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MEDIA RELEASE

POSITIVE RESPONSE TO FINANCIAL REPORTING REGULATORY MEASURES - ACRA releases key findings from its review of FY2014 Financial Statements

Singapore, 27 September 2016 – Companies are responding positively to measures taken to improve quality financial reporting instituted by ACRA's Financial Reporting Surveillance Programme (FRSP). In the second annual FRSP report issued today, it was observed that companies took quick action to rectify financial reporting gaps highlighted through the FRSP.

2 Of 21 non-compliances¹ and 19 areas for improvement¹ communicated to companies before their FY2015 Financial Statements were finalised, 95% and 63% were rectified, respectively. A further four non-compliances and one area for improvement were pre-emptively rectified by the companies in the FY2015 Financial Statements, well before their reviews were concluded. The high rectification rate, especially for those cases with areas for improvement for which corrections are not mandatory, is highly encouraging. It shows that the vast majority of boards of listed companies in Singapore are committed to delivering high quality financial information to investors.

Key Findings for the FY2014 Financial Statements

3 The primary objective of the FRSP is to guide companies to meet the requirements in the accounting standards so that investors and other stakeholders are provided with reliable and meaningful financial statements. A total of 50 sets² of FY2014³ Financial Statements of listed companies incorporated in Singapore were reviewed in this second review cycle, for which 17 reviews were completed without

¹ All non-compliances and areas for improvement are instances where the financial statements were not compliant with the accounting standards, differentiated by the nature and extent of the misstatements. ACRA highlights areas for improvement for directors' future consideration but does not mandate them to be rectified.

² Financial statements were selected using the FRSP's risk-based approach. 49 sets were reviewed in the first review cycle, for which 5 warning letters, 30 advisory letters and 12 closure letters were issued.

³ Financial year ended between 1 January 2014 and 31 December 2014 (both dates inclusive).

any enquiry needed. Of the remaining 33, two warning letters, 21 advisory letters and seven closure letters were issued, while three reviews are ongoing.

4 Overall, a good level of quality in financial reporting was observed among those listed companies reviewed. In most cases, Boards took ownership over financial reporting with many taking steps to document their deliberations on complex accounting matters. There were fewer cases with findings when compared to last year's report, which saw five warning letters and 30 advisory letters issued. However, there remains room for improvement as a number of non-compliances with the accounting standards were identified.

5 The four areas with the highest instances of findings were new consolidation standards, business acquisitions, impairment of long-lived assets and fair value of properties. These areas were consistent with the areas of review focus highlighted in ACRA's Practice Guidance issued in January 2015 to guide directors in preparing the FY2014 Financial Statements.

6 In terms of behavioural root causes leading to the findings, it was observed that:

- (a) Information asymmetry between a company's business operations and its finance function could lead to accounting lapses. This occurs when the finance team was unable to understand the business rationale of unique arrangements or not alerted to important non-standard contract terms negotiated by the operations team;
- (b) Directors were also often not given opportunity and sufficient time to review and deliberate on whether the accounting is appropriate and consistent with their understanding of the business. Typically, such discussions were delayed till year-end board meetings, which would focus on financial results with little time set aside for directors to robustly discuss accounting treatments; and
- (c) Failing to upskill finance team or engage experts also resulted in directors not being informed of the right accounting implication of certain transactions and hence, did not give those matters an appropriate deliberation.

7 Commenting on the raised level of awareness on the importance of ensuring high quality financial reporting, Mr Kenneth Yap, Chief Executive of ACRA said "It is encouraging to note that many directors of listed companies are making the effort to promptly rectify financial reporting gaps identified by ACRA". Mr Yap also noted that "in this current economic climate, when companies are facing thinning margins and

weaker growth prospects, it is even more critical that financial statements give an accurate picture of the financial standing of the company”.

8 ACRA will publish the areas of review focus for the next FRSP review cycle by December 2016. This will help companies and directors guard against potential misstatements as they prepare the FY2016 Financial Statements.

Driving improvement and collaboration – Continuous review of the FRSP

9 With the experience gained from two review cycles, it is timely for ACRA to undertake a review the FRSP’s policies and processes. Bearing in mind the overarching objective of the FRSP in raising financial reporting quality, the review will take into account market feedback and seek to recalibrate the fine balance between enforcement and collaboration with stakeholders.

10 Commenting on the review of the programme, Mr Yap said “Going forward, ACRA’s main focus will be to ensure that there is timely restatement of financial statements when companies misapply the accounting standards. Investors will in turn benefit from a more informed perspective when making investment decisions”.

11 The FRSP Second Report 2016 is available at www.acra.gov.sg.

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Attachments:

Annex A: Key findings from review of FY2014 Financial Statements

Annex B: Fact Sheet on ACRA’s Financial Reporting Surveillance Programme

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About ACRA

The Accounting and Corporate Regulatory Authority (ACRA) is the national regulator of business entities, public accountants and corporate service providers in Singapore. ACRA also facilitates the development of business entities and the public accountancy profession.

As a regulator and facilitator, ACRA constantly strives to provide a responsive and trusted regulatory environment for businesses, public accountants and corporate service providers and make Singapore the best and trusted place for doing business.

For more information, please visit www.acra.gov.sg.

Key findings from the FY2014 Financial Statements

- A.1 50 sets of FY2014 Financial Statements of listed companies incorporated in Singapore were reviewed in this second review cycle of the FRSP. These financial statements were selected based on the FRSP's risk-based approach. Consistent with last year, enquiries were focused on areas that might significantly impact the key measures used by investors such as revenue, profit and operating cash flows.
- A.2 A good level of quality in financial reporting was observed. The boards took ownership over financial reporting. Many have also stepped up the game in documenting their deliberations on complex accounting matters. However, there is still room for improvement as a number of non-compliances with the accounting standards were identified.
- A.3 The four areas with the highest instances of findings were as follows:
- (a) New consolidation standards;
 - (b) Business acquisitions;
 - (c) Impairment of long-lived assets; and
 - (d) Fair value of properties.

These areas were consistent with the areas of review focus in ACRA's Practice Guidance issued in January 2015 to guide directors in their preparation of the FY2014 Financial Statements.

Root cause analysis

- A.4 Recognising the complexity in the areas of review, more than 30 meetings were held with directors this year to better understand the business rationale and judgements made. During these discussions, three behavioural root causes leading to the findings were observed:

(a) Information asymmetry between business operations and finance function

Information asymmetry between a company's business operations and its finance function can lead to accounting lapses. While accounting should not drive business, it is important to involve the finance team upfront so that they can understand the business rationale of unique arrangements and be alerted to important non-standard contract terms.

We noted instances where the operations team would proceed first to negotiate deals and then handover the signed contracts to the finance team with little explanations for accounting.

(b) Lack of time and process to consider complex accounting matters

Directors, with their deep experience and good understanding of the board's business strategies, are best placed to provide critical scrutiny on the accounting of major complex transactions. At year-end board meeting, the focus of discussion is usually concentrated on the financial results of the company, with little time set aside for directors to consider whether the accounting is appropriate and consistent with their understanding of the business.

It is therefore crucial that directors are given the opportunity and sufficient time to review and deliberate on complex accounting matters. This process should also be conducted upfront when the board is deciding on a deal rather than to wait till the year-end board meeting. It is also important to involve the entire board in such deliberations and not leave them entirely to the audit committee.

(c) Failure to upskill finance team or engage experts

A qualified and experienced finance team is the directors' first line of defence in ensuring reliable financial reporting. Directors should periodically assess the adequacy of the finance team's skills and fill the gap(s). External experts could also be brought in to supplement.

Companies, in the midst of expansion or restructuring, might sometimes find their management neglecting to gear up their finance teams to support the new business or transaction. As a result, the right accounting implications were not highlighted to the boards for consideration.

Restatements to address findings

A.5 For less serious non-compliances, companies are required to rectify in the subsequent year's financial statements. Most (89%) of the findings in the second review cycle were communicated before the companies issued their FY2015 financial statements. Of this, 95% of non-compliances and 63% of areas for improvement were addressed in the FY2015 Financial Statements. A further four non-compliances and one area for improvement were pre-emptively rectified by the companies in the FY2015 Financial Statements, well before their reviews were concluded. The high rectification rate, especially for

those cases with areas for improvement for which corrections are not mandatory, is highly encouraging. It shows that the vast majority of boards of listed companies in Singapore are committed to delivering high quality financial information to investors.

- A.6 For serious non-compliances that led to warning letters, companies are required to restate, re-audit and re-file their past financial statements. Arising from the first review cycle, two companies have restated, one company was exempted from doing so in view of a reverse take-over situation and two are in progress.

Conclusion

Ensuring high quality financial reporting is a collective responsibility. For Singapore to maintain its reputation for trust and its pole position as a leading business and financial centre, it is imperative for all stakeholders in the financial reporting value chain – directors, management, finance teams, auditors, investors, and regulators to work together to raise the bar on financial reporting.

Fact Sheet on the Financial Reporting Surveillance Programme (FRSP)

Background

B.1 ACRA expanded the scope of its FRSP in July 2014 to include (full) reviews of financial statements, including those with ‘clean’ audit reports of listed companies. Previously, the FRSP was focused on (partial) reviews of accounting issues highlighted in modified audit reports⁴ of listed companies.

Directors’ duties over financial reporting

B.2 ACRA administers the Companies Act that applies to companies incorporated in Singapore. Companies incorporated outside Singapore as well as other investment vehicles such as real-estate investment funds and business trusts do not come under ACRA’s purview.

B.3 Through the FRSP, ACRA guides companies to comply with the prescribed accounting standards in Singapore. Only when non-compliances are serious, ACRA enforces directors’ duties under Sections 201(2) and 201(5) of the Companies Act. This enforcement is necessary to ensure that the quality of financial reporting in Singapore is on par with global standards and instil greater confidence in investors.

B.4 Sections 201(2) and 201(5) of the Companies Act require the directors to present and lay at annual general meeting, financial statements that:

- (a) comply with the prescribed accounting standards in Singapore; and
- (b) give a true and fair view of the financial position and financial performance of the company.

The directors must fulfil both conditions in the discharge of their responsibilities under the Companies Act.

Focusing on what matters to investors

B.5 Financial statements are selected for review using a risk-based approach. Enquiries are made to directors when a desktop review of the financial statements indicates a potential significant non-compliance with the accounting standards.

⁴ Modified audit reports refer to those other than true and fair audit opinions. They comprise audit opinions that are qualified, with adverse opinions and disclaimer of opinions.

- B.6 The ultimate goal of the FRSP is to ensure that investors are provided with reliable and meaningful financial statements for their decision-making. As such, ACRA has focused its review and enquiries on areas that might significantly impact the key measures used by investors such as revenue, profit and operating cash flows.

Applying principle-based standards

- B.7 The prescribed accounting standards in Singapore are principle-based accounting standards, which require judgement during their application. It is important that preparers, auditors, users and regulators make the judgement faithfully. If two or more methods are appropriate to achieve the outcome, both methods would be accepted by ACRA. The judgements made should be documented in support of honest and fair attempt to meet the principle(s).

Expert opinions from ISCA-FSRC and FRTAP

- B.8 To benchmark enquiries and findings of the FRSP to expert views and market practices, ACRA collaborated with the Financial Statements Review Committee of the Institute of Singapore Chartered Accountants (ISCA-FSRC) to review all financial statements. Established more than 30 years ago, the ISCA-FSRC comprises more than 20 experienced audit partners from the various audit firms in Singapore, with a majority from the Big-Four audit firms.
- B.9 To ensure that any enforcement decision is undertaken judiciously, complex and/or judgemental serious findings are referred to the Financial Reporting Technical Advisory Panel (FRTAP) for a second independent expert opinion. The FRTAP comprises senior audit partners, directors, chief financial officers, financial controllers and academia of the broader financial reporting community. A review group of five members is drawn from the 20-member FRTAP to deliberate on each case.

Restatements to address findings

- B.10 To ensure investors obtain reliable financial information for their decision-making, companies are required to rectify the misstatements identified through the FRSP. This practice of restatements is in line with those of other leading regulators.
- B.11 Companies are required to rectify all non-compliances in the subsequent year's financial statements. For serious non-compliances that led to sanction, companies may also be required to restate, re-audit and re-file their past financial statements.