FP

Chartered Accountant
SINGAPORE

Singapore CA Qualification (Foundation) Examination

16 June 2020

Advanced Financial Reporting

INSTRUCTIONS TO CANDIDATES:

1. The time allowed for this examination paper is **3 hours 15 minutes**.

2. This examination paper has **FOUR (4)** questions and comprises **FORTY-THREE (43)** pages (including this instruction sheet, Appendix A and Appendix B). Each question may have **MULTIPLE** parts and **ALL** questions are examinable.

3. This is a restricted open book examination. You are allowed to have only the following materials with you at your exam location:

   - One A4-sized double-sided cheat sheet
   - One A4-sized double-sided blank scratch paper

4. During the examination, you are allowed to use your laptop and any calculators that comply with the SAC's regulations. Please note that watches, mobile phones, tablets, and all other electronic devices **MUST NOT** be used during the examination and **MUST NOT** be within reach or sight or hearing from where you are seated to write the exam. Use of these devices, or, the sight or hearing of these devices, will be flagged as integrity breaches and investigated, unless it is for the purpose as stated under paragraph 6 below.

5. During the examination, videos of you and your computer screen will be recorded for the purpose of ensuring examination integrity and you have consented to these recordings.

6. Should you encounter any issues during the examination, please contact any of these four (4) hotlines for an invigilator to assist you. The hotlines will be operational from one hour before the scheduled start time of the examination to one hour after the scheduled end time of the examination.

Name of invigilator	Hotline number
N.A.	N.A.
N.A.	N.A.
N.A.	N.A.
N.A.	N.A.

7. This examination paper and all video recordings of this exam are the property of the Singapore Accountancy Commission.

ISCA INSTITUTE OF SINGAPORE CHARTERED ACCOUNTANTS

SINGAPORE ACCOUNTANCY COMMISSION

MODULE-SPECIFIC INSTRUCTIONS:

8. Assume that all dollar amounts are in Singapore dollar (S$) unless otherwise stated.

9. Unless specified otherwise, assume that all the reporting entities in all the questions adopt, for all the relevant years, the Singapore Financial Reporting Standards (International) (SFRS(I)) that were issued by the Accounting Standards Council as at 1 January 2020.

Examplify Question Number	Compulsory pre-exam steps to be recorded in video
1	Before you begin this exam, you are to perform a 360 degrees environment scan (via webcam), including a view of your table top, so that the location where you are taking the exam is being recorded in the video.

Next, show each side of your A4-sized double-sided cheat sheet to the webcam so that your cheat sheet is being recorded in the video.

Lastly, if you are using a calculator and a blank sheet of A4-sized scratch paper, show the calculator and both sides of the blank scratch paper to the webcam so that these items will be recorded in the video.

Should you encounter any issues during the examination, please contact any of these four (4) hotlines for an invigilator to assist you.

Name of invigilator	Hotline number
N.A.	N.A.
N.A.	N.A.
N.A.	N.A.
N.A.	N.A.

Question 1 – (a), (b) and (c)

Hilcom Pte Ltd (Hilcom) acquired 80% of Sinocom Pte Ltd (Sinocom) on 1 January 20x2 and 40% of Aircom Pte Ltd (Aircom) on 1 January 20x5. The following are the summarised financial statements of the respective companies:

Statement of Comprehensive Income

For the financial year ended 31 December 20x9

	Hilcom	**Sinocom**	**Aircom**
	$'m	***$'m***	***$'m***
Sales	67,845	72,411	17,268
Cost of sales	(10,555)	(36,772)	(12,476)
Gross profit	**57,290**	**35,639**	**4,792**
Other income	979	3,464	258
Operating expenses	(54,203)	(40,491)	(2,240)
Interest expenses	0	(20)	(10)
Profit/(Loss) before tax	**4,066**	**(1,408)**	**2,800**
Tax expense	(690)	(152)	(480)
Profit/(Loss) after tax	3,376	(1,560)	2,320
Other comprehensive income/(loss)	(130)	420	640
Total comprehensive income/(loss)	**3,246**	**(1,140)**	**2,960**

Statement of Financial Position

As at 31 December 20x9

	Hilcom	Sinocom	Aircom
	$'m	***$'m***	***$'m***
Non-current Assets			
Property, plant and equipment	9,157	7,835	2,855
Investment in Sinocom Pte Ltd (at cost)	10,490	0	0
Investment in Aircom Pte Ltd (at cost)	4,128	0	0
Financial assets measured at fair value through other comprehensive income	1,805	3,725	6,430
	25,580	11,560	9,285
Current Assets			
Inventories	682	8,196	650
Trade and other receivables	2,510	4,200	2,160
Cash and cash equivalents	20,551	14,704	10,810
	23,743	27,100	13,620
Total Assets	**49,323**	**38,660**	**22,905**
Equity			
Share capital	9,522	4,100	6,500
Fair value reserves	321	3,450	4,200
Retained earnings	32,593	21,550	9,610
	42,436	29,100	20,310

Current Liabilities

Trade and other payables	5,356	9,020	1,710
Provision for tax	1,531	540	885
	6,887	9,560	2,595
Total Equity and Liabilities	**49,323**	**38,660**	**22,905**

Statement of Changes in Equity (extract)

For the financial year ended 31 December 20x9

	Hilcom		Sinocom		Aircom	
	Fair value reserves ***$'m***	**Retained earnings** ***$'m***	**Fair value reserves** ***$'m***	**Retained earnings** ***$'m***	**Fair value reserves** ***$'m***	**Retained earnings** ***$'m***
Balance as at 1 January 20x9	451	29,892	3,030	23,650	3,560	7,770
Total comprehensive income	(130)	3,376	420	(1,560)	640	2,320
Dividend paid	-	(675)	-	(540)	-	(480)
Balance as at 31 December 20x9	**321**	**32,593**	**3,450**	**21,550**	**4,200**	**9,610**

Additional information:

1. The Group, consisting of Hilcom and Sinocom, adopts the proportionate share of the fair value of the subsidiaries' identifiable net assets in measuring any non-controlling interest.

2. Ignore all income tax and deferred tax effects, if any, arising from business combinations.

3. There has been no change in the share capital of all the above companies since the respective acquisition dates.

4. Other income consists of dividend income, interest income, gain on disposal of property, plant and equipment and other miscellaneous income.

5. When Hilcom acquired Sinocom on 1 January 20x2:

    - The amount of Sinocom's fair value reserve and retained earnings were $870m and $4,750m respectively.

    - The net book value of Sinocom's warehouse exceeded its fair value by $500m. As at that date, the remaining useful life of the warehouse was 25 years. The warehouse is still held by Sinocom as at 31 December 20x9.

    - The fair value of Sinocom's inventories exceeded the carrying amount by $20m, and the relevant inventories were sold during the financial year ended 31 December 20x2.

6. On 1 January 20x9, Sinocom sold an office building, with a carrying amount of $750m to Hilcom at a gain of $240m, and the remaining useful life as at that date was 24 years. As at 31 December 20x9, Sinocom had settled half of the amount outstanding arising from the sale, and the office building was still held and used by Hilcom as at 31 December 20x9.

7. On 1 October 20x9, Hilcom advanced a short-term loan of $1,500m to Sinocom at 4% per annum. As at 31 December 20x9, the interest owing from Sinocom to Hilcom was fully settled but loan amount remained unpaid.

8. When Hilcom purchased its stake in Aircom on 1 January 20x5, the value of Aircom's fair value reserves and retained earnings were at $420m and $3,100m respectively, while the fair value of Aircom's manufacturing plant exceeded its net book value by $300m. Remaining useful life of the plant was 10 years as at acquisition date.

9. Assume that a shareholding of more than 50% gives rise to control, while a shareholding between 20% and 50% gives rise to significant influence.

10. The Group adopts the cost model and straight-line method to depreciate its property, plant and equipment, and records depreciation as an operating expense. Assume that the residual value of its property, plant and equipment is zero.

Examplify Question Number	**Question 1 required:**
	Apply Singapore Financial Reporting Standard (International) (SFRS(I)) 3 *Business Combinations*, SFRS(I) 10 *Consolidated Financial Statements* and SFRS(I) 1-28 *Investments in Associates and Joint Ventures* when answering **(a)** and **(b)**:
2	**(a)** Prepare the relevant consolidation and equity accounting entries for Hilcom Pte Ltd Group for the financial year ended 31 December 20x9. Show the consolidation and equity accounting entries for the current financial year separately from those relating to the prior years.

Present your answers in the following format:	
Transaction date	
DR Account Name	xxx
CR Account Name	xxx
(Narration for Journal Entry)	

(28 marks)

3	**(b)** In relation to the Consolidated Statement of Financial Position as at 31 December 20x9, provide independent proof for Retained Earnings. **(6 marks)**

Examplify Question Number

4

(c) During a monthly departmental meeting, the accountant of Hilcom Pte Ltd proposed not to prepare the consolidated financial statements for the Group for statutory financial reporting purposes, since Management assessed performance and allocated resources by reviewing the individual financial statements of the companies in the Group and not the consolidated financial statements. With reference to the SFRS(I) 10 *Consolidated Financial Statements*, advise Management of the requirements for Hilcom Pte Ltd to be exempted from preparing consolidated financial statements.

(4 marks)

(Total: 38 marks)

Question 2 – Part I and Part II

Part I

Futuristic Pte Ltd (Futuristic), a software engineering company, has a financial year-end of 31 December. The following shows the intangible assets and their relevant information:

Intangible assets	Patent	Customer list
Date acquired	30 June 20x7	1 August 20x8
Amortisation method	Straight-line	Double declining
Residual value	Nil	Nil
Useful life	5	3
Cost ($'000)	5,950	2,450

Examplify Question Number	**Question 2 Part I required:**
	Apply SFRS(I) 1-38 *Intangible Assets* when answering the following:
5	**(a)** Compute the amortisation expenses for the financial year ended 31 December 20x9 of each of the above individual intangible assets and each of their carrying amounts as at 31 December 20x9. Show your workings clearly and round off your answers to the nearest thousand. **(5 marks)**

Part II

For the financial year ended 31 December 20x9, Futuristic Pte Ltd (Futuristic) commenced work on a prototype of a new product as follows:

20x9	Events and Expenditures
January to March	• Market surveying costs of $120,000 to source for customer requirements. • Technical research fees of $530,000 to assess possibilities of new product incorporating customer preferences.
April to June	• Prototype development fees of $670,000.
July to September	• Design and trial fees of $250,000 to test the functions of the prototype for July and August. • On 1 September, prototype development was completed, and Management estimated that their own engineers would take less than 6 months to finalise the product and announced to launch the new product in the 1st quarter of the following year. Based on the earlier market research done, Management is confident to capture 50% of the existing market share with this new product.
October to December	• Purchased equipment for $1,380,000 for prototype development. • Incurred engineers' monthly salaries of $60,000 from September to December to perfect the designs and functions of the prototypes in preparation for the product launch.

Examplify Question Number	Question 2 Part II required:
	Apply SFRS(I) 1-38 *Intangible Assets* when answering the following:
6	**(a)** From the list of events and expenditures that took place during the financial year ended 31 December 20x9, explain briefly if each of the expenditures relating to the prototype should be capitalised or expensed off in profit or loss. **(11 marks)** **(Total: 16 marks)**

Question 3 – Part I and Part II

Part I

Verizon Ltd (Verizon), with a financial year end of 31 December, granted 12,000 employee share options to each of its 200 employees, with an exercise price of $26 on 1 January 20x5. The vesting date of these options is on 31 December 20x7 whereas their expiry date is on 31 December 20x9. The options would be forfeited if the employee leaves before the vesting date.

The fair value of each option was estimated as follows:

1 January 20x5: $11.20
31 December 20x5: $9.75
31 December 20x6: $10.30
31 December 20x7: $10.15

In 20x5, a few employees left Verizon. As at 31 December 20x5, Management estimated the forfeiture rate to be 10% of the 200 employees.

In 20x6, more employees left Verizon. As at 31 December 20x6, Management updated the estimated forfeiture rate to be 20% of the 200 employees.

On 1 January 20x7, Management revised the exercise price of the share option to $22. As a result of this modification, the fair value of the modified option was estimated to be $11.50.

As at 31 December 20x7, 170 out of the 200 employees remained in the company.

On 30 June 20x8, the share price of Verizon was $26 and 40% of the 170 employees exercised all the share options granted to them.

On 1 March 20x9, the share price of Verizon rose to $27.50, and all the remaining options were exercised.

Examplify Question Number	Question 3 Part I required:
7	**(a)** Prepare the journal entries for the financial years ended 31 December 20x5 to 20x9 in accordance with SFRS(I) 2 *Share-based Payment*. Ignore the tax effect, if any.

Present your answers in the following format:	
Transaction date	
DR Account Name	xxx
CR Account Name	xxx
(Narration for Journal Entry)	

(18 marks)

Part II

Verizon Ltd (Verizon) is a local company listed on the Singapore Exchange. On 1 February 20x9, the Accountant (who is a member of the Institute of Singapore Chartered Accountants) of Verizon, came across an invoice issued by a law firm, billing the company for legal advice rendered in January 20x9. After investigation, the Accountant found out the legal advice was sought because a customer had filed a lawsuit against Verizon in December 20x8. Based on the attached documentation, it was assessed that there is a 50% probability of Verizon having to pay damages of $1 million.

The Accountant approached the Finance Manager to discuss if there is a need to record a provision for the legal damages for the financial year ended 31 December 20x8. The Finance Manager initially responded, “Let’s be optimistic. The customer may NOT win the case, and the probability is 50% anyway. If we win the case, then we would have to reverse the provision again. Don’t think too much about it.”

The Accountant reiterated the requirements of SFRS(I) 1-37 *Provisions, Contingent Liabilities and Contingent Assets* to the Finance Manager. The Finance Manager explained, “I am aware of the financial reporting requirements. However, if we were to record this provision, the company might breach the loan covenant for the year. Our gearing would be adversely affected, and the company will report a loss for the year! This would affect our overseas expansion plan, and worst of all, it could affect our company’s cash flows. Who knows? All of us may not get our bonus this year! Let’s do everyone a favour then!”

Examplify Question Number	Question 3 Part II required:
	With reference to Ethics Pronouncement (EP) 100 the *ISCA Code of Professional Conduct and Ethics*:
8	**(a)** Identify and explain ONE fundamental principle which is being threatened from the perspective of the Accountant. **(3 marks)**
9	**(b)** Describe ONE threat that could compromise, or be perceived to compromise, the Accountant's compliance with the fundamental principle identified in **(a)** above. **(3 marks)**
10	**(c)(i)** Identify TWO relevant stakeholders and explain how they could be affected if the Accountant were to follow the instructions of the Finance Manager and; **(3 marks)**
	(c)(ii) Recommend ONE appropriate action that the Accountant could take to eliminate or reduce the threat to the fundamental principle identified in **(b)** above. **(2 marks)**
	(Total: 29 marks)

Question 4 – Part I and Part II

Part I

Comfy Home Pte Ltd (Comfy Home), a residential property developer company, entered into an agreement on 1 January 20x7 to take on a three-year project to construct a residential building for a contract price of $12 million. Based on the terms and conditions of the sales and purchase agreement, Comfy Home would be deemed to have breached the contract if it decides to sell the property to another buyer, and would result in a penalty of 50% of the contract price payable to the customer. According to the terms of the contract, Comfy Home would bill the customer per the schedule of progress billings on specific dates, and it has the right to enforce payment by the customer for the construction work performed to-date.

Management concluded that the revenue for this construction contract should be recognised over time and records the revenue using the percentage-of-completion method, using the proportion of costs incurred to-date in relation to the estimated total costs of the contract to determine the percentage of completion.

Relevant data extracted from the construction records for both financial years ended 31 December 20x7 and 20x8 are as follows:

For the financial year ended 31 December	**20x7 ($'000)**	**20x8 ($'000)**
Costs incurred to-date	2,430	6,560
Estimated costs to complete	6,520	3,090
Billings to-date	3,300	7,530
Cash collected to-date	1,830	6,880

Examplify Question Number	**Question 4 Part I required:**
	Apply SFRS(I) 15 *Revenue from Contracts with Customers* when answering the following:
11	**(a)** Prepare the journal entries for the financial year ended 31 December 20x8. Express your answers to the nearest thousand. Ignore the tax effect including Goods and Services Tax, if any.

Present your answers in the following format:

Transaction date

DR Account Name xxx

CR Account Name xxx

(Narration for Journal Entry)

(8 marks)

Part II

The following shows the shareholding of Comfy Home Pte Ltd (Comfy Home):

Shareholders	Percentage (%) of Shareholding
Lam Chong Ltd	60
William Shen	15
Wilson Shen	10
Thomas Young	15

William Shen is the Finance Director of Comfy Home. His son, Wilson Shen, is the Finance Manager of the company. Thomas Young is a long-time business partner of William Shen.

In the last financial year, Comfy Home also acquired 80% of the shareholding in Global Ventures Pte Ltd (Global Ventures), which in turn held 30% of the shareholding in Wembley Pte Ltd (Wembley).

For the financial year ended 31 December 20x9,

- Besides his monthly salary and annual bonus, the compensation package of William Shen includes the share appreciation rights issued by Lam Chong Ltd.
- In view of the succession plans of William Shen who is due to retire in the following year, Comfy Home sponsored Wilson Shen for the part-time Masters in Business Administration programme so that he could take over William's role upon completion of the programme.
- In order for Global Ventures to obtain a loan from National Bank, Comfy Home had agreed to be the guarantor for the loan.

The shares held in these companies carry voting rights at the general meetings of the companies, where a shareholding of more than 50% gives rise to control and a shareholding of 20% to 50% gives rise to significant influence.

Examplify Question Number	**Question 4 Part II required:**
	Apply SFRS(I) 1-24 *Related Party Disclosures* when answering the following:
12	**(a)** For the financial year ended 31 December 20x9, explain if the following companies and individuals are related parties of Comfy Home Pte Ltd: **(i)** William Shen **(ii)** Wilson Shen **(iii)** Thomas Young **(iv)** Lam Chong Ltd **(v)** Global Ventures Pte Ltd **(vi)** Wembley Pte Ltd **(5 marks)**
13	**(b)** State the items and relationships that require disclosure in the financial statements of Comfy Home Pte Ltd for the financial year ended 31 December 20x9. **(4 marks)** **(Total: 17 marks)**

END OF PAPER

Appendix A

Standardised Common Content Reference Material

Advanced Financial Reporting

(For Jun 2020 Exam, last updated: 20 May 2020)

Important notes

1. This Standardised Common Content Reference Material (Reference Material) was first published on the SAC website on 4 May 2020.

2. The Reference Material was updated and published on SAC website on:

    - 20 May 2020 - Principle of Objectivity

3. The latest Reference Material will be incorporated into the examination question paper as an Appendix, and will be uploaded within your Exam in the e-exam software, Examplify.

Recognition, Measurement, and Reporting of Assets and Liabilities

SFRS(I) 1-36 *Impairment of assets*

Irrespective of whether there is any indication of impairment, an entity shall assess at the end of each reporting period:

(a) test an intangible asset with an indefinite useful life or an intangible asset not yet available for use for impairment annually by comparing its carrying amount with its recoverable amount
(b) test goodwill acquired in a business combination for impairment annually

Recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs of disposal and its value in use.

SFRS(I) 15 *Revenue from Contracts with customers*

- Combination of contracts (excluding Construction Contracts);
- Unbundling of physical and service elements; and
- Deferred, variable (SFRS(I) 15), and contingent consideration (SFRS(I) 3)

Revenue Recognition – Application of Revenue from Contracts with Customers

Step 1: Identify the contract(s) with a customer
Step 2: Identify the performance obligations in the contract

Step 3: Determine the transaction price
Step 4: Allocate the transaction price to the performance obligations in the contract
Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

SFRS(I) 1-38 *Intangible assets*

- Internally generated goodwill is within the scope but is not recognised as an asset because it is not an identifiable resource.
- Expenditure for an intangible item is recognised as an expense, unless the item meets the definition of an intangible asset, and:
- It is probable that there will be future economic benefits from the asset; and
- The cost of the asset can be reliably measured.
- The costs of generating other internally generated intangible assets are classified into a research phase and a development phase. Research expenditure is recognised as an expense. Development expenditure that meets specified criteria is recognised as an intangible asset.

    - Research phase: No intangible asset arising from research (or from the research phase of an internal project) shall be recognised. Expenditure on research (or on the research phase of an internal project) shall be recognised as an expense when it is incurred.
    - Development phase: An intangible asset arising from development (or from the development phase of an internal project) shall be recognised if, and only if, an entity can demonstrate all of the following:

        (a) the technical feasibility of completing the intangible asset so that it will be available for use or sale.
        (b) its intention to complete the intangible asset and use or sell it.
        (c) its ability to use or sell the intangible asset.
        (d) how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
        (e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.
        (f) its ability to measure reliably.

- Intangible assets are measured initially at cost.
- An intangible asset with a finite useful life is amortised.
- An intangible asset with an indefinite useful life is not amortised but is tested annually for impairment.
- When an intangible asset is disposed of, the gain or loss on disposal is included in profit or loss.

SFRS(I) 5 *Non-current Assets Held for Sale and Discontinued Operations*

A non-current asset must be classified as held for sale if most of its carrying amount is expected to be recovered via future cash flows from the sale of the asset rather than future cash flows from use. To classify an asset as held for sale, the asset or disposal group must be available for immediate sale in its present condition and the sale must be highly probable. IFRS 5 sets out criteria for the sale to be highly probable:

- Management must be committed to a plan to sell the asset;
- An active program to find a buyer must be initiated;
- The asset must be actively marketed for sale at a price that is reasonable to its current fair value;
- The sale must be completed within one year from the date of classification;
- Significant changes to be made to the plan must be unlikely.

A discontinued operation is a component of an entity that has been disposed of or is classified as held for sale, and:

- Represents a separate major line of business or geographical area of operations,
- Is part of a plan to dispose of, or
- Is a subsidiary acquired solely with a view to resale.

Discontinued operations are to be presented as follows:

1. In the statement of profit and loss and other comprehensive income: a single amount comprising the total of:
    - The post-tax profit or loss of the discontinued operation,
    - The post-tax gain or loss recognised on the measurement to fair value less costs to sell, and
    - The post-tax gain or loss recognised on the disposal of assets or the disposal group making up the discontinued operation.

    The analysis of the single amount can be presented in the notes or on the face of the statement of profit or loss and other comprehensive income.

2. In the statement of cash flows: the net cash flow attributable to the operating, investing and financing activities of discontinued operations.

3. In the statement of financial position: non-current assets of a disposal group must be presented separately from other assets. The same applies for liabilities of a disposal group classified as held for sale.

Financial Assets and Financial Liabilities

<u>SFRS(I) 7 *Financial Instruments: Disclosures*</u>

- For presentation, financial instruments are classified into financial assets, financial liabilities and equity instruments. Differentiation between a financial liability and equity depends on whether there is an obligation to deliver cash (or some other financial asset).
- A compound financial instrument, such as a convertible note, is split into equity and liability components. When the instrument is issued, the equity component is measured as the difference between the fair value of the compound instrument and the fair value of the liability component.
- Financial assets and financial liabilities are offset only when the entity has a legally enforceable right to set off the recognised amounts, and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.
- Classification of a financial instrument as a financial liability or equity determines the treatment of the interest, dividends, losses or gains on the financial instrument as items of income or expense, or as changes in equity. Dividends on shares classified as liabilities are recognised as expenses and affect profit or loss.

<u>SFRS(I) 9 *Financial Instruments*</u>

- Fair value hedge: a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or a component of any such item, that is attributable to a particular risk and could affect profit or loss. As long as a fair value hedge meets the qualifying criteria, the hedging relationship shall be accounted for as follows:

  (a) the gain or loss on the hedging instrument shall be recognised in profit or loss (or other comprehensive income, if the hedging instrument hedges an equity instrument for which an entity has elected to present changes in fair value in other comprehensive income).

  (b) the hedging gain or loss on the hedged item shall adjust the carrying amount of the hedged item (if applicable) and be recognised in profit or loss. If the hedged item is a financial asset (or a component thereof) that is measured at fair value through other comprehensive income, the hedging gain or loss on the hedged item shall be recognised in profit or loss. However, if the hedged item is an equity instrument for which an entity has elected to present changes in fair value in other comprehensive income, those amounts shall remain in other comprehensive income. When a hedged item is an unrecognised firm commitment (or a component thereof), the cumulative change in the fair value of the hedged item subsequent to its designation is recognised as an asset or a liability with a corresponding gain or loss recognised in profit or loss.

- Cash flow hedge: a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with all, or a component of, a recognised asset or liability (such as all or some future interest payments on variable-rate debt) or a highly probable forecast transaction, and could affect profit or loss. As long as a cash flow hedge meets the qualifying criteria, the hedging relationship shall be accounted for as follows:

  (a) the separate component of equity associated with the hedged item (cash flow hedge reserve) is adjusted to the lower of the following (in absolute amounts):
      (i) the cumulative gain or loss on the hedging instrument from inception of the hedge; and
      (ii) the cumulative change in fair value (present value) of the hedged item (i.e. the present value of the cumulative change in the hedged expected future cash flows) from inception of the hedge.

  (b) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge (i.e. the portion that is offset by the change in the cash flow hedge reserve calculated in accordance with (a)) shall be recognised in other comprehensive income.

  (c) any remaining gain or loss on the hedging instrument (or any gain or loss required to balance the change in the cash flow hedge reserve calculated in accordance with (a) is hedge ineffectiveness that shall be recognised in profit or loss.

  (d) the amount that has been accumulated in the cash flow hedge reserve in accordance with (a) shall be accounted for as follows:

      (i) if a hedged forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, or a hedged forecast transaction for a non-financial asset or a non-financial liability becomes a firm commitment for which fair value hedge accounting is applied, the entity shall remove that amount from the cash flow hedge reserve and include it directly in the initial cost or other carrying amount of the asset or the liability. This is not a reclassification adjustment and hence it does not affect other comprehensive income.
      (ii) for cash flow hedges other than those covered by (i), that amount shall be reclassified from the cash flow hedge reserve to profit or loss as a reclassification adjustment in the same period or periods during which the hedged expected future cash flows affect profit or loss (for example, in the periods that interest income or interest expense is recognised or when a forecast sale occurs).
      (iii) however, if that amount is a loss and an entity expects that all or a portion of that loss will not be recovered in one or more future periods, it shall

immediately reclassify the amount that is not expected to be recovered into profit or loss as a reclassification adjustment.

- Hedge of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, shall be accounted for similarly to cash flow hedges:

  (a) the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognised in other comprehensive income; and
  (b) the ineffective portion shall be recognised in profit or loss.

  The cumulative gain or loss on the hedging instrument relating to the effective portion of the hedge that has been accumulated in the foreign currency translation reserve shall be reclassified from equity to profit or loss as a reclassification adjustment on the disposal or partial disposal of the foreign operation.

SFRS(I) 13 *Fair Value Measurement*

Three-level framework classifying fair value measurements based upon “inputs,” the assumptions that would be used by market participants when pricing the item being measured. Inputs can be either:
1. Observable,
2. Based on data that is readily available, or
3. Unobservable, based on assumptions by management.

SFRS(I) 1-32 *Financial Instruments: Presentation*

- For presentation, financial instruments are classified into financial assets, financial liabilities and equity instruments.
- Differentiation between a financial liability and equity depends on whether there is an obligation to deliver cash (or some other financial asset).
- A compound financial instrument, such as a convertible note, is split into equity and liability components. When the instrument is issued, the equity component is measured as the difference between the fair value of the compound instrument and the fair value of the liability component.
- Financial assets and financial liabilities are offset only when the entity has a legally enforceable right to set off the recognised amounts, and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.
- Classification of a financial instrument as a financial liability or equity determines the treatment of the interest, dividends, losses or gains on the financial instrument as items of income or expense, or as changes in equity.

Dividends on shares classified as liabilities are recognised as expenses and affect profit or loss.

SFRS(I) 2 *Share-based Payment*

An entity is required to recognise share-based payment transactions in its financial statements. Equity-settled share-based payment transactions are generally those in which shares, share options or other equity instruments are granted to employees or other parties in return for goods or services.

Cash-settled share-based payment transactions are generally those to be settled in cash or other assets. They are share-based because the payment amount is based on the price of the entity's shares.

The share-based payment transaction is recognised when the entity obtains the goods or services. Goods or services received are recognised as assets or expenses as appropriate. The transaction is recognised as equity (if equity-settled) or as a liability (if cash-settled).

Equity-settled share-based payment transactions are measured at the fair value of the goods or services received. If the fair value of the goods or services cannot be estimated reliably, the fair value of the equity instruments at grant date is used.

- In the case of employee and similar services, it is difficult to estimate reliably the fair value of additional benefits received by the entity, so the fair value of the equity instruments measured at grant date is used instead.
- In other cases, there is a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. If not, the fair value of the equity instruments is used instead. If the identifiable consideration received is less than the fair value of the equity instruments granted or the liability incurred, the unidentifiable goods or services are measured by reference to the difference between the fair value of the equity instruments granted (or liability incurred) and the fair value of the identifiable goods or services received at grant date. In other cases, the fair value is measured at the date the entity obtains the goods and services.

Cash-settled share-based payments are measured at the fair value of the liability. The liability is remeasured at the end of the reporting period and at the date of settlement. Changes in value are recognised in profit or loss.

In some cases, the entity or the other party may choose whether the transaction is settled in cash or by issuing equity instruments. The accounting treatment depends on whether the entity or the counterparty has the choice.

Equity-settled share-based payments - Treatment of vesting conditions

- A grant of equity instruments might be conditional upon satisfying specified vesting conditions. For example, a grant of shares or share options to an employee is typically conditional on the employee remaining in the entity's employ for a specified period of time. There might be performance conditions that must be satisfied, such as the entity achieving a specified growth in profit or a specified increase in the entity's share price.

- Vesting conditions, other than market conditions, shall not be taken into account when estimating the fair value of the shares or share options at the measurement date. Instead, vesting conditions, other than market conditions, shall be taken into account by adjusting the number of equity instruments included in the measurement of the transaction amount so that, ultimately, the amount recognised for goods or services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest.

- Hence, on a cumulative basis, no amount is recognised for goods or services received if the equity instruments granted do not vest because of failure to satisfy a vesting condition, other than a market condition, for example, the counterparty fails to complete a specified service period, or a performance condition is not satisfied.

- The entity shall recognise an amount for the goods or services received during the vesting period based on the best available estimate of the number of equity instruments expected to vest and shall revise that estimate, if necessary, if subsequent information indicates that the number of equity instruments expected to vest differs from previous estimates. On vesting date, the entity shall revise the estimate to equal the number of equity instruments that ultimately vested, subject to the requirements.

- Market conditions, such as a target share price upon which vesting (or exercisability) is conditioned, shall be taken into account when estimating the fair value of the equity instruments granted. Therefore, for grants of equity instruments with market conditions, the entity shall recognise the goods or services received from a counterparty who satisfies all other vesting conditions (e.g. services received from an employee who remains in service for the specified period of service), irrespective of whether that market condition is satisfied.

Cash-settled share-based payment – Treatment of vesting conditions

- A cash-settled share-based payment transaction might be conditional upon satisfying specified vesting conditions. There might be performance conditions that must be satisfied, such as the entity achieving a specified growth in profit or a specified increase in the entity's share price. Vesting conditions, other than market conditions, shall not be taken into account when estimating the fair value of the cash-settled share-based payment at the measurement date. Instead, vesting conditions, other than market conditions, shall be taken into account by adjusting the number of awards included in the measurement of the liability arising from the transaction.

- The entity shall recognise an amount for the goods or services received during the vesting period. That amount shall be based on the best available estimate of the number of awards that are expected to vest. The entity shall revise that estimate, if necessary, if subsequent information indicates that the number of awards that are expected to vest differs from previous estimates. On the vesting date, the entity shall revise the estimate to equal the number of awards that ultimately vested.

- Market conditions, such as a target share price upon which vesting (or exercisability) is conditioned, as well as non-vesting conditions, shall be taken into account when estimating the fair value of the cash-settled share-based payment granted and when remeasuring the fair value at the end of each reporting period and at the date of settlement.

- The cumulative amount ultimately recognised for goods or services received as consideration for the cash-settled share-based payment is equal to the cash that is paid.

SFRS(I) 1-24 *Related Party Disclosures*

The standard prescribes the necessary disclosures to draw attention to the possibility that the financial position and profit or loss of an entity may be affected by the existence of related parties, transactions and outstanding balances with related parties.

A party is related to an entity if it:

(a) directly, or indirectly controls, is controlled by, or is under common control with, the entity;
(b) has significant influence over the entity;
(c) has joint control over the entity;
(d) is a close member of the family of any individual who controls, or has significant influence or joint control over, the entity;
(e) is a close member of the family of the key management personnel of the entity or its parent;
(f) is an associate of the entity;
(g) is a joint venture in which the entity is a venturer;
(h) is a member of the key management personnel of the entity or its parent;
(i) is an entity that is controlled, jointly controlled or significantly influenced by any of the key management personnel or their close family members;
(j) is a post-employment benefit plan for the benefit of employees of the entity, or of any of its related parties.

The following related party disclosures are required:

- Relationships between a parent and its subsidiaries shall be disclosed irrespective of whether there have been transactions between them. An entity shall disclose the name of its parent and, if different, the ultimate controlling party.

- Where there are transactions between related parties, an entity shall disclose the following:

  (a) the nature of related party relationship;
  (b) the amount of the transactions;
  (c) the amount of outstanding balances, their terms and conditions and details of any guarantees given or received;
  (d) the amount of provision for doubtful debts in relation to the outstanding balances; and
  (e) the expense recognized during the period in respect of bad and doubtful debts due from related parties.

- Disclosure of key management personnel compensation in total, short-term and long-term employee benefits (monetary and non-monetary), post-employment benefits, termination benefits and share-based payment.

Such disclosures are made separately for each of the following categories: the parent, entities with joint control or significant influence over the entity, subsidiaries, associates, joint ventures in which entity is a venturer, key management personnel, and other related parties.

Consolidated Financial statements

SFRS(I) 3 *Business Combinations*

SFRS(I) 3 requires entities to determine whether a transaction or other event is a business combination by applying the definition in the standard. The three components of a business are inputs, processes and outputs.

Business combinations are accounted for using the acquisition method. This requires:
(a) Identifying the acquirer
(b) Determining the acquisition date
(c) Recognising and measuring the identifiable assets acquired, liabilities assumed and any non-controlling interest (NCI)
(d) Recognising and measuring goodwill or a gain from a bargain purchase

Goodwill is measured as the excess of the aggregate of:
- consideration transferred,

- the non-controlling (minority) interest, and
- fair value of any previously held equity interest in acquiree, over the identifiable net assets of the acquiree.

The non-controlling (minority) interest is measured at acquisition either at fair value or as a proportion of the fair value of the net assets of the acquiree.

The general rule under SFRS(I) 3 is that the subsidiary's identifiable assets and liabilities **must be measured at fair value** except in **limited, stated cases**. The identifiable assets and liabilities that are recognised in a business combination include all of the acquiree's assets and liabilities that the acquirer assumes.

Fair values may be incorporated into the books of the acquiree in either of the following ways:

(a) The subsidiary company might incorporate any necessary revaluations in its own books of account where allowed by the standards. In this case, we can proceed directly to the calculation of goodwill and in turn the consolidation, taking asset values and reserves figures straight from the subsidiary company's statement of financial position.
(b) The revaluations may be made as a consolidation adjustment without being incorporated in the subsidiary company's books. In this case, we must make the necessary adjustments to the subsidiary's statement of financial position as a working. Only then can we proceed to the consolidation.

SFRS(I) 10 *Consolidated Financial Statements*

A parent is an entity that controls one or more other entities. There are therefore three elements to control:

(a) Power over the investee
(b) Exposure or rights to variable returns from involvement with the investee, and
(c) The ability to use the power to affect the amount of returns.

Power is defined as existing **rights that give the current ability to direct the relevant activities of the investee**. There is no requirement for that power to have been exercised. Other than voting or potential voting rights, which individually, or in combination, can give an investor de facto power, examples of substantive rights include:

- Rights to appoint, reassign or remove key management personnel who can direct the relevant activities
- Rights to appoint or remove another entity that directs the relevant activities

- Rights to direct the investee to enter into, or veto changes to transactions for the benefit of the investor
- Other rights, such as decision-making rights specified in a management contract that give the holder the ability to direct the relevant activities

A parent **need not present** consolidated financial statements if and only if all of the following hold:

(a) The parent is itself a **wholly-owned subsidiary** or it is a **partially owned subsidiary** of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements.
(b) Its debt or equity instruments are **not publicly traded**.
(c) It is **not in the process of issuing securities** in public securities markets.
(d) The **ultimate or any intermediate parent** publishes consolidated financial statements that apply when an entity prepares separate financial statements in compliance with either Singapore Financial Reporting Standards (International) (SFRS(I)), or with another reporting framework.

<u>An Investment Entity is an entity that:</u>

(a) Obtains funds from one or more investors for the purpose of providing those investors with investment management services,
(b) Commits to its investors that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both, and
(c) Measures and evaluates the performance of substantially all of its investments on a fair value basis.

If a parent company meets the definition of an investment entity, it is prohibited from consolidating its subsidiaries (other than as noted below) or applying acquisition accounting (SFRS(I) 3) when it obtains control of another entity. Instead it must measure its investments at fair value. An exception to this requirement is made where an investment entity parent company has subsidiaries that provide services relating to its own activities (i.e. subsidiary is not an investment entity and the subsidiary's main purpose is to provide services and activities that are related to the investment activities of the investment entity parent). Such subsidiaries are consolidated as normal.

General steps taken for the consolidation of financial statements of subsidiaries with the parent

1. Elimination of investment in a subsidiary
2. Record of non-controlling interest
3. Elimination of realised intragroup transactions (including dividends paid by subsidiary during the financial year)
4. Elimination of Intragroup balances

5. Adjustments of unrealised profit of loss arising from intercompany transfers

SFRS(I) 11 *Joint Arrangements*

A **joint operation** is a joint arrangement whereby the parties that have joint control (the joint operators) have rights to the assets, and obligations for the liabilities, of that joint arrangement. A joint arrangement that is **not structured through a separate entity** is always a joint operation.

A **joint venture** is a joint arrangement whereby the parties that have joint control (the joint venturers) of the arrangement have **rights to the net assets** of the arrangement.

A **joint arrangement** that is structured through a **separate entity** may be either a joint operation or a joint venture.

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The existence of a contractual agreement distinguishes a joint arrangement from an investment in an associate. **If there is no contractual arrangement, then a joint arrangement does not exist**. The agreement is the key evidence of shared control.

Accounting for Joint Operations:

- SFRS(I) 11 requires that a joint operator recognises line-by-line the following in relation to its interest in a joint operation:

  (a) Its assets, including its share of any jointly held assets
  (b) Its liabilities, including its share of any jointly incurred liabilities
  (c) Its revenue from the sale of its share of the output arising from the joint operation
  (d) Its share of the revenue from the sale of the output by the joint operation, and
  (e) Its expenses, including its share of any expenses incurred jointly.

- On the acquisition of a joint operation, the joint operator must:

  (a) Measure the identifiable assets and liabilities at fair value (or in accordance with SFRS(I) 3);
  (b) Recognise acquisition costs in accordance with SFRS(I) 3;
  (c) Recognise goodwill for the excess consideration given;
  (d) Perform an impairment test for the cash-generating unit to which goodwill is allocated annually.

SFRS(I) 12 *Disclosure of Interests in Other Entities*

An entity that has investments in other entities must disclose:

(a) The **significant judgments and assumptions** made in determining whether the entity has control, joint control or significant influence over the other entities, and in determining the type of joint arrangement
(b) The **significant judgments and assumptions** made in determining that an entity is an investment entity

Disclosure of subsidiaries

(a) The interest that non-controlling interests have in the group's activities and cash flows, including the name of relevant subsidiaries, their principal place of business, and the interest and voting rights of the non-controlling interests
(b) Nature and extent of significant restrictions on an investor's ability to use group assets and liabilities
(c) Nature of the risks associated with an entity's interests in consolidated structured entities, such as the provision of financial support
(d) Consequences of changes in ownership interest in subsidiary (whether control is lost or not)

Disclosure of investment entities

(a) The fact that the investment entity exception has been applied
(b) Details of each unconsolidated subsidiary
(c) Any significant restrictions on the ability of an unconsolidated subsidiary to transfer funds to the investment entity and any commitments or intentions to provide support to an unconsolidated subsidiary
(d) Details of any support provided to an unconsolidated subsidiary in the period

Disclosure of associates and joint arrangements

(a) Nature, extent and financial effects of an entity's interests in associates or joint arrangements, including name of the investee, principal place of business, the investor's interest in the investee, method of accounting for the investee and restrictions on the investee's ability to transfer funds to the investor
(b) Risks associated with an interest in an associate or joint venture
(c) Summarised financial information, with more detail required for joint ventures than for associates

<u>SFRS(I) 1-28 *Investments in Associates and Joint Ventures*</u>

If an investor holds (directly or indirectly) **20% or more** of the voting power of the investee, it can be presumed that the investor has significant influence over the investee, unless it can be clearly shown that this is not the case.

SFRS(I) 1-28 requires all investments in associates to be accounted for using the equity method, **unless** one of the following applies:

1. The investment is classified as 'held for sale' in accordance with SFRS(I) 5.
2. The investment is held by a venture capital organisation (or similar). In this case it may elect to measure that investment at fair value through profit or loss.
3. The following exemption applies.

   An investor is exempt from applying the equity method if:

   (a) It is a parent exempt from preparing consolidated financial statements under SFRS(I) 10, para. 4a;
   or
   (b) All of the following apply:

   (i) The investor is a **wholly-owned subsidiary** or it is a **partially owned subsidiary** of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the investor not applying the equity method;
   (ii) Its securities are **not publicly traded**;
   (iii) It is **not in the process of issuing securities** in public securities markets; and
   (iv) The **ultimate or intermediate parent** produces consolidated financial statements available for public use in which subsidiaries are consolidated or measured through profit or loss.

<u>Accounting under the equity method:</u>

- Consolidated statement of profit or loss and other comprehensive income

  The investing group should take account of its share of the earnings of the associate whether or not the associate distributes the earnings as dividends.
  - Add to consolidated profit the group's share of the associate's profit after tax
  - Add to consolidated other comprehensive income the group share of the associate's other comprehensive income after tax

- For upstream and downstream transactions, when an associate is involved, only the group's share is eliminated.

- When the equity method is being used and the investor's share of losses of the associate equals or exceeds its interest in the associate, the investor should **discontinue** including its share of further losses. The investment is reported at nil value.

Considerations for the professional accountants

Code of Professional Conduct and Ethics
Ethics Pronouncement (EP) 100 the *ISCA Code of Professional Conduct and Ethics*

Fundamental Principles

A professional accountant shall comply with the following fundamental principles:

(a) Integrity – to be straightforward and honest in all professional and business relationships.
(b) Objectivity – to not allow bias, conflict of interest or undue influence of others to override professional or business judgements.
(c) Professional Competence and Due Care – to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional services based on current developments in practice, legislation and techniques and act diligently and in accordance with applicable technical and professional standards.
(d) Confidentiality – to respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not disclose any such information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor use the information for the personal advantage of the professional accountant or third parties.
(e) Professional Behaviour – to comply with relevant laws and regulations and avoid any conduct that discredits the profession.

Threats and Safeguards

Threats may be created by a broad range of relationships and circumstances. When a relationship or circumstance creates a threat, such a threat could compromise, or could be perceived to compromise, a professional accountant's compliance with the fundamental principles. A circumstance or relationship may create more than one threat, and a threat may affect compliance with more than one fundamental principle. Threats fall into one or more of the following categories:

(a) Self-interest threat – the threat that a financial or other interest will inappropriately influence the professional accountant's judgement or behaviour;
(b) Self-review threat – the threat that a professional accountant will not appropriately evaluate the results of a previous judgement made, or activity or service performed

by the professional accountant, or by another individual within the professional accountant's firm or employing organisation, on which the accountant will rely when forming a judgement as part of performing a current activity or providing a current service;

(c) Advocacy threat – the threat that a professional accountant will promote a client's or employer's position to the point that the professional accountant's objectivity is compromised;

(d) Familiarity threat – the threat that due to a long or close relationship with a client or employer, a professional accountant will be too sympathetic to their interests or too accepting of their work;

(e) Intimidation threat – the threat that a professional accountant will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the professional accountant.

Parts B and C of this Code explain how these categories of threats may be created for professional accountants in public practice and professional accountants in business, respectively. Professional accountants in public practice may also find Part C relevant to their particular circumstances.

Appendix B – Common verbs used by the Examiners

Verb	Description
Advise	**Advise** requires you to give **specific guidance** to an individual or a group (e.g. a taxpayer, audit client, management, etc.), so your answer must provide specific information or make a recommendation tailored to the individual or group and justify your position.
Calculate / Compute	Do the number crunching and derive the correct answer. Make sure that you write down your workings and crosscheck your numbers.
Describe	**Describe** requires you to provide the characteristics and features of an item or situation without going into step-by-step **detail** of how to perform that procedure.
Explain	**Explain** requires you to write at least several sentences conveying how you have analysed the information in a way that a layperson can easily understand the concept or grasp the technical issue at hand.
Identify	**Identify** is similar to list, but requires you to also provide an **explanation** as to why the item/s that you have **identified** is/are relevant to the facts given in the question.
In accordance with	This instruction requires you to relate your answer back to a specific document. Failure to make specific mention of the document in your answer will result in a loss of marks.
Recommend	Make a statement about the most appropriate course of action. If there is more than one possible course of action, **state** which action you would choose and why (**justify** your choice). Your professional judgment and your ability to **interpret** the wider situation are critical to scoring well in these types of questions. Don't forget to think about the future and the past, not just the present when making a **recommendation**.
Prepare / Present	**Prepare** (or **present**) requires you to produce your answer using a specific format. For instance, "**Present** an extract of the notes to the accounts for …" or "**Prepare** all the relevant journal entries for …".
Propose / Provide	**Put forward** (for example, a point of view, idea, argument, alternatives, etc.) **for consideration or action**. For instance, "Based on the facts of the case, propose the most tax-effective entity type …", or "Propose audit adjusting entries to correct …".

Verb	Description
State	**State** is similar to **list**, but the items require your professional judgement. For instance, "**State** any restrictions that apply". One of the easiest ways to make sure that you **state** comprehensively is to think, "**lis**t <u>and</u> **justify**". You will note that **state** appears in many of the verb descriptions given.
With reference to	This instruction requires you to relate your answer back to a specific document/s or set of facts. Failure to make specific mention of the document/s or facts in your answer will result in a substantial loss of marks.