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Into the Minds of Investors

Investors' Views of Financial Reporting, Audit and Corporate Governance

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Audit and Corporate Governance

Survey Partners: ACRA, ISCA and NUS Business School

Author and Lead Researcher: Associate Professor Mak Yuen Teen, NUS Business School

Research Analyst: Chew Yi Hong, MBA (LBS), BA (Cornell)

Supporters: MAS, ACGA, IMAS, SIAS

Disclaimer:

The findings from this study are based on responses to questions in a survey and focus group discussion. The findings reflect the views of those who participated in them. Caution should be exercised in generalising the findings to other investors.

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FOREWORD

The Accounting and Corporate Regulatory Authority (ACRA), Institute of Singapore Chartered Accountants (ISCA) and the NUS Business School are pleased to present this report on investors' views of financial reporting, audit and corporate governance in Singapore. As a key stakeholder group, the views of institutional and retail investors are important inputs in the shaping of regulatory initiatives for Singapore's financial reporting landscape.

The findings also provide important takeaways for directors, management, auditors, investors, regulators, professional bodies and other stakeholders. One clear message that resonated from both institutional and retail investors alike was the importance that they place on high quality financial reports that allow for effective and informative analysis. The recent financial lapses reinforce the importance of high quality financial reporting in building trust and confidence in capital markets. Conversely, companies with vague, imprecise and seemingly elusive financials in today's complex business structures are seen as riskier investments. It is therefore in the interest of every stakeholder in the financial reporting value chain that we continue to uphold high standards in terms of the reliability and integrity of corporate and financial information. This holds all the more true amidst the current uncertain economic climate when a transparent business environment is crucial for market confidence and growth.

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Kenneth Yap
Chief Executive
Accounting and Corporate
Regulatory Authority

Lee Fook Chiew
Chief Executive Officer
Institute of Singapore
Chartered Accountants

Mak Yuen Teen
Associate Professor
National University
of Singapore

EXECUTIVE SUMMARY

ABOUT THE STUDY

In April 2016, the Accounting and Corporate Regulatory Authority (ACRA), the Institute of Singapore Chartered Accountants (ISCA) and the NUS Business School launched a survey seeking investors' views on financial reporting, audit and corporate governance, as well as inputs on how these areas could be further improved.

The survey sought the views of institutional and retail investors, with some customisation of the questions for the two groups given their different means of engaging with companies. The survey was conducted online.

A total of 33 institutional investors (including analysts) and 171 retail investors completed the survey. A focus group discussion with institutional and retail investors was also held to gain deeper insights into the issues covered in the survey.

KEY FINDINGS

The key findings and takeaways from the survey are:

Investors view financial statements as the most important source of information for decision making

Investors rated financial statements as the most important source for investment decision-making compared to other information sources (e.g. company announcements, one-to-one meetings/conference calls, analyst reports, etc), with 94% of institutional investors rating financial statements as "important" or "very important", and 81% of retail investors doing so.

However, feedback from investors from the focus group discussion appeared to suggest that at times, the usefulness of financial statements is limited by too much aggregation of information, lack of sufficient disclosures and disclosures that are difficult to understand.

Key Takeaways:

- *Companies (board of directors, audit committees and management) should ensure continued relevance of financial statements by focusing on providing high quality disclosures that are useful, sufficient and understandable.*
- *Investors should continue to hold companies to high standards of financial reporting. Greater transparency and clarity in disclosures will help them derive an accurate picture of the business which is vital for investment decisions.*

Institutional and retail investors differ on extent and nature of financial information used for decision-making

Both institutional and retail investors placed emphasis on quantitative financial measures such as net profit, operating cash flows and dividends. However, institutional investors also focused on qualitative financial statement items relating to related party transactions, critical accounting judgements and estimates and accounting policies compared to retail investors.

Institutional investors also spent more time analysing financial statements and placed emphasis on different financial ratios compared to retail investors.

Key Takeaway:

- *More education and awareness is needed to help investors understand, consider and use both qualitative and quantitative types of information in financial statements as they provide a holistic view of the company's financial affairs and operations and will translate into better investment decision making.*

Statutory audits significantly increase investor confidence in the financial statements

There was substantially more investor confidence in audited financial statements compared to non-audited financial statements, with the number of investors expressing confidence over the financial statements increasing close to five times when they were audited. Modified audit opinions were also more likely to affect investment decisions of institutional investors. Investors have also indicated that they were more likely to engage auditors with the impending new requirement that auditors indicate Key Audit Matters (KAMs) in financial reports under the enhanced auditor reporting standards from January 2017.

Investors also recognised the significance of auditor independence to audit quality. They view factors such as the audit fees, tenure of audit firm and partner, non-audit fees and the nature of non-audit services as important considerations on auditor independence, with the latter two given greater emphasis by institutional investors.

Key Takeaway:

- *With the added responsibility of KAMs reporting from January 2017 onwards, auditors should prepare to communicate more with investors and seize this opportunity to bring the quality of audits to a new level.*

Investors welcome more transparency and improved interactions with audit committees

Investors overwhelmingly believed that audit committees should provide a commentary to the shareholders about their views on the significant accounting issues highlighted as KAMs by the auditors. They also welcome greater transparency on information relating to the quality of auditors appointed. A high percentage of investors surveyed (82% of institutional investors and 90% of retail investors) would like audit committees to use audit quality indicators (AQIs) to evaluate auditors. These investors would similarly like audit committees to explain to them the basis for selecting the recommended auditor. With the introduction of the multiple proxies regime from 3 January 2016, investors, particularly retail investors have also expressed that they were more likely to attend Annual General Meetings (AGMs) to ask directors and audit committees questions, especially when there were contentious issues.

Key Takeaways:

- *Companies should be prepared for deeper levels of engagement with investors who, armed with greater insights into the audit process and the underlying drivers of a company's performance, will* *demand greater accountability from its directors and management.*

- *Audit committees should provide greater transparency to investors by:*
  - *Issuing an audit committee commentary in the company's annual report to explain significant financial reporting issues and to complement KAMs reporting by auditors.*
  - *Evaluating auditors using AQIs and communicating to investors the basis of selecting the recommended auditors.*

Investors value regulatory programmes and initiatives aimed at improving financial reporting and audit quality, although more can be done to raise awareness on these initiatives

More than 75% of the investors surveyed agreed that independent regulatory oversight programmes over financial reporting and audits were important in ensuring good quality financial reporting. There was however little awareness and understanding of the specific regulatory initiatives employed such as ACRA's Financial Reporting Surveillance Programme (FRSP) and the Practice Monitoring Programme (PMP) that conducts audit inspections.

Key Takeaway:

- *More outreach efforts by professional bodies and regulators are needed to enable investors to better understand the regulatory programmes and initiatives that ensure a robust financial reporting regime and how they can leverage on the regulatory outcomes and findings for their own investment reviews and decisions. An example would be the recent introduction of the Audit Quality Indicators Disclosure framework by ACRA which could help investors better understand the thought process of the audit committee and be assured that the appointment process for auditors is sound.*

Directors' experience, remuneration, independence and the company's internal control and risk management matters are most common aspects of corporate governance that investors are interested in

When assessing the quality of corporate governance of a company, both groups focused on qualification / experience of directors, remuneration of directors / senior management and internal control and risk management matters. In particular, remuneration, independence of directors and risk management were the three areas that investors have asked most questions about, with institutional investors also often asking questions about competencies of directors. In general, institutional investors also placed more importance and asked more questions on corporate governance matters compared to retail investors.

Key Takeaway:

- *Companies should ensure sufficient attention is given towards providing greater transparency and better disclosures on their corporate governance practices and ensure that they stand up to scrutiny.*

INTRODUCTION

Financial statements are important sources of information for investors to make investment decisions and assess how effectively boards and management discharge their stewardship role, create value and promote the long term success of companies. However, the usefulness of financial statements is dependent on their quality, and management, directors, auditors, investors, regulators and other stakeholders all play important roles in ensuring the quality of financial statements. External auditors, through their assurance role, play a particularly important role in improving trust in financial statements.

The importance of high quality financial reporting and audit to good corporate governance is recognised in the G20/OECD Principles of Corporate Governance through the "Disclosure and Transparency" Principle. For example, under this Principle, there should be disclosure of material information on the "financial and operating results of the company", "information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial reporting", and "an annual audit should be conducted by an independent, competent and qualified, auditor in accordance with high-quality auditing standards".

Accounting and auditing is an area of strength for Singapore based on the biennial CG Watch published by the Asian Corporate Governance Association (ACGA), with Singapore consistently ranked first or joint first on this factor among all the Asian countries covered since the first report. Under the category that it refers to as "IGAAP", the survey assesses areas such as the adoption of international financial reporting standards and international standards of auditing, auditor independence and independent regulatory oversight of auditors.

Independent oversight of auditors is carried out by the Accounting and Corporate Regulatory Authority (ACRA) under its Practice Monitoring Programme (PMP)[1]. Cognisant that high-quality audits alone cannot uphold good quality financial reporting, ACRA also instituted the Financial Reporting Surveillance Programme (FRSP)[2] in 2011 to strengthen the financial reporting value chain right at the source of preparation of the financial statements. In recent years, ACRA has introduced a number of initiatives to raise greater awareness on financial reporting and audit quality across stakeholders in the financial reporting value chain. In 2015, ACRA introduced the Audit Quality Indicators (AQIs) Disclosure Framework, comprising eight comparable audit quality markers to help audit committees better evaluate and select their auditors. With the enhanced auditor's reporting standards taking effect from 2017, ACRA and ISCA are also collaborating with industry partners and stakeholders to raise awareness on the standards, particularly on Key Audit Matters (KAMs) reporting[3].

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1 Under the PMP, ACRA inspects audits performed by auditors in accounting entities that audit listed companies and other public interest entities to check if quality audits have been performed in compliance with the Singapore Standards on Auditing (SSAs). Public accountants that do not audit public interest entities (PIEs) are inspected by practice reviewers employed by ISCA and appointed by ACRA's Public Accountants Oversight Committee (PAOC).

2 Under the FRSP, ACRA reviews selected financial statements lodged with it to ascertain whether they comply with the Singapore Financial Reporting Standards (SFRSs).

3 KAMs, as the name suggests are matters that, in the auditor's judgement, were of the most significance in the audit of the financial statements for the period in question. This may include areas of the financial statements most susceptible to misstatements, areas that depend on management estimates and judgements and audits of significant events or transactions during the year.

Whilst recognising the collective efforts of the respective stakeholders in contributing towards high quality financial reporting, effective audits and good corporate governance, investors are an important component in this equation. As ultimate beneficiaries of financial reporting, audits and corporate governance, investors are in the position to demand for quality and to shape companies' (management, directors, audit committees) and auditors' behaviour to provide relevant and timely information that best serve their needs. In light of this, it is hence timely to conduct a study to gauge investors' perceptions in these areas and to raise greater awareness on the existing initiatives to improve the quality of financial reporting and audits. This study will also help inform regulators and the relevant industry stakeholders as they develop future initiatives to meet investors' information needs.

1. THE STUDY

In April 2016, ACRA, ISCA and the NUS Business School launched a survey of investors' views of financial reporting, audit and corporate governance, including regulatory initiatives in Singapore to improve these areas. As investors are a key stakeholder group, their views on financial reporting, audit and corporate governance are important inputs into regulatory and market initiatives.

The survey was conducted online. Given the importance of both institutional and retail investors in the Singapore market, the survey sought the views of both groups of investors, with some customisation of the questions for the two groups given their different means of engaging with companies. A total of 33 institutional investors (including analysts) and 171 retail investors completed the survey. The institutional investors who participated in the survey covered Singapore companies. A profile of the survey respondents is provided in Annex A.

A focus group discussion with institutional and retail investors was also held to gain deeper insights into the issues covered in the survey.

2. FINDINGS

This study covered areas of financial reporting, audit and corporate governance. In addition, investors were asked about their awareness of regulatory initiatives in these areas. In this section, we present the results of the survey, together with additional insights from the focus group discussion.

A. FINANCIAL REPORTING

The first area covered by the survey deals with investors' views on:

- the importance of the various information sources for decision-making;
- the importance of key financial statement line items and ratios for decision-making;
- the types of questions raised by shareholders on financial reporting matters;
- directors' responsibility for ensuring financial statements comply with accounting standards; and
- regulatory oversight in relation to financial reporting.

a. *Importance of Financial Statements*

Table 1 shows how institutional and retail investors rated the importance of different information sources for making investment decisions. Both groups of investors rated financial statements as more important than other information sources, with 94% of institutional investors rating financial statements as "important" or "very important", and 81% of retail investors doing so. This is consistent with the remarks made by participants in the focus group discussion, whereby they highlighted that they generally trust the quality of financial reporting in Singapore.

Table 1: Importance of different information sources for making investment decisions

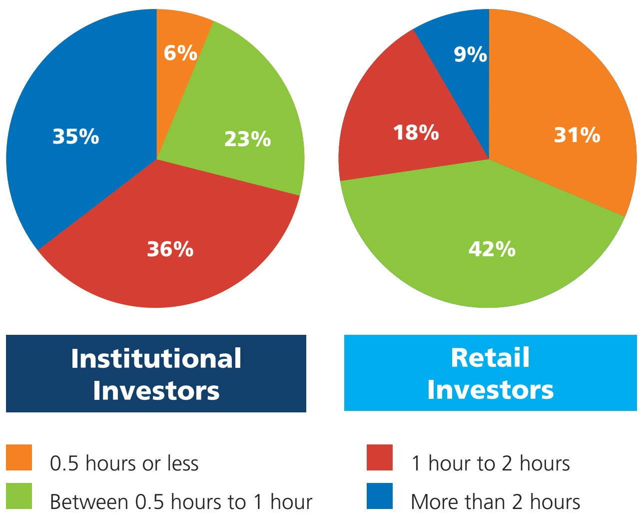
Institutional Investors						Retail Investors				
I have never used it	Not important at all	Somewhat important	Important	Very important		I have never used it	Not important at all	Somewhat important	Important	Very important
6%	0%	3%	36%	55%	**Annual reports**	7%	3%	22%	31%	37%
6%	0%	0%	9%	85%	**Financial statements**	4%	1%	14%	37%	44%
6%	0%	6%	30%	58%	**Company announcements**	2%	0%	19%	40%	39%
6%	0%	6%	21%	67%	**Company briefings/ One-to-one meetings**	12%	3%	33%	31%	21%
15%	6%	43%	21%	15%	**Shareholder meetings**	9%	8%	25%	31%	27%
6%	3%	49%	24%	18%	**Analyst reports**	4%	5%	39%	33%	19%
6%	27%	49%	15%	3%	**Stockbrokers**	9%	15%	45%	22%	9%
6%	18%	40%	24%	12%	**Newspapers/ online portals/ social media**	1%	9%	32%	45%	13%

For institutional investors, company briefings/one-to-one meetings, annual reports and company announcements were considered next most important, while retail investors considered the latter two sources as next most important.

Institutional investors rated financial statements, company briefings/one-to-one meetings, annual reports and company announcements to be more important, compared to retail investors. Retail investors rated other information sources such as shareholder meetings, analyst reports, newspapers/ online portals/social media, and stockbrokers to be relatively more important, compared to how institutional investors rated them.

The greater importance that institutional investors place on financial statements compared to retail investors was also reflected in the higher average time spent on reading financial statements by institutional investors (Figure 1). More than 70% of institutional investors spent at least one hour reading

Figure 1: Time spent on reading the financial statements per company



the financial statements per company, with half (35%) of them spending two hours or more. In contrast, only nine percent of retail investors spent two hours or more per company, with another 18% percent spending between one and two hours.

Participants in the focus group discussion emphasised that the importance of financial statements and different financial statement items for investment decision-making depended on factors such as the industry and investment style. They also highlighted that the usefulness of financial statements was often limited by the following:

i. too much aggregation of information (e.g. large other operating expenses or income);

ii. lack of sufficient disclosures (e.g. debt and contingent liabilities of associates); and

iii. difficult-to-understand disclosures (e.g. in areas relating to deferred taxes, mark-to-market accounting, financial risk management, derivatives and revenue recognition relating to service concession contracts).

b. Key Financial Statement Items and Ratios

Both institutional and retail investors rated net profit, operating cash flow, dividends and earnings per share as the most important quantitative financial statement items, although more retail investors rated earnings per share as "very important" compared to other ratios (Table 2). Institutional investors also rated related party transactions as "very important" and also placed greater importance on qualitative financial statement items relating to critical accounting judgements and estimates, and accounting policies and changes, compared to retail investors. This could be due to such information being perceived to be too technical and not easily understood by non-accounting trained investors.

Table 2: Importance of financial statement items for making investment decisions

Institutional Investors						Retail Investors				
I have never used it	Not important at all	Somewhat important	Important	Very important		I have never used it	Not important at all	Somewhat important	Important	Very important
0%	0%	7%	51%	42%	**Revenue**	1%	0%	17%	44%	38%
0%	0%	7%	29%	64%	**Net profit**	1%	0%	7%	43%	49%
0%	3%	7%	45%	45%	**EBIT/EBITDA**	9%	2%	14%	41%	34%
0%	3%	3%	26%	68%	**Operating cash flows**	1%	1%	10%	42%	46%
0%	0%	13%	45%	42%	**Net assets**	2%	0%	18%	46%	34%
3%	0%	3%	47%	47%	**Earnings per Share**	1%	1%	13%	34%	51%
0%	3%	3%	42%	52%	**Dividends**	1%	1%	13%	40%	45%
0%	0%	19%	45%	36%	**Accounting policies and changes, if any**	4%	7%	35%	36%	18%
0%	3%	16%	36%	45%	**Critical accounting judgements and key estimation uncertainties**	6%	6%	27%	39%	22%
0%	0%	13%	36%	51%	**Related party transactions**	6%	4%	28%	38%	24%

Institutional and retail investors also differed in terms of importance placed on different ratios (Table 3). Institutional investors placed most importance on gearing ratio, return on equity and return on invested capital, while retail investors placed most importance on dividend yield, price/earnings ratio and net profit margin.

Table 3: Importance of ratios for making investment decisions

Institutional Investors: I have never used it	Institutional Investors: Not important at all	Institutional Investors: Somewhat important	Institutional Investors: Important	Institutional Investors: Very important		Retail Investors: I have never used it	Retail Investors: Not important at all	Retail Investors: Somewhat important	Retail Investors: Important	Retail Investors: Very important
0%	0%	0%	39%	61%	**Gearing ratio**	6%	2%	17%	42%	33%
0%	10%	19%	48%	23%	**Current ratio**	6%	3%	26%	44%	21%
0%	7%	19%	38%	36%	**Net profit margin**	3%	2%	12%	46%	37%
0%	0%	19%	42%	39%	**Return on assets**	2%	3%	18%	52%	25%
0%	3%	3%	32%	62%	**Return on invested capital**	2%	4%	18%	50%	26%
0%	3%	0%	36%	61%	**Return on equity**	2%	3%	13%	47%	35%
3%	0%	26%	39%	32%	**Dividend yield**	1%	1%	13%	35%	50%
3%	0%	19%	39%	39%	**Price/earnings ratio**	1%	2%	13%	44%	40%

Institutional Investors | **Retail Investors**

c. *Shareholder Questions on Financial Reporting Matters*

Institutional investors tended to engage with companies through different means compared to retail investors, with the former being able to meet management and sometimes the board of directors through one-to-one meetings, analyst briefings and conference calls. In contrast, retail investors usually have access to management and directors only through shareholder meetings. Based on investors' profile from the survey, it was evident that the institutional investors in the survey participated in many more one-to-one meetings, analyst briefings and conference calls compared to the frequency with which retail investors attended AGMs. Therefore, it is not surprising that Table 4 shows that a much higher percentage of institutional investors have asked questions relating to financial reporting matters compared to retail investors.

Table 4: Areas of the financial statements for which investors are most likely to have asked questions

Questions relating to:	Percent
Revenue recognition	87%
Business acquisitions or disposals	87%
Related party transactions	87%
Accounting for complex or significant transactions (other than business acquisitions or disposals)	70%
Provisions	70%
Fair value estimates and assumptions	67%
Impairments of goodwill and other long-lived assets	67%
Going concern	37%
Others	17%

Institutional Investors

Questions relating to:	Percent
Business acquisitions or disposals	19%
Revenue recognition	18%
Going concern	15%
Provisions	15%
Fair value estimates and assumptions	13%
Related party transactions	12%
Impairments of goodwill and other long-lived assets	11%
Accounting for complex or significant transactions (other than business acquisitions or disposals)	11%
Others	16%
No, I have not asked any questions at AGMs relating to the company's accounting matters	59%

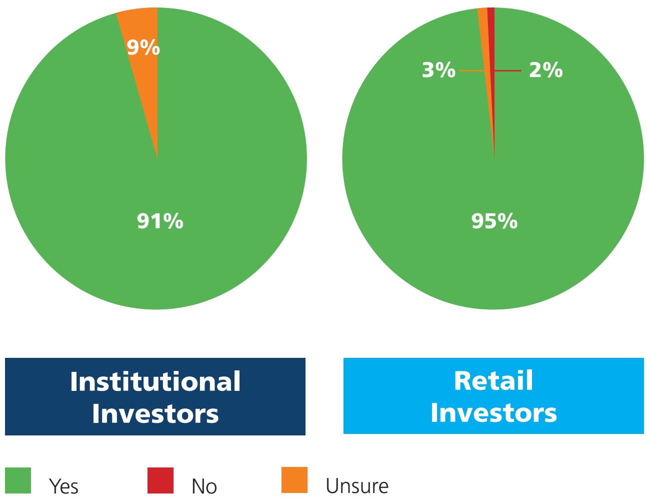
Retail Investors

In the case of institutional investors, the top three areas of the financial statements where they have asked questions were revenue recognition, business acquisitions or disposals, and related party transactions. Retail investors were also most likely to have asked questions about revenue recognition and business acquisitions or disposals, followed by going concern and provisions.

d. Responsibility for Compliance with Accounting Standards

When asked if directors should be responsible for ensuring that financial statements comply with accounting standards, more than 90% of both institutional and retail investors thought so (Figure 2). The results overwhelmingly reaffirm investors' expectations of directors' duties over financial reporting as provided for under the Companies Act[4].

Figure 2: Whether directors should be responsible for ensuring that the financial statements comply with accounting standards



e. Regulatory Oversight in Relation to Financial Reporting

When asked whether an independent regulatory programme to review financial statements' compliance with accounting standards would provide investors with greater confidence over a company's financial statements, around 80% of both institutional and retail investors agreed that it would. However, there were also a relatively high percentage of both groups of investors (21% of institutional investors and 15% of retail investors) who were unsure about whether such a programme will provide investors with greater confidence. A possible explanation is that investors believe that the effectiveness of the programme depends on how it is implemented such as the extent of review scope and coverage, remedial actions taken and the efficacy of the regulatory actions in driving improvement efforts across companies.

In enforcing directors' responsibilities over the financial statements in Singapore, ACRA introduced the FRSP in 2011. ACRA collaborates with ISCA's Financial Statements Review Committee to review selected financial statements lodged with ACRA to ascertain whether they comply with the Singapore Financial Reporting Standards (SFRSs). The financial statements are selected for review using a risk-based approach and enquiries are made when the review indicates possible non-compliance with the SFRSs. Depending on the severity of the non-compliance, companies may be requested to restate, re-audit and re-lodge the corrected financial statements with ACRA.

Whilst investors generally agree that independent regulatory programmes such as the FRSP are useful, they have low actual awareness of the regulator's work in this aspect, with 85% of institutional investors and 81% of retail investors being unaware of the FRSP. In the focus group discussion, participants were very positive about the FRSP and other regulatory initiatives to improve financial reporting, audit and corporate governance in Singapore and expressed the view that such initiatives be continued and reinforced. Nevertheless, in order for these initiatives to translate into greater trust in the quality of financial reporting, audit and corporate governance, more effort should be put into increasing awareness of these programmes to investors.

[4] Sections 201(2) and 201(5) of the Companies Act require the directors of a company to present and lay before the company, at its annual general meeting, financial statements that: (a) comply with the prescribed Accounting Standards in Singapore; and (b) give a true and fair view of the profit or loss, and the state of affairs of the company. The directors must fulfil both conditions in the discharge of their responsibilities under the Companies Act.

B. STATUTORY AUDIT

The second area covered by the survey deals with investors' views on the:

- level of confidence provided by audited financial statements (vis-à-vis unaudited financial statements);
- impact of modified audit opinion on investments decisions;
- impact of auditor choice on audit quality;
- independent regulatory oversight of auditors;
- audit quality indicators;
- interactions with audit committees and auditors; and
- KAMs reporting under the enhanced auditor's report.

a. Auditor's Report

Institutional investors were more likely to read the independent statutory auditor's report compared to retail investors, with slightly more than three-quarters (76%) of the former doing so, compared to less than two-thirds (64%) of the latter.

b. Confidence in Unaudited Versus Audited Financial Statements

Table 5 shows investors' views about their confidence over unaudited financial information compared to audited financial statements. In general, retail investors had less confidence over unaudited financial information compared to institutional investors, based on the much higher percentage of these investors who were "not confident at all" and the lower percentage who were "confident" or "very confident". The confidence of retail investors in audited financial statements was more varied compared to institutional investors, with a higher percentage being "very confident" and also a higher percentage who were "not confident at all" or only "somewhat confident" compared to institutional investors.

Table 5: Confidence over unaudited financial information and audited financial statements

Institutional Investors: Not confident at all	Institutional Investors: Somewhat confident	Institutional Investors: Confident	Institutional Investors: Very confident		Retail Investors: Not confident at all	Retail Investors: Somewhat confident	Retail Investors: Confident	Retail Investors: Very confident
6%	76%	15%	3%	Unaudited financial information (e.g. quarterly results announcements)	36%	49%	13%	2%
0%	12%	79%	9%	Audited financial statements	4%	25%	55%	16%

Table 6: Impact of modified audit opinion on investment decisions

Institutional Investors

	Percent
Yes	88%
No	3%
Unsure	9%

Retail Investors

	Percent
Yes	71%
No	6%
Unsure	23%

Nonetheless, for both groups of investors, the statutory audit significantly increased their confidence in the financial information, as can be seen by the large increases in percentage of those who are "confident" or "very confident" when comparing unaudited financial information with audited financial statements (88% (audited) versus 18% (unaudited) for institutional investors, 71% (audited) versus 15% (unaudited) for retail investors), and the corresponding decline in percentages of those who were "not confident at all" or "somewhat confident" (12% (audited) versus 82% (unaudited) for institutional investors, 29% (audited) versus 85% (unaudited) for retail investors).

c. Impact of Modified Audit Opinion

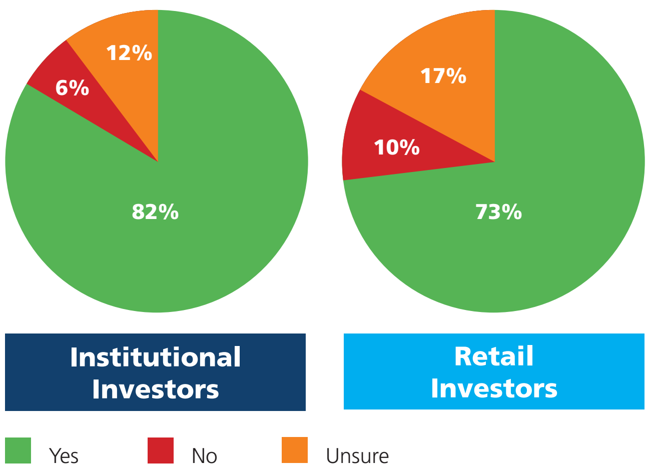
About 88% of the institutional investors said that a modified audit opinion (i.e., qualified, adverse or disclaimer) will affect their investment decisions, compared to about 70% of retail investors. Nearly a quarter (23%) of retail investors were unsure as to whether a modified audit opinion will affect their investment decisions, compared to less than 10% of institutional investors. Together with the earlier observation that the confidence of retail investors in audited financial statements was more varied compared to institutional investors, this suggests that retail investors have more diverse views was about the value of the statutory audit.

We analysed the impact of a modified audit opinion on investment decisions further for the retail investors group. More than three quarters (76%) of the retail investors who have university or post-graduate qualifications said that a modified audit opinion will affect their investment decisions and about 20% said that they were unsure about this. In contrast, only 60% of retail investors without university or post-graduate qualifications said that a modified audit opinion will have an impact on their investment decisions and 30% were unsure. Therefore, the results suggest that a modified audit opinion would be more likely to affect the investment decisions of retail investors who were more educated.

d. Impact of Auditor Choice on Quality of Audits

As shown in Figure 3, institutional and retail investors generally agreed that the choice of auditors would affect the quality of audits performed. However, this sentiment was higher for institutional investors compared to retail investors (82% versus 73%). The percentage of those who were unsure about the impact of auditor choice on quality of audits was also lower for institutional investors compared to retail investors (12% versus 17%).

Figure 3: Impact of choice of auditors on quality of audits



In the focus group discussion, participants said that they find it difficult to evaluate the quality of auditors and generally place reliance on proxies for audit quality, such as the size and tiering of audit firms to infer audit quality. They also relied on auditors to have mechanisms in place to monitor and ensure audit quality. In general, they did not have concerns about the quality of audits performed by auditors in Singapore and were more concerned over the quality of audits performed by foreign auditors.

e. Independent Regulatory Oversight of Auditors

Investors were asked if an independent regulatory programme involving the inspection of working papers of auditors for compliance with auditing standards would give them greater confidence over the financial statements of listed entities. 82% of institutional investors and 78% of retail investors agreed that such a programme will enhance confidence. Similar to the FRSP, the relatively high percentage who did not agree or were unsure suggests the effectiveness of implementation of such a programme is key.

In Singapore, the independent inspection of the auditor's work has been carried out by ACRA since 2004 under its PMP. Under the PMP, the auditor's work is assessed for compliance with the SSAs. If an auditor has failed to comply with the SSAs, the auditor may be ordered to undertake remedial actions, or be subjected to sanctions which include restricting the auditor from providing audits of financial statements over a stipulated period, suspension orders and cancellation of the auditor's licence.

Somewhat disappointingly, even though the PMP has been in place since 2004, the level of investors' awareness on the programme was very low, with 94% of institutional investors and 82% of retail investors being unaware of it. The lack of awareness could be attributable to the fact that investors preferred to leave audit related matters to the company and its directors. They generally also have a high level of trust in the audit profession in Singapore. Hence, investors tended to place greater reliance on auditors as an independent third party providing assurance to the company's financial statements without asking much questions.

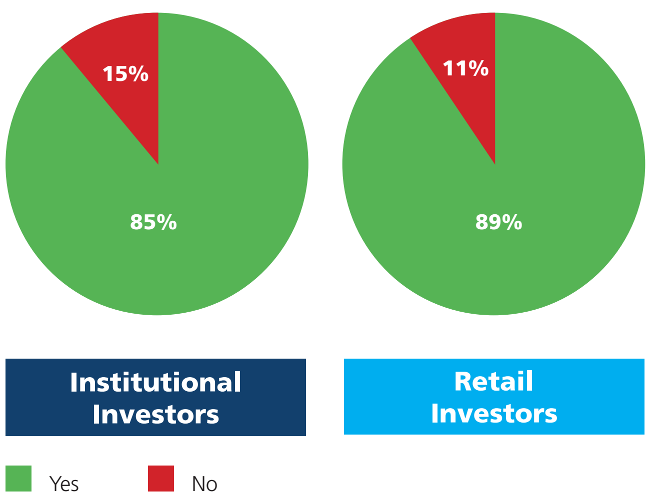
Nonetheless, investors' affirmation of the value of such regulatory programmes was encouraging and professional bodies and regulators can do more to raise awareness on these programmes. This understanding will enable investors to place greater scrutiny over the financial reporting and audit process and further enhance trust and confidence in the marketplace. In the focus group discussion, there was a view that more information on trends such as PMP results over the years would enable investors and companies to understand the audit risk areas and provide greater transparency for them to engage the auditors.

f. Audit Quality Indicators (AQIs) and Auditor Evaluation and Selection

Investors were also asked about their level of awareness and views on AQIs. In 2015, ACRA introduced the AQIs Disclosure Framework, comprising eight comparable quality markers that correlate closely with audit quality. Singapore is the first in the region to introduce such a framework which aims to help audit committees better evaluate and select their auditors using a standard set of quality indicators (e.g. the results of audit inspections by a regulator, the hours spent by the audit partner and experience of the audit engagement team). The framework has been available for voluntary adoption by audit firms auditing listed entities in Singapore from 1 January 2016.

Considering the development of AQIs is still at a nascent stage globally, it is encouraging that about one-third (33%) of institutional investors and 28% of retail investors were aware of the concept of AQIs. It is also noteworthy that 82% of institutional investors and 90% of retail investors said that they would like audit committees to use AQIs to evaluate auditors. As shown in Figure 4, a further 85% of institutional investors and almost 90% of retail investors would like audit committees to explain to them the basis for selecting auditors. During the focus group discussion, participants mentioned that they welcomed greater transparency from auditors, particularly on AQIs specific to the audit engagement.

Figure 4: Investors' views on whether audit committees should explain basis of selecting the recommended auditor to them



In addition to AQIs, the survey also sought investors' views about the importance of other factors that were considered to have a potential impact on auditor independence (and therefore affecting audit quality). As Table 7 shows, institutional investors believe that non-audit fees and nature of non-audit services are the most important, while retail investors viewed most factors as about equally important.

Table 7: Importance of other audit-related factors to auditor independence

Institutional Investors: I have never used it	Institutional Investors: Not important at all	Institutional Investors: Somewhat important	Institutional Investors: Important	Institutional Investors: Very important	Factor	Retail Investors: I have never used it	Retail Investors: Not important at all	Retail Investors: Somewhat important	Retail Investors: Important	Retail Investors: Very important
0%	6%	12%	55%	27%	Tenure of the audit firm	8%	5%	26%	43%	18%
0%	6%	27%	43%	24%	Tenure of the audit partner	8%	4%	24%	43%	21%
0%	9%	15%	52%	24%	Total audit fees paid to the auditor and its affiliated firms	8%	7%	23%	43%	19%
0%	6%	15%	24%	55%	Total non-audit fees paid to the auditor and its affiliated firms	8%	5%	29%	39%	19%
0%	6%	18%	40%	36%	Nature of non-audit services provided by the auditor and its affiliated firms	8%	5%	27%	38%	22%

g. Interactions with Audit Committees and Auditors

As mentioned earlier, the primary means of engagement with listed entities for institutional investors were one-to-one meetings, analyst briefings and conference calls. In these meetings, auditors were not available. For retail investors, the AGM is the main means of engagement. The Singapore Code of Corporate Governance recommends that auditors be present at AGMs to answer queries. Table 8 shows that 70% of institutional investors and 80% of retail investors have not asked the auditors any questions relating to the audit.

Table 8: Questions posed by investors to auditors about audits

Questions relating to:	Percent
Auditing areas involving significant management judgements and estimates	21%
Deficiencies in internal control	18%
Audit adjustments	15%
Areas of disagreements with management	15%
Audit materiality	12%
Auditor independence	12%
Others	3%
No, I have not asked any questions relating to the company's audit	70%

Institutional Investors

Questions relating to:	Percent
Auditing areas involving significant management judgements and estimates	8%
Areas of disagreements with management	7%
Audit adjustments	7%
Audit materiality	6%
Deficiencies in internal control	6%
Auditor independence	5%
Others	5%
No, I have not asked any questions at AGMs relating to the company's audit	80%

Retail Investors

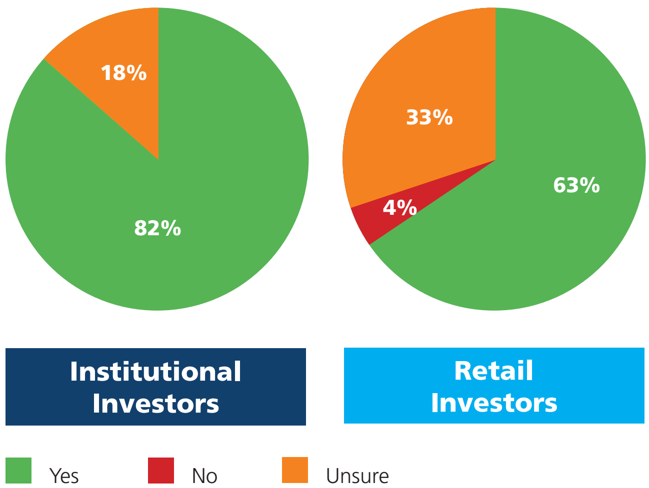
During the focus group discussion, the institutional investor representatives who participated had differing views as to whether there should be more interactions between them and auditors, outside of the AGM. A representative from an institutional investor body said that meetings between institutional investors and auditors as a group (e.g. via focus groups, consultation sessions), rather than on an individual listed entity basis, is becoming more common and is welcome. Some institutional investors were reluctant to engage directly with auditors in one-to-one meetings because of concerns about receiving non-public information from the auditors at such meetings. When challenged that a similar risk exists when institutional investors meet with company management, the response was that the assurance role played by the external auditors increased the risk of receiving non-public information.

Rather, institutional investors would like more interactions with audit committees and audit committee chairmen on matters relating to the audit. They felt that access to audit committee chairmen was often difficult.

h. Enhanced Auditor's Report

Issued by ISCA in July 2015, the enhanced auditor reporting standards will be effective for audits of financial statements for periods ending on or after 15 December 2016. The standards were revised in response to strong calls by investors and users of financial statements for more pertinent information to be included in the auditor's report to augment their decision-making. The most significant change was the new requirement for auditors to communicate KAMs in the auditor's reports on the financial statements of listed entities beyond the traditional "Pass/Fail" audit opinion. KAMs may include significant risk areas of the financial statements most susceptible to misstatements, the entity's major transactions during the year that required extensive auditing efforts or areas involving key management judgments and estimates such as the valuation of investments.

Figure 5: Investors' views on usefulness of KAMs reporting by auditors



With the impending introduction of the enhanced standards in Singapore, the study also sought to understand the views of investors with regards to usefulness of KAMs in the auditor's reports. Figure 5 shows that majority of investors believed that KAMs reporting will be useful, particularly for institutional investors (82%).

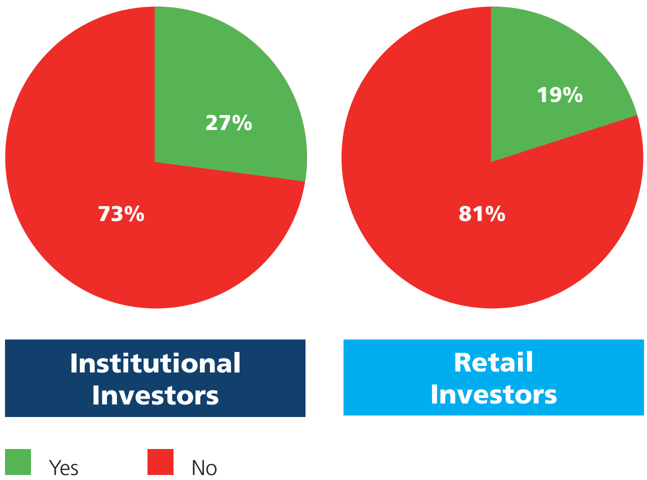
Both groups of investors felt that observations of control deficiencies and why a matter was identified as a KAM are most important in KAMs reporting (Table 9). Institutional investors also felt that how audit materiality was determined was important while retail investors viewed the outcome of audit procedures as important. In general, investors were less interested in the summary of audit procedures.

Table 9: Aspects of KAMs reporting by auditors that are most useful to investors

Institutional Investors: Not useful at all	Institutional Investors: Somewhat useful	Institutional Investors: Useful	Institutional Investors: Very useful		Retail Investors: Not useful at all	Retail Investors: Somewhat useful	Retail Investors: Useful	Retail Investors: Very useful
3%	6%	52%	39%	Why the matter was identified as a KAM	4%	22%	48%	26%
9%	18%	55%	18%	Summary of audit procedures performed	7%	24%	48%	21%
3%	15%	64%	18%	Outcome of the audit procedures performed	6%	16%	50%	28%
3%	15%	55%	27%	Audit materiality and how it was determined	6%	25%	46%	23%
3%	12%	55%	30%	Observations of control deficiencies	6%	19%	45%	30%

Institutional Investors **Retail Investors**

Figure 6: Awareness of KAMs Reporting



However, the study showed that there was still a generally low level of awareness of KAMs reporting, as shown in Figure 6. This could be because the enhanced auditor's report was not yet effective in Singapore and there are only a handful of early adopters in the market at the time of the study.

Although 64% of institutional investors and 46% of retail investors said that the expanded auditor's report will encourage them to ask auditors questions, one-third (33%) of institutional investors and nearly half (47%) of retail investors were unsure. Given that only a very small number of listed entities here have chosen to early adopt KAMs reporting, investors were probably adopting a wait-and-see attitude about the usefulness of such reporting and whether it will provide them with better information to ask auditors questions.

There may also be uncertainty in the minds of some investors as to whether it was appropriate to ask auditors questions directly, as opposed to asking the audit committee chairmen or management. To promote greater responsible shareholder activism and to encourage more investors to do their part in holding auditors accountable for their work, regulators may wish to consider educating investors about their right to ask auditors questions about the audit.

Both institutional and retail investors overwhelmingly believe that audit committees should provide a commentary to the shareholders about their views on the significant accounting issues highlighted as KAMs by the auditors. All the institutional investors and 95% of retail investors who were surveyed felt so. Such commentary by audit committees would enable them to communicate their independent views to the shareholders and demonstrate how they have discharged their oversight duties with respect to financial reporting. It was also brought up during the focus group that the audit committees of listed companies in the United Kingdom presented their Audit Committee report as a separate report in the annual report. Audit committees need to step up and meet investors' expectations of more communications between them and investors.

C. CORPORATE GOVERNANCE

The final part of the study covered investors' views about corporate governance in Singapore. Institutional investors were more likely to read the corporate governance statement/report of listed entities when making investment decisions, compared to retail investors, with the percentages being 76% and 54% respectively.

Institutional investors placed more importance on corporate governance factors based on the percentage of respondents rating such factors as "important" or "very important". For institutional investors, the most important areas in assessing the quality of corporate governance were the qualifications/experience of directors, remuneration of directors/senior management, number of independent directors, risk management and internal control, and audit committee-related matters (Table 10). For retail investors, qualifications/experience of directors, remuneration of directors/senior management, and risk management and internal control were most important.

Table 10: Importance of different factors in assessing the quality of corporate governance

Institutional Investors						Retail Investors				
I have never used it	Not important at all	Somewhat important	Important	Very important		I have never used it	Not important at all	Somewhat important	Important	Very important
15%	46%	27%	9%	3%	Gender diversity in board	15%	41%	29%	10%	5%
3%	9%	52%	30%	6%	Number of board members	11%	15%	37%	28%	9%
3%	0%	12%	46%	39%	Number of independent directors	6%	9%	26%	43%	16%
3%	0%	15%	52%	30%	Tenure of directors	8%	7%	28%	40%	17%
3%	0%	12%	39%	46%	Qualifications/ experience of directors	4%	2%	17%	41%	36%
3%	6%	9%	27%	55%	Remuneration of directors/senior management	4%	2%	23%	42%	29%
3%	3%	18%	40%	36%	Audit committee-related matters	7%	1%	25%	45%	22%
3%	0%	18%	40%	39%	Risk management and internal control	6%	1%	16%	44%	33%
3%	0%	30%	43%	24%	Internal audit	6%	2%	25%	44%	23%

Institutional investors were much more likely to have asked questions relating to the company's corporate governance (Table 11). They were most likely to have asked questions about independence of directors, remuneration, competencies of directors, and risk management. Retail investors were also more likely to ask questions about these factors, other than competencies of directors. Nonetheless, a high percentage (70%) of retail investors surveyed indicated that they have not asked any questions at AGMs.

Table 11: Investors' questions about corporate governance

Institutional Investors

	Percent
Independence of directors	67%
Remuneration	61%
Competencies of directors	61%
Risk management	61%
Internal control	46%
Internal audit	27%
Audit committee-related matters	24%
Others	6%
No, I have not asked any questions at AGMs	21%

Retail Investors

	Percent
Remuneration	15%
Risk management	14%
Independence of directors	12%
Competencies of directors	9%
Audit committee-related matters	7%
Internal control	7%
Internal audit	4%
Others	4%
No, I have not asked any questions at AGMs	70%

Finally, we asked investors whether the amendment to the Companies Act to allow indirect investors (including institutional investors and CPF investors) to be appointed as proxies and attend AGMs in Singapore will encourage them to attend more AGMs. Only 18% of institutional investors said that they will attend more AGMs, with 61% saying that they will do so where there were contentious issues. For retail investors, nearly half (47%) said that they were more likely to attend AGMs and another one-third (33%) said that they will do so where there were contentious issues. This is not surprising as focus group participants highlighted that attending AGMs were a "last resort" for institutional investors when other means of engagement have failed. However, they also felt that the change was important as it allowed them the option of attending where there were contentious issues. Investors welcomed the multiple proxies regime.

3. CONCLUSION

This study examined the views of institutional investors and retail investors about financial reporting, audit and corporate governance in Singapore. These views were obtained through a questionnaire survey of 33 institutional investors and 171 retail investors, and a focus group discussion involving both types of investors.

Based on the findings, a number of broad themes emerged:

- Financial statements are the most important source of information for investment decision-making compared to other common information sources.
- Institutional and retail investors differ on extent and nature of financial information used for decision making.
- Statutory audits significantly increases investors' confidence in the financial information.
- Investors welcome more transparency and improved interactions from audit committees on the evaluation and selection of auditors, KAMs and other significant financial reporting matters.
- Investors value programmes and initiatives aimed at improving financial reporting and audit quality, although more can be done to raise awareness on these initiatives.
- Directors' experience, remuneration, independence and the company's internal control and risk management matters are most common aspects of corporate governance that investors are interested in.

This study suggests several key takeaways to further raise investor trust and confidence in Singapore's capital market. All participants in the eco-system ranging from board of directors and audit committees, auditors, professional bodies, regulators and investors themselves have an important role to play to collectively raise the quality of financial reporting, audit and corporate governance in Singapore. The key takeaways are summarised below.

BOARD OF DIRECTORS AND AUDIT COMMITTEES

- Work closely with management to ensure continued relevance of financial statements by focusing on providing high quality disclosures that are useful, sufficient and understandable.
- Prepare for deeper levels of engagement with investors who, armed with greater insights into the audit process and the underlying drivers of a company's performance, will demand greater accountability from its directors and management.
- Provide greater transparency to investors in the following aspects:
  - Issuing an audit committee commentary in the company's annual report to explain significant financial reporting issues and to complement KAMs reporting by auditors.
  - Ensuring sufficient attention is given towards providing better disclosures on the company's corporate governance practices and ensuring they stand up to scrutiny.
  - Evaluating auditors using AQIs and communicating to investors the basis of selecting the recommended auditors.

AUDITORS

- Prepare for more communication with investors given the added responsibility of KAMs reporting from January 2017 onwards.
- Seize the opportunity from KAMs reporting to bring the quality of audits to a new level.

PROFESSIONAL BODIES AND REGULATORS

- More outreach efforts are needed to enable investors to:
    - understand, consider and use both qualitative and quantitative information in financial statements for better decision making;
    - understand long established regulatory programmes (such as ACRA's PMP and FRSP) and new initiatives (such as KAMs reporting and AQIs) that ensure a robust financial reporting regime and how they can leverage on the regulatory outcomes and findings for their own investment reviews and decisions.

INVESTORS

- Make use of resources available (e.g. regulators' publications such as the annual PMP and FRSP reports, initiatives by professional bodies, investor communication channels, etc) to exercise greater scrutiny over the company's financial report, audit and corporate governance practices.
- Do not accept mediocrity – Continue to hold companies to high standards of financial reporting and corporate governance and demand for greater transparency and clarity in disclosures relevant to make investment decisions.

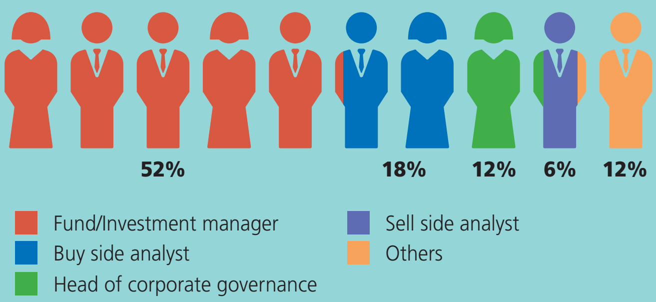
Annex A

Profile of Survey Respondents

A total of 33 institutional investors (including analysts) and 171 retail investors completed the survey.

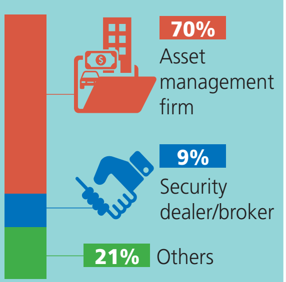
Institutional Investors

Position of respondents

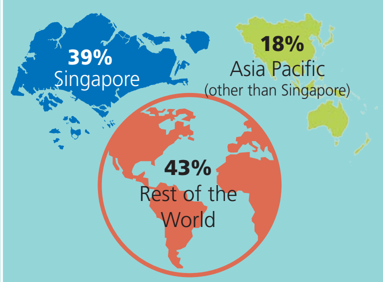


Investment responsibility of respondents

Type of organisations

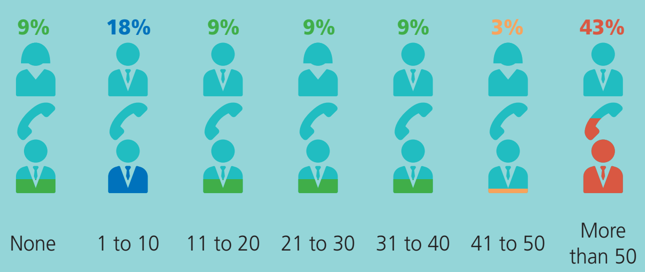


Headquarters of Organisation

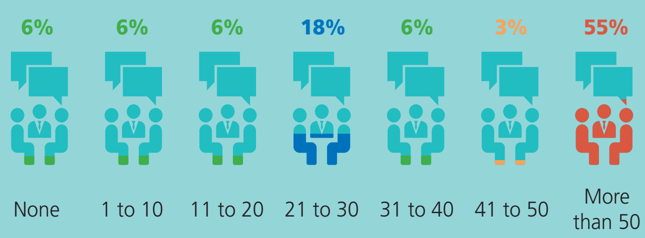


Total funds managed/advised by organisation

Participation in analyst briefings/conference calls annually



Number of one-to-one meetings (in person or through conference call) with management or board of directors each year

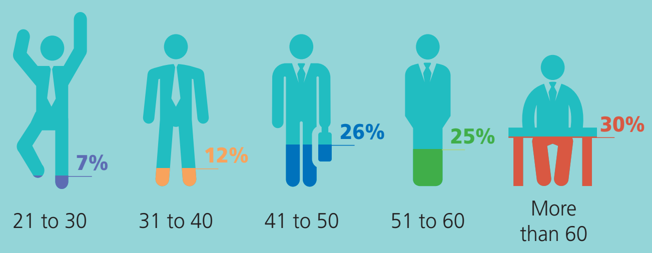


Annex A

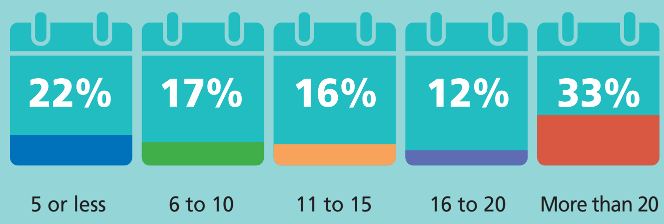
Profile of Survey Respondents

Retail Investors

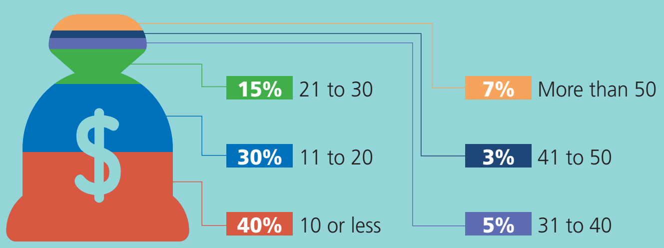
Age group of retail investors



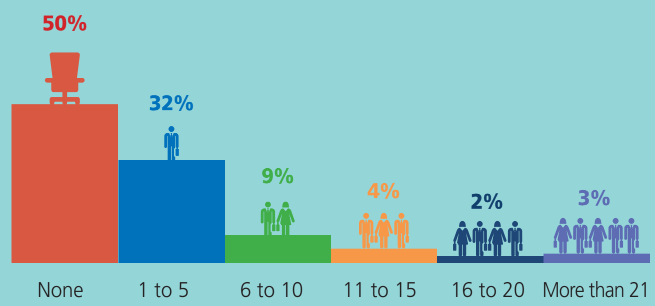
Years of investment experience



Number of listed entities invested in



Annual Attendance of AGMs



About the **ACCOUNTING AND CORPORATE REGULATORY AUTHORITY (ACRA)**

The Accounting and Corporate Regulatory Authority (ACRA) is the national regulator of business entities, public accountants and corporate service providers in Singapore. ACRA also facilitates the development of business entities and the public accountancy profession.

As a regulator and facilitator, ACRA constantly strives to provide a responsive and trusted regulatory environment for businesses, public accountants and corporate service providers and make Singapore the best and trusted place for doing business. ACRA's role is to achieve synergies between the monitoring of corporate compliance with disclosure requirements and regulation of public accountants performing statutory audit.

ACRA's goal is to make good corporate governance, quality corporate financial reporting and high quality audit the hallmarks of our financial and corporate sectors.

For more information, please visit: www.acra.gov.sg

About the **INSTITUTE OF SINGAPORE CHARTERED ACCOUNTANTS**

The Institute of Singapore Chartered Accountants (ISCA) is the national accountancy body of Singapore. ISCA's vision is to be a globally recognised professional accountancy body, bringing value to our members, the profession and wider community. There are over 30,000 ISCA members making their stride in businesses across industries in Singapore and around the world.

Established in 1963, ISCA is an advocate of the interests of the profession. Possessing a Global Mindset, with Asian Insights, ISCA leverages its regional expertise, knowledge, and networks with diverse stakeholders to contribute towards Singapore's transformation into a global accountancy hub.

ISCA is the Administrator of the Singapore QP and the Designated Entity to confer the Chartered Accountant of Singapore - CA (Singapore) - designation.

ISCA is an Associate of Chartered Accountants Worldwide – supporting, developing and promoting over 325,000 Chartered Accountants in more than 180 countries around the world.

For more information, visit www.isca.org.sg

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The National University of Singapore (NUS) Business School is known for providing management thought leadership from an Asian perspective, enabling its students and corporate partners to leverage global knowledge and Asian insights.

The school has consistently received top rankings in the Asia-Pacific region by independent publications and agencies, such as The Financial Times, Economist Intelligence Unit, and QS Top MBA, in recognition of the quality of its programmes, faculty research and graduates. In the Financial TimesGlobal Rankings, the NUS MBA was ranked 32nd in 2016, while the NUS-UCLA Executive MBA and Asia-Pacific Executive MBA were ranked 5th and 25th respectively in 2015.

In the biannual Forbes rankings for two-year MBA programmes, NUS Business School was ranked 7th among business schools outside the United States in 2015. Quacquarelli Symonds (QS) has also ranked the school 12th in the world for accounting and finance.

The school is accredited by AACSB International (Association to Advance Collegiate Schools of Business) and EQUIS (European Quality Improvement System), endorsements that the school has met the highest standards for business education. The school is also a member of the GMAC Council, Executive MBA Council, Partnership in Management (PIM) and CEMS (Community of European Management Schools).

For more information, please visit bschool.nus.edu.sg, or go to the Think Business portal, which showcases the School's research.