



Financial Reporting Webinar Series: Navigating potential accounting fraud

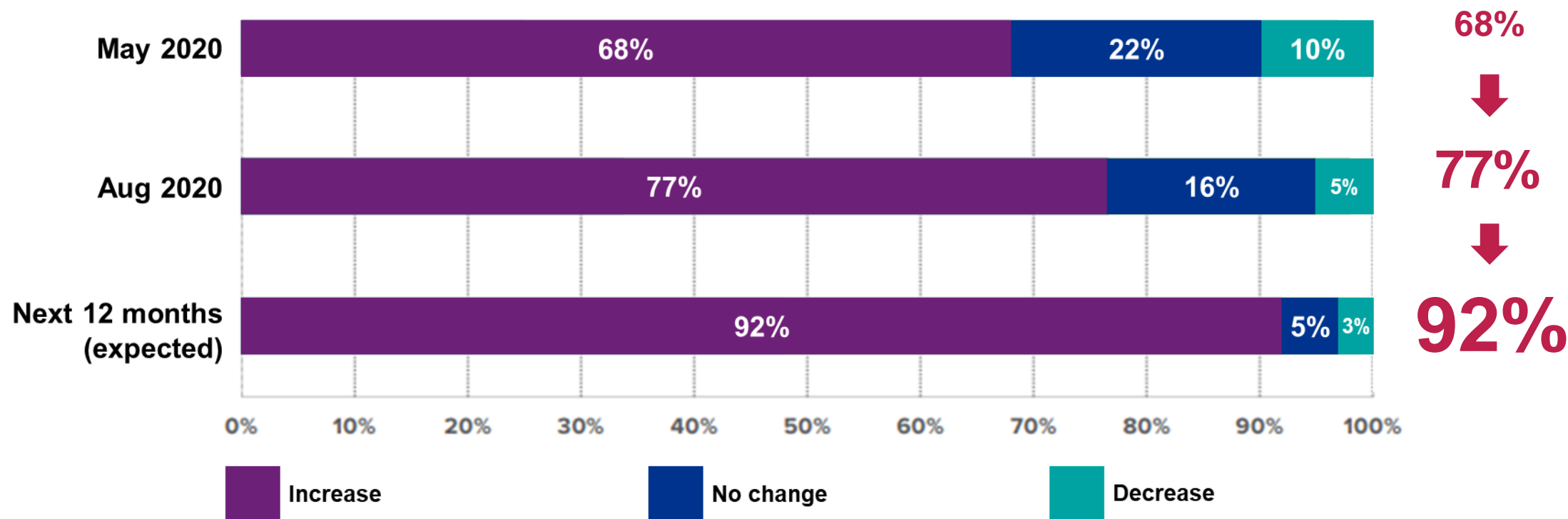
Friday 29 January 2021



1. Recent survey on Fraud

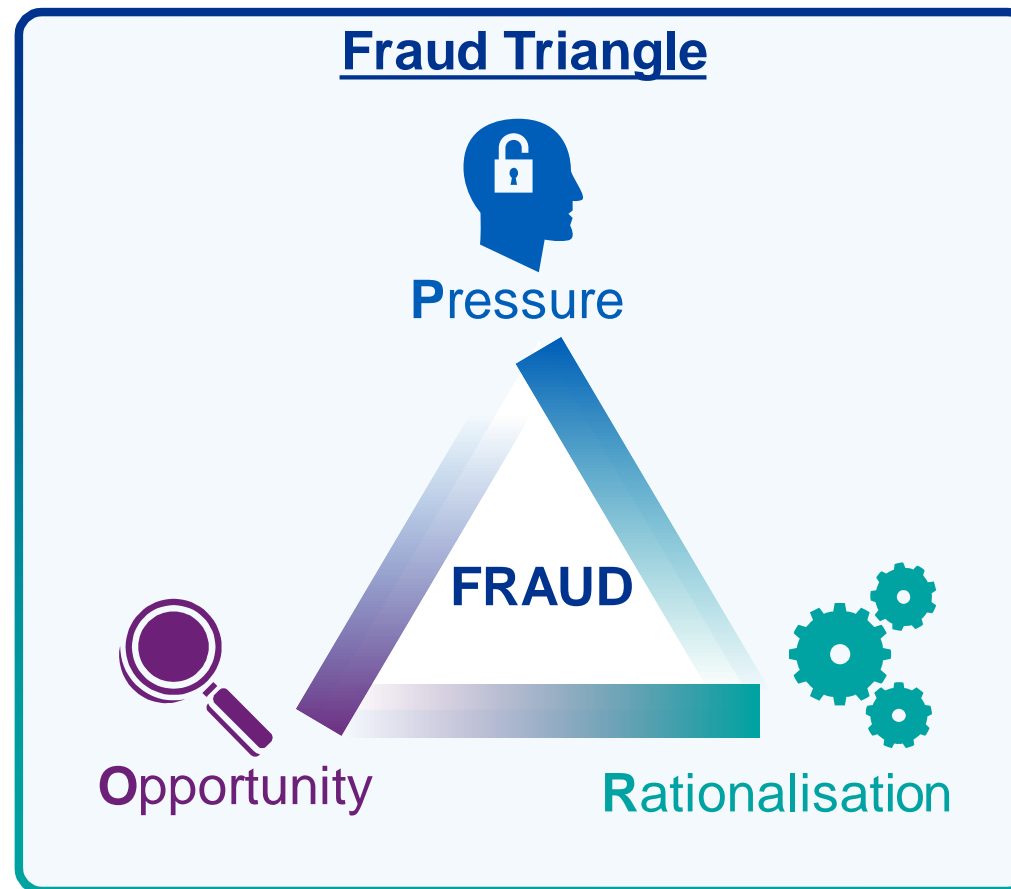


Fraud cases during the pandemic



Source: ACFE, Fraud in the Wake of COVID-19: Benchmarking Report

2. Increasing pressure and new opportunities and the Fraud Triangle



3. Financial Statement Fraud – Short-sellers



Financial anomalies

- **Filings:** Inconsistencies with financial filings
- **Receivables:** Unusual variances in receivables balances
- **Trading:** Significant stock price movements
- **Liquidity issues:** Poor cash flow/ low cash balances
- **Borrowings:** Large build up of debt
- **Revenues:** Significant unexplained increases in revenues and/or margins
- **Performance:** Outlier statistics when benchmarked against competitors and peers in similar industries



Non Financial anomalies

- Opaque transactions
- Management inexperience in the industry
- Management having a lavish lifestyle
- Large number of employees leaving
- Perceived weak corporate culture and/or frequent management changes or differences
- Low transparency in acquisition and divestitures
- Disparities between output and non-financial metrics such as labor force when output increases or decreases
- Discrepancies from site visits
- Incompatible business entities and operations
- Negative press or allegations about management
- Entity controlled and managed by one or two persons who are often family
- Opaque corporate structures
- Environmental practice concerns and contingent liabilities
- Business or personal associations with troubled companies
- Production volumes that vary from industry or government data
- Change in company auditors / using discredited auditing firms
- Market presence not supported by external data

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4. Regulatory landscape



SFC's regulatory approach and priorities



A “front-loaded” approach to address market quality and corporate conduct issues



Corporate fraud and misbehaviour remain a priority



SFC intervention in listing matters and “suspicious corporate transactions”



Focused enforcement against senior management of listed companies and people in gatekeeping roles

4. Regulatory landscape (cont'd)



SFC enforcement powers under Securities and Futures Ordinance



Extensive powers of investigation



Civil or criminal liability

e.g. Ss 277/298 : Disclosure of false and misleading information

Andrew Left and Citron Research (2016)



Other powers

e.g. S. 213 injunctions and restorative orders

S. 214 disqualification of directors / compensation orders

Chin Jong Hwa, RMB 20.3 million re Minth Group Limited (2019)



Co-operation with ICAC, HKP, CSRC, US SEC, UK FCA etc.

5. The Mitigation Framework



Prevent

- **Reassess** risks and controls in light of less staff / new operating model / new technology
- **Consider new technology** to assist in prevention and detection
- **Reinforce values** and tone from the top expectations **and garner feedback**



Detect

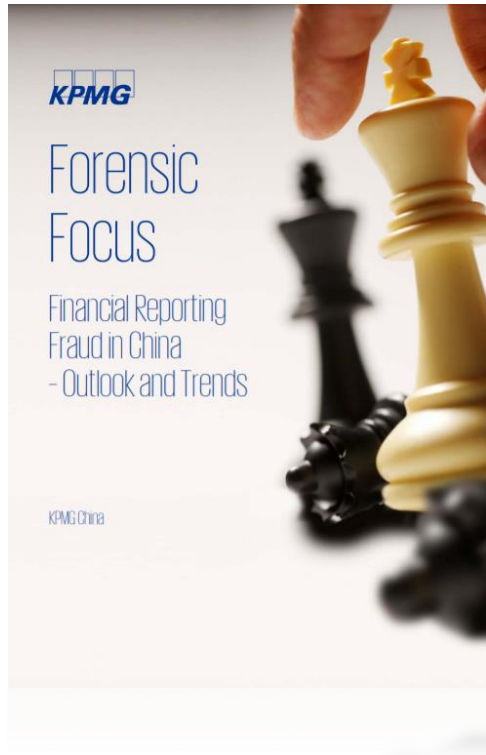
- **Re-evaluate detection methods:**
 - **Whistleblowing** systems & outreach
 - **Embedding forensic experience and techniques** to controls & audits
 - Artificial intelligence detection methods
- Add **additional oversight**




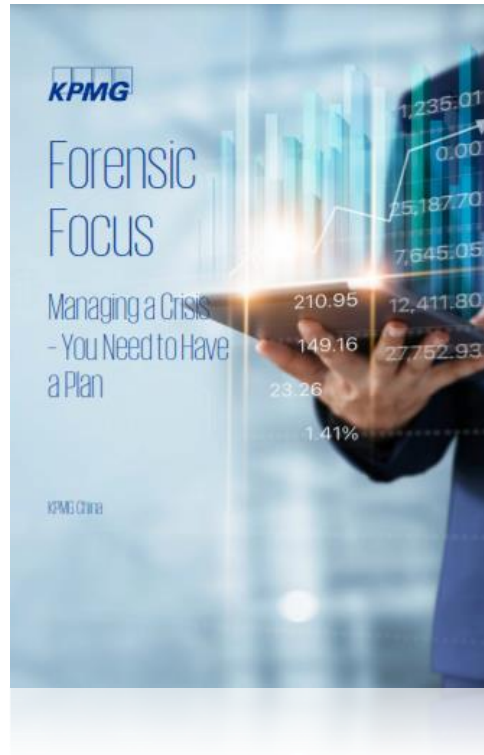
Respond


- Need a **response plan** or **playbooks** specific to indicators of anomalies and short-seller attacks, including:
 - **Timely** engagement of legal counsel and forensic accountants
 - Team for fielding media and regulatory enquiries
 - Co-ordinate all of above with various internal functions

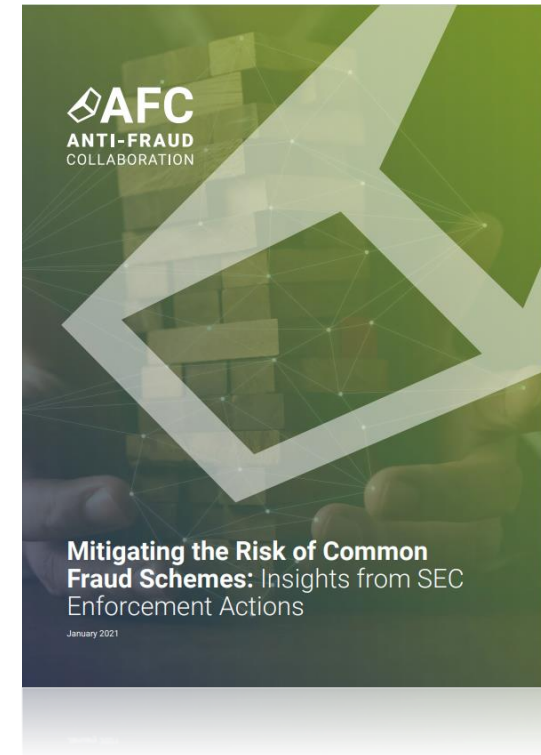
Resources



 [Forensic Focus: Financial Reporting Fraud in China - Outlook and Trends](#)



 [Forensic Focus: Managing a Crisis - You Need to Have a Plan](#)



 [Mitigating the Risk of Common Fraud Schemes: Insights from SEC Enforcement Actions](#)

Resources – cont'd



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Non-GAAP measures – fact or fiction?
Financial reporting hot topics

25 January 2021

Through various forums, questions regarding the usage of Non-GAAP financial measures or alternative performance measures have been raised repeatedly as companies approach the preparation of their annual financial reports. The "unprecedented" year in 2020 effectively sums up the challenging year for most companies in the past 12 months. So how could non-GAAP measures be used by companies to communicate to investors the impact that Covid-19 has had on their performance in FY 2020? What do companies need to look out for when considering the type of adjustments to present as non-GAAP measures to investors? There are obviously no right or wrong answers to these questions, but for those who use non-GAAP measures, here are some ways we think could maximise the potential of how non-GAAP measures are used in communicating companies' financial performance.

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Coherent communication strategy - use of non-GAAP measures is one of the tools in a company's communication toolkit, not the only tool

Companies thinking of using non-GAAP measures to communicate how the pandemic has impacted their businesses would benefit from thinking about their communication strategy in a holistic manner. What do we mean by that? Using non-GAAP measures is one way to explain the Covid-19 impact. Narrative explanation in the MD&A and notes to the financial statements are other channels companies could use to provide investors with the information they need to understand the magnitude of the impact, areas of the business that are most affected, strategies that management has deployed to navigate the challenges and where the uncertainties lie in the coming months ahead.

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In fact, non-GAAP measures should act as a bridge to GAAP information. Historical financial information provides an important input into investors' evaluation of a company's prospects; non-GAAP information allows investor a glimpse into management's own perspective of the company's performance and facilitates forecasts of future performance. The two types of information serve different objectives and purposes for investors. Both local and overseas regulators alike, have similar prohibitions on giving non-GAAP measures greater prominence to GAAP measures to ensure the information quality in a company's reporting is kept high. Overall, the information that management chose to provide to investors, should provide more clarity and understanding to an investor on the business's underlying performance, without injecting some form of management bias to the information presented.

FRHT IFRS Column: Non-GAAP measures – fact or fiction?

Webinar dates and topics for 2021

- **29 January – Navigating potential accounting fraud**
- **19 March – TBD**
- **14 May – Interim reporting reminders**
- **16 July – TBD**
- **17 September – TBD**
- **19 November – TBD**
- **17 December – Year-end reporting reminders**



For more details and access to our webinar series:

<https://home.kpmg/cn/en/home/services/audit/ifrs-news/financial-reporting-webinar-series.html>

Speakers



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Thank you



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