

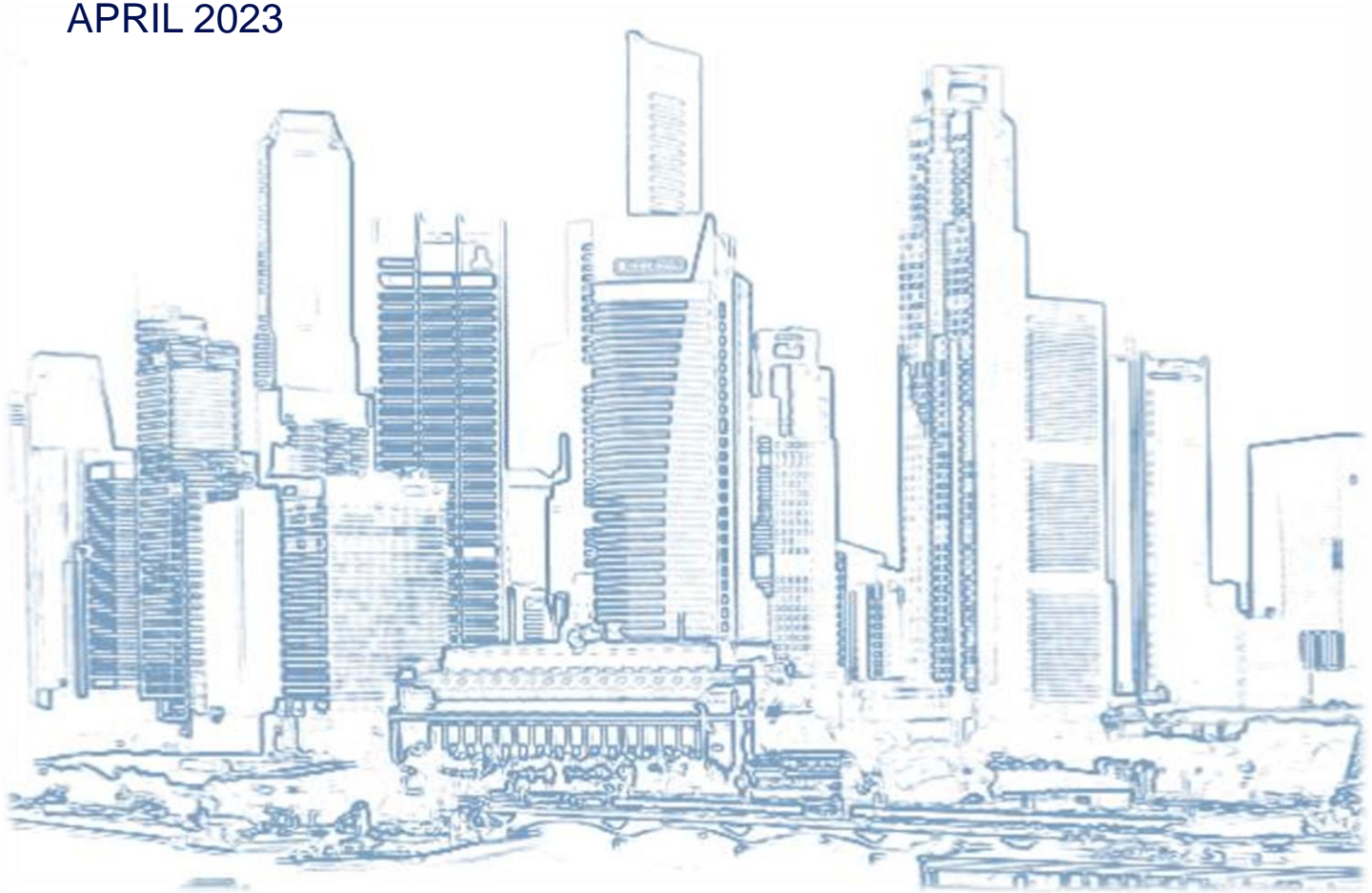


Monetary Authority of Singapore

CORPORATE FINANCE THEMATIC INSPECTION: GOOD PRACTICES AND KEY FINDINGS

INFORMATION PAPER

APRIL 2023



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A. Introduction

This information paper sets out MAS' supervisory expectations for financial institutions ("FIs") carrying out corporate finance ("CF") advisory activities for Initial Public Offers ("IPOs"). Such FIs, as Issue Managers ("IMs"), play an important role in acting as gatekeepers for potential companies seeking a listing in Singapore.

MAS conducted thematic inspections of eight IMs from June 2018 to September 2021¹ that focused on their controls, policies and procedures ("P&Ps") relating to the due diligence process for IPOs. Where such IMs were also acting as placement agents, MAS also covered their placement activities to assess the internal controls for such activities. Both banks and holders of a capital markets services licence to carry out CF advisory activities were covered in the thematic inspections.

This information paper sets out the good practices and weaknesses observed, and MAS' expectations from the inspections. Further guidance on MAS' expectations of the due diligence process is set out in Section B. MAS expects all IMs to incorporate these expectations, and where appropriate, the good practices into their conduct of CF advisory and placement activities.

Areas covered are as follows:



**Governance,
Compliance
& Audit**
- Section C



**Due
Diligence on
issuers**
- Section D



**Experts and
Advisers**
- Section E



**Record
keeping**
- Section F

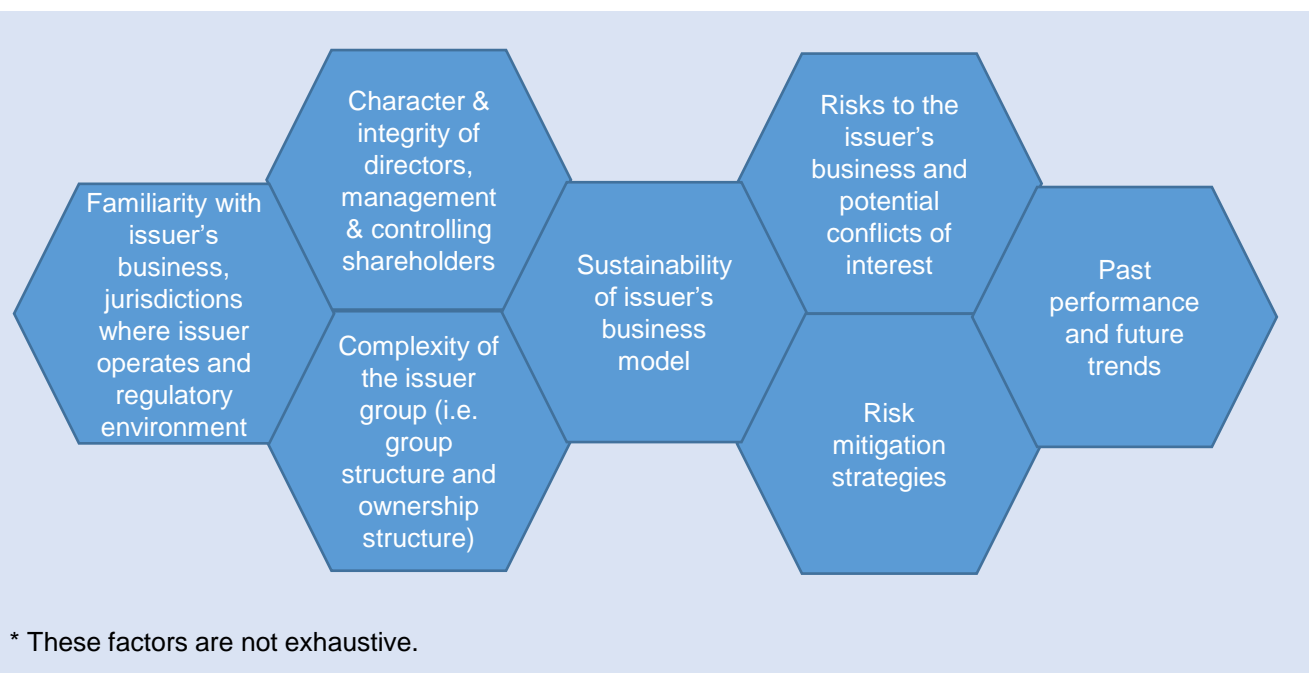
¹ The inspections occurred over a longer period of time as regular inspections were suspended to allow financial institutions to focus their efforts on dealing with Covid-19. Please refer to MAS' press release, "[MAS Takes Regulatory and Supervisory Measures to Help FIs Focus on Supporting Customers](#)" of 7 Apr 2020.

B. Expectations of IMs' Due Diligence Process

When conducting due diligence² on issuers, IMs should:

- Have a critical and questioning mind, and not overly rely on the representations made by the proposed issuer, particularly when encountering unusual or unfamiliar circumstances.
- Be alert to information that contradicts or brings into question the reliability of any other statements, representations and information obtained in the course of the due diligence process.
- Perform checks to verify material information or representations, such as through interviews, on-site visits and background checks on the issuer, its group of companies, directors, management and controlling shareholders. Independent verification checks should also be made where potential red flags are identified.
- Form a holistic understanding of the issuer's business and risk profile, particularly if the issuer is operating in unfamiliar markets, or has significant operations in higher-risk jurisdictions.

Factors* that determine the extent and depth of the due diligence to be undertaken by the IMs:



² IMs should also take guidance from the ABS Listings Due Diligence Guidelines

C. Governance, Compliance and Audit



IMs should exercise adequate management oversight of its CF advisory activities, including instituting robust P&Ps and ensuring that there is proper supervision of its representatives carrying out CF advisory activities. Effective compliance and internal audit (“IA”) arrangements should also be put in place to support management in their oversight of CF advisory activities.

Good practice that we observed



- One IM established an IPO review committee comprising of senior professionals with diverse backgrounds from the banking, legal, compliance, business standards and equity capital market functions. This committee oversaw key aspects of the IPO process, including conflict clearance, Know-Your-Customer (“KYC”) vetting, due diligence plan, and the outcome of the due diligence performed, including reviewing material issues and risks identified by the deal team.



Areas of weaknesses that we observed

1. Inadequacy in management oversight



Case examples

- One IM held only one management committee meeting prior to the submission of the listing application to SGX. There were no subsequent check-ins with the management committee on the resolution of red flags or new material issues uncovered since the meeting.

C. Governance, Compliance and Audit



Areas of weaknesses that we observed

1. Inadequacy in management oversight (cont'd)



Case examples (cont'd)

- There were also instances of a lack of escalation by the deal teams to the relevant management committees on matters such as an issuer's past and potential material breaches of laws and regulations, as well as red flags such as sanctions and fines imposed on the issuer's business partner and lawsuits against the issuer's major customers.
- Relevant information such as the deal team's assessment of the potential risks of the proposed IPO and supporting public adverse information on the financials of the issuer were not provided to the relevant management committee.
- One IM did not report the allegations in a poison pen letter and the additional due diligence it conducted to the relevant management committee for their decision, as required by the IM's policies and procedures.
- In one IM, there was minimal management oversight and P&Ps to govern the placement process. A new Customer X, had introduced a few other customers to subscribe for the placement alongside Customer X. All these customers proceeded to subscribe for the shares with the IM, and payments for their subscriptions were consolidated and made by a single customer. These subscriptions made up a substantial portion of the total value of the placement. The IM also accepted large subscription orders from existing customers, which was not consistent with their investment profile / history. Payments for the subscriptions were also received from third parties. These unusual payment patterns were not detected by the IM for any risk assessment or enhanced monitoring for potential money laundering and market manipulation concerns.

C. Governance, Compliance and Audit



Areas of weaknesses that we observed

2. Unclear roles & responsibilities and inadequacies in P&Ps

Case examples

- In one instance, there were no terms of reference for the management committee approving transactions that posed underwriting risks and/or reputational risks to the IM.
- There was a lack of clarity in the IM's P&Ps on (a) the delegation of approving authority for investments made by another function into a transaction for which the FI was acting as IM, (b) the roles and responsibilities of deal team members, and (c) the handling of poison pen letters.

3. Weakness in the compliance function (“Compliance”)

Case examples

- In one IM, Compliance only conducted conflicts of interests (“COI”) checks and was not involved in other aspects of CF advisory activities such as assessing the Money Laundering/Terrorist Financing (“ML/TF”) risks of potential issuers. Compliance’s reviews of CF activities were also found to be cursory. Compliance was also not represented at key committees such as the approving committee for new client mandates and subsequent fora on due diligence matters.
- In one instance, Compliance did not provide timely regulatory updates to management, such as amendments to listing rules and updates to the ABS Due Diligence Guidelines, when it was within their mandate to do so.

C. Governance, Compliance and Audit



Areas of weaknesses that we observed

4. Weakness in the IA function



Case example

- An IM did not conduct any audit on CF advisory activities although such activities were required to be subject to an audit cycle according to its risk rating. This was attributed to a lack of resources in the IA function.
- In another instance, the audit was not effective as it did not uncover any material findings, including those on due diligence and documentation found by MAS for the same samples that were also reviewed by the IA.

MAS' expectations



1

Management should exercise adequate oversight over the due diligence process. There must be clarity on the issues which are to be escalated to management, and a proper process for deal teams to escalate such issues to management for their deliberation. These issues should also be documented and tracked to ensure that they are resolved accordingly.

2

IMs should implement effective written policies on its operational areas to comply with [regulation 13\(b\)\(i\)](#) of the Securities and Futures (Licensing and Conduct of Business) Regulations. The roles and responsibilities of management members or committees and the deal team must be clearly set out in the IM's P&Ps for clear accountability. IMs should also periodically review their due diligence P&Ps, as well as conduct testing to assess the robustness of its internal controls and continued relevance of its procedures.

C. Governance



MAS' expectations (cont'd)

3

To act as an effective second line of defense in the company's risk management framework, Compliance should be vested with sufficient authority and representation, and be actively involved in discussions at relevant approval fora. Compliance should also conduct regular compliance reviews on business operations, and provide timely updates to management on compliance or regulatory matters.

4

IA, as the third line of defense, should perform regular risk assessments and audits of CF activities and be staffed with adequately skilled and experienced auditors to ensure good quality audit outcomes.

D. Due Diligence on Issuers



IMs should perform their role with rigour, due care and appropriate professional scepticism in order to assess the suitability of potential issuers for listing in Singapore. IMs should also consider the expectations on the conduct of IM's due diligence set out in Section B of this paper.

Good practice that we observed



- Detailed guidelines and checklists were developed to provide more guidance to the deal team in executing the due diligence plan.



Areas of weaknesses that we observed

1. Weakness in customer onboarding



Case examples

- In one instance, there was inadequate guidance provided in the P&Ps on mitigation of ML/TF risks such as when, and the extent of, additional due diligence measures that should be taken when red flags are detected.
- In one instance, there was delayed verification of the identity of the proposed issuer and other relevant parties beyond the threshold of 30 business days as recommended in the Guidelines to MAS Notice SFA04-N02 on the prevention of ML/TF.
- Some IMs did not adequately review and document the reasons for the dismissal of false hits when screening the proposed issuer and other relevant parties for adverse records.

D. Due Diligence on Issuers



Areas of weaknesses that we observed

2. Weakness in handling COIs



Case examples

- One IM had P&Ps to guide the conduct of COI checks on the business interests and directorships of board members, review committee members and CF advisory representatives. However, the company did not actively carry out such checks and only relied on voluntary self-declarations from the relevant parties to identify any potential COIs.
- One IM failed to identify potential COI concerns as it engaged a company (Company A) to conduct reviews for client onboarding even though the person from Company A was part of the IM's management committee responsible for reviewing submissions of listing applications.

3. Inadequacy in due diligence on issuer's controlling shareholders, directors and key management



Case examples

- One IM failed to conduct due diligence on two controlling shareholders of the issuer, being a fund and a fund manager.
- An IM did not conduct background checks on one executive director of the issuer, even though this director was granted with powers to take custody of company stamps and carry out the duties of a legal representative in the event the current legal representative was not able to perform his duties. The IM had rationalised that this director was not key to the issuer group as he was not involved in the daily operations of the group.
- One IM did not conduct adequate scrutiny on a group of potentially connected persons who had made large subscriptions during the placement process of the IPO.

D. Due Diligence on Issuers



Areas of weaknesses that we observed

4. Inadequacy in conduct of interviews and site visits



Case examples

- There were instances where (i) interviews with major customers and suppliers were conducted at the premises of the issuer; (ii) identities of interviewees were not verified; and (iii) interviews were conducted in the presence of issuer's officers.
- In another example, site visits to the issuer's material assets were not conducted.

5. Inadequacy in assessment or verification of material licences or material contracts



Case examples

- IMs did not conduct independent verification on persons providing critical services to the listing group. Some examples observed were (i) whether individuals held valid licences to practice; (ii) whether a vendor had a valid manufacturing licence.
- One IM did not verify the validity of the professional licences of staff employed by the issuer.
- One IM did not conduct any review on the validity of a trade concession (a material contract) granted to the issuer.
- Another IM did not review the existence of a financial security that was required under a material contract for the issuer.

D. Due Diligence on Issuers



Areas of weaknesses that we observed

6. Over-reliance on representations by issuers



Case examples

- Some IMs had solely relied on representations from the management of proposed issuers concerning Interested Party Transactions (“IPTs”) and had not adequately assessed or verified and documented their bases that the IPTs were conducted at arm’s length and on normal commercial terms.
- One IM did not verify that an unsecured loan was indeed provided by a third party and not a related party as represented by the issuer’s management. This was despite unusual circumstances such as the fact that the loan provider was a foreign non-bank entity.
- In another instance, there was no independent verification by the IM on the timing of the provision of security deposits, and on the existence of collateral underpinning the security deposit arrangements.

7. Failure to conduct further enquiries, or adequate assessment of potential red flags



Case examples

- In one case, there was a material financial dependency on the sponsor for the performance of the properties in a proposed REIT listing. There was limited public information on the sponsor and underlying properties. In particular, these properties were located overseas. Notwithstanding these circumstances, the IM did not make further enquiries on the financial standing of the sponsor.
- Another IM did not perform adequate assessment of the impact of changes in political conditions which were directly relevant to the issuer’s operating rights for its business.

D. Due Diligence on Issuers



Areas of weaknesses that we observed

7. Failure to conduct further enquiries, or adequate assessment of potential red flags (cont'd)



Case examples (cont'd)

- One IM did not perform adequate scrutiny on a group of large subscriptions to the IPO placement tranche despite knowledge that the investors were the vendors that had sold properties to the sponsor in the first instance, and the sponsor had in turn sold the properties to the proposed REIT

8. Inadequacy in review of offering documents



Case examples

- Errors in the offering documents were found, such as omission of past or present directorships of certain directors, erroneous disclosure of an individual as a board director, mistakes in the names of holding entities for certain properties and the corporate guarantor for a bank loan of the issuer.

D. Due Diligence on Issuers



MAS' expectations

1

There should be timely verification of the identities of customers. In addition, IMs should provide clear guidance to staff on how to identify potential ML/TF red flags during customer onboarding and properly document steps taken to address potential ML/TF risks arising from the IPO transaction.

2

IMs should conduct proper checks, prior to the commencement of the transaction, to identify and mitigate potential COI for key parties working on the transaction.

3

Adequate due diligence should be conducted on key personnel of the potential issuer such as directors, executive officers, founding as well as intended controlling shareholders. Where shareholders are corporate vehicles, due diligence should be extended to the natural controlling persons of such entities. This allows the investing public to better assess the issuer and make an informed decision on the investment.

4

Identities of interviewees should be verified prior to conducting interviews (e.g. by asking for their name cards, looking up the issuer's website or other sources of information and conducting interviews at the premises of the customer or supplier). The conduct of interviews with staff of adequate seniority from major customers or suppliers at their work premises also allows the IM to corroborate material matters such as the business volume between issuer and business partner. Conducting such interviews without the presence of the issuer's officers reduces undue influence from the issuer, and hence enhances the objectivity and independence of the views provided.

D. Due Diligence on Issuers



MAS' expectations (cont'd)



5

Site visits should be conducted on key assets of the issuer so as to ascertain the existence and quality of the issuer's assets and provide insights to the level of business activity for corroboration with the issuer's historical and future performance (e.g. based on the physical size of the factory and/or business activities observed on-site).

6

IMs should verify the validity of material licences held by the issuer and its key service providers, as these are the basic hygiene factors for the business operations of the issuer. IMs should also verify key aspects of contracts material to the issuer.

7

IMs should not solely rely on representations from proposed issuers for material matters such as potential IPTs and financial arrangements that may have an impact on the merits of the proposed listing. As set out in Section B, the extent of due diligence to be conducted depends on various factors, and IMs should exercise professional judgement in determining this. Independent verification of IPTs could be conducted via benchmarking of fees charged by the interested parties vis-à-vis third parties. Independent verification of key financial arrangements could be conducted through reviewing supporting documents and verifying with third parties as needed.

8

IMs should exercise professional scepticism and be alert to potential red flags that surfaced during the IPO process. There should be follow up enquiries and independent verification to address such potential red flags.

9

IMs should exercise due care in reviewing offering documents to ensure that accurate information is provided to investors.

E. Experts and Advisers³



Experts and advisers play an important part in the due diligence process. IMs should take steps to satisfy themselves that they can rely on the findings and opinions of such third parties, such as assessing that these parties are suitably qualified and independent, and that the scope of services provided by these parties is appropriate for the purpose of the IPO transaction.



Areas of weaknesses that we observed

1. Inadequacy in engagement of experts and advisers



Case examples

- Some IMs did not have formal P&Ps on the selection of experts and advisers.
- Some IMs did not document the suitability assessment of the experts and advisers engaged by the proposed issuer.
- Some IMs did not check if there were any potential COIs before engaging the experts and advisers.
- Some IMs did not review or document any review on whether the scope of work to be undertaken by the experts and advisers is appropriate.

³ Experts and advisers in this paper refer to third parties engaged to assist in the due diligence process, such as accountants, auditors, legal advisers, valuers and private investigators.

E. Experts and Advisers¹



Areas of weaknesses that we observed

2. Lack of due care and follow-up in review of expert and adviser reports



Case examples

- One IM failed to detect gaps in the periods covered by certain screening checks, as well as in specific financial information presented in the private investigator (“PI”) report.
- Another IM failed to follow up adequately on discrepancies between the legal due diligence report and the issuer’s financial statements relating to the value of a material contract of the issuer group. In this case, the auditor had recorded a value in the financial statement but the legal adviser was unable to ascertain the value of the contract.

E. Experts and Advisers



MAS' expectations



1

IMs should assess the suitability of experts and advisers appointed to conduct any aspect of due diligence and upon whose work the IMs will be relying on. In assessing their suitability, IMs should perform COI checks, in addition to considering other factors such as their experience and qualifications, to ensure that they can be reasonably relied on to carry out the specific due diligence work. IMs should also review the terms of engagement of experts and advisers from the outset and consider whether the scope of work to be undertaken and resources to be applied by them are appropriate in the specific circumstances. The bases for appointing experts and advisers should also be documented by the IMs.

2

IMs should exercise due care and diligence in identifying and following up on gaps, inconsistencies and potential red flags arising from experts' and advisers' reports.

F. Record Keeping

Sufficient documentation of due diligence work performed by the IM serves to demonstrate that the IM has discharged its duties and obligations under the relevant rules and regulations.



Areas of weaknesses that we observed

Incomplete or absence of documentation



Case examples

- Many IMs were unable to produce records to demonstrate that they had conducted appropriate due diligence and taken actions to remediate issues and red flags. Minutes of material discussions with the issuer's management and professionals regarding the issuer's internal audit findings, verifications of inconsistent or concerning information in PI reports, and documentation on resolution of red flags and COIs were not maintained.
- One IM did not keep minutes of verification meetings between the IM, proposed issuers, lawyers and other parties.
- Some IMs did not maintain basic details for interviews conducted with the proposed issuer's key customers and suppliers such as the list of attendees, full name and designation of attendees, date, and location of the interview.
- Some IMs failed to document decisions taken by the relevant management committees and required follow-up actions.
- In onboarding some placees as new customers, one IM did not adequately document its bases for dismissal of false hits arising from screening these placees against its databases for adverse records.

F. Record Keeping



MAS' expectations



1

IMs should maintain proper records of the due diligence work conducted. This includes records of key discussions both internally within the IM and with external parties (such as the proposed issuer, key suppliers and customers, and experts and advisers), and internal management approvals, and the bases of key decisions made.

IMs should also keep proper records of the onboarding process, including for places during the placement process and actions taken to address potential ML/TF risks that may arise.

G. Conclusion



MAS' thematic inspection of IMs showed that there is much room for improvement in the conduct of IMs' advisory activities for IPOs, as well as IMs' placement activities. IMs should periodically review their internal controls and P&Ps and strengthen their management oversight and control over such activities. MAS will provide further guidance (where appropriate) to improve industry practices for the CF advisory sector in Singapore.

