IS Chartered Accountant Journal

MARCH 2020

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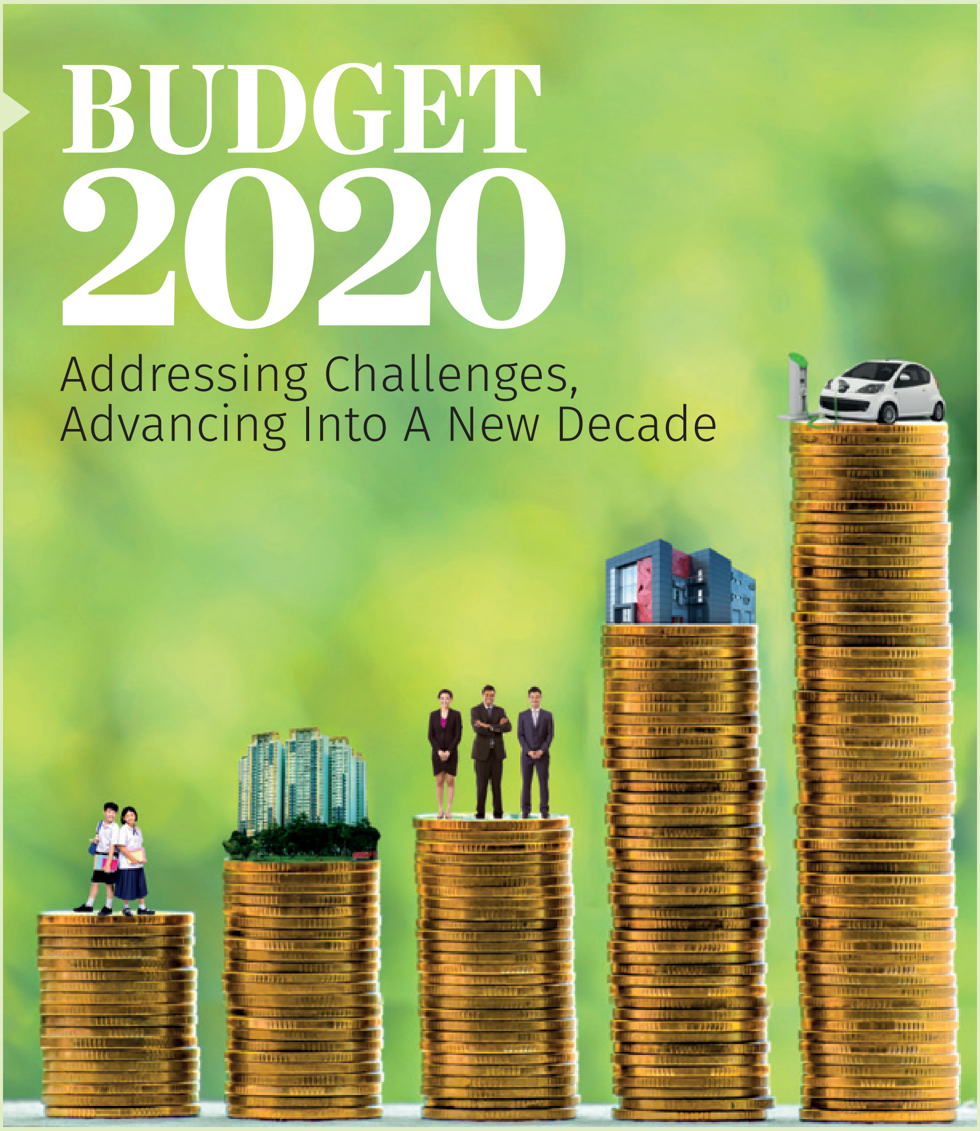

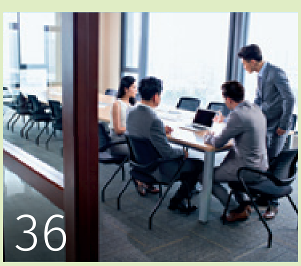

ISCA INSTITUTE OF SINGAPORE CHARTERED ACCOUNTANTS

Right Skills, Right Mindset; Be Prepared For The Unexpected

Dear members,

THE GLOBAL ECONOMY HAS BEEN EXPERIENCING SLOWER GROWTH IN RECENT YEARS, due largely to the trade tensions between the world's two largest economies, a sharper-than-expected downturn in major economies and financial turmoil in the emerging markets and developing economies. The effects have been felt by Singapore, which is deeply plugged into the global economy. Singapore grew by a modest 0.7% in 2019, its weakest since the 2008 financial crisis. Just as the global economy was beginning to show signs of recovery, the coronavirus disease 2019, or Covid-19, outbreak hit us. Covid-19 will certainly impact our economy and for 2020, Singapore's GDP forecast has been downgraded to between -0.5% to 1.5%, from the earlier 0.5% to 2.5%.

Against the backdrop of the ongoing Covid-19 outbreak, as well as uncertainties in the broader landscape beyond Singapore, Deputy Prime Minister (DPM) and Finance Minister Heng Swee Keat delivered the Budget Statement on February 18. He acknowledged the challenges facing Singapore, such as the long-term structural shifts, decline in support for globalisation, shift in economic weight towards Asia, technological disruption, and the aging population in many countries; presented the Budget details, and concluded on the uplifting note that "together, we can ensure that Singapore remains exceptional".

As expected, the Budget – dubbed the "Unity" Budget – had provisions to help enterprises and Singaporeans manage the immediate challenges brought on by Covid-19, and it did not lose sight of the country's focus to position itself for future growth and continued success. The Budget is a strategic financial plan to prepare Singapore and Singaporeans to seize emerging opportunities, and in the cover story, we bring you the key points and further insights from our panel of experts.

As I was watching Mr Heng's delivery in Parliament, a few thoughts came to my mind. As you know, the Institute is an active advocate for member upgrading and upskilling, and our initiatives are centred on equipping members with the competencies to navigate the more complex business landscape. Accountancy is the backbone of economies, and it will remain so as ISCA members with the requisite skill sets and agile, adaptable mindsets continue to play their part to support Singapore's longer-term plans to be positioned as a Global-Asia node of technology, innovation and enterprise.

While schemes like the SkillsFuture Credit top-up, as announced by DPM Heng, will help defray some CPE training fees, it is more essential for members to stay the course as it takes time and concerted effort to keep ahead in an evolving business environment. In this respect, I encourage members to remain profoundly committed to your individual learning journey as it is often what you know that bolsters you when you meet with the unexpected. Have a glimpse into the future of accountancy in the article, "Re-imagining The Future Accountant". Are there any surprises? Do you have the right skills and mindset for success?

On a different note, March 8 is International Women's Day which celebrates the social, economic, cultural and political achievements of women. The day also marks a call to action for accelerating women's equality. Although Singapore has come some way to achieve gender parity at the workplace, more can still be done, says ISCA member Grace Fu, Minister for Culture, Community & Youth, in a special interview in conjunction with International Women's Day. Be inspired by the Minister as she encourages women to stand up and be counted – even if it means a change in self-perception – in this month's Member Profile.

Speaking of change, one area that has changed significantly is the tax landscape. In 2010, ISCA, in partnership with the Tax Academy, had set up a subsidiary – Singapore Institute of Accredited Tax Professionals (SIATP) – to support ISCA members specialising in tax. Today, with the increased complexity in tax developments, there is a need to widen SIATP's ambit beyond serving accountancy-trained tax professionals to include a wider audience, to strengthen Singapore's status as a financial hub. To facilitate its next stage of development, SIATP will operate as an independent entity by the second quarter of 2020, while continuing to work closely with ISCA to support tax professionals in Singapore.

We all know that change is a constant, and we can better manage the unexpected (caused by change) if we have the right attitude and knowhow. Be prepared!

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Only 17% Of Organisations Globally Considered "Leaders" In Cyber Resilience

DESPITE HIGHER LEVELS OF INVESTMENT in advanced cybersecurity technologies over the past three years, less than one-fifth of organisations are effectively stopping cyberattacks and finding and fixing breaches fast enough to lower the impact, according to a new report from Accenture.

Based on a survey of more than 4,600 enterprise security practitioners around the globe, Accenture's Third Annual State of Cyber Resilience study explores the extent to which organisations prioritise security, the effectiveness of current security efforts, and the impact of new security-related investments.

From detailed modelling of cybersecurity performance, the study identified a group of elite "leaders" – 17% of the research sample – that achieved significantly better results from their cybersecurity technology investments than other organisations. Leaders were characterised as among the highest performers in at least three of the following four categories: stop more attacks, find breaches faster, fix breaches faster and reduce breach impact. The study identified a second group, comprising 74% of the respondents, as "non-leaders" – average performers in terms of cyber resilience but far from being laggards.

"Our analysis identifies a group of standout organisations that appears to have cracked the code of cybersecurity when it comes to best practices," says Kelly Bissell, who leads Accenture Security globally. "Leaders in our survey are far quicker at detecting a breach, mobilising their response, minimising the damage and getting operations back to normal."

For instance, leaders were four times more likely than non-leaders to detect a breach in less than one day (88% vs 22%). And when defences fail, nearly all (96%) of the leaders fixed breaches in 15 days or less on average, whereas nearly two-thirds (64%) of non-leaders took 16 days or more to remediate a breach, with nearly half of those taking more than a month.

The study also found that more than four in five respondents (83%) believe that organisations need to think beyond securing just their own enterprises and take better steps to secure their vendor ecosystems. Additionally, while cybersecurity programmes designed to protect data and other key assets are only actively protecting about 60% of an organisation's business ecosystem, which includes vendors and other business partners, 40% of breaches come through this route.

"The sizeable number of vendor relationships that most organisations have poses a significant challenge to their ability to monitor that business ecosystem," says Mr Bissell. "Yet, given the large percentage of breaches that originate in an organisation's supply chain, companies need to ensure that their cyber defences stretch beyond their own walls."

Key differences in cybersecurity practices between leaders and non-leaders

- Leaders focused more of their budget allocations on sustaining what they already have, whereas the non-leaders place significantly more emphasis on piloting and scaling new capabilities.
- Leaders were nearly three times less likely to have had more than 500,000 customer records exposed through cyberattacks in the last 12 months (15% vs 44%).
- Leaders were more than three times as likely to provide users of security tools with the required training forthose tools (30% vs 9%).

PHOTOS **SHUTTERSTOCK**

AI Will Be An Essential Business Driver For Financial Services Within Two Years

ACCORDING TO SENIOR EXECUTIVES SURVEYED IN THE FINANCIAL SERVICES INDUSTRY, artificial intelligence (AI) is expected to be an essential business driver across the industry, with 77% of respondents anticipating AI to possess high or very high overall importance to their businesses in the next two years. The findings are from Transforming Paradigms: Global AI in Financial Services Survey, a new global survey assessing the current state of AI adoption by financial services organisations. The survey was led by the Cambridge Centre for Alternative Finance at the University of Cambridge Judge Business School and the World Economic Forum, and co-sponsored by EY and Invesco.

The study also revealed that 85% of respondents have already implemented AI within their organisations and expect to use AI for new use cases in the coming years. Additionally, nearly two-thirds (64%) expect to use AI for new revenue generation, process automation, risk management, customer service and client acquisitions within two years.

Increased adoption of AI technologies across the financial services industry also comes with challenges, as data quality, access to data and competition for talent are all seen as major obstacles to implementing AI by more than 80% of senior executives. When it comes to respondents who predominantly use autonomous AI, the attitudes shift, with 80% of respondents perceiving trust and user adoption to be the most significant hurdle.

Nigel Duffy, EY Global Artificial Intelligence Leader, says, "AI is transforming the financial services industry and we can expect widespread adoption to continue. As the technologies start to disrupt business models and transform business functions, it's increasingly important for organisations to focus on the long-term implications of AI adoption: trust in AI, workforce transformation and how customer and stakeholder value can be radically reimagined."

Matthew Blake, Head of Financial and Monetary Systems, World Economic Forum, affirms that AI is "impacting the financial system at an accelerating pace". With the rising trend of mass adoption of the technologies throughout financial services, there will be a significant gap between firms that quickly implement AI and firms that lag behind.

SINGAPORE CONTINUES TO BUILD AI ECOSYSTEM

As Singapore develops its digital economy, there is a need for a trusted ecosystem where organisations can benefit for tech innovations, and consumers are confident to adopt and use AI. A Model AI Governance Framework (Model Framework) was released in January 2019 for broader consultation, adoption and feedback, and the second edition of the Model Framework was released on 21 January 2020.

Recognising that there is much to gain from AI, Singapore has been looking to develop niches with AI research and development (R&D), building local capabilities and fostering partnerships among relevant parties. This is done through a national programme called AI Singapore, which will bring together all Singapore-based research institutions and the vibrant ecosystem of AI startups and companies developing AI products, to grow the knowledge, create the tools and develop the talent to power Singapore's AI efforts. It is driven by a government-wide partnership of agencies.

More Singapore Enterprises Stepped Up Transformation Efforts Amid Challenging 2019

DESPITE THE CHALLENGING ECONOMIC CONDITIONS in Singapore last year, 11,450 enterprises embarked on 13,560 projects to raise productivity, enhance innovation and accelerate internationalisation, says Enterprise Singapore (ESG), and it expects a total of S$17.3 billion in value added and 21,700 PMET jobs to be generated through these projects. The data was shared on February 7 at the ESG year-in-review event.

Small and medium-sized enterprises (SMEs) undertook the majority of these projects. Both the number of enterprises and projects supported increased significantly (43% and 52% respectively) over 2018.

Productivity and capability-building projects increased by 85% as compared to 2018. These were undertaken by 8,300 enterprises, with the majority from the services sectors – lifestyle, trade, transport and logistics – to improve business processes and be more manpower-lean. Many of these efforts to automate and digitalise were done through easy-to-adopt solutions supported under the Productivity Solutions Grant.

The number of innovation projects remained consistent, with 550 enterprises supported last year. Enterprises have benefitted from connections with technology resources and experts, as well as participation in open innovation calls and collaborations with public and large private-sector organisations. The Centres of Innovation assisted 120 enterprises on 180 innovation projects.

Some 2,000 startups benefitted from mentorship, incubation opportunities and funding through the Startup SG programmes and partners. The startup ecosystem was further strengthened with the appointment of 17 new Accredited Mentor Partners and 23 accelerators across food manufacturing, agritech, edutech, healthcare and biomedical, and transport and logistics sectors to groom high-growth startups.

Of the 3,000 internationalisation projects undertaken by 2,600 enterprises, 60% were by enterprises in the wholesale trade, professional services, ICT (information and communications technology) and retail sectors. ESG facilitated and provided on-the-ground assistance to 600 projects, which are expected to bring about S$8.8 billion of overseas sales and S$8.9 billion of overseas investments. China and Southeast Asia remained the top markets of interest based on the projects ESG facilitated.

ESG also enhanced its international connections to help more startups and tech SMEs access overseas collaboration and innovation opportunities by expanding the Global Innovation Alliance (GIA) network to four new cities – Shanghai, Ho Chi Minh City, Bangalore and London – in 2019. The GIA network now spans across 13 cities in 10 markets.

PHOTO SHUTTERSTOCK

Stay Atop CPF And Tax Changes

AMID THE HUSTLE AND BUSTLE OF THE NEW YEAR, many accredited tax professionals continue to scale the heights of tax excellence as they recently attended a *Tax Excellence Decoded* session organised by the Singapore Institute of Accredited Tax Professionals (SIATP). Characterised by vigour and filled with insights, the session highlighted the key concepts and interpretations of the Central Provident Fund (CPF) Act.

Diving into the case law on independent contractor versus employees, participants were able to tap on the expertise of Sandesh Kumar, Director, and Sharon Chiam, Associate Director, both from the People Advisory Services – Mobility, EY Corporate Advisors team, as the facilitators shed light on their perspectives and the various tax implications for business owners. Coupled with a robust Q&A session joined by Accredited Tax Advisor (Income Tax) Kerrie Chang, Partner, People Advisory Services – Mobility, Ernst & Young Solutions, an array of issues were discussed, dispelling the many doubts of participants.

Accredited Tax Advisor (Income Tax) Kerrie Chang, Partner, People Advisory Services – Mobility, Ernst & Young Solutions, together with her team, discussed the finer points of the CPF Act and its interpretations

Participants were able to raise their areas of concern with regard to CPF contributions on reimbursement

If you too wish to traverse the terrain and stay atop the tax mountain, contact enquiry@siatp.org.sg.

ISCA Journal Wants You!

The *IS Chartered Accountant Journal* invites and welcomes original articles of relevance to the accountancy profession on a continuous basis.

IS Chartered Accountant Journal

PREFERRED TOPICS

- Mergers and acquisitions (e.g. valuation methods)
- Climate change and sustainability reporting
- Data protection and privacy
- Risk management and the use of technology
- Technology-related articles (e.g. artificial intelligence, cybersecurity, data analytics, natural language processing, etc)
- Impact of global development on the economy (e.g. trade tensions between US and China, protests in Hong Kong, Brexit, US Elections 2020, etc)
- Issues related to small and medium-sized enterprises (e.g. Impact of Free Trade Agreements on business strategies, internationalisation, digitalisation, etc)
- Diversity and inclusivity of the labour force in areas such as gender and ethnicity

IMPORTANT NOTES

1) All articles must be the author's original work and must not have been published before in another medium of any kind.
2) All articles may be edited for clarity or length. The copyright of the edited article will belong to ISCA.
3) All articles should be submitted in electronic form using Microsoft Word.
4) All articles should be between 1,200 and 1,400 words.
5) All sources referenced must be cited using proper footnotes.

Please reach out to the editorial team at **editor@isca.org.sg** with your articles now.

MARK YOUR CALENDAR

12 MAR — ISCA Budget Update 2020

In It to Ace It. Get in tune with SG Budget 2020 in 4 hours!

Join us at the ISCA Budget Update 2020 Seminar where SMU's Professor of Accounting (Practice) Sum Yee Loong will analyse the tax implications of the various Budget 2020 proposals and how these will affect businesses and individuals. Mr Irvin Seah, Executive Director, Group Research, DBS Bank, will deliver a presentation on the Economic Outlook and Analysis of Budget 2020, followed by a panel discussion with industry leaders on Budget proposals.

18 MAR — Ethical Whistle Blowing: Is It My Responsibility To Report?

Explore the ethical and legal issues surrounding whistle blowing, including a discussion on "grey situations" to enable participants discern when to whistle blow.

19 MAR — Managing GST Audits

This workshop aims to provide participants with the following :-

- GST audit process
- GST risks areas
- Common errors noted by IRAS during audits conducted by them

20 MAR — Master Class Boardroom Presentation Skills

UTAP Funding approved

This course aims to:

- Empower Senior Management Executives with skills to boost personal and professional presentation performance that will enable the board to make the appropriate decisions following your presentation
- Equip participants with tools and techniques to deliver compelling, dynamic and effective presentations

24 MAR — Accounting for Financial Instruments under FRS 32, FRS 107 and FRS 109

This seminar aims to provide a practical overview and insights on the classification, recognition, measurement and disclosure requirements of financial instruments under FRS 109.

It covers the business model concept as well as hands on guidance on the identification whether a financial instrument is based on determinable cash flows.

26 & 27 MAR — Applied Robotics Process Automation (RPA) for Auditors

NEW!

Participants from Small and Medium-sized Practices "SMPs" are entitled to ESG funding

This course aims to equip participants with the skills to easily create useful RPA scripts to automate the audit processes, without coding or programming knowledge. They will learn how to achieve this through using a RPA software.

At the end of the course, participants will be able to immediately use the RPA solutions and adopt the use of RPA in their workplace.

Dates and events are subjected to change without prior notice.

BY STELLA LAU AND FELIX WONG

BUDGET 2020

Addressing Challenges, Advancing Into A New Decade

DEPUTY PRIME MINISTER AND MINISTER FOR FINANCE HENG SWEE KEAT delivered the 2020 Singapore Budget Statement on February 18 in Parliament. Opening his speech, Mr Heng stressed that growing uncertainties in the global economic climate and the Covid-19 virus outbreak demanded quick responses to address them. Alluding to additional efforts by the government, Mr Heng set the stage for a comprehensive set of measures he was to announce by pointing to the increased number of Budget files he had with him this year and jokingly requested the audience to be patient while listening to him.

Indeed, Budget 2020 rose to the occasion, setting out a spending injection of $106 billion and wide-ranging measures to address short-term challenges due to the Covid-19 outbreak and economic downturn, as well as longer-term transformation and growth plans. The broad-based Budget, commended by many industry and business leaders as "far-reaching", "substantive'" and "extraordinary", represents a historic deficit of $10.9 billion – the highest in a decade.

To tackle the ongoing geopolitical uncertainties exacerbated by the virus outbreak, the Stabilisation and Support Package will render targeted support to sectors hit by the Covid-19 crisis. This includes up to 30% property tax and 25% corporate income tax rebates, rental waivers and schemes to sustain wages and retain jobs, as well as providing financing for enterprises. Another major relief to businesses and the public is the deferment of the Goods and Services Tax (GST) hike.

Economic transformation and growth have also remained as priorities for Budget 2020. This year, the government allocated $8.3 billion for the next three years to catapult enterprises and the economy into transformation and growth. This funding will be pumped into supporting measures under three main thrusts:

Help also needs to be delivered in a targeted manner. For instance, as the profiles of business owners in different industries are unique, the approach to driving outreach and administering help may need to be more targeted.

PHOTO SHUTTERSTOCK

1) Enabling stronger partnerships

A small and open economy like Singapore must continue to strengthen partnerships globally and within itself. An established extensive network of economic linkages has been built, including Free Trade Agreements (FTAs) and International Investment Agreements. More needs to be done to enhance digital connectivity, and to continue to support the digitalisation of Finance, such as fintech (financial technology) and digital banking.

Another priority is to strengthen partnerships within Singapore to drive innovation and deepen industry-wide capabilities. For example, Enterprise Singapore will launch a pilot Executive-in-Residence programme which will fund more than 10 trade associations and chambers (TACs) covering all sectors of the economy. Funding will go towards hiring experienced executives to provide professional advice to enterprises in their industries with the aim to scale up and raise the capabilities of the industries.

2) Deepening enterprise capabilities

On the transformation agenda, the Budget metes out enhanced support to enterprises at each stage of growth, building on existing measures. One focus is on catalysing investments into deep-tech startups. For growing and more mature enterprises, measures include expanding the existing SMEs Go Digital programme and increasing coverage of the Market Readiness Assistance grants to include FTA consultancy costs. A new initiative, the Enterprise Transform Package focuses on nurturing business leaders of promising small and medium-sized enterprises (SMEs) with training and mentorship. A new one-stop GoBusiness platform has also been launched for enterprises to transact with the government digitally.

3) Developing people

As enterprises restructure, the nature of jobs will change. To help the workforce stay relevant, measures have been designed to encourage workers and enterprises to commit to upskilling and training. Apart from the one-off SkillsFuture Credit top-up of $500 for every Singaporean aged 25 years and above, enterprises will be incentivised to send existing workers for skills upgrading through the new SkillsFuture Enterprise Credit, with the aim to transform both their workforce and enterprise. Employers can utilise this $10,000 enterprise credit to defray 90% of out-of-pocket costs of business transformation, job redesign and skills training.

Support is also extended to mid-career and senior workers. This includes incentives and credits for employers to hire mature workers, more reskilling programmes and a special SkillsFuture Credit top-up of another $500 for every Singaporean aged 40 to 60 years in 2020.

Institutes of higher learning (IHLs) also play a pivotal role in preparing the future workforce. Several programmes such as the Asia-Ready Exposure Programme will be introduced to increase overseas exposure of our students and to help them acquire cross-cultural skills. In addition, IHLs will also work with more enterprises through the SkillsFuture Work-Study Programmes to enable our students to learn in a real work environment.

ISCA POST-BUDGET 2020 FOCUS GROUP SESSION

To gather immediate feedback on Singapore Budget 2020 ahead of the Committee of Supply debates, ISCA convened a focus group session attended by representatives from TACs and accountancy firms. An annual event, the ISCA Post-Budget 2020 Focus Group event was held three days after the Budget Statement was delivered.

PHOTO SHUTTERSTOCK

Overall, representatives concurred that the Budget is comprehensive and strategically balances varying needs in the year ahead. It addresses short-term requirements and lends immediate support to tide enterprises over the current Covid-19 crisis and economic slowdown. At the same time, there are plans towards longer-term priorities to pitch Singapore as a global player. The Budget also caters to businesses across industries and segments of the population. Many praised the move to delay the GST increase, as it will be helpful to businesses to mitigate current challenging times.

The panel also discussed specific schemes and initiatives laid out in the Budget, and how they can be better rolled out to help enterprises, particularly the smaller ones. We highlight some of the key discussion points here.

Budget 2020 presents a buffet of grants

Panellists were unanimous that Budget 2020 presents overwhelming support to the business community. They acknowledged the buffet of grants available and felt very encouraged.

While this means enterprises will have more chips in hand, panellists also highlighted that the plethora of grants are compounded by specific requirements and eligibility criteria, which may be confusing to enterprises. On top of this, many enterprises may not be aware of existing grants and how to access them.

Therefore, it is necessary to support enterprises in identifying relevant grants to address differing needs. Small businesses can turn to an SME Centre as the one-stop touchpoint for one-to-one customised help. But some panellists pointed out that, based on past observations, some consultants at SME Centres may not be sufficiently familiar with specific industries to provide useful advice. There is a need to ensure that SME Centre consultants are trained and matched with relevant expertise to specific industries.

Small businesses are struggling; immediate financial support is the crux

The onus is now on enterprises to proactively reach out for help, to find out about available grants and apply for relevant schemes. In line with this, panellists also called for quicker and more timely disbursement of grants in order to avail immediate financial support.

Many small businesses, especially micro-enterprises, are struggling to keep their businesses afloat and some have already closed down, even before the Budget Statement was delivered. Unlike larger businesses, smaller enterprises tend to have less reserves and hence, are less likely to set aside funds for emergency purposes. Spare cash is typically reinvested into the business, such as in acquiring equipment or digitalising their business. As such, small businesses are likely to be more vulnerable to an economic downturn. They require immediate financial support and cash flow to tide them through the difficulties they are now experiencing. In all likelihood, they cannot wait till the disbursement of grants, such as the Jobs Support Scheme in July, as they face the impending prospects of laying off their workers. Separately but tied to this, while property tax rebates will be provided, it is uncertain if landlords will pass on the cost savings to tenants through reduced rentals.

Larger businesses could also play a bigger role to render quick support to smaller businesses by giving out micro-loans. A notable example is the $5 million SBF-YBLN HOPE Fund (Singapore Business Federation-Young Business Leaders Network "Helping Our Promising Enterprises" Fund) set up by a group of next-generation Singapore-based family offices to help SMEs. Industry and business leaders commended this as a quick and useful initiative and called for more of such similar ground-up funds to be raised.

Delivering help in a better way: be direct, flexible and targeted

For small businesses, help needs to be provided directly. This means cutting away intermediaries. For example,

Managing business sentiment well is important and a better positioning can help to calm the business community in this time of crisis, and reduce anxiety. Panellists called for the government to communicate stronger reassurance – that more help will be given based on developments.

... to complement the government's efforts, TACs can work closer together to "cross-fertilise" and offer mutual help in their respective areas of expertise.

providing financing via financial institutions may result in potential delays. Some panellists also mentioned that grants provided to support the hiring of external consultants to implement transformation projects may not have been the best use of the money, and that enterprises could have been more empowered to decide the best ways to use it.

Help also needs to be delivered in a targeted manner. For instance, as the profiles of business owners in different industries are unique, the approach to driving outreach and administering help may need to be more targeted.

In addition, allowing more flexibility in issuing grants will help enterprises with differing needs. For example, limiting the scope of certain grants to cover only specific software solutions or consultancy services may be too restrictive. It was recommended for the scope of grants to be broadened to include any software solutions that can help enterprises digitalise, such as human resources software.

Also, more flexibility could be exercised when assessing whether enterprises meet qualifying grant requirements, so that more enterprises can benefit from the grants. A suggestion was to reinstate the Productivity Innovation Credit (PIC) scheme – but in a more targeted manner – to help SMEs and to prevent misuse.

Manage sentiments with more balanced messaging to raise business confidence

Another recommendation was for the government to present a more balanced position on the current challenges and economic situation. The government may have exercised too much caution in communicating about the current geopolitical and Covid-19 situation.

Managing business sentiment well is important and a better positioning can help to calm the business community in this time of crisis, and reduce anxiety. Panellists called for the government to communicate stronger reassurance – that more help will be given based on developments.

One suggestion was for the government to focus on communicating what businesses can do to cope better. For example, encouraging enterprises to digitalise by featuring success stories of how enterprises that have digitalised have successfully overcome similar crisis situations. To support this, key statistics can be shared, such as online businesses performing better than brick-and-mortar stores.

PHOTO SHUTTERSTOCK

The government can also encourage businesses to plan ahead. Engaging in scenario-planning for the longer term can help enterprises better prepare for an economic recovery. Another suggestion was to lay out potential solutions for enterprises to support their decision-making. For instance, consultancy advice on how to manage cash flow will be helpful.

To boost confidence and raise morale, the government can share success stories of how small enterprises overcame challenging times, such as during the 2003 SARS outbreak. This could provide valuable lessons which enterprises can learn from. These stories can be broadcasted in the mass media and shared on social media platforms.

Leverage shared resources model and drive collaboration

Enterprises can also work closer to help one another. One way is to utilise a shared resources model. For example, while small businesses may not be able to afford hiring a full-time experienced professional, they can look into co-employing one with a few enterprises. This will enable small enterprises to acquire skilled talent while minimising costs. This will also ensure that the experienced professional receives a competitive remuneration from being contracted to a few employers.

With the development of the gig economy, it becomes increasingly important to put in place supportive measures for freelancers. Panellists suggested that the Ministry of Manpower can take the lead to issue guidelines when engaging freelancers, centring on requiring enterprises to use written contracts, contribute to Central Provident Funds accounts and make available insurance products, among others.

Furthermore, to complement the government's efforts, TACs can work closer together to "cross-fertilise" and offer mutual help in their respective areas of expertise. For example, the Association of Small and Medium Enterprises (ASME) can work with the Singapore Institute of Accredited Tax Professionals (SIATP) so that smaller businesses who need tax advisory services can reach out to SIATP.

The academic community can also play a part. Driving collaboration between IHLs, TACs and enterprises, such as getting students from IHLs to support enterprises in their digitalisation efforts, is one good example.

To encourage partnership and collaboration, as well as to help many small businesses that lack knowledge in managing cash flow matters, one suggestion was to organise an "SME Day". This will bring together small business owners and larger enterprises who are providing HOPE funds. TACs with the technical expertise can also run knowledge sessions on relevant topics such as cash flow management at this SME Day.

CONCLUSION

Overall, there has been resounding approval for Budget 2020. The direction is clear – address pressing immediate challenges while still gearing up for the future. As the government enhances support for enterprises, there is also a need for enterprises to reflect on their roles and how they can help one another. All stakeholders including TACs and academia can explore ways to work more closely. In doing so, we may find resilience in closer collaboration and a tighter-knit ecosystem.


PHOTO SHUTTERSTOCK

To encourage enterprises to continue investing in their businesses and also provide a boost to the economy, enterprises will be provided with an option to accelerate the write-off of the cost of plant and machinery acquired in FY 2020, with 75% of the cost to be written off in YA 2021 and the balance of 25% written off in YA 2022.

TAX MEASURES

Corporate tax measures to help businesses with cash flow

To ease the financial pressure on cash-strapped businesses, a corporate income tax rebate of 25%, capped at $15,000, has been introduced for Year of Assessment (YA) 2020. While the rebate is available to all enterprises, it will be more important to alleviate the cashflow of SMEs.

An extension of two months of interest-free instalments will also be granted to enterprises paying their corporate income tax by GIRO. This extension will apply to enterprises that file their estimated chargeable income (ECI) from 19 February 2020 to 31 December 2020, or enterprises that file their ECI before 19 February 2020 and have ongoing instalment payments to be made in March 2020. As the extension is automatic, there will be no additional administrative burden on enterprises.

Enterprises that are not in a tax-paying position in YA 2020 (and hence unable to benefit from the corporate tax rebate) but are profitable in the past YAs may look to the enhanced carry-back relief scheme. Under the enhanced scheme, qualifying deductions (unabsorbed capital allowances and trade losses) for YA 2020, capped at $100,000, may be carried back up to three immediate preceding YAs (previously, it was only up to the immediate preceding YA). To accelerate the tax refund, eligible enterprises may elect to carry back an estimated amount of qualifying deductions before the actual filing of their YA 2020 tax returns.

To encourage enterprises to continue investing in their businesses and also provide a boost to the economy, enterprises will be provided with an option to accelerate the write-off of the cost of plant and machinery acquired in financial year (FY) 2020, with 75% of the cost to be written off in YA 2021 and the balance of 25% written off in YA 2022. They will also be provided with an option to accelerate the deduction of qualifying expenditure incurred on renovation and refurbishment for YA 2021 in one YA (instead of over three consecutive YAs currently).

Property tax rebate to support specific sectors

As part of the Stabilisation and Support Package, property tax rebate of up to 30% will be granted to licensed hotels, serviced apartments, prescribed Meetings, Incentives, Conferences and Events (MICE) venues, and other qualifying commercial properties for year 2020. The property tax rebate seeks to alleviate the impact on the sectors most severely affected by the Covid-19 situation, such as tourism and retail.

As the property tax rebate will be made to qualifying commercial property owners, the positive impact of this measure will depend on whether the property owners will heed Mr Heng's call to pass on the benefits to their tenants, who are the hardest hit group in this crisis.

The whole-of-Singapore spirit of the 2020 "Unity" Budget shone through. Within days, several property developers had announced that they would pass on the full savings from the property tax rebate to their tenants.

Refining Singapore's tax system

Several tax schemes that remain relevant to Singapore will be extended and refined.

The Mergers and Acquisitions (M&A) scheme, which encourages enterprises to grow through strategic acquisitions, will be extended to cover qualifying acquisitions made on or before 31 December 2025. Similarly, the Double Tax Deduction for Internationalisation (DTDi) scheme will also be extended till 31 December 2025. The scope of the DTDi scheme, which allows businesses an enhanced tax deduction on qualifying market expansion and investment development expenses, will be expanded to cover certain categories of expenses, including third-party consultancy fee to identify suitable talent and build up business network, from 1 April 2020.

The scheme under Section 13Z of the Income Tax Act providing upfront certainty of non-taxation of gains on disposal of ordinary shares by enterprises will be extended to 31 December 2027. However, it will no longer apply to disposals of unlisted shares in an investee company that is in the business of trading, holding or developing immovable properties, whether situated in Singapore or abroad, from 1 June 2022.

Notably, there was unanimous and collective relief when Mr Heng announced the deferment of the 2% GST increase. However, this will still take place between 2022 to 2025. To reassure the public, especially the lower-income group, a $6-billion Assurance Package was rolled out to cushion the impact of the future GST increase. ISCA

Stella Lau is Manager, Insights and Publications, ISCA, and Felix Wong is Head of Tax, SIATP.

"That's my wish – for corporate leaders and the wider society to have the attitude that men and women can play equal roles. Everyone, man or woman, deserves a chance to balance work and family commitments however they like."

MEMBER PROFILE

STAND UP, Be Counted

WITH INTERNATIONAL WOMEN'S DAY FALLING ON MARCH 8, renewed attention is being paid to the issue of gender equality and women's empowerment. This is all in a day's work for Grace Fu, 56, as it has been throughout her journey in both the private and public sectors. Ms Fu has occupied top executive business positions as well as high political office at different times in her career. In 2012, she became only the second woman in Singapore's history to be promoted to full Minister and, following her appointment as Minister for Culture, Community and Youth in 2015, became the first to helm a ministry. However, her fight for gender equality is far from over.

Grace Fu, FCA (Singapore), Minister For Culture, Community And Youth

PRIORITIES AND TRADE-OFFS

Women are definitely better off today than in previous generations, thanks to decades of hard-won gains that gender rights advocates have made at the workplace. But there is a long way to go yet. "Despite our meritocratic ideals, the reality is that leadership opportunities are still unequal between men and women," laments Ms Fu. Gender bias – whether explicitly stated in company policies or shaped by implicit cultural norms – still exists, and hinders women's career progression to senior management.

Oftentimes however, she notes that it is the women who hold themselves back from advancement by putting up self-imposed barriers. "As women, we are not just professional accountants but also mothers, daughters, sisters and wives, with all of the caregiving burden these roles bring. The societal role of women, including the role women expect of themselves, remains different from that of men."

Ms Fu's own experience, in a way, bears this out. In 1995, the then-mother of two – she now has three sons aged 28, 26 and 23 – left her job at Haw Par Group to spend more time at home with her family. "Because my job required a lot of travelling, I missed several important milestones in my children's lives, like my second son walking for the first time," says Ms Fu. Joining the Port of Singapore Authority (PSA) allowed her to have more manageable work hours while still working in an exciting environment, as the statutory board was then in the midst of being privatised.

Likewise, Ms Fu turned down invitations to take up political positions before finally saying yes in 2006, when her children were older and more independent. By that time, she had also acquired sufficient grounding in the commercial sector and felt ready to make the switch. Most of all, the "call to serve" was one Ms Fu could no longer ignore. "I felt a call to make a bigger contribution towards nation-building – to make people around me better, and not just myself or one company."

Striking a balance between work and family did not come easily to Ms Fu and even today, it continues to be a constant juggling act. "There is a tendency to want to have everything, but real life is not like that. You

CAREER HIGHLIGHTS

1985
Auditor, Overseas Union Bank

1991
Worked in corporate planning, financial controls and business development at Haw Par Group

1995
Assistant Director (Finance), Port of Singapore Authority (later renamed PSA Corporation)

1998
Financial Controller, PSA Corporation

1999
Executive Vice President (Finance), PSA Corporation

2003
CEO, PSA Singapore

2004
CEO, PSA South East Asia and Japan

2006
Minister of State for National Development
Member of Parliament, Jurong GRC (Yuhua) (until 2011)

2008
Senior Minister of State for National Development and Education

2011
Senior Minister of State for Information, Communications and the Arts
Senior Minister of State for the Environment and Water Resources
Member of Parliament, Yuhua SMC (until present)

2012
Minister, Prime Minister's Office
Second Minister for Foreign Affairs
Second Minister for the Environment and Water Resources

2015 to Present
Minister for Culture, Community and Youth

have to make trade-offs based on what your priorities are at that time," she explains. During her children's early years, that meant prioritising family over work. A regular jogger and yoga enthusiast, she also filled her "me" time back then with family-oriented outdoor activities like swimming and cycling.

For women who decide to take a back seat at work to raise their children, the trade-off is that they will probably not get ahead as quickly as their colleagues who have put in more effort at work. But that does not mean their career aspirations are completely dashed, as long as employers are supportive in leaving the door open for women to eventually re-enter the workforce and return to the leadership track.

In a truly gender-equal world, according to Ms Fu, men have just as much chance to contribute at home as women do in the office. Out are traditional views segregating men as breadwinners and women as homemakers; in are company HR practices offering work-life flexibility to all employees. "That's my wish – for corporate leaders and the wider society to have the attitude that men and women can play equal roles. Everyone, man or woman, deserves a chance to balance work and family commitments however they like," she says.

CRACKING THE GLASS CEILING

Jokingly calling herself "a reluctant accountant", Ms Fu chose a career in accountancy for pragmatic reasons. The promise of steady employment and financial stability was uppermost in her mind when considering which degree to pursue. Later on, as the years passed, the flexibility and transferable skills afforded by Ms Fu's accountancy training enabled her to excel in a variety of roles. From her first job as an internal auditor at a bank, she would go on to join the C-suite at PSA, where she was responsible for the business performance of the group's flagship terminals in Singapore, Thailand, Brunei and Japan.

Heading the Ministry of Culture, Community and Youth (MCCY) has also, to her surprise, presented situations where Ms Fu relies on her past experiences in internal controls and fraud investigation. "At MCCY, our efforts are centred on building social capital. The Commissioner of Charities falls under MCCY's purview; ensuring regulatory compliance of charities is a big part of what we do. My financial operations background is very helpful in assessing whether there are competent people running a charity outfit, and whether measures are in place to detect fraud," she explains.

Indeed, accountancy professionals can play a big role in aiding the growth of the non-profit sector. Participating in ISCA Cares is one avenue; another is volunteering with social service organisations to improve their accounting processes and prevent funds from being mishandled. "With a solid and efficient system in place, social service organisations can ensure that the cost of a particular programme is well accounted for," says Ms Fu. "This aids the government's work in administering grants and deciding how best to dispense funds. Moreover, it increases public confidence in

> "Don't short-change yourself. You have so much to offer in so many ways. Give yourself a chance to go beyond what you think you can do. Think about how you can create a positive impact on the people around you, and believe in yourself to make this happen."

the charity sector so the act of giving among the public can be better promoted."

Ms Fu's rise to the top is all the more impressive given how few women there are at the senior level. Despite the significant female talent pool, gender diversity in senior management and Boards – while slowly improving – remains elusive in most workplaces, including the accountancy industry. Greater support from organisational stakeholders is vital. Companies stuck in the "old boys' club" mentality should review their policies surrounding Board renewals and appointments to bring in fresh female faces. Ms Fu also urges shareholders and existing female Board directors to be more vocal in championing women leaders at work. After all, research shows that companies with gender-diverse Boards tend to perform financially better than those with all-male Boards.

Aspiring women leaders, on their part, are encouraged to take a proactive stance. "Open communication with your supervisor is important. Whether you plan to take a step back from work for family reasons or are keen to take on more work tasks, share with your supervisor your goals. Otherwise, time and opportunities may be missed by second-guessing one another," advises Ms Fu. Getting an objective, third-party mentor or a sponsor from within the firm may also help, she adds. "A great place to find a mentor is the Young Women's Leadership Connection, which I support. We have a growing list of female mentors across different fields, from legal to the arts to banking, all of whom are selfless in offering their networks and guidance to women mentees."

None of this matters, however, if the women themselves lack the confidence or willingness to step up to begin with. "As women, we tend to be hardest on ourselves. We often reject job offers or new opportunities because we think we'll fail at them or mess up," says Ms Fu. "Don't short-change yourself. You have so much to offer in so many ways. Give yourself a chance to go beyond what you think you can do. Think about how you can create a positive impact on the people around you, and believe in yourself to make this happen." ISCA

BY SINGAPORE ACCOUNTANCY COMMISSION

OUTLOOK FOR THE ACCOUNTANCY SECTOR IN 2020

Transformation, Technology, Capability Development

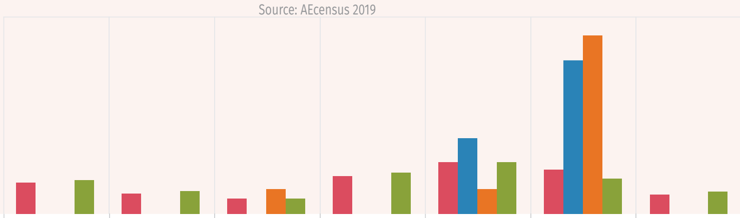
2019 WAS A CHALLENGING YEAR FOR MANY SINGAPORE COMPANIES. The Singapore economy expanded by 0.7% in 2019, according to the Ministry of Trade and Industry Singapore – the slowest in a decade – due to the heightened and ongoing trade tensions between the United States and China. This has dampened growth expectations for many Singapore enterprises across multiple sectors, including accounting entities (AEs). According to the 2019 census conducted by the Singapore Accountancy Commission (SAC), the sector expects to see moderate growth of 5% in revenues for 2020, slightly lower than the growth expectations of 5.7% polled in the previous year.

Despite the slight decrease in growth expectations for 2020, the census showed that more than half of the 200 respondents (52%) indicated that they expect to see positive revenue growth in 2020 (Figure 1). Interestingly, the poll showed that the Big Fours and Large AEs are more optimistic about growth prospects (100% and 89% respectively). In comparison, only about half of the smaller firms, which includes Medium, Small and Micro AEs, expect their revenues to grow (49%). Almost a third of the smaller firms expect to see their revenues decline in 2020 (32%).

On the other hand, the census found that demand for accounting talent

Figure 1 Overall expected annual revenue growth for 2020, by AE size

Source: AEcensus 2019



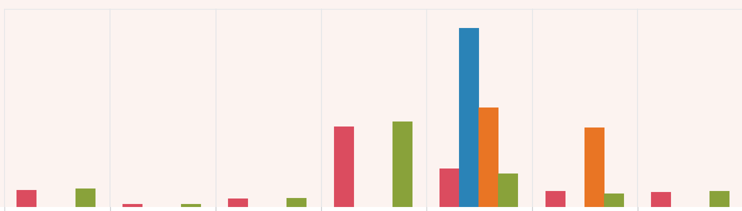
	≤-10%	-10% To -6%	-5% To -1%	0%	1% - 5%	6% - 10%	>10%
Overall	14%	10%	7%	17%	23%	20%	9%
Big 4	0%	0%	0%	0%	33%	67%	0%
Large	0%	0%	11%	0%	11%	78%	0%
MSM	15%	10%	7%	18%	23%	16%	10%

Overall Big 4 Large MSM

PHOTO SHUTTERSTOCK

Figure2 Overall expected manpower growth for 2020, by AE size

Source: AEcensus 2019



	≤-10%	-10% To -6%	-5% To -1%	0%	1% - 5%	6% - 10%	>10%
Overall	10%	2%	5%	45%	22%	9%	9%
Big 4	0%	0%	0%	0%	100%	0%	0%
Large	0%	0%	0%	0%	56%	44%	0%
MSM	10%	2%	5%	48%	19%	8%	9%

Overall Big 4 Large MSM

continues to be strong (Figure 2). Based on the poll, the sector expects to create 566 accounting jobs in 2020, with 39% of the AEs expecting to add to their headcounts in 2020. In comparison, only 17% of the AEs expect a decline in their manpower. All the Big Fours and Large AEs expect to increase their workforce between 1% and 10% in 2020. However, only 36% of the smaller AEs expect to do so as they have difficulties attracting talent partly due to the tightening of the labour market.

GROWTH DRIVEN BY DIVERSIFICATION INTO NON-AUDIT SERVICES

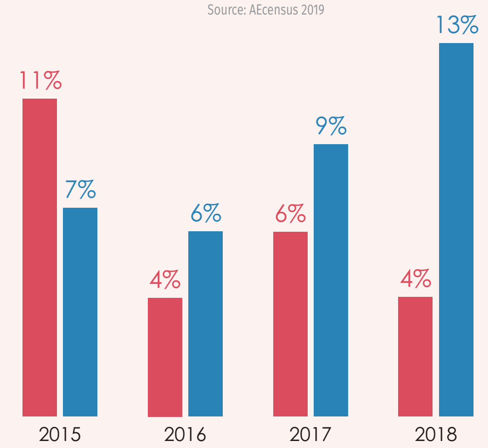
Despite ongoing challenges and trade uncertainty, the census showed that the accountancy sector has been experiencing robust growth ranging between 5% and 9% over the last few years. In 2018, the sector grew 8% with operating receipts estimated to have increased to $2.53 billion. Audit & assurance revenues continued to remain the main source of work for AEs with total revenues from such work growing 4% to $1,213 million in 2018.

The census also revealed increased diversification of work among AEs (Figure 3). While 66% of the AEs indicated that audit & assurance revenues contributed more than 50% of their total revenues in 2014, this proportion dropped to 60% in 2018. A longitudinal analysis on the growth of audit & assurance revenues also showed that growth of audit work has slowed over the years from 11% in 2015 to 4% in 2018. In contrast, growth of non-audit revenues have picked up over the years and increased steadily from 7% in 2015 to 13% in 2018. Growth of non-audit revenues outpaced that of audit by more than three times in 2018.

A deeper analysis found that revenues from advisory services increased 22% in 2018, significantly higher compared to audit & assurance, tax advisory & compliance, and corporate services (4%, 5% and 3% respectively). Of note, IT advisory services increased 70% in 2018. With digitalisation and finance transformation being more cited as the top priority for organisations, many enterprises are seeking external assistance and expertise to increase their value-add through automation.[1] Coupled with the need to enhance risk management practices amid growing concerns on cyber and digital risks, we foresee continuing strong demand for technology-related services.

Figure 3 Growth of audit vs non-audit revenues

Source: AEcensus 2019



STRONG DEMAND FOR TALENT WITH MULTIDISCIPLINARY SKILLS

In recent years, concerns about technology disrupting jobs in the accountancy sector has put the sector in the spotlight. However, fears that automation may replace jobs in the sector appear to be misplaced. On the contrary, the accountancy workforce expanded by over 16%, from 17,419 in 2014 to 20,280 in 2018. Of note, the number of jobs in AEs and their related firms grew by 7% in 2018, the highest year-on-year growth since 2014.

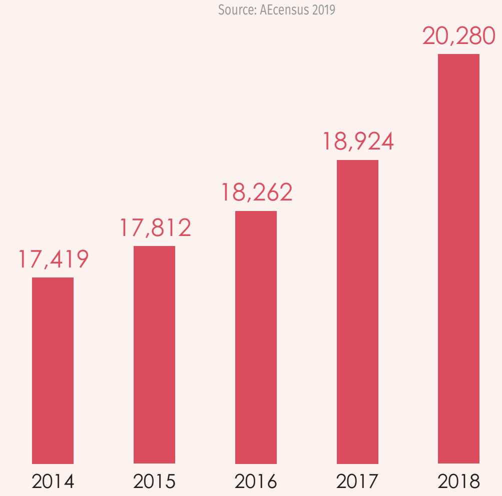
More than 1,300 jobs were created in 2018. This was attributed largely by the Big Fours as their total workforce grew by 1,061 (11%). Hiring also increased across Large, Small and Micro AEs, with the exception of Medium AEs which reported a 4% decrease in their workforce. With a tight Singapore labour market and strong demand for talent from the bigger AEs, smaller AEs reported that they face difficulties in attracting and retaining talent. Another interesting observation is that the Big Fours and Large AEs expanded their audit & assurance teams in 2018 (increased by 299 or 5%) with revenues generated from such services increasing $29 million (3%). However, for the Medium, Small and Micro entities, despite increasing such revenues by $18 million (6%) in total, their total audit & assurance workforce declined 9%.

To address the talent gap, the local universities have ramped up the supply of accounting graduates to ease the supply crunch. SAC is also working on a study, with the Institute of Singapore Chartered Accountants (ISCA) and relevant government agency, to assist AEs improve their human resource capabilities to attract and retain talent.

The census also found that while 48% of the workforce of accounting entities work in audit & assurance services, the growth in the workforce appears to be driven largely by increased hiring for business advisory. In 2018, jobs in business advisory services increased 23%, creating over 800 new jobs.

Figure 4 Estimated size of accountancy workforce (in AEs and related entities)

Source: AEcensus 2019



DIGITALISATION ENABLES PRODUCTIVITY GROWTH IN AUDIT AND CORPORATE SUPPORT SERVICES

With rapid digitalisation, firms that do not digitalise and change their work processes are at risk of becoming obsolete. To assist small and medium-sized accountancy firms adopt technology, SAC, together with ISCA and the Infocomm Media Development Authority (IMDA), have developed the Accountancy Industry Digital Plan (IDP). Firms can look at the Digital Roadmap under the IDP to decide on the type of digital solutions to adopt, and type of employment training to undergo at each stage of their digital development. There is an umbrella of initiatives under the IDP which firms can tap on to digitalise and innovate.

In the last few years, the census found that audit & assurance services tended to generate the lowest revenue per employee, a measure of productivity, compared to other services. However, efforts and investments made by AEs in the last few years to adopt increasing levels of technology appear to have reaped positive returns for AEs. The census found that audit & assurance generated a 5% improvement in revenue per employee in 2018. The revenues generated per employee for corporate support services also saw a 19% improvement. These encouraging results reflect the importance of taking active steps and investing in technology for AEs and accounting professionals to enhance their digital capabilities.

A MULTIDISCIPLINARY PRACTICE WITH STRONG DIGITAL CAPABILITIES

In 2017, the Committee on the Future Economy Working Group on Legal and Accounting Services identified several high-growth practice areas that can help drive demand for Singapore's legal and accounting services. It also encouraged accounting firms to diversify their businesses and provide higher-value services to meet clients' needs. In line with its recommendations, the census found that such work accounted for a significant portion of the sector's growth. It is imperative for AEs to continue their transformations, leverage on technology, and broaden their capabilities to become multidisciplinary firms. ISCA

This article was written by the Singapore Accountancy Commission.

[1] "Market Demand For Professional Business And Advisory Services – Singapore, ASEAN Region And China", 2018, ACCA-SAC

BY DR ANG HAK SENG

NEED FOR CHANGE TO EMBRACE CHANGE

A Different Approach To Corporate Social Responsibility

BUSINESSES SERVE AS THE BACKBONE OF OUR SOCIETY. In fact, about 65% of our working population is employed by small and medium-sized enterprises (SMEs). SMEs, collectively, have the power to positively influence many Singaporeans by inspiring their employees to care for those in need.

Many businesses have demonstrated their corporate social responsibility (CSR) through traditional ways such as donating money to a certain cause or volunteering at various beneficiary organisations. From a business perspective, CSR helps SMEs to build brand equity as customers will see the company as an ethical and caring business.

However, over the years, there has been a shift in the CSR mindset of businesses – CSR is becoming a part of their core business. In a recent corporate giving survey, 64% of corporate givers shared that they have tried to integrate giving into their core business functions[1] (Figure 1).

Figure 1

64% of corporations have tried to integrate giving into their core business functions

Procurement 30%	Marketing & Branding 28%	Staff Development 28%
Sales & Business Development 19%	Recruitment 16%	Product & Service Development 15%

... working is not simply about earning a salary to pay the bills; it is also about purpose, meaning and making a contribution to society. With this changing tide in workers' mindsets, it is crucial for a company to have a strong focus on doing good and making an impact.

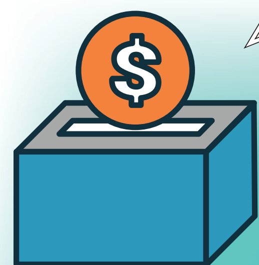


PHOTO SHUTTERSTOCK

Truth is, CSR does not merely build the brand equity of a business – it directly helps to increase profits and reduce cost. Therefore, to benefit from this, I would like to suggest four big changes. First, the *change in customers*; second, the *change in operating model*; third, the *change in bottom line*, and fourth, the *change in CSR strategy*.

1) CHANGE IN CUSTOMERS

Regardless of whether it is the provision of a product or service, businesses are built and sustained by catering to the demands of customers. In the changing business landscape, we see a shift in customer behaviour. Customers no longer view businesses as a place where they can obtain products but they also expect businesses to do good. Just to cite a few key statistics, 88% of Singaporeans think that businesses have a responsibility to do social good, and 56% believe that businesses have a responsibility to ensure their supply chain does not harm the environment.[2]

But what does the change in customers' mindset mean to businesses, exactly? Well, by doing good, businesses will be trusted by their customers. This will lead to more loyal customers who will not only buy more but will also recommend others to buy from that particular business. This is evident from a finding that 51% of Singaporeans indicated that they would more likely recommend a brand that gives a small portion of its annual profits to charity.[3]

One example of how a business has managed to do good and expanded its customer base is Carousell. Carousell is an online marketplace where people can sell and buy new and pre-loved goods. Weaving its CSR strategy into its main business, Carousell not only helps customers buy and sell items, it also champions causes. This is demonstrated through its #AllForFree campaign where sellers were encouraged to give away their items to someone in need.

2) CHANGE IN YOUR OPERATING MODEL

Doing good and integrating the value of care into your business goes beyond improving engagements with customers.

[1] Corporate Giving Survey 2017, National Volunteer and Philanthropy Centre

[2] "56% Of Singaporeans Believe Businesses Have A Responsibility To Prevent Environmental Damage", YouGov SG

[3] Ibid

Ⓐ Dr Ang Hak Seng speaking at a conference on corporate giving, October 2019

It affects the entire operating model in terms of *people*, *process* and *structure* (Figure 2).

People

What is the strongest asset of any business? While some may say it is the intellectual property or the state-of-the-art technology, I would say it is the *people* as they are the ones who run the business and think of bright ideas to improve business. By doing good, people will be inspired to serve and contribute more.

When a company's drive is about social impact, there is more internal energy in the firm. This is because to many employees, and in particular to millennials, working is not simply about earning a salary to pay the bills; it is also about purpose, meaning and making a contribution to society. With this changing tide in workers' mindsets, it is crucial for a company to have a strong focus on doing good and making an impact.

In addition to inspiring employees, integrating the value of care into business also helps to deepen employees' skill sets. By caring for others and helping those in need, employees are able to pick up one very important skill – empathy. Empathy is key to improving service delivery as it helps employees to place themselves in the shoes of the customers and understand their needs, their pains, their challenges and their concerns. By understanding the customers, solutions and products will be tailored to better fit their needs. This will strengthen the company's value position and allow for more business.

For example, in the public service, officers in the senior management are given the opportunity to have short attachments at frontline roles to work on operational issues and interact with service users. This programme is very helpful as it allows the senior management to understand the impact of policies and the needs on the ground. More importantly, it also fosters a deeper sense of empathy that will enable officers to draft better policies.

Process

Next, by focusing on doing good, the business *processes* will improve. To succeed in this dynamic business environment, products and services need to be produced in a cheap, good and fast way. By focusing on doing good, this can be achieved. One take on this is by seeking to strengthen environmental sustainability practices through the reduction of waste. For example, Subaru adopts a zero-landfill manufacturing practice when building its cars. The company also recycles more than 95% of its waste, resulting in both the promotion of environmental sustainability and a sustainable supply chain. This has helped the company reduce costs and boost its bottom line.

In truth, this notion of maximising all materials is nothing new. In fact, most of us do this on a very regular basis without knowing it. Take the example of using reusable shopping bags instead of single-use plastic bags. If we can reduce wastage, recycle products and maximise efficiency in our food usage, this can also be done in business.

Structure

Apart from *people* and *process*, business *structure* is also very important. In particular, the financial structure will also be in a better state if businesses choose to focus on doing good. There is an emerging trend in the ways that capital is raised and this resides in the changing mindsets of the world's richest people. Currently the richest 1% of the world's population owns about half of the world's wealth (45%)[4] and this 1% of the population is increasingly focused on channelling their funds to the social good.

This emerging trend is well summarised by Jack Ma, who said, "When you have one billion dollars, that is not your money. That is the trust that society gives you; they believe that you can manage the money." Increasingly, we also see asset managers investing in companies that have a positive impact on society. For example, in Blackrock's 2020 letter to CEOs, Larry Fink wrote about the importance of sustainable investing, as climate change is a key investment risk. This shift means that doing good is not only about boosting a company's image or brand equity, it helps to open doors to more capital.

In addition, there are new financial instruments that focus on raising funds for projects that promote social good. For example, Green bonds are a way for companies to raise capital for projects that seek to sustain the environment. Another instrument is social impact bonds, which seek to raise capital for certain causes or projects that benefit society.

3) CHANGE IN BOTTOM LINE

Given that businesses are profit-driven, doing good makes sound business sense. Companies with stronger CSR efforts have recorded an increase in revenue of up to 20%[5] as rising numbers of customers are more inclined to purchase from them while encouraging others to do so. Furthermore, by positioning the company as a sustainable one, the company's goods may become more demand-inelastic as they become more niche and unique.

Apart from improving revenues and profits, good CSR practices will lead to a more productive workforce. In general, businesses with strong CSR saw a reduction of staff turnover of up to 50%, increased productivity of up to 13% and increased employee engagements of up to 7.5%.[6] Simply put, when a company does good, it not only benefits the bottom line but also gives purpose and drive to its employees. This will help the business grow even faster and better as motivated staff give rise to better ideas and better solutions.

4) CHANGE CSR STRATEGY TO BECOME CORE STRATEGY

Thus far, I have shared about the importance of doing good due to customers' changing behaviour and how this can also improve your *people*, *process* and *structure*, resulting in a boost to the bottom line. This begs one big question, "How can I make this change?"

For a start, the business' CSR strategy needs to be part of the business' core strategy. Here, I would like to suggest three actions that businesses can consider adopting, to make CSR an integral part of core business (Figure 3).

Invisible to visible

First, make the *invisible become visible* by linking CSR objectives to direct and measurable outcomes. This will allow everyone to easily understand the outcomes of efforts, leading to more transparent tracking and robust communications. For example, a company wishes to focus on environmental sustainability by reducing carbon footprint. However, carbon footprint is hard to measure and it is difficult for employees and customers to see the direct outcomes. So how can this *invisible* impact be made *visible* to everyone? One possible way may be to focus on lowering the utility bills as that makes it easier for everyone to track progress, leading to more transparency.

Integrate with core

Second, CSR efforts can only be part of the core strategy if it is linked with business expertise. Every business is special and has a core expertise. It is thus effective to focus on *what you do best* and use that skill or resource to contribute to society and care for others, creating a more meaningful and impactful CSR strategy.

Partnership

Finally, similar to the second point, a business could *focus on what you do best, and outsource the rest.* Just like no man is an island, partnership is key in developing a strong strategy. Collaboration between government, corporates, charities and the community is crucial to effectively address social needs.

CONCLUSION

Doing good makes good business sense. It helps to deepen engagement with customers, inspires employees, opens doors to capital and boosts the bottom line. Doing good is no longer a "good-to-have" but is increasingly a "must-have" for businesses. Through partnerships and through strategic integration with the company's core expertise, I believe that everyone – from individuals to employees in the private and public sectors and the wider community – can benefit and make Singapore not only a home but also a home that cares. ISCA

Dr Ang Hak Seng is Deputy Secretary (Singapore Cares), Ministry of Culture, Community and Youth; Commissioner of Charities, and Adjunct Professor, Nanyang Technological University.

Figure 2

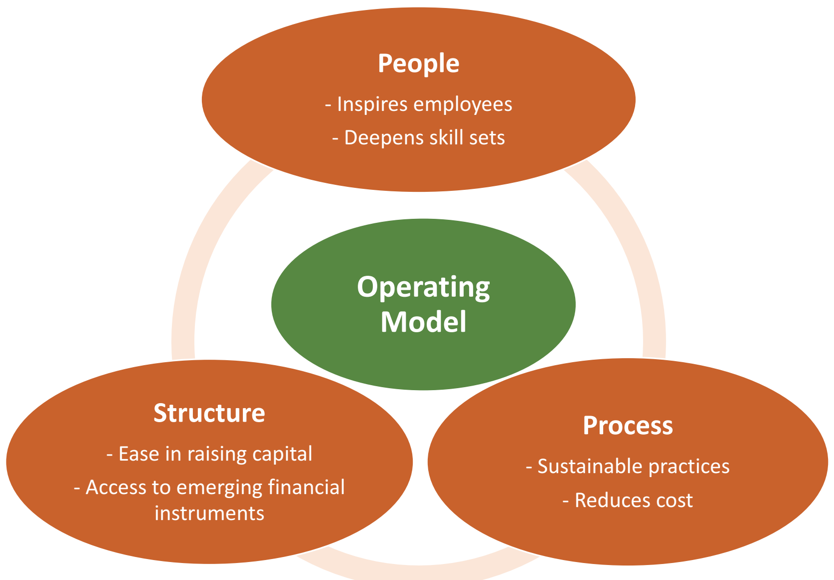
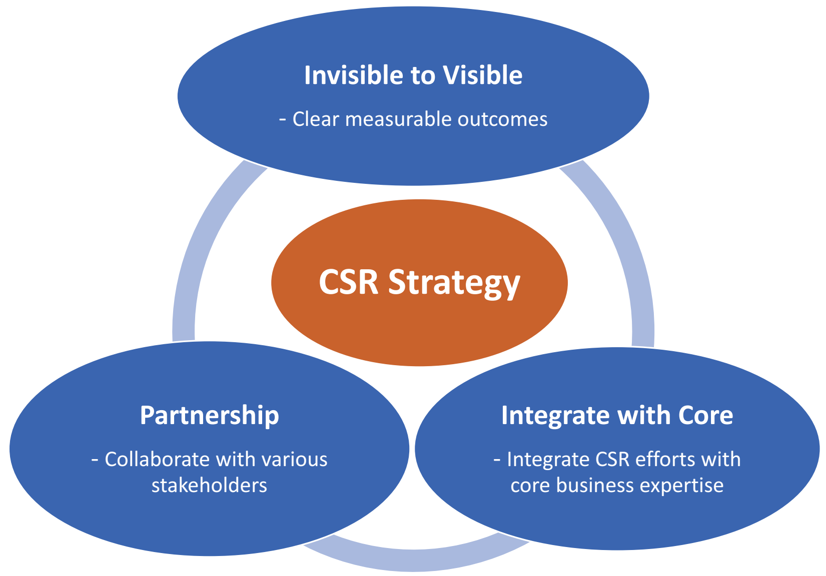


Figure 3



[4] Global inequality, Inequality.org
[5] "Doing Good Is Good Business, But Can You Prove It", Aug 2015, Forbes
[6] Ibid

PHOTO SHUTTERSTOCK

BY KEVIN DANCEY

CLIMATE ACTION IN A CLIMATE EMERGENCY

Accountants Can Be A Powerful Force For Sustainability

CLIMATE CHANGE IS SERIOUS. The threat is immediate. There is no long-term planning horizon. It is one of those big, scary, multifaceted societal problems that will require serious, coordinated vision and leadership to solve. This is not a problem we can wish away or hope that technology will somehow come to the rescue and save us. It won't.

Solving this issue will require a healthy dose of honest, realistic dialogue. Everyone has a role to play, and professional accountants are no exception. We need to understand the extent of this climate emergency and look ahead to what we can and must do, and how to do it. Economic growth and the stability of financial markets depend on it. But despite the inevitable economic stress and strain we will face, adapting to climate change will also usher in an era of great opportunity.

On 28 August 2019, at the end of her two-week transatlantic voyage, Greta Thunberg, the Swedish teenage climate activist, was met in New York Harbor by a flotilla of 17 sailboats. Each represented one of the 17 UN Sustainable Development Goals (SDGs). The following week, leading accountancy professionals will meet at a forum, "Creating Value in a Climate Emergency", hosted by the International Federation of Accountants (IFAC) and the Association of Chartered Certified Accountants (ACCA). Many of the SDGs that greeted Greta are on our agenda, including SDG 13, on Climate Action, and the same crisis inspiring the youth movement has brought us all together.

We have posed several urgent questions for ourselves.

1) What role does the accountancy profession play in accelerating a just and prosperous low-carbon transition?

Professional accountants are becoming a more powerful force for sustainability. This is thanks in part to the shift to responsibly managing and reporting on all of an organisation's resources, including its environmental resources – not just its finances.

IFAC members can influence policy and regulatory action for a transition to a low-carbon society. They can support market-based policy initiatives and incentives, consistent and well-considered regulation, and more useful disclosure. CPA Australia's white paper on Business and the Environment[1] is an admirable example of a member taking action, as is CPA Canada's series of briefs and case studies[2].

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[1] Policy Statement: Business And The Environment (March 2019), CPA Australia

[2] "Resources That Suit Your Needs", Chartered Professional Accountants Canada

Climate change adaptation strategies will create opportunities for businesses, and professional accountants can identify and help businesses capitalise on these opportunities.

As market-based climate action, such as carbon pricing, gains traction with the support of IFAC and its members, the pressure on all organisations to adapt to the climate emergency will grow. The Institute of Chartered Accountants in England and Wales has responded well by creating an online "climate hub" for information on the climate emergency.[3]

The world has to act together. International agreements are an important step. IFAC strongly supported the Paris Agreement. It gives a clear framework for international action. It also sets the tone for investment and innovation in climate action which, to date, has been woefully inadequate.

The right national policies and targets, inspired by international agreements, can help achieve large reductions in greenhouse gas emissions, and they must. Greenhouse gas emissions are increasing, and current national emissions reduction efforts will not keep global warming below the critical two-degree Celsius threshold.

2) How can the accountancy profession better assess and disclose the realities of climate risk?

Built into the Paris Agreement is "a robust transparency and accounting system to provide clarity on action". There is little use in an agreement without assessment, and there can be no assessment without measurement and disclosure. That's where professional accountants come in, at the highest level – developing high-quality information and insights. We're essential to this fight.

Climate risk reporting is also promoted by the recommendations of the Financial Stability Board Task Force on Climate-related Financial Disclosures. Integrated Reporting is also a foundation for better-informed decision-making by investors and lenders. The results of their adoption will be not only more sustainable environmental practices, but also greater long-term value creation.

[3] ICAEW Climate Hub, Institute of Chartered Accountants in England and Wales

Surveys frequently show that climate risk is a top concern for investors, insurers, businesses, and CFOs alike. As this risk grows, accountants are in a good position to drive awareness, measurement, and planning for climate risk. Auditors give confidence to disclosures. Tax professionals can also give clients advice on expected changes in tax law dealing with emissions regulations and help them fulfil evolving tax requirements.

3) How can the accountancy profession lead and support the business model and strategy transformation required to radically re-purpose how companies create and protect value?

IFAC and its members encourage professional accountants to contribute to organisational efforts to integrate climate change risk into strategy, finance, operations, and communications. With their unique perspective on an organisation's strategy and business model, accountants must have a central role in addressing and communicating climate change-related risks. And the flip side of risk is opportunity. Climate change adaptation strategies will create opportunities for businesses, and professional accountants can identify and help businesses capitalise on these opportunities.

International and national policy and regulations are changing the political environment and concrete requirements for business and public sector responses to climate risk. Accountants need to help businesses and governments get ahead of targets, regulation and exposures. For example, emissions reduction targets on certain industries, such as those set by the European Union for car manufacturers, are getting tighter. As another example, directors will need to think about their own liability risk as directors should they choose to ignore their fiduciary responsibilities or fail to adequately disclose the risk of climate change to their businesses. Businesses will need to adapt quickly, and professional accountants can be part of the solution.

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4) In what ways can the accountancy profession improve how it collaborates with others to influence the transition to low-carbon economies?

Governments, non-profits and businesses large and small can't run without professional accountants. This puts the profession in a powerful position to influence all organisations' approach to climate action. And for all organisations seeking to act, effective action will require the trust and expertise that professional accountants bring to the table.

Many climate-focused public and private organisations should welcome input from and partnership with professional accountancy organisations (PAOs) as allies and valuable sources of information and influence. PAOs can cultivate working relationships with governments, businesses, business associations and others to spur them to support climate action. They also have an important role in keeping accountants informed of how they can support efforts to manage emissions and adapt to climate change.

A UNIQUE POSITION AND A UNIQUE MANDATE

The climate emergency is a monumental challenge to social, economic and financial market stability. As instrumental members of nearly every business, government, and non-governmental organisation, professional accountants are in a unique position to make a difference. As the professionals charged with managing the flow of essential information and insight, we also have a mandate unlike any other: to act in the interest of the public and investors to ensure that all entities are equipped to pursue sustainable, long-term value creation.

IFAC, with its member organisations, will continue to advocate for the transition to low-carbon economies.

Soon after IFAC's climate forum, the UN General Assembly will meet just a few blocks away. The climate emergency will be paramount on its agenda. Business as usual is not an option. We have much work to do as a society and professional accountants are part of the solution.

Let's get to work preparing a better future. ISCA

Kevin Dancey is Chief Executive Officer, IFAC. This article was first published in "Knowledge Gateway".

BY MARK HOLTON

DEVELOPING YOUR BUSINESS ADVISORY SERVICES PART 2

A Step-by-step Guide

IN THE FIRST OF THIS TWO-PART ARTICLE, published in the February issue of ***IS Chartered Accountant Journal***, we highlighted the opportunities in business advisory for small and medium-sized accountancy practices (SMPs). Such services can bring about a new revenue stream and already, some SMPs have made a tentative start in that direction.

We had introduced a framework that provides a step-by-step guide for SMPs that want to evolve from being a compliance-focused firm to one that gains a substantial percentage of income from advisory work. Step 1 of the Enabler™ process was discussed in the earlier piece. In this article, we continue the discussion with Steps 2 to 7 to help firms achieve success in their implementation.

GUIDE TO IMPLEMENTATION

Step 2: Unlock your client's needs

You can't service your clients effectively unless you know what they need and want. Business advisory is not a one-size-fits-all proposition. But for many accountants entrenched in compliance work, the process of finding out what a client's needs are can be intimidating, especially when you are conducting your first few needs analysis meetings.

As with many other things, confidence comes from practice and repetition. One technique we use with our clients is to conduct "mock needs" reviews. In some sessions, the client manager takes the role of the client and others interview him/her; in others, the client manager gets the chance to rehearse his/her own role in the needs review meeting, while someone else plays the client.

Issues to be covered in needs review meetings may include, among many other points, business strengths and weaknesses, future goals, competitive issues, risk management, succession planning, funding management and lifestyle issues.

Once you've elicited your client's needs, you'll be able to submit a personalised and customised proposal to your client inviting them to commence the business advisory process.

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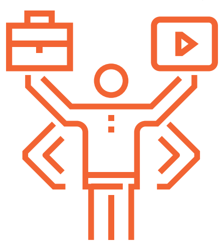

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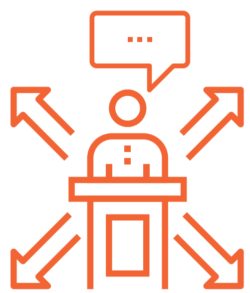
Step 3: Create a disturbance in your client's mind

Being able to quickly demonstrate the value and validity of your advisory services to your clients is critical to success. So, how will you do that?

In many instances, providing a business value indication of your client's business is an effective tool to help you initiate an engagement. Why? Because many SME owners want to know how much their businesses are worth, and often, those business value indications turn out to be below their expectations. The gap between expectation and reality creates an incentive for them to implement the changes necessary for them to increase their business value and, consequently, they become more likely to pay for your business advice.

... if you want your advisory practice to flourish, you'll need to develop a mindset in which you constantly look for opportunities, market them effectively and proactively sell them to your clients.



Alternatively, if your client is looking for or expecting to need finance for their business soon, conducting a lending pre-assessment can help them understand whether they're likely to be able to access funding from lenders. Again, if their expectations aren't aligned with the likely outcome of their loan application, you may have your foot in the door as you can offer to help them reach their goals. Using scenario-planning software that allows you to address the key lending covenants (EBITDA, interest cover, debt service cover, liquidity, gearing and capital adequacy) can help you work with your clients to overcome their funding gaps.

Other types of disturbances may include discussing their financial preparedness for retirement or the expenses of their kids' education.

Step 4: Analyse your client's financial performance

The previous step of the Enabler™ process was a historical review, that is, what has happened in the business so far. Next, you need to add value to your client by looking into the future for them.

You're asking your client, "Now that we're working together, what levers do we need to pull and how hard, in order to reach your goals?"

Scenario-planning software that allows you to develop what-if scenarios and the power of one projection is ideal for this purpose. It enables you to show your clients the financial impact of various business decisions before they make them, gives you the tools to analyse their strengths and determine how to make them stronger, and finds any weaknesses and implements fast fixes so they turn into strengths too.

Effective utilisation of scenario-planning software really can establish you as a true expert in your clients' eyes. Just showing them the effects that small changes can make to their profitability and cash flow can quickly have them viewing you as a genius. Scenario-planning software also helps you to easily develop plans, budgets and KPIs for your clients to work towards.

Step 5: Ensure your client implements action

Like it or not, you're competing for business advisory work with coaches and other advisors who often have less financial expertise than you and are often not as qualified to successfully influence your clients' financial future. What they do have on their side are tried-and-tested systems and strategies for holding clients accountable and getting them to stick to their goals.

As a business advisor, you need to adopt some of those strategies, continually bringing your clients' attention back to their wants and needs, the gap between where they are now and where they want to be, and their strategy for bridging that gap.

It's up to you to be a financial and business coach to keep track of how your clients are progressing. Send regular email reminders, call them by phone or get your client service manager to call the clients for updates. Regular enthusiastic contacts help your clients to keep moving. This is often the hardest part of making changes for them, so help them be accountable.

You'll also need to be both patient and consistent. Despite your convictions, it's not uncommon for clients to take six to 12 months or more to come around to implementing all your suggestions.

Step 6: Service additional client needs

Budgets and cash flow targets should evolve as month-by-month action plans as a result of the financial analysis you performed for your client in Step 4 of this process and, in many cases, these disciplines alone will revolutionise the profitability of small businesses.

However, as your relationship with your client develops, so too will their trust in you, your understanding of their business, and the amount of influence you have on its performance.

Over time, you'll find opportunities to help your advisory clients with more and more of their business needs, above and beyond pure finance. HR, IT, succession issues, estate planning – the opportunities are endless, but only if you're alert to them.

Once again, that means having a system in place for making sure you're aware of what's going on in your client's business, for example, by revisiting their needs reviews and gap analyses on a regular six or 12 monthly cycle.

To maximise the potential of these engagement opportunities for your firm, you'll also need to have planned for these scenarios in advance and have taken the time to develop either inhouse expertise or a strong referral network.

Step 7: Generate new business opportunities

As an accountant, sales and marketing is probably not your first love. But if you want your advisory practice to flourish, you'll need to develop a mindset in which you constantly look for opportunities, market them effectively and proactively sell them to your clients.

The place to start is with your existing client base. As mentioned earlier, once your firm is ready to start offering advisory services, it's a matter of deciding which clients are most suitable for advisory engagements, identifying their needs, working with them to get things happening, and then expanding your offer to them in your regular three- or six-month review meetings. ISCA

Mark Holton is Director, Smithink Advisory Pty Ltd.

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BY ANNE-MARIE VITALE

RE-IMAGINING THE FUTURE ACCOUNTANT

A Call To Action To All PAOs, Organisations And Individuals

TRANSFORMATIONAL CHANGES ARE RE-SHAPING THE ROLES ACCOUNTANTS PERFORM WITHIN SOCIETY. According to "The Future of Jobs Report 2018" by the World Economic Forum, by 2022, 75 million jobs may be displaced by a shift in the division of labour between humans and machines. Of note, the report names a cluster of job profiles set to become increasingly redundant, including accountants and auditors. It also indicates that 133 million jobs may emerge by 2022, pointing to a growing rather than shrinking world economy.

What does this mean for us as we re-imagine the role of the future accountant?

As automation and technology continue to drive changing business models, the role of accountants and auditors will need to rapidly evolve and adapt. As the profession looks to the future, we must anticipate:

- Areas of demand for our skills;
- Behaviours and competencies needed to be successful in the future business ecosystem, and
- Changing expectations about what it means to be an accountant.

According to the Report, there is accelerating demand for data analysts and scientists, big data specialists, digital transformation specialists, and information technology services. Accountants have the behaviours and competencies that overlap with these future in-demand roles.

Today's rapidly evolving landscape requires agility. The International Federation of Accountants (IFAC) has implemented an approach to advancing accountancy education at the global level. The International Panel on Accountancy Education (the Panel) is a key feature of this approach and instrumental in advising IFAC on how to assist professional accountancy organisations (PAOs) to re-imagine the future accountant and prepare future-ready accountants.

The Panel proposed a vision of PAOs "contributing actively to the development of a future-ready profession – relevant, reputable, valued, sustainable – that is attractive to a diversity of existing and new talent and meets the needs of organisations (in the public and private sectors) and society".

To ensure accountancy education can meet the challenge of competency and skills-based changes, we need to understand where the profession is heading.

MAKING EVOLUTIONARY AND REVOLUTIONARY CHANGE HAPPEN

Each of us in the global profession has an important role to play to effect change.

IFAC's role: harness its comparative advantage to facilitate this evolution and, ultimately, revolution

- **Speaking out.** This is about embracing and taking advantage of disruption. It requires stimulating dialogue about the profession's Total Addressable Market (TAM), which is a way to view the profession as measured by jobs held by accountants and auditors. Predictions from the Report show that the profession's TAM will decrease, assuming no action is taken by the profession. IFAC is advancing global dialogue by asking questions such as: In what ways can we grow our TAM? What actions can we take today to increase our TAM for tomorrow? The actions we take today will benefit the capital markets' ecosystem.

- **Preparing a future-ready profession.** IFAC is helping PAOs and other stakeholders prepare future-ready accountants by promoting and enabling knowledge-sharing, capacity-building, and thought leadership.
- **Supporting the adoption and implementation of high-quality international standards.** The International Education Standards (IES) set forth learning outcomes that support the competency of accountants during their initial professional development. A newly developed e-tool can facilitate access to IES and implementation support material.

PAOs' role: start the dialogue and modernise the behaviours and competencies of accountants

PAOs should consider whether their business models are fit-for-purpose and whether their organisational strategies are built for a future where accountants do different things. We can all relate to:

- **Accountants doing the same things,** such as gathering, extracting, and manipulating data and information, reconciling information across separate systems, and making decisions based on samples or limited information. These skills are normally obtained through classroom-based, prescribed learning – a one-size-fits-all approach to learning.
- **Accountants doing the same things differently,** such as evolving skill sets using automation, visualisation for more powerful insights, and leveraging communication technologies to make a greater impact – all tend to rely on increased self-learning and personal exploration.
- **Accountants doing different things,** however, will be defined by the actions we take today. PAOs can facilitate this future in several ways. Consider these four critical steps:

1) ***Mobilising stakeholders and engaging experts.*** Start early, facilitate dialogue among your stakeholders and experts. Learn from other PAOs. Develop a vision and strategy for the profession in your jurisdiction.
2) ***Implementing the new IES.*** The IES were revised with a lens on professional scepticism and information and communications technologies (ICT). To support their implementation, non-authoritative learning outcomes for ICT were also developed.
3) ***Facilitating reskilling and upskilling.*** Focus on relevant competencies, including business acumen, behavioural competence, digital acumen, data integration, synthesis and analysis, and communication.
4) ***Preparing your PAO to thrive in a digital era.*** Challenge yourself on the time to market for changes to your curricula and assessment innovations. Take advantage of EdTech. Meet personalised needs of your members based on competencies and not roles.

Organisations' role: develop effective and efficient finance functions

Accountants are deeply engrained in, and increasingly vital, to the success of organisations. Finance functions should identify the enablers of change and associated development plans to ensure they are fit-for-purpose to support and partner within the business, public sector, or other entities. They should have the right mix of talent, skills, and technology to enhance effectiveness and efficiency.

To help facilitate finance function transformation, IFAC has developed an evaluation tool for Boards and management to identify strengths and areas of improvement for their finance function.

Individuals' role: focus on personal growth, hone existing technical skill sets, and develop skills that are increasingly important

At the heart of future readiness is the individual. There is an unquestionable need for each of us to take personal responsibility for our own lifelong learning and career development – taking learning from being a passive, compliance-based approach to one which is tailored, reflective, and actively driven by our own individual needs. IES 7 *Continuing Professional Development* (CPD) includes several innovations that can support individuals in planning effective CPD in a changing workplace.

Changing business models and evolving business needs are creating new opportunities for those accountants who are ready to learn. What are important competencies for the individual?

- **Business acumen.** Today, strategic business decisions are increasingly based on how individuals can integrate appropriately analysed large data using their professional judgement. Business models are rapidly changing, impacting how vendors, employees, and customers interact, and how business is conducted and measured.
- **Behavioural competence.** This includes how individuals can use intellectual curiosity, critical thinking, adaptability, and lifelong learning to effectively respond to an environment of rapid technological change while also demonstrating the intellectual agility to embrace new or alternative ways of working and adapting to changing circumstances quickly. Behavioural competence also includes the ethical use and dissemination of data.
- **Digital acumen.** Accountants should understand how new and emerging technologies impact what they do, or what they likely need to do, in an evolving or revolutionising landscape – how such technologies operate, are used, and affect the generation, processing and flow of data and information. Data governance and security are also key elements of digital acumen.
- **Data interrogation, synthesis, and analysis.** The competencies needed by individuals to effectively work with structured and unstructured data, for example, evaluating whether data is complete, accurate and relevant, and understanding exceptions to expectations. These competencies also include conducting risk assessments, predictive analysis and effective use of visualisation tools.
- **Communication.** New and emerging technologies have changed the channels of communication from and across systems, for example, using social media and smart devices.

We each have a responsibility to acknowledge, embrace, and seek out the uncertainty surrounding our profession. This is our *call to action* to all PAOs, organisations, and individuals. ISCA

At the heart of future readiness is the individual. There is an unquestionable need for each of us to take personal responsibility for our own lifelong learning and career development – taking learning from being a passive, compliance-based approach to one which is tailored, reflective, and actively driven by our own individual needs.

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Anne-Marie Vitale is Chair, International Panel on Accountancy Education, International Federation of Accountants (IFAC). This article was first published in "Knowledge Gateway", IFAC.

TECHNICAL HIGHLIGHTS

AUDITING AND ASSURANCE

SGX REGCO EXTENDS REPORTING DEADLINE FOR ISSUERS AFFECTED BY 2019-NCOV SITUATION

SGX RegCo will grant a time extension of up to two months (that is, till 30 June 2020) to issuers with significant operations in China holding annual general meetings to approve their 31 December 2019 financial results, subject to conditions. Issuers are still required to release their unaudited financial statements by 29 February 2020.

For more information, please visit https://www2.sgx.com/media-centre/20200207-sgx-regco-gives-issuers-30-june-2020-hold-agms-approve-fy-dec-2019-results

ETHICS

FINANCIAL INSTITUTIONS THAT ARE NOT PUBLIC INTEREST ENTITIES UNDER ISCA EP 100 AND ACRA CODE

ISCA issued a communique to inform that certain financial institutions (FIs) are not public interest entities (PIEs) for the purpose of ISCA EP 100.

ACRA has also issued Practice Direction No. 1 of 2020 to clarify the scope of FIs which are not PIEs for the purpose of the ACRA Code.

For more information, please visit https://isca.org.sg/ethics/ethics-headlines/ethics-headlines/2020/january/financial-institutions-that-are-not-public-interest-entities-under-isca-ep-100-and-acra-code/

IESBA ALIGNS PART 4B TO ASSURANCE TERMS AND CONCEPTS USED IN ISAE 3000 (REVISED)

The International Ethics Standards Board for Accountants (IESBA) released in January 2020, Revisions to Part 4B of the Code to Reflect Terms and Concepts Used in ISAE 3000 (Revised). Part 4B of IESBA's Code comprises the independence standards for assurance engagements other than audit and review engagements.

For more information, please visit https://www.ethicsboard.org/news-events/2020-01/iesba-revises-part-4b-international-code-ethics?utm_medium=email&utm_source=transactional&utm_campaign=GKG_Latest

FINANCIAL REPORTING

IASB CLARIFIES REQUIREMENTS FOR CLASSIFYING LIABILITIES AS CURRENT OR NON-CURRENT

The amendments clarify, but do not change, existing IAS 1 requirements. But they could result in entities reclassifying

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some liabilities from current to non-current, and vice versa; this could affect an entity's loan covenants. The amendments are effective 1 January 2022 to give entities time to prepare for them.

For more information, please visit https://www.ifrs.org/news-and-events/2020/01/iasb-clarifies-requirements-for-classifying-debt-as-current-or-non-current/

HELP SHAPE IFRS STANDARDS IN 2020

In 2020, IASB plans to publish a number of consultation documents, including a discussion paper on Goodwill and Impairment, and an exposure draft on IBOR Reform and its Effects on Financial Reporting (Phase 2). Stakeholders are encouraged to provide their views on these consultations.

For more information, please visit https://www.ifrs.org/news-and-events/2020/01/help-shape-ifrs-standards/

REGULATORY

MAS AND ACRA LAUNCH VARIABLE CAPITAL COMPANIES FRAMEWORK

The Variable Capital Companies is a new corporate structure that can be used for a wide range of investment funds and provides fund managers greater operational flexibility and cost savings.

For more information, please visit https://www.mas.gov.sg/news/media-releases/2020/mas-and-acra-launch-variable-capital-companies-framework


BY LIM JU MAY AND DONAPHAN BOEY

GETTING THE MEASURE OF CRYPTOASSETS

ISCA Issues Financial Reporting Guidance 2

ASK ANYONE ABOUT THE ACCOUNTING FOR HOLDINGS OF CRYPTOCURRENCIES and one may intuitively expect it to be similar to the accounting for holding cash. However, the IFRS Interpretations Committee (IFRIC) concluded otherwise in its agenda decision on the holdings of cryptocurrencies in June 2019, as "cryptocurrencies do not currently have the characteristics of cash". This is just one of the many facets of how accounting for cryptoassets – a digital asset class that includes assets recorded on a blockchain such as cryptocurrencies – is complex and could require significant judgement.

In order to address the uncertainty potentially faced by the Singapore accounting profession in the accounting for cryptocurrencies and other types of cryptoassets, ISCA, through its Financial Reporting Committee (FRC) and FRC Core Sub-Committee, issued Financial Reporting Guidance 2 (FRG 2) "Accounting for Cryptoassets: From a Holder's Perspective" on 5 March 2020. Guidance on accounting for cryptoassets from the issuer's perspective will be the subject of a separate FRG expected to be issued at a later date.

BACKGROUND OF FRG 2

Knowing the developments leading up to this point could be helpful to understand the purpose of FRG 2. When cryptocurrencies were first created in 2009, it was envisioned that they would provide potential benefits that enable them to be used as an alternative payment method or for financing. Since then, trading volume for the more reputable cryptocurrencies has increased significantly in recent years, even as viable solutions for their inherent limitations continue to be sought so they can be used as a transaction currency. At the same time, the continued evolution in cryptocurrencies has resulted in the development of digital tokens that provide functions other than payment and given rise to cryptoassets as a new digital asset class.

As cryptoassets grow more complex, entities that transact in cryptoassets will need to ensure that the related accounting and disclosures in the financial statements are appropriate and adequate to meet the informational needs of stakeholders. However, a potential roadblock is that cryptoassets are not explicitly within the scope of any IFRS Standard. In addition, the International Accounting Standards Board decided "to monitor the development of cryptoassets" and "not to add to its work plan a project on holdings of cryptocurrencies or initial coin offerings"[1] due to the lack of prevalence of such transactions for entities that report using IFRS Standards. Nevertheless, in June 2019, some clarity on this matter was provided in the aforementioned agenda decision by IFRIC on the holdings of cryptocurrencies, a subset of cryptoassets.

ISCA's FRC deliberates over issues which are likely to result in divergent or unacceptable treatment, are pervasive or relate to complex accounting areas. FRGs are issued under the ISCA Financial Reporting Codification Framework to help in the application of accounting standards by explaining how the principles and requirements in the accounting standards apply to these issues. Hence, FRG 2 was issued to guide preparers who report under the Singapore Financial Reporting Standards (International) (SFRS(I)s), International Financial Reporting Standards (IFRSs) or Financial Reporting Standards (FRSs) issued by the Accounting Standards Council, on the accounting for holdings of cryptoassets.

FRG 2 "ACCOUNTING FOR CRYPTOASSETS: FROM A HOLDER'S PERSPECTIVE"

The following are some key highlights of FRG 2.

FRG 2 gives an overview of cryptoassets in the following areas:

- What is a cryptoasset?
- What are the different types of cryptoassets?
- What are the relevant guidelines and regulations on cryptoassets in Singapore?

[1] IASB Update November 2018

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Table 1 A possible decision process to apply the most relevant FRS in accounting for a particular cryptoasset

	Cryptocurrencies	Utility tokens	Asset tokens	Security tokens
FRS relevant to underlying asset	Not applicable	Not applicable	If the asset token represents control over the underlying asset	Not applicable
FRS 32 *Financial Instruments: Presentation* and FRS 109 *Financial Instruments*		If it represents a contract to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments	The relevant FRS depends on the underlying asset, and not the asset token	If it meets the definition of a financial asset in FRS 32
FRS 2 *Inventories*	If the entity holds it for sale in the ordinary course of business or if the entity is a broker-trader of cryptocurrencies	If the entity holds it for sale in the ordinary course of business or if the entity is a broker-trader of cryptocurrencies		Not applicable
FRS 38 *Intangible Assets*	If it meets the definition and recognition criteria of an intangible asset and FRS 2 is not applicable	If it meets the definition and recognition criteria of an intangible asset and FRS 2 and FRS 109 are not applicable		
FRS 116 *Leases*	Not applicable	If it represents a right to use an underlying asset for the lease term		
Prepayment		If it represents payment made in advance of the entity obtaining a right to access goods or receiving services		
FRS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* paragraphs 10 to 12 are applied to develop an accounting policy that results in relevant and reliable information if no FRS specifically applies				

In addressing the accounting for cryptoassets by the holder, FRG 2 provides guidance, together with illustrative examples. Table 1 sets out a possible decision process to apply the most relevant FRS in accounting for a particular cryptoasset.

FRG 2 highlights that there may be cryptoassets which have terms and conditions and/or other characteristics that may not fit the general definition of any type of cryptoasset. The accounting for holding cryptoassets depends on the facts and circumstances of each individual case and may require the use of judgement with emphasis placed on the substance of the transaction over its form. Auditors or professional advisors should be consulted if necessary.

CLOSING REMARKS

Perhaps the emergence of cryptoassets is just one instance of how technological disruptions, along with other global developments, provide new challenges in classification and measurement and are extremely relevant to the accountant. Beyond just quantification in financial reporting, it is also emblematic of the constant need for accountants to understand and adapt to these developments. For example, blockchain, which was invented to enable cryptocurrency transactions, is now being evaluated by enterprises and governments alike for other significant applications, such as automated contracting, and is at the forefront of digital transformation. In adapting to these developments, the accountant positions himself to contribute his knowledge, judgement and insight, and rises up the value chain in the organisation.

ISCA will continue to support the development needs of members, such as by guiding members in meeting financial reporting challenges via the FRC. ISCA

Lim Ju May is Deputy Director, Technical, ISCA, and Donaphan Boey is Manager, Financial & Corporate Reporting, Technical, ISCA.

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BY FELIX WONG AND ANGELINA TAN

BE COOL AND CLEAR ON THE CPF ACT

Key Considerations On CPF Contributions

THE CENTRAL PROVIDENT FUND (CPF) BOARD has stepped up enforcement inspections on employers in recent years. Nearly S$2.7 billion in CPF arrears were recovered from employers within a five-year period from 2014 to 2018, whether through desktop audits, on-site audits or simply acting on complaints by employees.

At a recent *Tax Excellence Decoded* session by the Singapore Institute of Accredited Tax Professionals (SIATP), Accredited Tax Advisor (Income Tax) Kerrie Chang, Partner, People Advisory Services – Mobility, Ernst & Young Solutions; Sandesh Kumar, Director, and Sharon Chiam, Associate Director, People Advisory Services – Mobility, EY Corporate Advisors, provided a timely reminder to businesses and highlighted the essentials in complying with CPF obligations in Singapore.



(From left) Accredited Tax Advisor (Income Tax) Kerrie Chang, Partner, People Advisory Services – Mobility, Ernst & Young Solutions; Sandesh Kumar, Director, and Sharon Chiam, Associate Director, both from People Advisory Services – Mobility, EY Corporate Advisors, navigated participants through the complexity of the CPF Act

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COMMON CPF MISTAKES OF EMPLOYERS

Errors in CPF contributions can be costly for employers. Unlike the Comptroller of Income Tax who can only raise additional assessment subject to the statutory time limit under the Income Tax Act, the CPF Board is not restricted by any statute of limitation in carrying out its recovery action.

Defaulting employers are subject to a late payment interest calculated daily at a rate of 1.5% per month (starting from the first day of the following month after the contributions are due), in addition to arrears of CPF contribution.

Some of the most common CPF mistakes by employers are highlighted below.

Misclassification of Wages

Misclassification of wages as Ordinary Wages (OW) instead of Additional Wages (AW) contributes to one of the highest amounts recovered through self-rectification by the CPF Board. Essentially, the different wage ceilings of OW and AW affect the amount of CPF contributions payable, and where wrongly classified, could result in an underpayment of CPF contributions.

Under the CPF Act, OW are defined as wages due or granted wholly and exclusively in respect of an employee's employment in that month, and wages payable before the due date for payment of CPF contributions for that month. Any other wages that do not fall into the definition of OW are AW (that is, wages that are not granted wholly and exclusively for the month, or wages made at intervals of more than a month).

The most commonly misclassified remuneration items are overtime payments, sales commission and back payments.

Non-payment of CPF Contributions on Reimbursements

Another common misconception is that reimbursements to employees do not attract CPF contributions.

Employers should note that where the cash payments increase the employee's wages, CPF contributions would be payable regardless of payment modes (that is, whether outright cash payments or via reimbursements). For example, if the company gives out red packets (in cash) to its employees during Chinese New Year, CPF contributions would be payable on such cash payments.

On the other hand, cash payments that are not wages, such as retrenchment benefits and genuine reimbursements (that is, monetary payments to employees for actual expenses incurred on behalf of the employer and capped at the expenditure incurred), do not attract CPF contributions. Examples of genuine reimbursements include taxi claims incurred for business purposes and meal expenses incurred for overtime work. Besides cash payments that are not wages, benefits-in-kind that do not include cash payments (such as employee share-settled incentive plans) also do not attract CPF contributions.

> With late interest payment charged at 18% per annum and in the absence of any statute of limitation, it is critical for employers to get their CPF obligations right as early as possible to avoid a potential time bomb.

Recent updates on CPF treatment of reimbursements of employee benefits

Since 1 January 2020, the exemption to pay CPF contributions on the reimbursements of medical and dental treatment has been expanded to include overseas treatment, so long as the doctors, dentists and Traditional Chinese Medicine (TCM) practitioners are registered in the location of practice.

In addition, reimbursements for dental treatment for an employee's spouse and child would no longer attract CPF contributions, while reimbursements to an employee for holiday-related expenses would attract CPF, regardless of whether such reimbursement is attributable to the employee or his/her immediate family member.

Application of the Incorrect CPF Contribution Rates

In practice, incorrect CPF contribution rates are often used when employers assume that employee information remains the same in the new filing period. For example, employers may overlook an employee's date of birth and not realise that he has moved into a different age bracket (with a different CPF contribution rate). Employers may also neglect the CPF obligation of foreign employees who may have since obtained the Singapore Permanent Resident (SPR) status.

To minimise the risk of applying the wrong CPF contribution rates, employers should relook at their system such that the CPF contribution rates could be automatically updated as certain events are triggered (such as when an employee moves to the next age group for CPF purposes). Employers should also check with their foreign employees regularly to ensure that any changes to their citizenship status are promptly updated.

Non-payment of CPF Contributions for Individuals Wrongly Classified as Independent Contractor

CPF contributions are only applicable if an individual is providing services under a contract of service. Therefore, ascertaining whether an individual is providing services under a contract of service or a contract for service is crucial.

Essentially, a contract of service establishes an employer-employee relationship between the two parties (including the terms of employment) where the employee does business for the employer. A contract of service may be covered by the Employment Act.

In contrast, a contract for service is an arrangement where a person is engaged as an independent contractor (such as a self-employed person engaged for a fee to carry out an assignment for the company). The independent contractor carries out business on his own account and is not covered by the Employment Act. Statutory benefits (such as leave benefits) do not apply to the independent contractor.

PP v Jurong Country Club [2019]

The importance of ensuring the right classification is highlighted in *PP v Jurong Country Club* [2019], where the High Court rejected a bid by the CPF Board to recover more than S$400,000 in alleged arrears of CPF contributions for a gym instructor who had worked at Jurong Country Club (the Club). The Club was also cleared of criminal charges of non-payment of CPF obligations.

The High Court's decision hinged on its conclusion that the gym instructor was an independent contractor, and not an employee of the Club. It was opined that in determining whether a person is an employee for the purposes of the CPF Act, due regard should be made for the parties' intention and the totality of the parties' working relationship. A multi-factorial approach should be adopted with a holistic assessment and due regard for all relevant factors.

In arriving at its decision, the High Court placed emphasis on the contracts entered into by the parties, which explicitly referred to the gym instructor as an independent contractor and stated that it was a contract for service. The contracts further stated that nothing in the terms should be construed as creating an employer-employee relationship.

Several factors were identified as suggestive of the gym instructor being an independent contractor. For example, the gym instructor was allowed to conduct programmes for the public at the Club's facilities outside of the stipulated work hours (in contrast to the general position that employees were not allowed

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to engage in personal work at the Club's premises without permission from the management). Unlike other employees who could access all areas of the Club's premises, he was only given access to the gym. The gym instructor was also not part of the Club's headcount and was not invited to staff events such as its Dinner and Dance. He was not required to sign personal data protection forms unlike other employees. The High Court opined that these differences were deliberate and demonstrated the parties' express intention for the gym instructor to be treated as an independent contractor.

The High Court's extensive analysis demonstrates that the factors to be considered in determining whether an individual is an employee or independent contract are not exhaustive. For a company to prove that its intention is to hire an independent contractor (and not an employee), such intention should be clearly and unambiguously articulated in the contract and carried out in a manner that is aligned with the factors indicating an independent contract relationship.

Non-alignment of CPF and Income Tax Treatment

It is important to note that CPF and income tax treatment do not necessarily align with each other.

Frequent business travellers

Employment income earned by employees who are based outside Singapore but travel into Singapore for business purposes are not CPF payable. On the other hand, from an income tax perspective, employment income attributable to services rendered in Singapore is taxable but exemption may be available either under the domestic tax law or under the Avoidance of Double Tax Agreement between Singapore and the individual's country of residence.

Bonus payments to cross-border employees

CPF contributions on bonus payments to cross-border employees are dependent on the employee's physical location. For example, bonuses (relating to an employee's Singapore employment) that are paid when the employee is posted overseas are not CPF payable, while bonuses (relating to the employee's overseas employment) that are paid when the employee is in Singapore are CPF payable.

From an income tax perspective, income earned in respect of the employee's Singapore employment would be subject to tax in Singapore, regardless of whether it is paid when the employee is in Singapore or outside Singapore.

In view of the discrepancies between CPF and income tax treatment, it would be good for employers who may have assumed their alignment to review their CPF obligations.

In light of the active enforcement inspections by the CPF Board, employers should perhaps consider performing a CPF compliance review if they have not done so recently. With late interest payment charged at 18% per annum and in the absence of any statute of limitation, it is critical for employers to get their CPF obligations right as early as possible to avoid a potential time bomb. ISCA

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BY LEE KIN WAI

DON'S COLUMN

INTEREST RATE RISK MANAGEMENT WITH FINANCIAL DERIVATIVES

Reduce Debt Financing Costs, Promote Capital Expenditures

THE USAGE OF FINANCIAL DERIVATIVES HAS INCREASED SUBSTANTIALLY IN RECENT YEARS. According to Bank of International Settlement's 2019 survey, the average daily turnover of over-the-counter (OTC) interest rate derivatives has risen significantly from $2.7 trillion per day in 2016 to about $6.5 trillion in April 2019. This rise appears to have been driven mainly by increased hedging and positioning amid shifting prospects for growth and monetary policy.

In general, interest rate risk affects the variability of a firm's profit and cash flow from the effect of changes in interest rates on a firm's assets or liabilities. Many large non-financial firms use interest rate derivatives (such as interest rate swaps and forward rate agreements) to manage their interest rate risk, especially exposures arising from their debt obligations. This paper examines the usage of financial derivatives by listed firms in Asia as a corporate risk management strategy to mitigate their interest rate risk. First, we examine the firm-level characteristics that affect the intensity of derivatives usage (that is, what are key drivers that lead firms to use more financial derivatives to hedge their interest rate risk?). Second, we examine whether derivatives usage and hedging affect firm valuation. Third, we examine the channels in which derivatives affect cost of financing and capital expenditure spending.

The sample consists of 483 listed industrial firms in Hong Kong, Indonesia, Korea, Philippines, Taiwan, Thailand, Malaysia and Singapore for the period 2008 to 2015. They are from various industries such as airlines, electrical equipment, petrochemicals, manufacturing industrial products, transportation, consumer products and shipping. We classify firms as users or non-users of derivatives based on their annual report disclosures on corporate financial risk management and derivatives usage. On average, for the whole sample, 32% of the firms hedge their interest rate risk. In general, the firms typically use interest rate swaps, forward rate agreements, caps and options to manage their interest rate risk exposure.

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WHICH FIRMS ARE MORE LIKELY TO HEDGE THEIR INTEREST RATE RISK?

First, derivative users that hedge their interest rate risk tend to have higher debt-to-assets ratio than non-derivative users. For the typical firm with floating rate debt obligations, sensitivity analysis indicates that a 1% increase in interest rates can potentially reduce the net profit of these firms by 5% if these firms do not hedge their interest rate risk exposure. Similarly, a 1% increase in interest rates can erode operating cash flow by 3% to 8% if these firms choose not to hedge their floating rate debt.

Second, derivative users that hedge their interest rate risk tend to have lower interest coverage ratio (operating profit divided by interest expense) than non-users. Similarly, derivative users have lower current ratio (measured as current assets divided by current liabilities) than non-users. These results suggest that derivative users are more likely to experience financial distress risk arising from their debt obligations.

Third, we find that firms that use derivatives (users) are significantly larger in size than non-users. This result suggests that larger firms and those with higher organisational complexity (such as many business segments) have greater exposure to interest rate risk. Furthermore, large firms are more likely to have formal financial risk management programmes that define risk management objectives, risk tolerance, and specific policies to mitigate financial risk and responsibilities to monitor the risk exposures.

Fourth, we find that firms that have stronger corporate governance structures are more likely to hedge their interest rate risk. Specifically, firms with higher proportion of independent directors on their Board, firms that separate their CEO and Chairman roles, and firms with higher institutional ownership, tend to use derivatives to hedge their interest rate risk.

WHAT IS THE ASSOCIATION BETWEEN DERIVATIVES USAGE AND FIRM VALUATION?

Using market-to-book equity as a measure of firm valuation, we provide evidence that firm valuation is positively associated with the intensity of derivatives usage. In terms of economic significance, we find that derivatives usage increases shareholder value, by between US$21 million and US$70 million, representing about 2% to 5% of equity valuation. Hence, derivatives usage has substantial positive economic effect on shareholder value. On average, firms are more likely to use derivatives for hedging purposes (rather than speculative reasons). Moreover, we find that derivative users have lower cash flow volatility than non-users.

Next, we examine how derivatives usage for risk management can affect corporate financial outcomes, namely, capital expenditure spending and cost of debt capital.

DERIVATIVES AND CAPITAL EXPENDITURE INVESTMENTS

We test the association between capital expenditure intensity and derivatives usage. Hedged cash flows can support a firm's capital expenditure planning decisions such as capital investments that are planned years in advance when it is difficult to predict its cash flows or access to external financing. Our result indicates that firms that use derivatives are able to invest more in capital expenditure than non-users of derivatives. In terms of economic significance, this result suggests that being a derivative user increases

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a firm's capital expenditure by 7% relative to a non-user.

Next, we focus on the sub-sample of firms that use financial derivatives. Using the ratio of the net absolute fair value of derivatives divided by total assets as a measure of the intensity of derivatives usage, we find that capital expenditure as a percentage of total assets is positively associated with the intensity of derivative usage. Holding constant various firm characteristics such as firm size, industry and profitability, a firm with "high derivatives usage" has a capital expenditure investment intensity that is about 15% higher than a "low derivatives usage" firm. By reducing the probability of negative cash flow scenarios, hedging with derivatives enables firms to direct more internal funds into future positive net present value projects. The benefit of hedging in promoting capital expenditure intensity is more pronounced in firms with high growth options and those that lack flexibility to obtain additional debt capacity. Without hedging, unexpected shocks to the cash flow may force firms to rely on costly external financing to support their capital expenditure investments. In the worst-case scenario, firms may be forced to reject value-increasing profitable projects.

Moreover, we document that the positive association between firm valuation and derivatives usage is higher in firms with higher capital expenditure investments. This result suggests that firms are more likely to invest in positive net present value capital investment projects (rather than value-destroying projects), which leads to higher firm valuation. Furthermore, the benefits of derivatives in promoting capital investments seem greater in firms with higher sales growth and those operating in volatile business environments.

As an additional test, we also examine whether the derivative users can pay higher dividend. We focus on firms with high capital expenditure spending as a fraction of sales. Among these firms, those that use interest rate swaps exhibit a higher propensity to pay higher dividends. Hence, the

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Our result indicates that firms that use derivatives are able to invest more in capital expenditure than non-users of derivatives. In terms of economic significance, this result suggests that being a derivative user increases a firm's capital expenditure by 7% relative to a non-user.

usage of derivatives helps firms with high capital investments to have sufficient cash flow to pay dividends to shareholders.

DERIVATIVES AND COST OF DEBT

In our sample, most firms use financial derivatives (such as interest rate swaps) to manage their liabilities, especially floating rate debt. Thus, it is important to examine the association between derivatives usage and cost of debt. We find that cost of debt (proxied by interest expense divided by long-term debt) is negatively associated with hedging intensity. In terms of economic significance, a one-standard deviation increase in the hedging intensity leads to a 1.2% reduction in interest expense. Relative to the average cost of debt of 6%, this represents a 19% reduction. Thus, by reducing the downside risk of low cash flow realisations, hedging helps the borrower to reduce its cost of debt.

The negative association between hedging and cost of debt is more pronounced in firms with higher expected financial distress costs, such as firms with high long-term debt as a percentage of total assets, firms with low interest coverage ratios and firms with weak current liquidity. In other words, the benefits of hedging are stronger for borrowers with weaker financial health.

To gain additional insight into these effects, we also examine a sub-sample of firms with floating rate debt. If these firms do not hedge, an increase in borrowing rates will increase the interest expense on their floating rate debt, which eventually reduces net profit. Sensitivity analysis indicates that net profit can be reduced by up to 5% for every one percentage point rise in interest rates. We find that about 36% of the firms with substantial floating rate debt attempt to hedge interest rate risk by using an interest rate swap. By transforming their floating rate debt into fixed rate debt, they are shielded from future interest rate increases. Hence, effective usage of derivatives can substantially lower the cost of debt. More generally, for firms with substantial debt, derivatives can potentially help firms to reduce the likelihood of breaching debt covenants by ensuring sufficient cash flow to meet debt obligations as and when they are due.

CONCLUSIONS

We find that firm valuation is positively associated with derivatives usage intensity. We provide evidence on two channels in which hedging with financial derivatives can affect corporate financial outcomes. First, hedging lowers the cost of external debt financing, especially in firms with high expected financial distress. Second, by reducing the downside risks associated with insufficient cash flow and narrowing the variability of future cash flows, hedging promotes capital expenditures in profitable projects. ISCA

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