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MEDIA RELEASE

RAISING THE QUALITY BAR ON FINANCIAL REPORTING

- Key findings from reviews of companies' financial statements disclosed

Singapore, 1 October 2015 – To ensure financial reporting remains reliable and of high quality, the Accounting and Corporate Regulatory Authority (ACRA) issued today, its inaugural report on key findings on financial statements reviewed under its Financial Reporting Surveillance Programme (FRSP). The outcome revealed that the state of financial reporting by Singapore-incorporated listed companies is generally healthy. However, there is still room for improvement as a number of instances of non-compliance with the Accounting Standards¹ were identified.

Key Findings for Listed Companies

2 The primary objective of the FRSP is to guide companies to meet the requirements in the Accounting Standards so as to provide investors with reliable and meaningful financial statements for decision-making. In July 2014, the scope of the FRSP was expanded to include full reviews of financial statements with 'clean' audit reports. A total of 49 sets of FY2013² Financial Statements of listed companies were reviewed.

3 The reviews focused on areas that might significantly impact key measures used by investors such as revenue, profit and operating cash flow. Many enquiries were made by ACRA in terms of accounting recognition and measurement. Key findings include misclassification of operating cash flow, wrong accounting for mixed-use property, inappropriate consolidation and wrong revenue recognition policy.

4 Through ACRA's engagements with these companies, it was apparent that many audit committees, particularly those from the larger-cap listed companies, exhibited a strong sense of ownership over their companies' financial reporting. Enquiries were addressed comprehensively, with clear explanations given on the commercial substance of transactions and their basis for accepting management's judgements. These directors also reflected a willingness to consider alternative viewpoints.

¹ Accounting Standards refers to the accounting standards issued by the Accounting Standards Council for application by companies incorporated in Singapore. They include the Singapore Financial Reporting Standards.

² Financial year ended between 1 January 2013 and 31 December 2013 (both dates inclusive).

5 ACRA can apply regulatory sanctions ranging from warning letter to financial penalties, depending on the severity and number of non-compliance(s). To date, warning letters were issued to the directors of four listed companies that have significantly misstated the key measures used by investors such as revenue, profits and/or operating cash flows. 54 instances of other non-compliance, of which half were due to a lack of proper disclosures, were also highlighted by ACRA. The bulk of these were communicated via 29 advisory letters and a few, via warning letters. Advisory letters do not carry any regulatory sanction. No prosecutions were undertaken, nor were composition fines imposed, in this review cycle.

6 Encouragingly, the directors took quick action to correct the instances of non-compliance and areas for improvement. Specifically, all instances of non-compliance highlighted to the directors before the finalisation of FY2014³ Financial Statements have been corrected. Similarly, over three quarters of the areas for improvement highlighted to the directors before the finalisation of FY2014³ Financial Statements have also been addressed. This shows a strong commitment on the part of directors to investors, who rely on financial statements for their decision-making.

7 To raise awareness on the expanded FRSP, ACRA has engaged over 1,400 directors and management at various seminars in the past year. ACRA also worked with the Singapore Institute of Directors and the Institute of Singapore Chartered Accountants to develop the Director Financial Reporting Essentials Course. Pitched at the directors' level, the course provides practical tips on how directors could apply rigour in their reviews of financial statements. ACRA will be publishing the FRSP areas of review focus for the FY2015⁴ Financial Statements soon.

8 Commenting on directors' responsibilities, Mr Kenneth Yap, Chief Executive of ACRA said "Directors as company stewards have a statutory responsibility to apply the right accounting standards in financial reporting. It is crucial that they review the financial statements carefully and when necessary, question management's judgements and estimates. They have a duty to provide their stakeholders with an accurate picture of the financial health of the company."

9 Commenting on the findings, Mr Yap said "The findings show that there is still room for improvement. We hope that the observations shared in the report will help directors avoid some common pitfalls and further enhance the quality of financial statements put out by their companies."

10 The inaugural report on the FRSP is available at www.acra.gov.sg.

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Attachments:

Annex A: Fact Sheet on the Financial Reporting Surveillance Programme

Annex B: Key findings on the FY2013 Financial Statements

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

⁴ Financial year ended between 1 January 2015 and 31 December 2015 (both dates inclusive)

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About ACRA

The Accounting and Corporate Regulatory Authority (ACRA) is the national regulator of business entities and public accountants in Singapore. ACRA also plays the role of a facilitator for the development of business entities and the public accountancy profession.

The mission of ACRA is to provide a responsive and trusted regulatory environment for businesses and public accountants. As at 31 August 2015, 476,610 business entities and 1,060 public accountants practising in public accounting firms, accounting limited liability partnerships and accounting corporations are registered with ACRA.

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

Fact Sheet on the Financial Reporting Surveillance Programme (FRSP)

Background

- A.1 In recent years, a growing number of companies have been thrust into the limelight with allegations of accounting irregularities. This has in turn resulted in significant volatility in the share prices of the affected companies. Concurrently, accounting standards are becoming increasingly complex as they evolve in tandem with a challenging and dynamic business environment and complex business models.
- A.2 A higher level of scrutiny is therefore necessary to uphold and maintain investors' and other stakeholders' confidence in the transparency, integrity and quality of financial reporting in Singapore.
- A.3 With this in mind, ACRA expanded the scope of its FRSP in July 2014 to include full reviews of financial statements with 'clean' audit reports of listed companies. Previously, the FRSP was focused on the (partial) reviews of accounting issues highlighted in the modified audit reports⁵ of listed companies.

Directors' duties over financial reporting

- A.4 ACRA administers the Companies Act that applies to companies incorporated in Singapore. Their financial statements lodged with ACRA are selected for review using a risk-based approach. Companies incorporated outside of Singapore as well as non-company entities do not come under ACRA's purview.
- A.5 The FRSP enforces the directors' duties in relation to financial reporting under the Companies Act. Specifically, sections 201(2) and 201(5) of the Companies Act require the directors of a company to present and lay before the company, at its annual general meeting, financial statements that:
- (a) comply with the prescribed Accounting Standards⁶ in Singapore; and
 - (b) give a true and fair view of the profit or loss, and the state of affairs of the company.

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

⁵ 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.

⁶ Accounting Standards refers to the accounting standards issued by the Accounting Standards Council for application by companies incorporated in Singapore. They include the Singapore Financial Reporting Standards.

Focusing on what matters to investors

A.6 The FRSP is primarily focused on the compliance with the Accounting Standards. Enquiries are made to directors when a desktop review of the financial statements indicates a potential non-compliance with the Accounting Standards in areas that might significantly impact the key measures used by investors such as revenue, profit and operating cash flow.

Expert Opinions from the ISCA-FSRC and the FRTAP

A.7 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 most of the financial statements. Established more than 30 years ago, the ISCA-FSRC comprises more than 30 experienced audit partners from the various audit firms in Singapore, with a majority from the Big-Four audit firms⁷.

A.8 To ensure that any serious enforcement decision is undertaken judiciously, so as to not impose unfair prejudice to directors, complex and/or judgemental instances of non-compliance leading to regulatory sanctions 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.

Regulatory outcomes

A.9 ACRA applies the following range of regulatory outcomes, depending on the severity and number of non-compliance(s):

- (a) Closure;
- (b) Advisory;
- (c) Warning;
- (d) Fine by offer of composition; or
- (e) Prosecution leading to fines and/or imprisonment.

A.10 Closure letters and advisory letters do not carry any regulatory sanction. For regulatory sanctions such as warning, composition and prosecution, ACRA interviews directors and takes their statements before imposing such outcomes. It should be noted that ACRA has the right to take regulatory action against auditors in respect of an inappropriate audit opinion, under section 207 of the Companies Act.

A.11. Directors of listed companies who received warning letters must disclose this fact at their appointment or re-appointment as a director under the SGX Listing Rule 704(7) and Appendix 7.4.1. Under the SGX Listing Manual Rule 703(1), the directors of a listed company must also consider whether the regulatory sanction constitutes 'material information' in relation to the company and, if so, an announcement should be made by the listed company.

⁷ Big-Four audit firms comprise Deloitte & Touche, Ernst & Young, KPMG and PwC.

Key Findings on the Listed Companies

- B.1 A total of 49 FY2013 Financial Statements of listed companies were reviewed under the first review cycle under the expanded FRSP. All reviews have been completed, except for two ongoing cases.
- B.2 Generally, a good level of financial reporting quality was noted from the 17 larger-cap listed companies with market capitalisation above S\$1 billion. The higher proportion of non-compliance among the 27 smaller-cap listed companies with market capitalisation below S\$500 million could be due in part to the increased complexity in accounting when the companies scale up and expand operations overseas. It could also be due to their audit committees not spending sufficient time on financial reporting.
- B.3 Collectively, 4 instances of severe non-compliance, 54 instances of other non-compliance and 74 areas for improvement were identified. All instances of non-compliance and areas for improvement were incidences where the financial statements were not compliant with the Accounting Standards, differentiated by the nature and extent of the misstatements.
- B.4 All instances of non-compliance and areas for improvement were communicated via the issuance of closure letters, advisory letters and warning letters. The regulatory outcomes for the completed cases were:

	Listed companies
Warning	4
Advisory	29
Closure	12
Total	45

- B.5 From the findings and interviews with the directors, three root causes of the non-compliances were identified:

(a) Insufficient scrutiny by directors when the reported financials did not accord with their understanding of the business

ACRA observed that some directors did not accord sufficient scrutiny to the financial statements and hence, were unable to discern that the reported financials were inconsistent with their knowledge and understanding of the business.

In one case, the listed company reported a negative operating cash flow, even though its directors were aware that the business was profitable and generating a positive operating cash flow.

In another case, the listed company accounted for the retail component of a mixed-use property as property held for sale, even though its directors were aware of the corporate strategy and business intention to keep the retail component for long-term investment.

(b) Over-reliance on accounting team who may lack competence or diligence

ACRA also observed that some directors depended heavily on management, accounting teams and auditors to ensure there were no accounting breaches. While such reliance is acceptable for basic financial reporting functions, these directors also deferred unreservedly to management's judgements on critical accounting issues. They did not consult further nor obtain additional accounting advice, even when they were uncomfortable with the judgements made by management.

Some directors were also unaware of the instances of non-compliance until highlighted by ACRA. This could be due to a lack of competent and/or adequately-resourced accounting teams.

(c) Independent directors did not adequately challenge management's judgement

There were also instances where management made judgements that were overly aggressive and deviated from the generally accepted accounting practices. The accounting positions were not supported by analyses. There was also a lack of documentary evidence to indicate robust discussion(s) on the issues.

In one case, the listed company recognised the entire revenue and profits on its construction contracts, well before the contracts were substantially completed. The listed company also wrongly presented the unbilled amounts as trade receivables.

In another case, the listed company consolidated a profitable subsidiary, even though the key decisions relating to that subsidiary remained with the seller. By consolidating prematurely, the listed company wrongly portrayed that it had a profitable ongoing business.

B.6 The findings and root causes showed that most of these non-compliances could have been avoided if the directors, even without the benefit of detailed accounting knowledge or professional support, review the financial statements carefully and with rigour.