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On the 2019 Audit Committee agenda

KPMG Singapore Audit Committee Institute

Audit committees can expect their company's financial reporting, compliance, risk and internal control environments to be put to the test in the year ahead. Top challenges and pressures to be mindful of include long-term economic uncertainty, technology advances and business model disruption, cyber risks, regulatory scrutiny, investor demands for transparency, and geo-political instability.

Drawing on insights from our interactions with audit committees and business leaders over the past 12 months, we have highlighted key items and areas of focus that audit committees should keep in mind as they consider and carry out their 2019 agendas:

1. Take a fresh look at the audit committee's agenda and workload.

In addition to its core oversight responsibilities, audit committees are overseeing major risks on its agenda. Issues such as cyber security and IT risks, supply chain and other operational risks as well as legal and regulatory compliance have become more complex, as have the committee's core responsibilities. Consider whether the committee has the time and expertise to oversee this increased scope of risks. Does cyber risk require more attention at the full-board level? Perhaps a separate board committee needs to be put in place. Is there a need for a compliance or risk committee?

2. Sharpen the company's focus on ethics and compliance.

The reputational costs of ethics or compliance failures are higher than ever. Transparency enabled by social media has resulted in a company's culture and values, commitment to integrity, legal compliance and brand reputation to be put on public display like never before. To what extent does the audit committee closely monitor the tone at the top as well as the culture throughout the organization. Is there a sharp focus on behaviours and not just results? Are the company's regulatory compliance and monitoring programs updated to clearly communicate the company's expectations for high ethical standards? Does the audit committee see all whistle-blower complaints and how have these complaints been addressed? If not, what is the process to filter complaints that are ultimately reported to the audit committee?

3. Understand how the finance function will reinvent itself to add more value.

Over the next few years, finance functions will undergo the greatest technological transformation. Today, many manual activities can be automated to help reduce costs and improve efficiencies for the function. As audit committees oversee and help guide finance's progress in this area, they should query the organization's plans to leverage robotics and cloud technologies. In time, with fully-automated historical analysis, the organization's analytics capabilities should evolve to include predictive analytics. How will finance use data and analytics as well as artificial intelligence to develop sharper predictive insights and better deployment of capital?

4. Monitor corporate reporting as well as progress on implementing new standards.

Singapore Exchange (SGX)-listed companies with calendar year-ends are reporting under Singapore Financial Reporting Standards (International) [SFRS(I)] for the first-time. Taking this and the revenue and financial instruments standards for 2018 into consideration, audit committees are encouraged to ensure that:

- explanations of the impact of transition in the financial statements are comprehensive and consistent with other sections in the annual report.
- policy changes are clearly described and explained, reflecting company specific information and any associated management judgements.

Earlier this year, Accounting and Corporate Regulatory Authority (ACRA) published its areas of review focus for FY 2018 financial statements, highlighting to directors possible reporting misstatements and questions for management. These include:

1) ***New accounting standards*** – What are the areas with critical judgements and significant estimates?

2) ***Impairment assessment and valuation*** – Are these performed using a suitable model with objective and realistic assumptions?
3) ***Major transactions*** – Does the accounting treatment reflect the economic substance of the arrangement?
4) ***Statement of cash flows*** – Are cash flows appropriately classified within operating, investing or financing cash flows?
5) ***Significant judgements and estimates*** – Are disclosures tailored to the company's circumstances?

Audit committees should ensure that management has proper documentation to support their accounting treatment of transactions that involve critical judgements and significant estimates.

Also, for some companies, implementation of the new standards would involve both manual processes as well as enabling technology and tools. Manual work-arounds should not become permanent. Audit committees will want to help ensure that any work-arounds are automated as soon as possible.

For calendar year-end companies, the new leases standard is effective by the time the FY 2018 financial statements are authorized for issue. Audit committees should focus on management's strategy on the assessed impacts (such as compliance with loan covenants), the progress of implementation (such as more data collection), updates to their documentation and significant changes in their systems, processes, and internal controls.

In line with ACRA's expectations, the audit committee should check that management adequately discloses known or reasonably estimable information relevant to assessing the possible impact (quantitatively and qualitatively) of adopting the new standards in the FY 2018 financial statements.

5. Reinforce audit quality by setting clear expectations for the auditor.

Overseeing the auditor selection process including any (mandatory) tender processes and auditor independence is a key part of an audit committee's role. Audit committees can refer to Guidance to Audit Committees on ACRA's Audit Quality Indicators (AQIs) Disclosure Framework to enhance their discussions with audit firms on audit quality matters during the selection or reappointment of auditors.

6. Ensure internal audit is independent, adequate, effective and focused on the key risks.

SGX Listing Rule 719(3) requires all issuers to establish and maintain on an ongoing basis, an effective internal audit function that is adequately resourced and independent of the activities it audits. The audit committee is also required under SGX Listing Rule 1207(10C) to comment on whether internal audits are independent, effective and adequately resourced. Audit committees should work with chief audit executives to help identify the risks that pose the greatest threat to the company and help ensure that internal audit is focused on those risks and related controls.

7. Expand scope of audit committee reports.

The SGX, ACRA and the Monetary Authority of Singapore (MAS) recommend that audit committees provide their own commentaries on significant financial reporting matters specific to their listed entities and audit issues, how they assessed those matters, and key judgement calls made. Consider expanding the audit committee's report to provide investors with more insight into how the committee carries out its oversight responsibilities, particularly its role in helping to ensure audit scepticism and maintain audit quality.

8. Clarify oversight of sustainability risks and reporting.

Listed companies are required to 'comply or explain' their sustainability practices relating to environmental, social and governance (ESG) practices from 2017 onwards. If the sustainability report is included in the annual report, the audit committee will need to be mindful of any material inconsistency with that report. Has the company established a process to identify and engage with material stakeholders to assist in identifying material ESG factors?

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