CHAPTER 4

ACCOUNTS AND AUDIT

I. INTRODUCTION

1 The provisions reviewed under this section relate to the preparation of company accounts and the requirement for those accounts to be audited. The Steering Committee recommends the abolition of the status of exempt private company and its replacement with a framework for small companies. Other matters considered include the reporting requirements for dormant companies, the directors' report and the provisions relating to auditors. A table summarising the recommendations in respect of the three main obligations of preparation of accounts, requirement for audit and filing of accounts for various types of companies is set out in Annex A.

II. FINANCIAL REPORTING FOR SMALL COMPANIES

2 Currently, all companies are required to prepare accounts in accordance with the Singapore Financial Reporting Standards (SFRS). All companies must be audited unless the company is an exempt private company[1] (EPC) S$5m revenue or less[2]. Companies, other than solvent EPCs, must file accounts with the Accounting and Corporate Regulatory Authority (ACRA). Solvent EPCs are required to file a confirmation of solvency.

(a) Audit exemption for small companies

3 Feedback was received that the threshold amount of $5 million, which was introduced with effect from 1 June 2004, is too low. Furthermore, it was noted that in other countries such as the UK, Australia and New Zealand, the criteria for determining what constitutes a small company for the purposes of differential statutory financial reporting requirements are generally based on revenue, assets and number of employees. Such criteria would recognise a broader group of stakeholders (e.g. creditors, employees, customers) who may find the financial information relating to a company valuable, other than just shareholders.

4 Small company criteria (based on revenue, assets and number of employees) should be used to determine whether a company is required to be audited. Small companies would be exempted from the statutory requirement for audit. This is in line with reducing the regulatory costs for smaller companies.

5 The proposed approach is that a company would qualify as a "small company" if it is a private company and fulfils two of the following criteria:

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[1] Under section 4 of the Companies Act, "exempt private company" is defined as —
(a) a private company in the shares of which no beneficial interest is held directly or indirectly by any corporation and which has not more than 20 members; or
(b) any private company, being a private company that is wholly owned by the Government, which the Minister, in the national interest, declares by notification in the *Gazette* to be an exempt private company.
[2] Section 205 of the Companies Act read with regulation 89A of the Companies Regulations.

Criterion One	Criterion Two	Criterion Three
Total annual revenue of not more than S$10 million.	Total gross assets of not more than S$10 million.	Number of employees not more than 50.

6 Where a parent company prepares consolidated accounts, the parent may qualify as a "small company" if the criteria in the preceding paragraph are met on a consolidated basis.

7 Based on the present definition of an exempt private company, a company with a corporate shareholder would not currently be able to qualify for an exemption from audit. By contrast, under the Steering Committee's proposed small company criteria, a company with a corporate shareholder can be exempt from audit if it qualifies under the proposed "small company" criteria, even if it is part of a group of companies of which the parent company does not qualify for audit exemption. This would be of concern because if the parent company of the group is required to prepare audited consolidated accounts, it would be difficult for it to do so where its subsidiaries are exempt from audit.

8 The Steering Committee therefore recommends that a subsidiary which is a member of a group of companies may be exempt from audit as a "small company" only if the entire group to which it belongs qualifies on a consolidated basis for audit exemption under the "small company" criteria.

9 There were some concerns that if the criteria are hardwired into the Act, they might not keep pace with changes with the business environment. It is therefore proposed that the threshold quantum for each of the criteria can be prescribed by way of regulations.

(b) Exempt private companies and filing obligations

10 The starting premise is that all companies, by choosing to use the company structure as a business vehicle, should provide disclosure of useful information to members of the public through filing with the Registrar, so as to enable persons who deal with them to make informed decisions. In the Asian context, however, family-run companies would want to keep financial information regarding their companies private. As such, a company which qualifies as an EPC currently has the advantage of being exempt from the requirement to file its accounts (if solvent).

11 An exempt private company is currently defined[3] as follows:

(a) a private company in the shares of which no beneficial interest is held directly or indirectly by any corporation and which has not more than 20 members; or
(b) a private company that is wholly owned by the Government, which the Minister, in the national interest, declares by notification in the *Gazette* to be an exempt private company (a "Government-owned EPC");

12 Solvent EPCs, which are exempt from filing, form more than half of all the companies in Singapore. This lack of transparency for a significant number of companies may prejudice

[3] Section 4(1) of the Companies Act.

persons dealing with solvent EPCs, given that they are not able to verify the financial position of an EPC declared as solvent. In particular, in the case of large EPCs, creditors and other interested persons may not have the bargaining power to ask for financial information from the EPC directly.

13 Furthermore, in recent years, new vehicles such as the limited liability partnership (LLP) and limited partnership (LP) have been introduced, which could be appropriate alternatives to the EPC regime.

14 The Steering Committee therefore proposes to abolish the concept of an EPC. It was observed that no other country studied had a similar concept. To preserve some level of confidentiality for smaller-sized companies, it is proposed that companies which fall within the "small companies" criteria as discussed above be required to file only basic information. The concession that not the full financial information is made available would preserve some level of confidentiality for smaller companies, while making at least some information available to members of the public. Using a "size test" is consistent with consultation feedback received that confidentiality is useful to "attract and grow" SMEs in Singapore.

15 One notable concern, however, is that even basic information may reveal too much in respect of certain types of companies, e.g. Government-owned companies, private investment companies. The "size test" also may not be the appropriate test for the need for confidentiality for some types of companies i.e. due to the nature of the activities, even large companies would be concerned with confidentiality.

16 The Steering Committee therefore proposes certain exemptions from filing of financial information under certain circumstances. A company will be exempt from filing any financial information if it is a private company which is –

(a) wholly-owned by the Government, which the Minister, in the national interest, declares by notification in the Gazette to be exempt; (following the current definition of limb (b) of the definition of an "exempt private company")

(b) part of a class of companies prescribed by the Minister as being a specific class to which the filing requirement does not apply (these would be in relation to specific industries where confidentiality of information is critical and public interest in the accounts is low, e.g. private family investment companies); or

(c) exempted by the Registrar upon application on a case-by-case basis and published in the Gazette.

17 The exemption from filing proposed above in paragraph 16 should still be subject to the condition that the company is solvent. This would mean the company would have to file the full accounts if it is insolvent, unless it is a Government-owned EPC gazetted under section 12(2A) CA.

Recommendation 4.1

Small company criteria should be introduced to determine whether a company is required to be audited. Small companies would be exempted from the statutory requirement for audit. The following are the criteria for determining a "small company" —

(a) the company is a private company; and

(b) it fulfils two of the following criteria:

Criterion One	Criterion Two	Criterion Three
Total annual revenue of not more than S$10 million.	**Total gross assets of not more than S$10 million.**	**Number of employees not more than 50.**

Recommendation 4.2

Where a parent company prepares consolidated accounts, a parent should qualify as a "small company" if the criteria in Recommendation 4.1 are met on a consolidated basis.

Recommendation 4.3

A subsidiary which is a member of a group of companies may be exempt from audit as a "small company" only if the entire group to which it belongs qualifies on a consolidated basis for audit exemption under the "small company" criteria.

Recommendation 4.4

The current status of "exempt private company" should be abolished.

Recommendation 4.5

Companies which qualify under the proposed "small company" criteria should file basic financial information, but with the following exceptions where such companies are solvent:

(a) private companies wholly-owned by the Government, which the Minister, in the national interest, declares by notification in the Gazette to be exempt;

(b) private companies falling within a specific class prescribed by the Minister as being exempt (e.g. specific industries where confidentiality of information is critical and public interest in the accounts is low); and

(c) private companies exempted by the Registrar upon application on a case-by-case basis and published in the Gazette.

III. FINANCIAL REPORTING FOR DORMANT COMPANIES

18 Currently, a dormant company is exempted from the statutory audit requirements but is still required to prepare accounts that are in compliance with the SFRS[4]. A company is taken to be dormant during a period where no "accounting transaction" occurs[5] and a list of transactions which may be disregarded as an accounting transaction are set out under section 205B(3) of the Companies Act.

19 The issues considered by the Steering Committee were whether the regulatory burden for dormant companies should be further lightened and whether the criteria for determining dormancy should be refined.

20 The regulatory regimes for dormant companies in the UK, New Zealand and Hong Kong were reviewed. Australia does not have a separate regulatory regime for dormant companies.

21 A dormant company does not carry out active trading, and therefore it is less likely that anyone will be prejudiced if the company does not prepare accounts, especially if such a company is not listed. Although there was feedback received that the reporting cost would be minimal if a company is dormant, the Steering Committee took the view that the cost of preparing accounts for such a company would outweigh the benefits of the accounts. If the requirement for preparing accounts is removed, there will also be no need for filing requirements. This is similar to the position in New Zealand and Hong Kong.

22 There would, however, be a need for some safeguards to ensure that the company is in fact dormant for the entire financial period in question and that persons are not unduly prejudiced. The following safeguards are proposed:

(a) The directors of a dormant company must lodge an annual declaration to the effect that:

  (i) the company is dormant for the whole duration of the financial year in question; and

  (ii) the shareholders of the company have been duly informed of the company's dormant status and that they will be notified if the company intends to enter into a relevant accounting transaction.

(b) The company must be dormant for the entire financial year in question.

(c) Shareholders and ACRA will be empowered to direct a dormant company to prepare its accounts, and to lodge them unless exempted under any other exemption.

23 In particular, an annual declaration by the directors would require the directors to address their mind to the matter and make a statement accordingly. One of the respondents suggested that this should be by way of statutory declaration. However, the Steering

[4] Section 205B(1) of the Companies Act.
[5] Section 205B(2) of the Companies Act.

Committee took the view that it is not necessary that the annual declaration be by way of statutory declaration as the penalties in respect of a false or misleading statements in an annual declaration under section 401(2) CA are sufficient.

24 Listed companies usually have a greater number of shareholders and stakeholders, and possibly more creditors, hence the Steering Committee is of the view that it would be prudent to retain financial reporting requirements for dormant listed companies. This is also consistent with the position in New Zealand.

25 Presently dormant companies are not subjected to the statutory audit requirements. The Steering Committee is of the view that this should be retained for dormant listed companies. If the company is dormant for the financial year in question, shareholders and other stakeholders are not likely to be unduly prejudiced if the accounts are not audited, even in the case of a listed company.

26 In light of this, dormant companies which are subsidiaries of listed companies should also continue to prepare accounts, since listed companies would need to incorporate the financial information from their subsidiaries for the purposes of consolidation of accounts.

(a) Disregarded transactions

27 The current list of disregarded transactions includes any fee payable under the Companies Act or composition amounts under section 409(4) of the Companies Act. The Steering Committee is of the view that the list of disregarded transactions be extended to cover statutory fees or fines under any Act. The Steering Committee is also of the view that the payment of costs and receipts of income (such as bank interest) of up to a specified amount should be disregarded for the purpose of determining whether a company can be considered dormant. This is the position in New Zealand. The threshold amount for nominal payments/receipts can be prescribed in regulations.

(b) Substantial assets threshold

28 A concern was noted as to whether a company which has not carried on transactions but which owns substantial assets (e.g. land) should qualify as a dormant company. With the recommendation to allow non-listed dormant companies to be exempt from all financial reporting requirements, it is necessary to provide a total asset threshold as a criterion for determining whether a company may benefit from the reduced financial reporting requirements for non-listed dormant companies. The Steering Committee is of the view that there should be a carve-out from the dormant company financial reporting regime if the company holds more than a threshold amount of total assets (e.g. S$500,000). This threshold figure may be varied by the Minister for Finance by way of regulations. A company with substantial assets should continue to prepare accounts so as to provide accountability in respect of the preservation of those assets. Such a company should be required to prepare accounts, but will be exempt from audit, similar to a listed dormant company.

29 There was feedback received that using an assets threshold is arbitrary and the value of a company's assets as the criteria may result in uncertainty as a company may fall in and out of the exemption on a year-by-year basis, especially with the use of fair value accounting. Another comment was that the benchmark used should not be confined to total assets as there may also be situations where a company may not have substantial assets but have significant

liabilities offset by negative equity, and such a company should have to prepare accounts. However, on balance, the Steering Committee is of the view that a substantial assets threshold is necessary and appropriate for determining a dormant company's exemption from preparation of accounts.

Recommendation 4.6

Dormant non-listed companies (other than subsidiaries of listed companies) should be exempt from financial reporting requirements, subject to certain safeguards.

Recommendation 4.7

To benefit from the dormant company exemption, the following proposed safeguards must be complied with:

(a) **Annual declaration of dormancy by the directors of a dormant company.**

(b) **The company must be dormant for the entire financial year in question.**

(c) **Shareholders and ACRA will be empowered to direct a dormant company to prepare its accounts, and to lodge them unless exempted under any other exemption.**

Recommendation 4.8

Dormant listed companies should continue to prepare accounts but be exempted from statutory audit requirements (status quo).

Recommendation 4.9

A dormant company which is a subsidiary of a listed company should continue to prepare accounts but be exempt from audit, similar to a dormant listed company.

Recommendation 4.10

The list of disregarded transactions in determining whether a company is dormant should be extended to include statutory fees/fines under any Act and nominal payments/receipts.

Recommendation 4.11

A total assets threshold test of S$500,000 (which may be varied by the Minister for Finance by way of regulations) should be introduced for dormant companies.

IV. SUMMARY FINANCIAL STATEMENTS

30 Under section 203A of the Companies Act, only listed companies have the option to provide summary financial statements to shareholders instead of the full set of accounts. Summary financial statements provide a summary of the information in the full set of accounts.

31 The Steering Committee is of the view that the use of summary financial statements should be extended to all companies so as to have a consistent treatment for all companies. This is in line with the practices in the UK, Australia and New Zealand.

32 One respondent pointed out that for small and medium sized companies, preparing of summary financial statements may not be necessary as it is usually not difficult to read through the whole financial statements, especially in light of the possible simplified FRS for SMEs. Preparation of a separate set of summary financial statements may incur additional costs which outweigh its benefits. However, as the preparation of summary financial statements is optional and not mandatory, each company would have a choice whether or not to prepare summary financial statements.

Recommendation 4.12

The use of summary financial statements should be extended to all companies.

V. THE DIRECTORS' REPORT

(a) Disclosure of directors' benefits

33 Section 201(8) of the Companies Act requires the directors' report to state whether a director has received or is entitled to receive a benefit (other than a benefit included in the aggregate amount of emoluments received or due and receivable by the directors shown in the accounts or, if the company is a holding company, the consolidated accounts in accordance with the accounting standards or the fixed salary of a full-time employee of the company) by reason of a contract made by the company or a related corporation with the director or with a firm of which he is a member, or with a company in which he has a substantial financial interest and, if so, the general nature of the benefit. At the same time, key personnel compensation needs to be disclosed under FRS 24. In addition, director's fees are also required to be disclosed to and approved by members of the company under sections 168 and 169 of the Companies Act.

34 In light of these existing disclosure requirements, the Steering Committee is of the view that there is no need to retain a separate requirement in section 201(8) to list directors' benefits in the directors' report.

35 In Australia, the directors' report of a listed company must include discussion of the board policy for determining, or in relation to, the nature and amount (or value, as appropriate) of remuneration of the key management personnel and the prescribed details in

relation to the remuneration of each member of the key management personnel[6]. In the UK, specified information about directors' remuneration must be disclosed in the notes to the company's accounts, and quoted companies are required to disclose details relating to their remuneration in a directors' remuneration report[7]. In New Zealand, the annual report of the company is required to state, in respect of each director or former director of the company, the total of the remuneration and the value of other benefits received by that director or former director from the company during the accounting period[8].

36 While noting that the scope of disclosure under s201(8) CA is conceptually wider than what is required under the SFRS, the Steering Committee took the view that in practical terms, the provision was not necessary.

Recommendation 4.13

Section 201(8) of the Companies Act which requires disclosure of directors' benefits in the directors' report should be repealed.

(b) Inclusion of business review

37 The summary financial statement of a listed public company must include a Chairman's statement covering a business review and future developments (under "Additional Information" in the Second Schedule to the Companies (Summary Financial Statement) Regulations). There is however no equivalent requirement in the accounts or reports accompanying the accounts.

38 The UK has detailed requirements in respect of the statement of business review and future developments. Unless the company is subject to the small companies' regime, the directors' report is required9 to contain a business review. The business review must contain:

(a) a fair review of the company's business; and

(b) a description of the principal risks and uncertainties facing the company10.

However, it is noted that these requirements are linked to the duty to promote the success of the company under section 172 of the UK Companies Act 2006, which is not being adopted in Singapore.

39 In Australia, the directors' report must refer to likely developments in the entity's operations in future financial years and the expected results of those operations.[11] In New Zealand, the board of directors must describe, in its annual report, so far as the board believes is material for the shareholders to have an appreciation of the state of the company's affairs

[6] Section 300A of the Australia Corporations Act 2001.
[7] This is required by regulations made under the UK Companies Act 2006.
[8] Section 211 of the New Zealand Companies Act 1993.
[9] Section 417 of the UK Companies Act 2006.
[10] Section 417(3) of the UK Companies Act 2006.
[11] Section 299(1)(e) of the Australia Corporations Act 2001.

and will not be harmful to the business of the company or of any of its subsidiaries, any change during the accounting period in:

(i) the nature of the business of the company or any of its subsidiaries; or

(ii) the classes of business in which the company has an interest, whether as a shareholder of another company or otherwise[12].

40 The Steering Committee is of the view that while listed companies usually prepare a business review, this is not necessary for all companies.

41 No differing views were received from the consultation feedback.

<u>Recommendation 4.14</u>

There is no need to require all companies to prepare a statement of business review and future developments in the accounts or directors' report under the Companies Act.

(c) Requirement for directors' report

42 The Steering Committee notes that, in Singapore, the directors' report for most companies is based on a standard boilerplate and that there is little value in having the directors' report as a separate document, if the relevant disclosures could be made elsewhere.

43 It was observed that New Zealand does not require a company to have a directors' report. However, the New Zealand Companies Act 1993[13] requires the company to set out, in its annual report, certain information such as particulars of entries in the interests register made during the accounting period and the total of the remuneration and the value of other benefits received by that director or former director from the company during the accounting period, similar to information contained in the directors' report in Singapore.

44 In Australia, a small proprietary company is generally exempted from the requirement to prepare a directors' report (or the financial report) unless:

(a) it is directed to do so by its shareholders or the Australian Securities and Investments Commission (ASIC); or

(b) it was controlled by a foreign company for all or part of the year and it is not consolidated for that period in financial statements for that year lodged with ASIC by:

(i) a registered foreign company; or

(ii) a company, registered scheme or disclosing entity[14].

[12] Section 211(1)(a) of the New Zealand Companies Act 1993.
[13] Section 211(1)(a).
[14] Section 292(2) of the Australia Corporations Act 2001.

45 The UK and Hong Kong require all companies to prepare directors' reports.

46 There was feedback received that directors' report serves a specific purpose, viz for directors to state their opinion on whether the financial statements are drawn up so as to give a true and fair view of the state of affairs of the company as at the end of the financial reporting year in accordance with the Companies Act and SFRS. Thus, the directors' report ought to be clearly delineated from the financial accounts or notes to financial accounts to avoid any confusion and for ease of reference. In particular, where there is a change of directors, a separate directors' report would allow new directors to make specific statements should they not agree with certain information in the financial statements.

47 The Steering Committee, however, took the view that the disclosures in the directors' report can be adequately made elsewhere, e.g. in the accounts, notes to the accounts, or the directors' statement in section 201(15) of the Companies Act. If there is a specific need for a directors' report for listed companies, SGX could include such a requirement in the listing rules.

48 If the recommendation for abolition of the directors' report is accepted, the Steering Committee is of the view that section 201(15) of the Companies Act should be clarified to require that the full list of directors of companies appear in the statement by the directors. This is to replace the current requirement in section 201(6)(a) and (6A)(a) of the Companies Act to state the names of the directors of the company or holding company in office at the date of the report. Most of the respondents agreed to such a clarification.

Recommendation 4.15

The requirement for a separate directors' report should be abolished.

Recommendation 4.16

Section 201(15) of the Companies Act should be clarified to require that the full list of directors of companies appear in the statement by the directors.

VI. OBLIGATIONS RELATING TO AUDIT

(a) Imposition of statutory duty on directors to ensure that auditors are aware of all relevant audit information

49 The Steering Committee considered and rejected a proposal to adopt the UK approach of requiring the directors to ensure that the company auditors are aware of all relevant audit information. Section 418(2) of the UK Companies Act 2006 requires the directors' report to contain a statement to the effect that so far as each director is aware, there is no relevant audit information of which the company's auditor is unaware, and that he has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company's auditor is aware of that information.

50 To impose such an obligation on the directors will be unduly onerous and may have the inadvertent consequence of shifting some of the auditors' obligations and duties onto the directors. Furthermore, the UK approach would be too onerous especially if there are changes to the accounti ng standards. It presupposes that a director knows what information the auditors would need to know.

51 On the other hand, supporters of the UK approach highlighted that it is desirable to adopt such an approach as long as there are sufficient safe harbour provisions to protect directors who are acting in good faith and who have discharged their responsibilities to the best of their abilities. It was suggested that such an approach would result in better-informed directors and greater communication in the audit process.

52 The Steering Committee noted that section 207 of the Companies Act already gives the auditors a right of access at all times to the accounting and other records of the company, including registers, and allows the auditors to require from any officer of the company (which is defined in section 4(1) to include a director) such information and explanations as may be desired for the purposes of audit. The Steering Committee is of the view that this provision would achieve adequate information flow and communication between the directors and the auditors. The Singapore position is in line with the position in Australia[15] and New Zealand[16].

Recommendation 4.17

The UK approach of requiring the directors to ensure that the company auditors are aware of all relevant audit information need not be adopted.

(b) Mandating auditing standards

53 Currently, section 207(3) of the Companies Act sets out a list of duties of auditors as to their reports on company accounts. In addition to these duties, as a matter of practice auditors in carrying out an audit usually also follow the Singapore Standards on Auditing (SSA) issued by the Institute of Certified Public Accountants of Singapore (ICPAS). Compliance with the SSA is currently not mandatory under the Companies Act. However, the SSA is one of the standards recognised under the Practice Monitoring Programme under the Accountants Act as a prescribed standard for the Programme.

54 In contrast, in Australia auditing standards are legally enforceable for audits conducted under the provisions of the Australia Corporations Act 2001. Breaches of the auditing standards are a criminal offence under section 307A of the Australia Corporations Act 2001.

[15] Under section 310 of the Australia Corporations Act 2001, an auditor has a statutory right of access at all reasonable times to the books of the entity and may require any officer to give information, explanation or assistance for the purposes of the audit or review, as long as the request is a reasonable one.

[16] Under section 206 of the New Zealand Companies Act 1993, the board of a company must ensure that an auditor of a company has access at all times to the accounting records and other documents of the company, and the auditor is entitled to require from a director or employee such information and explanations as he thinks necessary for the performance of his duties as auditor.

55 The Steering Committee considered whether auditing standards should have the force of law so that auditors are required under the Companies Act to comply with the standards. It has decided not to follow the position in Australia but recommends that the existing requirements in respect of the duties and responsibilities of auditors should be streamlined. Matters pertaining to corporate governance should be retained in the Companies Act, but work procedures should be left to the requirements in the auditing standards. Most of the consultation respondents agreed with the views of the Steering Committee.

Recommendation 4.18

There is no need to legislatively mandate compliance with auditing standards, but the existing requirements in section 207(3) of the Companies Act, which set out a list of duties of auditors, should be streamlined.

(c) Requirement to report on record-keeping

56 One of the duties imposed under section 207(3)(b) of the Companies Act is that the auditor should form an opinion on whether proper accounting and other records (excluding registers) have been kept by the company. The issue is whether this duty is still relevant.

57 All of the countries studied have imposed a duty on the auditor to state an opinion on record-keeping, although the exact wording of the obligation varies between the countries.

58 One of the consultation respondents noted that it is not too burdensome to retain this requirement as part of the job of the auditor would be to do a check of such documents. Another respondent, however, suggested that the Singapore Standards on Auditing would adequately provide for this and that no express obligation in the Companies Act was necessary.

59 The Steering Committee takes the view that section 207(3)(b) of the Companies Act sets out an important obligation that should be retained in the Companies Act. It however noted that the drafting of this section could be clarified, such that the reference to "other accounting records" is in line with section 199 of the Companies Act. This would give greater clarity to the meaning of the phrase "other accounting records".

Recommendation 4.19

Section 207(3)(b) of the Companies Act, which requires an auditor to form an opinion on whether proper accounting and other records (excluding registers) have been kept by the company, should be retained, but the drafting of that section should be clarified.

(d) Requirement to comment on consolidation procedures

60 Section 207(3)(d) of the Companies Act requires an auditor to form an opinion on whether the procedures and methods used by a holding company or a subsidiary in arriving at

the amounts taken into any consolidated accounts are appropriate to the circumstances of the consolidation.

61 None of the countries studied have an equivalent provision. The UK and Australian legislation are silent on the duty to report in respect of any aspect of consolidation of accounts, whilst the obligation in New Zealand just requires the auditor to state an opinion that the group accounts comply with generally accepted accounting practice and give a true and fair view[17]. One respondent opined that the proposal to repeal the section will align Singapore's practice with international best practices. On the other hand, there were comments that the requirement in section 207(3)(d) should be retained since stakeholders, investors and users of financial statements rely on the auditor to give an opinion on this and that it was not unduly onerous for the auditors to do so.

62 The Steering Committee is of the view that, in line with international practice, there is no need for an express requirement in the Companies Act for an auditor to form an opinion on the procedures and methods of consolidation. The auditors' opinion on whether the accounts comply with the accounting standards and are true and fair would give sufficient to assurance in respect of the consolidation procedures. As such, section 207(3)(d) of the Companies Act should be repealed.

Recommendation 4.20

The requirement for an auditor to form an opinion on the procedures and methods of consolidation in section 207(3)(d) of the Companies Act should be repealed.

(e) Requirement to report on fraud

63 Under section 207(9A) of the Companies Act, an auditor of a public company or a subsidiary of a public company who has reason to believe that a serious offence involving fraud or dishonesty[18] is being or has been committed against the company by officers or employees of the company, must immediately report the matter to the Minister for Finance.

64 From the definition of the phrase "a serious offence involving fraud or dishonesty" in section 207(9D) of the Companies Act, it would appear that the nature of the offences contemplated by the section are offences relating to acts where the fraud or dishonesty lead to the misappropriation of the property of the company. It does not appear to cover deliberate mis-statements of accounts (ie, accounting fraud).

65 Auditors are already required to deal with any material mis-statements of accounts in their audits. If the auditor detects a mis-statement (fraudulent or otherwise) during the course of the audit, the auditor would raise this to the company.

[17] Section 16(1) of the New Zealand Financial Reporting Act 1993.

[18] The phrase "a serious offence involving fraud or dishonesty" is defined in section 207(9D) of the Companies Act to mean —
(a) an offence that is punishable by imprisonment for a term that is not less than 2 years; and
(b) the value of the property obtained or likely to be obtained from the commission of such an offence is not less than $20,000.

66 If the mis-statement is not a case of fraud, and adjustments are made, there is no breach of accounting standards or Companies Act requirements. As the adjusted accounts are true and fair, there should also be no concern of the users of the accounts being misled.
67 On the other hand, if the management of the company agrees with the auditor that the transaction is suspicious and no adjustment is made, the financial effect of the suspicious transaction would be disclosed in the accounts (as is required under the SFRS), and users of the accounts would be put on notice. If the management of the company is not co-operative in disclosing the financial effect of the transaction in the accounts, the auditor would qualify his opinion, and if there is a breach of the provision of the Act which cannot be dealt with adequately in the auditors' report, will have to report this immediately to the Registrar of Companies under section 207(9)(a) of the Companies Act. A user of those accounts would therefore be put on notice that there is something irregular (at the very least) in respect of the accounts. The risk that shareholders/investors would be misled by the accounts is therefore reduced.

68 While the Steering Committee noted the views received during the consultation that the consequences of accounting fraud were serious and that auditors can exercise their professional judgment in assessing whether there are instances of accounting fraud, it noted that it may be difficult in practice for an auditor to determine from the circumstances of a mis-statement whether there is case of accounting fraud or if it is just a mistake.

69 Therefore, on balance, the Steering Committee is of the view that section 207(9A) should not be extended to include a requirement for an auditor to report on instances of suspected accounting fraud which he may come across in the course of the performance of his duties as auditor.

70 There was also a suggestion for an increase of the threshold stated in s207(9D), where "the value of the property obtained or likely to be obtained from the commission of such an offence" is used as the threshold to define a "serious offence involving fraud or dishonesty". The threshold amount had been set at $20,000 in 1989. The Steering Committee agreed that this was an area that needed to be addressed and proposed that the threshold level be raised to $250,000 as the appropriate amount to be considered a serious offence in current times.

Recommendation 4.21

Section 207(9A) should not be extended to include a requirement for an auditor to report on instances of suspected accounting fraud.

Recommendation 4.22

The amount stated in section 207(9D)(b) used as the threshold to define a "serious offence involving fraud or dishonesty", should be raised from $20,000 to $250,000.

VII. RESIGNATION OF AUDITORS

71 Section 205(14) and (15) of the Companies Act allow an auditor to resign only if he is not the sole auditor or at a general meeting, and where a replacement auditor is

appointed. This provision makes it difficult for an auditor to resign in a situation where the company which appointed it refuses to hold a general meeting or appoint a new auditor to replace the outgoing one. In contrast, in the UK and Hong Kong, the resignation of the auditor takes effect upon the company being notified or on a date specified in the resignation notice.

72 In line with the position in the UK and Hong Kong, the Steering Committee's view is to allow the auditor of a non-public-interest company (other than a subsidiary of a public company) to resign upon giving notice to the company.

73 The status quo should, however, be retained for the auditor of a non-public-interest company which is a subsidiary of a public-interest company, i.e. such a company's auditor may only resign if he is not the sole auditor or at a general meeting, and where a replacement auditor is appointed. A non-public-interest company which is a subsidiary of a public-interest company should be treated differently from other non-public-interest companies since the auditor of a public interest company is required to seek ACRA's consent before he can resign.

74 It is noted that ACRA would take an interest in the premature resignation of auditors of "public-interest entities". As such, the Steering Committee is of the view that where the company concerned is a public-interest company, the auditor may only resign with the consent of ACRA. This is similar in approach to that in Australia where resignation of auditors of non-proprietary companies[19] requires the consent of the Australian Securities and Investments Commission (ASIC)[20]. ASIC will only consent to the resignation where ASIC is satisfied that there are no disputes with the company management connected with the auditor ceasing to hold office and no concerns such as lack of independence of the audit or opinion shopping, and where the resignation is other than at an annual general meeting, that there are exceptional circumstances[21].

75 There was some feedback received that it would be onerous and unwieldy to wait for ACRA's approval for the resignation of an auditor of a public-interest company and notification of ACRA was suggested as an alternative. Another comment against the requirement for ACRA's consent was that auditors may resign on routine and commercial grounds which are of little interest to ACRA. There were also concerns with ACRA getting involved in disputes between the auditor and the company and doubts as to how ACRA would form a view on whether or not to consent. The Steering Committee noted these responses but took the view that in most instances, an auditor would be appointed from one annual general meeting to the next and that it would only be in unusual situations that the

[19] A proprietary company is a company which:

- is limited by shares or is an unlimited company with a share capital;
- has no more than 50 non-employee shareholders; and
- must not engage in any activity that would require disclosure to investors under Chapter 6D of the Australia Corporations Act 2001 (relating to public fundraising).

A non-proprietary company is a company other than a proprietary company.

[20] Section 329 of the Australia Corporations Act 2001.

[21] ASIC's Policy Statement 26. Examples of exceptional circumstances are:

(a) the failing health of the auditor;
(b) loss of independence of the auditor;
(c) the company is not audited by the auditor of its parent entity; or
(d) a relocation of the company's or auditor's principal place of business resulting in circumstances where it would be impractical for the auditor to perform the audit.

auditor would resign mid-term. In such instances, ACRA would be interested in the reasons for the auditors' resignation and an approval mechanism would allow ACRA to stop the resignation where such resignation is not appropriate. It is likely that ACRA would adopt an approach similar to that in Australia in terms of the circumstances under which ACRA would grant consent.

76 The determination of what constitutes a "public-interest company" would follow a similar concept to that used for the purposes of the Practice Monitoring Programme conducted by ACRA[22]. The details as to what are the exceptional situations under which an auditor of a public-interest company may resign could be stated in a Practice Direction issued by ACRA.

77 A further issue considered was whether the resigning auditor should be required to disclose to the shareholders of the company the reasons for its resignation before the AGM. In the UK and Hong Kong, there is an express provision which requires a resigning auditor to state the circumstances of his resignation or if there are none, a statement of that fact. The statement of circumstances of the auditor's resignation would be given to the company unless a court has determined that the auditor is using the process to secure needless publicity for a defamatory matter[23]. In New Zealand, the resigning auditor must distribute to the shareholders a statement of the reasons for his resignation[24]. No distinctions are made in these countries between public-interest or non-public-interest companies. In Australia, the auditor of a non-proprietary company must state the reasons for his resignation in his application to ASIC for consent to the resignation. While the reasons are not disseminated to the company, ASIC will only grant consent if it is satisfied that there are no issues of concern to the company.

78 The Steering Committee took the view that the Companies Act need not expressly provide for disclosure of reasons by the auditor of a non-public interest company. While there was feedback received that the auditor should provide to the shareholders of the company the reasons for their resignation as a matter of transparency and accountability, the Steering Committee noted that there may be some concerns with defamation, and that the shareholders could request the information from the company where necessary.

79 For a public-interest company, there would also be no need for a requirement in the Companies Act for disclosure to be made to the shareholders where the company is regulated specifically under other rules and requirements, and would have to comply with other disclosure obligations (e.g. the listing manual), as such other disclosure requirements would be sufficient.

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[22] A "public-interest entity" for the purposes of the Practice Monitoring Programme is:-
(a) a company listed on the Singapore Stock Exchange;
(b) a company in regulated industries such as banks and insurance companies; or
(c) any other entity which raise funds from the public, such as charities.

[23] Section 520 of the UK Companies Act 2006; section 140A of the Hong Kong Companies Ordinance.

[24] Section 203(1) of the New Zealand Companies Act 1993.

Recommendation 4.23

The auditor of a non-public-interest company (other than a subsidiary of a public-interest company) should be allowed to resign upon giving notice to the company.

The status quo should be retained for the auditor of a non-public-interest company which is a subsidiary of a public interest company, viz, such a company's auditor may only resign if he is not the sole auditor or at a general meeting, and where a replacement auditor is appointed.

Recommendation 4.24

The auditor of a public-interest company should be required to seek the consent of ACRA before he can resign.

Recommendation 4.25

There is no need for an express requirement for an auditor to disclose to the shareholders of the company that appointed it the reasons for his resignation.

VIII. AUDITOR'S INDEPENDENCE

80 The current Companies Act includes some specific provisions relating to independence of auditors under section 10(1)[25]. This area is also dealt with in the Code of Professional Conduct and Ethics as set out in rules under the Accountants Act[26].

81 In Australia, provisions relating to auditor's independence are included in the Australia Corporations Act 2001. In the UK, auditor's independence requirements are largely prescribed by professional bodies as codes of conduct. In New Zealand, the Companies Act 1993 requires an auditor of a company to ensure, in carrying out the duties of an auditor, that his or her judgment is not impaired by reason of any relationship with or interest in the company or any of its subsidiaries[27].

82 The Code of Professional Conduct and Ethics prescribed under the Accountants (Public Accountants) Rules provides greater detail as to the requirements for independence than what is set out in section 10 of the Companies Act in respect of company auditors. The Steering Committee is of the view that all the provisions relating to independence of auditors could be consolidated in the rules under the Accountants Act, so as to reduce duplication in legislation on this issue. Moreover, the Code of Professional Conduct and Ethics would be of more general application, whereas the provisions in the Companies Act would only relate to company auditors.

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[25] Section 10(1) of the Companies Act lists certain restrictions on a person being appointed as an auditor of a company, amongst which there are criteria relating to his independence. Section 206(1A) of the Companies Act requires a public company, under certain circumstances, to undertake a review of auditors' fees to determine whether the independence of the auditor has been compromised.

[26] Fourth Schedule to the Accountants (Public Accountants) Rules.

[27] Section 204 of the New Zealand Companies Act 1993.

83 However, one member of the Steering Committee expressed the view that the requirement for an independent audit of the accounts of a company is a consequence of incorporation and hence the requirement for an auditor's independence from the company should conceptually remain in the Companies Act rather than be moved to the Accountants Act. One of the respondents to the consultation also added that a requirement for independence under the Companies Act is a form of good corporate governance to protect the reliability and integrity of the financial statements of companies.

Recommendation 4.26

The provisions relating to auditor independence in section 10 of the Companies Act should be consolidated under the Accountants Act.

IX. LIMITATION OF AUDITOR'S LIABILITY

84 A review of the practices in the United States (US), the UK, Australia and certain European Union (EU) countries was carried out in respect of the regulatory provisions dealing with the limitation or apportionment of liability of auditors. Notably, reform to the auditor-liability regime has been made in the UK in their Companies Act 2006, which allows auditors to limit their liability through contractual agreements or "liability limitation agreements". In the US, the Private Securities Litigation Reform Act 1995 adopts the principle of proportionate liability (which divides the plaintiff's loss among the defendants according to their share of responsibility), but does not specifically limit the liability of auditors for class action suits.

85 Provisions relating to the limitation or apportionment of auditors' liability seek to address the impact of a major suit against a large audit firm on the market and business community. It is observed that the main reason why auditing firms were brought down (such as Arthur Anderson in the Enron case) was the negative impact on their reputation rather than their involvement in litigation. A further observation is that the US is more litigious and the damages awarded in US are usually higher than in Singapore, and therefore the concerns surrounding auditor liability in the US may not be applicable in Singapore.

86 It is further noted that in the US, audit fees and a cap of liabilities are often used as bargaining terms in audit engagements. In Singapore, however, audit fees are generally lower, and therefore there is less incentive for any agreement for a cap on liability. However, Singapore should keep pace with the developments in other countries in this area and ACRA will continue to monitor this issue.

87 Some respondents to the consultation expressed the view that if limitations to liability are not imposed, this may put Singapore accountants at a disadvantage and would encourage fewer accountants to take up partnership roles in Singapore. Those not in favour of a statutory limitation, on the other hand, felt that auditor liability should be determined by the courts and that the auditors already had the protection of professional indemnity insurance.

88 The Steering Committee considered the feedback received and concluded that on balance, there was no pressing need to statutorily provide for a limitation of auditor's liability

at the moment. However, noting that Singapore should not fall behind other jurisdictions on this issue, ACRA should monitor the developments in this area.

Recommendation 4.27

There is no need to introduce statutory provisions on the limitation of liability of auditors at this time, but the issue will be monitored by ACRA.

X. INDEMNITY FOR AUDITORS UNDER SECTION 172 OF COMPANIES ACT

89 Section 172(1) of the Companies Act states that any provision, whether in the articles or in a contract or otherwise, indemnifying any officer or auditor against any liability for negligence, default, breach of duty or breach of trust in relation to the company is void.

90 Section 172(2)(b) of the Companies Act does not prevent a company from indemnifying any officer or auditor against any liability incurred by him:

(i) in defending any proceedings (civil or criminal) in which judgment is given in his favour or in which he is acquitted; or

(ii) in connection with any application under section 76A(13) or section 391(2) or any other provision of the Companies Act, in which relief is granted to him by the court.

91 The review of these provisions in respect of directors was considered separately. The Steering Committee suggested that section 172 be amended to expressly allow a company to provide indemnity against liability incurred by its directors to third parties.

92 Australia and Hong Kong, like Singapore, have a single provision governing indemnities of both officers/directors and auditors. The UK has separate provisions governing indemnities for directors and auditors, while New Zealand only has provisions in relation to directors.

93 One respondent pointed out that auditors may manage their risks against claims for negligence, error/omission, misrepresentation and any other form of professional negligence by taking out adequate professional liability insurance to cover any third party liabilities arising from auditors' acts, negligence or omissions in their capacity as auditors. Another comment received was that a company should not be allowed to indemnify auditors for claims brought by third parties as the auditor is not an employee of the company nor is he an officer of the company, unlike a director. A further view was that allowing the company to indemnify its auditors may compromise the independence of the auditors.

94 On the other hand, other respondents favoured allowing a company to indemnify its auditors for qualifying claims brought by third parties, as is allowed under the legal frameworks in Australia and New Zealand.

95 The Steering Committee takes the view that an auditor should not be treated in the same way as a director, given that he is not an officer or employee of the company and is appointed to carry out an independent review of the accounts. On that basis, the Steering Committee is unwilling to extend the extension of scope of protection for directors in respect of indemnification for claims brought by third parties to auditors.

96 The Steering Committee also considered and accepted a proposal to amend section 172(2)(b) to clarify that a company is allowed to indemnify its directors against potential liability[28]. On this issue, the Steering Committee agrees that the indemnity in respect of auditors in section 172(2)(b) of the Companies Act can be extended to liabilities which are to be incurred.

Recommendation 4.28

A company should not be expressly allowed to indemnify auditors for claims brought by third parties.

Recommendation 4.29

The drafting of section 172(2)(b) of the Companies Act should be amended to clarify that a company is allowed to indemnify its auditors against potential liability.

XI. AUDIT COMMITTEE PROVISIONS

97 Section 201B of the Companies Act provides a statutory requirement for listed companies to have an audit committee and sets out the composition and duties of such committees. Part of the functions of audit committees and the establishment of other listed company committees are set out in the Code of Corporate Governance.

98 In line with the strategy towards streamlining the Companies Act to contain only core company law, the Steering Committee considered whether to retain this requirement in the Companies Act.

99 The Steering Committee noted that the provisions relating to audit committees only apply to listed companies. There was feedback received from the consultation that there is no compelling reason to move the provisions and that retaining the provisions in the Companies Act will facilitate the possibility in future, if determined necessary, to extend them to non-public companies. However, the Steering Committee took the view that as the bulk of the requirements relating to audit committees are set out in the Code of Corporate Governance, the requirement for an audit committee should be moved out of the Companies Act.

[28] There appears to be some uncertainty as to whether the use of the word "incurred" in section 172(2)(b) is wide enough to cover potential liability. The concern is that the restrictions on a company's power to make loans to its directors have prevented companies from lending money to its directors on a "to be incurred" basis even to pay for his legal expenses.

100 The Steering Committee recognised that there is value in retaining the audit committee as a statutory committee in that failure to comply with the requirements in a statute would attract penalties. The suggestion is therefore that the provisions should be more appropriately located under the Securities and Futures Act or some other Act pertaining only to listed companies.

Recommendation 4.30

The provisions relating to audit committees should be moved to the Securities and Futures Act.

XII. ACCOUNTING RECORDS AND SYSTEMS OF CONTROL

(a) Keeping of accounting records

101 Section 199(1) of the Companies Act requires every company to keep such accounting and other records as are necessary to explain the transactions and financial position of the company and to allow a profit and loss account and a balance-sheet to be prepared. This obligation is cast expressly upon the directors and managers of the company. A similar duty is imposed on directors in the UK, Australia, New Zealand and Hong Kong.

102 This obligation was reviewed by the Directors' Duties Study Team (DDST), led by the Accounting and Corporate Regulatory Authority (ACRA) and comprising industry professionals, representatives of professional bodies and regulators separately. The DDST had separately reviewed the provisions in the Companies Act which set out or affect duties and responsibilities of directors. The DDST opined that this duty of directors is still relevant today and found that section 199(1) is adequate.

103 The DDST also considered that in some overseas jurisdictions, the law provided some details on what accounting records should be kept for the purposes of fulfilling the obligation[29]. The DDST took the view that it would not be possible or desirable to provide a comprehensive list of the type of accounting records that are to be kept. It felt that the existing requirement for accounting and other records to be kept in order to sufficiently explain the transactions and financial position of the company, and to enable the preparation

[29] In the UK, section 386 of the UK Companies Act 2006 states that accounting records must contain: (i) entries from day to day of all sums of moneys received and expended by the company and the matters in respect of which the receipt an expenditure takes places; and (ii) record of assets and liabilities of company. In New Zealand, the accounting records must contain —

(a) Entries of money received and spent each day and the matters to which it relates;

(b) A record of the assets and liabilities of the company;

(c) If the company's business involves dealing in goods —

(i) a record of goods bought and sold, except goods sold for cash in the ordinary course of carrying on a retail business, that identifies both the goods and buyers and sellers and relevant invoices;

(ii) a record of stock held at the end of the financial year together with records of any stocktakings during the year;

(d) If the company's business involves providing services, a record of services provided and relevant invoices.

(Section 194(2) of the New Zealand Companies Act 1993).

of true and fair profit and loss accounts and balance-sheet, already provides the scope and principles for such record keeping. The DDST concluded that the test for the adequacy of the accounting and other records to be kept is rightly based on the principle that true and fair financial statements could be prepared from those records.

104 The Steering Committee agreed with the DDST's recommendations and is of the view that the duty of directors to keep accounting and other records as provided in section 199(1) should be retained as currently drafted.

105 The general view from most of the respondents to the consultation was that there was no need to change the provision in section 199(1).

Recommendation 4.31

The directors' duty to keep accounting and other records in section 199(1) does not require amendment.

(b) Devising and maintaining system of internal controls

106 Section 199(2A) of the Companies Act requires every public company and its subsidiaries to devise and maintain a system of internal accounting controls sufficient to provide a reasonable assurance that:

(a) assets are safeguarded against loss from unauthorised use or disposition; and

(b) transactions are properly authorised and that they are recorded as necessary to permit the preparation of true and fair profit and loss accounts and balance-sheets and to maintain accountability of assets.

107 This legal requirement for internal controls for public companies and their subsidiaries was introduced via the Companies (Amendment) Act 1989, in which a number of amendments were aimed at strengthening the statutory means to prevent and detect company fraud. The requirement was reviewed by the DDST and its recommendations have been considered by the Steering Committee.

108 One issue is whether the legal requirement to devise and maintain a system of internal controls should be extended to private companies.

109 On the one hand, since all companies are required to prepare financial statements that are true and fair, all companies should have internal controls in order to ensure the credibility of the financial statements to be prepared. Further, it may be difficult for the auditors to convey to the directors of private companies that they have the responsibility to ensure that the companies have sound internal controls, if the legislation does not expressly provide for such a duty or responsibility. Without internal controls, it would be difficult for the auditors to give an opinion on whether the financial statements are true and fair. In addition, a system of internal controls does not necessarily mean an elaborate system of internal controls. Therefore, private companies should not have difficulty complying with such a legal requirement.

110 Respondents to the consultation also had the following comments in support of the imposition of an express obligation on private companies –

(a) If a sizeable group of private companies is going to be exempted from audit under the proposed small company regime, there would be an even greater need for private companies to have internal controls.

(b) The absence of a provision in the Companies Act for private companies may be misinterpreted as meaning that there is no requirement for internal controls for private companies.

111 On the other hand, there may be no need to impose such a legal obligation on private companies, especially when the users of smaller private companies' financial statements are limited. The number of investors who would be affected by the financial situation of the smaller private companies is also limited. Further, imposing a legal obligation on private companies to have a system of internal controls may lead to an increase in compliance cost. The directors of such companies may perceive the express requirement in law as a "stricter duty" than the present situation. Hence, private companies may think that there is a need to separately engage professionals to advise them whether the internal controls maintained by them are adequate, since non-compliance would be an offence.

112 In the case of larger private companies which have more stakeholders, even if there is no express legal requirement imposed on the companies, the auditors who are not satisfied with the internal accounting controls of private companies and opined that this affects the credibility of the financial statement of the company can qualify the company's financial statements. Market forces would then intervene and cause the company to look into its internal controls. ACRA as the corporate regulator would also step in to investigate, where warranted.

113 It is noted that it would be more desirable to let the market drive corporate behaviour, unless there is a compelling need for the law to provide for regulation to protect public interest which is not the case here. There is also no similar legal requirement in the other major jurisdictions. If Singapore decides to impose the legal requirement on private companies, it may lead to over-regulation and an increase in business costs.

114 Respondents to the consultation also highlighted that duties in a private company cannot practically be segregated in a small family-run company with only a few shareholders/ directors, or single-director companies, making it difficult for such a company to comply with formal internal accounting controls.

115 One of the Steering Committee members highlighted that with the change in the Companies Act which allows even private companies to raise funds from the public, there is now less of a distinction between private companies and public companies. He highlighted that at the time section 199(2A) CA was drafted, the law still permitted only public companies to raise funds from the public. Since the distinction had since been removed, the rationale of balancing the costs and benefits of a mandatory requirement for internal accounting controls should equally apply to both public and private companies of a significant size.

116 Although a private company may be able to solicit a significant amount of funds from the public while not being subjected to the mandatory requirement to maintain internal accounting controls, it is noted that there is still an over-arching directors' duty under section 157 CA to use reasonable diligence to carry out their duties diligently, which would include ensuring sufficient internal accounting controls to facilitate the preparation of proper accounts.

117 Moreover, using the size of the company as the criteria to determine the mandatory requirement would make it difficult for a director to determine at any one point in time what his obligation was, as the size of the company may vary within short periods of time. Having a size test would also present difficulties in enforcement as it would be difficult to determine at what point in time the obligation was mandatory and whether a breach had occurred.

118 On balance, the Steering Committee takes the view that it may to amount over-regulation to impose a mandatory requirement on private companies for which failure to comply would constitute an offence. It, however, recognises that it is important for directors of private companies to be aware of the need for internal accounting controls, so there must be promotion of awareness in this respect. To avoid the public misconception that private companies do not require internal controls, some form of non-statutory guidance should be given.

Recommendation 4.32

The requirement under section 199(2A) for a public company to devise and maintain a system of internal controls need not be extended to private companies.

Recommendation 4.33

Any misconception that private companies currently do not require internal controls should be corrected through non-statutory guidance.

119 Another issue that has been considered is whether it would be necessary to extend the legal requirement under section 199(2A) to the associated companies and related companies of public companies. The Steering Committee notes that as directors of a public company have no control over its associated companies and related parties, the legal requirement to devise and maintain internal controls should not be extended to the associated companies and related parties. This view was generally supported by the consultation feedback.

Recommendation 4.34

The requirement under section 199(2A) for a public company and its subsidiaries to devise and maintain a system of internal controls need not be extended to the associated companies and related companies of a public company.

XIII. COMPONENTS OF STATUTORY ACCOUNTS

120 Currently, the Companies Act requires the preparation of true and fair balance-sheets and profit and loss accounts[30]. It does not provide for the other components of accounts, namely the cash flow statement, statement of changes in equity, accounting policies and explanatory notes. Furthermore, under the current Companies Act provision, there is no requirement for the components of the accounts other than the profit and loss account and the balance-sheet to be "true and fair". There is also no express requirement that these other components be filed with the Registrar of Companies together with the annual return[31].

121 The Steering Committee is of the view that components of the accounts in the relevant provisions in the Companies Act should be clarified by referring to the definition of accounts contained in the Singapore Financial Reporting Standards (SFRS). This is similar to the position in the Australia Corporations Act 2001, which defines "financial statements" as the financial statements in relation to the entity reported on that are required by the accounting standards[32].

122 The SFRS has a clear definition in paragraph 10 of FRS1 as to what comprises a full set of accounts:

(a) a statement of financial position as at the end of the period;

(b) a statement of comprehensive income for the period;

(c) a statement of changes in equity for the period;

(d) a statement of cash flows for the period;

(e) notes, comprising a summary of significant accounting policies and other explanatory information; and

(f) a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

123 The preference is for a revised definition which refers to the components set out in the SFRS rather than to list the various components expressly in the Companies Act, so that if there are changes to the components in the SFRS, it would not be necessary to make subsequent amendments to the Companies Act. One member of the Steering Committee, however, was of the view that the definition of "accounts" should be retained in the Companies Act.

124 Most of the respondents agreed with the majority view of the Steering Committee.

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[30] See section 201(1A), (3) and (3A) of the Companies Act.

[31] Regulation 38 of the Companies (Filing of Documents) Regulations requires a company to file the profit and loss accounts, the balance-sheet, the directors' report and statement, the auditors' report and the notes to the accounts together with the annual return.

[32] Section 295 of the Australia Corporations Act 2001.

Recommendation 4.35

The components of the accounts in the relevant provisions in the Companies Act should be clarified by referring to the definition of "accounts" contained in the SFRS.

XIV. PRESENTATION OF THE ACCOUNTS

125 The DDST reviewed the current duties on directors in respect of the requirement to lay accounts at the annual general meeting under section 201(1) of the Companies Act, and to send a copy of the accounts to all persons entitled to receive notice of general meetings under section 203(1).

126 The DDST agreed that these existing legal duties of directors were still relevant and recommended that no amendments to the corresponding statutory provisions are necessary. The Steering Committee agrees with these recommendations.

127 Most of the respondents also agreed with these views.

Recommendation 4.36

The directors' duties in section 201 to lay the financial statements before the company at every annual general meeting and to ensure that the financial statements are audited do not require amendment.

Recommendation 4.37

The directors' duty in section 203(1) to send to all persons entitled to receive notice of general meetings a copy of the company's profit and loss account and balance-sheet does not require amendment.

XV. FRAMEWORK FOR CONSOLIDATION OF ACCOUNTS

(a) Determination of which entity needs to prepare consolidated accounts

128 Currently the definitions under section 5 of the Companies Act[33] and FRS 27[34] in respect of the term "holding company" and "parent" respectively are similar but not identical.

[33] Section 5 of the Companies Act defines when a holding company - subsidiary relationship exists. A holding company is defined as a company which:
(a) controls the composition of the board of directors of subsidiary;
(b) controls more than half of the voting power of subsidiary; or
(c) owns more than half of issued share capital of subsidiary (not counting preference shares).
[34] Under FRS 27 of the Singapore Financial Reporting Standards, a "parent" is required to present consolidated accounts in which it consolidates its investments in subsidiaries. A "parent" is defined as an entity that has one

As a result, a company may meet the definition "subsidiary" or "holding company" under the Companies Act but not the accounting definition of "subsidiary" or "parent" under FRS 27. For example, a company may own more than half of the issued share capital of another company but may not control its financial and operating policies. Under section 5 of the Companies Act, such a company is a subsidiary whereas under FRS 27, it is not.

129 In Australia, the obligation to consolidate accounts is located in the accounting standards rather than spelt out in the Corporations Act 2001. The obligation for a company to consolidate accounts is indirectly given the force of law by virtue of section 296 of the Australia Corporations Act 2001, which requires entities to comply with the accounting standards. In the UK, the Companies Act 2006 specifically defines "parent undertaking" and "subsidiary undertaking" for the purposes of the sections relating to the preparation of accounts, which are similar to the definition of the parent-subsidiary relationship in the accounting standards. New Zealand has a specific Financial Reporting Act which defines "subsidiary" consistently with the definition in the accounting standards. The New Zealand Companies Act 1993 has a separate definition of the term "subsidiary".

130 The Steering Committee is of the view that the determination of which companies should prepare consolidated accounts should be aligned and determined by the financial reporting standards. This is similar to the approach in Australia and is consistent with the earlier suggestion to clarify the components of the accounts in the relevant provisions in the Companies Act by referring to the definition of "accounts" contained in the SFRS. Section 5 of the Companies Act can continue to remain for the purposes of other sections in the Companies Act. This approach would minimise future alignment issues if and when the definitions in the accounting standards change, which may be the disadvantage if the UK approach is adopted.

131 No differing views were received from the consultation feedback.

Recommendation 4.38

The determination of whether a company should prepare consolidated accounts should be set by only the financial reporting standards and not the Companies Act.

(b) Alignment of financial year-end of subsidiary and parent

132 In general, the directors of a holding company must take steps to ensure that the financial years of each of its subsidiaries coincides.[35] For foreign subsidiaries, under section 200(2A) of the Companies Act, the financial year of a foreign subsidiary must end on a date not earlier than 2 months before the end of the financial year of the holding company, while the difference between the reporting date of a subsidiary and that of its parent can be up to 3 months under the FRS 27.[36] Where a company has foreign subsidiaries, there appears to be a

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or more subsidiaries and a "subsidiary" is an entity, including an unincorporated entity such as a partnership, which is controlled by another entity. "Control" is defined in FRS 27 as the power to govern the financial and operating policies of the other entity so as to obtain benefits from its activities.

[35] Section 200(1) of the Companies Act.

[36] Paragraphs 26 and 27.

mismatch between the requirements in section 200(2A) of the Companies Act and those in the FRS 27.

133 Both the UK and Australia have statutory provisions which require alignment of the financial year-ends of a parent and its subsidiaries. In Australia, there is a general exemption power which allows the Australian Securities and Investments Commission (ASIC) to grant relief from the requirement.[37] In the UK, the financial year-ends of a parent company and a subsidiary undertaking need not be aligned where in the directors' opinion there are good reasons against it.[38] If the financial year of a subsidiary undertaking included in the consolidation does not end with that of the parent company, the group accounts must be made up:

(a) from the accounts of the subsidiary undertaking for its financial year last ending before the end of the parent company's financial year, provided that year ended no more than 3 months before that of the parent company; or

(b) from interim accounts prepared by the subsidiary undertaking as at the end of the parent company's financial year.[39]

134 In New Zealand, the balance date of a subsidiary may precede the balance date of the reporting entity.[40] If so, a subsidiary's balance date must be not more than 3 months earlier than its parent. Otherwise, interim accounts must be prepared in respect of the period that is the same as the accounting period of the parent.[41]

135 The Steering Committee is of the view that the alignment of the financial year-end of a parent company and its subsidiaries should be determined by the SFRS, rather than specified in the Companies Act.

136 Most of the respondents agreed with the views of the Steering Committee.

Recommendation 4.39

The requirements for alignment of the financial year-end of a parent company and its subsidiaries should be set in accordance with the financial reporting standards.

XVI. REVISION OF DEFECTIVE ACCOUNTS

137 ACRA has noted a need for an alternative enforcement action where defective accounts are detected. Currently, the only enforcement action available where there is non-compliance with the accounting standards and the statutory requirements relating to accounts is to prosecute the directors of the company for an offence under section 204 of the

[37] Section 340 of the Australia Corporations Act 2001.
[38] Section 390(5) of the UK Companies Act 2006.
[39] Schedule 6, rule 2(2) of the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 and the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.
[40] Section 7(11) of the New Zealand Financial Reporting Act 1993.
[41] Section 14(4) of the New Zealand Financial Reporting Act 1993.

Companies Act. An express procedure which allows ACRA to require a company to revise its defective accounts where such defects had been detected could serve as a complementary enforcement action.

138 The UK, Hong Kong and Australia have regimes in which the regulatory authority which conducts surveillance of compliance with statutory requirements for accounts refers the matter to a separate authority (either a court or an independent panel) for adjudication of non-compliance for the purpose of requiring the company to revise its accounts. In the US, while cease and desist orders (which may include an order to rectify defaults) are issued by the US Securities Exchange Commission (SEC), matters regarding non-compliance are heard and determined by administrative law judges within the US SEC before such an order is issued. There is currently no provision in respect of mandating revision of accounts in New Zealand.

139 There was feedback received that referring non-compliance matters to the courts slows down the revision process considerably and may result in revisions that are not timely. The suggestion was therefore to grant authority such as ACRA the power to require companies to make such revisions. However, it would not be appropriate for ACRA to act both as the regulator and the adjudicator, unless an independent body can be established within ACRA to adjudicate the issue. The Steering Committee considered that referring the case through the court system, which was well established, would be preferred.

140 The Steering Committee therefore is of the view that the most appropriate regulatory framework to adopt in Singapore is that similar to the UK. In Singapore's context, this would entail ACRA bringing proceedings for determining a breach requiring revision of accounts to the court, and the determination of whether an order for revision of the accounts is made is decided by the court.

141 Jurisdictions such as the UK and Hong Kong also have provisions relating to the voluntary revision of accounts in their respective legislation. Currently, there is no express provision in the Companies Act which allows a company to voluntarily revise its accounts. There is value in including a provision relating to voluntarily revision, as it would allow diligent directors of a company to revise the accounts of the company on their own accord before the accounts in respect of the next financial period are prepared.

142 Directors may choose to voluntarily revise the company's accounts if there are errors in their company accounts. This may especially be so if they are concerned with reputation risk or possible civil liability where stakeholders of the company place reliance on an error not corrected by the company, apart from any concern that ACRA may take action against the directors under the Companies Act. A provision for voluntary revision would allow the directors to correct the error at an earlier opportunity than in the next year's accounts if the directors of a company so wish to do so. No differing views were received on this issue from the consultation feedback.

<u>Recommendation 4.40</u>

A regulatory framework similar to that in the UK should be adopted for the purposes of requiring the revisions of defective accounts, i.e. the determination of whether an order for revision of defective accounts is made is decided by the courts.

<u>Recommendation 4.41</u>

Provisions for the voluntary revisions of defective accounts should be introduced in Singapore.

SUMMARY TABLE OF FINANCIAL REPORTING OBLIGATIONS

	(1) Preparation of accounts	(2) Requirement for audit	(3) Filing of accounts
(A) Full requirement	All types of companies other than (1)(C)	All types of companies other than (2)(C)	All types of companies other than (3)(B) and (3)(C)
(B) Reduced requirement	N.A.	N.A.	A small company must file basic financial information (see Recommendation 4.5)
(C) Exempted	A dormant[i] non-listed company (other than a subsidiary of listed company), subject to the substantial asset threshold test (see Recommendations 4.6 & 4.11) The directors of a dormant non-listed company so exempted must lodge an annual declaration of dormancy.	(i) A small company[ii] (see Recommendation 4.1), subject to (ii) below. (ii) A subsidiary which is a member of a group of companies may be exempt from audit as a small company only if the entire group to which it belongs qualifies on a consolidated basis for audit exemption under the small company criteria (see Recommendation 4.3) (iii) A dormant listed company, a dormant non-listed subsidiary of a listed company, a dormant non-listed company which exceeds the substantial asset threshold test. (see Recommendations 4.8 & 4.9) (iv) A company not required to prepare accounts under (1)(C).	(i) A company which is one of the following, and is solvent: (a) a private company wholly-owned by the Government, which the Minister, in the national interest, declares by notification in the Gazette to be exempt; (b) a private company falling within a specific class prescribed by the Minister as being exempt (e.g. specific industries where confidentiality of information is critical and public interest in the accounts is low); (c) a private company exempted by the Registrar upon application on a case-by-case basis and published in the Gazette. (see Recommendation 4.5) (ii) A company not required to prepare accounts under (1)(C).

[i] A company is taken to be dormant during a period where no accounting transaction occurs (Section 205B(2) CA). A list of transactions that are disregarded as accounting transactions are set out under section 205B(3) CA. This list is proposed to be extended to include statutory fees/fines under any Act and nominal payments/receipts (see Recommendation 4.10).

[ii] A company would qualify as a small company is it is a private company and fulfils two of the following criteria:

(a) Total annual revenue of not more than S$10 million;

(b) Total gross assets of not more than S$10 million;

(c) Number of employees not more than 50.

(see Recommendation 4.1)