Board Matters Quarterly offers thought-provoking perspectives and insights into leadership and governance issues for boards and audit committees, supporting them to navigate the increasingly complex business environment.

Changes in the business landscape are unceasing. Read more to keep updated on the latest global and technological issues that will impact board strategies.

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Digital audit for stronger boards

Emerging technologies will transform audit and the way audit committees of the future work. Technology is a means to support the board — a key enabler to uncovering issues and maximizing business potential.

By Christopher Wong

The digitalization of audit mirrors a broader transformation taking place across the business landscape. With new tools and techniques emerging, the use of technology in audit gives companies greater levels of oversight, assurance and insights, enabling boards to discharge their fiduciary and governance duties more confidently.

Next-level audits
For audit committees (ACs), a game-changing technology is data analytics. The technology allows auditors to move past auditing small samples of data to auditing large samples, or even entire datasets.

Data analytics helps to paint a more holistic picture of an event for high quality discussions within the board, and further investigation of the issue with the management when necessary. In the case of fraud detection, data analytics equips the auditor to identify signs of fraud or manipulation of accounts easily and focus recalculations on high-risk areas. This allows for top-down analytical checks on data for financial control and internal audit, and proactive management of potential issues.

Another technology, artificial intelligence (AI), is seen as the next frontier in audit, as it allows for analysis of unstructured data such as emails, social media posts and conference call files to search for evidence of fraud. In other instances, it allows for extraction of key information from large numbers of contracts, such as leases.
AI adds logic to the “reasonableness” test to examine the validity of accounting information. In the past, auditors would look at statistical variances and ask if it is reasonable, and the reason for the variances. Today, AI does more thorough analyses by cross-referencing data to provide a broader perspective beyond the board’s combined experience for more relevant insights on the level of “reasonableness”.

Another emerging technology that has the potential to transform audit is robotic process automation (RPA). It can be used to generate audit-ready work papers, and when combined with the use of drones, is an effective way for auditors to conduct inventory counts in remote locations. Together with data analytics and AI, these technologies could bring substantial improvements to the quality of future audits.

"Given the importance of digitalization to the company’s strategy and operations, ACs and boards need to bring in directors who are subject matter experts or conversant with technology to ask the right questions and work closely with the management."
The role of AC in the digital shift

High-quality audits are not just about investing in and adopting technological tools; they also rely on higher-quality data sets. Despite the increasing use of data analytics, few companies today are of the maturity where analytics are fully optimized to be applied effectively.

ACs are in prime position to drive change. With technology, the output is only as good as the input. A database with good quality data and clear rules is fundamental to financial control, because risk management systems need to be informed by accurate data. This in turn allows for efficient extraction of the data for more meaningful insights.

The transition from traditional models of data capture and audit also requires a host of different skillsets and an understanding of how the outputs and data can be used. Also, data is a company asset and should be treated with the appropriate level of confidentiality and security.

In today’s environment where we may accept cyberattacks as an unavoidable reality, the pressure to keep data safe underscores why cyber risk must feature prominently on the agendas of the AC. Regular reviews and monitoring of the cyber risk dashboard environment with the rest of the board is a must.

Given the importance of digitalization to the company’s strategy and operations, ACs and boards need to bring in directors who are subject matter experts or conversant with technology to ask the right questions and work closely with the management. Alternatively, boards can be supported by a digital committee that updates the board on the latest technological trends and issues.

Emerging technologies have great potential to transform audit and the way ACs of the future will work. Still, technology is not an end-all for ACs. In the course of discharging board duties, there is a lot of judgment involved. While technology cannot fully take that on, smart technologies and robots can help to simplify and uncover issues that may be critical to the future performance of the company.

Questions for boards:

1. How is the AC evolving with increasing adoption of technology in the business and operations?
2. In what areas can digital audit provide the board with better oversight and insights?
3. Is the AC well-versed in technology, and what are the measures taken to manage the board’s strengths and gaps in this area?
4. While maximizing the opportunities to go digital, what are the areas of vulnerability that need to be proactively managed?
5. What is the corporate culture towards the collection, analysis and handling of data?
Bots for future boards

With an estimated 20%-40% of professionals at risk of automation in the coming years, boards must lead the change to adequately manage the risks and benefits of smart technologies for the backbone of the organization — its people.

Artificial Intelligence (AI) solutions fall broadly into two categories — those that support insight and decision-making, such as data analytics and visualization tools, and those that automate highly complex processes or human interactions such as machine vision and natural language processing. A combination of these intelligent automation technologies enables end-to-end processes to be automated to increase efficiency, improve decision-making and enhance control environment.

Most organizations look for financial savings to fund the qualitative benefits of an intelligent automation program. Depending on the maturity of the current processes and systems, potential savings from implementation range from 15% to 30%.

It is estimated that 20% to 40% of professionals are at risk of automation in the coming years. This means that boards must lead the change with their management to adequately manage the risks and benefits of intelligent automation for the backbone of the organization — its people.

Understanding automation

One of the challenges for boards is understanding what exactly intelligent automation comprises. For many, it is an umbrella term for a range of automation technologies, from relatively simple robotic process automation (RPA) software to highly specialized AI tools that can mimic, or even outperform human intelligence in some cases.

RPA is often a first step to the adoption of automation due to its relative simplicity and combined with the opportunity to make significant improvements in operational efficiency. However, unlike a pre-configured, out-the-box systems, RPA...
needs to be programmed specifically for the processes and actively managed by a combination of business and technology specialists.

RPA robots (bots) work best when activities are structured and repetitive – data entry, reconciliations and reporting are prime examples. The technology sits on top of legacy systems and does not require deep integration, so implementation timelines are relatively short, typically weeks for a simple process. Multiple transferable bots can perform a range of tasks concurrently, so at scale, RPA acts like a virtual workforce within the organization.

However, not all processes can be guided by a simple set of rules. For processes that are more complex than RPA, RPA must be augmented with cognitive automation, a solution that leverages machine learning to enable it to learn unstructured processes.

Boards must bear in mind that technology is just an enabler to the outcomes. Smart technologies can be thought of as a digital workforce and should be managed as such.
and adapt to changing business logic by continually observing human co-workers.

For these transformative endeavors, the implementation timelines are longer and the costs are typically higher than a RPA-only project, due to the training required to process a large amount of historical data or real-time examples.

AI processes that are more complex use algorithms built to function like human intelligence. Developing these solutions requires a huge amount of data and significant computational power, in addition to the expertise needed to codify the problem statement and train the bot. While they are complex to develop, AI solutions can be procured “pre-trained” and integrated with other automation tools.

**Implementing intelligent automation effectively**

Intelligent automation offers a powerful premise for boards looking to transform business processes. However, if automation programs are not correctly managed, they can become costly exercises without the expected results.

Boards need to reinforce three guiding principles when implementing and investing in automation programs. Firstly, process re-engineering accounts for 20%-50% of the effort in successful implementations. Standardizing, simplifying and eliminating activities before they are automated not only reduces overall implementation effort, but also improves the resilience and ease of maintenance of the final digitized process.

Next, strong governance with clear roles and responsibilities must be embedded throughout the automation life cycle – most importantly after the digital workforce goes live. Intelligent automation solutions are typically customized for specific requirements, so they must be actively managed, measured, trained and improved over time.

Lastly, boards must bear in mind that ultimately, technology is just an enabler to the outcomes. Even the smartest AI systems outperform humans in only very specific activities. We are probably decades away from solutions that are as adaptable, resilient and collaborative as our human workforce.

A coherent workforce transition strategy with a future-focused ethos must be the foundation of any AI program. Smart technologies can be thought of as a digital workforce and should be managed as such. Automation is certain to bring a range of benefits across the organization – increased efficiency, improved decision making and an enhanced control environment, in line with the board’s purpose. Embracing this opportunity should be a key for boards today.

**Questions for boards:**

1. Do you have a trusted advisor who can help to inform the board on AI and its impacts on the organization?
2. How are you challenging the management to respond strategically to both the opportunities and the risks associated with AI?
3. How is the management reimagining the way the business delivers value by anticipating the shift to the potential scale AI offers?
4. In which areas of the business is smart technologies most suited for implementation, for the highest returns?
5. Does your organization have a talent strategy for recruiting and retaining people with the necessary skillsets to manage and staff AI-related projects?

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Digital technology and unprecedented regulatory changes are transforming the future of tax. Boards must urge companies to seize the opportunity to shape their tax functions to drive value beyond compliance and reporting.

By Chung-Sim Siew Moon

Digital technology and unprecedented regulatory changes are transforming the future of tax. Tax administrations around the world are going digital rapidly, harnessing digital tools to improve their administration of tax, simplifying and automating tax filing processes and requiring submission of source accounting and transactional data in digital format.

Increasingly, they are demanding near real-time information from businesses, overhauling the way taxes are reported, filed and collected, disrupting the traditional compliance process and accelerating reporting and filing obligations for businesses. Data matching and data analytics tools are also deployed to mine for errors, inconsistencies, anomalies and systemic frauds, enabling the authorities to identify tax audit targets and controversies.

Technology is also facilitating the sharing of information by tax administrations globally. The digitization of country-by-country reports filed by multinational companies enables tax authorities to share them across boundaries to assess risks, trends and anomalies, enhancing their efficiency.

Technology creates both benefits and complexities

For businesses, technology such as robotic process automation and new systems that offer real-time collaboration, scenario planning and risk simulation are transforming traditional accounting, finance and tax functions. Repetitive, high-volume tasks and low-value processes can now be performed 24/7 by robotics and artificial intelligence (AI) faster, at lower cost and more accurately.
Technology also allows tax professionals more time to pursue tax value creation by using digital and automation tools earlier in the tax life cycle instead of focusing purely on reporting. However, robotics and AI cannot replace tax professionals completely, especially in the more technical or subjective areas where human experience, insights and judgment are needed.

With the implementation of higher levels of data analytics and data matching, a greater number of incoming inquiries are generated by tax authorities. When such incoming inquiry triggers the audit, such audits can tend to be aggressive in nature. Clearly, the tax function must always be audit-ready, and technology can help enable that.

The intense global debate about the taxation of companies that use digitally-enabled business models to penetrate markets with no physical presence supporting the digital revenue streams is not abating either. It is important that such digital businesses, typically running on thin margins, are confident of assessing, quantifying, planning for and complying with a myriad of new laws that aim to levy tax on the profits generated by fast-growing electronic transactions.

Boards to take the lead

Given the rapid shifts in the tax landscape, companies must now assess their digital readiness and whether their people, legacy systems and processes can support the change.

Boards and management need to understand the data requirements of the tax authorities in each of their operating jurisdictions, have the appropriate tools to prepare digital tax submissions, “sensitize” data for tax purposes and check for errors before filing, and be prepared for clarifications. The close partnership between tax, finance and IT functions is essential.

In addition, companies should have the tools and processes to monitor the company’s global tax compliance and reporting obligations, so that they can respond in a timely manner to tax authority demands. Boards must also be regularly updated on the tax risks and controversies in every jurisdiction, and the potential impact to the company’s tax governance framework with each change.

What this means is that investments will be needed to enable the tax function to be robust and nimble – business strategies and revenue creation activities must be viewed with a tax lens at the design stage.
To that end, boards must take a proactive role in supporting their companies’ tax transformation journeys. Do you want to be reactive to regulatory demands and leave little time for value-adding activities, or be proactive with change and better enable your tax professionals to drive value, innovation and ultimately, contribute to profitability? The answer is clear.

Questions for boards:

1. Does the business have a proper governance and global operating model, demonstrating risk aversion, visibility and cost effectiveness?
2. How is the management team monitoring global changes to submission requirements and preparing for new mandates?
3. Is the business’ approach to digital and technology keeping pace with that of the tax authorities?
4. Does the board have visibility and understanding of what the tax authorities are doing with the company’s data?
5. How assured are you that digital audit defense activities are integrated into the tax function’s daily processes?

“Given the rapid shifts in the tax landscape, companies must assess their digital readiness and whether their people, legacy systems and processes can support the change. Business strategies and revenue creation activities must be viewed with a tax lens.”

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The board’s role in navigating geopolitics

Geopolitics is not a problem to be solved but an external force to be understood and managed. The board should set the tone for confronting the challenge and ensure the right people are overseeing the ensuing risks and opportunities.

By Max Loh

Executives today are increasingly feeling the pressures of policy uncertainty, geopolitical tensions and shifts in trade policy and protectionism on their business. Such geopolitical issues can significantly impact an organization’s business strategy and operations, underscoring the need for board-level involvement in addressing them.

Just as one would prepare for any business risks and black swan events, geopolitical risks must be considered within the company’s overall enterprise risk management framework. A more deliberate approach to better understand and incorporate these risks and opportunities into strategy setting and risk management process is needed. For the board, it is critical to understand the management’s approach, which at its core should involve a process for understanding, preparing for and acting on geopolitical events.

Addressing geopolitical developments requires companies to understand the full universe of these forces, the likelihood of them materializing to meaningfully affect the business, as well as the corresponding disciplined approach to assess such exposures.

These forces could include trade barriers and tax policies that can impact revenue drivers for the company across its current global footprint, as well as its supply chain, human capital, corporate functions and stakeholders. Without a comprehensive
Just as one would prepare for any business risks and black swan events, geopolitical risks and opportunities must be considered within the company’s overall strategy and enterprise risk management framework. and prioritized review of all reasonable sources of potential geopolitical impacts, some critical risks or opportunities may be overlooked.

Boards should seek the opportunity to review and provide input to the geopolitical risks identified by management as potentially relevant. With its independent perspective and unique combination of expertise, the board can help challenge management to fully understand the risks embedded in their business strategies and uncover potential opportunities.

Once the risks and opportunities have been identified, the management needs to prepare itself by assessing the possible scenarios and impact, and the likelihood and timeframe to the events taking place. This assessment will highlight the key issues and whether the business strategy needs to be adjusted.

This assessment process must also take into consideration the company culture and its stakeholder interests. Taking advantage of opportunities presented by geopolitical changes may create consequences that can impact the company’s relationships with key stakeholders, its reputation and even its social license to operate.

Thereafter, boards need to decide the next course of action – accept, mitigate, eliminate or transfer the risk, or strategically pivot to seize opportunities – while avoiding knee-jerk reactions. Companies need to create and evaluate their options for addressing various scenarios that may result. These may include a range of stress-test exercises, including tabletops, quarantines and any number of resiliency plans, such as rapid deployment of assets, capabilities, lines of credit. Postmortems and “lessons learned” analyses
to assess what was missed and how well the company responded to an incident will be highly useful.

**Building board competency**

Navigating geopolitical concerns may not come naturally to many. It is important to make sure that the right people are in the boardroom to effectively oversee the geopolitical risks and opportunities facing the company. For some boards, that may mean having a director with specific regulatory or public policy expertise, or expertise relevant to volatile regions or markets where the company operates in or is planning to expand into. For others, it means consulting with an expert on the relevant topics.

Boards also need to consider their process for getting information and how they can stay current on geopolitical developments and how the company strategy is evolving in tandem. Boards should expect timely, valuable information from management in a manner that facilitates rich dialogue. Boards also need to gain more exposure to external viewpoints so as to be able to challenge management and offer informed input.

As with other priorities on the board agenda, having a board and management team that are well-aware of the external business context, deeply understand the company’s strategy and the underlying assumptions, and can be nimble when executing strategic pivots is key to weathering any black swan event and creating long-term value. Given that geopolitical issues are complex and can be unpredictable, it is tempting to see geopolitics as impossible to prepare and plan for or control. While the fundamental nature of geopolitics can be volatile, most organizations understand that geopolitics is not a problem to solve but an external business force that must be understood and proactively managed – and the board must set the tone for confronting it.

Questions for boards:

1. To what extent are geopolitical opportunities and risks considered as part of the company’s strategy setting process, and embedded into its enterprise risk management?

2. What is the management’s process for mitigating geopolitical risks through scenario analysis and stress-testing?

3. Does the board have holistic visibility around the potential geopolitical impacts that the company faces or is it only approaching such impacts from an “event” lens?

4. If shifting geopolitical risk is challenging management’s critical risk assumptions, is the company prepared to effect a strategic pivot and has the board provided input?

5. Does the board have the right directors, committee structure and access to information to oversee key geopolitical risks, and challenge the management?

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Disruption is forcing boards to examine their portfolios more frequently. For the first time in a decade, more respondents to the EY Global Capital Confidence Barometer, which was released in the first half of 2019, are performing strategic reviews quarterly instead of annually.

In Asia-Pacific, 57% of respondents review their strategy and portfolios quarterly, compared to 9% who schedule annual reviews. The increased frequency of reviews allows boards to identify capital recycling opportunities and make smarter capital allocation decisions. Fifty-one percent of Asia-Pacific business leaders surveyed for the Barometer said they intend to pursue deals in the next 12 months, significantly above the 10-year average of 42%.

More frequent reviews are helping boards to not just acquire but also identify non-core, or underperforming, businesses and assets, and taking action to divest them in a timely manner. Alongside M&As, divestitures should be an integral part of an active portfolio strategy. Strategic divestitures reduce complacency that can build up over time in a complex organizational structure. When done right, it is a relatively inexpensive means to finance new growth opportunities.

What drives active portfolio management

The drive for active portfolio management partly stems from attempts by companies to counter the unrelenting pace of disruption and the potential impact of a global economic slowdown.
Activist shareholders appear to also play a part in this drive for acquisitions. As they look for evidence of improved shareholder value, business leaders are compelled to focus on value creation - and seeking out merger and acquisition (M&A) opportunities is a means to that end.

In fact, the Barometer had found that globally, activists and other pressures have pushed 60% of board members to review their portfolios quarterly or more frequently, and of these, 24% have identified areas with acquisition opportunities. As activists typically have strong strategic views and are well-informed about the company and its business environment, boards should engage activists to assess the merits of their business case.

Digital technology is another key catalyst. Most board respondents see digital as either fundamental to or having a very impactful influence on their business. To that end, many companies are acquiring digital businesses as an alternative to building digital competencies organically.

However, is such an approach truly effective?

**How to realize internal digital capital**

Many of such digital acquisitions often end up being an adjunct to the primary business with no real plans to incorporate the newly acquired business into the main stream of activities. The efficacy of corporate venture funds - a vehicle used by many companies - and their ability to influence the core of the company is questionable as well. Too often, these investments are kept at arm’s length and not embraced by the core business.
The important point here is: companies cannot just acquire their way into the new digital economy. They need to fundamentally understand how their business model can be changed and use a combination of acquisitions, collaborations and internal changes to be able to become a disrupter themselves.

Boards are therefore encouraged to think afresh and push management to unleash the true digital capital of their traditional businesses. With a few exceptions, mostly in financial services and telecommunications, many companies have yet to fully appreciate their internal digital capital and how to bring it to life.

There is little doubt that targeted investments and recalibration of capital allocation will be the new normal, with investments in digital technology as top capital allocation priorities. However, companies need to stop at taking the easy path of making small tentative acquisitions. Instead, they should embrace change in the core of their business and use relevant digital and analytical opportunities and tools to refresh their business models and portfolios for the future.

Greater frequency and discipline around portfolio performance will serve companies well in the long term as the board scans the horizon more regularly to drive a robust strategy that embeds their digital investments into the core business model of their existing business.

Questions for boards:

1. What is the true full digital capital potential of your traditional business?
2. What is the rationale for the quantum and direction of digital investments?
3. What avenues besides acquisitions have the company explored?
4. What is the current view on the risk of digital cannibalization of the core business?
5. What is the plan for bringing the investments into the core business model of the business?
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