

Income Tax Implications Arising from the Adoption of the Singapore Financial Reporting Standard (“SFRS”) for Small Entities (“SE”)

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1. What is SFRS for SE?

The Accounting Standards Council (“ASC”) has issued a separate set of accounting standards for use by smaller entities in Singapore. This set of standards, known as the “Singapore Financial Reporting Standard for Small Entities”, applies for accounting periods beginning on or after 1 January 2011.

Eligible entities have the option to apply the SFRS for SE or to continue to apply the full set of Singapore Financial Reporting Standards (“SFRS”).

2. Who can apply SFRS for SE?

An entity in Singapore is eligible to use the SFRS for SE if it is not publicly accountable and it is a “small entity” by virtue of satisfying 2 out of 3 of the quantitative criteria below:

- i) Total annual revenue of not more than S\$10 million;
- ii) Total gross assets of not more than S\$10 million;
- iii) Total number of employees of not more than 50.

An entity is considered to be “publicly accountable” if:

- i) Its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market; or
- ii) It is a deposit-taking entity and/or holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, insurance companies, securities brokers/dealers, mutual funds and investment banks; or
- iii) It is a public company defined under the Singapore Companies Act (Cap. 50); or
- iv) It is a charity defined under the Charities Act (Cap. 37).

An entity is eligible to apply the SFRS for SE only if it satisfies the above requirements for each of the previous 2 consecutive years. A newly incorporated company is eligible to use the SFRS for SE in the first 2 years of its incorporation provided it is not publicly accountable.

For details on SFRS for SE and the eligibility requirements, please refer to the [ASC's website](#).

3. Will IRAS accept accounts and tax computation prepared in accordance with SFRS for SE?

IRAS will accept accounts prepared in accordance with SFRS for SE that are submitted together with the entity’s Income Tax Return. Tax adjustments would still have to be made in the tax computation based on the current tax rules and principles.

4. **Can an entity continue to align the tax treatment for financial instruments on revenue account with the accounting treatment?**

To minimise the tax adjustments an entity has to make, IRAS is prepared to accept, for tax purposes, the accounting treatment for financial instruments **on revenue account**.

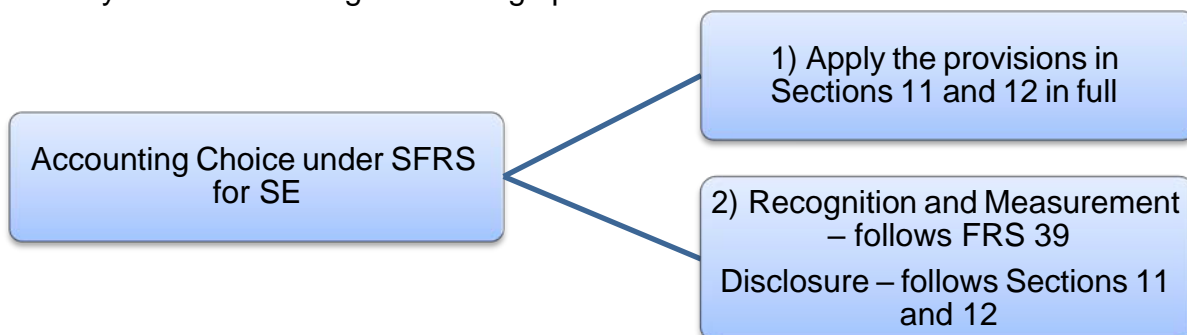
This is to the extent that the difference between the existing tax treatment and the accounting treatment under SFRS for SE is one of timing of taxation and deduction only. The income tax treatment for financial instruments **on revenue account** based on SFRS for SE is hereinafter referred to as “SFRS-SE Tax Treatment”.

The accounting treatment and SFRS-SE Tax Treatment are described below.

Accounting Treatment for Financial Instruments under SFRS for SE (Sections 11, 12)

Sections 11 and 12 of the SFRS for SE deal with the recognition, measurement and disclosure of financial instruments. Under Sections 11 and 12, financial instruments are to be measured either at amortised cost (subject to the impairment test) or fair value through profit or loss.

An entity has the following accounting options:



An entity who wishes to move from FRS 39 to a full application of Sections 11 and 12 of the SFRS for SE have to reclassify its financial instruments into the 2 prescribed categories. The one-time transitional adjustments to the existing measurements arising from a reclassification of the instruments will be recognised directly in retained earnings.

SFRS-SE Tax Treatment

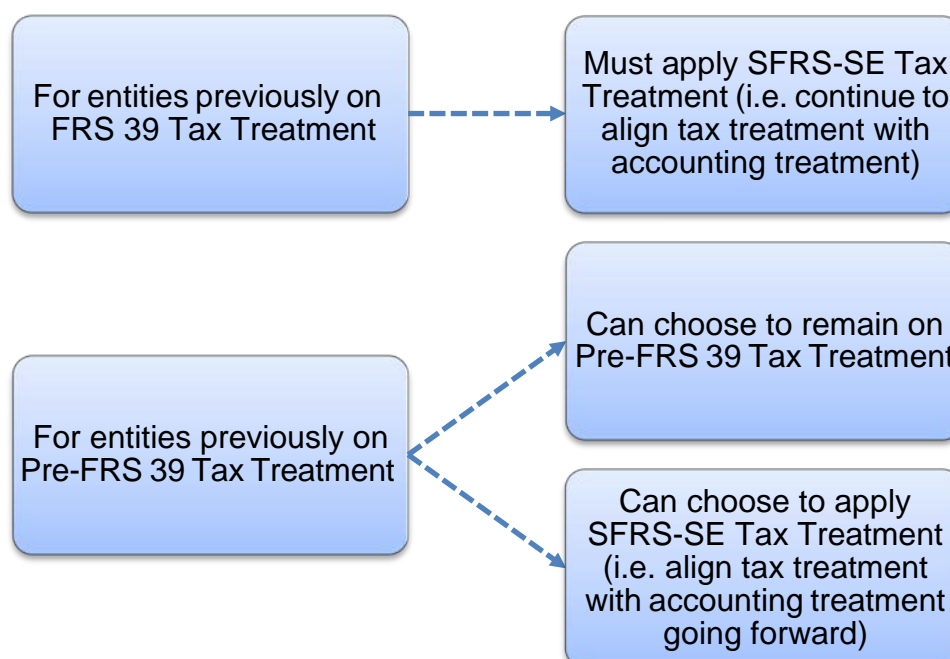
With the adoption of SFRS for SE, an entity that has elected to remain on pre-FRS 39 tax treatment (i.e. did not align the tax treatment with the accounting treatment for financial instruments on revenue account) when FRS 39 came into effect on 1 January 2005 can choose to:

- (i) continue to remain on pre-FRS 39 tax treatment; or

(ii) align the tax treatment for financial instruments **on revenue account** with the accounting treatment under SFRS for SE. This may result in tax adjustments (see Tables 2 and 3 below).

On the other hand, an entity that has already moved to the FRS 39 tax treatment has to move to the SFRS-SE Tax Treatment.

In summary, when an entity chooses to prepare its accounts in accordance with SFRS for SE, the tax treatment to be applied will be:



For newly incorporated entities that have prepared their first set of accounts in accordance with SFRS for SE, the default tax treatment will be the SFRS-SE Tax Treatment (i.e. the alignment of tax treatment with the accounting treatment for financial instruments **on revenue account**).

Table 1 below provides a summary of SFRS-SE Tax Treatment. Tables 2 and 3 set out the accounting options for an SE and the consequential tax implications.

Table 1: Summary of SFRS-SE Tax Treatment on the measurement and recognition of financial instruments

	Accounting Treatment	SFRS-SE Tax Treatment
A) Full Application of Sections 11 and 12		
1) Measurement	<p><u>Basic financial instruments</u> To be measured at amortised cost using the effective interest method</p> <p>The amortised amount and discount/premium (using effective interest method) are reflected as “interest” in Profit & Loss at each year-end</p>	<p>For assets <i>on revenue account</i>, to adopt the accounting treatment, i.e. to tax/allow the interest income/expense computed using the effective interest method</p> <p>For assets <i>on capital account</i>, to tax/allow interest income/expense based on the contractual rate, i.e. tax adjustments will be required</p>
	<p><u>Other financial instruments</u> To be measured at fair value through profit or loss</p> <p>Fair value changes at each year-end for financial instruments are recognised in Profit & Loss</p>	<p>For assets <i>on revenue account</i>, to adopt the accounting treatment and tax/allow the unrealised gains/losses</p> <p>For assets <i>on capital account</i>, to make tax adjustments so that the unrealised gains will not be taxed and the unrealised losses will not be allowed</p>
2) Impairment	Impairment losses to be recognised in Profit & Loss	<p>For assets <i>on revenue account</i>, to adopt the accounting treatment, i.e. to allow a deduction for impairment losses and to tax the reversal amount of impairment losses with no indexation</p> <p>For assets <i>on capital account</i>, to disallow any deduction for impairment losses</p>
B) Application of Sections 11 and 12 disclosure requirement only (Recognition and measurement provisions of FRS 39 applied)		
Measurement and Recognition	The accounting and tax treatments under SFRS for SE are the same as that outlined in the FRS 39 e-Tax Guide	

Table 2: Scenarios and tax implications - For an existing SE that chooses the full application of Sections 11 & 12 of SFRS for SE:

Scenario	If the Entity is currently applying the following tax treatment:	The Entity may apply the following tax treatment after the adoption of SFRS for SE:	Adjustments arising from the change in Financial Reporting Standards
1	Entity has previously elected to remain on pre-FRS 39 tax treatment	Entity chooses to remain on pre-FRS 39 tax treatment	No change Entity can continue to apply pre-FRS 39 tax treatment, subject to the conditions specified in paragraph 31 of the FRS 39 e-Tax Guide .
2	Entity has moved to FRS 39 tax treatment	Entity has to apply SFRS-SE tax treatment	The transitional adjustments recognised in the opening balance of the retained earnings will be taxed or allowed in the first YA that the SFRS-SE tax treatment is applied (i.e. once the entity adopts SFRS for SE for accounting purposes)
3	Entity has previously elected to remain on pre-FRS 39 tax treatment	Entity now elects to move to SFRS-SE tax treatment (i.e. alignment of the tax treatment of financial instruments on revenue account with the accounting treatment)	Once an election is made to align the tax treatment with the accounting treatment, the election is irrevocable. The applicable tax treatment will then follow the accounting standards that the entity has chosen to apply Tax adjustments (including transitional adjustments) arising from the alignment of the tax treatment with accounting treatment

			<p>have to be made</p> <p>The adjustments recognised in the opening balance of retained earnings will be taxed or allowed as a deduction in the first YA that the SFRS-SE tax treatment is applied</p>
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Table 3: Scenarios and tax implications - For an existing SE that chooses to apply the recognition and measurement provisions of FRS 39 and the disclosure requirements in Sections 11 and 12 of SFRS for SE:

Scenario	If the Entity is currently applying the following tax treatment:	The Entity may apply the following tax treatment after the adoption of SFRS for SE:	Adjustments arising from the change in Financial Reporting Standards
1	Entity has previously elected to remain on pre-FRS 39 tax treatment	Entity chooses to remain on pre-FRS tax treatment	<p>No change</p> <p>Entity can continue to apply pre-FRS tax treatment, subject to the conditions stated in paragraph 31 of the FRS 39 e-Tax Guide.</p>
2	Entity has moved to FRS 39 tax treatment	Entity has to apply SFRS-SE tax treatment	<p>No change</p> <p>FRS 39 tax treatment will continue to apply for financial instruments on revenue account as the recognition and measurement of financial instruments will still follow the provisions of FRS 39</p>
3	Entity has previously elected to remain on pre-FRS 39 tax treatment	Entity now elects to move to SFRS-SE tax treatment (i.e. alignment of the tax treatment of financial instruments on revenue account with the accounting	<p>Once an election is made to align the tax treatment with the accounting treatment, the election is irrevocable. The applicable tax treatment will then</p>

		treatment)	<p>follow the accounting standards that the entity has chosen to apply</p> <p>Tax adjustments (including transitional adjustments) arising from the alignment of the tax treatment with accounting treatment have to be made</p> <p>The adjustments recognised in the opening balance of retained earnings will be taxed or allowed as a deduction in the first YA that the SFRS-SE tax treatment is applied</p>
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5. Can a newly incorporated entity that has prepared its first set of accounts in accordance with SFRS for SE choose not to apply the SFRS-SE Tax Treatment?

Yes. The entity must make an election in writing, at the time of submitting the tax return for its first YA, that it wishes to apply the pre-FRS 39 tax treatment. It may choose to move to the SFRS-SE tax treatment at any time thereafter.

6. When must the election to move to SFRS-SE Tax Treatment be made?

An entity that has previously opted out of the FRS 39 tax treatment or the SFRS-SE Tax Treatment as the case may be, must make the election in writing at the time of submitting its tax return for the first YA that it wishes to move to the SFRS-SE Tax Treatment. Once an election is made to align the tax treatment with the accounting treatment, the election is irrevocable. The applicable tax treatment will then follow the accounting standards that the entity has chosen to apply.

7. What happens if an entity that is applying the SFRS for SE fails to satisfy the prescribed threshold criteria for two consecutive years?

If an entity that is applying the SFRS for SE fails to satisfy the prescribed threshold criteria for two consecutive years, it would have to switch to the full SFRS. If this entity has previously elected to align the tax treatment for its financial instruments on revenue account with the accounting treatment (i.e. has elected to apply the SFRS-SE Tax Treatment), upon the switch to the full SFRS, it will have to apply the FRS 39 Tax Treatment.

8. For tax purposes, what are some of the other differences between the full SFRS and SFRS for SE that an entity should look out for?

(a) Property, Plant and Equipment (Section 17 of SFRS for SE)

Section 17 provides that property, plant and equipment are to be measured at cost less accumulated depreciation, and subject to the impairment test. The revaluation model is not permitted. As part of the transitional rules, an SE can choose to deem the previously revalued amount of the property, plant or equipment as the cost of the asset at the date of transition.

For tax purposes, the current rules on claiming for capital allowances will continue to apply. In the case where the SE has previously chosen to defer its claim for capital allowance on the revalued asset, when capital allowance is subsequently claimed, it will be given based on the actual cost incurred in acquiring the property, plant or equipment, and not the revalued amount.

(b) Intangible Assets other than Goodwill – in particular, Research and Development Costs (Section 18 of SFRS for SE)

Section 18 requires that all research and development costs be expensed as incurred.

For tax purposes, the current tax rules on claiming for research and development costs will continue to apply. For more information on the deduction of research and development expenses, you may refer to the write-up on "[research and development \(R&D\) expenses](#)".

(c) Borrowing Costs (Section 25 of SFRS for SE)

Section 25 requires all borrowing costs to be recognised as expenses when incurred.

For tax purposes, the current tax rules on claiming for deduction of borrowing costs will continue to apply. For property developers, the existing tax treatment of capitalising all borrowing costs as allowable development costs will also continue to apply.