KEYNOTE ADDRESS BY MR KENNETH YAP, CHIEF EXECUTIVE, ACCOUNTING AND CORPORATE REGULATORY AUTHORITY AT THE ACRA-SGX-SID AUDIT COMMITTEE SEMINAR, FRIDAY, 13 JANUARY 2017, MARINA MANDARIN HOTEL, MAIN BALLROOM

Mr Willie Cheng, Chairman of SID

Mr Tan Boon Gin, Chief Regulatory Officer of SGX

Mr Ng Yao Loong, Executive Director, Markets Policy and Infrastructure of MAS

Distinguished guests

Ladies and gentlemen

Good morning. It is my pleasure to be here this morning at the third ACRA-SGX-SID Audit Committee seminar. I know I speak for my fellow organisers, SGX and SID when I say that we are much encouraged by yet another record-breaking attendance at the third iteration of this seminar. Your support is a clear testament of the commitment that audit committees are vesting in their mission to uphold financial integrity and trust in your companies.

Staying Globally Competitive by Maintaining Market Confidence

2 In the latest Corporate Governance Watch 2016 report released by the Asian Corporate Governance Association (ACGA), Singapore maintained its top position in the regional corporate governance ranking. It is a fitting acknowledgement of the joint effort of companies, professional bodies, regulators and other stakeholders to strengthen our corporate governance landscape in the last few years.

3 With a gloomy global outlook ahead, it may be tempting to call for a time-out and relegate regulatory matters to the back burner. After all, why worry about guarding the pot when you have trouble filling it. This, however, is short-sighted. It is when

companies come under pressure that the risk of corporate wrongdoing is ironically at its greatest. And when the chips are down, it is a strong corporate governance and financial reporting culture which shores up confidence among investors looking for a safe haven amidst troubled times.

4 Indeed, corporate reporting is an area which both SGX and ACRA have been paying very close attention to, given the increasing importance of accurate and timely financial disclosure in a volatile market. SGX has stepped up its public enforcement with a focus on prevention and containment. Several listed companies have been issued 'public reprimands' for failures to make balanced and fair announcements. A separate and independent regulatory subsidiary will also be set up later this year. Concurrently, ACRA has strengthened and evolved our Financial Reporting Surveillance Programme or FRSP in short, in a way we believe will bring greater transparency to the market and raise its effectiveness.

Financial Reporting - Focusing on Timely and Reliable Disclosure for Investors' Benefit

5 At the company level, directors play a critical role in ensuring the reliability and integrity of the business and financial information that is imparted to investors. They alone have a duty under sections 201(2) and 201(5) of the Companies Act to prepare true and fair financial statements that are in compliance with accounting standards.

6 Indeed, the misapplication of accounting standards can have drastic implications. In a recent case reviewed by ACRA's FRSP, a listed company invested in a property project that was handled through a BVI company. However, it did not directly own the BVI company as is usual under circumstances. Instead it entered into a notes receivable arrangement coupled with rights of control over the BVI company. The directors neglected to consider the commercial reality of the arrangement and did not consolidate on the basis that they had no ownership of the BVI company. The losses made by the BVI company were therefore not captured, while instead, the interest income from the notes was recognised as profits. This grossly inflated the

company’s profits by more than 90%. Needless to say, this makes a staggering difference to any investor.

7 It is therefore comforting that, after completing two review cycles of the FRSP, we find that listed companies accept the importance of complying with accounting standards. Many are taking steps to improve the quality of their financial statements. Indeed we are very heartened to see in the second round of the cycle that the results have really improved and there have been less findings. Many listed companies also took quick action to remediate financial reporting gaps highlighted by the programme. This validates our belief that most non-compliances are neither intentional nor fraudulent in nature, but arise from inadequate knowledge of accounting standards and inadequate support made available to directors.

8 Having garnered these insights over the past two years, ACRA will be revising our enforcement approach. Previously, our first course of action was to sanction directors for breaches of accounting standards. With effect from 1 April 2017, ACRA will instead adopt a ‘restatement first’ approach. Our emphasis will be on ensuring that companies remediate the financial reporting gaps and communicate their effects to the public in a timely manner for the benefit of investors. Depending on the severity of the breaches, remediation could range from restating comparatives in the following year’s financial statements to restating, re-auditing and re-filing past years’ financial statements.

9 For the minority of companies that fail to comply with our order, ACRA will soon be able to apply to court to compel companies to re-state financial statements where necessary. Investors can thereby be assured that companies will re-mediate financial reporting gaps promptly. And only if companies fail to do so, will we hold the directors accountable. Sanctions could then be levied through the issuance of warnings, composition fines or even prosecution for the egregious cases. To ensure that investors are informed on a timely basis, ACRA will issue company-specific press releases in these instances, to ensure that any gaps in financial reporting are quickly brought to light.

Audit Committees - Taking the Lead to Drive Financial Reporting Quality

10 Ultimately, whilst enforcement is necessary to set the right tone, sustainable improvement in financial reporting quality must be driven by a collective effort. In this regard, audit committees must take the lead and set the bar high. Regulators such as ACRA and SGX and professional bodies such as SID will continue to provide support but the drive to improve financial reporting quality must be initiated and realised from within. In this regard, I would like to suggest four approaches for audit committees to consider.

a) Self-Learn: Audit Committee (AC) Guide and Mini-Guide
First, audit committees should "self-learn" and keep up to date with the ever-evolving and ever-complex financial reporting landscape. This could be done by leveraging on the audit committee guide that is launched today. I also encourage audit committees to tap on the 2017 AC Mini-Guide, put together jointly by SID, PWC and ACRA, which usefully summarises key regulatory signposts such as the enhanced auditor's report that audit committees should look out for when approving 2016 financial statements.

b) Self-Help: AC Chapter
The second approach that I would propose as most useful is "self-help" from the audit committee fraternity itself. In this regard, I must extend my commendation to the SID for its timely establishment of an AC Chapter. By tapping on the wealth of members' experience, the AC Chapter can provide thought leadership, share best practices and help audit committee members stay attuned to financial reporting developments and trends. It will also be an extremely useful forum to provide feedback to regulators on what can and cannot be done and to explore practical solutions to common challenges together. I urge audit committee members present today to seize this opportunity to actively participate in a meaningful way. Treat the AC Chapter as your collective voice, both to step up your game internally as well as to represent your interests and provide feedback to other stakeholders.

c) Self-assess: ACRA's Financial Reporting Indicators (FRIs) project

The third approach I would encourage audit committees to adopt is one of self-assessment. Our observation over two years of surveillance have shown that inadequate resources and support for finance function is the root cause for deficiencies. Audit committees must pro-actively identify your company's financial reporting gaps and discuss with management on how to address them. Quality financial reporting starts with having the right processes and the right people. CFOs and AC Chairmen should champion this cause with senior management and the Board, and it would be most helpful if there was an objective and commensurable basis to advocate this position.

In 2015, ACRA launched the Audit Quality Indicators (AQI) disclosure framework to help audit committees of listed firms better evaluate and select auditors. This was followed by the introduction of six AQI targets last year, which provide audit committees with common yardsticks to compare audit quality.

Building on the same principle, audit committees can likewise develop indicators to self-assess the adequacy and competency of the company's finance function. ACRA will be exploring the feasibility of developing a set of financial reporting indicators that can help companies measure where they stand in terms of their financial capability, as well as provide an objective industry benchmark that will allow directors and management to take stock of their ability to deliver quality financial statements. We plan to seek your inputs on this study in the near future, and look forward to working with SID's new AC Chapter to co-create the concept of financial reporting indicators.

d) Self-account: Adoption of AC Commentary by audit committees

Finally, I urge ACs to adopt the principle of self-accounting in its engagement with stakeholders. With the advent of enhanced auditor reporting, auditors of listed companies will soon report on Key Audit Matters (KAMs). This refers to matters that took the most time and effort for auditors to resolve during the process of auditing financial statements. Typically, these are matters that are highly complex and judgmental.

However, the auditor commentary on KAMs alone may not be able to fully convey the company's position to investors and other stakeholders. Audit committees should consider providing a commentary that shares their perspectives on how significant financial reporting matters are being addressed. This helps to round up the conversation that has been opened with enhanced auditor reporting. AC commentary has been practised in leading jurisdictions such as the UK.

I am acutely aware that this proposition will require a significant shift in mind-set. Directors may feel that the company's position is often conveyed in the annual report itself, and that a response by way of an AC commentary is superfluous and merely adds to compliance cost. I fully agree that it would be a waste of time for an AC commentary that is a boilerplate repetition of already published material. However, that was and is never the intent. The point of an 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. This is also why it is not the regulatory intent to mandate such a commentary – for in some cases, it may not be necessary at all if there is little left to respond to.

Having said that, there is strong demand for such a commentary. In a recent joint study by ACRA, ISCA and the NUS, all institutional investors and 95% of retail investors surveyed wanted audit committee commentaries. The strength of this feedback suggests that investors want audit committees to speak directly to their role as guardians of the sanctity of the financial statement. This can only increase transparency and raise confidence among investors in the companies' decision-making process. For this reason, ACRA and SGX will continue to champion and monitor the publication of such reports by companies. Together with MAS, ACRA and SGX will also be issuing letters to encourage you to provide such commentaries for your 2016 financial statements.

Conclusion

11 To conclude, in an economic climate of uncertainty, it is critical that we work together as directors, company management, auditors and regulators to assure investors of the integrity and reliability of the business information they receive. We should do so because there is intrinsic value in this process, and not maintain high corporate governance standards just because the market regulators say so, or because we want to win international accolades.

12 With these developments, I do believe 2017 will be a watershed year as far as the development of quality financial reporting is concerned. On that note, I wish everyone a fruitful seminar, and a most productive and successful year ahead. Thank you.