Plain truth about audit adjustments

INVESTORS in Singapore-listed companies can now have an idea of the accuracy of their financial statements prior to audits, and just how much adjustments had to be made by auditors.

In a landmark study, it was revealed that S$33.9bil (RM85.6bil) worth of adjustments had to be proposed for a third of all listed companies, for the year ended Dec 31, 2013, said the Singapore Business Times (SBT).

It was discovered that 13% of the companies in the sample (33 companies), mainly those in growth stages, had more than 20 proposed adjustments each, said SBT.

These accounted for nearly three-quarters (73%) of all proposed amounts, totalling S$24.7bil. The study said this could be due to accounting systems and capabilities not keeping pace with the companies’ expansion, and that these companies should improve their internal control systems and processes, said SBT.

The study, the first of its kind in the world, was published by the Accounting and Corporate Regulatory Authority (Acra) and the Singapore Management University.

Acra’s chief executive Kenneth Yap said: “Companies with multiple audit adjustments need to shape up. Investors and company directors can and should also demand higher quality accounting from their companies.”

Taking a leaf from this study, other countries in the region should also look into how much audit adjustments have been made for their listed companies, as an indication of the quality of financial reporting.

These would serve as indications of how much financial preparers have to further improve their game.

In its latest move to rein in shadow banking, China is requiring its banks to “comprehensively” supervise risks stemming from financing activities through securities firms, insurers and trust companies in the form of entrusted loans or wealth management products (WMP), said Reuters.

Banks will also need to apply the same risk control practices for each of their subsidiaries, while off-balance sheet assets will need to be categorised by levels of risk and capital cost, Reuters said, quoting the draft rules posted on the banking regulator’s website.

Shadow banking may involve up to 27 trillion yuan (US$4.39 trillion) of assets, which would be equivalent to one-fifth of China’s formal banking sector, said Reuters, quoting a report by the Chinese Academy of Social Sciences.

Fund mnagement company (FMC) subsidiaries alone have issued more than 2 trillion yuan (US$325bil) worth of structured investment products since they were allowed to enter the market in 2012, said Reuters, quoting estimates from Shanghai-based fund researchers Z-Ben Advisors.
The agency regulating these FMC subsidiaries is the China Securities Regulatory Commission.

Two defaults lately have further rattled the market for these high risk WMPs.

One involved a default by a fund marketed by a group of subsidiaries and partners of Noah Holdings, a Chinese WMP company listed in New York, said Reuters.

Chinese media reported that the fund had experienced repayment problems with a one billion yuan (US$162.5mil) WMP that was due to mature earlier last month.

In a second recent case, Mirae Asset Huachen Fund Management Co, a joint venture between South Korea’s Mirae Asset Financial Group Co and two Chinese FMCs, announced on Aug 11 that it had failed to pay more than 32 million yuan worth of interest due on trust loans in July due to project difficulties, said Reuters.

As the economy slows, there could potentially be more of such defaults springing up especially in the high risk sector.

Understanding and control of risk when bundling and purchasing these products is vital especially for a huge market like China.

Bad loans are on the rise in India’s banking sector and the authorities are planning to impose stricter limits on lending to a single corporate group.

Currently, banks are allowed to lend up to 40% of their core capital to a single corporate group.

The ceiling could rise to a maximum 55% including infrastructure loans and bank board approvals in what were deemed “exceptional circumstances,” said Reuters.

In its annual report, the Reserve Bank of India (RBI) said it planned to review the cap during this fiscal year that started on April 1 to gradually align it with a 25% ceiling set by global standard-setter Basel Committee on Banking Supervision, said Reuters.

Two straight years of less than 5% economic expansion has led to a surge in bad loans for Indian lenders.

As of March, more than 4% of banks’ total advances were categorised as bad loans, compared with 2.9% two years earlier, said Reuters.

Control on risky and unbalanced bank lending is vital for the eventual health of the economy.

Realising the dangers, the RBI is acting fast to contain the rot before it spreads further.

Columnist Yap Leng Kuen notes that audit adjustments are sensitive and may just indicate the need for better quality reporting, and not necessarily any wrongdoing.