ACRA LEGAL DIGEST

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A WORD FROM THE EDITORIAL TEAM

Welcome to the fifth issue of our Digest and the second from the Accounting and Corporate Regulatory Authority ("ACRA "). In this issue, we introduce the work done by the Council on Corporate Disclosure and Governance. We also bring to you the highlights of the Companies (Amendment No. 2) Bill 2004 and we invite you to give us your feedback on the Bill. Lastly, we update you on the latest addendum to the first practice direction in 2004 issued by ACRA on publication of the registration numbers on selected company's documents, which will be operative from October 2004.

All information contained herein is correct at the time of publication. Please do not hesitate to send us your comments or suggestions at www.acra.gov.sg/feedback.

The Editorial Team
Accounting and Corporate Regulatory Authority
1 September 2004

1 HIGHLIGHTS OF THE WORK OF THE COUNCIL ON CORPORATE DISCLOSURE AND GOVERNANCE

1.1 Background

The Companies Act, Cap. 50 (Section 200A) provides the Minister for Finance with the power to set up the Council on Corporate Disclosure and Governance ("CCDG"). The CCDG was set up on 16 August 2002 with Mr J Y Pillay as the Chairman. The CCDG comprises members that come from businesses, professional organisations, academic institutions and government. Officers from ACRA and MAS currently provide secretariat support to the CCDG. The terms of reference of the CCDG are:

- To prescribe accounting standards in Singapore;
- To strengthen the existing framework of disclosure practices and reporting standards, taking into account trends in corporate regulatory issues and international best practices; and
- To review and enhance the existing framework on corporate governance and promote good corporate governance in Singapore taking into account international best practices.

1.2 Adoption of Financial Reporting Standards

The CCDG has prescribed accounting standards, known as Financial Reporting Standards ("FRSs") for Singapore-incorporated companies and foreign companies registered under Division XI of the Companies Act. Companies are required under the Companies Act to comply with FRSs for financial statements covering periods beginning on or after 1 January 2003. The FRSs prescribed by the CCDG are based closely on the International Accounting Standards and International Financial Reporting Standards issued by the International Accounting Standards Board ("IASB").

The CCDG has also issued Interpretations of FRS ("INT FRSs") to give guidance on issues that are likely to receive divergent or unacceptable treatment in the absence of such guidance. The INT FRSs are also based closely on the Interpretations issued by the International Financial Reporting Interpretations Committee.

The CCDG has recently adopted the following FRSs:

- FRS 102 *Share-based Payment* (based on IFRS 2 *Share-based Payment*) – As a new Standard, FRS 102 requires entities to recognise all share-

based payment transactions (including employee stock options) in its financial statements;

- FRS 103 *Business Combinations* (based on IFRS 3 *Business Combinations*) – Unlike the predecessor FRS 22 *Business Combinations*, FRS 103 will not allow entities to apply the 'pooling of interest' method for accounting of business combinations. Amortisation of goodwill is no longer required though entities have to apply the impairment tests;

- FRS 104 *Insurance Contracts* (based on IFRS 4 *Insurance Contracts*) – As a new Standard, FRS 104 provides guidance on accounting for insurance contracts and aims to achieve convergence if widely varying insurance industry accounting practices around the world; and

- FRS 105 *Non-current Assets Held for Sale and Discontinued Operations* (based on IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*) – As a new Standard, FRS 105 specifies the accounting for assets held for sale, and the presentation and disclosure of discontinued operations. The Standards also replaces the existing FRS 35 *Discontinuing Operations*.

The FRSs and INT FRSs prescribed by the CCDG are freely accessible at the CCDG website at http://www.ccdg.gov.sg.

1.3 Exposure Drafts for Public Comments

Similar to the IASB, the CCDG believes it is important to seek comments from the various constituencies on new accounting proposals or revisions to existing Standards. Whenever the IASB issues any new exposure drafts ("EDs") for public comments, the CCDG will also issue similar EDs to gather comments from the local constituents. The CCDG will then consider the comments and send the final response to the IASB.

The following EDs are currently available at the CCDG website for public comments:

- ED INT FRS Employee Benefit Plans with a Promised Return on Contributions or Notional Contributions;

- ED Amendments to FRS 39 Cash Flow Hedge Accounting of Forecast Intragroup Transactions;

- ED Amendments to FRS 39 and FRS 104 Financial Guarantee Contracts and Credit Insurance;

- ED Amendments to FRS 39 Transition and Initial Recognition of Financial Assets and Financial Liabilities; and

- ED FRS *Financial Instruments: Disclosures*.

Interested parties are invited to provide their comments on the various EDs before the deadlines as indicated accordingly. The CCDG will consider the comments received in working out the final responses to the IASB.

1.4 Operating and Financial Review Guide

In February 2004, the Ministry of Finance accepted the CCDG's recommendations to issue an Operating and Financial Review ("OFR") Guide to raise the quality of reporting by listed companies. The OFR Guide is principle-based and provides guidance to listed companies for the preparation of the OFR in their annual reports. The OFR Guide also states that it is a good practice for listed companies to present their OFR in a distinct section of their annual reports. Adherence to the OFR Guide by listed companies is voluntary. Listed companies are urged to consider the principles and guidelines in the OFR Guide in preparing their annual reports for financial years starting from 1 January 2004.

1.5 Review of the Code of Corporate Governance

The CCDG is currently reviewing the Code of Corporate Governance (the "Code") which was first issued by the Corporate Governance Committee in March 2001. The review is intended to introduce improvements to the Code, taking into account feedback received since the inception of the Code and international developments in corporate governance. In the past two years, several countries have revised or issued some form of corporate governance rules and guidelines, namely the revised UK Combined Code, the Australian Stock Exchange's Principles of Good Corporate Governance and Best Practice Recommendations, and the New York Stock Exchange's Corporate Governance Listing Standards. The CCDG has formed a review committee consisting of members and non-members to study the matter in detail, seek views from the public, and submit a report to the CCDG. The CCDG aims to complete its review and submit its recommendations to the Ministry of Finance by the first half of 2005.

2 HIGHLIGHTS OF THE COMPANIES (AMENDMENT NO. 2) BILL

2.1 Background

The Ministry of Finance has initiated a public consultation exercise to seek comments on the proposed draft Companies (Amendment No. 2) Bill 2004. The consultation closes on 20 September 2004. A copy of this Bill and the relevant information are available at: http://www.mof.gov.sg/quick_guide/public_con_COY.html.

The draft Bill 2004 covers the following:

- Abolishing the concept of par value and authorised share capital;
- Introducing an alternative capital reduction process which does not require court sanction;
- Liberalising the financial assistance restrictions to allow financial assistance to be provided under additional circumstances;
- Allowing share-buyback to be funded out of profits as well as capital where supported by a solvency statement;
- Allowing repurchased shares to be held as treasury shares; and
- Introducing a more effective and efficient statutory form of merger/amalgamation process.

In relation to the 6 areas of reform highlighted above, we set out below the present position in the Companies Act, the proposed changes and the issues raised for public consultation. While specific issues are raised for feedback, respondents are free to give their comments/views on any other issues relating to the amendments proposed.

2.2 Abolition of Par Value of Shares and Authorised Capital

Currently, all shares issued by a company must have a par value which is the minimum amount of money that shareholders are statutorily required to put into the company. The company is also required to report the registered capital in its Memorandum of Association. The registered capital acts as a pre-planned ceiling on the maximum amount of capital and maximum number of shares the directors can issue. The reason is that the authorised capital gives certainty to shareholders of his ownership and degree of control over the company.

However, the law presently allows the company to increase its authorised capital at relative ease, usually with an ordinary resolution. The company is also required to report the increase in its authorised capital to the regulators. The impact of the abolition of authorised capital means that companies are no longer limited by an upper limit on the shares that a company may issue, for a start.

Clause 9 of the Bill abolishes the concept of par value shares. It also provides that the abolition applies to shares issued before the date of amendment as well. This means that upon commencement of the amendment, all companies in Singapore will not have a par value for their shares. The transitional provisions provide that the outstanding amount in the share premium account and capital redemption reserve becomes part of the company's share capital, and there are limited uses for the amounts standing to the credit of its share premium account immediately before the date of amendment.

As for abolition of authorised capital, Clause 13 of the Bill abolishes the need for a company to report its increase in share capital when it goes beyond the registered capital. However, we have retained during consultation the requirement to report the registered capital in the Memorandum, which will be the share capital that the company has reported that it will be starting with. The company may increase their capital and there is no reporting to the regulators required.

Throughout the Bill, consequential amendments are made to implement the abolition of par value shares and four specific issues are raised for public consultation. The issues raised are –

- *Clause 10: Whether we should impose an additional reporting requirement for consideration unpaid on the shares at the point of allotment?*

- *Clause 11: Should Section 67 be repealed totally or some basic conditions such as authorisation by the articles to allow payment of commissions should be retained?*

- *Clause 24: Is the amendment necessary in view of the fact that the substantial shareholdings are likely to remain unchanged under the new section 83?*

- *Clause 26: Is it necessary to impose the disclosure requirement of consideration unpaid on shares in parallel to clause 10 of the Bill?*

2.3 Reduction of Share Capital Without a Court Order

Currently, Section 73 requires a company to obtain the court's approval before it may reduce its share capital. The reason for court supervision is to ensure that creditors are not prejudiced by this capital reduction. However, the Company Legislation and Regulatory Framework Committee ("CLRFC") took the view that Singapore should introduce an alternative and simplified process of capital reduction. The new Division 3A will allow companies to reduce their share capital without a court order subject to certain conditions, and in particular, if supported by a solvency statement.

The draft Bill makes a distinction between reduction of share capital by public companies and private companies. Public companies, for example, are subjected to fairly stringent requirements, such as publicity of the proposed reduction. The issues raised for public consultation are:

- *Clause 21: Do you think that the differences in requirements for reduction of share capital for public and private companies are justified? How would these new provisions compare with the current regime which is retained under the new Section 78I in this Bill?*

2.4 Giving of Financial Assistance

A company is generally prohibited from giving financial assistance to third parties to acquire shares in the company. The proposed amendments to Section 76 will allow companies to give financial assistance to third parties if shareholders unanimously agree and the assistance given is less than 10% of the paid up capital. The financial assistance should also be supported by a solvency statement, as in the case of a capital reduction without a court order.

Clause 16 introduces the proposed new sub-sections 76(9A) to (9B) which will set out the conditions under which a company may give financial assistance, and sub-sections (9C) to (9D) contain the safeguards for the interests of the company, its members and its creditors.

2.5 Redemption of Preference Shares Using Capital

Companies are currently allowed to redeem their preference shares out of profits or a fresh issue of shares. The proposed amendment to Section 70 will also allow a company to do so out of capital provided the directors have made a solvency statement.

2.6 Reforming the Share Buyback Regime

Since 1998, share buy-backs by companies have been allowed. The CLRFC considered if share buy-backs should only be funded out of distributable profits. The CLRFC finally recommended that the share buy-backs should be funded out of distributable profits or capital. But if it is the latter, it has to be supported by a declaration of solvency. Please refer to note for 2.9.

Companies will be allowed to buy back shares out of profits or capital provided the company is solvent. The amendments have included a test for solvency which is essentially a combined cash-flow test and an assets-over-liabilities test. You would note that the test is also required for 2.3, 2.4 and 2.5. The issues raised for public consultation are:

- *Clause 19 (relating to Section 76F): Should the solvency test for share buybacks under Section 76F (when the company buys back out of capital or profits or a combination of both) be identical to the test in Section 7A?*

2.7 Introduction of Treasury Shares

Hitherto, all shares bought back by the company must be cancelled immediately upon re-acquisition by the company. The new Sections 76H-76K will allow the company to hold these re-acquired shares in treasury instead of cancelling them. To prevent any abuse of these treasury shares, the proposed new Section 76J suspends the voting and dividend rights of the treasury shares.

The issues raised for public consultation are:

- *Clause 19 (relating to Section 76L): Do you think the 12 month period is too long? What do you suggest is an appropriate period? We propose that the company should dispose or cancel the shares within one month.*

- *Clause 19 (relating to Section 76J): Is it necessary or desirable to expressly provide for share splits of treasury shares (see Section 76J(5)(b)?*

- *Clause 19 (relating to Section 76K): Do you think that the uses of treasury shares should be expanded further? We have received suggestions for additional uses but we are concerned that there are no accounting standards for additional uses of treasury shares. Are these valid concerns?*

- *Clause 43 (relating to Section 76K): Do you agree with the above restrictions (contained under Section 403) imposed on profits that are payable as dividends to shareholders?*

2.8 Mergers and Amalgamations

The CLRFC noted that the provision for amalgamation of companies under supervision by the court (Section 212) was seldom used in practice as the courts applied this provision restrictively. It recommended adopting a regime for amalgamation of companies without a court order for a more efficient amalgamation process. The new Sections 215A to 215J, based on the New Zealand Companies Act, set out the procedures to be adopted for amalgamation of all types of companies, including holding companies and their subsidiaries. The amalgamation must be supported by two solvency statements from each amalgamating company.

In the first solvency statement (referred to in Section 215I), the directors of each amalgamating company must state that the *amalgamating* company:

- has no ground on which it can be found to be unable to pay its debts; and
- the value of the *amalgamating* company's assets is not less than that of its liabilities.

In the second solvency statement (referred to in Section 215J), the directors of each amalgamating company must state that the *amalgamated* company:

- will be able to pay its debts as they fall due 12 months after the amalgamation; and
- the value of the *amalgamated* company's assets will not be less than that of its liabilities.

The issues raised for public consultation are:

- Clause 39 (relating to proposed Sections 215I to 215J): *Would you agree that the solvency test to be adopted should be consistent with that crafted under Section 7A? If you disagree could you suggest how the solvency test should be constructed?*

2.9 Solvency Test

Almost all the amendments mentioned above require a solvency statement that confirms the solvency status of the company in question. The proposed new Section 7A sets out the matters directors must consider when making a solvency statement referred to in the new Division 3A, Section 76 and Section 70. The solvency tests for share buy-backs and amalgamations (similar to that in Section 7A) are found in Section 76F and Section 215I-J respectively.

The solvency statement requires the directors to declare that:

- the company will be able to pay its debts as they fall due 12 months from the date of the statement; and
- the value of the company's assets will not be less than the value of its liabilities after the transaction.

The issue raised for public consultation is:

- *Clause 5: Do you agree that the solvency test (modelled after the UK Bill 2002) should require the directors to take into account all liabilities including contingent and prospective liabilities?*

Note: The CLRFC had recommended that the transactions above must be supported by a "declaration of solvency". The term used in the draft Bill, however, is a "solvency statement" as defined in Section 7A and Sections 215I-J.

3 UPDATES ON ADMINISTRATIVE PRACTICES

ACRA issued an addendum to Practice Direction No. 1 of 2004 in August 2004. The purpose of the addendum was to further assist the business community and professionals to comply with the requirements under Section 144(1A)[1] that shall be operative from 1 October 2004.

The following questions were addressed in ACRA's addendum.

- *What constitutes official notices and publications of or purporting to be issued or signed by or on behalf of the company,*
- *How does a company decide whether it is necessary to print the company registration number on the material concerned?*

[1] Section 144(1A) reads "The registration number of a company shall appear in a legible form on all business letters, statements of account, invoices, official notices, and publications of or purporting to be issued or signed by or on behalf of the company."

- *What are the acceptable formats that can be used for the registration numbers?*
- *If the company has printed other forms of identifiers, can it be exempted from printing its company registration number?*
- *If some other written law requires the company to print its name and address but not the registration number on its product packaging and/or labels, is the company required by Section 144(1A) to print the registration number on the product packaging and/or labels?*
- *In view of the practical concerns raised and the 1 October 2004 deadline, would ACRA be lenient in enforcing Section 144(1B) if companies are unable to meet the requirements of Section 144(1A) by 1 October 2004?*
- *Does Section 144(1A) apply to foreign companies or business firms?*
- *Company ABC, a local company, is the sole proprietor/partner of DEF, a business firm. Does Company ABC's name and registration number have to appear on DEF's documents?*

The addendum is available at:
http://www.acra.gov.sg/legislation/practice0408.html.

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