



# Changes to the financial reporting framework in Singapore



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#### **Acronyms**

ASC	Accounting Standards Council
ED	Exposure Draft
FRS	Singapore Financial Reporting Standards
FASB	United States Financial Accounting Standards Board
IASB	International Accounting Standards Board
ICPAS	Institute of Certified Public Accountants of Singapore
IFRIC	IFRS Interpretations Committee (known as International Financial Reporting Interpretations Committee before 31 March 2010)
IFRS	International Financial Reporting Standards
INT FRS	Interpretation of Singapore Financial Reporting Standards
RAP	Recommended Accounting Practice
US GAAP	United States Generally Accepted Accounting Principles

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# Introduction

The purpose of this publication is to provide a regular update of the recent changes in the Singapore financial reporting framework which we believe are important to accounting and audit professionals.

In this edition, we continue to provide a summary of the new/revised FRSs and INT FRSs, as well as Exposure Drafts issued since the last edition in November 2009, including an updated comparison of FRS against IFRS. We have also retained summaries of the new/revised FRSs and INT FRSs issued before November 2009, which are effective for financial periods beginning on or after 1 June 2009.

# Section I: Financial Reporting Standards

# Revised/amended FRSs issued in 2008

Revised/amended FRS	
General amendments	<i>Improvements to FRSs (October 2008)</i> - Amendment to FRS 105 <i>Non-Current Assets Held for Sale and Discontinued Operations</i> (effective for annual periods beginning on or after 1 July 2009)
FRS 39 (Amended)	<i>Financial Instruments: Recognition and Measurement</i> - Eligible Hedged Items (effective for annual periods beginning on or after 1 July 2009)

## *Improvements to FRSs (October 2008)*

The Improvements to FRSs are intended to deal with non-urgent, minor amendments to FRSs. These amendments focus on areas of inconsistency in FRSs or where clarification of wording is required. Most of the key improvements in this first set of Improvements to FRSs were effective from 1 January 2009 and have been excluded from this summary. The following key improvement became effective from 1 July 2009.

Standard	Subject of amendment	New requirements
FRS 105 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	Plan to sell a controlling interest in a subsidiary	Clarification that assets and liabilities of a subsidiary should be classified as held for sale if the parent is committed to a sale plan involving loss of control of the subsidiary, regardless of whether the entity will retain a non-controlling interest after the sale.  Effective date aligned with FRS 27 (2009) (i.e. from 1 July 2009).



## FRS 39 *Financial Instruments: Recognition and Measurement* - Eligible hedged items

The amendment clarifies how the existing principles underlying hedge accounting should be applied in below given situations:

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

### **Identifying inflation as a hedged risk or portion**

The amendment clarifies that it is not possible to designate the inflation component of a fixed rate instrument as a hedged risk or portion because inflation is not a separately identifiable component of such an instrument. Also, changes in inflation do not have a reliably measurable effect on the cash flows or fair value of the entire financial instrument. However, inflation may only be hedged in the instance where changes in inflation are a contractually-specified portion of cash flows of a recognised financial instrument. This may be the case where an entity acquires or issues inflation-linked debt. In such circumstances, the entity has a cash flow exposure to changes in future inflation that may be designated as a hedged portion of an inflation linked bond.

### **Hedging one sided risk with options**

FRS 39 permits an entity to designate purchased (or net purchased) options as a hedging instrument in a hedge of a financial or non-financial item. An entity may designate an option as a hedge of changes in the cash flows or fair value of a hedged item above or below a specified price or other variable (a one-sided risk).

The amendment make it clear that the 'intrinsic value' not the 'time value' of an option reflects a one-sided risk, therefore, an option designated in its entirety cannot be perfectly effective. The 'time value' of a purchased option is not a component of the forecast transaction that impacts profit or loss. Entities can continue to use option-hedging but will need to designate only the intrinsic value of the option within the relationship. As a result of this designation, changes in the time value of the option will be recognised immediately in profit or loss.

The amendments are to be applied retrospectively for annual periods beginning on or after 1 July 2009. Therefore, if an entity has a hedge accounting relationship which, following the amendments would be considered non-qualifying, the entity must restate its comparative information, including the opening reserves, in order to reflect that hedge accounting was not applied in the reporting period.

It is not permitted to restate the comparatives to reflect an alternative hedge accounting designation as hedge accounting can only ever be applied prospectively when all hedge accounting documentation is complete.

# Revised/amended FRSs and INT FRSs issued in 2009

New/revised/amended FRSs/INT FRSs	
General amendments	<i>Improvements to FRSs (June 2009)</i> (refer to document for effective dates)
FRS 27 and FRS 103 (Revised)	Revised FRS 27 <i>Consolidated and Separate Financial Statements</i> and FRS 103 <i>Business Combinations</i> (effective for annual periods beginning on or after 1 July 2009)
FRS 32 (Amended)	FRS 32 <i>Financial Instruments: Presentation</i> - Amendments on Classifications of Rights Issues (effective for annual periods beginning on or after 1 February 2010)
FRS 39 and INT FRS 109 (Amended)	FRS 39 <i>Financial Instruments: Recognition and Measurement</i> and INT FRS 109 <i>Reassessment of Embedded Derivatives</i> - Amendments regarding the assessment of embedded derivatives on reclassification (effective for periods ending on or after 30 June 2009)
FRS 101 (Revised)	<i>First-time Adoption of Financial Reporting Standards</i> - Amendments to improve the structure of the Standard (effective for annual periods beginning on or after 1 July 2009)
FRS 101 (Amended)	<i>First-time Adoption of Financial Reporting Standards</i> - Additional Exemptions for First-time Adopters (effective for annual periods beginning on or after 1 January 2010)
FRS 102 (Amended)	FRS 102 <i>Share-based payment</i> – Group Cash-settled Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2010)
INT FRS 117	<i>Distributions of Non-cash Assets to Owners</i> (effective for annual periods beginning on or after 1 July 2009)
INT FRS 118	<i>Transfer of Assets from Customers</i> (effective for transfers of assets on or after 1 July 2009)

## *Improvements to FRSs (2009)*

This is the second set of Improvements to FRSs that are intended to deal with non-urgent, minor amendments to FRSs. These amendments focus on areas of inconsistency in FRSs or where clarification of wording is required. The improvements are effective from 1 January 2010 except if otherwise specified.

### **Detail of amendments**

The following table provides a summary of each of the amendments.

Standard	Subject of amendment	New requirements
FRS 102 <i>Share-based Payment</i>	Scope of FRS 102 and revised FRS 103	Amendment to confirm that, in addition to business combinations as defined by FRS 103 (2009) <i>Business Combinations</i> , contributions of a business on formation of a joint venture and common control transactions are excluded from the scope of FRS 102 <i>Share-based Payment</i> .  Effective for annual periods beginning on or after 1 July 2009. Linked to application of FRS 103 (2009).
FRS 105 <i>Non-current Assets Held for Sale and Discontinued Operations</i>	Disclosures required in respect of noncurrent assets (or disposal groups) classified as held for sale or discontinued operations	Amendment to clarify that FRS 105 <i>Non-current Assets Held for Sale and Discontinued Operations</i> specifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations. Consequently, disclosures in other FRSs do not apply to such assets (or disposal groups) unless: <ul style="list-style-type: none"> <li>• Those FRSs specifically require disclosures in respect of noncurrent assets (or disposal groups) classified as held for sale or discontinued operations; or</li> <li>• The disclosures relate to the measurement of assets or liabilities within a disposal group that are outside the scope of FRS 105's measurement requirements and the information is not disclosed elsewhere in the financial statements.</li> </ul> <p>To be applied prospectively. Earlier application permitted</p>
FRS 108 <i>Operating Segments</i>	Disclosure of information about segment assets	Minor textual amendment to the Standard, to clarify that an entity is required to disclose a measure of segment assets only if that measure is regularly reported to the chief operating decision maker.  Segment information for prior periods presented as comparatives shall be restated unless the necessary information is not available and the cost to develop it would be excessive.  Earlier application permitted.

FRS 1 <i>Presentation of Financial Statements</i>	Current/non-current classification of convertible instruments	<p>Clarification that the potential settlement of a liability by the issue of equity is not relevant to its classification as current or non-current.</p> <p>By amending the definition of current liability, the amendment permits a liability to be classified as non-current (provided that the entity has an unconditional right to defer settlement by transfer of cash or other assets for at least 12 months after the accounting period) notwithstanding the fact that the entity could be required by the counterparty to settle in shares at any time.</p> <p>Earlier application permitted.</p>
FRS 7 <i>Statement of Cash Flows</i>	Classification of expenditures on unrecognised assets	<p>Amendment to require that only expenditures that result in a recognised asset in the statement of financial position can be classified as investing activities.</p> <p>Earlier application permitted.</p>
FRS 17 <i>Leases</i>	Classification of leases of land and buildings	<p>Amendments made to IAS 17 - Deletion of specific guidance regarding classification of leases of land. Leases of land should be classified as either finance or operating using the general principles of IAS 17.</p> <p>To be applied retrospectively to existing leases if the necessary information is available at the inception of the lease. Otherwise land leases should be reassessed on the date of adoption of the amendment. Earlier application permitted.</p> <p>Comparison of FRS 17 and IAS 17 - Before the amendments, IAS 17 stated that land normally has an indefinite economic life and, if title is not expected to pass to the lessee by the end of the lease term, the lessee does not receive substantially all of the risks and rewards incident to ownership.</p> <p>On the other hand, FRS 17 did not explicitly state that leases of land will be operating leases unless title passes.</p> <p>Thus, with this amendment, FRS 17's treatment of leases of land does not change, but IAS 17's treatment of leases of land appears to be more consistent with FRS 17.</p>
FRS 18 <i>Revenue</i>	Determining whether an entity is acting as a principal or as an agent	<p>Additional guidance added to the appendix to FRS 18 <i>Revenue</i> regarding the determination as to whether an entity is acting as a principal or an agent.</p> <p>No effective date is applicable for this as the appendix is not part of the Standard.</p>

FRS 36 <i>Impairment of Assets</i>	Unit of accounting for goodwill impairment test	Amendment to clarify that the largest cash-generating unit (or group of units) to which goodwill should be allocated for the purposes of impairment testing is an operating segment as defined by paragraph 5 of FRS 108 <i>Operating Segments</i> (i.e. before the aggregation of segments with similar economic characteristics permitted by FRS 108.12).
		To be applied prospectively. Earlier application permitted.
FRS 38 <i>Intangible Assets</i>	Additional consequential amendments arising from revised FRS 103 (2009)	Amendments to FRS 38 <i>Intangible Assets</i> to clarify the requirements under FRS 103 (2009) regarding accounting for intangible assets acquired in a business combination.
		FRS 103 (2004) included reliability of measurement as a recognition condition for intangible assets. FRS 103 (2009), on the other hand, presumes that if an intangible asset acquired in a business combination is separable or arises from contractual or other legal rights, sufficient information exists to measure the fair value of the asset reliably.
		Related amendments are made to FRS 38 to be consistent with the recognition criteria in FRS 103 (2009).
		Effective for annual periods beginning on or after 1 July 2009. To be applied prospectively. Linked to application of FRS 103 (2009).
	Measuring the fair value of an intangible asset acquired in a business combination	Amendments to FRS 38 to clarify the description of valuation techniques commonly used by entities when measuring the fair value of intangible assets acquired in a business combination that are not traded in active markets.
		To be applied prospectively. Earlier application permitted.

FRS 39 <i>Financial Instruments: Recognition and Measurement</i>	Treating loan prepayment penalties as closely related derivatives	Clarification that prepayment options, the exercise price of which compensates the lender for loss of interest by reducing the economic loss from reinvestment risk, should be considered closely related to the host debt contract.  Earlier application permitted.
	Scope exemption of business combination contracts	Amendments to the scope exemption in FRS 39 <i>Financial Instruments: Recognition and Measurement</i> to clarify that: <ul style="list-style-type: none"> <li>• It only applies to binding (forward) contracts between an acquirer and a vendor in a business combination to buy an acquiree at a future date;</li> <li>• The term of the forward contract should not exceed a reasonable period normally necessary to obtain any required approvals and to complete the transaction; and</li> <li>• The exemption should not be applied to option contracts (whether or not currently exercisable) that on exercise will result in control of an entity, nor by analogy to investments in associates and similar transactions.</li> </ul> <p>To be applied prospectively to all unexpired contracts. Earlier application permitted.</p>
	Cash flow hedge accounting	Amendment to clarify when to recognise gains or losses on hedging instruments as a reclassification adjustment in a cash flow hedge of a forecast transaction that results subsequently in the recognition of a financial instrument. The amendment clarifies that gains or losses should be reclassified from equity to profit or loss in the period in which the hedged forecast cash flow affects profit or loss.  To be applied prospectively to all unexpired contracts. Earlier application permitted.
INT FRS 109 <i>Reassessment of Embedded Derivatives</i>	Scope of INT FRS 109 and revised FRS 103	Amendment to confirm that, in addition to business combinations as defined by FRS 103 (2009), derivatives acquired in the formation of a joint venture and in common control transactions are outside the scope of INT FRS 109.  Effective for annual periods beginning on or after 1 July 2009. To be applied prospectively. Linked to application of FRS 103 (2009).
INT FRS 116 <i>Hedges of a Net Investment in a Foreign Operation</i>	Amendment to the restriction on the entity that can hold hedging instruments	Amendment to clarify that hedging instruments may be held by any entity or entities within the group. This includes a foreign operation that itself is being hedged.  Effective for annual periods beginning on or after 1 July 2009. Earlier application permitted.

## FRS 103 (Revised) *Business Combinations* and FRS 27 (Revised) *Consolidated and Separate Financial Statements*

### Overview

The revised Standards include the following significant changes:

- a greater emphasis on the use of fair value, potentially increasing the judgement and subjectivity around business combination accounting, and requiring greater input by valuation experts;
- focusing on changes in control as a significant economic event – introducing requirements to remeasure interests to fair value at the time when control is achieved or lost, and recognising directly in equity the impact of all transactions between controlling and non-controlling shareholders not involving a loss of control; and
- focusing on what is given to the vendor as consideration, rather than what is spent to achieve the acquisition. Transaction costs, changes in the value of contingent consideration, settlement of pre-existing contracts, share-based payments and similar items will generally be accounted for separately from business combinations and will generally affect profit or loss.

The revised Standards resolve many of the more contentious aspects of business combination accounting by restricting options or allowable methods. As such, they should result in greater consistency in accounting among entities applying FRSSs.

### Summary of main changes to FRS 103

The main changes to FRS 103 are as follows:

- **Acquisition-related costs:** Acquisition-related costs e.g. finder's fees, advisory, legal, accounting, valuation and other professional or consulting fees are generally recognised as period expenses (rather than included in goodwill). Costs incurred to issue debt or equity securities will be recognised in accordance with FRS 32 and FRS 39.
- **Step acquisitions:** Changes to FRS 27 and FRS 103 work together with the effect that a business combination leading to acquisition accounting applies only at the point where control is achieved. This has a number of implications:
  - Where the acquirer has a pre-existing equity interest in the entity acquired: that equity interest may be accounted for as a financial instrument in accordance with FRS 39, as an associate or a joint venture using the equity method in accordance with FRS 28 *Investments in Associates* or FRS 31 *Interests in Joint Ventures*, or as a jointly controlled entity using the proportionate consolidation method in accordance with FRS 31. If the acquirer increases its equity interest sufficiently to achieve control (described in the revised FRS 103 as a 'business combination achieved in stages'), it must remeasure its previously-held equity interest in the acquiree at acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss.
  - Once control is achieved: all other increases and decreases in ownership interests are treated as transactions among equity holders and reported within equity (see below). Goodwill does not arise on any increase, and no gain or loss is recognised on any decrease.

- **Goodwill:** The acquirer recognises goodwill at the acquisition date, measured as the difference between:
  - the aggregate of:
    - (i) the acquisition-date fair value of the consideration transferred;
    - (ii) the amount of any non-controlling interest (“NCI”) in the entity acquired; and
    - (iii) in a business combination achieved in stages, the acquisition date fair value of the acquirer’s previously-held equity interest in the entity acquired; and
  - the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed, both measured in accordance with the revised FRS 103.
  
- **Non-controlling interests (formerly known as minority interests):** On a transaction-by-transaction basis, the acquirer has an option to measure any NCI in the entity acquired either at fair value or at the non-controlling interest’s proportionate share of the net identifiable assets of the entity acquired. The latter treatment corresponds to the measurement basis in the current version of FRS 103.

For the purpose of measuring NCI at fair value, it may be possible to determine the acquisition-date fair value on the basis of market prices for the equity shares not held by the acquirer. When a market price for the equity shares is not available because the shares are not publicly-traded, the acquirer must measure the fair value of the NCI using other valuation techniques.

Note: *Improvements to FRSs* was issued in October 2010, and it clarifies that the option to measure NCI either at fair value or at the proportionate share of the acquiree’s net identifiable assets at the acquisition date applies only to NCI that are:

- (i) present ownership interests; and
- (ii) entitle their holders to a proportionate share of the acquiree’s net assets in the event of liquidation.

All other components of NCI should be measured at their acquisition date fair value, unless another measurement basis is required by FRSs. For example, a share-based payment transaction that is classified as equity shall be measured in accordance with FRS 102 *Share-based Payment* and the equity component of a convertible instrument shall be measured in accordance with FRS 32 *Financial Instruments: Presentation*. The clarification is effective for annual periods beginning on or after 1 July 2010, with earlier application permitted.

- **Contingent consideration:** The revised FRS 103 requires the consideration for the acquisition to be measured at fair value at the acquisition date. This includes the fair value of any contingent consideration payable. FRS 103 permits very few subsequent changes to this measurement and only as a result of additional information about facts and circumstances that existed at the acquisition date. All other changes (e.g. changes resulting from events after the acquisition date such as the acquiree meeting an earnings target, reaching a specified share price, or meeting a milestone on a research and development project) are recognised in profit or loss or in accordance with other FRSs.

Note: *Improvements to FRSs* was issued in October 2010, and it clarifies that the accounting requirements for changes to contingent consideration above do not apply to contingent consideration that arose from business combinations whose acquisition dates preceded the application of the revised FRS 103. For those contingent considerations, the requirements of the previous FRS 103 continue to apply. The clarification is effective for annual periods beginning on or after 1 July 2010, with earlier application permitted.



- **Re-acquired rights:** Where the acquirer and acquiree were parties to a pre-existing relationship (e.g. the acquirer had granted the acquiree a right to use its intellectual property), there are two implications for acquisition accounting:
  - firstly, where the terms of any contract are not market terms, a gain or loss is recognised and the purchase consideration adjusted to reflect a payment or receipt for the non-market terms; and
  - secondly, an intangible asset (being the rights re-acquired) is recognised at fair value and amortised over the contract term.
- **Reassessments:** The revised FRS 103 clarifies that an entity must classify and designate all contractual arrangements at the acquisition date with two exceptions: (i) leases, and (ii) insurance contracts.

In other words, the acquirer applies its accounting policies and makes the choices available to it as if it had acquired those contractual relationships outside of the business combination. The existing treatment applied by the acquiree for classification of leases and insurance is applied by the acquirer and therefore is not reassessed. Reassessing assets and liabilities is particularly relevant when acquiring financial assets and financial liabilities in a business combination.

Consideration will be required as to how financial instruments are classified, whether embedded derivatives exist (which the acquiree may not have previously recognised) and whether hedge accounting performed by the acquiree will continue to be highly effective by the acquirer.

The revised FRS 103 shall be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. Earlier application is permitted. However, the revised FRS 103 shall be applied only at the beginning of an annual reporting period that begins on or after 30 June 2007.

### **Summary of main changes to FRS 27**

The main changes of the revised FRS 27 are as follows:

- **Acquisitions and disposals that do not result in a change of control:** Changes in a parent's ownership interest in a subsidiary that do not result in a loss of control are accounted for within shareholders' equity as transactions with owners acting in their capacity as owners. No gain or loss is recognised on such transactions and goodwill is not re-measured. Any difference between the change in the NCI and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the parent.
- **Loss of control:** A parent can lose control of a subsidiary through a sale or distribution, or through some other transaction or event in which it takes no part (e.g. expropriation or the subsidiary being placed in administration or bankruptcy).

If a parent loses control of a subsidiary, it:

- (a) derecognises the assets (including any goodwill) and liabilities of the subsidiary at their carrying amounts at the date when control is lost;
- (b) derecognises the carrying amount of any non-controlling interests in the former subsidiary at the date when control is lost (including any components of other comprehensive income attributable to them);

(c) recognises:

(i) the fair value of the consideration received, if any, from the transaction, event or circumstances that resulted in the loss of control; and

(ii) if the transaction that resulted in the loss of control involves a distribution of shares of the subsidiary to owners in their capacity as owners, that distribution;

(d) recognises any investment retained in the former subsidiary at its fair value at the date when control is lost;

(e) reclassifies to profit or loss, or transfers directly to retained earnings if required in accordance with other FRSs, the amounts recognised in other comprehensive income in relation to that subsidiary on the same basis as would be required if the parent had directly disposed of the related assets or liabilities e.g. if a subsidiary has available-for-sale financial assets and the parent loses control of the subsidiary, the parent shall reclassify to profit or loss the gain or loss previously recognised in other comprehensive income in relation to those assets; and

(f) recognises any resulting difference as a gain or loss in profit or loss attributable to the parent.

- **Attribution of profit or loss to non-controlling interests:** The revised Standard requires an entity to attribute their share of total comprehensive income to the NCI even if this results in the NCI having a deficit balance.
- **Loss of significant influence or joint control:** Amendments to FRS 28 and FRS 31 extend the treatment required for loss of control to these Standards. Thus, when an investor loses significant influence over an associate, it derecognises that associate and recognises in profit or loss the difference between the sum of the proceeds received and any retained interest, and the carrying amount of the investment in the associate at the date significant influence is lost. A similar treatment is required when an investor loses joint control over a jointly controlled entity.

The revised FRS 27 is to be applied for annual periods beginning on or after 1 July 2009. Earlier application is permitted. However, an entity shall not apply these amendments for annual periods beginning before 1 July 2009 unless it also applies the revised FRS 103. An entity shall apply the revised FRS 27 retrospectively, with the following exceptions:

- (a) the requirements for accounting for acquisitions and disposals that do not result in a change of control. Therefore, the requirements do not apply to changes that occurred before an entity applies the amendments.
- (b) the requirements for accounting for the loss of control of a subsidiary. An entity shall not restate the carrying amount of an investment in a former subsidiary if control was lost before it applies those amendments. In addition, an entity shall not recalculate any gain or loss on the loss of control of a subsidiary that occurred before the amendments are applied.
- (c) the amendment for attributing total comprehensive income to the owners of the parent and to the NCI even if this results in the NCI having a deficit balance. Therefore, an entity shall not restate any profit or loss attribution for reporting periods before the amendment is applied.

### **Consequential amendments to FRS 21 *The Effects of Changes in Foreign Exchange Rates***

As a consequence of the amendments to FRS 27, FRS 21 has also been amended to clarify the meaning of disposals as opposed to partial disposals of a foreign operations i.e. where disposals are those that result in loss of control of a subsidiary, loss of significant influence of an associate, or loss of joint control over a jointly controlled entity. On the disposal of a foreign operation, the cumulative amount of the exchange differences relating to that foreign operation, recognised in other comprehensive income and accumulated in the separate component of equity, shall be reclassified from equity to profit or loss.

Any other reduction in an entity's ownership interest in a foreign operation is considered as partial disposals. On partial disposal of a subsidiary that includes a foreign operation, the entity shall re-attribute the proportionate share of the cumulative amount of the exchange differences recognised in other comprehensive income to the non-controlling interests in that foreign operation. In any other partial disposal of a foreign operation the entity shall reclassify to profit or loss only the proportionate share of the cumulative amount of the exchange differences recognised in other comprehensive income.

Note: *Improvements to FRSs* was issued in October 2010, and it clarifies that the above amendment made to FRS 21 should be applied prospectively. The clarification is effective for annual periods beginning on or after 1 July 2010, with earlier application permitted.

## FRS 32 (Amended) *Financial Instruments: Presentation*

### - Amendments on classifications of rights Issues

Under the amendments, rights, options and warrants issued to acquire a fixed number of an entity's own non-derivative equity instruments for a fixed amount in any currency are classified as equity instruments provided that the offer is made pro-rata to all existing owners of the same class of the entity's non-derivative equity instruments.

The amendment is effective for annual periods beginning on or after 1 February 2010 with earlier application permitted

## FRS 39 (Amended) *Financial Instruments: Measurement* and INT FRS 109 (Amended) *Reassessment of Embedded Derivatives*

### - Amendments regarding the assessment of embedded derivatives on reclassification

The amendments require an assessment of embedded derivatives when there is a reclassification of a financial asset out of the 'fair value through profit or loss' ("FVTPL") category as permitted by the December 2008 amendments to FRS 39 and FRS 107 on reclassifications.

Prior to the amendments, INT FRS 109 prohibited the reassessment of the separation of an embedded derivative after an entity first became a party to the contract unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract. INT FRS 109 did not consider whether reassessment is appropriate when a financial asset is reclassified out of FVTPL because such reclassifications were prohibited at the time INT FRS 109 was issued.

The amendments added new requirements where:

- an entity should assess whether an embedded derivative is required to be separated from a host contract when the entity reclassifies a hybrid (combined) financial asset out of the FVTPL category;
- such an assessment should be made based on circumstances that existed on the later of (a) when the entity first became a party to the contract, i.e. when the financial asset was initially recognised and (b) when there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract; and
- if the fair value of an embedded derivative cannot be reliably measured on reclassification, the entire hybrid financial instrument must remain in the FVTPL category.

An entity shall apply these amendments for periods ending on or after 30 June 2009, and must be applied retrospectively.

## FRS 101 (Revised) - *First-time Adoption of Financial Reporting Standards* - Amendments to improve the structure of the Standard

The objective of the revision is to improve the structure of the Standard – no new or revised technical material has been introduced. FRS 101 had been amended a number of times, so that the text of the Standard had become increasingly complex.

The revisions are designed to make the Standard clearer and easier to follow by reorganising and moving to appendices most of the Standard's numerous exceptions and exemptions. The improved structure is also intended to better accommodate future changes to the Standard.

Material has been reorganised within appendices as follows:

- exceptions to the retrospective application of other FRSs (new Appendix B);
- exemptions for business combinations (new Appendix C); and
- exemptions from other FRSs (new Appendix D).

Interestingly, another appendix (Appendix E) was created which for the moment is unused, but which could be used for future possible short-term exemptions from FRSs on first-time adoption.

Certain out-of-date transitional provisions are also removed and some minor wording amendments made.

The revisions are effective for periods beginning on or after 1 July 2009, with earlier application permitted.

## FRS 101 (Amended) - *First-time Adoption of Financial Reporting Standards* - Additional Exemptions for First-time Adopters

The amendments relate to two new exemptions related to the accounting on first-time adoption for oil and gas assets and arrangements containing leases.

The new exemptions will be reflected in FRS 101 and will be effective for annual periods beginning on or after 1 January 2010 with earlier application permitted.

### **Exemption for oil and gas assets**

For the purposes of this exemption, the term 'oil and gas assets' is limited to those assets used in the exploration and evaluation (FRS 106) or development and production (FRS 38) of oil and gas.

Under some national GAAPs, exploration and development costs for oil and gas properties in the development or production phases are accounted for in cost centres that include all properties in a large geographical area.

FRS 101 has been amended to permit a first-time adopter that has previously used this basis of accounting to elect to measure the related oil and gas assets at the date of transition to FRSs on the following basis:

- exploration and evaluation assets at amounts determined under the entity's previous GAAP; and
- oil and gas assets in the development or production phases at the amount determined for the cost centre under the entity's previous GAAP. The entity shall allocate this amount to the cost centre's underlying assets pro rata using reserve volumes or reserve values as of that date.

Entities electing to use the exemption are required to test both exploration and evaluation assets and assets in the development and production phases for impairment at the date of transition to FRSs. The exploration and evaluation assets are tested in accordance with FRS 106 *Exploration for and Evaluation of Mineral Resources* and development and production assets are tested in accordance with FRS 36 *Impairment of Assets*.

Any identified impairment losses must be recognised at the date of transition.

Entities are required to disclose the fact that they have used the deemed cost exemption for oil and gas assets and disclose the basis on which the carrying amounts determined under previous GAAP were allocated.

**Decommissioning liabilities included in the cost of property, plant and equipment** - Decommissioning liabilities are included in the cost of property, plant and equipment. If an entity elects to use the deemed cost exemption discussed above for oil and gas assets in the development or production phases, the entity must:

- measure decommissioning, restoration and similar liabilities as at the date of transition to FRSs in accordance with FRS 37; and
- recognise directly in retained earnings any difference between that amount and the carrying amount of those liabilities at the date of transition to FRSs determined under the entity's previous GAAP.

This treatment differs from the existing exemption in FRS 101 which requires entities to measure the liability as at the date of transition to FRSs in accordance with FRS 37 and then estimate the amount that would have been included in the cost of the related asset when the liability first arose, and calculating accumulated depreciation on the amount, as of the date of transition.

#### **Exemption for leases**

Under INT FRS 104 *Determining whether an Arrangement contains a Lease*, the assessment as to whether an arrangement contains a lease is made at the inception of the arrangement. Prior to this new exemption, FRS 101 contained an exemption for all first-time adopters which allowed them to undertake that assessment for existing arrangements based on facts and circumstances at the date of transition to FRSs. Alternatively, if the exemption was not used an entity was required to refer to facts and circumstances at the inception of the arrangement.

An additional exemption has been added to provide further relief to certain first-time adopters. The new exemption applies to a first-time adopter who has made an assessment of whether an arrangement contains a lease under its previous GAAP that is consistent with INT FRS 104, but at a date other than that required under INT FRS 104. With the exemption, a first-time adopter will not be required to reassess its determination of whether an arrangement contains a lease under previous GAAP if that previous determination would have given the same outcome as that resulting from the application of FRS 17 *Leases* and INT FRS 104.

## FRS 102 (Amended) *Share-Based Payment* – Group Cash-Settled Share-Based Payment Transactions

The amendments to FRS 102 clarify the scope of FRS 102, as well as the accounting for group cash-settled share-based payment transactions in the separate (or individual) financial statements of an entity receiving the goods or services when another group entity or shareholder has the obligation to settle the award.

Guidance in these areas previously provided in INT FRS 108 *Scope of FRS 102* and INT FRS 111 *FRS 102 – Group and Treasury Share Transactions* have been incorporated into the amended FRS 102 and, as a result, these Interpretations have been withdrawn from the effective date of the amendments.

The amendments are effective for annual periods beginning on or after 1 January 2010, with earlier application permitted.

### **Key principles**

The amendments to FRS 102:

- provide additional guidance on the accounting for share-based payment transactions among group entities (incorporating guidance previously contained in INT FRS 111); and
- amend the scope of the Standard to incorporate the guidance previously provided in INT FRS 108.

### **Share-based payment transactions among group entities**

FRS 102 applies when an entity enters into a share-based payment transaction regardless of whether the transaction is to be settled by the entity itself, or by another group member on behalf of the entity.

The amendments to FRS 102 clarify the classification of share-based payment transactions for both the entity that receives the goods or services, and the entity that settles the share-based payment transaction. These amendments are summarised below.

**The entity receiving the goods or services** - will recognise the transaction as an equity-settled share-based payment transaction only if:

- the awards granted are its own equity instruments; or
- it has no obligation to settle the transaction.

In all other circumstances, the entity will measure the transaction as a cash-settled share-based payment.

Subsequent remeasurement of such equity-settled transactions will only be carried out for changes in non-market vesting conditions.

**The entity responsible for settling the transaction** - will recognise it as an equity-settled share-based payment only if the transaction is settled in its own equity instruments. In all other circumstances, the transaction will be recognised by the entity that settles the award as a cash-settled share-based payment.

The guidance incorporated into FRS 102 can be illustrated for the most commonly occurring scenarios as follows:

Entity receiving goods and services	Obligation to settle share-based payment transaction	How is it settled?	Classification: Subsidiary's individual financial statements	Classification: Consolidated financial statements
Subsidiary	Subsidiary	Equity of the subsidiary	Equity	Equity
Subsidiary	Subsidiary	Cash	Cash	Cash
Subsidiary	Subsidiary	Equity of the parent	Cash	Equity
Subsidiary	Parent*	Equity of the parent	Equity	Equity
Subsidiary	Parent*	Cash	Equity	Cash

\* The same classification will result if the settlement obligation lies with the shareholders or another group entity (e.g. a fellow subsidiary).

#### **Amendment of the scope of FRS 102**

The scope of FRS 102 has been amended to clarify that it applies to all share-based payment transactions, whether or not the goods or services received under the share-based payment transaction can be individually identified.

Any unidentifiable goods and services are measured on the grant date as the difference between the fair values of the share-based payment and the identifiable goods and services. This guidance was previously set out in INT FRS 108.

The amendments to FRS 102 arising from the incorporation of the requirements of INT FRS 108 and INT FRS 111 are subject to the effective date and transitional provisions of the original Interpretations (now withdrawn). The other amendments to FRS 102 are to be applied retrospectively for annual periods beginning on or after 1 January 2010 (subject to the transitional provisions in FRS 102), with earlier application permitted. If sufficient information for retrospective application is not available, the entity will reflect in its separate or individual financial statements the amounts previously recognised in the group's consolidated financial statements.



## INT FRS 117 *Distributions of Non-cash Assets to Owners*

The Interpretation provides guidance on the appropriate accounting treatment when an entity distributes assets other than cash as dividends to its shareholders.

### Scope

The interpretation applies to non-reciprocal distributions of non-cash assets made by an entity to its shareholders acting in their capacity as owners, covering:

- distributions of non-cash assets (e.g. items of property, plant and equipment, businesses as defined in FRS 103 *Business Combinations*, ownership interests in another entity and disposal groups as defined in FRS 105); and
- distributions that give owners a choice of receiving either non-cash assets or a cash alternative.

Specifically excluded from the scope of the Interpretation are:

- distributions in which all owners of the same class of equity instruments are not treated equally. For example, the Interpretation will not apply if the distribution is made to a specific shareholder and is not offered to other shareholders of the same class of shares;
- distributions of non-cash assets that are ultimately controlled by the same party or parties before and after the distribution; and
- distributions by an entity of some of its ownership interest in a subsidiary where the entity retains control of that subsidiary. In such circumstances, FRS 27 sets out the appropriate accounting treatment.

### Issues and Consensus

The specific questions addressed in the Interpretation are:

#### **1) When should the entity recognise the dividend payable?**

It was concluded that an entity should recognise a liability when it has incurred an obligation to pay that liability. In the context of non-cash distributions, the point at which an obligation arises is the point at which the dividend is appropriately authorised (and is no longer at the discretion of the entity), which will vary according to the legal requirements in particular jurisdictions.

INT FRS 117 concludes that the entity should recognise a liability for a non-cash distribution:

- in jurisdictions where the approval of shareholders (or an equivalent authority) is required, when that approval is obtained; and
- in jurisdictions where further approval of dividends is not required, when the dividend is declared (e.g. by management or the board of directors).

## **2) How should the entity measure the dividend payable?**

It was concluded that the liability should be measured at the fair value of the non-cash assets to be distributed. If shareholders have a choice of receiving either a non-cash asset or a cash alternative, the liability should be measured considering both the fair value of each alternative and management's assessment of the probabilities for each outcome.

## **3) When the entity settles the dividend payable, how should it account for any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable?**

When an entity settles the dividend payable, the interpretation requires that it should recognise the difference, if any, between the carrying amounts of the assets distributed and the carrying amount of the dividend payable in profit or loss.

### **Consequential amendment to FRS 105 *Non-current Assets Held for Sale and Discontinued Operations***

The Interpretation has resulted in consequential amendments to FRS 105 regarding the appropriate treatment of the non-cash assets held for distribution. Whether or not a non-cash asset is classified as 'held for distribution to owners' is determined using FRS 105's general principles regarding whether the transaction is highly probable. Reclassification under FRS 105 can be triggered in advance of approval by shareholders, but it will be necessary to consider the probability of that approval being obtained (if required in the jurisdiction) as part of the assessment as to whether the transaction is highly probable.

When the non-cash asset is classified as held for distribution to owners, it is remeasured at the lower of its carrying amount and fair value less costs to distribute, with any adjustment to carrying amount recognised in accordance with the general principles of FRS 105. Therefore, where the fair value less costs to distribute of an asset accounted for using the cost model is less than its carrying amount, an impairment loss should be recognised in profit or loss. Where the fair value less costs to distribute is higher than the carrying amount, no adjustment is made until the distribution is made.

This interpretation is to be applied prospectively. Retrospective application is not permitted.

## INT FRS 118 *Transfers of Assets from Customers*

The Interpretation provides guidance by recipients for transfers of property, plant and equipment from customers.

### **Scope**

The Interpretation applies to all agreements in which an entity receives from a customer an item of property, plant and equipment (or cash to construct or acquire an item of property, plant and equipment) that the entity must then use either to:

- connect the customer to a network; or
- to provide the customer with ongoing access to a supply of goods or services; or
- to do both.

In some cases, the transferor of the asset may not be the entity that will be the recipient of the ongoing supply of goods and/or services. However, for convenience, the Interpretation refers to the entity transferring the asset as the 'customer'.

Specifically excluded from the scope of the Interpretation are:

- transfers of assets that are government grants as defined in *FRS 20 Accounting for Government Grants and Disclosure of Government Assistance*;
- transfers of assets that are infrastructure used in service concession arrangements within the scope of INT FRS 112 *Service Concession Arrangements*; and
- accounting for the transfer by the customer.

### **Issues and consensus**

The basic principle of INT FRS 118 is that when the item of property, plant and equipment transferred from a customer meets the definition of an asset under the FRS Framework from the perspective of the recipient, the recipient must recognise the asset in its financial statements. If the customer continues to control the transferred item, the asset definition would not be met even if ownership of the asset is transferred to the recipient entity.

The deemed cost of that asset is its fair value on the date of the transfer.

INT FRS 118 provides guidance on how to identify the entity's obligation to provide one or more separately identifiable services in exchange for the transferred asset – and, therefore, how to recognise revenue. The following lists out revenue recognition for the various forms of service obligations:

- If the entity has only one service obligation, it would recognise revenue when the service is performed in accordance with FRS 18;
- If the entity has more than one separately identifiable service obligation, it should allocate the fair value of the total consideration received to each service and recognise revenue from each service separately in accordance with FRS 18; and
- If the entity has an obligation to provide ongoing services, the period over which revenue is recognised is generally determined by the terms of the agreement with the customer. If the agreement does not specify a period, the revenue shall be recognised over a period no longer than the useful life of the transferred asset used to provide the ongoing service.

In addition to the above, the Interpretation suggests that when a connection to a network is delivered to the customer and represents stand-alone value for that customer, and the fair value of the connection to that network can be measured reliably, the entity would conclude that connecting the customer to a network is a separately identifiable service, and is thus an event for which revenue should be recognised.

The Interpretation also addresses agreements where an entity receives cash instead items of property, plant and equipment from customers, and such agreements are in scope of INT FRS 118. The accounting for the credit side of such transactions is outlined above.

The Interpretation must be applied prospectively to transfers of assets from customers received on or after 1 July 2009. Earlier application is permitted provided the valuations and other information needed to apply to the Interpretation to past transfers were obtained at the time those transfers were made.

# Revised/amended FRSs and INT FRSs issued in 2010

New/revised/amended FRSs/INT FRSs	
General amendments	<i>Improvements to FRSs (October 2010)</i> (refer to document for effective dates)
FRS 24 (Revised)	<i>Related Party Disclosures</i> (effective for annual periods beginning on or after 1 January 2011)
FRS 101 (Amended)	<i>Limited Exemption from Comparative FRS 107 Disclosures for First-time Adopters</i> (effective for annual periods beginning on or after 1 July 2010)
INT FRS 114 (Amended)	<i>Prepayments of a Minimum Funding Requirement</i> (effective for annual periods beginning on or after 1 January 2011)
INT FRS 115	<i>Agreements for the Construction of Real Estate, with an Accompanying Note</i> (effective for annual periods beginning on or after 1 January 2011)
INT FRS 119	<i>Extinguishing Financial Liabilities with Equity Instruments</i> (effective for annual periods beginning on or after 1 July 2010)

## *Improvements to FRSs (October 2010)*

This is the third set of Improvements to FRSs that is intended to deal with non-urgent, minor amendments to FRSs. These amendments focus on areas of inconsistency in FRSs or where clarification of wording is required. The improvements are effective from 1 January 2011 except if otherwise specified.

### Detail of amendments

The following table provides a summary of each of the amendments.

Standard	Subject of amendment	New requirements
FRS 103 (2009) <i>Business Combinations</i>	Measurement of non-controlling interests	<p>Specifies that the option to measure non-controlling interests either at fair value or at the proportionate share of the acquiree's net identifiable assets at the acquisition date under FRS 103 (2009) <i>Business Combinations</i> applies only to non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the acquiree's net assets in the event of liquidation</p> <p>All other components of non-controlling interests (e.g. equity component of convertible preference shares), should be measured at their acquisition date fair value, unless another measurement basis is required by FRSs.</p> <p>Effective for annual periods beginning on or after 1 July 2010. To be applied prospectively from the date the entity first applied FRS 103 (2009). Earlier application permitted.</p>

Standard	Subject of amendment	New requirements
	Un-replaced and voluntary replaced share based payment awards	<p>Specifies that the current requirement to measure awards of the acquirer that replace acquiree's share-based payment transactions in accordance with FRS 102 at the acquisition date ('market-based measure') applies also to share-based payment transactions of the acquiree that are not replaced.</p> <p>Specifies that the current requirement to allocate the market-based measure of replacement awards between the consideration transferred for the business combination and post-combination remuneration applies to all replacement awards regardless of whether the acquirer is obliged to replace the awards or does so voluntarily.</p> <p>Effective for annual periods beginning on or after 1 July 2010. To be applied prospectively from the date the entity first applied FRS 103 (2009). Earlier application permitted</p>
	Transitional requirements for contingent consideration from a business combination that occurred before the effective date of FRS 103 (2009)	<p>Clarifies that FRS 32 <i>Financial Instruments: Presentation</i>, FRS 39 <i>Financial Instruments: Recognition and Measurement</i> and FRS 107 <i>Financial Instruments: Disclosures</i> do not apply to contingent consideration that arose from business combinations whose acquisition dates preceded the application of FRS 103 (2009).</p> <p>For such contingent considerations, the requirements of FRS 103 (2004) continue to apply.</p> <p>Effective for annual periods beginning on or after 1 July 2010. Earlier application permitted.</p>
FRS 1 <i>Presentation of Financial Statements</i>	Clarification of statement of changes in equity	<p>Clarifies that an entity may present the analysis of other comprehensive income by item either in the statement of changes in equity or in the notes to the financial statements.</p> <p>Earlier application permitted.</p>

Standard	Subject of amendment	New requirements
FRS 27 <i>Consolidated and Separate Financial Statements</i>	Transitional requirements for consequential amendments as a result FRS 27 (2009)	<p>Clarifies that the amendments made to FRS 21 <i>The Effects of Changes in Foreign Rates</i>, FRS 28 <i>Investments in Associates</i> and FRS 31 <i>Interests in Joint Ventures</i> as a result of FRS 27 (2009) should be applied <u>prospectively</u> with an exception for new disclosure requirements for associates and joint ventures e.g. when there are changes in ownership interests in those investments. Such disclosure requirements apply retrospectively.</p> <p>Effective for annual periods beginning on or after 1 July 2010. Earlier application permitted.</p>
FRS 107 <i>Financial Instruments: Disclosures</i>	Clarifications of disclosures	<p>Encourages qualitative disclosures in the context of the quantitative disclosure required to help users to form an overall picture of the nature and extent of risks arising from financial instruments.</p> <p>Clarifies the required level of disclosure around credit risk and collateral held and provides relief from disclosure of renegotiated loans.</p> <p>Earlier application permitted.</p>
FRS 34 <i>Interim Financial Statements</i>	Significant events and transactions	<p>Emphasises the principle in FRS 34 that the disclosure about significant events and transactions in interim periods should update the relevant information presented in the most recent annual financial report.</p> <p>Clarifies how to apply this principle in respect of financial instruments and their fair values.</p> <p>Earlier application permitted.</p>
INT FRS 113 <i>Customer Loyalty Programmes</i>	Fair value of credit awards	<p>Clarifies that the 'fair value' of award credits should take into account:</p> <ul style="list-style-type: none"> <li>• the amount of discounts or incentives that would otherwise be offered to customers who have not earned award credits from an initial sale; and</li> <li>• any expected forfeitures.</li> </ul> <p>Earlier application permitted.</p>

## FRS 24 (Revised) *Related Party Disclosures*

The revised FRS 24 has the two main areas of change as follows:

- (a) providing a partial exemption from the disclosure requirements for government-related entities; and
- (b) simplifying the definition of a related party, clarifying its intended meaning and eliminating inconsistencies from the definition.

### **Partial exemption for government-related entities**

The previous version of FRS 24 contained no specific exemption for government-related entities. Many entities, particularly in an environment where government control is pervasive, found it problematic in practice to identify all government-related entities, and to quantify all related party transactions and balances with those entities.

As a result, the revised Standard provides a partial exemption from the disclosure requirements of FRS 24 for government-related entities. Specifically, a reporting entity is exempt from the general disclosure requirements set out in FRS 24 in relation to related party transactions and outstanding balances (including commitments) with:

- a government that has control, joint control or significant influence over the reporting entity; and
- another entity that is a related party because the same government has control, joint control or significant influence over both the reporting entity and the other entity.

In this context, government refers to government, government agencies and similar bodies whether local, national or international.

However, where a reporting entity is exempt from the general disclosure requirements in accordance outlined above, the revised Standard requires the reporting entity to disclose the following information about the transactions and related outstanding balances:

- the name of the government and the nature of its relationship with the reporting entity (i.e. control, joint control or significant influence);
- The following information in sufficient detail about:
  - the nature and amount of each individually significant transaction; and
  - for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent.

Regarding the level of detail to be disclosed in relation to transactions that are collectively (but not individually) significant, the revised FRS 24 states that the closeness of the related party relationship and other factors relevant in establishing the level of significance of the transaction should be considered. Examples of factors to be considered are whether the transaction:

- is significant in terms of size;
- is carried out on non-market terms;
- is beyond normal day-to-day business operations (e.g. purchases and sales of businesses);
- has been disclosed to regulatory or supervisory authorities;
- has been reported to the senior management; and
- requires shareholders' approval.

The revised FRS 24 contains some illustrative examples in relation to the application of the revised requirements for government related entities.



### Revised definition of a related party

The revised definition of a related party is as follows:

*A related party is a person or entity that is related to the entity that is preparing its financial statements (i.e. 'reporting entity').*

*(a) A person or a close member of that person's family is related to a reporting entity if that person:*

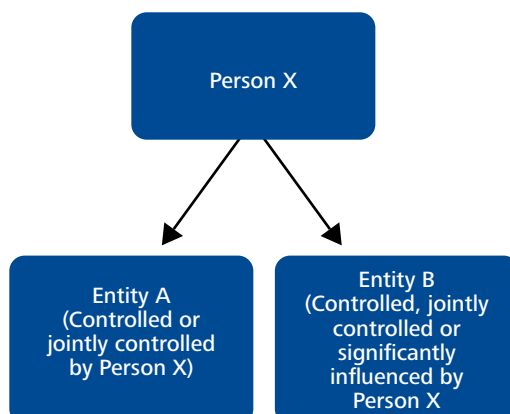
- (i) has control or joint control over the reporting entity;*
- (ii) has significant influence over the reporting entity; or*
- (iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.*

*(b) An entity is related to a reporting entity if any of the following conditions applies:*

- (i) The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).*
- (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).*
- (iii) Both entities are joint ventures of the same third party.*
- (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.*
- (v) The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.*
- (vi) The entity is controlled or jointly controlled by a person identified in (a).*
- (vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).*

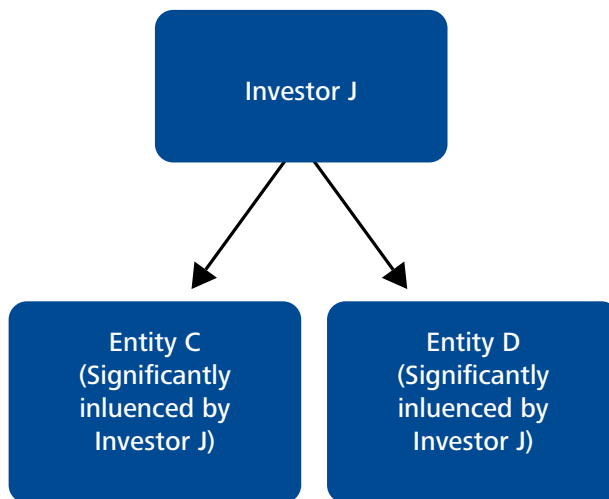
The following are some examples of related parties under the revised FRS 24.

#### **Situation 1 – Person as an investor**



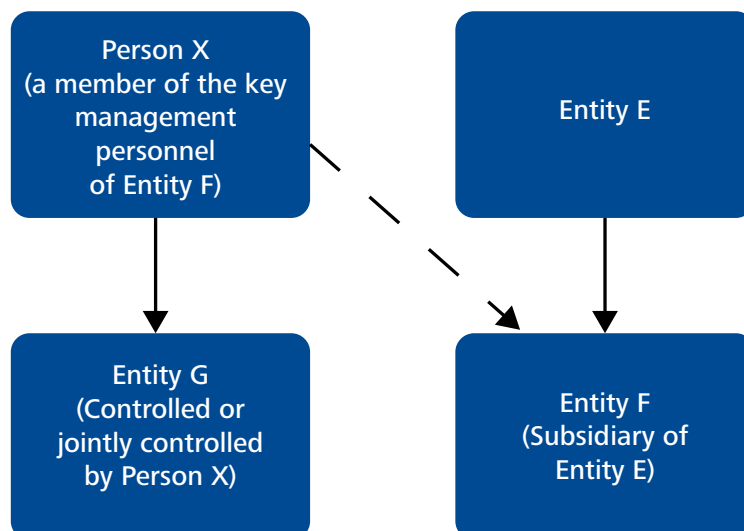
Person X has control or joint control over Entity A. Person X has control, joint control or significant influence over Entity B. The revised FRS 24 states that Entity A and Entity B are related parties for the purposes of the financial statements of both entities.

**Situation 2 – Two associates of an investor**



Entity C and Entity D are associates of Investor J. The revised FRS 24 makes it clear that Entity C and Entity D are not related parties of each other. The rationale as expressed by the IASB in the Basis for Conclusions to IAS 24 (Revised) is that common investment in two associates is not sufficient to conclude that the two associates are related parties.

**Situation 3 – Investments of members of key management personnel**



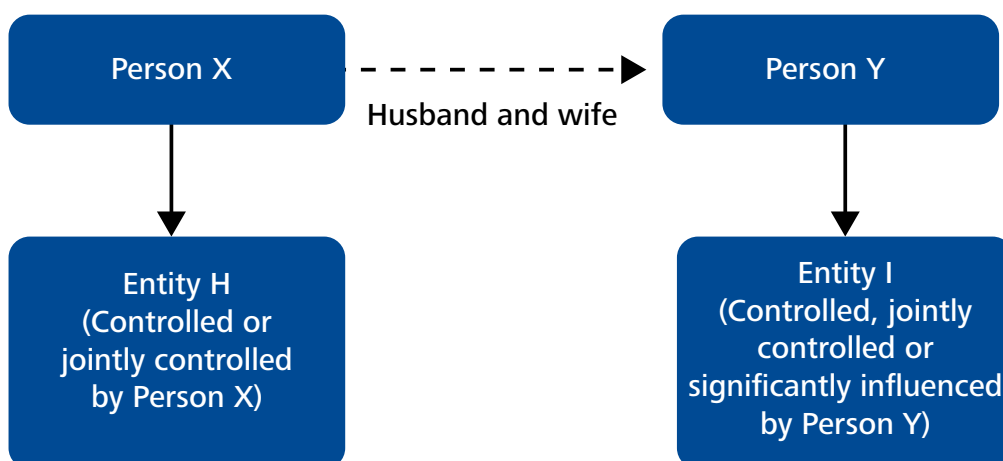
Entity G is controlled or jointly controlled by Person X. Person X is a member of the key management personnel of Entity F.

Under the revised FRS 24, Entity F (i.e. the entity managed by Person X) is a related party of Entity G for the purposes of the financial statements of Entity G.

The previous version of FRS 24 treated some investees of the key management personnel of a reporting entity as related parties to the reporting entity. However, the previous version of the FRS 24 did not include the reciprocal of such a situation. Therefore, to remove the inconsistency, the definition of a related party has been revised to ensure that Entity F and Entity G are treated as related parties in the financial statements of Entity F and Entity G.

Note: The outcome will be the same if Person X is a member of key management personnel of Entity E and not Entity F.

#### **Situation 4 – Close members of the family holding investments**



Person X and Person Y are husband and wife. Person X has control or joint control over Entity H while Person Y has control, joint control or significant influence over Entity I. The revised FRS 24 states that Entity H and Entity I are related parties for the purposes of the financial statements of both entities.

In addition, the revised Standard states that, in relation to the definition of a related party, references to “an associate” and “a joint venture” include subsidiaries of the associate and subsidiaries of the joint venture. Therefore, an associate’s subsidiary and the investor that has significant influence over the associate are related to each other.

The revised Standard is effective for annual periods beginning on or after 1 January 2011 and requires retrospective application. Therefore, in the year of initial application, disclosures for the comparative period will need to be restated.

Earlier application is permitted, either of the whole revised Standard or of the partial exemption for government-related entities. If an entity applies either the whole Standard or the partial exemption for a period beginning before 1 January 2011, it is required to disclose that fact.

## FRS 101 (Amended) *First-time Adoption of Financial Reporting Standards* - Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters

In 2009, an amendment to FRS 107 *Financial Instruments: Disclosures* was issued entitled Improving Disclosures about Financial Instruments ('the FRS 107 Amendments'). These amendments expanded the disclosures required, for each class of financial instruments, in respect of fair value measurements recognised in the statement of financial position, introduced a three-level fair value hierarchy and clarified the scope of items to be included in the maturity analyses required under FRS 107.

The transitional provisions within the FRS 107 Amendments provide relief in the first year of application from providing comparative information for the disclosures required by the FRS 107 Amendments for current FRS preparers. However, FRS 101 was not amended to accommodate the relief at that time.

Consequently, FRS 101 was amended in 2010 to clarify that first-time adopters will receive the same relief from providing comparative period disclosures required by the FRS 107 Amendments as the current FRS preparers.

In addition, it was further clarified that, for both existing FRS preparers and first-time adopters, an entity need not provide comparative information for the disclosures required by the FRS 107 amendments for any annual comparative periods ending before 31 December 2009, any interim periods within an annual comparative period ending before 31 December 2009, and any statement of financial position presented within these periods including any statement of financial position as at the beginning of the earliest comparative period, if the statement of financial position is as at a date before 31 December 2009. This clarification provides relief to reporting entities presenting more than one period of comparative information and opening statements of financial position in those cases when an entity is required to present three statements of financial position in accordance with FRS 1 or FRS 101.

The amendment to FRS 101 is effective for annual periods beginning on or after 1 July 2010 with earlier application permitted.

## INT FRS 114 (Amended) *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* – Prepayments of a Minimum Funding Requirement

The amendments have been made to remedy an unintended consequence of INT FRS 114 where entities are in some circumstances not permitted to recognise prepayments of minimum funding contributions as an asset.

### **Background**

INT FRS 114 was issued in 2008 to address three issues:

- when refunds or reductions in future contributions should be regarded as 'available' in accordance with FRS 19 *Employee Benefits*;
- how minimum funding requirements might affect the availability of reductions in future contributions; and
- when minimum funding requirements might give rise to a liability.

### **Issue**

INT FRS 114 (as originally issued) unintentionally reduced the economic benefits available in accordance with FRS 19 arising from voluntary prepayments of minimum funding contributions.

If an entity is subject to minimum funding requirements for contributions relating to future benefits, INT FRS 114.20 (as originally issued) limited the economic benefit available in the form of reductions in future contributions to the present value of:

- (a) the estimated future service cost in each year; less
- (b) the estimated minimum funding contributions required in respect of the future accrual of benefits in that year.

INT FRS 114 (as originally issued) did not consider that a plan surplus may result from a prepayment of future minimum funding contributions and, in some situations, entities may have been prevented from recognising as an asset the economic benefit arising from the prepayment. This is because, to the extent that minimum funding contributions required in respect of the future accrual of benefits exceed service costs calculated under FRS 19 in any given year, INT FRS 114 specifies that the present value of that excess reduces the amount of the asset available as a reduction in future contributions.

### **Consensus**

Under the amended INT FRS 114.20, if there is a minimum funding requirement for contributions relating to future service, the economic benefit available as a reduction in future contributions (and, therefore, the surplus that should be recognised as an asset) comprises of:

- (a) any amount that reduces future minimum funding requirement contributions for future services because the entity made a prepayment (i.e. any amount that the entity has paid before being required to do so); and
- (b) the estimated future service cost in each period less the estimated minimum funding requirement contributions that would be required for future service in that period if there were no prepayment of those contributions as described in (a).

Further, INT FRS 114 clarifies that while the amount calculated under (b) may be negative for a given period (i.e. the estimated minimum funding requirement contribution for that period exceeds the estimated future service cost for that same period), the total amount calculated under INT FRS 114.20 (b) can never be less than zero. Accordingly, the economic benefit available as a reduction in future contributions will correspond, as a minimum, to the amount of the prepayment, if any.

### **Effective date and transition**

The amendments are effective for annual periods beginning on or after 1 January 2011. Earlier application is permitted. If an entity applies the amendments for an earlier period, it should disclose that fact.

The amendments must be applied from the beginning of the earliest comparative period presented in the first annual financial statements in which the entity applied INT FRS 114 (mandatory for annual periods beginning on or after 1 January 2008, but may have been adopted for an earlier accounting period). Any initial adjustment arising from the application of the amendments by an entity that had previously applied INT FRS 114 shall be recognised as an adjustment to retained earnings at the beginning of the earliest comparative period presented.

## INT FRS 115 *Agreements for Construction of Real Estate* – with an Accompanying Note

INT FRS 115 is based on its international equivalent IFRIC 15, which standardises accounting practice across jurisdictions for the recognition of revenue among real estate developers for sales of units, such as apartments or houses, 'off plan', i.e. before construction is complete.

### **Background**

The Interpretation provides guidance on how to determine whether an agreement for the construction of real estate is within the scope of FRS 11 *Construction Contracts* or FRS 18 *Revenue* and when revenue from the construction should be recognised.

### **Issue and consensus**

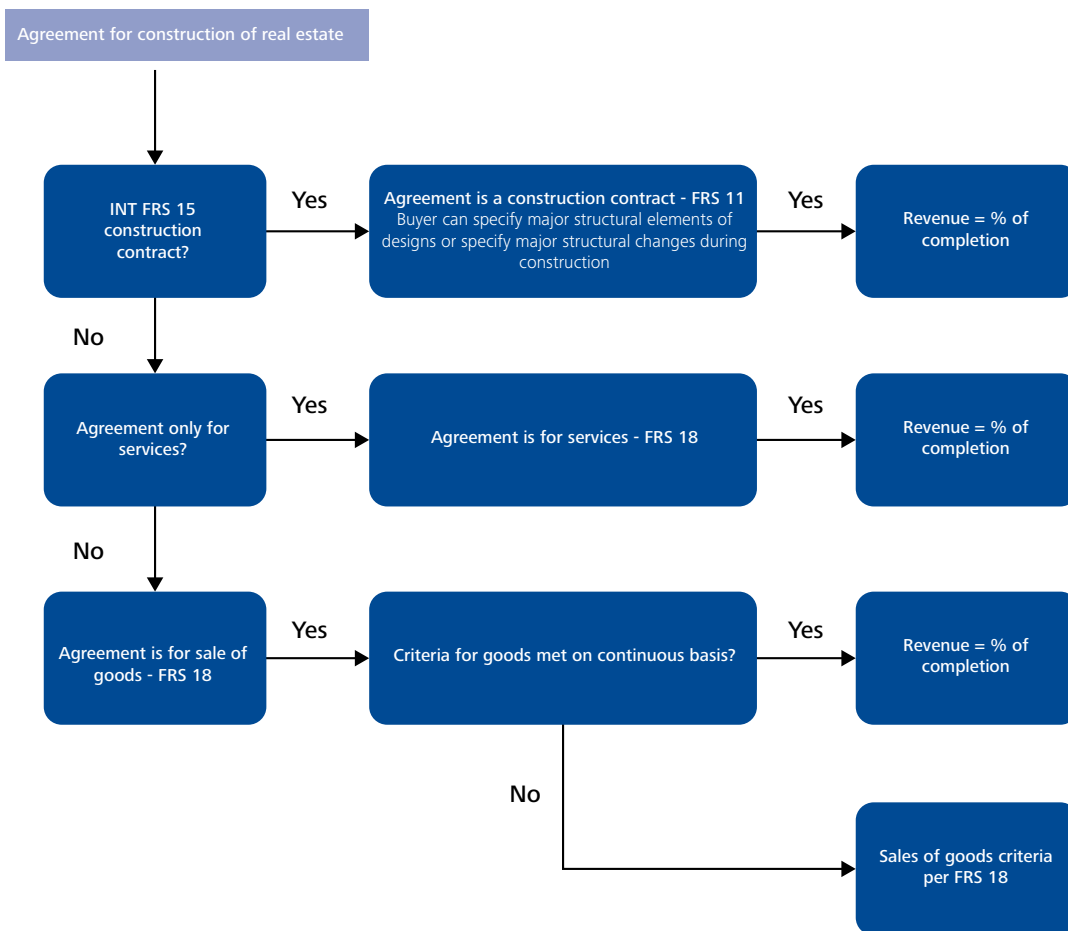
An agreement for the construction of real estate is a construction contract within the scope of FRS 11 only when the buyer is able to specify the major structural elements of the design of the real estate before the construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not). If the buyer has that ability, FRS 11 applies. If the buyer does not have that ability, FRS 18 applies.

Under FRS 18:

- an agreement can be considered as "rendering of services" if the entity is not required to acquire and supply construction materials, and revenue is recognised by reference to the stage of completion; and
- an agreement will be considered as "sale of goods" if it involves the provision of services together with construction materials in order to perform its contractual obligations to deliver real estate to the buyer, and revenue can only be recognised when the entity has met all the criteria in FRS 18.14 i.e., transfer to the buyer control and the significant risks and rewards of ownership of the goods.

The interpretation introduces a new concept that the transfer of control and significant risks and rewards in a sale of goods under FRS 18 could occur continuously as construction progresses, and revenue can be recognised using percentage completion method. When an entity adopts such accounting, specific disclosures are required, including how it determines which agreements meet all the criteria in FRS 18.14 continuously as construction progresses. One of the important indicators of "continuous transfer" appears to be that, if the agreement is terminated before the construction is complete, the buyer retains the work in progress and the entity has the right to be paid for the work performed to date.

The following diagram summarises the above concepts:



The main expected change in practice is a shift for some entities from recognising revenue using the percentage of completion method (i.e. as construction progresses, by reference to the stage of completion of the development) to recognising revenue at a single time (i.e. at completion upon or after delivery).

The main differences between INT FRS 115 and IFRIC 15 are in the effective dates, and that INT FRS 115 was issued with an Accompanying Note.

**Effective date**

INT FRS 115 is effective for annual periods beginning on or after 1 January 2011. IFRIC 15 however, was effective for annual periods beginning on or after 1 January 2009. Both require retrospective application. RAP 11 *Pre-Completion Contracts for the Sale of Development Property* will cease to have effect after INT FRS 115 becomes effective.

### **Accompanying Note**

The Accompanying Note explains the application of the Interpretation to property development sales in Singapore by considering the Singapore legal framework. The Accompanying Note concluded that sales of uncompleted residential property in Singapore that are regulated under the Singapore Housing Developers (Control and Licensing) Act (Chapter 130) and use the standard forms of the sale and purchase agreements prescribed in the schedule to the Housing Developers Rules, generally meet the criteria set out in the Interpretation on continuous transfer of control and the significant risks and rewards of ownership of the uncompleted property units. Consequently, such sales should be accounted for on a percentage of completion method.

### ***INT FRS 119 Extinguishing Financial Liabilities with Equity Instruments***

INT FRS 119 addresses divergent accounting by entities issuing equity instruments in order to extinguish all or part of a financial liability (often referred to as “debt for equity swaps”).

### **Background and scope**

A borrower may enter into an agreement with a lender to issue equity instruments to the lender in order to extinguish a financial liability owed to the lender. This is particularly common when the borrower is in financial difficulty.

Prior to issuance of INT FRS 119, it was noted that there was diversity in practice in accounting for these transactions. Some measure the equity instruments issued at the carrying amount of the financial liability derecognised and do not recognise any gain or loss on extinguishment of the liability in profit or loss. Others recognise the equity instruments at the fair value of either the liability extinguished or of the equity instruments issued, and recognise any difference between this amount and the carrying amount of the liability in profit or loss. INT FRS 119 eliminates this diversity.

INT FRS 119 addresses only the accounting by the entity which issues equity instruments in order to extinguish, in full or in part, a financial liability. It does not address the accounting by the lender. In addition, it is not to be applied in situations where:

- the lender is also a direct or indirect shareholder and is acting in its capacity as direct or indirect shareholder;
- the lender and the entity are controlled by the same party or parties before and after the transaction and the substance of the transaction includes an equity distribution from, or contribution to, the entity; or
- extinguishing the financial liability by issuing equity shares is in accordance with the original terms of the financial liability.



### Issues

FRS 39.41 states that the difference between the carrying amount of a financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, should be recognised in profit or loss. INT FRS 119 addresses the following issues:

- whether the issue of equity instruments meets the definition of 'consideration paid' in accordance with FRS 39.41;
- how an entity should initially measure the equity instruments issued to extinguish such a financial liability; and
- how an entity should account for any difference between the carrying amount of a financial liability extinguished and the initial measurement of equity instruments issued.

### Consensus

It was concluded that the issue of equity instruments to extinguish all or part of a financial liability constitutes consideration paid in accordance with FRS 39.41. The issue of equity instruments to extinguish financial liabilities can be seen as consisting of two transactions: first, the issue of equity instruments for cash and second, acceptance by the creditor of that amount of cash to extinguish the financial liability.

An entity should measure the equity instruments issued as extinguishment of the financial liability at their fair value on the date of extinguishment of the liability, unless that fair value is not reliably measurable. In this case the equity instruments should be measured to reflect the fair value of the liability extinguished.

If only part of a financial liability is extinguished through the issue of equity instruments, the entity should assess whether some of the consideration paid represents a modification of the portion of the liability which remains outstanding. If it is determined that part of the consideration paid relates to a modification of the outstanding liability, the entity should apportion the consideration between that portion which has been extinguished and that which remains outstanding.

Any difference between the carrying amount of the liability (or the part of the liability) extinguished and the fair value of equity instruments issued is recognised in profit or loss. When consideration is partly allocated to the portion of a liability which remains outstanding, the part allocated to this portion forms part of the assessment as to whether there has been an extinguishment or a modification of that portion of the liability. If the remaining liability has been substantially modified, the entity should account for the modification as the extinguishment of the original liability and the recognition of a new liability as required by FRS 39.40.

The Interpretation is effective for annual periods beginning on or after 1 July 2010, with earlier application permitted. Where adoption of the Interpretation results in a change in accounting policy, that change should be applied from the beginning of the earliest comparative period presented in the year of adoption, in accordance with FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. An entity is not required to restate the accounting for debt for equity swaps which occurred before the beginning of the earliest comparative period.

## First phase of joint project on *Conceptual Framework for Financial Reporting* – Completed

The IASB and the FASB has completed the first phase of their joint project to develop an improved and converged conceptual framework for IFRS and US GAAP with their issue of Chapter 1: *The objective of general purpose financial reporting* and Chapter 3: *Qualitative characteristics of useful financial information*.

### **The objective of general purpose financial reporting**

Chapter 1 states that the objective of financial reporting is “to provide financial information about the reporting entity that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the entity”.

### **Qualitative characteristics of useful financial information**

Chapter 3 states that the fundamental qualitative characteristics of useful financial information are “relevance” and “faithful representation”. These fundamental characteristics are further enhanced if information is “comparable, verifiable, timely, and understandable”.

In addition, the chapter states that the decision about whether to include information in financial reports should take into account materiality and cost-benefit constraints. The cost to report certain financial information should be justified by the benefits of providing that information.

# Section 2: Exposure draft issued in 2010

#### Exposure Drafts issued in 2010

- ED *SFRS for Small Entities*
  - including a summary of IFRS for *Small and Medium-sized Entities*
- ED Measurement of Liabilities in FRS 37 (Limited re-exposure of proposed amendment to FRS 37 issued in 2005)
- ED *Revenue from Contracts with Customers*
- ED Proposed amendments to FRS 1 *Presentation of Financial Statements*
  - Presentation of Items of Other Comprehensive Income
- ED Proposed amendments to FRS 19 *Employee Benefits*
  - Defined benefit plans
- ED *Leases*
- ED Proposed amendments to FRS 12 *Income Tax*
  - Deferred Tax: Recovery of Underlying Assets
- ED Proposed amendment to FRS 101 *First-time Adoption of Financial Reporting Standards - Severe Hyperinflation*
- ED Proposed amendments to FRS 101 *First-time Adoption of Financial Reporting Standards*
  - Removal of Fixed Dates for First-time Adopters
- ED *Insurance Contracts*
- Draft Interpretation *Stripping Costs in the Production Phase of a Surface Mine*
- ED on *Conceptual Framework - Description of the Reporting Entity*
- ED *Fair Value Option for Financial Liabilities*
  - (Accompanied by a summary of ED *Financial Instruments: Classification and Measurement* issued in 2009)
- ED *Financial Instruments: Amortised Cost and Impairment*
- ED *Measurement Uncertainty Analysis Disclosure for Fair Value Measurements*

## Adoption of *SFRS for Small Entities*

The ASC has issued a statement of intent that sets out the reasons on its intention to adopt IFRS for *Small and Medium-sized Entities* issued by the IASB, without modification. The Singapore equivalent will be called *SFRS for Small Entities*. The ASC proposes to allow small entities with no public accountability and meeting certain criteria the option to use a simplified set of accounting principles.

The ASC proposes that an entity is eligible to use the *SFRS for Small Entities* if:

- (I) it is not publicly accountable; and
- (II) it qualifies as a small entity by virtue of it satisfying two out of the three threshold criteria as prescribed by the ASC.

### **(I) An entity is deemed to be publicly accountable if:**

- (a) Its debt or equity instruments are traded in a public market or it is 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), or
- (b) It is a deposit-taking entity and/or holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, insurance companies, securities brokers/dealers, mutual funds and investment banks, or

*(The ASC has clarified that all regulated or exempt financial institutions are not permitted to use the SFRS for Small Entities, except for money changers, financial advisers, insurance brokers, captive insurers and Lloyds Asia Scheme service companies. These entities may elect to use the SFRS for Small Entities only if they meet the qualifying criteria as prescribed by the ASC.)*

- (c) It is a public company defined under the Singapore Companies Act, or
- (d) It is a charity defined under the Charities Act, or
- (e) It is a credit society defined under the Co-operative Societies Act or a society deemed to be a credit society under the Co-operative Societies (Amendment) Act 2008.

### **(II) An entity qualifies as a small entity if it satisfies two of the following three criteria (determined on a consolidated basis):**

- (a) Total annual revenue of not more than S\$10 million;
- (b) Total gross assets of not more than S\$10 million; and
- (c) Number of employees not more than 50.

The ASC intends to provide transitional relief for entities that fall in and out of the eligibility threshold criteria due to year-on-year fluctuation in financial / operational results, by requiring the preparation of financial statements under the full FRS only if the entity fails to satisfy the prescribed threshold criteria for two consecutive years. Likewise, an entity that prepares financial statements based on the full FRS is eligible to apply the *SFRS for Small Entities* only if it has satisfied the prescribed threshold criteria for two consecutive years.

The *SFRS for Small Entities* would be available for eligible entities to apply for financial periods beginning on or after 1 January 2011.

The following summary is based on the Standard issued by the IASB.

### **IFRS for SMEs**

The *IFRS for SMEs* is a self-contained Standard, incorporating accounting principles that are based on full IFRSs but that have been simplified to suit the entities within its scope (known as SMEs). By removing some accounting treatments permitted under full IFRSs, eliminating topics and disclosure requirements that are not generally relevant to SMEs, and simplifying requirements for recognition and measurement, the *IFRS for SMEs* reduces the volume of accounting requirements applicable to SMEs by more than 90 per cent when compared with the full set of IFRSs.

Where financial statements are prepared using the Standard, the basis of presentation note (and, where applicable, the auditor's report) would refer to compliance with the *IFRS for SMEs*. Many SMEs may find that this internationally recognised 'cachet' for their financial statements will improve their access to capital.

The IASB has not set an effective date for the Standard because the decision as to whether to adopt the *IFRS for SMEs* (and also, therefore, the timing for adoption) is a matter for each jurisdiction.

The *IFRS for SMEs* is intended by the IASB for use by entities that have no public accountability and are required, or choose, to publish general purpose financial statements for external users. Essentially, an entity is considered to have public accountability if its debt or equity instruments are publicly traded, or if it is a financial institution or other entity that, as part of its primary business, holds and manages financial resources entrusted to it by clients.

Ultimately, the decision regarding which entities should use the *IFRS for SMEs* rests with national regulatory authorities and standard-setters – and those bodies will often specify more detailed eligibility criteria, including quantified criteria based on revenue, assets etc.

The effective date of the *IFRS for SMEs* will be determined in each jurisdiction that adopts it. The Standard contains a section on transition which contains all of the exemptions in IFRS 1 *First-time Adoption of International Financial Reporting Standards*– with additional simplifications in relation to comparative information. IFRS 1 requires an entity's first IFRS financial statements to include at least one year of comparative information under IFRSs. The *IFRS for SMEs* provides some relief from this by including an 'impracticability' exemption. Similarly, it provides an impracticability exemption with respect to restating the opening statement of financial position.

### **Topics that have been omitted from the IFRS for SMEs**

The *IFRS for SMEs* does not address the following topics that are dealt with in full IFRSs, because these topics are not generally relevant to SMEs:

- earnings per share;
- interim financial reporting;
- segment reporting;
- insurance (because entities that issue insurance contracts will not be eligible to use the *IFRS for SMEs*); and
- assets held for sale.

### **Accounting treatments disallowed under the IFRS for SMEs**

The *IFRS for SMEs* **does not allow** the following accounting treatments that are available under full IFRSs (generally because a simplified method is available to SMEs):

- the revaluation model for property, plant and equipment and intangible assets;
- proportionate consolidation for investments in jointly controlled entities;
- for investment property, measurement is driven by circumstances rather than allowing an accounting policy choice between the cost and fair value models. Under the *IFRS for SMEs*, if an entity can measure the fair value of an item of investment property reliably without undue cost or effort, it must use fair value. Otherwise cost is applied;
- various options for government grants permitted by IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*;
- capitalisation of borrowing costs;
- capitalisation of development costs; and
- deferral of actuarial gains and losses of defined benefit pension plans.

Regarding financial instruments, the Standard drops the 'available-for-sale' and 'held-to-maturity' categories of IAS 39, has no fair value option, and has simplified hedge accounting and derecognition requirements. However, there is a fallback that allows entities to choose to apply IAS 39 in its entirety instead of the financial instrument requirements in the *IFRS for SMEs*. This is the only fallback option to full IFRSs in the *IFRS for SMEs*. It is expected that most SMEs will not choose to apply IAS 39 due to the additional complexity.

### ***IFRS for SMEs recognition and measurement simplifications***

The main simplifications to the recognition and measurement principles in full IFRSs are:

#### Financial instruments

- Financial instruments meeting specified criteria are measured at cost or amortised cost. All others are measured at fair value through profit or loss. This avoids the inherent complexities of classifying financial instruments into four categories, such as assessing management's intentions and dealing with 'tainting provisions'.
- The IFRS establishes a simple principle for derecognition. The 'pass-through' and 'continuing involvement' tests in full IFRSs are dropped.
- Hedge accounting requirements, including the detailed calculations, are simplified and tailored for SMEs.

#### Goodwill and other indefinite-life intangible assets

- Goodwill and other indefinite-life intangible assets are always considered to have finite lives. Therefore, such assets are amortised over their estimated useful lives. If the useful life cannot be estimated, then the assets are amortised over 10 years. An impairment test is performed only if there is an indication of impairment (full IFRSs would require the test at least annually).
- Investments in associates and joint ventures can be measured at cost unless there is a published price quotation (when fair value must be used).
- All research and development costs, and borrowing costs, must be expensed.
- Residual value, useful life and depreciation method for items of property, plant and equipment, and amortisation period/method for intangible assets, only need to be reviewed if there is an indication they may have changed since the most recent annual reporting date (full IFRSs requires an annual review).

#### Defined benefit plans

- All past service cost must be recognised immediately in profit or loss.
- All actuarial gains and losses must be recognised immediately either in profit or loss or other comprehensive income.
- An entity is only required to use the projected unit credit method to measure its defined benefit obligation and the related expense if it is possible to do so without undue cost or effort.

#### Others

- There is no separate **asset held-for-sale** classification. Instead, holding an asset (or group of assets) for sale is an impairment indicator.
- **Exchange differences recognised initially in other comprehensive income** are not reclassified to profit or loss on disposal of the related investment. This eliminates the need for tracking such exchange gains or losses after initial recognition.
- The directors' best estimate of the fair value of an **equity-settled share-based payment** is used to measure the expense if observable market prices are not available.



### ***Reductions in disclosure requirements***

The disclosure requirements in the *IFRS for SMEs* are substantially reduced when compared with those in full IFRSs. Disclosures required by full IFRSs have been omitted from the *IFRS for SMEs* for two principal reasons, i.e. either:

- they relate to topics or accounting policy options in full IFRSs that are omitted from the *IFRS for SMEs*, or they relate to recognition and measurement principles in full IFRSs that have been replaced by simplifications in the *IFRS for SMEs*; or
- they are not considered appropriate based on users' needs and/or cost-benefit considerations. For example, some disclosures in full IFRSs are more relevant to investment decisions in public capital markets than to the transactions and other events and conditions encountered by typical SMEs.

### ***Additional guidance material***

To accompany the Standard, the IASB has produced implementation guidance consisting of illustrative financial statements and a presentation and disclosure checklist.

## ED Measurement of Liabilities in FRS 37 (Limited re-exposure of proposed amendment FRS 37 *Provisions, Contingent Liabilities and Contingent Assets* issued in 2005)

ED on amendments to FRS 37 originally proposed in 2005 sought to treat items previously described as 'contingent liabilities' more consistently in and outside a business combination. The proposed revised FRS 37 would be wider in scope and would apply to all non-financial liabilities that are not within the scope of other standards.

In 2010, the ED *Measurement of Liabilities* in FRS 37 was issued which deals with only one section of the proposed amendment to FRS 37 and addresses the measurement requirements for liabilities that are within the scope of FRS 37.

### **Key features of the 2010 ED:**

The 2010 ED clarifies the measurement objective i.e. that a liability should be measured at the amount that the entity "would rationally pay at the end of the reporting period to be relieved of the present obligation". It proposes that that amount should be determined as the lowest of:

- the present value of the resources required to fulfil the obligation; or
- the amount an entity would have to pay to cancel the obligation; or
- the amount an entity would have to pay to transfer the obligation to a third party.

Under the proposals, the amount an entity would have to pay to cancel or transfer the obligation is the price that the counterparty or a third party would demand, plus any costs of cancellation or transfer. If there is no evidence that an entity could cancel or transfer an obligation for a lower amount, the entity should measure the liability at the present value of the resources required to fulfil the obligation.

The 2010 ED also adds guidance on applying expected value techniques. It proposes that the present value of the resources required to fulfil an obligation should be estimated taking into account:

- the expected outflow of resources (i.e. estimate the probability-weighted average of the outflows for the range of possible outcomes) and the time value of money; and
- the risk that actual outflows might differ from those expected.

Finally, the 2010 ED specifies that when the obligation is to undertake a service at a future date and there is a market for the service, the 2010 ED would require that the outflows be the amounts that the entity would rationally pay a contractor at the future date to undertake the service on its behalf. When there is not a market for the service, the 2010 ED requires the entity to estimate the amount it would charge another party at the future date to undertake the service, based on the costs the entity expects to incur and the profit margin it would require to undertake the service.

## *ED Revenue From Contracts with Customers*

This ED is a result of the IASB's and FASB's objectives of developing a common, comprehensive, principles-based revenue standard that can be applied consistently to complex transactions across a wide range of industries. Some of the proposals may have significant implications for FRS reporters as they represent significant differences from current practice under FRS.

The ED would require retrospective application. A separate consultation document is expected to be issued seeking stakeholder input about effective dates and transition methods on a range of projects.

The proposals would apply to a contract with an entity's customer except for:

- financial instrument contracts;
- insurance contracts;
- leasing contracts; and
- nonmonetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange (e.g. swaps of similar items).

### **Identification of separate performance obligations**

Under the ED, an entity evaluates all goods and/or services promised in the contract to determine whether there are separate performance obligations. The proposals would require an entity to account separately for a good or service if it is distinct, meaning that the good or service either is sold separately in the customer's market or could be sold separately because it would be useful in itself or in conjunction with another product that is available separately.

FRSs do not currently provide guidance relating to the unbundling of multiple element arrangements, and there may currently be diverse methods in unbundling.

### **Allocation of the transaction price to different elements**

The ED requires the transaction price to be allocated between distinct elements in proportion to the stand-alone selling price of each element. The best evidence of a stand-alone selling price is the observable price of a good or service that is sold separately. However, in situations where goods or services are not sold separately, the ED would require an entity to develop an estimate based on a reasonable approach. Any discount to the aggregate of stand-alone selling prices is allocated strictly in proportion to the stand-alone selling price of each distinct good or service.

There is currently limited guidance under FRSs relating to the allocation of the transaction price to different elements. Entities that look to other GAAPs, such as the U.S. guidance on Vendor Specific Objective Evidence, may find that the allocation of revenue is very different under the proposals. In addition, entities like mobile phone operators that provide free or heavily discounted handsets to customers may find that their accounting for multiple element contracts changes under the proposals. The proposals may result in allocations that do not necessarily reflect the economics of the transaction.

For example, when low-margin elements are bundled with high-margin elements, an entity may provide a discount

to the customer on the high-margin element. Under the proposals, that discount must be allocated pro rata to all elements in the contract which may result in the entity recognising a loss on the low-margin element even though no discount was provided on that particular element. For example, this might affect software suppliers that grant discounts against the licence element within a package. Also, in some cases estimating the stand-alone selling price of an item that is not sold separately could be particularly challenging.

#### **Variable consideration**

When an entity has delivered goods or services, sometimes the amounts it will receive in the future are not fixed. Under the proposals, future variable consideration would be recognised using an 'expected value' approach, but only where that expected value can be measured reliably. Such an approach requires management to develop probabilities for each possible scenario based on the relevant past experience and assess as to whether it believes circumstances will change significantly.

A consequence of this could potentially be that revenue will be recognised earlier under the proposed approach if the variable consideration is reliably measurable. Estimates may need to be updated based on changes in facts and circumstances which could lead to increased volatility.

#### **Credit risk of the customer**

Under the proposals, the customer's credit risk affects how much revenue is recognised rather than whether revenue is recognised. An entity would adjust the transaction price to reflect the customer's credit risk using a probability-weighted approach.

Under current FRSs, the customer's credit risk affects whether revenue is recognised. Revenue is only recognised if it is probable that the benefits will flow to the entity. Therefore, entities that currently defer the recognition of revenue because of significant uncertainties over whether the customer will be able to pay would likely recognise revenue earlier than at present and at a different amount.

#### **Recognising allocated revenue**

Revenue would be recognised when the customer obtains control of the goods or services. This aspect of the proposals is of fundamental importance to many, but it is also one that will likely require the most judgement. The principle outlined is that "a customer obtains control of a good or service when the customer has the ability to direct the use of, and receive the benefit from, the good or service". A customer has obtained control if it has the present right to use the asset for its remaining economic life or to consume the asset in the customer's activities, together with the present right to obtain substantially all of the potential cash flows from that asset. The transfer of control of a product or service can be at a point in time or continuous.

Under FRS 18, revenue from the sale of goods is typically recognised at a single point in time when the risks and rewards have been transferred to the customer. Revenue from services and construction contracts is typically recognised using the percentage of completion method as services are being performed. Under the proposals, entities must assess whether the customer has obtained control of the product or service. Revenue would not be recognised until control is transferred to the customer.

The proposals may have a significant impact for entities that currently apply a percentage of completion model but the customer has neither physical possession of nor title to any work in progress. They may be required to recognise revenue when the product is completed and delivered to the customer. For example, this might affect entities that produce customer-specific reports, software or specialist equipment.

Under FRS 11 and INT FRS 115, whether the design or function of the good or service is customer-specific determines if a contract is a construction contract and, therefore, whether revenue is recognised on a percentage of completion basis. Under the proposals, this factor will no longer be sufficient in and of itself and judgement will be required as to whether the customer has control of any work in progress.

### **Onerous performance obligations**

An entity would evaluate an individual performance obligation to determine whether it is onerous. A performance obligation would be onerous if the direct costs that would be incurred to satisfy the obligation are greater than the allocated transaction price. If so, a separate liability would be recognised for that individual performance obligation.

Under current FRSs, an entity evaluates the contract as a whole to determine whether it is onerous. If so, a provision is recognised for that onerous contract. Some entities choose to sell items at a loss to generate future profitable business. Under the proposals, any contract that includes such items will, at the date of signing, result in the recognition of an onerous performance obligation provision – even if those items are bundled with other profitable items so that the contract as a whole is profitable.

### **Warranties**

The proposals distinguish between a product warranty that provides coverage for latent defects and a warranty that covers faults that arise after the product is transferred. A latent defect is one that exists but is not apparent when the asset is transferred to the customer. A separate performance obligation would not be recognised for these types of product warranties; instead, revenue relating to the product itself is restricted to reflect the fact that a defective product has been supplied. Accordingly, an entity would need to estimate the amount of unsatisfied performance obligations relating to these types of warranties at the end of the reporting period based on the likelihood and extent of latent defects in the products it has sold to customers. An entity would not recognise revenue for products it expects to be required to replace and would not recognise the portion of revenue that can be attributed to components that the entity expects to be required to repair.

A warranty that is provided to a customer that covers faults that arise after the product is transferred to the customer gives rise to a separate performance obligation. Therefore, a portion of the transaction price should be allocated by the entity to that warranty performance obligation.

Under current FRSs, warranties are often recorded as a liability at inception of the contract on the basis of the estimated costs to repair or replace the product. Under the ED, revenue would instead be deferred and recognised on an appropriate basis over the warranty period. This change could have a significant effect on some entities that provide warranties to their customers, particularly in respect of faults other than latent defects.

### **Rights of return**

An entity would not recognise the portion of revenue for goods expected to be returned. Instead, a liability would be recognised for the expected amount of returns and that liability would be updated for any changes in estimate. Additionally, an asset and a corresponding credit to cost of sales would be recognised for the right of recovery from the customer.

### **Licences of intellectual property**

A licence that transfers control of the entire licensed intellectual property to the customer (e.g. an exclusive licence for the entire economic life) would be treated as a sale. An entity that licenses the use of its intellectual property but does not transfer control of the entire licensed intellectual property to the customer (e.g. a licence for less than its economic life) would need to determine whether the licence is exclusive or non-exclusive. For exclusive licences, the performance obligation would be extinguished over time so revenue would be recognised over the term of the licence. For non-exclusive licences, the performance obligation would relate only to transfer of the licence and therefore revenue would often be recognised at the date the customer is able to use the licence.

Under current FRSs, an entity that licenses the use of its intellectual property would generally recognise revenue when the contractual performance has occurred and to the extent that reliable measurement of revenue is possible. For example, the fixed element of royalty revenues is typically recognised at inception of the contract if there are no outstanding contractual obligations. The proposals may result in entities recognising revenues over the term of the licence instead of recognising revenue upon the granting of the licence. Entities in the pharmaceutical and media sectors, and manufacturers of customer-specific software that allow customer choice over whether to renew a licence may be particularly affected by these proposals.

### **Contract costs**

The proposals include specific guidance on which types of costs would be capitalised or expensed. For example, amounts paid to obtain a customer contract must be expensed when incurred.

The proposed guidance may result in the expensing of costs that were previously capitalised which may affect the profit profile of a contract. For example, entities that pay significant amounts to third parties (e.g. agents) in order to secure contracts, and currently capitalise the amounts paid, would recognise such costs as an expense when incurred.

## **ED Proposed amendments to FRS 1 *Presentation of Financial Statements*- Presentation of Items of Other Comprehensive Income**

It proposes a limited amendment to FRS 1 regarding the presentation of items contained in other comprehensive income ("OCI") and their classification within OCI. The ED proposes the following:

### **Presentation of profit or loss and OCI as separate components in a single financial statement**

Currently, entities have an option under FRS 1 to present either a single statement of comprehensive income or two separate statements i.e. a statement of profit or loss and a separate statement of OCI. Under the proposals, the latter option of presenting two separate statements would be eliminated. As a result, all entities would be required to present a single continuous statement comprising 2 sections - profit or loss section and OCI section for the period.

### **Separate presentation in OCI of items that will be reclassified to profit or loss in a subsequent period.**

The proposals require items of OCI to be grouped based on the following categories:

- Items that might be reclassified to profit or loss in subsequent periods; and
- Items that will not be reclassified to profit or loss in subsequent periods.

The proposals also require allocation of income tax between the above groupings of OCI where OCI is presented before related income tax effects.

### **Title change**

The ED proposes the title "Statement of Profit or Loss and Other Comprehensive Income" for the single, two-section statement. However, in line with the current requirements of FRS 1, the proposals would continue to permit entities to use other titles for this statement.

## ED Proposed amendments to FRS 19 *Employee Benefits* - Defined Benefit Plans

The ED proposes several significant changes to the current requirements under FRS 19.

### **Elimination of the corridor method**

The proposal to eliminate the option to apply the corridor method is likely to have the most significant impact in practice. The corridor method permits an entity to defer a portion of actuarial gains and losses that fall outside a specified corridor (being the greater of 10% of the defined benefit obligation (“DBO”) or 10% of the fair value of plan assets). Consequently, all actuarial gains and losses would be recognised immediately through OCI and the net pension asset or liability recognised in the statement of financial position would reflect the full amount of the over-funded or underfunded status of the benefit plans. The option to recognise actuarial gains and losses in profit or loss is removed.

### **Change in presentation approach**

The ED proposes a new presentation approach for changes in defined benefit obligations and the fair value of plan assets. Entities would segregate changes in the defined benefit obligation and the fair value of plan assets into those associated with (1) service costs, (2) finance costs and (3) rereasurement.

### **Disclosures**

To improve the clarity of the information disclosed with respect to defined benefit plans, the Board proposes to set out several objectives to guide the preparation of these disclosures i.e.

- Explain the characteristics of an entity’s defined benefit plans.
- Identify and explain the amounts in the financial statements resulting from those plans.
- Describe how future cash flows (amount, timing and uncertainty) may be affected by the defined benefit plans offered by the entity.

### **Classification of employee benefits**

The ED proposes to simplify the classification of the different employee benefits arrangements by grouping in a single category long-term employee benefit arrangements that are currently defined as “post employment benefits” and “other long-term employee benefits”. As a result, all long-term defined benefit arrangements would be recognised and measured in the same manner and would be subject to the same disclosure requirements.

The ED also proposes to change the factors used to determine whether an employee benefit plan is short-term or long-term. Short-term benefits are restricted to plans that are expected to be settled within 12 months after the end of the reporting period in which the related services have been rendered and before the completion of employment. All other employee benefits plans (except termination benefits) would be considered as long-term employee benefits.

### **Tax and administrative costs**

The ED proposes to eliminate the option currently available in FRS 19 to include plan administrative costs either as a reduction of the return on plan assets or as an adjustment to the defined benefit obligation. Instead, the ED specifies that only costs relating to the management of the plan assets would be presented as a reduction of the return on plan assets. The ED also clarifies that current service cost would include taxes payable by a plan on contribution and benefits relating to services rendered before the reporting date.

### **Future salary increases**

The ED proposes to remove a source of ambiguity in FRS 19 by specifying that future salary increases must be considered in determining whether a benefit formula results in employee’s service in later years contributing to materially higher level of benefit than in earlier years. When this is the case, the benefit must be recognised on a straight-line basis.

## ED Leases

The exposure draft proposes to eliminate the distinction between operating leases and finance leases and introduces new accounting models for lessees and lessors. Lessees would no longer be permitted to treat leases as “off-balance sheet” financings but instead would be required to recognise an asset and liability for all leases within the scope of the proposals.

The exposure draft has significant implications for lessors and lessees. It would affect key performance metrics e.g. an increase in assets and liabilities could result in lower asset turnover ratios, lower return on capital, and an increase in debt to equity ratios which could impact borrowing capacity or compliance with loan covenants.

### **Scope**

Contracts specifically identified as not being within the scope of the ED are:

- leases of intangible assets,
- leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources,
- leases of biological assets, and
- leases between the date of inception and date of commencement of a lease if they meet the definition of an onerous contract under FRS 37 *Provisions, Contingent Liabilities and Contingent Assets*

### **Investment properties**

A lessee of investment property that elects to measure the property at fair value under FRS 40 *Investment Property* would measure the right-of-use asset in accordance with FRS 40 after initial recognition. Changes in the liability to make lease payments after initial recognition would be recognised in profit or loss in accordance with FRS 40. Also, a lessor that leases investment property to others would not apply the proposals if the lessor elects to measure the property at fair value in accordance with FRS 40. For lessors that use the fair value model, the ED proposes to amend FRS 40 to require income on investment property to be recognised on a straight-line basis over the lease term.

### **Purchases or sales**

Contracts that represent the purchase or sale of the underlying asset would be scoped out of the proposed standard and accounted for under existing FRSs. A contract would be considered a purchase or a sale if at the end of the term the contract transfers:

- control of the underlying asset; and
- all but a trivial amount of the risks and benefits associated with the entire underlying asset to another entity. The transfer of title of the underlying asset, in and of itself, would not be sufficient for an entity to conclude that the transaction should be considered a purchase or sale. All but a trivial amount of the risks and benefits must also be transferred to the lessee.

### **Short-term leases**

The ED defines a short-term lease as “a lease that, at the date of commencement of the lease, has a maximum possible lease term, including options to renew or extend, of twelve months or less”. A lessee still would need to record a right-of-use asset and a corresponding liability but could elect, on a lease-by-lease basis, to measure the liability at the undiscounted amount of the lease payments and the right-of-use asset at the undiscounted amount of lease payments plus initial direct costs.

A lessor could elect, on a lease-by-lease basis, not to recognise a lease receivable or a liability but continue to recognise the underlying asset and recognise lease payments in profit or loss over the lease term.



### **Contracts that contain both lease and service components**

If a contract contains a lease, but also contains a service component, the ED would generally not apply to the “distinct” service components within the contract. A service component would be considered distinct if the entity or another entity either sells an identical or similar service separately or the entity could sell the service separately because the service has a distinct function and a distinct profit margin.

If the service component is not distinct (or if they are unable to allocate the payments between the distinct service and lease components), lessees and lessors that apply the performance obligation approach<sup>(1)</sup> would treat the entire contract as a lease. Lessors that apply the derecognition approach<sup>(1)</sup> would be required to allocate the payments between the service and lease components on a reasonable basis even if the service component is not distinct.

<sup>(1)</sup>The performance obligation and derecognition approach is discussed below.

The determination of whether a service component is distinct is made at lease inception. If the payments required under the contract change after the commencement of the lease, an entity would determine the amount of the change attributable to the lease and service components. If such a determination is not possible, an allocation applying the same proportion as used at the date of commencement would be acceptable.

### **Lessee accounting**

The lessee accounting model is based on a right-of-use approach. Upon lease commencement, the lessee obtains a right to use an asset for a specified period and would recognise an asset reflecting that right and a liability for its obligation to pay rentals. The proposed model differs from the current lease accounting model where a lessee accounts for its right to use the leased asset either by recognising an asset and liability (i.e. capital/finance lease) or as an executory contract (i.e. operating lease) depending on the terms of the lease.

Other than short-term leases, the initial measurement of the obligation to make lease payments would be at the present value of the lease payments, discounted using the lessee’s incremental borrowing rate or the rate the lessor charges the lessee, if it can be readily determined. The right-of-use asset would be initially measured at the same amount as the obligation to make lease payments plus any initial direct costs. The two key components that a lessee must take into account when initially measuring the right-of-use asset and the lease liability are (1) the lease term and (2) the lease payments – both of these concepts are discussed in more detail below.

### **Lease term**

According to the ED, the lease term is defined as “the longest possible term that is more likely than not to occur”. An entity would need to estimate the probability that each possible lease term would occur by taking into account explicit and implicit renewal options or early termination options included in the contract and by operation of the statutory law. The ED lists out factors that a lessee would consider in assessing the probability of each possible lease term.

The current lease accounting model requires renewal options to be included in the accounting lease term if they are “reasonably certain” of being exercised. Current practice has generally interpreted “reasonably certain” as a high threshold. As a result, it is likely that the lease term under the proposed model would be longer, or at least as long, as the accounting lease term under FRS 17. In addition, lessees will need to consider carefully all renewal options – including “month-to-month” renewals where a lessee has the unilateral right to continue using the leased asset on a month-to-month basis at the end of the contractual lease term – as part of this analysis.

### **Lease payments**

The proposals would require a lessee to determine the lease payments payable during the lease term using an expected outcome approach that is described in the ED as “the present value of the probability-weighted average of the cash flows for reasonable number of outcomes”. The lease payments include estimates of contingent rentals, payments under residual value guarantees between the lessee and lessor and payments to the lessor under term option penalties.

The inclusion of contingent rentals using an expected outcome approach would represent a significant change from the current lease accounting model that generally excludes contingent rentals from minimum lease payments. The need to develop scenarios and probabilities based on information that could differ from lease to lease could make this requirement costly and time-consuming for many entities.

### **Lessor accounting**

The ED proposes two accounting models for lessors – the performance obligation approach and the derecognition approach. The model to apply for a particular lease contract would be based on whether the lessor retains significant risks and benefits associated with the underlying asset. A lessor that retains exposure to significant risks or benefits associated with the underlying asset would apply the performance obligation approach; otherwise, the lessor would apply the derecognition approach. The determination on the appropriate model to apply would be made at inception of the lease and would not be reassessed.

### **Performance obligation approach**

Under the performance obligation approach, the lessor has a performance obligation to permit use of the underlying asset during the lease term. A lessor would recognise an asset for its right to receive lease payments equal to the sum of the present value of the lease payments, including initial direct costs incurred by the lessor, discounted using the rate charged by the lessor. A lessor would not derecognise the underlying asset.

The initial measurement of the lease receivable at the date of inception of the lease would be based on the longest possible lease term that is more likely than not to occur determined using an expected outcome approach (like the approach used by the lessee as described above), and includes contingent rentals and residual value guarantees provided by the lessee if these amounts can be “measured reliably”.

The lease payment receivable would be measured subsequently at amortised cost using the effective interest method. The liability would be amortised on the basis of the pattern of use of the underlying asset by the lessee (e.g. hours of use or units produced) or on a straight-line basis if the pattern of use cannot be determined reliably.

A lessor would be required to reassess the carrying amount of the lease receivable if there is a change in facts or circumstances that indicates that there is a significant change to the reported amount of the lease receivable.

A lessor would present the underlying asset, lease receivable, and lease liability on a gross basis in the statement of financial position, with a total of these items as a net lease asset or net lease liability. A lessor would present in profit or loss the interest income on the lease receivable, lease income resulting from the satisfaction of the performance obligation and depreciation expense separately.

### **Derecognition approach**

Under the derecognition approach, the obligation to deliver the asset to the lessee is the performance obligation and it is satisfied at lease commencement. A lessor would recognise an asset for the right to receive rental payments measured at the present value of the lease payments discounted using the rate the lessor charges the lessee plus any initial direct costs incurred by the lessor. It will remove a portion of the carrying amount of the underlying asset from its statement of financial position and reclassify as a residual asset the portion of the carrying amount of the underlying asset that represents the lessor's rights in the underlying asset that it did not transfer.

The lessor would measure the lease receivable at amortised cost using the effective interest method. The residual asset would not be remeasured unless there is a change in lease term or the asset is impaired.

Additionally, at the date of commencement of the lease, a lessor would recognise lease income representing the present value of the lease payments and lease expense representing the cost of the portion of the asset derecognized. These amounts would be classified as revenue and cost of sales if generated in the course of the lessor's ordinary activities.

The expected lease payments (including the lease term, contingent rentals, term option penalties and residual value guarantees) would be reassessed at each reporting period if any new facts or circumstances indicate a significant change in the right to receive rental payments.

A lessor would present the lease receivable separately from other financial assets. The residual assets would be presented separately within property, plant and equipment. The presentation in profit or loss will either be gross or net in a single line item, on the basis of the lessor's business model. If a lessor's business model is to use leasing arrangements for the purposes of providing finance, then the lessor would present income and expense net. However, manufacturers and dealers that utilise leasing as an alternative way to sell their products that would otherwise sell would present income and expenses gross as revenue and cost of sales. Also, a lessor would present interest income on its leased assets separately from other interest income.

### **Sale and leaseback transactions**

An entity may enter into contracts to transfer an asset to another party and then lease that asset back. The contracts taken together would be considered a "sale and leaseback transaction" if they are "entered into at or near the same time, negotiated as a package with a single commercial objective or performed either concurrently or consecutively."

According to the ED, if the transaction meets the criteria to be considered a sale and leaseback transaction and meets the conditions for a sale (i.e. control of the underlying asset has been transferred along with all but a trivial amount of the risks and benefits associated with the underlying asset), the transferor would account for the transaction as a sale in accordance with other applicable FRSs and for the right-of-use asset and obligation to make lease payments in accordance with the proposed guidance for lessees. Likewise, a transferee would account for the transaction as a purchase in accordance with other applicable FRSs and the lease in accordance with the performance obligation approach.

The ED lists conditions that would normally preclude purchase and sale accounting. If the transaction is not a sale or purchase, the transferor would account for the contract as a financing with the amount received recognised as a financial liability and the transferee would recognise the amount paid as a receivable in accordance with applicable FRSs.

If the consideration for a purchase or sale and the lease payments are not at fair value, the transferor adjusts (1) the right-of-use asset to reflect current market rates and (2) the gain or loss by any difference between the present value of lease payments based on the terms specified in the lease and the present value of the lease payments based on current market rates. A transferee adjusts the carrying amount of the underlying asset and the lease liability it recognises under the performance obligation approach to reflect current market rates for the lease payments for that lease contract.

The proposed sale and leaseback rules could represent a significant change to the current accounting under FRS 17. Under the ED, an entity that sells an asset and subsequently leases that asset back needs to consider carefully its continuing involvement with the underlying asset before recognising a sale. Many of the conditions listed in the ED that may preclude sale and leaseback accounting may not be considered under current practice.

### **Disclosure**

The ED would significantly increase the required disclosures related to lease arrangements. An entity would be required to disclose quantitative and qualitative information that “identifies and explains the amounts recognised in the financial statements arising from leases” and “describes how leases may affect the amount, timing and uncertainty of the entity’s future cash flows”. Disclosures would need to be disaggregated to a level so that the information provided is useful to the users of the financial statements.

Disclosures would include, among others, descriptions of the terms of contingent rentals, renewal options, and residual value guarantees as well as information about changes in assumptions and judgements relating to options, contingent rentals, residual value guarantees and discount rates. The ED would also require both lessees and lessors to provide a reconciliation between opening and closing balances of assets and liabilities related to lease arrangements.

## ED Proposed Amendments to FRS 12 *Income Tax - Deferred Tax: Recovery of Underlying Assets*

The ED contains a proposal to amend FRS 12 *Income Tax* to provide an exception to the principle that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities.

The ED proposes that in specified circumstances, the measurement of deferred tax liabilities and deferred tax assets should reflect a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale.

The specified circumstances are that the deferred tax liability or deferred tax asset arises from:

- (a) investment property, when an entity applies the fair value model in FRS 40 *Investment Property*;
- (b) property, plant and equipment or intangible assets, when an entity applies the revaluation model in FRS 16 *Property, Plant and Equipment* or FRS 38 *Intangible Assets*; and
- (c) investment property, property plant and equipment or intangible assets acquired in a business combination if they are subsequently measured using the fair value or revaluation models.

The presumption is rebutted only when an entity has clear evidence that it will consume the asset's economic benefits throughout its economic life. The proposed amendments are intended to provide a practical approach for measuring deferred tax liabilities and deferred tax assets when it would be difficult and subjective to determine the expected manner of recovery.

## ED Proposed amendment to FRS 101 *First-time Adoption of Financial Reporting Standards - Severe Hyperinflation*

This ED proposes to amend FRS 101 *First-time Adoption of International Financial Reporting Standards* to provide guidance on how an entity should resume presenting financial statements in accordance with FRSs after a period when the entity was unable to comply with FRSs because it had a functional currency that was subject to severe hyperinflation.

The proposed amendment will add an exemption to FRS 101. This exemption would allow an entity that has been subject to severe hyperinflation to measure assets and liabilities at fair value and use that fair value as the deemed cost of those assets and liabilities in the opening FRS statement of financial position.

## ED Proposed amendment to FRS 101 *First-time Adoption of Financial Reporting Standards - Removal of Fixed Dates for First-time Adopters*

The ED proposes to provide relief to first-time adopters of FRSs by amending FRS 101 as follows:

- it amends the date of prospective application of the derecognition of financial assets and liabilities from '1 January 2004' to 'the date of transition to FRSs' so that first-time adopters of FRSs do not have to apply the derecognition requirements in FRS 39 retrospectively; and
- it amends the date of prospective application of the requirement to fair value financial assets and liabilities to transactions entered into 'on or after the date of transition to FRSs' which would relieve first-time adopters from recalculating 'day 1' differences on initial recognition for those transactions occurring before the date of transition to FRSs.

## ED Insurance Contracts

The ED is a result of a more comprehensive review of insurance accounting subsequent to the issuance of FRS 104. FRS 104 was issued in 2004 as an interim standard that permitted many existing international accounting practices at that time to be retained.

Key features of the ED:

The ED proposes a comprehensive measurement approach for all types of insurance contracts issued by entities (and reinsurance contracts held by entities), with a modified approach for some short-duration contracts. The approach is based on the principle that insurance contracts create a bundle of rights and obligations that work together to generate a package of cash inflows (premiums) and outflows (benefits and claims). An insurer would apply to that package of cash flows a measurement approach that uses the following building blocks:

- (a) a current estimate of the future cash flows
- (b) a discount rate that adjusts those cash flows for the time value of money
- (c) an explicit risk adjustment
- (d) a residual margin.

For most short-duration contracts, a modified version of the measurement approach would apply:

- (a) During the coverage period, the insurer would measure the contract using an allocation of the premium received, on a basis largely similar to much existing practice.
- (b) The insurer would use the building block approach to measure claims liabilities for insured events that have already occurred.

## Draft Interpretation *Stripping Costs in the Production Phase of a Surface Mine*

The Draft Interpretation was developed in response to a request for guidance on accounting for waste removal costs incurred in the production phase of a surface mine.

The Draft Interpretation proposes that costs of a stripping campaign incurred during the production phase would be capitalised as a component of an existing asset, whereas routine stripping costs would be expensed. In addition, the stripping campaign component would be classified according to the nature of the existing asset to which it relates. Stripping campaign costs would initially be measured at cost and subsequently carried at cost less depreciation or amortisation and impairment.

The proposals would be applied prospectively from the date of adoption, with any existing stripping cost assets being reclassified as a component of the asset to which it relates.

## *ED on Conceptual Framework - Description of the Reporting Entity*

This ED forms part of the multi-phased joint IASB and FASB project to develop a common conceptual framework. The IASB and the FASB believe that establishing a common definition of the reporting entity concept at the framework level will assist in developing a consistent approach on the consolidation project at the standard-level.

The ED proposes that a reporting entity is a “circumscribed area of economic activities whose financial information has the potential to be useful to existing and potential equity investors, lenders and other creditors who cannot directly obtain the information they need in making decisions about providing resources to the entity and in assessing whether management and the governing board of that entity have made efficient and effective use of the resources provided.”

The ED specifies three necessary features of a reporting entity as follows:

- economic activities are being conducted, have been conducted, or will be conducted;
- the economic activities can be objectively distinguished from those of other entities and from the economic environment in which the entity exists; and
- financial information about the economic activities has the potential to be useful to existing and potential equity investors, lenders and other creditors.

The ED reconfirms that the existence of a legal structure is not determinative of the existence of a reporting entity. Instead of placing emphasis on the legal structure, the ED focuses on the economic activities. This approach may result in a portion of a legal entity being considered a reporting entity.

Where multiple entities are involved, the identification of control is the primary means for determining which entities should be reported as a single unit in consolidated financial statements. When an entity (parent) controls another entity, the parent should present consolidated financial statements.

The ED mandates the presentation of consolidated financial statements whenever a parent controls one or more entities. However, the IASB and the FASB recognise that other types of financial statements may provide useful information. Therefore, the ED proposes that a parent entity may present parent-only financial statements, as long as they are presented together with the consolidated financial statements. Similarly, the ED acknowledges that combined financial statements that include two or more commonly controlled entities may provide useful information about those commonly controlled entities as a group. However, combined financial statements are no substitute for consolidated financial statements.

## *ED Fair Value Option for Financial Liabilities*

In 2009, ED *Financial Instruments: Classification and Measurement* was issued with the objective of improving the decision-usefulness of financial statements for users by simplifying the classification and measurement requirements for financial assets. The project will ultimately replace many financial asset classification categories and associated impairment methods in FRS 39 *Financial Instruments: Recognition and Measurement*.

In 2010, the ED *Fair Value Option for Financial Liabilities* was issued as part of the plan to replace FRS 39. This ED focuses on two areas (1) the presentation of the effects of changes in an entity's own credit risk and (2) the elimination of the cost exception for derivative liabilities.

While the above remain as EDs in Singapore, the IASB has issued IFRS 9 *Financial Instruments: Classification and Measurement* in 2009 and an updated version in 2010 which addresses the objectives mentioned above. IFRS 9 issued in 2009 addresses classification and measurement of financial assets, while IFRS 9 issued in 2010 addresses classification and measurement of financial liabilities. Both versions of IFRS 9 are summarised below.

[Note: The adoption of IFRS 9 in Singapore has been deferred to a later date to be advised by the ASC.]

### **IFRS 9 Financial Instruments: Classification and Measurement (issued in 2009)**

In 2009, the IASB issued IFRS 9 *Financial Instruments*. This Standard introduces new requirements for the classification and measurement of financial assets and is effective from 1 January 2013 with early adoption permitted.

The exposure draft for this Standard included both financial assets and financial liabilities within its scope. However, due to concerns raised with the proposals for financial liabilities, the scope of IFRS 9 (issued in 2009) was restricted to only financial assets. In 2010, new requirements for classification and measurement of financial liabilities were added (see below).

New requirements for impairment, hedge accounting and asset and liability offsetting are expected to be added to IFRS 9 in 2011. As a result, IFRS 9 will eventually be a complete replacement for IAS 39 *Financial Instruments: Recognition and Measurement*.

An early adopter of IFRS 9 continues to apply IAS 39 for other accounting requirements for financial instruments within its scope that are not covered by IFRS 9 (e.g. recognition and derecognition of financial assets and financial liabilities, impairment of financial assets, hedge accounting, etc.).

In summary, IFRS 9 requires recognised financial assets that are currently in the scope of IAS 39 to be measured at either amortised cost or fair value.

### **Debt instruments**

A debt instrument (e.g. loan receivable) that:

- (1) is held within a business model whose objective is to collect the contractual cash flows (i.e. "business model test"); and
- (2) has contractual cash flows that are solely payments of principal and interest on the principal amount outstanding (i.e. "contractual cash flow characteristic test");



generally must be measured at amortised cost. All other debt instruments must be measured at fair value through profit or loss ("FVTPL"). A fair value option is available (provided that certain specified conditions are met) as an alternative to amortised cost measurement.

#### Business Model and Contractual Cash Flow Characteristic Test

##### *(1) Business Model Test*

IFRS 9 includes guidance on how the business model test is met. For instance, the assessment of a business model is made at a level higher than individual instrument (e.g. portfolio or business unit level). Thus, a business model test is not based on management's intent for individual instruments. In addition, IFRS 9 also includes guidance on reclassification requirements when an entity changes its business model for managing financial assets.

##### *(2) Contractual Cash Flow Characteristic Test*

As for contractual cash flow tests, the concept in IFRS 9 is that only instruments with contractual cash flows of principal and interest on principal (hereafter referred to as "principal and interest") may qualify for amortised cost measurement. IFRS 9 describes interest as consideration for the time value of money and the credit risk associated with the principal outstanding during a particular period of time. Therefore, an investment in a convertible loan note would not qualify because of the inclusion of the conversion option which is not deemed to represent payments of principal and interest.

The application guidance to IFRS 9 includes examples of contractual cash flows that are payments of principal and interest on the principal amount outstanding and those that are not payments of principal and interest on the principal amount outstanding.

#### Fair Value Option

An entity may irrevocably elect on initial recognition to measure a financial asset at FVTPL if that designation eliminates or significantly reduces an accounting mismatch had the financial asset been measured at amortised cost. For example, an entity may hold a fixed rate loan receivable that it commercially hedges with an interest rate swap, with matching terms, that swaps the fixed rate to a floating rate. Assuming the conditions for amortised cost measurement are met, measuring the loan asset at amortised cost would create a measurement mismatch with the interest rate swap held at FVTPL. In this case the loan receivable could be designated at FVTPL under the fair value option to reduce the measurement mismatch that arises from measuring the loan at amortised cost.

### Equity instruments

All equity investments within the scope of IFRS 9 are to be measured on the statement of financial position at fair value with the default recognition of gains and losses in profit or loss. Only if the equity investment is not held for trading can an irrevocable election be made at initial recognition to measure it at fair value through other comprehensive income ("FVTOCI") with only dividend income recognised in profit or loss.

If the equity investment is designated as at FVTOCI then all gains or losses (except dividend income) are recognised in other comprehensive income without any subsequent reclassification to profit or loss (although a transfer of the cumulative gain within equity is permitted). Dividend income is recognised in profit or loss in accordance with IAS 18 *Revenue*. Designation as at FVTOCI means that the current requirements in IAS 39 to perform an assessment of impairment and to reclassify cumulative fair value gains or losses on disposal no longer apply because all fair value movements other than dividend income remain permanently in equity.

The current exemption in IAS 39 that requires unquoted equity investments to be measured at cost less impairment where fair valuation is not sufficiently reliable is not available under the new Standard. However, IFRS 9 does contain guidance on when cost might be the best estimate of fair value of an unquoted equity investment that is difficult to value because of little or no timely or relevant information. It also gives examples of when cost will not be representative of fair value such as when there has been a significant change in the performance of the investee compared with budgets, plans or milestones.

### Derivatives

All derivatives within the scope of IFRS 9 are required to be measured at fair value. This includes derivatives that are settled by the delivery of unquoted equity instruments, however, in limited circumstances cost may be an appropriate estimate of fair value.

Derivatives embedded in a financial host that is within the scope of IFRS 9 shall not be bifurcated. Instead the contractual cash flow of the hybrid financial asset (i.e. financial host and the embedded derivative) are assessed in their entirety and the hybrid financial asset as a whole is required to be classified as FVTPL if any of its cash flows do not represent payments of principal and interest.

Because IFRS 9 (issued in 2009) only applies to assets within the scope of IAS 39, the embedded derivative concept was retained for all hybrid financial liabilities and asset host contracts that are outside the scope of IAS 39.

### **IFRS 9 Financial Instruments: Classification and Measurement (issued in 2010)**

In October 2010 the IASB added to IFRS 9 (issued in 2009) the requirements related to the classification and measurement of financial liabilities. Those additional requirements are described below:

### Requirements for classification and measurement of financial liabilities

Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. Under IAS 39 most liabilities were subsequently measured at amortised cost or bifurcated into a host, which is measured at amortised cost, and an embedded derivative, which is measured at fair value. Liabilities that are held for trading (including all derivative liabilities) were measured at fair value.

Although the IASB had originally proposed a symmetrical approach for financial assets and financial liabilities, the IASB decided to retain most of the requirements in IAS 39 for classifying and measuring financial liabilities because constituents told the IASB that those requirements were working well in practice. Consistently with its objective to replace IAS 39 in its entirety, the IASB relocated those requirements from IAS 39 to IFRS 9.

### Derivatives

Consistent with the requirements in IFRS 9 for investments in unquoted equity instruments (and derivative assets linked to those investments), the exception from fair value measurement was eliminated for derivative liabilities that are linked to and must be settled by delivery of an unquoted equity instrument. Under IAS 39, if those derivatives were not reliably measurable, they were required to be measured at cost. IFRS 9 requires them to be measured at fair value.

### Fair value option

The requirements related to the fair value option for financial liabilities were changed to address own credit risk. The requirements distinguish between financial liabilities held for trading and financial liabilities designated as at FVTPL using the fair value option. Financial liabilities that are **required** to be measured at FVTPL would continue to be measured at fair value with all changes being recognised in profit or loss.

The amount of change in the fair value of financial liabilities designated as at FVTPL that is attributable to changes in the credit risk of that liability is required to be presented in other comprehensive income while the remaining amount of change in the fair value of the liability shall be presented in profit or loss. The only exception to this requirement would be when the treatment of the effects of changes in the liability's credit risk described above would create or enlarge an accounting mismatch in profit or loss.

### Derecognition

The requirements in IAS 39 related to the derecognition of financial assets and financial liabilities were carried forward unchanged to IFRS 9.

### Effective date

An entity shall apply this IFRS for annual periods beginning on or after 1 January 2013. Earlier application is permitted. However, if an entity elects to apply this IFRS early and has not already applied IFRS 9 (issued in 2009), it must apply all of the requirements in this IFRS at the same time (but see also Note below). If an entity applies this IFRS in its financial statements for a period beginning before 1 January 2013, it shall disclose that fact and at the same time apply all the consequential amendments to other IFRSs.

[Note - For annual periods beginning before 1 January 2013, an entity may elect to apply IFRS 9 issued in 2009 instead of applying this version of IFRS 9.]

### *ED Financial Instruments: Amortised Cost and Impairment*

This ED is based on an equivalent ED issued by the IASB, as part of its project to replace IAS 39 *Financial Instruments: Recognition and Measurement* with an entirely new standard (IFRS 9). The ED proposes principles for the measurement of financial instruments at amortised cost including a new impairment methodology based on expected losses.

The ED applies to all financial instruments that are measured at amortised cost and describes the objective of amortised cost measurement, underpinned by new measurement principles for financial assets, based on an expected cash flow methodology.

Under the proposed measurement principles, an entity would determine the initial carrying amount of a financial asset (or portfolio of financial assets) measured at amortised cost, on the basis of the present value of the future expected cash flows from the asset, taking into consideration expectations about future credit losses (referred to as the 'expected loss' approach).

Subsequent to initial recognition an entity would be required to revise its estimates of expected cash flows at each measurement date. Any resulting adjustment to the carrying amount of the financial instrument would be recognised in profit or loss. The proposed 'expected loss' approach is designed to result in earlier loss recognition compared to the 'incurred loss' approach currently in FRS 39 by taking into account future credit losses expected over the life of the financial asset measured at amortised cost.

Under this approach the initial estimate of expected future losses is gradually recognised over the life of the instrument as it is incorporated into the effective interest rate.

The ED also proposes comprehensive presentation and disclosure requirements that would enable users of the financial statements to evaluate the financial effects of interest revenue and interest expense as well as the quality of financial assets including credit risk.

If adopted, the expected loss model would involve significant costs and an extended period of implementation given the expected significant changes required to financial systems, particularly in the financial services industry.

### *ED Measurement Uncertainty Analysis Disclosure for Fair Value Measurements*

ED *Fair Value Measurement* was issued in 2009 ("2009 ED") which proposed a three-level fair value hierarchy that would categorise observable and non-observable market data used as inputs for fair value measurements. According to that hierarchy, Level 3 inputs are 'unobservable inputs' used for the fair value measurement of assets or liabilities for which market data is not available.

The 2009 ED would require that, if changing one or more of the inputs to reasonably possible alternative assumptions would change fair value significantly, an entity should state that fact and disclose the effect and the calculation of those changes. However, it was not clear whether an entity would be required to take into account interdependencies or correlation between inputs, or whether an entity would provide an analysis of changes in observable inputs or unobservable inputs, or both.

ED *Fair Value Measurement Disclosures* ("2010 ED") proposes that an entity should, at a minimum:

- i. provide a measurement uncertainty analysis disclosure for fair value measurements categorised within Level 3 of the fair value hierarchy that are fair valued in the statement of financial position;
- ii. if changing one or more of the unobservable inputs used in a fair value measurement to a different amount that could have reasonably been used in the circumstances (ignoring remote scenarios) would result in a significantly higher or lower fair value measurement, to disclose the effect of using those different amounts and how that effect is calculated;
- iii. take into account the effect of correlation between unobservable inputs, if such correlation is relevant, when estimating the effect on the fair value measurement of using those different amounts;
- iv. take into account the effect of correlation for unobservable inputs only; and
- v. describe the valuation technique(s) and the inputs used in the fair value measurement for level 3 fair value measurements.

The proposed disclosure differs from the market risk sensitivity analysis required in FRS 107. The proposals attempt to highlight the degree of subjectivity of the unobservable inputs included in the fair valuation; they do not attempt to illustrate how the fair valuation would have differed had the economic environment at the period end been different.

# Section 3: Summary of differences between FRS and IAS/IFRS

The FRSs and INT FRSs issued by the Accounting Standards Council (“ASC”) are largely aligned with the standards and interpretations under IAS/IFRS, except for certain modifications e.g. to effective dates and transitional provisions, and differences in timing of adoption. Below, we identify the key differences between FRS and IAS/IFRS as at the date of this publication:

FRS	Content	IAS /IFRS	Comments
ED SFRS for Small Entities	Small and Medium-sized Entities (“SMEs”)	IFRS for SMEs	<p>The IFRS for SMEs provides an alternative framework that can be applied by eligible entities in place of the full set of IFRSs in issue. It is effective immediately on issue. It is for each jurisdiction to determine which entities are eligible to use this framework.</p> <p>This Standard has not been adopted in Singapore yet.</p> <p>ASC has issued a Statement of Intent that proposes the IFRS for SMEs be adopted without modification as the <i>SFRS for Small Entities</i>. The <i>SFRS for Small Entities</i> would be available for eligible entities to apply for financial periods beginning on or after 1 January 2011.</p>
FRS 16	Property, Plant and Equipment	IAS 16	FRS 16 exempts regular revaluation for assets on which any one-off revaluation is performed between 1 January 1984 and 31 December 1996 (both dates inclusive) or for assets that have been revalued prior to 1 January 1984, whereas IAS 16 does not give such an exemption.
FRS 27, 28 and 31	Consolidated Financial Statements and Accounting for Investments in Subsidiaries, Associates and Joint Ventures	IAS 27, 28 and 31	The revised FRS 27 exempts a parent from presenting consolidated financial statements if its holding company produces consolidated financial statements available for public use, whereas under the revised IAS 27, such an exemption applies only if the holding company produces consolidated financial statements available for public use that comply with IFRS.

FRS	Content	IAS /IFRS	Comments
FRS 102	Share-based Payment	IFRS 2	The cut-off grant date for retrospective treatment of equity-settled share-based payment is 7 November 2002 under IFRS 2 and 22 November 2002 under FRS 102.
ED Financial Instruments	Financial Instruments: Classification and Measurement issued in 2009 and 2010	IFRS 9	<p>IFRS 9 is effective for annual periods beginning on or after 1 January 2013.</p> <p>This Standard has not been adopted in Singapore yet.</p> <p>ASC has deliberated the adoption of IFRS 9 and decided to defer its adoption in Singapore.</p>
ED INT FRS	Members' Shares in Co-operative Entities and Similar Instruments	IFRIC 2	<p>IFRIC 2 is effective for annual periods beginning on or after 1 January 2005.</p> <p>This Interpretation has not been adopted in Singapore yet.</p>
INT FRS 115	Agreements for the Construction of Real Estate	IFRIC 15	IFRIC 15 is effective for annual periods beginning on or after 1 January 2009 whereas INT FRS 115 is effective from 1 January 2011. In addition, INT FRS 115 contains an Accompanying Note that takes into account the legal framework in Singapore that is directly relevant to the application of INT FRS 115 in Singapore and summarises the ASC's considerations in reaching its consensus on the accounting treatment for the sale of uncompleted residential properties "off-plan".



# Resources

IASPlus – [www.iasplus.com](http://www.iasplus.com) - provides Deloitte IFRS e-Learning modules, newsletters, IAS/IFRS model financial statements, disclosure checklist and a wealth of information on IAS/IFRS projects and issues.

Deloitte Touche Tohmatsu – [www.deloitte.com](http://www.deloitte.com) - the website provides a global e-library and links to websites of member firms around the world.

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**Deloitte & Touche LLP**

Certified Public Accountants

6 Shenton Way #32-00

DBS Building Tower Two

Singapore 068809

Telephone: +65 6224 8288

Facsimile: +65 6538 6166

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