THE AUDIT COMMITTEE SEMINAR 2017
RISING ABOVE COMPLEXITIES

The third ACRA-SGX-SID Audit Committee Seminar weighed up the upcoming changes in accounting standards and other regulatory developments impacting audit committees, and saw the announcement of several measures that can help directors navigate through those complexities.

Another record turnout of more than 550 directors and professionals came for this year's Audit Committee Seminar, "Rising Above Complexities – What Audit Committees Should Consider". Jointly organised by ACRA, SGX and SID, the event, which saw an overwhelming response, was held at the Marina Mandarin Singapore on 13 January 2017.

Opening the event, SID Chairman Willie Cheng, observed that the large turnout reflected the increasing demands expected of audit committees (ACs). For the coming year, this included the change to the prescribed accounting framework in Singapore, a new audit report with expectations of AC commentaries, targets for some audit quality indicators, and updates in regulatory reviews. He assured directors that SID and the regulators are doing what they can to help, with several support measures announced that day.

Guest-of-honour Mr Kenneth Yap, Chief Executive of ACRA, recapped Singapore's journey in improving financial reporting.

He announced changes to the Financial Reporting Surveillance Programme and initiatives that ACs can take to improve quality financial reporting.

The event also witnessed the launch of the new AC Guide produced by SID with the support of ACRA, MAS and SGX. This was followed by a short presentation on the AC Guide by Mr Gerard Tan, Treasurer of SID, and Mr Ng Siew Quan, Partner and Corporate Governance Lead of PwC.

Ms Bong Yap Kim, Senior Director, Financial Reporting and Strategy Division of ACRA, and Ms June Sim, Senior Vice President and Head of Listing Compliance of SGX, then updated the audience on the latest regulatory developments at ACRA and SGX respectively, using case studies to illustrate key findings and insights.

This was followed by a panel discussion on the topic "Working together to enhance quality and transparency of corporate reporting and disclosures". Moderated by Mr Daniel Ee, Vice Chairman of SID, the panellists included ACRA's Mr Yap; Mr Danny Teoh, AC Chairman on several boards; Mr Yeoh Oon Jin, Executive Chairman of PwC Singapore; and Mrs Chng Sok Hui, Chief Financial Officer of DBS Group. They shared their perspectives on the regulatory and practical challenges that ACs face.

In his closing address, Mr Tan Boon Gin, Chief Regulatory Officer of SGX touched on the three kinds of discipline – self-discipline, regulatory discipline and market discipline – which are critical for a disclosure-based regime to work.

At the Seminar, SID also announced the establishment of its first ever Chapter, the AC Chapter, which is aimed at building capacity and enhancing the effectiveness of ACs.

At the end of the seminar, participants took away not only new insights and lessons, but also the new AC Guide, and a 2017 AC Mini-Guide of hot topics for the year.

Launch of the AC Guide

Self-Steps to Financial Reporting Quality

In his keynote address, Mr Kenneth Yap suggested four approaches that audit committees should consider in driving financial reporting quality:

- **Self-Learn.** ACs should keep up to date with the ever-evolving and ever-complex financial reporting. This could be achieved by leveraging resources such as the AC Guide and 2017 AC Mini-Guide.

- **Self-Help.** Directors should seek support from the audit committee fraternity itself. He encouraged AC members to actively participate in the SID AC Chapter to "treat it as your collective voice; both to step up your game internally as well as to represent your interests and provide feedback to other stakeholders."

- **Self-Assess.** ACs can develop indicators to self-assess the adequacy and competency of the company's finance function. ACRA will be developing a set of financial reporting indicators that can help companies measure where they stand in terms of their financial capability. This would provide an objective industry benchmark for directors and management to assess their ability to deliver quality financial statements.

- **Self-Account.** ACs should adopt the principle of self-accounting in its engagement with stakeholders. ACs should consider providing a commentary on the auditors' KAMs in the annual report.

AC Guide Raises Corporate Governance Bar

Mr Danny Teoh who is an AC Chair on several companies and a member of the AC Guide Review Panel, commented that the AC Guide can be a doubled-edged sword. On the one hand, it is meant to help the AC, but on the other, it sets the bar high. He concluded that AC members should "therefore strive to read and understand the Guide thoroughly".

L to R: Mr Tan Boon Gin (Chief Regulatory Officer, SGX), Mr Ng Yao Loong (Executive Director, MAS), Mr Kenneth Yap (Chief Executive, ACRA), Mr Willie Cheng (Chairman, SID), Mr Yeoh Oon Jin (Executive Chairman, PwC Singapore).

The AC Guide: More than a third edition

The co-leads of the AC Guide Working Committee, Mr Gerard Tan, SID Treasurer and Mr Ng Siew Quan, Corporate Governance Leader of PwC Singapore presented on the journey and contents of the AC Guide. Summarised here are their key points:

- The original guide for ACs, the *Guidebook for Audit Committees in Singapore* was released by ACRA, MAS and SGX in 2008, with a second edition in 2014. The AC Guide incorporates all the contents of the original guidebook plus more.

- The AC Guide is one of seven Guides in the *Corporate Governance Guides for Boards in Singapore* series.

- It is a one-stop resource for AC members of Singapore-listed companies with practical guidance on the discharge of their functions, duties and responsibilities in the context of Singapore's business and regulatory environments.

- What's in the 512-page book:
  - 7 sections with 92 FAQs.
  - 50 appendices containing templates, forms and processes.
  - 25 practical case studies.

- New topics include data analytics; anti-money laundering and countering financing of terrorism; audit quality indicators; new external auditor's report and AC's commentaries; Financial Reporting Surveillance Programme; and consolidated disclosure requirements and guidelines.

Mr Gerard Tan

Mr Ng Siew Quan

- Leading practices suggest that AC members should:
  - Understand the business of the company.
  - Understand the nature and trends of the industry it is operating in.
  - Understand the people in-charge of the business.
  - Sponsor, protect and promote the internal auditor, the paid staff working for and reporting to the AC.
  - Do their homework to prepare for the AC meeting.
  - Trust management (if appropriate), but verify what is presented.
  - Have a point of view and add value to the AC.

- In the same light, an AC member should not:
  - Pass the buck, relying on other AC members.
  - Pretend to understand, instead ask questions to clear any doubts.
  - Bark up the wrong tree and cause the loss of productivity.
  - Be led round and round the garden by management.
  - Simply rely on a standard checklist in reviewing the work.
  - Miss the forest for the trees.
  - Leave the auditors in the lurch by not appropriately supporting them.

SGX Regulations

Review of CG Disclosures by Mainboard Companies

- Survey on the existence and quality of disclosure of 545 mainboard companies conducted by KPMG.

- Report published on 5 July 2016 and presented at "The State of Corporate Governance Disclosures Forum" held on 16 August 2016. (Ed: see report on the forum in *SID Directors' Bulletin* 2016 Q4, page 66).

"Low Hanging Fruits" to Improve Disclosures

- Most companies do not appoint alternate directors but two-thirds of them do not state this in the CG Report.

- Disclosure of poll voting and voting results.

- Disclosure of whether the company has dedicated policy or protocol in place for investors.

- Explicit statement of whether the company is required to have at least half the board comprising independent directors or to have a lead independent director.

- Disclosure of whether any AC members were previous partners or directors of the existing auditing firm within the previous 12 months and whether any of the AC members hold any financial interest in the auditing firm.

- Explicit statement on preparation of minutes and it being available on website or to shareholders upon request.

Disciplines in a Disclosure-Based Regime

- **Self Discipline.** This is where companies make quality disclosures on their own accord. For example, AC commentaries on KAMs will give investors an additional perspective and further insights.

- **Market Discipline.** The last two years have shown how market can punish the share price of a company when there is a lack of confidence in a company's disclosure. This is where investors are playing their part in a disclosure-based regime.

- **Regulatory Discipline.** This requires enforcement actions on errant companies:
  - Regulatory action cannot take too long because it has an impact on market confidence. Thus, SGX has been taking prompt and proportionate action against disclosure breaches.
  - SGX seeks to achieve its regulatory objectives in a more effective manner using a more targeted approach, for example, its refinements on "trade with caution" alerts and minimum trading price requirements in the last year.
  - With the increased transparency of financial statements, the more individual and targeted engagement with companies, the broadened definition of materiality, and the more robust enforcement of disclosure breaches by both the regulators and the market, in other words, an increase in all three disciplines – SGX sees the opportunity to recalibrate its continuous disclosure regime, including its policy on quarterly reporting.

Does it matter if a misleading disclosure had no effect on share price?

"The recent amendment to the Securities and Futures Act has now clarified that the test for materiality is not tied to just whether the information caused any movement in share price, but whether or not the information, viewed objectively, is likely to wrongly influence investor behaviour. This clarification establishes a wider test for materiality and sets a higher standard for disclosures."

Mr Tan Boon Gin

Why is remuneration disclosure so poor?

"Disclosure of remuneration is the poorest with an average score of 53 per cent. A common reason given is fear of poaching. But how can the founding director who is the controlling shareholder of the company be concerned about poaching? The company should be transparent about remuneration including how rewards are linked to performance; and whether performance measures have been met."

Ms June Sim
Senior Vice President and Head of Listing, Singapore Exchange

"Singapore is a small market. The risks from remuneration disclosures on a named basis, such as staff poaching and unhealthy comparisons, are particularly significant in certain industries. DBS currently discloses the aggregate remuneration of its 18-member management committee, which I believe adequately preserves the spirit of this requirement which is to afford greater transparency of pay scales at the most senior levels."

Mrs Chng Sok Hui

"The banking industry is susceptible to poaching of key personnel. I can, therefore, understand the reluctance of banks to provide detailed information on the remuneration of their top management."

Mr Danny Teoh

"Are companies conveniently using the reason of poaching to avoid disclosing the remuneration of both directors' as well as senior executives' pay in the annual report?"

Mr Edward Lee
Director, QAF Limited

Financial Reporting Surveillance Programme (FRSP)

2nd FRSP Report

- ACRA issued report in September 2016, covering 50 sets of 2014 listed companies' financial statements.
- Key conclusions:
  - Good quality of financial reporting.
  - Fewer cases with serious breach.
  - Prompt remediation by company.

FRSP Adopts Restatement First Approach

- **Restatements first.** Come 1 April 2017, ACRA will adopt a "restatement first" approach to ensure financial reporting breaches are remediated on a timely basis and communicated promptly for the benefit of investors. While previously the first course of action was to sanction directors for breaches, the new approach will have companies that have committed serious financial reporting breaches, restate, re-audit and re-file their financial statements. Later this year, ACRA will be empowered to apply to court to compel companies to restate should they fail to comply. And only if companies fail to do so, will ACRA then hold the directors accountable.
- **Streamlined enquiries.** Enquiry letters will seek directors' views on potential non-compliances with accounting standards (NCs). In complex cases, facts and circumstances will be clarified via meetings with company representatives or e-mails with CFOs or both.
- **Hear other views.** For selected potential serious NCs (e.g. judgemental issues), auditors and specialists will be engaged formally in the review process.
- **Upfront on outcome.** For serious NCs, a closing meeting will be held with the directors before finalising the outcome. For other NCs, regulatory outcome will be indicated in enquiry letters, where practicable.
- **Timely restatements and more transparency.** To keep investors informed on a timely basis, ACRA may issue a press notice when a company unreasonably refuses to restate and announce within the prescribed time for NCs that materiality affect key financial statements line items.

FRSP Review Focus for 2016 Financial Statements

- **Going concern.** Is this assumption appropriate? If yes, are the disclosures adequate?
- **Value of long-life assets.** Is there any indication of impairment? If yes, was impairment test conducted? If no impairment charge, why so and are the assumptions realistic?
- **Significant one-off gain / loss.** Does it reflect the economic reality of arrangements?
- **Consolidation or Equity Accounting.** Have reserved matters or other contractual rights been considered?
- **Business acquisitions.** Have significant specific intangible assets, for which a premium was paid, been carved out from goodwill and separately recognised?
- **Statements of cash flows.** Are the cash flows appropriately classified within operating, investing or financing cash flows?
- **Significant judgement and critical estimates.** Are disclosures tailored to the circumstances?

Directors not responsible?

"In the first two review cycles since 2014, we have seen ACRA taking a tough stance towards directors when serious non-compliance with accounting standards was identified. With this shift towards 'restatements first', does this mean that ACRA has 'seen the light' and hence, is taking a step back from holding directors responsible?"

Mr Daniel Ee

"The objective of the FRSP is not to hang anyone but to protect the interests of the public. As the previous FRSP approach was perceived as adversarial, moving forward, ACRA's new approach is based more on fact-finding, instead of issuing enquiry letters. ACRA intends to engage the CFO and management to ask questions and gain insight into the situation."

Mr Kenneth Yap

Restatements First or Not At All?

"ACRA is always guided by the public interest. With this new initiative, ACRA envisions a smoother process with greater transparency without the shadows of fear and suspicion from the companies. Contrary to common perception, there will be less requests for restatement as ACRA intends to move through the questions in a quicker manner to cover ground. For complex cases, it will seek the advice of a technical advisory panel and independent reviewers from ISCA. Be rest assured that ACRA does not proceed further unless there is a unanimous agreement amongst these parties."

Mr Kenneth Yap

"When a set of financial statements requires restatement, it means it contains material misstatement. It calls into question whether the pre-restatement financial statement gave a true and fair view."

Mr Kyle Lee
Director, Great Eastern Life

"Restatement is a super serious thing. In the US, a restatement could result in an avalanche of lawsuits directed against the company."

Mr Danny Teoh

"Now that it will have new powers, will ACRA still be just as judicious in the use of these powers and how rigorous are the internal review processes before it request companies to restate their financial statements?"

Mr Wang Kai Yuen
Director, Comfort Delgro Group

Enhanced Auditor's Report

L to R: Mr Daniel Ee (Chairman, SID AC Chapter), Mrs Chng Sok Hui (Chief Financial Officer, DBS Group), Mr Danny Teoh (AC Chairman, Keppel Corporation), Mr Kenneth Yap (Chief Executive, ACRA), Mr Yeoh Oon Jin (Executive Chairman, PwC Singapore).

New Auditing Standard

- The enhanced auditor's report (EAR) will be effective for 2017 audits of financial statements for all listed companies.
- At least 10 listed companies have early adopted the standard in 2016.
- EAR will add transparency through new reportable items, in particular:
  - Material uncertainty on going concern.
  - Key audit matters (KAMs).
  - Other information (OI).

KAMs

- Matters which, in the view of the auditor, were of most significance in the audit of the financial statements.
- ACs should:
  - Engage the auditor and review the KAMs well in advance of reporting deadlines.
  - Prepare for AGM and analyst questions on the KAMs.
  - Be cognisant of inconsistencies between KAM and related matters disclosed in annual report.

Other Information (OI)

- OI = annual report – financial statements.
- Auditors' responsibilities grew for OI from reading OI to ascertain consistency with financial statements, to reviewing OI for material misstatements and reporting on it.
- Expectation gap exists when OI is not ready before audit report is signed off. ACs should resolve this with their auditors.

AC Commentary

- AC commentary on KAMs in annual report serves to inform shareholders on the AC's view on significant financial reporting matters.
- AC commentary should highlight the AC's due consideration, judgement calls made, and bases for conclusions.
- AC commentaries are practised in the UK and are increasingly being demanded by investors here.
- ACRA, MAS and SGX will be issuing letters to encourage ACs to provide such commentaries in the 2016 financial statements.

How are you preparing for the EAR?

"To me, EAR is another effort on the journey to communicate and engage stakeholders more meaningfully. Integrated reporting, sustainability reporting and enhanced risk disclosures are all part of this journey. At DBS, there is a standard agenda item at every AC meeting, namely, "Significant Matters Update". This update covers significant financial reporting matters requiring the exercise of judgement such as loan loss provisions, valuation of complex instruments and goodwill impairment. These are the same topics that our external auditors would look into, and this alignment has permitted a smooth transition to EAR."

Mrs Chng Sok Hui

"As EARs can sometimes involve disclosure of complex accounting or judgemental issues, PwC has formed an internal panel to review each EAR with our clients to ensure that the information is disclosed in a clear and concise manner for the average investor. There is also a need to raise the awareness level and education of the public shareholders on the EARs."

Mr Yeoh Oon Jin

What if "Other Information" (OI) is not available?

"The new requirements of the auditor to read and opine on OI could create some practical difficulties. If, at point of signing the auditors' report, the OI is not ready – as is usually the case – then, the auditor needs to state so. The auditor could potentially close the gap later on through a separate communication to audit committees prior to the AGM. Investors and market analysts will need to understand this anomalous gap in the auditor's opinion."

Ms Bong Yap Kim

"If the annual report is not available for review at the time of results announcement, typically at the end of February for those with calendar year ends, the auditor would now have to qualify the opinion regarding the OI. One of the possible way forward is to have a separate auditor's opinion on the OI prior to AGM to clarify that the information has been reviewed but not audited."

Mr Yeoh Oon Jin

Would an AC Commentary be useful?

"The purpose of the AC commentary is to respond, pointedly and in a targeted fashion, to issues that were highlighted by auditors and not fully resolved in the eyes of investors. While it is not mandatory, a recent study by ACRA, ISC and NUS found that all institutional investors and 95 per cent of retail investors surveyed wanted AC commentaries. "

Mr Kenneth Yap

"The investing community will always want more information and the AC commentary will certainly give more insights on the work of the AC. Despite this, I think shareholders will continue to focus their questions on business performance and future prospects of the company at AGMs."

Mr Danny Teoh

Audit Quality Indicators (AQIs)

The AQI Journey

- In October 2015, ACRA launched the AQI Disclosure Framework.
- In January 2016, data for the eight AQIs were provided to ACs.
- In August 2016, ACRA sets six targets for selected AQIs.

The AQIs

- Engagement-level indicators:
  (1) Audit Hours
  (2) Experience

- Engagement- & Firm-level indicators:
  (3) Training
  (4) Inspections
  (5) Independence

- Firm-level indicators:
  (6) Quality Control
  (7) Staff Oversight
  (8) Attrition Rate

Targets are meant as conversation starter

"Whilst enticing, audit committees should not conclude on an auditor's ability to execute quality audits purely by number comparison to the AQI targets. AQIs should be used as a conversation starter, and it is the conversation between audit committees and the auditors on audit quality that matters more."

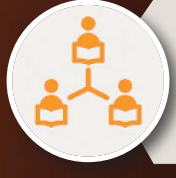
Ms Bong Yap Kim

AQI Targets

- The six targets on AQIs to kick-start discussion on audit quality are:

Firm-Level Targets

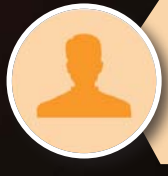
Staff retention rate: 75% to 80%



Staff per partner < 15
Staff per manager < 5

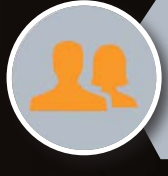
No. of listed company audits with same FY-end: 5

Engagement-Level Targets



Lead audit partner hours over total audit hours
≥ 5% for normal risk audit
≥ 10% for high risk audit

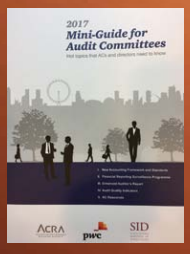
Concurring partner hours
≥ 13 hours



Partner and manager hours
≥ 20% of total hours

Other AC Resources

AC Mini-Guide 2017



- The second edition of a quick and handy guide for AC members to obtain a birds-eye view of the hot topics for 2017.
- Topics include: New Accounting Framework and Standards, FRSP, Enhanced Auditor's Report, AQIs and AC Resources.

SID AC Chapter

- SID has established an AC Chapter to build the capacity and improve the effectiveness of ACs.
- It will be for a community of people involved with ACs – AC chairmen and members, management personnel in companies who provide support to or interact closely with ACs, and professionals who provide support to ACs.
- The aims of the AC Chapter include:
  - Providing a platform for active discussion on issues relevant to ACs.
  - Developing thought leadership for ACs.
  - Contributing to the professional development of ACs.
  - Advocating on issues that are relevant to ACs.
- Any SID member can sign up to be a Chapter member. There is no chapter membership fee.

AC Chapter Pit Stops 2017

1. **Relevance of the Enhanced Auditor's Report to Directors, ACs and Management**
   16 February 2017, 0900 to 1100
   Partner: Deloitte

2. **Financial Reporting Surveillance Programme (FRSP) and Audit Quality Indicators (AQIs)**
   12 April 2017, 0900 to 1100
   Partner: ACRA

3. **Practical Implications of FRS 115 Revenue from Contracts with Customers**
   27 July 2017, 0900 to 1100
   Partner: KPMG

4. **Practical Implications of FRS 109 Accounting for Financial Instruments**
   7 September 2017, 0900 to 1100
   Partner: PwC Singapore

5. **Demystifying Sustainability Reporting and Integrated Reporting**
   16 November 2017, 0900 to 1100
   Partner: EY

"As audit committees lead a fast-paced life and work very hard, we have organised some pit stops along the way for them to recharge and refresh themselves."

Mr Daniel Ee
Chairman, SID AC Chapter