

# Audit Committee Alert

KPMG Audit Committee Institute

KPMG LLP in Singapore

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## Considerations related to the current financial crisis in Singapore

A financial storm is brewing over the Asia Pacific region, and showing no immediate sign of dispersing. In Singapore, the business environment is changing dramatically, and we are likely to see more changes—perhaps a tightening up of regulations, a less leveraged economy, continued volatility of commodity prices and markets, and greater expectations for effective corporate governance.

### About the KPMG Audit Committee Institute

Recognising the importance of audit committees, the KPMG Audit Committee Institute (ACI) has been created to help provide audit committee members and members of boards with a resource to help them to keep up to date on current and emerging issues.

The KPMG ACI offers thought leadership on trends and current topics and provides a range of resources including publications, topical forums and roundtables to host the exchange of views and insights on audit committee best practices and processes, and other topics of interest to members of boards and audit committees.

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For boards and audit committees in Singapore, understanding the company's risk profile— and improving governance processes for risk management and oversight—should be a top priority.

From liquidity and access to capital, to fair value and asset impairments, and ultimately, to the adequacy of the company's processes to manage these and other risks effectively, audit committees should be focused on the risks their companies are facing in the current environment. Here are some critical risks—and key questions—that audit committees should consider:

- 1. Liquidity and access to capital.** What are the company's plans to raise debt / equity in the short and medium term? How dependent is the company on short-term financing? Are credit lines secure? Is the company at risk of default on debt covenants?
- 2. Exposure to counterparties and other third parties in financial distress.** Have we inventoried the company's potential exposure to third parties domestically and internationally — e.g., customers, suppliers, banks, lenders, underwriters, guarantors— that are experiencing financial difficulty or have filed for bankruptcy? Has the company identified the impact on contracts and other arrangements it has with these entities?
- 3. Ability to hedge against interest rate, currency, and commodity price volatility.** What will be the impact of inflation and recession on commodity costs and procurement strategies? How will changes impact the ability to obtain economic hedges against interest rate, currency, and commodity price volatility?

4. **Disclosures.** How is the application and impact of fair value accounting described in the Management Discussion and Analysis (MD&A)? Is the description of the company's liquidity risks robust and specific to the company?
5. **Threat of a deep recession.** What restructuring is the company considering? What capital expenditures should be deferred, given the prospects of a retracting economy?
6. **Fair value and asset impairments.** Have we reviewed the company's investment portfolio and inventoried its debt and equity securities to identify declines in value or impairments that should be reflected in the financials? Have we identified triggering events that may warrant impairment assessments of goodwill, deferred taxes, patents, and other intangibles? If so, are the fair values determined by management and valuation experts realistic in light of current market conditions? How have changes in financial markets impacted the valuation of pension plan assets and funding requirements?

## Reassessing Risk

As a result of the financial crisis, many boards are reassessing the adequacy and effectiveness of the company's governance processes for managing the risks to the business. The general consensus is that there is a need to improve the way companies manage risk; but how to accomplish that is a matter of ongoing debate. While no organisation has all the answers, it is critical to ask the right questions, including:

- Can management provide a holistic view of the company's major risks—both on and off the balance sheet risks? What are the top five risks crossing all parts of the business?
- How tolerant is management of risks? Does management understand that a catastrophic risk that poses even a 'less than one percent' chance of failure for the enterprise is unacceptable and must be avoided or mitigated to the extent possible?
- How rigorously does management stress-test key risk assumptions?
- How frequently does management review the risks associated with its products, particularly high-growth and high-margin products?
- Are the board's risk-related information sources adequate and varied? Is there sufficient internal transparency?
- How does culture—including the incentive compensation structure—impact the company's risk profile?

## Contact us

If you would like more technical information on any of the issues discussed, please contact us.



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