ACRA-SGX-SID
AUDIT COMMITTEE SEMINAR 2019
[The Audit Committee in the New Normal]

16 January 2019
Marina Mandarin Hotel

ACRA Regulatory Updates

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Agenda

1. Tips to ACs when dealing with:
   - modified audit reports
   - new business arrangements

2. New legislation effective 20 Apr 2018
   - voluntary revision of defective accounts

Modified audit reports

Director's duties for financial reporting

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Shareholders rely on financial statements

s201 of Companies Act - Directors must table financial statements (FS) that are:
- true and fair, and
- comply with the accounting standards

FS should receive "clean" audit report

FS of SG-listed companies

	FY2016	FY2017
Clean opinion	537	516
Modified opinion	40 (7%)	44 (8%)
Total companies	577	560

Areas qualified by auditors
- Opening balance only: 8 (FY2016: 2)
- Going concern only: 6 (FY2016: 2)
- Others: 30 (23 may have accounting issues)

ACs to enquire before changing auditors

ACs could help resolve some issues. See next slides

Case 1 - Changes in views

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FY14	FY15	FY16	FY17
Clean audit opinion	Clean audit opinion	Qualified audit opinion	Clean audit opinion
Loss	Loss	Profit	Loss

Pre-tax losses for 3 consecutive years + <$40m average daily market cap in the past 6 months => placed under "watch list"

Qualified Auditor's Report

"The Group's PPE of $20 million, included equipment not in use of about $2 million. We were unable to obtain sufficient appropriate audit evidence on key assumptions used"

Notes to the FS

"The management is confident that … will be able to fully utilise the PPE including those currently not in use."

Restated the comparative by impairing PPE of $2 million

".. The plant and equipment was not in use since 2016 and should have been impaired in 2016…"

Current year impairment of PPE of $11 million

Key assumption used:

- Gross margin: 12% (FY16: 20%)

Tip #1 - Critically assess before accepting changes in views

Tip #2 – Evaluate if impairment should be recognised in FY16?

Case 2 - Rectify timely

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Disclaimer — FY15

Qualified opinion — FY16

2months later — Q1'FY17

Qualified opinion — FY17

FY16

Net Assets = $2.1m

Q1'FY17

FY16 (restated) Net Liabilities = ($2.1m)

FY17

FY16 (restated) Net Assets = $3.1m

FY15

Auditor's Report
Due to 2 areas

FY16

Auditor's Report
3rd area qualified - "A subsidiary did not translate its PPE into the Group's presentation currency using the closing rate as required by FRS 21.

Had it been translated, net assets would decrease by $4.2m…"

Net Liabilities ($2.1m)

Q1'FY17

Announcement
"The restatement of the Company's …. followed an adoption of audit opinion…"

Tip #1 – Rectify in FS as far as possible

Tip #2 – Why error not identified last year?

Tip #3 – Analyse the root cause

FY17

Notes to FS
"During the financial year, the Group raised prior year adjustments for correction of the below error: .. The changes in fair values of the interest-free loans in relation to the changes in time to maturity were also not accounted ….".

Auditor's Report
4 areas were qualified (of which 2 were from FY15).

New business arrangements

Case 3 - Evidence on change in use (1)

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Fact Pattern

Type of Property	Business model	FS Classification	Measurement
Residential only and residential-commercial developments	Sell 	Development Property	Cost
Industrial properties	Rent 	Investment Property (IP)	Fair value
Industrial properties	Own use	Property, Plant and Equipment	Cost

Accounting Requirements

(Para 57 of SFRS 40)

- An entity shall transfer a property to, or from, IP when, and only when, there is a change in use.
- A change in use occurs when the property meets, or ceases to meet, the definition of IP and there is evidence of the change in use.
- In isolation, a change in management's intention for the use of the property does NOT provide evidence of a change in use.

Case 3 - Evidence on change in use (2)

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Fact Pattern

Property under construction

8-storey industrial building

1 Jan — 30 Sept — (3 months) — 31 Dec

Own use (PPE at cost) → **Sell** (Development property at cost) → **Rent/Capital appreciation** (Investment property at fair value)

Tip #2 – Be comfortable with reasons for multiple transfers in a short period of time

Tip #1 – Ask CFO for the alternative accounting treatment

Had it been transferred directly from PPE to IP, fair value gain taken to <u>EQUITY</u>

Fair Value Gain (~50% of PBT)

Case 3 - Evidence on change in use (3)

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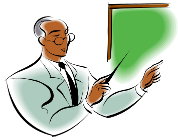

Company's evidence on change in use

- Management meeting in Sept attended by executive directors, the CFO and the Finance Manager:
  (i) One director suggested selling the property under construction for better cash flow management.
  (ii) The management decided that if the sale was unsuccessful in 3 months, the property will be held for rental income.

- 2 emails with sale agents provided by management as evidence on the efforts to sell:

  (i) *"…**Is it for sale or lease?** If sale, what is the price and if leasing what is the rate?"*

  (ii) *"…We can* consider *to sell…**can your buyer sign the NDA before we release information** e.g. valuation report etc…"*

Tip #3 – Distinguish between change in intention and change in use

Tip #4 – Assess evidence on the change in use (e.g. under construction, able to sell in 3 months)?

Voluntary Revision of Defective FS

Voluntary Revision of Defective FS (1)

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20 Apr '18

Issued Regulations to operationalise s202A and s202B of Companies Act

Purpose: Allow diligent directors to revise the company's FS on their own[1]

Can revise in respect of any financial year, but

revisions are confined to non-compliances with Companies Act

No need to deal with subsequent events or changes in Accounting Standards

New directors' statement and amended auditor's report (illustrated in the Guidance)

No need to call for AGM/EGM to table revised FS (table at the next AGM/EGM), but

must circulate to members and file with ACRA within 30 days after revision

20 Apr '18

Issued Guidance for Companies[2] (available at www.acra.gov.sg)

1 Intent of the Steering Committee appointed by MOF to review the Companies Act then.

2 Consulted with ISCA's Financial Statements Review Committee and ISCA's Auditing and Assurance Standards Committee.

Voluntary Revision of Defective FS (2)

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Assume that directors authorised FY2016 FS on 31 Mar 2017 and revised it on 20 Nov 2018.
Extract of new Directors' Statement:

This new directors' statement replaces the original directors' statement signed on 31 March 2017. This new directors' statement and the revised Financial Statements have been prepared in accordance with Companies (Revision of Defective Financial Statements, or Consolidated Financial Statements or Balance-Sheet) Regulations 2018. [Regulations 6(2)(b) and (c)]

The bases for revisions are explained in Note 2 to the revised financial statements. This new directors' statement is taken as having been prepared on the date of the original directors' statement and accordingly, does not consider those events occurring between 1 April 2017 and 20 November 2018. [Regulation 6(2)(d)]

No need to update for subsequent events

Voluntary Revision of Defective FS (3)

In the opinion of the directors,

New opinion by directors in office at date of revision

(a) the revised balance sheet of the Company and the revised consolidated financial statements of the Group are drawn up so as to give a true and fair view of the financial position of the Company and of the Group as at 31 December 2016 and the financial performance, changes in equity and cash flows of the Group for the financial year covered by the original consolidated financial statements [Regulation 4(2)(c)(ii)(A)]; and

(b) as at the date of the original directors' statement (31 March 2017), there were reasonable grounds to believe that the Company would be able to pay its debts as and when they fell due. [Regulation 4(2)(c)(ii)(B)]

Opinion of directors in office at date of original FS

[Name of Director 1]
Director [Regulation 4(2)(c)(i)]
20 November 2018 [Regulation 6(2)(a)]

Date of revision

[Name of Director 3]
Director [Regulation 4(2)(c)(i)]

Voluntary Revision of Defective FS (4)

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Made adjustment to FY2016 comparatives in FY2017 FS

30 Apr 2018

1 Feb 2018

Noted an error in FY2016 FS when preparing FY2017 FS

Should the Co voluntarily revise its FY2016 FS under section 202A as well?

As a minimum, directors to consider the following factors, when deciding whether to voluntarily revise its FY2016 FS:

(a) nature and materiality of errors (both quantitatively and qualitatively) in FY2016 FS
(b) level of public interest in FY2016 FS
(c) likelihood of users relying on the defective FY2016 FS that is available in the public domain (SGXNET and ACRA's register)

Thank You!