FINANCIAL REPORTING MATTERS

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In this issue, we feature the 2011 Budget Speech by providing an overview of the income tax changes for businesses and highlight how these changes can benefit businesses. We also discuss the accounting treatment for tax benefits under the Productivity and Innovation Credit scheme. In addition, we summarise the proposed changes to hedge accounting that are expected to have a significant impact in Singapore and briefly explain the differences between the newly issued *SFRS for Small Entities* and full FRS.

Highlights of Budget 2011 – Income tax changes for businesses

On 18 February 2011, the Minister for Finance delivered his Budget Speech for the financial year 2011. In this section, we provide an overview of some of the tax changes and highlight how these changes can benefit businesses.

What are the income tax changes for businesses?

We highlight the following seven key income tax changes for businesses:

1. Enhancement of the Productivity and Innovation Credit (PIC) Scheme
2. One-off Corporate Tax (CIT) Rebate or SME Cash Grant
3. Foreign Tax Credit (FTC) Pooling System
4. Streamlining of Sections 14B and 14K Tax Deduction Schemes
5. Enhancing claim of Pre-commencement Expenses
6. Extending Tax Deduction for Employee Equity-based Remuneration (EEBR)
7. Enhancement to deductions on donations

1. Enhancement of the Productivity and Innovation Credit (PIC) Scheme

First introduced in the Budget 2010, the PIC scheme has been simplified and enhanced in four main areas:

a) **The quantum of tax deduction or allowance** is increased to 400% (currently 250%) of qualifying expenditure for the first $400,000 (currently $300,000) spent on each qualifying activity.

b) **The PIC benefits are made available to overseas research & development (R&D)** which is related to an existing trade or business (currently only R&D done in Singapore).

c) **Businesses are allowed to combine the $400,000 expenditure cap** per YA for YA 2013 to YA 2015 into a new ceiling of $1,200,000 over the three YAs.

d) **For each YA, businesses can opt to receive, in lieu of a tax deduction** or an allowance benefit, a non-taxable cash payout of 30% of the first $100,000 of qualifying expenditure, up to $30,000 (currently at rate of 7% of $300,000 of qualifying deductions or allowances, up to $21,000).

All other existing conditions of the current scheme continue to apply. Please see details in the December 2010 issue of *Financial Reporting Matters.*

The IRAS plans to release further details by the end of June 2011.

Further enhancements to the PIC Scheme announced subsequent to the Budget Day

On 2 March 2011, the Minister for Finance announced a *Tax Deferral* option for businesses to defer a dollar of current YA tax for every dollar of PIC qualifying expenditure incurred for the current financial year. The tax deferred will be due for payment when the first assessment for the following YA is raised. By allowing businesses to enjoy their PIC benefits one year in advance, this PIC Tax Deferral will help businesses, especially for small and medium entities (SMEs), with their cash flow and investments in productivity.

What are the income tax changes for businesses? (continued)

The election is available for the deferment of tax payable for YA 2011 to YA 2014 based on the qualifying PIC expenditure incurred in the corresponding financial years 2011 to 2014.

The amount of tax that can be deferred is at least $100, subject to a cap of $100,000, and is the lower of:

- the tax payable assessed for the current YA
- the qualifying PIC expenditure incurred in the current financial year.

This means that a business that invests in PIC activities in the financial year 2011 can defer its YA 2011 tax payable immediately based on the PIC qualifying expenditure incurred, up to the cap of $100,000. The deferred tax for YA 2011 will only be due for payment when the first assessment for YA 2012 is raised.

How can businesses benefit from the enhanced PIC scheme?

✓ With the enhancement of the PIC scheme, up to $400,000 of business spending on each qualifying activity qualifies for to a maximum tax deduction or allowance of $1,600,000 ($400,000 x 400%). This translates to $272,000 of tax savings (based on prevailing corporate income tax rate of 17%), which means that the government effectively funds up to about two-thirds of the value of the qualifying investments ($272,000/$400,000 = 68%).

✓ Businesses should look closely at taking advantage of the scheme, especially in areas of investments in automation equipment and training of employees. For a start, businesses could evaluate their needs for automated equipment addition/renewal. They could also focus on training programmes for their staff since they may enjoy tax benefits under the PIC on top of the various Workforce Development Agency (WDA) subsidies.

✓ The PIC scheme has been expanded to cover expenditure for R&D done abroad. This would allow those businesses where there is lack of expertise or facility for R&D to be done in Singapore to benefit from the PIC.

✓ The liberalisation of the combined annual expenditure caps ($800,000 for YA 2011 and YA 2012, and $1,200,000 for YA 2013 to YA 2015, for each qualifying activity) will help businesses that are planning large investments in any of the qualifying activities in any one year to maximise their benefit from the full 400% tax deduction or allowance. Businesses should therefore take advantage of the enhanced PIC scheme as a powerful tool to reap tax savings.

✓ Businesses which pay little or no tax can also benefit from the increased cash payout of up to $30,000 per YA, in lieu of tax deductions or allowances. Given that the value of the cash conversion under the enhanced cash conversion option is equivalent to 7.5% of qualifying deductions or allowances [i.e. $30,000/($100,000 x 400%)], it would be more beneficial for businesses that are subject to tax at a concessionary rate of less than 7.5% (say 5%) to convert their qualifying expenditure into cash. For businesses that are subject to tax at the prevailing corporate tax rate of 17%, they will lose out on the tax differential of 9.5% if they opt for the cash conversion (i.e. cash conversion rate of 7.5% compared to 17% tax savings if utilised against taxable income).

What are the income tax changes for businesses? (continued)

✓ Care should be exercised when selecting qualifying expenditure for the cash conversion so as to maximise the tax benefit under the PIC. This is because for registration or acquisition of intellectual property rights (IPRs) and purchase of prescribed automated equipment, partial conversion is not allowed (i.e. conversion option must be made on a "per filing", "per IPR" or "per equipment" basis) and there is claw-back if the equipment or IPR is disposed of before the minimum ownership period.

✓ The PIC Tax Deferral will allow businesses to obtain cash in the same year as they invest by deferring the taxes that they would have to pay in the current year to the following year. Businesses can consider taking advantage of this tax deferral rather than waiting for the cash conversion which will only be available in the following year.

2. One-off Corporate Income Tax (CIT) Rebate or SME Cash Grant

All companies and registered business trusts, regardless of their tax residency status and whether they enjoy a concessionary rate of tax, will automatically receive, after filing their YA 2011 tax return, the higher of:

- CIT rebate of YA 2011 CIT payable, capped at $10,000
- SME cash grant (which is not taxable) based on 5% of revenue for YA 2011, capped at $5,000.

The CIT rebate, computed on the tax payable amount after deducting tax set-offs (e.g. double tax relief, unilateral tax credits and tax deducted at source), is not applicable to income of a non-resident company that is subject to final withholding tax.

To enjoy the SME cash grant, the company must have made Central Provident Fund (CPF) contributions for at least one employee (including any shareholder or director who is an employee) during the basis period for YA 2011.

The IRAS plans to release more details by the end of April 2011.

How can businesses benefit from the CIT rebate?

✓ To maximise the benefit of the CIT rebate, companies may consider deferring their YA 2011 capital allowance claim in respect of capital expenditure on plant and machinery which does not qualify for the PIC.

3. Foreign Tax Credit (FTC) Pooling System

Foreign income is taxable upon remittance to Singapore unless specifically exempt from tax. Resident companies may however claim for FTC for the foreign taxes paid against the Singapore tax payable on the same income. Currently, FTC is computed on a source-by-source and country-by-country basis. FTC granted is capped at the lower of the foreign tax paid and the Singapore tax payable on the particular source of remitted foreign income. Any excess foreign tax paid over the Singapore tax payable for any particular source cannot be used to reduce the Singapore tax payable on other sources of remitted income.

The change announced in the Budget 2011 is that FTC can now be computed on a pooled basis. The amount of FTC granted would be based on the lower of the *aggregate* foreign taxes paid or *aggregate* Singapore tax payable on the pooled foreign income.

All of the three following conditions need to be satisfied before resident companies can elect for the FTC pooling system:

- Foreign income has been subjected to tax in the foreign jurisdiction from which it was received
- The headline tax rate (highest corporate tax rate) of the foreign jurisdiction from which the foreign income is received is at least 15% at the time the income is received in Singapore

What are the income tax changes for businesses? (continued)

- The foreign income is subject to tax in Singapore and the company is entitled to claim FTC on the income.

Where the above conditions are not met, or where companies choose not to elect for FTC pooling system, the current FTC rules will apply.

The FTC pooling system will take effect from YA 2012.

The IRAS plans to release further details by the end of June 2011.

How can businesses benefit from the FTC pooling system?

✓ Resident companies can benefit from the FTC pooling system if they have different sources of foreign income with some sources having foreign withholding tax rates higher than the Singapore corporate tax rate of 17% while others are lower. This will allow any excess of the foreign tax paid over the Singapore tax payable for the first category of income to be used to reduce the Singapore tax payable on the second category of income, as illustrated in the numerical example below:

Facts	Dividend	Interest	Total
Gross foreign income ($)	500	300	800
Withholding tax rate	20%	10%	
Foreign tax paid ($)	100 (f1)	30 (f2)	130 (ft)

Current FTC system	Dividend	Interest
Singapore tax payable @17%	85 (=500 X 17%) (s1)	51 (=300 X 17%) (s2)
Less: FTC	(85) (lower of f1 or s1)	(30) (lower of f2 or s2)
Net Singapore tax payable ($)	NIL	21
Total tax paid: $151 = ($130 + $21)		

FTC Pooling system	Total
Singapore tax payable @17%	136 (=800 X 17%)(st)
Less: FTC (lower of ft or st)	(130)
Net Singapore tax payable ($)	6
Total tax paid: $136 = ($130 + $6)	

4. Streamlining of Sections 14B and 14K Tax Deduction Schemes

The further/double deduction schemes under Section 14B (for expenses relating to approved trade fairs, exhibitions or trade missions, or maintenance of overseas trade offices) and Section 14K (for overseas investment development expenditure) will be merged into a single scheme . The merged scheme will be simplified to allow more businesses to benefit from it.

International Enterprise (IE) Singapore will continue to administer the merged scheme, which has a sunset clause of 31 March 2016. The merged scheme will be effective for applications submitted and approved on or after 1 April 2011.

IE Singapore plans to release further details by the end of March 2011.

How can businesses benefit from the merged schemes for Section 14B and 14K?

✓ Merging the schemes will ease the administrative process for businesses to apply for and to take advantage of. For example, businesses will be able to submit their applications at a later date, i.e., up to the day of their overseas marketing trip instead of seven days before the trip. This means that expenses relating to last minute trips will now be eligible for tax deduction under the merged scheme.

What are the income tax changes for businesses? (continued)

✓ Businesses intending to internationalise and expand overseas should watch out for more details on this merged scheme (expected to be released by IE Singapore by the end of March 2011) to see how they can benefit from the scheme.

5. Enhancing claim of Pre-commencement Expenses

Under the concession for enterprise development which was effective from YA 2004, all expenditures that are deductible against income incurred from the first day of the accounting year in which a business earns its first dollar of trade receipt are deductible. This concession has been enhanced to allow deduction for revenue expenses incurred one year prior to the accounting year in which the business earns its first dollar of trade receipt. This means that businesses can claim pre-commencement revenue expenses incurred in the basis period for YA 2011 in the YA 2012 tax return if the first dollar of trade receipt is earned in YA 2012.

This enhanced concession will take effect from YA 2012.

All other existing conditions of the current concession apply.

The IRAS plans to release further details by end June 2011.

6. Extending Tax Deduction for Employee Equity-based Remuneration (EEBR)

With effect from YA 2012, a company will be given a tax deduction for the costs it incurs to acquire its parent company's shares through a special purpose vehicle (SPV) for fulfilling its obligations under its EEBR scheme where the SPV:

- is set up as a company or a trust solely to administer the EEBR scheme for companies within the group; and
- acquire the parent company's shares from the parent company or the market and holds them in trust for the employees of the companies within the group for the EEBR scheme.

The tax deduction is the lower of:

- The amount paid by the company to the SPV for the parent company's shares; or
- The cost incurred by the SPV to acquire the parent company's shares, less any amount recovered from the company's employees for the parent company's shares.

The company is eligible to claim the tax deduction at the later of:

- The date when the entity "applies" the parent company's shares for the benefit of its employees under its EEBR scheme through the SPV
- When the entity is liable to pay the SPV for the shares transferred.

Like before, no deduction will be allowed for costs incurred by the company in the purchase of its parent company's newly issued shares through the SPV.

The IRAS plans to release further details by the end of June 2011.

7. Enhancement to deductions on donations

The tax deduction of 250% will be extended for another five years for donations made during 1 January 2011 to 31 December 2015. All other existing criteria to qualify for the tax deduction of donations remain unchanged.

Other income tax changes for businesses

	Income tax changes
All sectors	– Renewal of tax exemption scheme for income derived by non-resident non-individuals from any structured product offered by a financial institution in Singapore. – Tax benefits for voluntary CPF medisave contributions by eligible companies to self-employed persons.
Banks	– Liberalisation of the withholding tax exemption scheme for banks. – Extension of tax incentive schemes for project finance.
Insurance companies	– Extension of captive insurance tax incentive scheme, marine hull and liability insurance tax incentive scheme and specialised insurance tax incentive scheme. – Withdrawal of withholding tax exemption scheme for financial guarantee insurers.
Shipping industry	– Streamlining all existing tax incentives for the maritime sector and consolidating them all under one umbrella scheme called 'the Maritime Sector Incentive'. – New enhancements will also be introduced under 'the Maritime Sector Incentive'.

How should the new tax measures introduced during Budget 2011 be reflected in the financial statements?

If an entity's financial year ends on 31 December 2010, should the financial statements be adjusted for the effect arising from the new tax measures introduced during Budget 2011?

No. The financial statements should *not* be adjusted.

FRS 12 *Income Taxes* requires changes in income tax laws and regulations to be taken into account in the measurement of current and deferred taxes from the date of substantive enactment of these changes. In Singapore, new tax measures are generally considered substantively enacted on the date of announcement by the Minister of Finance during the Budget Speech or Budget Roundup Speech.

Therefore, measurement of current and deferred taxes for financial statements for years ended 31 December 2010 should *not* take into consideration the effect of the *new* tax measures introduced during the Budget Speech 2011.

Where the authorisation of the entity's financial statements is *after* 18 February 2011, the date of the Budget Speech, the entity should disclose the nature of the new tax measures only when material to the entity, and an estimate of their financial effect as a "subsequent event".

Find out more

For a more detailed analysis of the possible implications to businesses arising from the Budget 2011 tax changes, you can refer to KPMG's *Singapore Budget Publication 2011* at: http://www.kpmg.com/SG/en/IssuesAndInsights/Pages/Tax_SgBudgetPublication2011.aspx

For more detailed information on the Budget 2011 tax changes, you can access IRAS' website at: http://www.iras.gov.sg/irasHome/page.aspx?id=11586

For details of the key budget initiatives and the Budget Speech, you can access MOF's website at: http://app.singaporebudget.gov.sg/budget_2011/default.aspx

Accounting for the benefits under the Productivity and Innovation Credit Scheme

In this section, we discuss the accounting for tax and cash benefits under the Productivity and Innovation Credit (PIC) scheme introduced in the Budget 2010.

The PIC scheme was introduced in the Budget 2010 (current PIC scheme) to encourage businesses to invest in a broad range of activities along the innovation value chain.

On 18 February 2011 and 2 March 2011, as part of the Budget 2011, enhancements to the current PIC scheme were announced by the Minister for Finance (new PIC scheme).

Details of the current PIC scheme and the new PIC scheme are discussed in the December 2010 issue of *Financial Reporting Matters* and on page 2 of this issue, respectively.

Benefits under the PIC scheme

Benefits under the PIC scheme

In summary, the PIC provides for further tax deduction or allowance (known as enhanced deduction or allowance) on expenditure in the following activities:

(i) R&D activities

(ii) Approved design projects done in Singapore

(iii) Registration of intellectual property rights (IPRs)

(iv) Acquisition of IPRs

(v) Acquisition or leasing of prescribed automation equipment

(vi) Training of employees.

Most businesses also have the option to convert a certain monetary amount of the tax deduction or allowance into a cash grant. Some of these enhanced deductions or allowances and cash grants could be recovered by the IRAS on the occurrence of specified triggering events.

In this issue, we discuss the accounting for the benefits available under the scheme. In particular, we address the following questions and illustrate them with an example:

1. How should an
   available under

2. If an entity's financial year ends on 31 December 2010, should the entity account for the benefits based on the *current* PIC scheme or the *new* PIC scheme?

1. How should an entity account for the enhanced tax deduction or allowance available under the PIC scheme?

From an accounting perspective, further tax deductions or allowances that are available only upon making qualifying expenditure are generally regarded as investment tax credits (ITCs).

Enhanced deductions or allowances can be accounted for using either FRS 12 or FRS 20 by analogy

However, the accounting for ITCs is not directly addressed in FRSs. In practice, ITCs are generally accounted for using either FRS 12 *Income Taxes* or FRS 20 *Accounting for Government Grants and Disclosure of Government Assistance* by analogy.

An entity therefore has a choice of applying either FRS 12 or FRS 20 to account for the enhanced tax deduction or allowance. The choice depends on management assessment of the approach that best reflects the economic substance of the tax incentive. The factors that might be considered in this assessment are detailed below:

What are the factors to consider in deciding whether to apply FRS 12 or FRS 20 by analogy?

Factors to consider	Comments
Are there conditions attached to the benefits available under the tax incentive scheme?	Generally, when conditions are attached, applying FRS 20 will be more appropriate.
Does the tax incentive scheme involve the receipt of cash (or refundable tax credit)?	Generally, when cash or tax is refundable, applying FRS 20 will be more appropriate.
Is the utilisation of the tax benefits under the tax incentive scheme dependent on current or future taxable income?	Generally, when the utilisation of the tax benefits is dependent on current or future taxable income, applying FRS 12 will be more appropriate.

The two possible accounting treatments of ITCs are outlined below:

i) Applying FRS 12 by analogy

- ITCs are presented in profit or loss as a deduction from current tax expense to the extent that an entity is entitled to claim the credit in the current reporting period.
- Any unused ITC is recognised as a deferred tax asset and income if it meets the recognition criteria.

ii) Applying FRS 20 by analogy

- ITCs are recognised as income over the periods necessary to match them with the related costs that they are intended to compensate.
- The ITC initially is shown in the statement of financial position as a receivable from the government when there is reasonable assurance that an entity will comply with the conditions of the ITC and the ITC will be received. If the entity is claiming the further tax deduction/allowance, the receivable from the government is offset against current tax payable when the entity is entitled to claim the ITC.
- For ITCs relating to acquisition of long-term assets, the ITC is either:
  - initially recognised as deferred income and subsequently amortised to the profit or loss over the useful life of the long-term asset either as "other income" or deduction from the related expense; or
  - initially offset against the cost of the long-term asset and reduces future depreciation or amortisation expense.
- For all other ITCs, the ITC is initially recognised as deferred income and subsequently presented in profit or loss either as "other income" or deduction from the related expense as appropriate.

Under the PIC scheme, an entity has to reflect its election whether to claim the tax deduction/allowance or convert the deduction/allowance into a cash grant in its tax return. Current and deferred taxes should generally be measured as of and subsequent to substantive enactment date based on an entity's expectations of elections that will be made in filing its tax return.

Therefore, if an entity expects to convert the qualifying deduction/allowance into a cash grant when it files its tax return, this should be reflected in the income tax provision for financial reporting purposes. In such circumstances, we believe that it will be more appropriate for the entity to apply FRS 20 to account for the cash grant.

On the other hand, if the entity expects to claim the qualifying deduction/allowance when it files its tax return, the entity will have to select an accounting treatment that best reflects the economic substance of the benefits.

The treatment, once selected, must be applied consistently to other similar tax incentives.

2. If an entity's financial year ends on 31 December 2010, should the entity account for the benefits based on the *current* PIC scheme or the *new* PIC scheme?

Entity with financial year ending before 18 February 2011 should account for the benefits based on the *current* PIC scheme

The entity should account for the benefits based on the ***current*** PIC scheme as the ***new*** PIC scheme is substantively enacted after the year-end. The substantive enactment of new tax laws after the year end but before the authorisation of the financial statements is a non-adjusting post balance sheet event. Where the effect of the ***new*** PIC scheme is expected to be significant, an entity should disclose the nature and an estimate of its financial effect as a "subsequent event" or an "event after balance sheet date".

If an entity's financial year ends before 18 February 2011 (date of the Budget Speech 2011), the benefits should be accounted for based on the ***current*** PIC scheme. If the authorisation of the entity's financial statements is after 18 February 2011, the entity has to disclose the nature and an estimate of the financial effect arising from the ***new*** PIC scheme if the effect is expected to be significant.

3. When should the effect of the new PIC scheme be reflected in the financial statements?

The effect of the *new* PIC scheme should be recognised after 18 February 2011

The effect of a change in tax laws should be accounted for in the financial periods ending on or after the date of substantive enactment of the new tax laws. In Singapore, new tax laws are generally considered substantively enacted on the date of announcement by the Minister for Finance during the Budget Speech or the Budget Roundup Speech. Therefore, the effect of the new PIC scheme would be reflected in the financial statements with financial periods ending after 18 February 2011.

Illustrative example

Facts

During the year ended 31 December 2010, Entity A with a calendar year end incurs qualifying training expenditure amounting to $100,000. As at 31 December 2010, Entity A has the following choices under the current PIC scheme:

Option A:

Claim a 250% tax deduction on the training expenditure against its taxable income. If Entity A chooses this option, the base and enhanced deductions (collectively known as "qualifying deduction") and the resultant tax savings, assuming an applicable tax rate of 17%, are as follows:

	Base	Enhanced	Total
Tax deduction	$100,000	$150,000	$250,000
Applicable tax rate	17%	17%	17%
Tax savings	$17,000	$25,500	$42,500

Option B:

Convert the qualifying deduction to cash at the rate of 7%. If Entity A chooses to convert the qualifying deduction to cash, Entity A will receive a non-taxable cash payout of $17,500 ($250,000 x 7%) from the government and the qualifying deduction converted to cash will no longer be available for tax deduction.

	Base	Enhanced	Total
Tax deduction	$100,000	$150,000	$250,000
Applicable conversion rate	7%	7%	7%
Cash grant	$7,000	$10,500	$17,500

Question

Applying the above guidance, how should Entity A account for the benefits under the PIC scheme as at 31 December 2010?

Analysis

Entity A should measure its current and deferred taxes as at 31 December 2010 based on its expectations of elections that it will make in filing its tax return.

If Entity A expects to claim the qualifying deduction, then Entity A should make an assessment as to whether it is more appropriate to apply FRS 12 or FRS 20 by analogy.

If Entity A expects to convert the qualifying deduction into a cash grant when it files its 2010 tax return, it is generally more appropriate for Entity A to apply FRS 20 to account for the cash grant.

Illustrative example (continued)

The accounting entries as at 31 December 2010 are illustrated below:

	Entity A expects to claim the qualifying tax deduction		Entity A expects to convert the qualifying deduction to cash grant
	FRS 12	FRS 20	FRS 20
On recognition of PIC		Dr Government grant receivable $25,500[2, 5] Cr Deferred income $25,500	Dr Government grant receivable $17,500[4, 5] Cr Deferred income $17,500
On recognition of the related expense in P&L		Dr Deferred income $25,500 Cr Other income or Training expense $25,500	Dr Deferred income $17,500 Cr Other income or Training expense $17,500
On entitlement to claim the tax deduction	Dr Current tax payable $42,500[1] Cr Current income tax benefit $42,500	Dr Current tax payable $42,500 Cr Government grant receivable $25,500 Cr Current income tax benefit $17,000[3]	
On receipt of the cash grant			Dr Cash $17,500 Cr Government grant receivable $17,500

1 Total deduction of $250,000 x 17% = $42,500
2 Enhanced deduction of $150,000 x 17% = $25,500
3 Base deduction of $100,000 x 17% = $17,000
4 Total deduction of $250,000 x 7% = $17,500
5 PIC is recognised when there is reasonable assurance that an Entity A will comply with the conditions of the PIC and the enhanced deduction will be received.

The amounts recorded for this transaction as at 31 December 2010 would be as follows:

		Entity A expects to claim the qualifying tax deduction		Entity A expects to convert the qualifying deduction to cash grant
		FRS 12	FRS 20	FRS 20
		$'000	$'000	$'000
Training expenses		(100,000)	(100,000)	(100,000)
Government grant[6]		-	25,500	17,500
Loss before tax	(A)	(100,000)	(74,500)	(82,500)
Current tax benefit	(B)	42,500	17,000	-
Loss after tax		(57,500)	(57,500)	(82,500)
Effective tax rate	(B)/(A)	-43%	-23%	0%
Statement of financial position				
Cash		(100,000)	(100,000)	(82,500)
Current tax receivable		42,500	42,500	-
Retained earnings		57,500	57,500	82,500

6 The government grant income can be presented either as other income or a reduction in training expense.

Impact on interim financial statements

If Entity A prepares interim financial statements for the interim period ending 31 March 2011, the effect of the *new* PIC scheme on the opening current and deferred taxes could be recognised immediately in the interim period. In addition, the anticipated credits arising from the *new* PIC scheme are generally reflected in computing the estimated annual effective income tax rate, unless the credit is accounted for under FRS 20 or relates to a one-time event.

Proposed changes to hedge accounting

In this section, we will touch on the pertinent changes proposed by IASB to the existing hedge accounting rules of IAS 39 as set out in the exposure draft ED/2010/13 *Hedge Accounting*.

Introduction

The ED on hedge accounting is the first instalment of the final phase of IASB's project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. This first instalment of proposals addresses hedges of single item and closed portfolios of items. A closed portfolio is a portfolio for which items cannot be added, removed or substituted without treating each change as a transition to a new hedging relationship for accounting purposes. The second instalment, expected during the second quarter of 2011, will address open portfolios or macro hedging.

Proposed hedge accounting to be more aligned to an entity's risk management activities

The ED proposes some significant changes to the hedge accounting requirements in IAS 39. These changes are intended to align the objective of hedge accounting with the entity's risk management activities. The end result is to achieve a set of financial statements that reflect the effects of an entity's risk management activities more closely.

The proposed changes, when finalised, are to be applied together with all existing IFRS 9 *Financial Instruments* requirements. IFRS 9 currently contains requirements that replace IAS 39 on classification and measurement of financial assets and liabilities. The IASB is also concurrently working to develop a new impairment model for financial assets. Once finalised, the new impairment and hedge accounting requirements will be included in IFRS 9 and they will replace the equivalent requirements in IAS 39.

In Singapore, the ASC has, to date, not endorsed the adoption of IFRS 9 as FRS.

How will the ED affect companies in Singapore?

This article focuses on the following proposed requirements that are expected to have a significant impact in Singapore:

1. Investments in equity instruments (e.g. shares in listed companies) designated at fair value through other comprehensive income (OCI) *cannot* be designated as a hedged item.
2. Risk components of a non-financial item can be designated as hedged risks.
3. Synthetic instruments can be designated as hedged items.
4. The 80% to 125% "bright line" test for assessing hedge effectiveness and retrospective hedge effectiveness test is eliminated.
5. Entities must rebalance certain existing hedge relationships that have fallen out of alignment instead of having to restart the hedge in a new relationship. Voluntarily discontinuing a hedge relationship is prohibited.

Financial instruments carried at fair value through other comprehensive income cannot be designated as a hedged item

1. Investments in equity instruments (e.g. shares in listed companies) designated at fair value through other comprehensive income (OCI) *cannot* be designated as a hedged item.

Under IFRS 9, investments in equity instruments can be designated at inception to be accounted for at fair value with changes recognised in OCI. This classification is similar to the available-for-sale category under IAS 39, except that under IFRS 9, other than dividend income, gains or losses recognised in OCI cannot be reclassified to profit or loss even upon the disposal of the investments.

IAS 39: Under IAS 39, entities can designate available-for-sale investments in equity instruments as hedged items as the gains or losses arising from these instruments are reclassified from OCI to profit or loss on impairment or on disposal.

ED: The ED specifically prohibits an entity from designating investments in equity instruments that are measured at fair value through OCI. This is because the hedged items as the risk exposure arising from the change in fair value does not affect profit or loss. However, if forecasted dividends from these equity investments are highly probable, the entity can choose to designate these dividends as hedged items.

Illustrative example 1
Hedges of foreign currency equity instruments

Facts

Company A's functional currency is the Singapore dollar. On 1 April 2010, A invested in a portfolio of equity shares of Company T on a foreign stock exchange in which transactions are denominated in USD. T's shares are traded on only one stock exchange. T's shares are acquired for USD 30 million and are classified as available-for-sale under IAS 39 (fair value through OCI under IFRS 9).

A's risk management strategy is to hedge all significant exposure to foreign risk beyond certain limits. A decides to hedge against foreign currency risk for a portion of the market value of T's shares. A enters into a foreign currency forward contract to sell USD 5 million and receive Singapore dollar on 15 October 2010.

Analysis

Under IAS 39, A can designate the forward contract as a fair value hedge of the currency risk associated with the USD 5 million portion of the fair value of the shares. Assuming that all criteria for hedge accounting have been met, the fair value change of the hedged item (i.e. the USD 5 million portion of the fair value of the shares) in respect of the foreign currency risk is reclassified to the profit or loss to offset the gain/loss arising from the hedging instrument (i.e. the forward contract).

Under the proposed ED, A cannot apply hedge accounting as A is prohibited from designating an investment in equity instrument measured at fair value though OCI as the hedged item.

Risk components of a non-financial item can be designated as hedged items

2. Risk components of a non-financial item can be designated as hedged items

IAS 39: Under IAS 39, non-financial items can be designated as the hedged item only in its entirety, or for its foreign currency risk component.

ED: This restriction is removed in the ED. Under the proposal, an entity can hedge a risk component of a non-financial item as long as the risk component is separately identifiable or contractually specified and the changes in cash flows or fair value of the item attributable to changes in the risk component can be reliably measured.

Illustrative example 2
Risk components of a non-financial item

Facts
Company B has a long-term supply contract to purchase natural gas that is priced using a contractually specified formula that references gas oil, fuel oil and transportation charges. B's risk management strategy is to hedge 100% of its exposure to gas oil risk and enters into gas oil forward contracts to hedge that price risk.

Analysis
Under IAS 39, the price risk of the entire purchase could be hedged, but not just the gas oil component.

Under the ED, the gas oil component is contractually specified and therefore can be separately identified and reliably measured. Company B will be able to designate the gas oil price exposure as the hedged risk.

Synthetic instruments can be designated as a hedged item

3. Synthetic instruments can be designated as hedged items

IAS 39: Under IAS 39, derivative instruments generally cannot be designated as hedged items. Therefore, synthetic instruments created by aggregating a derivative and a non-derivative instrument cannot qualify as hedged items.

ED: The ED proposes that an aggregated exposure that is a combination of an exposure and a derivative may be designated as a hedged item, if that combination that creates a different aggregated exposure is managed as a single exposure for a particular risk (or risks).

Illustrative example 3
Synthetic instruments

Facts
Company C's functional currency is in Singapore dollars (SGD). C has a 10-year fixed rate foreign currency debt. C plans to hedge the foreign currency risk for the entire term of a 10-year fixed rate foreign currency debt. However, C requires fixed rate exposure in SGD only for two years and floating rate exposure in its SGD for the remaining term to maturity. On a two-year rolling basis, C fixes the next two years' interest rate exposure.

C enters into a 10-year fixed-to-floating cross-currency interest rate swap that swaps the fixed rate foreign currency debt into a variable rate SGD debt. This is overlaid with a two-year SGD interest rate swap that swaps SGD variable rate debt into fixed rate debt.

For accounting purposes, C designates the 10-year fixed-to-floating cross-currency interest rate swap as a fair value hedge of the foreign currency and interest rate risks arising from the foreign currency debt. The fixed rate foreign currency debt and the fixed-to-floating cross-currency interest rate swap in combination are viewed as a 10-year SGD variable rate debt (a synthetic instrument).

Illustrative example 3
Synthetic instruments

Analysis
Under IAS 39, derivative instruments generally cannot be designated as the hedged item, therefore, in the above example, C is prohibited from designating the interest rate risk arising from the synthetic 10-year SGD variable rate debt in a hedging relationship.

Under the ED, the synthetic SGD 10-year variable rate debt could be designated as a hedged item in a cash flow hedge of interest rate risk for two years.

80% to 125% "bright line" test for hedge effectiveness is eliminated

4. The 80% to 125% "bright line" test for assessing hedge effectiveness and retrospective hedged effectiveness test is eliminated

IAS 39: To qualify for hedge accounting under IAS 39, a hedging relationship must be expected to be highly effective, both prospectively and retrospectively, in achieving offset of changes in fair value or cash flows attributable to the hedged risk. The hedging relationship is regarded to be highly effective if the extent of offsetting is within the range of 80% to 125%. IAS 39 requires the prospective and retrospective hedge effectiveness tests to be performed at a minimum at each reporting date.

ED: Under the ED, entities must still meet the hedge effectiveness requirement. However, the ED removes the 80% to 125% bright line test, and instead, replaces it with an objective-based assessment. Under the ED, a hedging relationship meets the hedge effectiveness requirement if it meets the objective of the hedge effectiveness assessment and is expected to achieve other than accidental offsetting. The objective of hedge effectiveness under the ED is to ensure that the hedging relationship would produce an unbiased result and minimise expected hedge effectiveness.

This hedge effectiveness assessment must be performed at the inception of the hedging relationship and at a minimum each reporting period or upon a significant change in circumstances affecting the hedge effectiveness requirements, whichever comes first. As the assessment relates to expectations about hedge ineffectiveness and offsetting, the test would be only forward looking or prospective.

However, it should be noted that the requirement to compute and record actual hedge ineffectiveness in profit or loss remains unchanged.

Hedging relationships are rebalanced when the risk management strategy remains unchanged

5. Entities must rebalance certain existing hedge relationships that have fallen out of alignment instead of having to restart the hedge in a new relationship. However, voluntarily discontinuing a hedge relationship is prohibited

IAS 39: Under IAS 39, hedge accounting must be discontinued when the hedging relationship is no longer assessed to be highly effective although the risk management objective has not changed. Voluntary discontinuation of hedge accounting is also allowed with no restriction under IAS 39.

ED: Under the ED, hedge accounting cannot be discontinued voluntarily. Hedge accounting has to be discontinued if the risk management objective for the hedging relationship has changed.

If a hedging relationship no longer meets the objective of hedge effectiveness assessment (i.e. unbiased results and minimise hedge ineffectiveness) but the risk management objective remains the same and the relationship continues to achieve other than accidental offset, the entity should rebalance the hedging relationship. They should do so by increasing or decreasing the volume of the hedged item or hedging instrument so that it meets the objective of the hedge effectiveness assessment again.

The ED also requires an entity to proactively rebalance the hedging relationship when it expects that a hedging relationship might cease to meet the hedge accounting qualifying criteria in the future.

Illustrative example 4
Rebalancing the hedging relationship

Facts

Company C hedges an exposure to foreign currency A using a foreign currency forward contract that references foreign currency B.

Currencies A and B are pegged (i.e. their exchange rate is maintained within a band or at an exchange rate set by a central bank or other authority) and the currency pair has been demonstrated to exhibit a high level of statistical correlation historically.

C determines that the foreign currency forward contract is an effective hedge against its exposure to foreign currency A and a hedge ratio of 90 units of currency A : 100 units of currency B would minimise hedge ineffectiveness. C formally designates this hedging relationship for hedge accounting purpose.

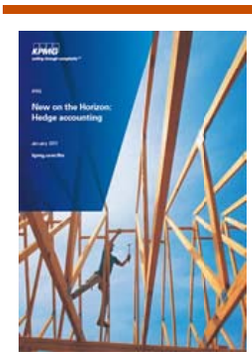
Subsequent to inception of hedge accounting, the exchange rate between currencies A and B were changed (i.e. a new band or rate was set). C's risk management objective remains the same for this hedging relationship.

Analysis

Under IAS 39, if the change in exchange rate between currencies A and B causes the hedge effectiveness test to fall out of the 80% to 125% range, C will have to discontinue hedge accounting.

Under the ED, the change in exchange rate will alter the statistical correlation between currencies A and B. Given that C's risk management objective remains the same and currencies A and B are still pegged, C has to rebalance the hedging relationship to reflect the new exchange rate. Rebalancing would ensure that the hedging relationship meets the objective of the hedge effectiveness assessment under the new circumstances.

For a more comprehensive and detailed discussion on the above changes and other changes proposed in the ED, please refer to KPMG's publication *New on the Horizon: Hedge Accounting*.



Find out more

New on the Horizon: Hedge Accounting is a publication produced by KPMG International Standards Group.

This publication focuses on the significant changes proposed by the ED/2010/13 *Hedge Accounting* to the general hedge accounting requirements of IAS 39, and the impact these changes are expected to have on the preparers and users of financial statements.

This publication is available for download at:
http://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/New-on-the-Horizon/Documents/New-on-the-Horizon-Hedge-Accounting-January-2011v2.pdf

SFRS for Small Entities

On 1 December 2010, the ASC announced the issuance of *Singapore Financial Reporting Standard (SFRS) for Small Entities.* The *SFRS for Small Entities* is an alternative framework to the full SFRS for eligible entities in Singapore. An entity can choose to apply the full FRS or the *SFRS for Small Entities* if it meets the eligibility criteria set by the ASC.

Who is eligible to apply the *SFRS for Small Entities*?

An entity is eligible to apply the *SFRS for Small Entities* if all of the following criteria are met:

1. It is not publicly accountable
   An entity is not publicly accountable if:
   a) its debt or equity instruments are not traded in a public market or it is not in the process of issuing such instruments for trading in a public market (such as a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets)
   b) it is not a deposit-taking entity and/or holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses, such as banks, insurance companies, securities brokers/dealers, mutual funds and investment banks
   c) it is not a public company defined under the Singapore Companies Act (Cap. 50)
   d) it is not a charity defined under the Charities Act (Cap. 37).
2. It publishes general purpose financial statements for external users.
3. It satisfies at least two of the three following criteria:
   a) Total annual revenue of not more than SGD 10 million
   b) Total gross assets of not more than SGD 10 million
   c) Total number of employees of not more than 50.

The *SFRS for Small Entities* is effective for financial reporting periods beginning on or after 1 January 2011.

Can an entity apply *SFRS for Small Entities* if its holding parent company reports under full FRS?

Although an entity (that is a subsidiary or an intermediate holding company) can qualify for reporting under *SFRS for Small Entities* for its own financial statements, it needs to consider the implications on the parents' group reporting that is under full FRS or IFRS.

Why was *SFRS for Small Entities* issued?

SFRS for Small Entities is intended to facilitate financial reporting for small entities by simplifying and reducing detailed requirements and guidance from full FRSs and by removing the more complex options in certain areas in which full FRSs allow more than one accounting option.

What are some differences between *SFRS for Small Entities* and full FRS?

Are there any tax implications arising from applying *SFRS for Small Entities?*

Some differences are that entities reporting under *SFRS for Small Entities* will:

1. **Have more disclosure reliefs** as compared with the disclosures required under full FRS, in areas such as:
   - **Financial instruments** – financial risk management and fair value measurements under FRS 107 *Financial Instruments: Disclosures* are not required.
   - **Impairment of non-financial assets** – events and circumstances that led to recognition of impairment loss, description of cash-generating unit and basis of determining recoverable amount are not required.
   - **Business combinations** – factors that contributed to the recognition of goodwill are not required.
   - **Financial statement presentation** – a third statement of financial position is not required.

What are some differences between *SFRS for Small Entities* and full FRS?

Are there any tax implications arising from applying *SFRS for Small Entities? (continued)*

2. **Expense all borrowing costs**, removing the requirement from full FRSs for entities to assess whether such costs should be capitalised.

   For income tax purposes, borrowing costs "incurred" (based on contractual terms) to acquire an income-generating capital asset are tax deductible. Since interest expense recognised for accounting purposes is calculated using the effective interest method, a tax adjustment may be necessary in arriving at taxable income. Interest expense recognised in accounting profit or loss would be added back and the qualifying "incurred" borrowing costs would be deducted. However, if IRAS agrees to accept interest expense based on effective interest method under *SFRS for Small Entities* as a deductible expense, then no tax adjustment would be needed for qualifying borrowing costs.

3. **Amortise goodwill and intangible assets** over a finite useful life (presumed to be 10 years if it cannot be determined reliably), removing the requirement from full FRS for entities not to amortise goodwill and intangible assets with indefinite useful lives, and to perform an annual mandatory impairment test.

   For income tax purposes, amortisation of goodwill and intangible assets are not deductible.

4. **Expense all internally incurred research and development (R&D) costs**, removing the requirement from full FRSs for entities to assess whether development costs should be capitalised.

   R&D costs that qualify for tax deduction may be claimed. In addition, qualifying R&D costs may be also eligible for the enhanced tax deduction under the Productivity and Innovation Credit Scheme (see our article on "Highlights of Budget 2011 Income Tax Changes for Businesses" for more details).

5. **Categorise all financial instruments in two categories: amortised cost or fair value**, simplifying the accounting requirements in FRS 39 *Financial Instruments: Recognition and Measurement* for financial instruments.

   Under full FRSs, IRAS aligned the tax treatment for certain financial assets and liabilities to be in line with the accounting treatment under FRS 39 *Financial Instruments: Recognition and Measurement*.

   Under the "FRS 39 tax treatment", accounting gains and losses arising from financial assets and liabilities that are "on revenue account" are also considered to be taxable income or deductible expenses for tax purposes. However, accounting gains and losses arising from financial assets and liabilities that are "on capital account" would not taxable or deductible. Hence, when considering the tax implications for financial instruments, an entity would need to determine whether it is on revenue or on capital account.

   Financial assets and liabilities are generally considered to be "on revenue" account when they are held for a short-term period of time, are frequently traded and are intended to be sold for the purposes of making a gain.

   Under *SFRS for Small Entities*, we are unsure if "FRS 39 tax treatment" would also apply since IRAS has not yet issued guidelines for financial instruments under this alternative framework.

6. **Account for associates and jointly controlled entities using either cost model, equity method or fair value model** in the consolidated financial statements. Full FRSs (with certain exemptions) require accounting for associates using the equity method and jointly controlled entities using either proportionate consolidation or equity method.

   For income tax purposes, entities are taxed on their stand-alone financial results. Therefore, profit or loss arising from equity-accounted for associates or jointly controlled entities are not included in the investee's taxable income.

7. **Recognise revenue only upon delivery of completed real estate to the buyer** in relation to the construction of real estate. This removes the requirement from the *Accompanying Note* to INT FRS 115 *Agreements for the Construction of Real Estate* for sale of uncompleted residential property units in Singapore to recognise revenue by reference to the stage of completion when all other recognition criteria under FRS 18 *Revenue* are met continuously as construction progresses.

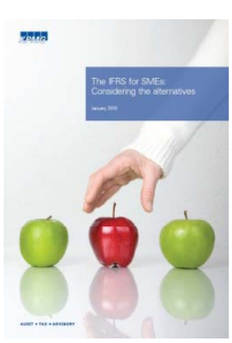
   The tax treatment for revenue recognition on the construction for real estate is the same as under *SFRS for Small Entities* , i.e. revenue is recognised upon completion of the project.

8. **Recognise government grants in income immediately** when performance conditions are met at the fair value of assets received. This removes the requirement under full FRSs to recognise the grant in income over the periods necessary to match government grants with related costs for which they are intended to compensate. This also removes the option to measure a non-monetary grant and asset received at a nominal amount.

   For income tax purposes, government grants relating to the purchase of capital assets are not taxable whereas those received to offset operating expenses are taxable, unless they are exempted from tax.

What are the effects on deferred tax?

The carrying amount of an asset or liability may change due to the adoption of *SFRS for Small Entities* in the entity's financial statements. This will have an effect on the amount of temporary differences (i.e. the difference between the carrying amount of an asset or liability in the statement of financial position and its tax base). Entities transitioning from full FRS to *SFRS for Small Entities* should refer to section 35 *Transition to the SFRS for Small Entities* in *SFRS for Small Entities* for guidance on the recognition of deferred income tax for first-time adopters.



Find out more

The IFRS for SMEs: Considering the alternatives is a publication produced by KPMG International Standards Group.

This publication provides a general overview of the requirements of the *IFRS for SMEs*. The publication also includes discussion on the scope and applicability, considerations for entities contemplating the adoption of the standard and a comparison of the *IFRS for SMEs* requirements to full IFRSs.

This publication is available for download at:
http://www.kpmg.com/Global/en/IssuesAndInsights/ArticlesPublications/The-IFRS-for-SMEs/Documents/Considering-the-alternatives.pdf

For more detailed information on the applicability of the *SFRS for Small Entities*, you can access the ASC's Statement on Applicability at:
http://www.asc.gov.sg/attachments/SFRS%20for%20SE%20(Statement)-z.pdf

International developments

Deferred Tax: Recovery of Underlying Assets - Amendments to IAS 12

On 20 December 2010, the IASB published *Deferred Tax: Recovery of Underlying Assets - Amendments to IAS 12* to provide an exception to the measurement principles in specified circumstances.

In general, the measurement of deferred tax assets and liabilities is based on the expected manner of recovery or settlement of the underlying asset or liability.

The amendments provide an exception to this measurement principle in respect of investment property measured using the fair value model in accordance with IAS 40 *Investment Property*. Under the exception, the measurement of deferred tax assets and liabilities is based on a rebuttable presumption that the carrying amount of the investment property will be recovered entirely through sale.

The presumption can be rebutted only if the investment property is depreciable and held within a business model whose objective is to consume substantially all of the asset's economic benefits over the life of the asset. Therefore, the presumption cannot be rebutted in respect of the land component of investment property as it is a non-depreciable asset.

The amendments also integrate the requirements of SIC 21 *Income Taxes—Recovery of Revalued Non-Depreciable Assets* into IAS 12 *Income Taxes.* As a result, SIC 21 is withdrawn.

The amendments to IAS 12 are effective for periods beginning on or after 1 January 2012 and are applied retrospectively. Earlier application is permitted.

In Singapore, the ASC has issued the equivalent amendments with the same effective date.

Amendments to IFRS 1 – *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters*

On 20 December 2010, the IASB published *Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters* (Amendments to IFRS 1).

The amendments add a deemed cost exemption to IFRS 1 that an entity can apply at the date of transition to IFRSs. This exemption applies in situations where the entity's functional currency was subject to severe hyperinflation before the date of transition to IFRSs.

When an entity's date of transition to IFRSs is on, or after, the date that the entity's functional currency ceases to be subject to severe hyperinflation (the functional currency normalisation date). With the amendments, the entity may elect to measure the assets and liabilities that were held before the functional currency normalisation date at fair value on the date of transition to IFRSs and use that fair value as the deemed cost of those assets and liabilities in the opening IFRS statement of financial position.

The amendments apply for annual periods beginning on or after 1 July 2011. Early adoption is permitted.

In Singapore, the ASC has issued the equivalent amendment with the same effective date.

IFRS Practice Statement *Management Commentary*

On 8 December 2010, the IASB issued an IFRS Practice Statement *Management Commentary*.

Management Commentary is a narrative report that provides a context within which to interpret the financial position, performance and cash flows of an entity, i.e., it supplements and complements financial statements.

The objective of the practice statement is to assist management to provide useful management commentary in respect of financial statements prepared in accordance with IFRSs. To achieve this objective, the practice statement contains a Framework for the presentation of management commentary: including its purpose, principles, presentation and elements (content).

The practice statement is not an IFRS and an entity need not comply with it in order to state compliance with IFRSs. An entity that chooses (or is otherwise required by a regulator) to apply the practice statement should explain the extent to which it has been applied and may state compliance with the practice statement only if it complies fully.

In Singapore, the ASC has issued the equivalent practice statement.
An entity may apply the FRS Practice Statement prospectively from 1 April 2011.

ED/2011/1 *Offsetting Financial Assets and Financial Liabilities*

On 28 January 2011, the IASB and the FASB issued ED/2011/1 *Offsetting Financial Assets and Financial Liabilities* which contains joint proposals on offsetting financial assets and financial liabilities in entities' statement of financial position. The proposed requirements would supersede the requirements on offsetting in IAS 32 *Financial Instruments: Presentation*. These proposed amendments will mostly affect entities reporting under U.S. GAAP rather than those reporting under IFRS.

Main proposals

- Offset of a recognised financial asset and a recognised financial liability would be required only when the entity has an unconditional and legally enforceable right to set-off and intends either to settle the asset and liability on a net basis or to realise the asset and settle the liability simultaneously.
- In all other cases, offsetting would be prohibited.
- Disclosures would be enhanced through improved information about rights of set-off and related arrangements and their effect on the entity's financial position.

The IASB has invited comments on the proposals contained in the ED by 28 April 2011. In Singapore, the ASC has issued the same ED and the deadline for comment closed on 4 March 2011.

Supplement to ED/2009/12 *Financial Instruments: Amortised Cost and Impairment*

On 31 January 2011, the IASB and the FASB published for comment proposals for accounting for impairment of financial assets managed in an open portfolio (the Supplement). The proposals are issued as a supplement to ED/2009/12 *Financial Instruments: Amortised Cost and Impairment* published by the IASB and the *Proposed Accounting Standard Update, Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities* published by FASB.

Supplement to ED/2009/12 *Financial Instruments: Amortised Cost and Impairment* (continued)

The Supplement discusses the recognition of expected credit losses for financial assets managed in an open portfolio. In an open portfolio, assets are added to the portfolio and removed from it throughout its life through origination, purchase, repayment, sale, transfer or a write-off. The Supplement proposes that financial assets that are managed on an open portfolio basis are split into two groups: the 'good book' and the 'bad book'. Impairment allowance for the expected credit losses in these books is recognised using different bases and at different timing, based on the credit risk of the respective books.

The Supplement therefore amended the earlier proposal to include expected credit losses in the determination of effective interest rate for interest income recognition. Expected credit losses are now recognised and reported separately from interest income.

The Supplement also sets out the proposed presentation and disclosure requirements of financial assets included in an open portfolio. In addition, the Supplement seeks feedback as to whether loan commitments that are not accounted for at fair value through profit or loss and financial guarantee contracts should also be included in the financial assets portfolio for impairment assessment.

The IASB has invited comments on the proposals contained in the Supplement by 1 April 2011. In Singapore, the ASC has issued the Supplement and the comment period closed on 25 February 2011.

Consultative Report on the Review of the IFRS Foundation's Governance

On 7 February 2011, the IFRS Monitoring Board published its *Consultative Report on the Review of the IFRS Foundation's Governance*. The report focuses on whether the current governance structure for the IFRS Foundation and the IASB effectively promotes the IASB's primary mission of setting high quality, globally accepted standards and whether the IASB is appropriately independent and accountable.

This consultation is separate from the strategy review currently being carried out by the Trustees of the IFRS Foundation (the Trustees). The Monitoring Board and the Trustees intend to co-ordinate their review and complete an integrated package of proposals by the third quarter of 2011.

In the report, the Monitoring Board proposes refinements rather than fundamental changes for the IASB and its oversight. The most significant changes are regarding the composition and role of the Monitoring Board itself, including proposals to expand its membership. The Monitoring Board also explores whether it should be involved more directly in selecting Trustee, appointment of the IASB chair and determining what projects the IASB adds to its agenda.

Comments on the proposals are due by 8 April 2011. In Singapore, the ASC has requested for comments on the report and the comment period closed on 6 March 2011.

Find out more

For a more detailed update on these, you can access our website at:

http://www.kpmg.com/SG/en/IssuesAndInsights/Pages/InTheHeadlines.aspx

Common abbreviations

ASC	Accounting Standards Council in Singapore
ACRA	Accounting & Corporate Regulatory Authority
DP	Discussion paper
ED	Exposure Draft
FASB	U.S. Financial Accounting Standards Board
FSP	FASB Staff Position
FRS	Singapore Financial Reporting Standard
GAAP	Generally Accepted Accounting Principles
IAS	International Accounting Standard
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
ICPAS	Institute of Certified Public Accountants of Singapore
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard
INT FRS	Interpretation of Financial Reporting Standard
IRAS	Inland Revenue Authority of Singapore
SGX	Singapore Exchange Ltd
YA	Year of assessment

Contact us

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

David Lee
Partner, Corporate Tax
T: +65 6213 2539
E: dlee2@kpmg.com.sg

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

kpmg.com.sg