2025 Mini-Guide for Audit and Risk Committees

Hot topics that ARCs and Directors need to know

- Areas of Review Focus for FY2024 Financial Statements
- Operation Unlock Value – Growth through 4 Forms and a Loop
- Generative AI: Creating Value through Governance
- SID Audit & Risk Committee (ARC) Chapter

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SGX Group
ACRA Accounting And Corporate Regulatory Authority
SID Singapore Institute of Directors

Areas of review focus for FY2024 financial statements

As businesses navigate an increasingly complex global landscape, the shifting macroeconomic environment and climate-related challenges will impact financial reporting in FY2024. In light of these developments, ACRA has issued its 2024 Financial Reporting Practice Guidance, identifying key financial reporting areas that require closer attention by Audit Committees (ACs) in their review and oversight of the FY2024 financial statements (FS).

Shifting macroeconomic environment

While the Singapore economy may achieve a small level of growth, it continues to face challenges from supply constraints, rising costs, and climate change efforts, potentially leading to within-sector consolidation and enduring inflationary pressures. Accordingly, the following areas of review focus were identified:

1. Expected credit loss assessment – the need to use reliable macroeconomic data including forward-looking assumptions, and perform unbiased scenarios evaluation.
2. Impairment assessment – consider inflation and interest rates impacts on cash flow projections and growth assumptions; reversal of impairment (excluding goodwill) is only possible when estimates change since the last impairment and there should be clear disclosure of the events that led to these reversals.
3. Fair value (FV) measurement – consider current market conditions and provide detailed disclosures of valuation techniques and inputs; for non-financial assets, consider their highest and best use value; ensure adequate disclosures, especially sensitivity to changes in unobservable inputs for Level 3 FV measurements, and FV hierarchy level and valuation techniques/inputs for assets and liabilities not measured at FV but the FV is disclosed.
4. Business acquisitions – when determining the acquisition date and assessing the level of control over investees, carefully evaluate the specific contractual terms and conditions and underlying rationale for the acquisition; evaluate whether there should be separate recognition of specific intangible assets from goodwill.

Climate-related considerations

Climate-related events have triggered sustainability measures and environmental policies to be put in place, such as implementation of carbon tax increase, which in turn, increases electricity and gas tariff. Companies' performance may be affected by climate-related regulations, risks, and initiatives like net-zero commitments, green financing, and involvement in the voluntary carbon market. Below are some of the key areas for ACs to focus their review on:

1. Ensuring a coherent and connected reporting between sustainability reports and financial statements.
2. Being mindful of the accounting implications and related disclosure requirements as a result of participation in any renewable energy projects and emission schemes.
3. Understanding and assessing the impact of climate-related risks on financial statements, especially impairment on non-financial assets. Any key climate-related assumptions used in impairment assessment should be reasonable, supportable, and clearly disclosed.

Spotlight on specific accounting standards

1	**Amendments to SFRS(I) 1-12 International Tax Reform – Pillar Two Model Rules related to Base Erosion and Profit Shifting (BEPS) Pillar Two**	Singapore will implement the Domestic Top-Up Tax and Income Inclusion Rule under Pillar Two for in-scope companies from financial years commencing on or after 1 January 2025. Affected companies should disclose the use of the mandatory temporary exemption for related deferred taxes and provide estimates of their exposures, where applicable. Companies should also separately disclose current tax expenses related to Pillar Two in jurisdictions where the legislation is effective.
2	**Scope of SFRS(I) 17 Insurance Contracts**	Effective from 1 January 2023, SFRS(I) 17 applies to all issued contracts meeting its criteria, not just those by insurers. Companies should assess if any of their contracts fall within SFRS(I) 17's scope. Some contracts may be excluded or allowed to be accounted for under other standards like SFRS(I) 9 and SFRS(I) 15.
3	**SFRS(I) 18 Presentation and Disclosure in Financial Statements**	Effective from 1 January 2027, SFRS(I) 18 will replace SFRS(I) 1-1 Presentation of Financial Statements. It restructures income statements presentation into operating, investing and financing categories and requires disclosures of management-defined performance measures. As retrospective application is required, early planning is essential for a smooth transition.

For more information, please scan this QR code to access ACRA's Financial Reporting Practice Guidance 2024.

https://go.gov.sg/frpracticeguidance
2024

"Operation Unlock Value – Growth through 4 Forms and a Loop"

> "I find the great thing in this world is not so much where we stand, as in what direction we are moving: To reach the port of heaven, we must sail sometimes with the wind and sometimes against it, but we must sail, and not drift, nor lie at anchor."
>
> – Oliver Wendell Holmes

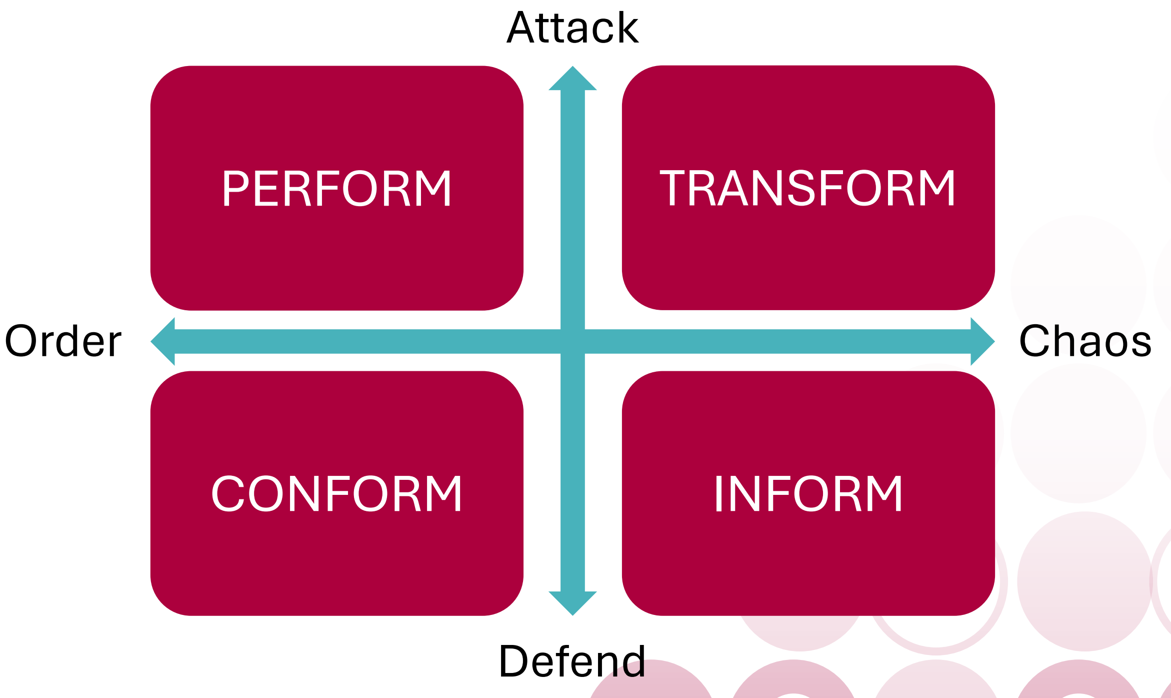
Businesses strive for growth. How do boards navigate the evolving global and business environment to deliver shareholder and stakeholder value?

GROWTH

Growth strategies come in different Forms. Corporate boards would be familiar with the expectation that they Conform and Perform. Boards must Conform to legal, regulatory, and other requirements that, among other things, establish a level playing field; at the same time, they must drive operational and commercial out-Performance. Conform is a defensive play that protects against potential downsides, while Perform focuses on the offensive to move the business forward.

But expectations are evolving along with the rapidly changing external environment. Against the uncertainties, boards are still expected to deliver and be seen to deliver shareholder and stakeholder value. In a more chaotic environment, they must go beyond Conform and Perform, to also Transform and Inform. New challenges also give rise to new opportunities, and the best companies are those that are able to Transform their business strategies and even operating models to reap the first-mover advantage. At the same time, boards and businesses must engage their shareholders and other stakeholders, to simultaneously become better Informed of their views and expectations, and to communicate and obtain their buy-in.

The 4 Forms can be represented by the following diagram:



ACTION PLAN

The OODA Loop – Observe, Orient, Decide, Act | repeat – is one example of a decision-making tool that can help guide a board in reforming and evolving its business strategy. This framework is well used in many fields such as business, military, and law enforcement. It was developed by United States Air Force Colonel John Boyd as an iterative process to help individuals and organisations make better decisions in an environment of constant change. Jamie Dimon, Chairman and Chief Executive Officer of JPMorganChase, is a strong believer in this management tool.[1] How do businesses use this tool in a corporate context?

Observe

All decisions require information as input. The company should review its current situation. This allows the company to gain situational awareness of its existing position.

This may include an analysis of the following areas:

- Business model: customer base and supplier profile, characteristics of products and services, geographical reach, revenue, cost and profit contribution of each business segment
- Market environment: size of the market, market share, penetration rate, characteristics of substitute products and services
- Competitive advantage: major factors of competitive advantage, such as technology, business model, reputation, human resources, economic capital
- Risks: major factors such as macroeconomics, cross-industry or idiosyncratic risks

The company should also select indicators to track its performance that are relevant to the company's long term value. The range of indicators can be financial and non-financial.

Some examples of financial indicators include the following:

- Market valuation: price-to-book (PB) ratio, price-to-earnings (PE) ratio
- Capital efficiency: return on equity (ROE), return on invested capital (ROIC), cost of equity (COE), weighted average cost of capital (WACC)
- Shareholder returns: dividend amount, dividend payout ratio, dividend yield, total shareholder return
- Growth: revenue growth, operating profit growth, asset growth
- Others: asset portfolio, debt ratio, free cash flow (FCF)

Examples of non-financial indicators include the following:

- Effectiveness of the board of directors
- Diversity of the board of directors
- Corporate culture of the company
- Protection of interests of shareholders as a whole

Orient

The company should then analyse and synthesise the observed data.

The company should be aware of the context in which it processes the data. For example, the same observed fact may give rise to different interpretations by different individuals, depending on their previous experience and background.

Similarly, the organisation has its own history and corporate culture. It may be caught up in its existing narrative based on strongly-held beliefs, without critically assessing if those beliefs are still valid.

Each orientation shapes the observation, and consequently the decision and action. Knowing the mental model in which information is consumed increases the chance of better decisions.

In this regard, it is important for the board to comprise diverse viewpoints and perspectives.

[1] https://www.jpmorganchase.com/ir/annual-report/2023/ar-ceo-letters

Decide

After taking into account the insights from the orientation phase, the board needs to refine its options, then decide on a course of action that would best deliver on its objectives and on shareholder and stakeholder value.

For the decision to be meaningful, it must be accompanied by a plan and blueprint for operationalisation, including a realistic assessment of the resources required. The plans should also include corporate goals – ideally linked to the indicators being observed – and collate metrics to track progress.

Research shows that for matters of high consequence, productive interaction and healthy debate is a key factor in making good and fast decisions.[2] Boards meetings should be conducted to encourage discussion.

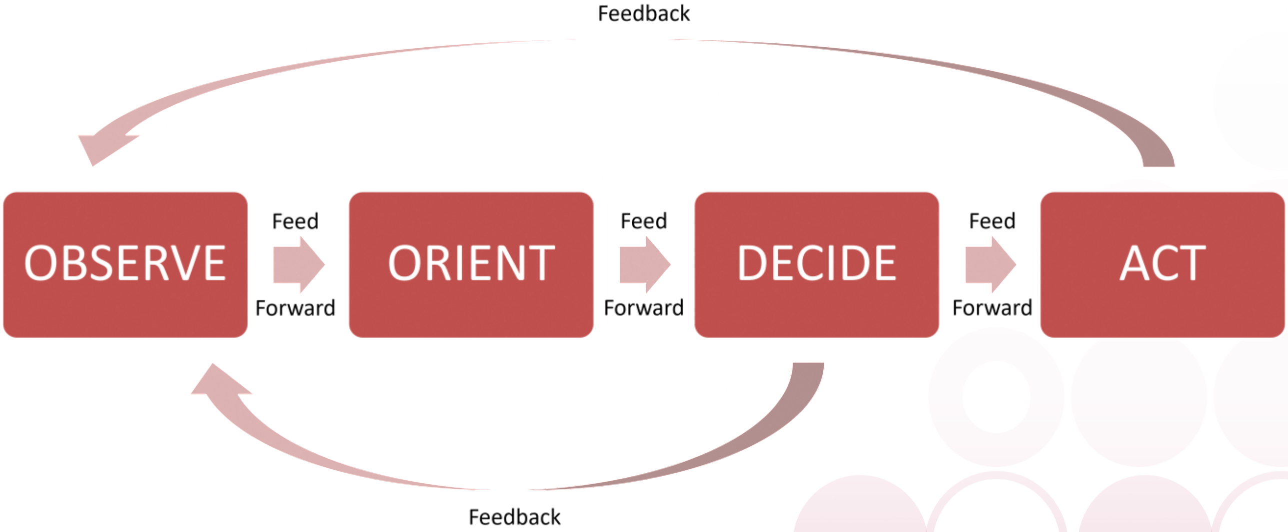
Act

The previous phases lead to the final one where decisions are translated into action. Plans are communicated and executed. It is not feasible to wait for perfect information before acting – in a rapidly-changing environment, one must make a reasonable assessment of the situation based on the best available data.

Communication of the company's corporate plan is important to ensure that shareholders are able to make informed decisions. It also sets accountability for the plans, and provides an impetus for growth.

Repeat

The OODA loop is an iterative process. As more observation and orientation is obtained, the information forms feedback for further evaluation. A diagrammatic representation of this loop is set out below.



[2] https://www.mckinsey.com/capabilities/people-and-organizational-performance/our-insights/three-keys-to-faster-better-decisions

Generative AI: Creating Value through Governance

The Evolution of Generative AI: Balancing Euphoria and Despair

In recent months, excitement around Generative AI (GenAI) has translated into palpable momentum. In PwC's Global Risk Survey 2023, 60% of survey participants considered GenAI as an opportunity rather than a risk. This optimism has spurred many organisations to launch GenAI-enabled capabilities, invest in GenAI skills and pursue ambitious AI strategies.

In the evolving GenAI ecosystem, Big Tech and venture capitalists are pouring investment into GenAI systems. Employees anticipate integrating GenAI tools into their daily workflows, and enterprise software vendors are augmenting their products with GenAI features.

Yet, organisations have also witnessed how things can go awry, from leakage of confidential data to public GenAI systems, struggles with "hallucinations", deep fakes, manipulated content, and bias.

Leveraging Existing Governance Frameworks

Developing a governance framework for GenAI does not necessarily require starting from scratch. Organisations with practices governing technology, from privacy and data governance to third-party risk management, and those with foundational components for AI governance, can adapt existing practices to address GenAI risks

One of the most pressing challenges is the scale of GenAI integration. Companies are offering new GenAI solutions almost daily, alongside abundant free or nearly-free tools online and GenAI capabilities provided by legacy software vendors. Getting a handle on enterprise-wide GenAI use and maintaining an up-to-date inventory of systems can pose significant challenge.

The nature of GenAI models exacerbates certain risks, such as those relating to data protection and IP. Consistent with risks seen with AI and emerging technologies, a holistic and standardised risk taxonomy around AI is likely to enable an organisation to triage systems based on their view of risks and align on approaches for remediation.

It is also imperative that risk management frameworks across regimes advocate AI governance that is proportionate to the associated risks. This alignment signals to the organisation that risk management is as important as the business goals it seeks to achieve with AI. Such alignment fast-tracks innovation by focusing on priority areas of investment where risk can be effectively managed.

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Establishing an Enterprise-wide Risk Taxonomy for AI

An effective risk taxonomy for AI could encompass the following categories:

Model risks

Risks related to the training, development, and performance of an AI system, including conceptual soundness, reliability of output and oversight.

Use risks

Risks related to intentional or unintentional misuse, manipulation, or attack against an AI system.

Data risks

Risks related to the collection, processing, storage, management, and use of data during the training and operation of the AI system.

Legal and compliance risks

Non-compliance with applicable laws, rules, and regulations, including privacy, sector-specific and function-specific guidance, and issues such as copyright and deep fakes.

System and infrastructure risks

Risks related to the acquisition, implementation, and operation of an AI system in a broader software and technology environment, including third-party and open-source risks.

Process impact risks

Unforeseen or unmitigated risks that arise from integrating the use of AI into an existing workflow.

It is of critical importance to educate governance personnel on how AI risks may manifest for the organisation's expected GenAI use cases and align on a mutually agreed point of view on risk prioritisation and appetite. AI systems that warrant closer supervision should be clearly identified, with designated teams made responsible for mitigating associated risks.

Updating Enterprise Perspectives on Risk and Values

Central to effective governance is a shared understanding of risks. The AI governance team needs to evolve beyond traditional operational risk management frameworks. This would warrant enhancing procurement, third-party risk management, security, privacy, data, and other associated risk and compliance measures to address risks that have either been elevated or created by AI.

Adopting a risk taxonomy for evaluating AI technologies and supervising established AI systems can assist in efficient oversight and resource allocation. The risk taxonomy should not only describe the nature of GenAI specific risks but establish a roles and responsibilities charter that formalises ownership of associated risk controls. Even internal codes of conduct must be refreshed to address instances of GenAI misuse.

As new dilemmas emerge around what it means to develop AI responsibly, there needs to exist formal channels to raise concern around them, facilitate their analysis and update policies, as needed.

Defining Roles and Responsibilities

To formalise governance, organisations will have to define new structures such as an AI steering committees or governance boards, who would influence internal policy development, support use case prioritisation, and address escalated issues.

These roles and responsibilities may be time-bound, or dialled up or down over time, considering the approvals, potential risks, decisions, and remediations that may occur at different stages of AI development, implementation, use, and monitoring.

Developing a Training and Change Management Programme

In the rush to embrace GenAI, employees may be tempted to use tools without proper understanding of the potential risks. Some organisations, as a result, have chosen to block internal use of publicly available GenAI. To allow employees to explore GenAI capabilities, focused training modules should be developed and implemented to educate them on how GenAI works and how risks manifest.

Organisations that move forward methodically, invest in a solid foundation of governance, and unite as a cross-functional team to face critical questions in unison, are most likely to be well positioned to celebrate the success offered by AI.

Responsible AI and Director’s Role

Responsible AI is crucial for a director of a company as it ensures that the deployment and utilisation of artificial intelligence align with ethical standards, legal regulations, and societal values. By prioritising responsible AI, directors can mitigate risks such as biases, privacy violations, and security threats, thereby protecting the company's reputation and avoiding potential legal repercussions. Directors of a company play an important role in the following aspects when it comes to enabling responsible AI.

Setting an AI Strategy
Integration of Data & AI Ethics into the core of the company's values involves a thorough consideration of the moral implications associated with the use of data and AI technologies. Directors must ensure that ethical principles such as fairness, transparency, and accountability are codified into the organisation's values, guiding the development and deployment of AI systems. Additionally, directors should stay ahead of key public policy and regulatory trends, anticipating changes that could impact the business. By understanding and aligning with these regulations, directors can establish robust compliance processes that not only mitigate legal risks but also reinforce the company's commitment to responsible and ethical AI usage.

Enabling Effective Governance
A comprehensive oversight mechanism should span across three lines of defence: operational management, risk and compliance functions, and internal audit. This multilayered oversight ensures that AI systems are monitored and evaluated rigorously from development through deployment and beyond. Directors must also expand traditional risk detection and mitigation practices to specifically address the unique risks and potential harms posed by AI technologies, including safeguarding against unintended consequences and compliance with regulations, organisational policies, and industry standards.

Enhancing day-to-day practices
Enabling responsible AI operational practices involves ensuring that AI models are interpretable and explainable, promoting transparent decision-making processes that stakeholders can understand and trust. At the same time, enhancing cybersecurity of AI systems is critical for ensuring robust protection against malicious threats and preservation of user data privacy. With the hype over AI, directors should assess problems at hand to justify the use of AI solutions, instead of jumping on the bandwagon without careful thought. Lastly, directors should consider the use of continuous monitoring for identification of model drift and emerging risks, ensuring that the AI systems remain effective and aligned with organisational goals and strategy.

The integration of AI into business operations presents both opportunities and challenges that require careful oversight from company leadership. As a director, it is imperative to stay informed and proactive in guiding your organisation through this transformative landscape. To assist any director in this endeavour, we have consolidated a list of critical questions designed to evaluate the company's current approach and use of AI. By addressing these key considerations, the company can navigate the complexities of AI implementation, mitigate potential risks, and capitalise on the benefits of this powerful technology.

The board's focus:

Develop a board approach

- How is the board continuing to get educated on AI and generative AI to better understand the technology?
- Who at the management-level is accountable for AI? Is there a management-level committee focused on AI to address opportunities, risks, controls and establish policies?
- Have we considered communications to stakeholders about our AI use? What are we communicating to investors?
- Given the pace of change, how do we enable agility to continue to innovate while addressing risks?

Oversee risks and controls for trusted AI

- What framework(s), if any, is the company using to implement AI technology responsibly?
- What policies, controls and processes does the company have in place to safeguard AI and generative AI models against related risks, misuse and unauthorised use? Are they aligned with established legal, privacy, security, and ethics policies and procedures? Is the board setting the tone on responsible AI use?
- What are the processes to independently validate and verify that AI systems are operating in a manner consistent with stated policies and objectives? Does internal audit have a role?

Understand strategic business opportunities

- What are the prioritised business use cases for our company? Are we looking at adoption at scale and in a holistic way? Are these use cases complementary to our other strategic business initiatives?
- Are the opportunities to disrupt ourselves (before we are disrupted) within our risk appetite?
- What processes do we have in place to evaluate the possible risks related to a third-party provider, if we are using such services?
- How will the talent strategy change? How will we engage and upskill existing talent to use the technology and what new skill sets will be needed for success? Has management considered the social implications and long-term talent development implications?

Keep up with emerging regulations

- Have we mapped our planned use of AI applications to existing laws and regulations? Are there any concerns that need to be addressed?
- How are we keeping up with compliance and legal issues that current and prospective AI initiatives might pose to our use of the technology? Do we have sufficient resources to do so?

SID Audit & Risk Committee (ARC) Chapter

The Audit & Risk Committee (ARC) Chapter was set up with the objective of building capacity and improving the effectiveness of ARCs. It is a community of people involved with ARCs - ARC chairs and members, management personnel who work closely with ARCs, and professionals who provide support to ARCs. The ARC Chapter aims to provide a platform for active discussion on issues relevant to ARCs with a view to helping ARCs carry out their roles effectively. Resources include thought leadership articles specific to ARC concerns, professional development courses and seminars, and networking events.

SID invites you to learn more about the specially-curated initiatives and programmes of the ARC Chapter, and to register your interest. This Network is open to members only, and there are no additional membership or joining fees.

You can join the various Networks and Chapters via your SID Member Account (under Profile tab). For queries about SID membership or Networks, please email membership@sid.org.sg.

2025 Professional Development Calendar for ARC Members

Date	Event	Programme
22 January	Audit and Risk Committee Seminar	Jointly organised by ACRA, SGX RegCo, SID
27 February	Director Financial Reporting Fundamentals	Fundamentals Programme
12-14 March	SDP3: Finance for Directors	SID-SMU Directorship Programme
6 March	Global Internal Audit Standards for Boards	SID ARC Pitstop
20 March	LED 5: Audit Committee Essentials	Listed Entity Director Programme
21 March	LED 6: Board Risk Committee Essentials	Listed Entity Director Programme
24-25 April	SDP4: Risk Management & Cybersecurity Governance	SID-SMU Directorship Programme
16-18 July	SDP3: Finance for Directors	SID-SMU Directorship Programme
22 July	LED 5: Audit Committee Essentials	Listed Entity Director Programme
22 July	LED 6: Board Risk Committee Essentials	Listed Entity Director Programme
11-12 September	SDP4: Risk Management & Cybersecurity Governance	SID-SMU Directorship Programme
19 September	Director Financial Reporting Fundamentals	Fundamentals Programme
21 October	LED 5: Audit Committee Essentials	Listed Entity Director Programme
22 October	LED 6: Board Risk Committee Essentials	Listed Entity Director Programme

Note: *The above are professional development courses by SID relevant to board members who deal with audit and risk issues. Course dates are subject to change — and the latest updates can be found at: www.sid.org.sg/pd*