. The monetary amounts shown represent the net investment in respect of these entities. In the case of B, the amount of £500M includes C's consolidated net assets of £159M.



The hedged risk is the foreign exchange risk between the functional currency of the foreign operation and the functional currency of any parent entity.

What is the hedged risk?

INT FRS 116 clarifies that hedge accounting can only be applied to the foreign exchange difference between the functional currency of the foreign operation and the functional currency of any parent entity (immediate, intermediate or ultimate) of the foreign entity.

This is because investing in an entity with a different functional currency from the investor's functional currency creates an 'economic exposure' to foreign exchange risk.

Hedge accounting cannot be applied to foreign exchange differences arising from a difference between functional currency of the foreign operation and the presentation currency of the parent's consolidated financial statements.

This is because an entity is free to choose a presentation currency other than its functional currency and therefore any difference arising as a result of the choice of presentation currency is simply an 'accounting exposure'.

In the example above, possible functional-to-functional currency risks eligible for net investment hedges in Parent's consolidated financial statements are:

- **€/¥** (Parent's investment in A) - ¥400M
- **€/£** (Parent's investment in B) - £500M
- **€/US\$** (Parent's investment in C) - US\$300M
- **£/US\$** (B's investment in C) - US\$300M

INT FRS 116 reflects the underlying core principle of hedge accounting under FRS 39 in that an entity cannot hedge the same risk twice.

Therefore, in the above example, if B hedges US\$300M of its **£/US\$** exposure in its consolidated financial statements, Parent can either:

- Retain B's hedge accounting and hedge the full £500M of its **€/**£**** exposure; or
- Reverse B's hedge accounting and hedge the US\$300M of its **€/US\$** exposure and £341M for its **€/**£**** exposure.

The hedging instrument can be held by any entity within the group except for the foreign operation itself.

Which entity within a group can hold a hedging instrument if hedge accounting is to be applied?

The consensus reached is that any entity within the group can hold the hedging instrument *except* the foreign operation itself as long as the designation, documentation and effectiveness requirements under FRS 39.88 are met.

In the example above, assume A is the treasury arm of the group and A holds an external debt of US\$300M. In Parent's consolidated financial statements, Parent can designate A's external debt of US\$300M as a hedging instrument to hedge the foreign exchange risk arising from its net investment in C.

To determine hedge effectiveness, the foreign exchange difference on the hedging instrument is calculated by reference to the functional currency of the parent entity which is hedging the risk.

If the entity holding the hedging instrument has a different functional currency from the Parent hedging the risk, how should the Parent determine hedge effectiveness?

In the above example, assume A is the treasury arm of the group and holds an external debt of US\$300M. In the absence of hedge accounting, the exchange difference arising from the US\$300M debt held by A is recorded as follows in Parent's consolidated financial statements:

- ~~US\$/¥~~ spot foreign exchange rate change, translated to Euro, in profit or loss; and
- ~~¥/€~~ spot foreign exchange rate change in FCTR of A.

INT FRS 116 requires the change in value (the foreign exchange difference) of the hedging instrument to be calculated by reference to the functional currency of the parent entity that is hedging the risk.

Hence, when assessing hedge effectiveness, the functional currency of the entity holding the hedging instrument is ignored.

If Parent designates the US\$300M debt held by A as the hedging instrument to hedge against the **€/US\$** risk arising from its net investment in C, Parent should use both amounts of foreign exchange difference for the purpose of calculating hedge effectiveness.

Amounts to be reclassified from FCTR to profit or loss depend on the method of consolidation.

What amount(s) should be reclassified from equity to profit or loss upon disposal of the foreign operation?

Upon disposal of a net investment, FRS 21.48 and FRS 39.102 require any cumulative amounts previously recognised in equity relating to both the net investment of the foreign operation and the effective portion of the hedging instrument to be reclassified to profit or loss.

A parent entity has an accounting policy choice to use the direct method to compute the amount to be reclassified.

In the previous example where the Parent designates the US\$300M debt held by A as the hedging instrument to hedge against the **€/US\$** risk arising from its net investment in C, the total **US\$/€** exchange differences arising from the foreign currency debt should be reclassified to profit or loss on disposal of C.

However, the amount of FCTR to be reclassified to profit or loss for the net investment in C on disposal may be affected by the method of consolidation.

In practice, there are two methods of consolidation:

- **Step-by-step method** – the financial statements of the foreign operation are first translated into the functional currency of any intermediate parent(s) and then translated into the functional currency (or presentation currency) of the ultimate parent.
- **Direct method** – the financial statements of the foreign operation are translated directly into the functional currency of the ultimate parent.

INT FRS 116 acknowledges that when an entity uses the step-by-step method of consolidation, the amounts identified under that method could be different from the amounts determined using the direct method.

In such circumstances, the choice of consolidation method would give rise to a mismatch on disposal of the foreign operation between the amounts reclassified from the FCTR to profit or loss in respect of the net investment, and the amounts reclassified in respect of the hedging instrument. Such mismatch will not arise if the direct method of consolidation is adopted.

In order to avoid the mismatch, INT FRS 116 allows a parent entity to adopt a policy of using the direct method to compute the amount to be reclassified from FCTR to profit or loss on disposal of a foreign operation, irrespective of the method of consolidation used by the parent entity to consolidate the foreign operation.

Making this adjustment is not required. However, it is an accounting policy choice that should be followed consistently for all net investments.

When is an entity required to apply the amendments?

The amendments outlined above are effective for annual periods beginning on or after 1 October 2008, however early adoption is permitted.

Existing hedging relationships should be reassessed at the time of adoption.

If the hedge does not meet the hedge accounting requirements described by this Interpretation, the entity should apply FRS 39 to discontinue hedge accounting prospectively.

H. International Developments

Revised version of IFRS 1 *First-time Adoption of International Financial Reporting Standards*

Refer to IFRS Briefing Sheet – Issue 114 for details.

IFRS 1 was first issued in June 2003. Since that date, there have been several amendments made to the standard resulting from new or amended IFRSs. The IASB believes that these amendments had made the structure of IFRS 1 increasingly complex to understand. Accordingly, the IASB has issued a revised version of IFRS 1 which restructures the format.

While not changing accounting or disclosure requirements, the revised IFRS 1 should be easier to refer to.

ED *Additional Exemptions for First-Time Adopters – Proposed amendments to IFRS 1*

Refer to IFRS Briefing Sheet – Issue 104 for details.

The IASB has issued an ED to propose additional optional exemptions for first-time adopters of IFRSs. This results from the collaboration with the Canadian Accounting Standards Board in response to potential challenges for jurisdictions adopting IFRSs in the near future.

The IASB is proposing the following:

- To exempt companies from retrospective application of IFRSs for oil and gas assets using the full cost method and for operations subject to rate regulation.
- To exempt companies with existing leasing contracts accounted for in accordance with IFRIC 4 *Determining whether an Arrangement contains a Lease* from reassessing the classification of those contracts according to IFRSs when the same classification has previously been made in accordance with national GAAP.

The IASB has invited comments on this ED by 23 January 2009. In Singapore, the ASC issued the same ED, and the deadline for comments was 23 November 2008. We do not expect the proposals to affect Singapore companies which have been using IFRS all along.

ED *Discontinued Operations – Proposed amendments to IFRS 5*

Refer to IFRS Briefing Sheet – Issue 105 for details.

The IASB has issued an ED which proposes to revise the definition of discontinued operations, and to include additional disclosure requirements for all components of an entity which have been disposed of or are classified as held for sale.

The ED proposes that a component of an entity be classified as a discontinued operation when it is either:

- An operating segment as defined by IFRS 8 *Operating Segments*. The current definition refers to a separate major line of business or geographical area of operations as currently defined; or
- A business as defined by IFRS 3 (2008) *Business Combinations* which meets the criteria to be classified as held for sale on acquisition. The current definition refers to a subsidiary.

The IASB has invited comments on this ED by 23 January 2009. In Singapore, the ASC has issued the same ED, and the deadline for comments was 23 November 2008.

DP Preliminary Views on Financial Statement Presentation

Refer to IFRS Briefing Sheet – Issue 110 for details.

This DP is the initial output from Phase B of the IASB's and FASB's joint financial statement presentation project.

Key proposals in the DP which would create significant changes include:

- **Classifying items** in the statement of financial position, comprehensive income and cash flows **into sections** (business, financing, equity, discontinued operations and income tax), **based on a management approach**.
- **Requiring a single statement of comprehensive income**, thus eliminating the option of presenting an income statement and a separate statement of comprehensive income.
- **Requiring cash flows from operating activities to be presented using the direct method**, thus eliminating the ability the more widely-used indirect method.
- **Introducing a new disclosure requirement** to reconcile cash flows to comprehensive income.

The IASB has invited comments on this DP by 14 April 2009. In Singapore, the ASC has issued the same DP, and the deadline for comments is 14 February 2009.

US Securities and Exchange Commission (SEC) issues final rules amending foreign private issuer (FPI) reporting requirements

Refer to IFRS Briefing Sheet – Issue 106 for details.

The SEC has approved changes to its current filing requirements for FPIs. Key aspects of the approved new rules include:

	Effective dates of final rules
Accelerating due dates for annual reports filed on Form 20-F from six months to four months	Fiscal year ending on or after 15 December 2011
Adding disclosures in Form 20-F including reporting of auditor changes and corporate governance matters	Fiscal year ending on or after 15 December 2009
Revising when an entity's ongoing qualification as a FPI is assessed	Fiscal year ending on or after 15 December 2008
Amending Item 17 of Form 20-F to require the disclosure of segment data and to eliminate the limited U.S. GAAP reconciliation option available to FPIs under item 17	Fiscal year ending on or after 15 December 2009
Modifying both the Rule 12g3-2(b) exemption qualification and the permission for entities that continue to qualify under that exemption to satisfy the filing requirements with electronic documents and Webpostings	Fiscal year ending on or after 10 October 2008

Additionally, on 19 September 2008, the SEC published Release No. 34-58597 *Commission Guidance and Revisions to the Cross-Border Tender Offer, Exchange Offer, Rights Offerings and Business Ownership Reporting Rules for Certain Foreign Institutions*. This rule addresses cross-border tender and exchange offers and other types of cross-border business combination transactions and rights offerings by FPIs.

Meetings of the International Accounting Standards Board – September, October and November 2008

Refer to IFRS in Brief – Issue 50, 51 and 52, and IFRS Briefing Sheets – Issue 107 and 112 for details.

Issues discussed during the IASB's meetings in September and October 2008 include:

(a) Fair Value Measurement Project

The IASB reaffirmed the preliminary view included in the DP Fair Value Measurements that fair value should be measured using the price that is most representative of fair value within the bid-ask spread. As part of its discussions on the fair value measurement project, the IASB tentatively decided:

- **Not to preclude for a fair value measurement** the use of mid-market pricing or another practically expedient pricing convention for a fair value measurement within a bid-ask price.
- **To specify that the bid-ask price spread** guidance applies to all levels of the fair value hierarchy

(b) IFRS for Private Entities (previously 'IFRS for SMEs')

The IASB continued its deliberations of the proposals contained in the ED of an IFRS for Private Entities. Some key issues were tentatively decided:

- **To prohibit an entity from recycling** through profit or loss any cumulative exchange differences previously recognised in equity when the entity disposes of a foreign operation.
- **The decision to sell an asset would be an indicator of impairment.** Held for sale classification for non-current assets (or disposal groups) would not apply in IFRS for Private Entities.

(c) Related party disclosures

The IASB is re-exposing the ED after deciding to exempt an entity from detailed disclosures of transactions with State-controlled Entities arising only because of control, joint control or significant influence by a state. They will be required to make disclosures limited to:

- **The name of state**, which has control, joint control or significant influence over them; and
- **The fact that the reporting entity had transactions with the state** or another entity, which is controlled, jointly controlled or significantly influenced by the same state.

The new exposure draft was published on 12 December 2008 and the deadline for comments is 13 March 2009.

(d) Annual Improvements

The IASB commenced its discussions on proposed amendments to be included in its third annual improvements. An ED is expected to be published in August 2009. It has tentatively decided to amend IFRIC 13 *Customer Loyalty Programmes* to clarify the measurement guidance for the fair value of the award credits in a customer loyalty programme.

Meetings of the International Accounting Standards Board – September, October and November 2008 (continued)

Refer to IFRS in Brief – Issue 50, 51 and 52, and IFRS Briefing Sheets – Issue 107 and 112 for details.

Common abbreviations defined

IASB – International Accounting Standards Board

FASB – US Financial Accounting Standards Board

FRS – Singapore Financial Reporting Standard

ACRA – Accounting & Corporate Regulatory Authority

SGX – Singapore Exchange

INT FRS – Interpretation Financial Reporting Standard

IAS – International Accounting Standard

IFRIC – International Financial Reporting Interpretations Committee

ASC – Accounting Standards Council

IFRS – International Financial Reporting Standard

GAAP – Generally Accepted Accounting Principles

DP – Discussion paper

ED – Exposure Draft

(e) Consolidation

The IASB continued its discussions of the ED for consolidation to be published by the end of the year of 2008. They have tentatively decided that a “reporting entity controls another entity when it has the power to direct the activities of that entity for its benefit” and this would apply to structured entities and how holding options or convertible instruments would affect the determination of who has power to direct the activities of an entity for its benefit. They have also tentatively decided that only prospective application of the proposed new IFRS on consolidation will be permitted.

(f) Global Advisory Group

The IASB and the FASB (the Boards) have created a global advisory group to address the global economic financial crisis. This group will consist of regulators, preparers, auditors, investors and other users of financial statements. The Boards have organised and just completed three round tables - one each in Europe, North America and Asia - to gather input on reporting issues arising from the current global financial crisis.

For a summary of the status of the IASB’s current projects, you may refer to *IFRS Briefing Sheet* Issue 107 and 112.

The KPMG International publications covered in this issue are:

- IFRS in Brief: Issues 50, 51 and 52
- IFRS Briefing Sheet: Issues 103 to 116

This section provides highlights of international developments, of relevance to the local context, reported in our international publications – *IFRS in Brief* and *IFRS Briefing Sheet*. You can access the electronic versions at:

IFRS in Brief:

http://www.kpmg.com.sg/newsletters/ifrs_in_brief.html

IFRS Briefing Sheet:

http://www.kpmg.com.sg/newsletters/ifrs_briefing_sht.html

Should you wish to discuss any matter highlighted in this publication, please contact:



Jeremy Hoon

Partner, Professional Practice Department
Tel: +65 6213 2608
jeremyhoon@kpmg.com.sg

KPMG LLP

16 Raffles Quay, #22-00 Hong Leong Building, Singapore 048581
Tel: +65 6213 3388 Fax: +65 6225 0984

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 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.

© 2008 KPMG LLP (Registration No. LL0801267X) is an accounting limited liability partnership registered in Singapore under the Limited Liability Partnership Act (Chapter 163A), and was converted from a firm to a limited liability partnership on and as from 1 October 2008. It is a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative. All rights reserved. Printed in Singapore. MICA (P) 200/11/2008