COMMITTEE ON BANKING DISCLOSURE

REPORT ON BANKING DISCLOSURE

May 1998

THE BANKING DISCLOSURE COMMITTEE

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CONTENTS

EXECUTIVE SUMMARY

1. The Committee on Banking Disclosure was appointed to make recommendations on the standards and practices of Singapore banks with a view to attaining the standard of disclosure in developed countries.

2. Under MAS Notice to Banks 608, the Monetary Authority of Singapore has allowed certain modifications and exceptions to the form and content of the financial statements of banks and this constitutes the minimum disclosure standard for Singapore banks. However, the financial crisis in East Asia has highlighted the need for greater transparency and disclosure of information about the financial condition of banks for the maintenance of confidence in the banking system. A higher standard of disclosure should further enhance Singapore's position as a leading regional financial centre. Furthermore, in the move from banking regulation to supervision, it is imperative for banks to adopt accounting practices and standards comparable to those of developed countries.

3. In a brief survey, the financial statements and annual reports of three banks in eight countries namely, the United States, the United Kingdom, Germany, Luxembourg, Switzerland, Japan, Australia and Singapore, and the Special Administrative Region of China, Hong Kong, were examined to assess the extent of their disclosure of financial and non-financial information. In general, the disclosure standard of Singapore banks is below that of the United States, the United Kingdom and Australia.

4. There was consensus that IAS 30, "Disclosures in the Financial Statements of Banks and Similar Financial Institutions", issued by the International Accounting Standards Committee, provides a useful model for good financial reporting and that harmonisation with IAS 30 is desirable. The Committee has taken IAS 30 into consideration in its recommendations.

5. The recommendations of the Committee cover eight major areas:

(a) Undisclosed reserves
(b) Accounting policies
(c) Profit and loss account
(d) Balance sheet
(e) Off-balance sheet
(f) Supplementary information
(g) Financial review
(h) Equity accounting

UNDISCLOSED RESERVES

6 The most controversial issue is Singapore Banks' practice of building up undisclosed or "hidden" reserves. Undisclosed reserves are build up principally by : (i) recording investments (in particular long-term equity investments or investment properties) at cost or written-down values without disclosing their fair market values, and (ii) taking realised profit from operations or from sale of long-term investments or properties to "other liabilities" or "assets" instead of to the profit and loss account.

7. The maintenance of reserves that are not disclosed in the financial statements is a common practice in some countries including Germany, Switzerland and Japan. A bank sets up undisclosed reserves with the objective of building up "inner strength". Banks use such reserves to even out reported earnings and to strengthen the balance sheet, thereby providing a cushion in the event of adverse situations. The building up of such reserves can play an important part in stabilising banks and maintaining confidence in periods of financial turmoil. In some countries like Germany and Switzerland, banks have built up substantial undisclosed reserves which have contributed to their financial strength and stability. There are therefore merits in the practice of building up undisclosed reserves.

8. However, an increasing number of central banks now require or encourage banks to be more transparent and to disclose all their reserves. The current market environment requires greater transparency and accountability. The provision of more information will enable investors to evaluate and analyse the bank's operations more effectively. Taking these factors into consideration, the Committee recommends that Singapore banks :

(a) disclose the market value of investments (including investments in property) which constitutes a substantial portion of the undisclosed reserves of Singapore banks;

(b) discontinue the practice of building up undisclosed reserves and henceforth disclose all reserves so as to give a true and fair view of the bank's financial results and position.

ACCOUNTING POLICIES

9. A bank's financial position and results are significantly affected by the choice of accounting policies especially where there is more than one acceptable accounting treatment and where an accounting policy adopted involves significant estimates and judgement. The Committee recommends that banks disclose their principal accounting policies, including those on the recognition of the principal types of income; basis for specific provision for loan losses and general provision for credit or other banking risks; valuation methods; basis of consolidation and translation of foreign currency assets and liabilities.

PROFIT AND LOSS ACCOUNT

10. For the profit and loss account, the main recommendations are as follows:

(a) Banks should provide further details of other principal sources of income, such as: (i) profit from trading/dealing in securities, foreign exchange and other financial instruments; (ii) gains on disposal of long-term investments and fixed assets.

(b) As provisions for losses relating to loans and investments generally have a significant effect on a bank's results, banks should disclose the following charges to (or write-back from) the profit and loss account: (i) specific provisions for loan losses and for diminution in value of investments and other assets; (ii) general provisions including provisions for possible loan losses and other banking risks.

(c) The build up of bank reserves through provisioning should be encouraged by the authorities through tax incentives, for example, by making specific loan loss provisions as well as general loan loss provisions fully tax deductible, as long as such provisions are accepted as necessary by the bank's external auditors and approved by the MAS.

BALANCE SHEET

11 For the balance sheet, the main recommendations are:

(a) Bank should provide a more detailed and distinct classification of securities held, e.g. dealing or investment securities, debt or equity, quoted or unquoted, investments in subsidiary and associated companies.

(b) Banks should continue with the current practice of valuation for dealing securities. It is normal banking practice in some countries to apply mark-to-market accounting to dealing securities and take the profit or loss to the profit and loss account. However, it is considered that it would be more prudent for banks not to adopt this approach and that banks should continue with the current practice of valuing dealing securities by the lower of cost or market value method. Banks should also continue the practice of valuing investment securities which are held for long term at cost.

(c) Banks should discontinue the current practice of provisioning on a line-by-line basis for dealing securities as this is not in line with international practice. The line-by-line provisioning policy requires provisions to be made for a loss on any item without recognising profits on other items. Provisioning for dealing securities should be determined on the basis of the entire portfolio of securities to take into account the effect of portfolio diversification. For investment securities, in line with international practice, provisions should be made where there is a diminution in the value of the investments that is anything other than temporary.

(d) Banks should disclose the aggregate amount of non-performing loans.

(e) Banks should provide details of loan loss provisions including a movement schedule showing the balance at the beginning of the year, the amount charged/released to profit and loss account during the year, the amount utilised to write off bad loans during the year and the balance at the end of the year for both specific and general provisions for loan losses.

(f) Banks should disclose major items under "other assets", for example, the accrual for interest receivable and the accrual for positive mark-to-market fair value of financial derivatives after taking into account the effect of legally enforceable netting arrangements.

(g) Banks should disclose major items under "other liabilities", for example, the accrual for interest payable, the accrual for negative mark-to-market fair value of financial derivatives after taking into account the effect of legally enforceable netting arrangements, and deferred taxation.

OFF-BALANCE SHEET

12. Banks increasingly engage in income-generating activities that involve risks that are accounted for off balance sheet. These include direct credit substitutes in the form of financial guarantees, commitments and financial derivatives. The Committee recommends that banks disclose, by way of a note to the financial statements, all contingent liabilities, commitments and financial derivatives.

SUPPLEMENTARY INFORMATION

13. The major recommendations relating to supplementary information are:

(a) Banks should disclose significant concentrations of exposure in respect of customer or industry groups, geographical areas and maturities to give a better appreciation of the risk profile of the bank.

(b) Banks should provide segmental analyses of such items as total assets, total income or profit by geographical areas.

(c) Banks should provide a maturity analysis of loans and deposits to reflect liquidity and interest rate risks from the mismatching of maturities and interest rates of their assets and liabilities.

FINANCIAL REVIEW

14. Banks should provide a financial review section in their annual reports covering such subjects as business description, analyses of results, income and expenses, loans and advances, provisions, risk management, effects of monetary and fiscal policies on the bank’s business, and the supervisory and regulatory framework in which the bank operates.

EQUITY ACCOUNTING

15. Banks should adopt equity accounting in accordance with Statement of Accounting Standard 27, “Accounting for Investments in Associates”.

REPORTING REQUIREMENTS

16. Banks should continue with the current practice of announcing interim results on a half-yearly basis.

IMPLEMENTATION

17. The Committee recommends that banks implement all the recommendations as set out in paragraphs 17 through 51 of this report for the financial year 1998, except Financial Review (paragraph 46) and Equity Accounting (paragraph 47) which, in view of the longer preparation time required for implementation, the Committee recommends for adoption for the financial year 1999.

REPORT ON BANKING DISCLOSURE

TERMS OF REFERENCE

1. The Committee on Banking Disclosure was appointed by the Financial Sector Review Group, chaired by Deputy Prime Minister Lee Hsien Loong to:

(a) Review and evaluate banking disclosure standards and practices in the developed and the Asia Pacific countries, and

(b) Recommend changes in disclosure with a view to attaining the standard of disclosure in developed countries.

NEED FOR IMPROVED DISCLOSURE STANDARDS

2. With the Monetary Authority of Singapore's (MAS) shift in emphasis from regulation to supervision, there is a need for greater transparency and a higher disclosure standard for Singapore-incorporated banks (Singapore banks). Further, with the globalisation of financial markets, banks have increasingly come under "market surveillance". In the light of this inexorable worldwide trend, the need for better financial disclosure has become more urgent given the extent and pace of change in financial markets and the trend towards deregulation which will give banks greater access to new products, new customers and new risks.

3. The East Asian financial crisis has also highlighted the need for greater transparency and disclosure of information about the financial condition of banks for the maintenance of confidence in the banking system. If the demand for information is not provided by banks directly, market participants may seek information from indirect sources, with the risk that the information obtained may be inaccurate or misleading. Singapore has been rated highly in all aspects of banking regulation and supervision, and a higher standard of disclosure should further enhance its position as a leading regional financial centre. It is thus imperative for banks to adopt accounting practices and standards comparable to those of developed countries.

CURRENT STATUS OF DISCLOSURE BY SINGAPORE BANKS

4. Currently, the main disclosure requirements for Singapore banks are those stipulated under the Companies Act, the Statements of Accounting Standard issued by the Institute of Certified Public Accountants of Singapore (ICPAS) and, for banks listed on the Stock Exchange of Singapore (SES), the SES's listing rules. However, section 201 (19) of the Companies Act permits banks to take into account certain modifications and exceptions allowed by the MAS to the form and content of their financial statements. The modifications and exceptions set out in MAS Notice to Banks 608 issued in 1973 allow banks:

(a) To make undisclosed transfers to and from reserves before arriving at published profits, particularly movements in and out of contingency accounts and reserves for bad and doubtful debts. However, such movements must be approved by the MAS.

(b) To avoid showing the charge for income tax as a deduction from published profits.

(c) To show investments without having to disclose their market value. However, the basis of valuation of the investments must be disclosed.

(d) To show fixed and other assets without having to show the accumulated depreciation and write-off separately. However, the method of valuation of the assets must be shown.

(e) To consolidate the accounts of the bank with directly-owned banking subsidiaries where a bank is a holding company. Directly-owned non-banking subsidiaries may be excluded as well as indirectly-owned subsidiaries irrespective of whether they carry on banking or non-banking activities.

5. In practice, exemptions (b) and (e) are no longer applicable as banks no longer apply these modifications and exceptions.

6. Traditionally, banks have been subject to lower standards of disclosure than other corporations for two reasons. First, the high regulatory and supervisory standards practised by MAS compensate somewhat for a more limited disclosure. Second, disclosure is constrained by concern that fuller disclosure of banking information may have an adverse impact on the stability of the banking system since, relative to other corporations, banks are especially vulnerable to a loss of confidence. However, in the move from banking regulation to supervision in Singapore, greater transparency in

financial reporting is now desirable.

COMPARATIVE ANALYSIS: SURVEY FINDINGS

7. In a brief survey, the financial statements and annual reports of three banks in eight countries namely, the United States, the United Kingdom, Germany, Luxembourg, Switzerland, Japan, Australia and Singapore, and the Special Administrative Region of China, Hong Kong, were examined to assess the extent of their disclosure of financial and non-financial information in their annual reports. The countries selected fall broadly into three groups:

- o the United States and the United Kingdom which lead in financial disclosure practices;
- o Germany, Luxembourg and Switzerland to gain a European perspective;
- o Japan, Australia and Hong Kong (SAR, China) for bench-marking within Asia Pacific.

8. Singapore banks have improved their standard of disclosure by disclosing *inter alia* the amount of non-performing loans and the aggregate amount of provisions made in their 1997 financial statements. But the disclosure standard of Singapore banks is still below that of the United States, the United Kingdom and Australia. The shortfall relates mainly to a lack of differentiation between general and specific provisions for loans, a breakdown of securities held for investment and dealing purposes, and market value of securities and investments.

9. Unlike the United States, the United Kingdom and Australia, Singapore banks do not separately disclose the amount of specific and general provisions for loan losses and movements in provisions. In addition, securities held are not categorised into investment and dealing, an important distinction as securities held for dealing purposes are usually marked to market but securities held for investment purposes are not. Further, the market value of listed securities and investment properties is not provided, resulting in substantial undisclosed reserves.

10. Other items which are provided in the financial statements of banks in the United States, the United Kingdom and Australia but are not given by Singapore banks include trading/dealing income, a breakdown of the components of other assets and liabilities, net replacement cost of financial derivatives, and a segmental analysis. A summary of the survey findings is attached as Appendix I.

BENCHMARK

11. International accounting standards are issued by the International Accounting Standards Committee (IASC) which has a current membership of 128 accounting bodies from 91 countries including Singapore. Its objective is to promote the worldwide acceptance and observance of standards on the presentation of audited financial statements. Despite efforts at harmonisation by the IASC, accounting objectives, standards and policies continue to differ among countries.

12. IAS 30, “Disclosures in the Financial Statements of Banks and Similar Financial Institutions”, was issued in 1990. Among others, the financial statements of banks in the United States, the United Kingdom and Australia are fully in compliance with or exceed the requirements of IAS 30, but accounting practices in some countries, notably Japan and Switzerland, still deviate considerably from IAS 30 guidelines.

13. There was consensus that IAS 30 provides a useful model for good financial reporting and that harmonisation with IAS 30 is desirable. The Committee has taken IAS 30 into consideration in its recommendations.

14. Another international accounting standard relevant to banks, IAS 32, “Financial Instruments: Disclosure and Presentation”, issued by the IASC in 1995 which provides useful guidelines for the accounting and disclosure of financial instruments has not yet been adopted as a Singapore standard by the Institute of Certified Public Accountants of Singapore (ICPAS). The Committee recommends that banks consider compliance with its requirements when adopted by ICPAS.

RECOMMENDATIONS FOR DISCLOSURE

Principles Underlying the Committee’s Recommendations

15. The Committee has adopted the following general principles of disclosure in arriving at its recommendations:

(a) Details of where and how total profits are derived to enable investors to assess the quality of earnings.

(b) Information on concentrations (geographical or industry groups) of assets and liabilities as a useful indication of the potential risks inherent in the realisation of the assets and the sources of funds available to the bank.

(c) The maturity profile of assets and liabilities which provides a basis to evaluate the liquidity of a bank.

(d) The market value of all marketable securities held for dealing and investment to provide an indication of the realisable value of these assets.

(e) The market value of long-term investments, including properties, to provide an indication of the realisable value of these assets.

(f) Provisions for losses on loans and advances at the balance sheet date and the movements in provisions during the period. This shows the impact that losses on loans and advances have on the results and financial position of the bank as well as the effectiveness with which the bank has managed its credit exposure.

(g) Information about the nature, amount and replacement value of off-balance sheet transactions undertaken by a bank which may have a significant bearing on the level of risk to which the bank is exposed.

Recommendations

16. The recommendations of the Committee cover eight major areas:

(a) Undisclosed reserves
(b) Accounting policies
(c) Profit and loss account
(d) Balance sheet
(e) Off-balance sheet
(f) Supplementary information
(g) Financial review
(h) Equity accounting

Undisclosed Reserves

17. The most controversial issue is Singapore banks' practice of building up undisclosed or "hidden" reserves. Undisclosed reserves are built up principally by: (i) recording investments (in particular long-term equity investments or investment properties) at cost or written-down values without disclosing their fair market values, and (ii) taking realised profit from operations or from sale of long-term investments or properties to "other liabilities" or "assets" instead of to the profit and loss account.

18. The maintenance of reserves that are not disclosed in the financial statements is a common practice in some countries including Germany, Switzerland and Japan. Undisclosed reserves are generally included in the balance sheet as other liabilities or as a deduction against assets or are implicit in the absence of disclosure of market value (where it is higher) of assets carried at cost or written-down value.

19. The Committee is cognisant of the various considerations relating to the issue of undisclosed reserves. A bank sets up undisclosed reserves with the objective of building up "inner strength". Banks use such reserves to even out reported earnings and to strengthen the balance sheet, thereby providing a cushion in the event of adverse situations. The building up of such reserves can play an important part in stabilising banks and maintaining confidence in periods of financial turmoil. Some members of the Committee have pointed out that in countries like Germany and Switzerland, banks have built up substantial undisclosed reserves which have contributed to their financial strength and stability. There have been occasions when banks have been able to use undisclosed reserves to cushion a substantial extraordinary loss.

20. However, an increasing number of countries now require or encourage their banks to discontinue this practice of building up undisclosed reserves because such practices could distort a bank's operating results in a particular year and, over a period of time, could mask the performance of its management. As many banks are listed companies with public shareholders, they should be subject to the same market discipline as other listed companies. The need for greater transparency in order to facilitate the evaluation and analysis of a bank's performance and the capability of its management is an important issue. The bank and its management should have greater accountability to shareholders and depositors.

21. Taking these factors into consideration, the Committee recommends that banks:

(a) disclose the market value of investments (including investments in property) which constitutes a substantial portion of the undisclosed reserves of Singapore banks;

(b) discontinue the practice of building up undisclosed reserves and henceforth disclose all reserves so as to give a true and fair view of the bank's financial results and position.

Accounting Policies

22. A bank's financial position and results are significantly affected by the choice of accounting policies especially where there is more than one acceptable accounting treatment and where an accounting policy adopted involves significant estimates and judgement. The Committee recommends that banks disclose their accounting policies on the following:

(a) Recognition of each of the principal types of income;

(b) Basis for specific provision for loan losses and general provision for credit or other banking risks;

(c) Valuation methods of:
- investment securities
- dealing securities
- financial derivatives including forward foreign exchange contracts;

(d) Depreciation of fixed assets;

(e) Basis of consolidation;

(f) Translation of foreign currency assets and liabilities.

Profit and Loss Account

23. ***Income* --** In addition to interest income and fees and commissions which are currently disclosed, the Committee recommends that banks provide further details of other principal sources of income and, in particular, the following types of income:

(a) *Profit (loss) from trading/dealing* in securities, foreign exchange and other financial instruments should be disclosed as dealing profit (loss) as appropriate. If significant, a breakdown of income from trading in foreign exchange, interest rates and securities should be provided;

(b) *Dividend income* from subsidiaries, associated companies and other investments should be shown separately;

(c) *Gains on disposal of long-term investments;*

(d) *Gains on disposal of fixed assets.*

24. ***Expenses* --** Currently, banks disclose directors' remuneration, auditors' fees, depreciation and amortisation expenses and personnel expenses. To provide a better understanding of a bank's expense structure, the Committee recommends that in addition to the above items, the following expense components be disclosed:

(a) Maintenance and hire of fixed assets, and

(b) Rental of premises.

25. Banks currently disclose the aggregate amount of provisions for loan losses and diminution in value of investments and other assets. To show the impact that losses on loans and investments have on the results and financial position of the bank, the Committee recommends that banks disclose the following charges to (or write-back from) the profit and loss account:

(a) Specific provision for loan losses;

(b) Specific provision for diminution in value of investments and other assets, and

(c) General provisions including provisions for possible loan losses and other banking risks.

26. The build up of bank reserves through provisioning should be encouraged by the authorities through tax incentives, for example, by making specific loan loss provisions as well as general loan loss provisions fully tax deductible, as long as such provisions are accepted as necessary by the bank's external auditors and approved by the MAS.

Balance Sheet: Assets

27. ***Securities and Investments* --** Currently, investments in subsidiaries and associated companies are separately disclosed. Securities are also categorised broadly into quoted and unquoted securities, rather than into investment and dealing securities. The latter is an important distinction as securities held for dealing purposes are usually marked to market while securities held for investment purposes are not. To provide a more detailed classification of securities held and a fuller description of the method of valuation, the Committee recommends that banks show the following items and their methods of valuation separately:

(a) *Dealing securities* which refer to those arising from transactions conducted regularly with a view to taking advantage of short-term changes in market prices and yields;

(b) *Investment securities* which refer to those held for the longer term, with a view to receiving a regular interest or dividend yield and potential capital appreciation;

(c) *Investments* in subsidiary companies;

(d) *Investments* in associated companies.

28. Apart from classifying securities into dealing and investment, the Committee recommends that banks comply with the existing Companies Act requirements by further categorising the securities into equity or debt and quoted or unquoted. A similar analysis should be made for investments in subsidiaries and associated companies.

29 ***Valuation and Provisioning for Quoted Securities*** -- It is normal banking practice in some countries to apply mark-to-market accounting to dealing securities and take the profit or loss to the profit and loss account. The Committee however considers that it would be more prudent for banks not to adopt this approach and recommends that banks continue with the current practice of valuing dealing securities by the lower of cost or market value method. Investment securities on the other hand are held for the long term and their valuation, therefore, should not take into consideration short-term market

fluctuations. For long-term investments the current practice of valuing them at cost should continue.

30 In regard to provisioning policy for dealing securities, the current practice is on a line-by-line basis. This requires provisions to be made for a loss on any item without recognising profits on other items. The current practice of provisioning on a line-by-line basis, which is not in line with international practice, should be discontinued. The Committee recommends that provisioning should be determined on the basis of the entire portfolio of securities to take into account the effect of portfolio diversification. For investment securities, in line with international practice, provisions should be made where there is a diminution in the value of the investments that is anything other than temporary.

31. ***Non-performing Loans (NPL) --*** The current international best practice discloses the amount of NPL to customers. But there is no international uniformity in the definition of NPL. Different banks (even in the same country of incorporation) adopt slightly different definitions for NPL. Typically, NPL include loans for which interest charged to customers' accounts has been placed in a suspense account and loans for which interest accrual has ceased. Some banks include under NPL, loans which have been restructured with an interest rate significantly lower than market, as well as those which are current as to payment of principal and interest, but serious doubts exist about the ability of the borrower to comply with the repayment terms.

32. The Committee recommends that the aggregate amount of NPL be disclosed. In the Singapore context, NPL will be defined as all loans classified in accordance with MAS loan grading guidelines, which are broadly in line with international practice.

33. ***Specific and General Provisions and Movement in Provisions*** -- To show the impact that losses on loans and investments have on the results and financial position of the bank, as well as the effectiveness with which the bank has managed its credit exposure, the Committee recommends that banks provide a movement schedule showing the balance of provisions at the beginning of the year, the amount charged/released to profit and loss account during the year, the amount utilised to write off bad loans during the year and the balance at the end of the year in respect of : (a) specific provisions for loan losses, (b) specific provisions for diminution in value of investments and other assets, and (c) general provisions including provisions for possible loan losses and other banking risks. Banks should make provisions in accordance with the provisioning requirements set out by the MAS. Details of the MAS current loan grading and provisioning guidelines are in Appendix II.

34. The Committee also recommends that banks provide a similar movement

schedule for interest-in-suspense which is equivalent to a specific provision against accrued interest receivable.

35. ***Other Assets* --** Currently, banks tend to report a lump-sum item as “other assets” without further analysis. The Committee recommends that banks disclose major items, for example, the accrual for interest receivable and the accrual for positive mark-to-market fair value of financial derivatives after taking into account the effect of legally enforceable netting arrangements.

36. ***Assets Pledged to Third Parties* --** Certain assets of the bank may be pledged to third parties as security for liabilities of the bank. The Committee recommends that assets so pledged, together with the aggregate amount of the related secured liabilities, be disclosed.

37. ***Fixed Assets* --** The Committee recommends that banks disclose details of fixed assets in accordance with the requirements of the Companies Act and Statement of Accounting Standard 14, “Property, Plant and Equipment”, (SAS 14). The information to be disclosed includes, for each major class of fixed assets, the gross carrying amount and the accumulated depreciation at the balance sheet date and a movement schedule showing the additions, disposals, depreciation and details of other movements during the year. Where a fixed asset is revalued, the basis and date of revaluation, whether an independent valuer was involved and other details specified under SAS 14, should be disclosed.

Balance Sheet: Liabilities

38. There are currently no major issues relating to the reporting of liabilities by Singapore banks other than the inclusion of undisclosed reserves as liabilities which is dealt with under paragraphs 17 to 21 of this report. As a refinement to disclosure relating to liabilities, the Committee recommends the following :

(a) For debt securities issued by the bank which mature after one year, disclose interest rate (if fixed rate) and repayment date; for floating-rate securities, disclose interest fixing method.

(b) For other liabilities, disclose major items, for example, the accrual for interest payable; the accrual for negative mark-to-market fair value of financial derivatives after taking into account the effect of legally enforceable netting arrangements, and deferred taxation.

Shareholders' Equity

39. The Committee recommends that the following information be provided for each type of reserves:

(a) the amount of each type of reserves at the beginning and end of the financial year, and

(b) the amount of any transfers to or from each type of reserves during the year.

40. The following information on the capital adequacy ratio and components as defined by the BIS should also be disclosed:

- Tier I capital
- Tier II capital
- Capital ratios
- Risk-weighted assets

Off-Balance Sheet

41. Banks increasingly engage in income-generating activities that involve risks that are accounted for off balance sheet. These include direct credit substitutes in the form of financial guarantees, commitments and financial derivatives. Appropriate disclosure is necessary for a better understanding of the income and risk profile of the bank. The Committee recommends that banks disclose, by way of a note to the financial statements, off-balance sheet items under three categories:

(a) *Contingent liabilities*, disclose the contract amount for each of the items below:

- Direct credit substitutes such as general guarantees of indebtedness, acceptances and endorsements and standby letters of credit serving as financial guarantees for loans;

- Transaction-related contingencies such as performance bonds and standby letters of credit related to particular transactions;

- Trade-related contingencies such as documentary credits; and

- Other contingent liabilities.

(b) C*ommitments*, disclose the committed amount for each of the items below:

- o Undrawn credit lines and other commitments to extend credit;
- o Undrawn note issuance facilities and revolving underwriting facilities;
- o Forward asset purchase/sale and forward deposits placed, and
- o Other commitments.

(c) *Financial derivatives* covering foreign exchange, interest rates, equity and equity indices, bullion as well as other commodities, and other related contracts are often collectively described as off-balance sheet financial instruments and arise from banks' treasury and capital market activities. They include forward sales and purchases of currencies and securities, interest rate and currency swaps, forward rate agreements and futures and options of various kinds. Where material, banks should disclose the contract amount, the gross positive mark-to-market value, the gross negative mark-to-market value and the effect of legally enforceable netting arrangements for each of the items. Where material, the same information should be provided for commodity and credit derivatives.

42. A table summarising the recommendations in respect of profit and loss account, balance sheet and off-balance sheet disclosures is provided in Appendix III.

SUPPLEMENTARY INFORMATION

43. ***Concentrations of Assets and Liabilities* --** To give a better appreciation of their risk profile, banks should disclose any significant concentrations of exposure, for example, customer or industry groups, geographical areas and maturities.

44. ***Segmental Reporting*** -- In segmental analysis, items such as total assets, total income or profit before taxation are separately analysed by geographical areas. This may be based on the location of the bank, branch or office where the business is sourced or on the location of customers. Banks are encouraged to provide analyses of all major areas of business activities, as they provide a useful indication of the potential risks involved:

(a) *Geographical Analysis* -- The Committee recommends that banks adopt the following geographical grouping:

- Singapore
- ASEAN
- Other Asia Pacific
- Rest of the world

(b) *Analysis of Loans and Advances by Industry* -- The Committee recommends that loans and advances be analysed by the following industry groups:

- Agriculture, mining and quarrying
- Manufacturing
- Building and construction
- Housing loans
- General commerce
- Transport, storage and communication
- Financial institutions
- Professional and private individuals (except housing loans)
- Others

45. ***Maturity Analysis*** -- A bank manages its liquidity and interest rate risks by matching or controlling the mismatching of maturities and interest rates of its assets and liabilities. For banks which have made public issues of debt securities, the Companies Act requires that its assets and liabilities be analysed into relevant maturity groupings for disclosure in its audited financial statements. The following maturity analysis should be disclosed, in addition to any other disclosures already required under the Companies Act, for both loans and deposits. The analysis into the relevant maturity groupings should be based on the remaining period to the contractual maturity date on the balance sheet date. The Committee recommends that the following maturity bands be adopted:-

- Maturing within one year
- Over one year but within three years
- Over three years but within five years
- Over five years.

FINANCIAL REVIEW

46. A financial review section should be provided covering analysis or further information of the following:

- o Business description
- o Results by business
- o Nature of income and expenses
- o Yields, spreads and margins
- o Capital resources including capital adequacy ratios
- o Deposits (analysis of sources)
- o Securities held (book value and current valuation)
- o Risk management (discussion of principal banking risks and how they are managed)
- o Loans and advances
- o Provisions for possible loan losses
- o Credit risk exposure by country and cross-border lending
- o Trading activities
- o Liquidity
- o Effects of monetary and fiscal policies on the bank's business
- o Supervision and regulatory framework in which the bank operates.

EQUITY ACCOUNTING

47. Equity accounting for investments in associated companies is a generally accepted accounting principle adopted in most developed countries, for example, the United States, the United Kingdom, Germany and Australia. Banks in Singapore currently do not equity account for the results of their investments in associated companies. They recognise only the dividends received from their associated companies in their consolidated profits.

48. Equity accounting should be adopted for investment in any company (not being a subsidiary or a joint venture as defined in Statement of Accounting Standard 29, “Financial Reporting of Interests in Joint Ventures”) in which the bank, directly or indirectly through subsidiaries, has a significant influence. Under Statement of Accounting Standard 27, “ Accounting for Investments in Associates”, if an investor holds, directly or indirectly through subsidiaries, 20% or more of the voting power of the investee, the investor is presumed to have significant influence unless it can be clearly demonstrated otherwise. Under equity accounting, the investor’s proportionate share of the profit before taxation, taxation charge and profit after taxation are brought into its consolidated profit and loss account on an accrual basis and dividends received are treated as realisation of the profit so accrued.

49. Equity accounting may result in either a more diversified earnings base or greater volatility in consolidated earnings. It however, provides a timely reflection of the performance of the investee within the consolidated financial statements of the bank. The Committee recommends that the equity method of accounting be adopted by Singapore banks in accordance with Statement of Accounting Standards 27, “Accounting for Investments in Associates”.

REPORTING REQUIREMENTS

50. Currently, banks listed on the Stock Exchange of Singapore announce interim financial results on a half-yearly basis. The information announced includes profit and loss account and balance sheet in a condensed report. While US banks provide quarterly reports under the SEC listing requirements, banks in other major countries are only required to report financial results on a half-yearly basis.

51. The Committee’s view is that the announcement of (unaudited) results on a quarterly basis may not be appropriate for Singapore banks. The Committee recommends that the current practice of announcing listed banks’ results on a half-yearly basis be continued.

IMPLEMENTATION

52. The Committee recommends that banks implement all the recommendations as set out in paragraphs 17 through 51 of this report, for the financial year 1998, except Financial Review (paragraph 46) and Equity Accounting (paragraph 47) which, in view of the longer preparation time required for implementation, the Committee recommends for adoption for the financial year 1999.

APPENDIX

APPENDIX I

SUMMARY OF SURVEY FINDINGS

1. The financial statements and annual reports of selected banks in eight countries, namely United States, United Kingdom, Germany, Luxembourg, Switzerland, Japan, Australia and Singapore, and the Special Administrative Region of China, Hong Kong were surveyed to assess the extent of their disclosure of financial and non-financial information in their annual reports.

2. The information items identified as key issues under current disclosure practices are categorised into four broad headings: income statement, balance sheet, off-balance sheet and supplementary information provided elsewhere in the annual report outside the financial statements (e.g. financial review by management). Notes to the financial statements form an integral part of the financial statements.

3. In this brief survey, three banks were selected for each of the countries surveyed on the basis of the amount of disclosure in their annual reports. In the case of Singapore, the big four were surveyed. The annual reports selected are for financial years ended between 31 December 1996 and 30 June 1997 depending on the normal financial reporting cycle of the country concerned. As it is not possible to have complete uniformity in the types of information disclosed by banks from the same country, an item is regarded as being commonly disclosed in a country if the majority of banks surveyed in that country disclose that item. Where appropriate, new disclosures made by Singapore banks in their 1997 annual reports have been taken into consideration. The findings relating to each of the items are summarised below.

APPENDIX I

SUMMARY OF SURVEY FINDINGS

Items	***Disclosed***
PROFT AND LOSS ACCOUNT	
Total specific and general provision for bad and doubtful loans	All countries surveyed
Trading/dealing income	US UK Australia Germany Switzerland Japan Hong Kong (SAR, China)
Profit/Loss on disposal of investment securities	US UK Australia Switzerland Hong Kong (SAR, China)
Personnel expenses	US UK Australia Germany Switzerland Hong Kong (SAR, China)
Premises and equipment expenses	US UK *(rental only)* Australia Switzerland Hong Kong (SAR, China)
Related party transactions	US UK Australia Luxembourg Switzerland Hong Kong (SAR, China) Singapore (In accordance with the requirements of SES and disclosed by way of separate announcement.)

Items	*Disclosed*
BALANCE SHEET: ASSETS	
Securities held categorised into investment and dealing This is an important distinction as under generally accepted accounting principles, securities held for dealing purposes are usually marked to market but securities held for investment purposes are not.	All countries surveyed except Singapore
Market value of listed securities (debt and equity)	US UK Australia Germany Switzerland Hong Kong (SAR, China)
Analysis of loans to customers by type (eg. Loans, mortgages, hire purchase, leases), maturity, customer or industry groups and by geographical areas	US UK Australia Germany Luxembourg *(by maturity; leases are separately disclosed)* Switzerland Hong Kong (SAR, China) *(type and industry)*
Specific provision for bad and doubtful loans/movement in provisions The current best practice is to disclose the amount of specific provision at the end of the year together with a movement schedule showing the balance at beginning of the year, amount charged/released to income statement and amount utilised to write off bad loans during the year.	US UK Australia Germany Switzerland Hong Kong (SAR, China)
Interest-in-suspense Interest-in-suspense refers to a balance sheet item which is equivalent to a specific provision against accrued interest receivable. The current best practice is to disclose the interest-in-suspense at the year-end together with a movement schedule in the same way as disclosing the specific provision.	US UK Australia Hong Kong (SAR, China)
General provision for bad and doubtful loans In addition to the specific provision which relates to identified bad and doubtful loans, the general provision relates to latent bad and doubtful loans which are present in any credit portfolio but have not been specifically identified. The current best practice is the same as that for disclosing the specific provision.	US UK Australia Germany Hong Kong (SAR, China)

Items	***Disclosed***
BALANCE SHEET: ASSETS	
Non-performing loans The current best practice discloses the amount of non-performing loans to customers. But there is no international uniformity in the definition of non-performing loans. Different banks (even in they are from the same country) adopt slightly different definitions for non-performing loans. Typically, non-performing loans include loans for which interest charged to customers' accounts has been placed in a suspense account and loans on which interest accrual has ceased. Some banks include under NPL, loans which have been re-structured with an interest rate significantly lower than market and those which are current as to payment of principal and interest but serious doubts exist about the ability of the borrower to comply with the repayment terms.	US UK Australia Hong Kong (SAR, China)
Components of other assets There is no uniformity in disclosing the components included in other assets but typically accrued interest receivable and accrual for mark-to-market gains in financial derivatives are components which are separately disclosed.	US UK Australia Germany Switzerland
BALANCE SHEET: LIABILITIES	
Maturity analysis of customer deposits Maturity is typically classified into bands, e.g. up to three months, three months to one year, one to five years and over five years. This classification is the same as that for loans.	US UK Australia Germany Switzerland
Components of other liabilities There is no uniformity in disclosing the components included in other liabilities but typically accrual for interest payable and accrual for mark-to-market losses on financial derivatives are components which are separately disclosed.	US UK Australia Germany Switzerland Japan Hong Kong (SAR, China)

Items	*Disclosed*
BALANCE SHEET: SHAREHOLDER'S EQUITY	
Movements in reserves	US UK Australia Germany Switzerland Hong Kong (SAR, China) Singapore
Capital adequacy ratio Capital adequacy ratio, which measures the level of the bank's eligible capital expressed as a percentage of its risk-weighted assets, is either disclosed in a note to the financial statements or elsewhere in the annual reports of banks outside the financial statements.	US UK Australia Germany Hong Kong (SAR, China) Singapore
Segmental Analysis In Singapore, segment reporting is a normal requirement of Statement of Accounting Standard 23 but banks have been exempted from providing such information. In the segmental analysis such items as total assets, total income or profit before taxation are normally analysed by geographical area and business segment.	US UK Australia Germany Switzerland Hong Kong (SAR, China)
OFF-BALANCE SHEET	
The disclosure of off-balance sheet items ranges from a one-line total shown below the balance sheet accompanied by a brief note showing the components making up the total (as currently practised in Singapore), and to several pages of analysis as practised by some banks in some countries.	
Contingent liabilities (credit equivalents) and commitments by type	US UK Australia Germany Switzerland Hong Kong (SAR, China) Singapore *(contingent liabilities only)*

Items	*Disclosed*
OFF-BALANCE SHEET	
Financial derivatives - Notional amount by type (eg. IRS, FRA, futures, options purchased/written etc)	US UK Australia Germany Switzerland Hong Kong (SAR, China)
Net replacement cost of financial derivatives Credit exposure or replacement cost of financial derivatives respresent the cost to replace contracts with a positive value (an asset to the bank) in the event of counterparty default and this is usually a small fraction of the notional amount of the contract.	US UK Australia Germany Switzerland Hong Kong (SAR, China)

APPENDIX II

MAS Guidelines on Loan Grading and Provisioning

Banks grade their loans into five categories: Passed, Special Mention, Substandard, Doubtful and Loss. Classified loans are those graded Substandard, Doubtful and Loss. The definitions are as follows [1] :-

(a) Substandard - loans are classified substandard when their normal repayments are overdue or may be in jeopardy. Also included in this category are performing loans which are graded substandard solely because of the borrowers' weak financials. The local banks make 10% provision for the unsecured portion of the loans classified as substandard.

(b) Doubtful - loans are classified doubtful when full liquidation of outstanding debts appear questionable and the accounts suggest that there will be a loss, the exact amount of which cannot be determined as yet. Banks make 50% provision for doubtful loans.

(c) Loss - loans are classified as loss when outstanding debts are regarded as uncollectible. Banks make 100% provision for loss loans.

[1] In addition to the grading criteria above, the local banks are required to automatically classify their loans when the principal or interest payments on those loans are three months or more in arrears.

APPENDIX III

COMPARISON OF SURVEY FINDINGS AND RECOMMENDATIONS

	Items	Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
	INCOME STATEMENT			
1	Total specific and general provision for bad and doubtful loans	All countries surveyed	Yes (since 1997)	To disclose the following charges against (or write-back from) the profit and loss account:- • Specific provision for loan losses; • Specific provision for diminution in value of investments and other assets; • General provisions for possible loan losses including provisions for other banking risks.
2	Trading/dealing income	US UK Australia Germany Switzerland Japan Hong Kong (SAR, China)	No	To disclose profits (losses) from trading/dealing in securities, foreign exchange and other financial instruments as dealing profits (losses) as appropriate. If significant, a breakdown of income from trading in foreign exchange, interest rate and securities should be provided.
3	Profit/Loss on disposal of investment securities	US UK Australia Switzerland Hong Kong (SAR, China)	Yes (since 1997)	To separately disclose gains on disposal of long-term investments.

Items		Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
4	Personnel expenses	US UK Australia Germany Switzerland Hong Kong (SAR, China)	Yes (since 1997)	
5	Premises and equipment expenses	US UK *(rental only)* Australia Switzerland Hong Kong (SAR, China)	Yes (depreciation figure)	To disclose the following expense items, in addition to depreciation of fixed assets: • Maintenance and hire of fixed assets • Rental of premises.
6	Related party transactions	US UK Australia Luxembourg Switzerland Hong Kong (SAR, China)	Yes	In accordance with the requirements of SES and disclosed by way of separate announcement.
	BALANCE SHEET: ASSETS			
7	Securities held categorised into investment and dealing	All countries surveyed except Singapore	No	To categorise securities into the following items: • Dealing securities; • Investment securities; • Investments in subsidiary companies; and • Investments in associated companies.
8	Market value of listed securities (debt and equity)	US UK Australia Germany Switzerland Hong Kong (SAR, China)	No	To categorise securities and investments in subsidiaries and associated companies into debt or equity and quoted or unquoted.

Items		Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
9	Analysis of loans to customers by type (eg. loans, mortgages, hire purchase, leases), maturity, customer or industry groups and by geographical areas	US UK Australia Germany Luxembourg *(by maturity; leases are separately disclosed)* Switzerland Hong Kong (SAR, China) *(type and industry)*	Yes (industry and maturity)	To analyse loans and advances by maturity (into 4 bands), industry and geographical areas.
10	Specific provision for bad and doubtful loans/ movement in provisions	US UK Australia Germany Switzerland Hong Kong (SAR, China)	No	To provide a movement schedule showing the balance in provision at the beginning of the year, amount charged/ released to profit and loss account during the year, the amount utilised to write off bad loans during the year and the balance at the end of the year in respect of:- • Specific provision for loan losses; • Specific provision for diminution in value of investments and other assets.
11	Interest-in-suspense	US UK Australia Hong Kong (SAR, China)	No	To provide similar movement schedule as point (10).
12	General provision for bad and doubtful loans	US UK Australia Germany Hong Kong (SAR, China)	No	To provide similar movement schedule as point (10).

Items		Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
13	Non-performing loans	US UK Australia Hong Kong (SAR, China)	Yes (since 1997)	To disclose the aggregate amount of non-performing loans.
14	Components of other assets	US UK Australia Germany Switzerland	No	To disclose separately significant items such as the amount of accrual for interest receivable and the accrual for positive mark-to-market fair value of financial derivatives after taking into account the effect of legally enforceable netting arrangements. To also show assets pledged to third parties as security for liabilities of the bank.
	BALANCE SHEET: LIABILITIES			
15	Maturity analysis of customer deposits	US UK Australia Germany Switzerland	Yes	To analyse deposits from customers and banks into four maturity bands.
16	Components of other liabilities	US UK Australia Germany Switzerland Japan Hong Kong (SAR, China)	No	To disclose separately major items such as accrual for interest payable, accrual for negative mark-to-market fair value of financial derivatives after tax and deferred taxation. For debt securities issued by the bank which mature after one year, to disclose interest rate (if fixed rate) and repayment date; for floating-rate securities, disclose interest fixing method.

Items		Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
	SHAREHOLDERS' EQUITY			
17	Movements in reserves	US UK Australia Germany Switzerland Hong Kong (SAR, China)	Yes (since 1997)	To provide the amount of each type of reserves at the beginning and end of the financial year, and the amount of any transfers to or from each type of reserves during the year.
18	Capital adequacy ratio	US UK Australia Germany Hong Kong (SAR, China)	Yes (BIS ratio only)	To disclose the following information on the capital adequacy ratio and components as defined by BIS:- • Tier I capital • Tier II capital • Capital ratios • Risk-weighted assets
19	Segmental analysis	US UK Australia Germany Switzerland Hong Kong (SAR, China)	No	To analyse items such as total assets and total income or profits before taxation by the following geographical groups:- • Singapore • ASEAN • Other Asia Pacific • Rest of the world.

Items		Countries which disclose the item	Do Singapore banks disclose the item?	Recommendations on disclosure of the item
	OFF-BALANCE SHEET			
20	Contingent liabilities (credit equivalents) and commitments by type	US UK Australia Germany Switzerland Hong Kong (SAR, China)	Yes (contingent liabilities)	To categorise off-balance sheet items into:- • contingent liabilities • commitments • financial derivatives
21	Financial derivatives - Notional amount by type (eg. IRS, FRA, futures, options purchased/written etc.)	US UK Australia Germany Switzerland Hong Kong (SAR, China)	No	To disclose the contract amount, the gross positive mark-to-market value, the gross negative mark-to-market value and the effect of legally enforceable netting arrangements for each type of financial derivatives.