

SAAC Singapore
Accountancy And Audit
Convention Series



PRACTITIONERS CONFERENCE

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Tuesday, 29 October 2019



2019 Audit Hot Spots

- **Audit implications arising from changes in Financial Reporting Standards**
 - FRS 116/ SFRS(I) 16 *Leases*
 - INT FRS 123/ SFRS(I) INT 23 *Uncertainty over Income Tax Treatments*
- **SSA 540 (Revised) *Auditing Accounting Estimates and Related Disclosures***
- **Key Audit Reminders**

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Key changes in Financial Reporting Standards and its audit implications

Effective from annual reporting period beginning on or after 1 January 2019

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FRS 116/ SFRS(I) 16 *Leases*

Applicable for annual reporting period beginning on 1 January 2019

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FRS 116/ SFRS(I) 16 *Leases*

Scope

- Similar to FRS 17 (applies to contracts meeting definition of a lease)

Recognition

- For lessee, most leases will be recognised on balance sheet with narrow exemptions (i.e. low value or short-term)
- For lessor, remains substantially unchanged from FRS 17

Transition

- Full retrospective; or
- Retrospective application without restatement of prior year comparatives (“modified retrospective”)

Implications for lessee

FRS 116/ SFRS(I) 16

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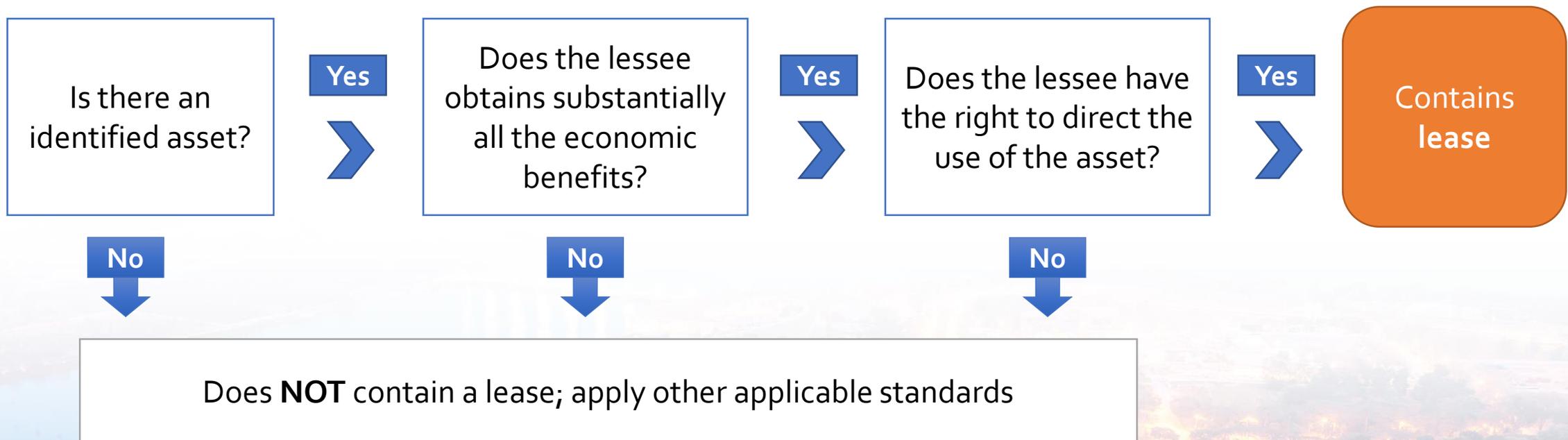


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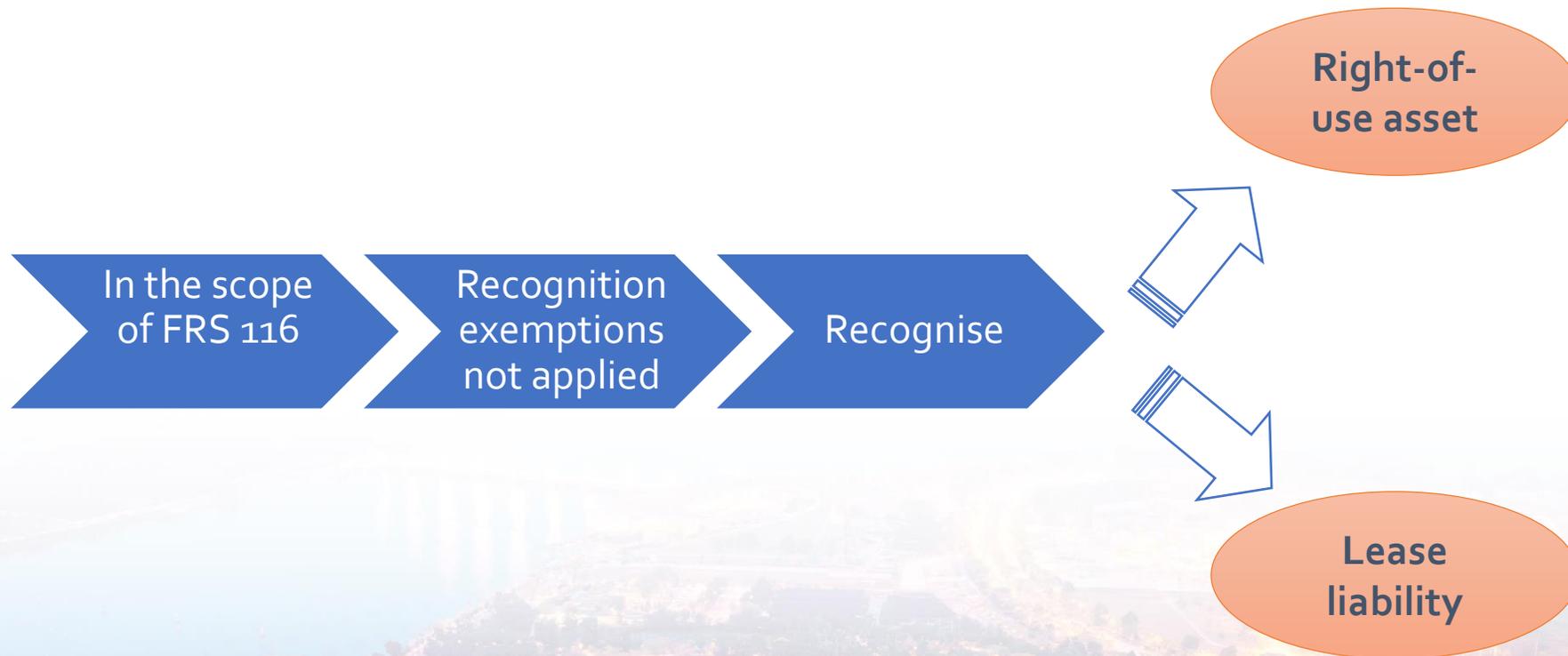


Identifying a lease

Lease = "A contract, part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration"

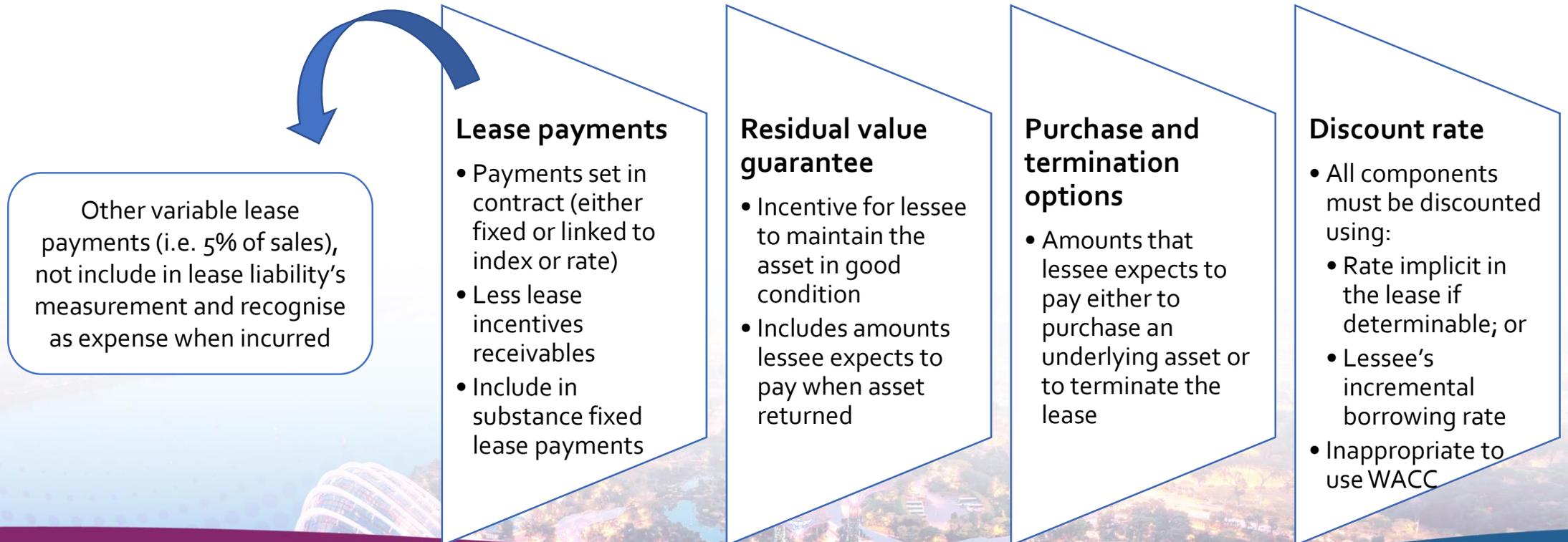


Recognition and Measurement – Lessee's perspective



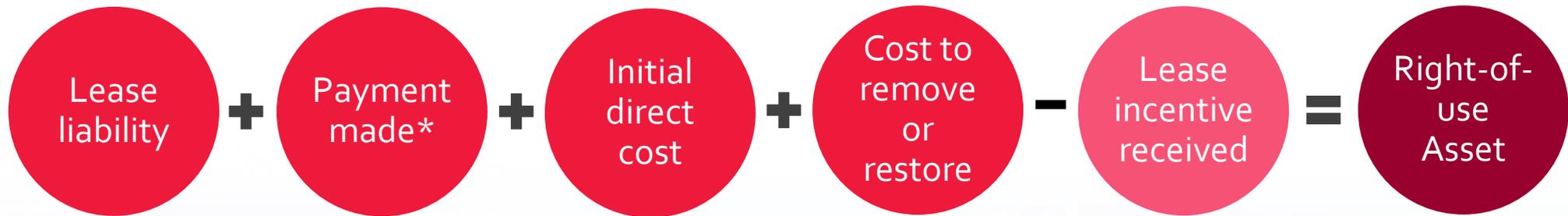
Recognition and Measurement – Lease liability

- Measurement of lease liability consists of the following components:



Recognition and Measurement – Right-of-use asset

- Measurement of right-of-use asset is based on the lease liability and some additional adjustments as below:



** Lease or other payment made either at or prior to commencement date*

Transition

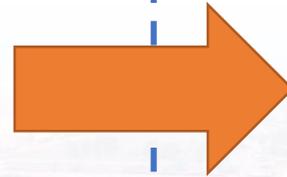
Full retrospective method	Modified retrospective method
Comparatives restated	Comparatives not restated
Cumulative effect recognised as adjustment to opening equity at the start of the earliest comparative period presented	Cumulative effect recognised as adjustment to opening equity at the start of the current period ('date of initial application')
3 rd statement of financial position presented at start of comparative period	No need of 3 rd statement of financial position
N/A	Two approaches for calculating RoU asset on a lease by lease basis: (i) equal to lease liability before DIA; or (ii) as if FRS 116 had always been applied
Limited transitional relief	Extensive transitional relief

Practical expedient – Definition of lease

Available for all transition methods

Date of initial application (start of current period of adoption)

May apply FRS 17 and INT FRS 104 definition to existing contracts



Must apply FRS 116 definitions to new lease contracts

Other practical expedients

– Only available for modified retrospective

#1: Apply a single discount rate to a portfolio of leases with reasonably similar characteristics

#2: Use onerous lease assessment and any provision recognised immediately before date of application instead of an FRS 36 impairment test

#3: Exclude initial direct costs from the measurement of right-of-use assets at the date of initial application

#4: No requirement to recognise leases when the term ends within 12 months of the date of initial application

#5: Use hindsight for judgements and estimates, such as in determining the lease term, if the contract contains options to extend or terminate the lease

Are your clients ready? Implications to our audit?

Completeness
of leases
identified

Management's
judgement –
Lease term

Management's
estimates -
Discount rate

Transition
method

Group audits

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INT FRS 123/ SFRS(I) INT 23

Uncertainty over Income Tax Treatments

Applicable for annual reporting period beginning on 1 January 2019

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INT FRS 123/ SFRS(I) INT 23 *Uncertainty over Income Tax Treatments*

- Transitional provisions available:
 - Retrospectively (restating comparatives) by applying FRS 8, if that is possible **without use of hindsight**; or
 - Retrospectively by adjusting the impact through retained earnings at the date of initial application (not restating comparatives)
- Tax treatment refers to the treatments used by an entity or that it plans to use in its income tax filings
- Uncertain tax treatment is a tax treatment for which there is uncertainty over whether the relevant taxation authority will accept the tax treatment under tax law

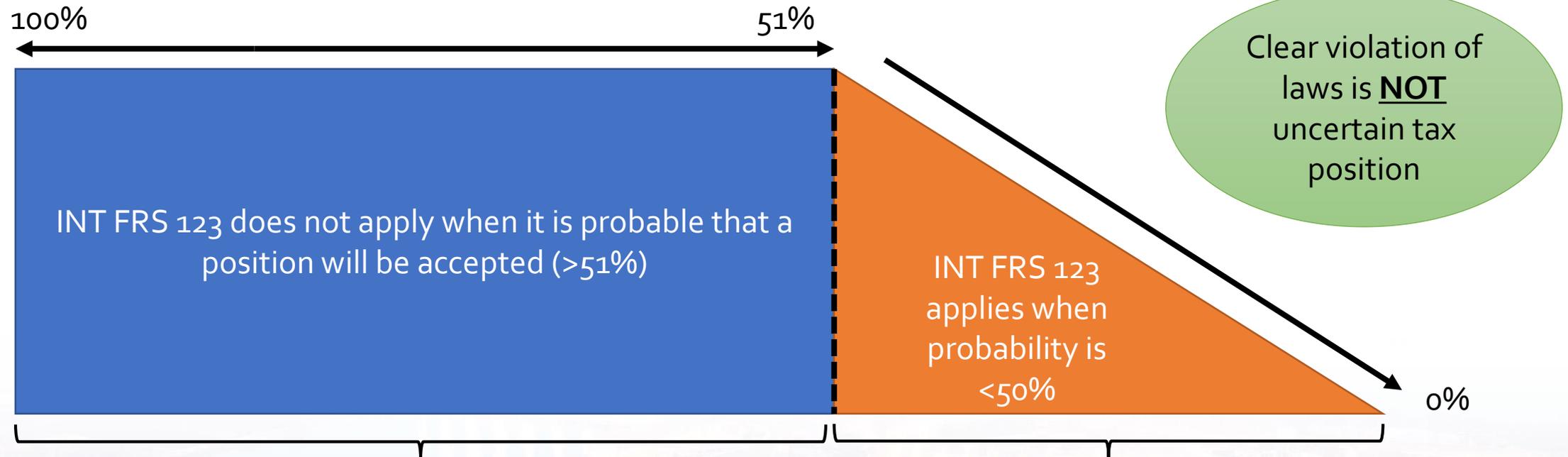
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Scope and issues addressed

Addressed by INT FRS 123	Not addressed by INT FRS 123
Whether an entity considers uncertain tax treatment separately or in combination	Measurement of current and deferred taxes (refer to FRS 12 <i>Income Taxes</i>)
The assumptions an entity makes about the examination of tax treatments by taxation authority (i.e. IRAS)	Interest and penalties associated with the uncertain tax position**
How an entity determines taxable profit or loss, tax bases, unused tax losses, unused tax credits as well as tax rates	<p>** Basis of conclusion noted that interest and penalties that are considered to be income taxes, are within the scope of FRS 12, and therefore, INT FRS 123 as well</p>
How an entity considers changes in facts and circumstances	

When to apply this interpretation?



If probable, use those assumptions in computing current and deferred tax

If not probable, uncertainty is a component of measurement

Measurement of uncertain tax positions

- Assume a tax audit will be conducted
- Only reflect the effect of uncertain tax position of which it is **not probable** that the tax authority will accept the uncertain tax position
- One of the following methods are to be used:

Most likely amount

- The single most likely amount in a range of possible outcomes

Expected value

- The sum of the probability-weighted amounts in a range of possible outcomes

- Difference from US GAAP, FIN 48 which uses a cumulative probability approach
- Need to reassess judgements and estimates

Measurement of uncertain tax positions

– Illustration

- Entity A has two subsidiaries, B and C, which operate in different tax jurisdictions
- B produces raw materials and sells them to third parties and C
- C produces various products for sale to end customers
- The Group has not completed a transfer pricing study. B is currently charging C 20% less than its third party customers. However, management notes this savings is due to lower administrative and shipping costs as C purchases in bulk

Measurement of uncertain tax positions

– Illustration

- Audit team has consulted with the tax expert, who believes it is not probable that the position will be accepted by tax authority (only 25% chance it would be accepted)
- It would result in additional \$1,000,000 tax assessment
- Based on recent activity and tax enforcement priorities announced by the government, the tax expert considers there is only a 5% chance that the position will be examined by tax authority before the examination period expires

Measurement of uncertain tax positions – Illustration

- Management accounts for the additional tax assessment as follows:



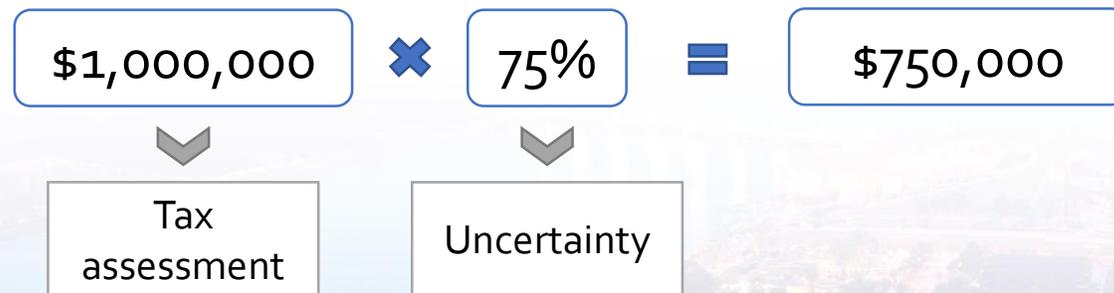
Question:

Is the above inline with INT FRS 123's requirements?

Measurement of uncertain tax positions – Illustration

Answer

- Paragraph 8 - *'In assessing whether and how an uncertain tax treatment affects the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, an entity shall assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations.'*



Dr. Current tax expense 750,000
Cr. Current tax liability 750,000

'Detection risk' cannot be incorporated in the measurement of the position.

Disclosure of uncertain tax positions

- INT FRS 123 does not introduce any new disclosure requirements. Instead, it refers to:

FRS 1.122

- Judgments made in determining taxable profit, tax bases, unused tax losses, unused tax credits and tax rates.

FRS 1.125 - 129

- Assumptions and estimates made in determining the same items as FRS 1.122.

FRS 12.88

- If conclusion is it is probable that a taxation authority will accept an uncertain tax treatment, consider disclosing the potential effect if they were to not accept the position.

Possible audit considerations

Transition & Application

- Selected transition method has been applied appropriately?
- Potential risk that entity (including overseas subsidiaries) fails to identify uncertain tax position

Estimation uncertainty

- Consultation with tax experts is recommended
- Measurement of uncertain tax positions will be a significant estimate in most situations so requirements in SSA 540, apply

Disclosure

- Risk that disclosures required are not complete and accurate
- Stand back and determine how significant the estimation included, consider whether it meets the definition of key audit matters

SSA 540 (Revised) Auditing Accounting Estimates and Related Disclosures

Effective for audits of financial statements for periods beginning on or
after 15 December 2019

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Why change?



Key enhancements

Inherent risk factors

- Characteristics of conditions and events that may affect the ***susceptibility of an assertion to misstatement***, before consideration of controls
- Include ***estimation uncertainty, complexity*** and ***subjectivity***

Controls relating to accounting estimates

- Emphasise the importance of auditor's decision about ***controls relating to accounting estimates***, including decisions about whether the relevant of such controls to the audit and its operating effectiveness

Separate assessment of control risk

- Take into account whether the planned audit procedures ***contemplate planned reliance*** on the operating effectiveness of control

Key enhancements

Responsive & Scalability

- **Objective-based work effort** – directed to methods (when complex model is used), data and assumptions
- **Allow scalability** – the higher the assessed risk of material misstatement, the more persuasive the audit evidence needs to be

Professional skepticism

- Requirements to **“stand back”** and evaluate audit evidence obtained, including both corroborative and contradictory audit evidence
- Use stronger language such as **“challenge”**, **“question”** and **“reconsider”**

Disclosure

- Require the auditor to design and perform further audit procedures on whether the **accounting estimates and related disclosures** are reasonable in the context of applicable financial reporting framework

Key Audit Reminders

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Key audit reminders

Keep up to date

Understand the business

Proper audit planning

Professional skepticism

Involvement of experts

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Thank You

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