Audit committees (ACs) continue to face significant challenges in overseeing companies’ compliance in financial reporting, legal and regulatory matters. In our first article, we summarize these year-end issues in preparation for the reporting season ahead.

We follow with a more in-depth look at the Accounting and Corporate Regulatory Authority's (ACRA) revised Financial Reporting Surveillance Program (FRSP) policies and processes effective from 1 April 2017, and the focus areas for FY2017 financial statements review.

We hope these discussions are useful as you prepare for conversations with the board, management and external auditors.
Audit committees (ACs) continue to face significant challenges in overseeing companies’ compliance in financial reporting, legal and regulatory matters. We take a look at the following year-end issues in preparation for the reporting season ahead.

### Regulatory and reporting

- **New financial reporting framework and accounting standards**
- **ACRA’s Financial Reporting Surveillance Program**
- **Sustainability reporting mandatory for listed companies from 2017**

### Tax

- **Global focus on BEPS**
- **The future of tax reporting and transparency**
- **US tax reform**

#### Regulatory and reporting

**New financial reporting framework and accounting standards**

In December 2017, the Accounting Standards Council (ASC) issued the Singapore Financial Reporting Standards (International) (SFRS(I)s). The new financial reporting framework is available for application for annual periods beginning on or after 1 January 2018. Also effective on the same date are the Financial Reporting Standards (FRS) 115 *Revenue from Contracts with Customers* and the FRS 109 *Financial Instruments*. The new FRS 116 *Leases* is effective for annual periods beginning on or after 1 January 2019.

Companies face a steady flow of new standards and interpretations that will affect different areas of accounting, measurement, presentation and disclosure. The changes may impact business decisions, such as the structuring of particular transactions, and some of these changes could potentially impact information systems.

With the mandatory adoption dates of significant new accounting standards looming, and continued investor and regulatory scrutiny of public company disclosures, ACs should ensure that management is on track with implementation plans and ready to make required disclosures in a timely and accurate manner.

**ACRA’s Financial Reporting Surveillance Program**

In January 2018, the Accounting and Corporate Regulatory Authority (ACRA) announced the revision to FRSP policies and processes, and the areas of review focus for the FY2017 financial statements. Under the revised FRSP regime, ACRA will review financial statements for any indication of a material misstatement, and where financial statements are found to contain material findings or findings of significance, ACRA will work with companies to correct the findings by restating the financial statements.
When a company refuses to remEDIATE within prescribed time or in egregious cases, ACRA will consider enforcing directors’ duties under the Companies Act (i.e., sanction against directors) and where necessary, entity-specific press notice will be issued to inform the public.

**Sustainability reporting mandatory for listed companies from 2017**

Globally, there is growing reliance by investors on the use of nonfinancial performance to make decisions and draw conclusions on the value of a company.

On 20 June 2016, the Singapore Exchange (SGX) introduced sustainability reporting for listed companies on a “comply or explain” basis, effective for financial year ending on or after 31 December 2017. With the introduction of this regulation, the quantity of sustainability disclosures is expected to increase, but the quality of reports remains to be seen.

It may be easy to demonstrate numbers and achievements in sustainability but the crux lies in the materiality and quality of disclosures, and how these disclosures can provide business insights. With clear guidelines by the SGX, more companies can step up their game and report in a more transparent and balanced manner.

As sustainability reporting continues to evolve, we expect to see greater alignment of financial and nonfinancial reporting, particularly as organizations integrate sustainability concerns into their core business strategy.

**Questions to consider**

1. What are the internal controls over financial reporting and what key actions have been taken by the management to implement revenue recognition, financial instruments, leases and other new accounting standards?
2. Did the entity consider the impacts of change in revenue recognition patterns on cost and margin recognition, and other effects of the new standard, such as financial covenants and incentive plans?
3. What disclosure has management provided or considered with regards to the adoption of the new accounting standards?
4. What is the planned transition method and expected timing of implementation for the new standards?
5. Do all departments in the company look at sustainability practices and disclosures as a collective responsibility, and disclose the sustainability aspects openly to stakeholders by way of various channels ranging from print reports to websites?

**Tax**

Tax policy and tax controversy are high on the list of issues that ACs should follow closely in the coming year. Geopolitical uncertainty is shifting tax compliance risk from emerging markets to developed economies, with the US, UK and Australia making it to the top five tax risk jurisdictions, together with China and India.

EY’s *2017 Tax Risk and Controversy Survey Series* finds that income taxation is undergoing a fundamental shift on a global scale, and the primary driver is the explosion of new transparency and reporting measures globally in recent years. In addition to the rapid changes to tax policy and enforcement brought by base erosion and profit shifting (BEPS) and the digital revolution, a wave of political uncertainties and unknowns, such as tax implications of Brexit and the US tax reform, have prompted businesses to analyze the potential impact these events could have on their tax strategy and business operations.

**Global focus on BEPS**

While the Organization for Economic Co-Operation and Development’s (OECD) October 2015 release of the final BEPS reports may have moved the project from theory to reality, for many organizations, the implications of BEPS remain uncertain. There has been a degree of clarity in some areas – most notably the new country-by-country reporting (CbCR) obligations introduced under Action 13 of the BEPS Action Plan – but many businesses still have a sense of uncertainty around how the implementation will unfold.

In view of the depth and breadth of the BEPS recommendations and their disparate impacts on different industries, there is no one-size-fits-all approach for BEPS. ACs should ensure that their organizations have protocols in place to continuously monitor tax law changes in the countries of operation and have an understanding of the expected impact of such changes on the organization’s tax provision. In order to reduce risk and controversy, ACs should ensure that their organizations have a robust dispute management system, as well as clear and consistently applied tax and transfer pricing policies in place.

**The future of tax reporting and transparency**

The enhanced transparency measures and new reporting requirements have profound implications for businesses’ tax compliance and reporting functions, audits and controversies, and reputational risks. There is an increased need for companies to develop a comprehensive and robust approach to managing tax risk and associated controversy.

Tax administrations are harnessing the power of digitization to make better use of limited resources and extract more value from the information collected. Tax authorities are making strategic use of data analytics to make compliance and audit determinations and are increasingly sharing
this data with tax authorities in other jurisdictions. This exposes businesses to more risk if their people, processes and systems are dated or out of sync with government requirements and expectations. ACs should ensure that the tax departments are equipped to operate in the era of digital tax by embracing enterprise initiatives and transformations that facilitate enhanced data management and compliance.

**US tax reform**

The US has enacted the first major overhaul of its federal income tax system in more than 30 years. The US tax reform legislation would include lower tax rates for corporations, pass-through businesses and individuals, a territorial international tax system, a temporary provision allowing for immediate expensing of certain capital investments, some limitation on interest deductions for corporations, and fewer targeted tax incentives.

Any new legislation would likely require companies to take steps such as marking their deferred tax assets and deferred tax liabilities to the reduced deferred tax assets and deferred tax liabilities to the reduced corporate tax rates, re-computing their effective tax rates for base changes and reduced interest deductions, calculating the toll charge on unremitting earnings and possibly, calculating a global minimum tax.

Legislation could move quickly and there will be many moving parts to the tax policy discussions in the months ahead. To keep up, ACs, together with the management, should be on board the following:

- Monitor tax policy changes and developments – both actual and potential – in key jurisdictions
- Ensure that the management models the potential impact of tax reforms that might affect any aspect of the company’s tax strategy
- Communicate and engage local and global policymakers about the potential impact of tax policy changes to ensure that they understand the business implications

Furthermore, as tax continues to be an area of frequent financial restatements, ACs should continue to monitor the related accounting and internal control implications arising from any tax changes.

**Questions to consider**

1. How does the company keep up with the developments in tax policy changes and opportunities?
2. Does the company have a strategy to manage tax risk and tax controversy?
3. Has the strategy been communicated to the AC and the rest of the board?
4. Does the organization have a clear policy explaining the company’s approach to tax planning, and are the board and management prepared to defend it publicly?
5. Has the management shifted its focus from traditional compliance activities to real-time digital audit readiness activities, and conducted a review of its technologies, processes and people to support the shift?
ACRA’s Financial Reporting Surveillance Program

Key revisions to the FRSP policies and processes

ACRA has established the FRSP to guide companies to meet the requirements of the prescribed accounting standards in Singapore for their financial reporting. ACRA may raise enquiries to solicit a comprehensive response from the company and its directors before concluding that the requirements in the accounting standards have been met.

Where financial statements reviewed are found to contain material findings or findings of significance, ACRA will work with companies to correct these findings by restating the financial statements. In situations where a company refuses to remediate within the prescribed timeline or in egregious cases, ACRA will consider enforcing directors’ duties under the Companies Act and where necessary, issue notices to inform the public as well.

ACRA has published the Guide on Review Procedures that provides information on the FRSP review procedures; we summarize the FRSP review process and remediation actions in the following pages.

Focus areas for FY2017 financial statements review

On 2 January 2018, ACRA issued Financial Reporting Practice Guidance No.1 of 2018 that highlights eight financial reporting areas that may require more attention by directors when approving the companies’ FY2017 financial statements (financial year ended between 1 January 2017 and 31 December 2017). These include impairment assessment (including reversals) of long-lived assets, recognition of one-off gain or loss and business acquisitions.

With a few major accounting standards effective in 2018 and 2019, companies should also report more progressive known or reasonably estimable quantitative information in the FY2017 financial statements to help shareholders assess the possible impact of these new accounting standards.

Directors should also ensure that minutes of directors’ meetings with sufficient details are maintained to demonstrate that there had been robust discussions on accounting matters involving significant judgments or estimates during their review of the FY2017 financial statements. We summarize the focus areas on page 8.
ACRA’s FRSP review process

ACRA reviews financial statements for any indication of a material misstatement

No indication of material misstatements

- ACRA closes the review with no points for enquiry.

No indication of material misstatements

- ACRA may send a Request Letter asking for an **opening meeting** with company representatives.

- ACRA may request for certain facts to be confirmed or additional documents to be provided.

- ACRA analyzes the relevant facts and documents obtained in consultation with the Institute of Singapore Chartered Accountants Financial Statements Review Committee (ISCA-FSRC)

Indication of material misstatements

- ACRA sends an Enquiry Letter to seek directors’ explanations.

- ACRA reviews the directors’ responses in consultation with ISCA-FSRC

- When a finding is considered judgmental and/or has significant financial impact, ACRA would obtain a second independent expert review from the Financial Reporting Technical Advisory Panel of ACRA (FRTAP).

- ACRA may engage other stakeholders such as the auditor or valuer.

- ACRA decides on the outcome after considering the expert view from FRTAP.

With material findings or findings of significance

- ACRA closes the review by requiring remedial actions such as enhancing disclosures in financial statements.

- ACRA may invite directors and management to a closing meeting before the Finding Letter is issued.

- ACRA issues Findings Letter to the directors.

No material findings or findings are minor

- ACRA closes the review with no points for enquiry.
1 Who should attend the opening meeting with ACRA?

ACRA encourages directors to assign a company representative who has a good understanding of matters identified in the Request Letter, such as the chief financial officer, and those who are in positions to provide oversight over the company’s financial reporting matters such as the chief executive officer or the audit committee chairman.

2 How should directors and management respond to the Enquiry Letter from ACRA?

To reduce the likelihood of follow-up enquiries, ACRA encourages directors and management to adopt the following good practices when responding to the Enquiry Letter:

- Address every question raised
- Explain the company’s circumstances and commercial substance of transactions
- Provide insights into the basis for adopting that accounting treatment
- Provide insights into how ACRA’s concerns may be alternatively addressed
- Maintain consistent fact pattern in all explanations

ACRA expects all directors to review and sign off on the responses to the Enquiry Letter before they are submitted on behalf of the board.

3 What is the purpose of the closing meeting?

During the closing meeting, ACRA informs the directors and management of the findings of significance and explains how and by when remedial action must be undertaken and completed.

4 Would ACRA check the proposed restatements before they are effected if the company is required to restate its financial statements?

To facilitate timely restatements, ACRA will not check the proposed restatements before they are effected.

After the restated financial statements have been issued, companies and their directors will submit the relevant extracts of the financial statements reflecting those restatements, together with supporting explanations and documents, to ACRA.

ACRA then checks to ensure that remediation is carried out satisfactorily and in accordance with the prescribed timeline.

FRSP remediation actions

<table>
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<tr>
<th>Material finding</th>
<th>Significant finding</th>
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<tbody>
<tr>
<td>Restate comparatives or add/improve disclosures in the next year’s financial statements</td>
<td>Restate comparatives in the next results announcements</td>
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<tr>
<td>+ Restate comparatives in the next results announcements</td>
<td>+ Restate comparatives in the next results announcements</td>
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<tr>
<td>+ Restate, re-audit and re-file past year(s)’ financial statements within timeline set</td>
<td>+</td>
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</tbody>
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After the restated financial statements have been issued, directors are required to submit the following documents to ACRA:

- Relevant extracts of the financial statements reflecting the restatements
- Supporting explanations and documents

If the restatement is not done properly or within the prescribed timeline, ACRA will consider:

- Issuing notices to inform the public
- Enforcing directors’ duties under the Companies Act

1 Findings are evaluated based on their impact to key measures used by investors such as revenue, profits and cash flows, based on both quantitative and qualitative factors.
2 To facilitate timely restatements, ACRA will not check the proposed restatements before they are effected.
Focus areas for FY2017 financial statements review

1. Upcoming changes in accounting standards
   - Is the financial effect adequately disclosed?
   - As the new revenue and financial instruments standards will be effective by the time the FY2017 financial statements are issued, has the company reported more progressive developments, including known or reasonably estimable quantitative information in the FY2017 financial statements, to help users assess the possible impact from the adoption of new accounting standards?

2. Going concern
   - Can the company continue to operate in the near term (at least 12 months)?
   - Does the company have indications of financial difficulty such as substantial operating losses, net current liability, unfavorable financial ratios, inability to pay creditors, breach of loan covenants or significant uncertainty on refinancing of maturing borrowings?
   - If yes, have the directors evaluated the key assumptions used to assess whether the company is able to continue as a going concern for a period that covers at least, but not limited to 12 months from the financial year-end?
   - If the directors conclude that the company is able to continue as a going concern but material uncertainties exist, have the directors disclosed fully the significant judgments made in that the going concern assumption is appropriate to enable investors to make informed decisions?
   - When the going concern assumption is supported by a letter of financial support from a related party, have the directors evaluated if the related party has the realistic ability and intention to provide the stated support?

3. Long-life assets value and impairment testing
   - Are there indicators of impairment, such as loss-making operating segments, loss of customers, cancellation of orders or plans to discontinue or structure operations?
   - Are the key assumptions used by management in the impairment test reasonable and supportable? Are they in line with the current business plan, economic outlook and other industry-specific conditions?
   - Did the company have material goodwill and other intangible assets with indefinite useful lives? If yes, has the impairment test been conducted annually even where there is no indication of impairment?
   - Are the key assumptions used by management in the impairment test reasonable and supportable? Are they in line with the current business plan, economic outlook and other industry-specific conditions?
   - Is there any change in the methodology used in the impairment test? If yes, have the directors evaluated the reason for the change?
   - Where the recoverable amount is determined using value-in-use method, have the directors asked management the following questions:
     - How did the management ensure that all cash outflows required to generate projected cash inflows are included in the impairment test?
     - Does the discount rate reflect the risks specific to the asset, rather than using the company's borrowing rate, the country's inflation rate or interest rate for government bond without any adjustments?
     - Are there significant differences between past year's projections and the actual results? If so, have the differences been properly explained?
     - Are the key assumptions used in the impairment test comparable to those used by industry peers?
Focus areas for FY2017 financial statements review (cont’d)

3 Long-life assets value and impairment testing

Where the headroom is small or the quantum of impairment charge is not aligned with the directors’ understanding of the business, have the directors:

- Asked the management which are the key assumptions where a reasonable possible change would significantly affect the impairment charge?
- Reviewed those key assumptions carefully to ensure that they are not overly aggressive or conservative?
- Requested for sensitivity analysis to assess the impact of reasonably possible changes of these assumptions?

- If there is a reversal of impairment loss, have the directors confirmed the following:
  - The reversal is a result of a real improvement in underlying factors and not from discounting effect such as when projected cash flows are getting closer to the reporting date.
  - The reversal of depreciable or amortizable asset is limited to its carrying amount, net of depreciation or amortization, had no impairment loss been recognized.
  - The reversal is not attributable to goodwill, which is prohibited by the standard?

Have the disclosures that are tailored to the facts and circumstances been made, particularly the commercial reasons for recognizing or not recognizing the impairment loss?

- Where the headroom is small and the carrying value of the assets is material, have the sensitivity analysis been adequately disclosed for investors to assess the safety margin?

Aside from the discount rate and long-term or terminal growth rate, have the key assumptions such as revenue growth, margins and specific costs that could significantly affect the recoverable amount been disclosed?

Has the company disclosed whether the assumptions reflect past experience or are consistent with external sources of information?

- If the assumptions do not reflect past experience or are not consistent with external sources of information, has the company disclosed how and why they differ from past experience or external sources of information?

4 Significant one-off gains or losses

- Are there significant one-off gains or losses arising from transactions arranged in certain legal forms for various reasons?
- Are these transactions accounted for based on the economic substance of the arrangements, rather than their legal forms?
  - Have all relevant facts and circumstances been considered, including the commercial intent of entering into the transactions, the contractual terms and financial instruments used?
  - Have alternative accounting treatment(s), if any, been evaluated? Have the deliberations for the adopted accounting treatment that is most appropriate been documented so that the directors’ decision could withstand future or external scrutiny?
  - Have significant judgments been made with supportable evidence and where necessary, advice from experts?

Does the company have assets or liabilities where the fair value may lead to significant gains or losses (e.g., investment property, derivatives, biological assets and investments)?

- Have the assistance of independent professional valuers been sought if such items are significant and specialized in nature?
- When a valuer is engaged, have the valuer’s credential, scope of work (full or desktop valuation) and valuation interval considering factors such as the significance of the asset and volatility of prices been reviewed?
- Has the fair value change been assessed on whether it is in line with directors’ understanding of the market conditions and assets attributes?
Focus areas for FY2017 financial statements review (cont’d)

5 Consolidation or equity accounting

- Where external parties have special rights to participate in decision-making of the investees or where potential voting rights exist, has the classification of investees been assessed?
- What is the value that each business partner (i.e., shareholder, lender or option holder) bring to the business cooperation?
- What is the rationale for including reserved matters over the relevant activities of investee that requires unanimous consent from all shareholders?
- What is the rationale for including contractual rights that accord power to direct relevant activities of the investee in the investment agreement, such as notes receivables and warrants investment agreements?
- Has the management evaluated the contractual rights in the agreements and considered whether the rights are “protective” or “substantive” for accounting purposes?
- Have the disclosures on significant judgment made in accounting for the investee as a subsidiary, associate or joint venture or joint operation been made?

6 Business acquisitions

- What are the reasons for acquiring the business and the factors considered in determining the purchase price paid for the business?
- Have significant specific intangible assets, for which a premium was paid, been carved out from goodwill and separately recognized?
- Has a professional valuer been engaged to identify and value the specific intangible assets for business acquisitions with material goodwill?
- Is the scope of valuation of the professional valuer restricted to identifying only specific intangible assets pre-identified by management? If yes, what is the rationale for the scope restriction?
- Does the scope of valuation include assessing reasonableness of management assumptions used in the overall valuation exercise?
- Has the acquisition date been properly determined?

7 Statement of cash flows

- Have adjustments been made to operating cash flows to exclude items that are not relating to working capital, e.g., foreign currency translation differences arising from the consolidation of foreign subsidiaries that are taken directly to equity and do not include cash flows?

8 Significant judgments and estimates

- Does the company have a rigorous process to identify and evaluate significant judgments and critical estimates made by directors in the preparation of financial statements?
- Have judgments with the most significant impact and are most subjective or complex been completely and meaningfully disclosed?
- Are the disclosures in the financial statements consistent with other publicly available information of the entity (e.g., SGX announcements, shareholders’ circulars, presentation slides to the analysts)?
Regulatory updates

Consultation to revise the Code of Corporate Governance

In January 2018, the Corporate Governance Council (Council) released a consultation paper on its recommendations to revise the Code of Corporate Governance (Code). The key objective of the revisions is to reinforce board competencies through active board renewal, strengthening of director independence and enhancing board diversity. Other proposed Code revisions include greater emphasis on disclosures of the relationship between remuneration and value creation, and the need for companies to consider and balance the needs of all stakeholders.

Beyond Code revisions, the Council is also proposing to clarify the intent of the comply-or-explain regime and the expectations of listed companies’ corporate governance disclosures. The Council recommends that:

- Compliance with the Code Principles is mandatory
- Companies are required to describe their corporate governance practices with reference to both the Principles and the Provisions underpinning each Principle
- Variations from the Provisions are acceptable to the extent that companies explicitly state and explain how their practices are consistent with the intent of the relevant Principle.

Consequential amendments to the SGX Listing Rules are also set out in the consultation paper. Feedback is due by 15 March 2018. Details of the consultation can be found here.

SGX consults on quarterly reporting

In January 2018, SGX sought feedback on whether to retain quarterly reporting (QR).

If QR is retained, SGX proposes the following options:

1. Companies with market capitalization of S$150m or more will do QR compared to the current S$75m cap.
2. Companies with market capitalization of S$150m and a shareholder with at least 15% of the companies' shares must do QR.
3. The above-mentioned options are tied to market capitalization. SGX is also seeking feedback on whether this is appropriate, and if not, other options that should be considered.

If QR is retained, SGX is also proposing that:

1. Minority shareholders of a reporting company can vote to opt out of QR every three years.
2. Content of any report for the first and third quarter will be simplified to the balance sheet, income statement, cash-flow statement, review of performance commentary of significant trends and board confirmation.
3. New issuers may be exempted from QR until the third AGM after the listing date.

Subject to feedback and approval of the Monetary Authority of Singapore, the proposals may be implemented together or separately. If adopted, SGX expects to implement a new QR requirement in the second half of 2018.

The public can submit feedback until 9 February 2018. Details can be found here.
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