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FINANCIAL REPORTING UPDATES

3Q 2020

This is your quarterly update on all things relating to international financial reporting standards or Singapore Financial Reporting Standards. We will bring you up to speed on topical issues, provide our comments and view points on any significant developments.

AUGUST 2020

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IASB issues amendments to IFRS Standards

A package of narrow-scope amendments to IFRS Standards

On 14 May 2020, the International Accounting Standards Board (IASB) has issued several small amendments to IFRS Standards.

The package of amendments includes narrow-scope amendments to three Standards as well as the Annual Improvements, which are changes that clarify the wording or correct minor consequences, oversights or conflicts between requirements in the Standards.

- **Amendments to IFRS 3 *Business Combinations*** update a reference in IFRS 3 to the Conceptual Framework for Financial Reporting without changing the accounting requirements for business combinations.
- **Amendments to IAS 16 *Property, Plant and Equipment*** prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss.
- **Amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*** specify which costs a company includes when assessing whether a contract will be loss-making.
- **Annual Improvements** make minor amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards*, IFRS 9 *Financial Instruments*, IAS 41 *Agriculture* and the Illustrative Examples accompanying IFRS 16 *Leases*.

All the above amendments are effective 1 January 2022.

Amendment to IFRS 16 *Leases*

On 28 May 2020, IASB has issued an amendment to IFRS 16 *Leases* to make it easier for lessees to account for covid-19-related rent concessions such as rent holidays and temporary rent reductions.

The amendment exempts lessees from having to consider individual lease contracts to determine whether rent concessions occurring as a direct consequence of the covid-19 pandemic are lease modifications and allows lessees to account for such rent concessions as if they were not lease modifications. It applies to covid-19-related rent concessions that reduce lease payments due on or before 30 June 2021. This optional exemption gives timely relief to lessees and enables them to continue providing information about their leases that is useful to investors. The amendment does not affect lessors.

The amendment is effective 1 June 2020 but, to ensure the relief is available when needed most, lessees can apply the amendment immediately in any financial statements (interim or annual) not yet authorised for issue.

Amendments to IFRS 17 *Insurance Contracts*

On 25 June 2020, IASB has issued amendments to IFRS 17 *Insurance Contracts* aimed at helping companies implement the Standard and making it easier for them to explain their financial performance.

The fundamental principles introduced when IASB first issued IFRS 17 in May 2017 remain unaffected. The amendments, which respond to feedback from stakeholders, are designed to:

- reduce costs by simplifying some requirements in the Standard;
- make financial performance easier to explain; and
- ease transition by deferring the effective date of the Standard to 2023 and by providing additional relief to reduce the effort required when applying IFRS 17 for the first time.

The deferral of the effective date by two years, to annual reporting periods beginning on or after 1 January 2023, is intended to allow time for an orderly adoption of the amended IFRS 17 by jurisdictions around the world. This should enable more insurers to implement the new Standard at the same time.

IASB has also issued an amendment to the previous insurance contracts Standard, IFRS 4, so that eligible insurers can still apply IFRS 9 *Financial Instruments* alongside IFRS 17.

IASB defers the effective date of amendments to IAS 1

On 15 July 2020, IASB has issued an amendment to defer by one year the effective date of *Classification of Liabilities as Current or Non-current*, which amends IAS 1 *Presentation of Financial Statements*.

Amendments to IAS 1 *Classification of Liabilities as Current or Non-current* was issued in January 2020, effective for annual reporting periods beginning on or after 1 January 2022. However, in response to the COVID-19 pandemic, IASB has deferred the effective date by one year to provide companies with more time to implement any classification changes resulting from those amendments. Amendments to IAS 1 *Classification of Liabilities as Current or Non-current* is now effective for annual reporting periods beginning on or after 1 January 2023.

IASB did not make any changes to *Classification of Liabilities as Current or Non-current* other than the deferral of the effective date.

ASC issues amendments to SFRS(I) / FRS Standards

Amendment to SFRS(I) 16 / FRS 116: *Covid-19-Related Rent Concessions*

On 28 May 2020, the Accounting Standards Council Singapore (ASC) has issued Amendment to SFRS(I) 16: *Covid-19-Related Rent Concessions* and Amendment to FRS 116: *Covid-19-Related Rent Concessions*, effective for annual reporting periods beginning on or after 1 June 2020. An entity may early apply the amendments in financial statements not authorised for issue at 28 May 2020.

Amendments to SFRS(I) 1-1 / FRS 1: *Classification of Liabilities as Current or Non-current*

On 29 May 2020, ASC has issued Amendments to SFRS(I) 1-1: *Classification of Liabilities as Current or Non-current* and Amendments to FRS 1: *Classification of Liabilities as Current or Non-current*, effective for annual reporting periods beginning on or after 1 January 2022.

Amendment to SFRS(I) 1-1 / FRS 1: *Classification of Liabilities as Current or Non-current*—Deferral of Effective Date

On 23 July 2020, ASC has issued Amendment to SFRS(I) 1-1: *Classification of Liabilities as Current or Non-current*—Deferral of Effective Date and Amendment to FRS 1: *Classification of Liabilities as Current or Non-current*—Deferral of Effective Date. The Amendment defers the effective date of *Classification of Liabilities as Current or Non-current* to annual reporting periods beginning on or after 1 January 2023.

ACRA's Audit Practice Bulletin No. 1 of 2020 *Key Audit Considerations – COVID-19*

On 20 May 2020, the Accounting and Corporate Regulatory Authority (ACRA) has issued Audit Practice Bulletin No.1 of 2020 to guide public accountants in the conduct of audits during the COVID-19 situation.

The bulletin covers the following key areas of audit that may be impacted arising from the COVID-19 outbreak:

- Identifying and Assessing the Risk of Material Misstatements and Materiality in Planning and Performing an Audit
- The Auditor's Responses to Assessed Risks
- Audit Evidence
- Group Audits
- Subsequent Events
- Going Concern
- Forming an Opinion and Reporting on Financial Statements
- Key Audit Matters
- Internal Control Considerations
- Impact from support measures by government
- Communications with Those Charged with Governance
- Quality Control of Audit Firms

This Audit Practice Bulletin provides guidance on the audit approach to address / tackle the accounting implications arising from COVID-19 (which we have covered in our FKT Financial Reporting Updates 2Q 2020).

ACRA has issued Financial Reporting Practice Guidance No. 1 of 2020

On 22 May 2020, ACRA has issued the following:

ACRA's Financial Reporting Practical Guidance No. 1 of 2020

To guide directors in the review and approval of their company's financial statements during the COVID-19 situation, ACRA is publishing the proposed areas of review focus for the financial statements that are affected by the COVID-19 pandemic. It highlights warning signs of some possible non-compliance(s) with accounting standards, and provides directors with questions to ask management and statutory auditors when assessing the impact from COVID-19 pandemic on the financial statements. Directors are urged to pay more attention to the following financial reporting areas:

1. Financial Position and Sustainability

   In respect of the carrying amount of assets

   Property, plant and equipment, goodwill and other intangible assets

   Due to the adverse impact of the COVID-19 pandemic on the profitability, asset values and market capitalisation of many companies, more vigilance and scepticism should be applied on impairment assessment. Accordingly, directors should expect management to perform impairment tests, and a smaller headroom (or impairment loss to be recognised) to result from these tests.

If the headroom from an impairment test does not fall within expectations, i.e. not smaller, but similar to, or larger than, that in the previous year, directors should check that:

(a) the discount rate used (to estimate the asset's recoverable amount) is updated to reflect the higher risks associated with the COVID-19 situation;

(b) the risks associated with the COVID-19 pandemic are reflected in the forecasted cash flows (e.g. sales, gross margin and changes in working capital) used to estimate the asset's recoverable amount;

(c) an expected cash flow approach based on a range of probability-weighted possible outcomes (according to their business strategies) is used;

(d) sensitivity analysis for reasonably possible changes in key assumptions (e.g. growth rate, discount rate) are meaningfully disclosed in the financial statements. In line with market uncertainties, directors should also expect that the reasonably possible changes in key assumptions would be higher than the typical 1% to 2% disclosed in the past.

Investment properties and other non-current assets held at fair value

In view of the circuit breaker measures, property valuers may not be able to conduct onsite inspections to value some properties, and can only perform desktop valuations based on information provided by the owner or from other sources. Directors should ensure that management has provided accurate information to valuers in these areas.

In the event that the fair value of some properties is expected to change significantly between the year-end date and the date that the financial statements is authorised for issue, directors should consider performing a revaluation.

Inventories

Directors should also ensure that inventories are written down to their net realisable value, especially those seasonal inventories and perishable products, in view of the reduced inventory movement, lower commodity prices and changing patterns of customer purchases, as a result of the COVID-19 pandemic.

Whilst some manufacturing companies may not be producing at their usual capacities as a result of the lockdown/restrictive measures implemented by the government globally, fixed overheads (such as rental and depreciation of fixed assets in all production lines) should continued to be expensed off in the period in which they are incurred.

Trade and other receivables and contract assets

Due to unstable trading conditions and some customers' inability to pay debts when due, estimating expected credit loss allowance (ECL) will require more judgments. Directors are reminded to apply more rigour when reviewing management's ECL estimates:

(i) consider re-segmenting debt portfolios based on factors that reflect risk characteristics such as by industry and geographical region, rather than only by the aging of amounts due and historical repayment profile;

(ii) consider whether securities obtained on debts such as a pledged asset or a guarantee issued by a third party, may be impacted;

(iii) consider how forward-looking adjustments should be updated to reflect the uncertainties from COVID-19; and

(iv) identify each significant credit incident(s) and/or loss(es) after the year-end date (e.g. bankruptcy of a major debtor), and consider whether each incident/loss should be an adjusting event to be recorded at year end.

In respect of carrying amounts of liabilities

Provisions

Directors should ask management to identify any onerous, or potentially onerous, contracts. For instance, If a company is making plans to restructure, directors are reminded that the related expense can be recognised only when there is a detailed formal plan and valid expectations had been set with the employees who will be affected. Provision for future operating losses or business recovery costs is strictly prohibited.

Borrowings

Due to unexpected impairment / write-downs in the carrying amount of assets and additional provisions being made, some companies may inadvertently breach loan covenants. To avoid last minute surprises, directors should ask management to forecast financial performance and positions for assessing compliance with loan covenants. In the case where a breach is possible, management should engage lenders early for waivers and/or to negotiate for re-financing arrangements. Waivers obtained after year-end cannot be used to remedy the classification at year-end.

Going Concern, Disclosures and Others

Going concern

Declining sales and collection issues can have an immediate impact on the working capital, particularly when fixed overhead costs are substantial and inevitable. Directors should carefully evaluate with management the impact on projected working capital and the company’s ability to repay its debt obligations as and when they fall due.

Cash flow projections should also be forecasted in sufficient granularity (e.g. by month) to ensure the company remains liquid and viable for the next 12 months and beyond. In cases where the financial statements may be approved many months after the financial year-end, cash flow projections should be updated and re-assessed before authorising the financial statements.

Financial instruments

As the prices for most commodities have fallen, in particular, oil prices that have dropped to an unprecedented low, companies in the energy and other commodity industries should re-look at the economic viability of their long-term commodity contracts, both from the financial sustainability of their counterparties and fair valuation of the contracts.

Directors should work with management to tailor the financial risk management disclosures to the company’s actual circumstances, and avoid boilerplate disclosures. Where applicable, the following should be disclosed:

- concentration of credit risk for certain sectors affected by the COVID-19 outbreak; and
- the company’s plan to manage liquidity risk when its cash flows from operating activities has turned negative, or if it faced difficulties in accessing cash through financing means.

Subsequent events

Notwithstanding that the COVID-19 outbreak is a non-adjusting event for companies with 31 December 2019 year-end, directors should pay attention to material subsequent events that require disclosures, such as:

- significant decline in carrying values of certain assets (e.g. commodity inventories, quoted investment securities) after the year-end;
- management’s plan to discontinue an operation, or temporarily downsize certain operations, after the year-end; or
- if certain acquisition or disposal of assets or businesses fell through due to inability to meet precedent conditions in the agreements after the year-end.

Government relief measures

Directors should discuss with management the applicable relief measures that were introduced by the government to alleviate the negative impact arising from the COVID-19 outbreak, and determine their appropriate accounting treatments. In the Singapore context, this includes accounting for the Singapore property tax rebate and the Jobs Support Scheme (JSS) which were announced by our Singapore Government as part of the relief measures.

The Institute of Singapore Chartered Accountants (ISCA) has published Financial Reporting Bulletins 5 and 6 to provide guidance on how to account for property tax rebates and JSS, respectively.

2. Internal control and audit considerations

   Due to movement restriction / lockdown measures implemented globally (including Singapore) to combat COVID-19, telecommuting becomes the "new normal". Such change in work procedures may introduce gap(s) in internal controls.

   Directors should engage management and internal auditors on measures put in place to mitigate risks, particularly for high risk areas such as cash management. Directors should also expect management to review and ensure adequate segregation of duties for key processes. In addition, Audit Committees should revise internal audit plans to prioritise the audits of high risk areas, and find ways to mitigate the risks.

   From the audit perspective, some statutory auditors may face limitation in the scope of their work (as a result of travel restrictions imposed due to COVID-19). Directors ought to work with management to facilitate the work of statutory auditors. If the issuance of the modified audit reports cannot be avoided, directors must implement a plan to address the qualification with the aim to receive a clean audit report in the next financial year.

   Directors and management are also advised to engage statutory auditors early to discuss the audit plan for the next financial year. For valuations and other accounting areas that involve more judgements and estimates due to market volatility, directors are highly encouraged to engage the help of specialists. It is essential for directors to ensure that management provides sufficient cooperation to the statutory auditors, and for statutory auditors to invest sufficient audit efforts in addressing the risks and issues arising from the COVID-19 outbreak.

ACRA has issued Financial Reporting Surveillance Programme Report 2020

On 14 July 2020, ACRA published the Financial Reporting Surveillance Programme (FRSP) Third Report 2020.

This FRSP report highlights key findings from review of annual financial statements that were selected by ACRA.

The three areas with the highest instances of material non-compliance were as follows:
a. accounting for major complex transactions (5 instances);
b. presentation in the statements of cash flows (4 instances); and
c. business valuations or impairment assessments (3 instances).

These areas had been suggested as areas of review focus by directors in the Practice Guidance issued by ACRA to guide directors in their review of 2016 and 2017 FS.

Contact us

If you need assistance or advice on the above, we are here to assist you.

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