Risk Management

The Sembcorp Marine Group continued its risk management efforts in support of its objectives and strategies which would inevitably entail participation in markets beyond the familiar and secure home base in Singapore. While the risks associated with such endeavors are manifold and highly consequential, the Group is aided by a sound risk management framework to effectively mitigate these risks.

To strengthen and ensure continued relevance of its enterprise risk management (ERM) framework in light of evolving regulatory requirements and guidance, the Group has, since 2012, been partnering external specialists who are providing valuable insights and recommendations to enhance the existing framework. The specialists' study covered the Group's internal control system and risk management policies, procedures, processes and limits, which are all part of the ERM framework. It also includes the governance structure comprising risk committees which focus on their respective significant risk areas of concern to the Group. In these committees, the directors and management work together to formulate and implement risk management strategies, policies, procedures and plans, in support of the Group's overall business processes and operations.

Risk Governance Structure

The Board Risk Committee (BRC) assists the Board of Directors to drive risk governance in the Group and communicate an appropriate tone from the top to all levels of the Group. This entails overseeing the design, implementation and monitoring of the Group's risk management and internal control systems as well as assessing the adequacy and effectiveness of these systems which cover strategic, operational (including IT), financial and compliance risks. The BRC engages in regular reviews and discussions with management staff from the Group's corporate functions and strategic business units at the committee meetings, covering the Group's top risks and treatment plans, projects and health, safety, security and environment risks amongst others. A total of four BRC meetings were held in the year, supplemented with other engagements via electronic mail and teleconferencing.

The management, through the Enterprise Risk Management (ERM) Committee, is responsible for identifying, assessing, managing, monitoring and reporting the key risks faced by the Group to the BRC.

Chaired by the President & CEO and supported by the Group Chief Risk Officer, this committee comprises the strategic business unit heads, their chief risk officers and management staff who are appointed as champions of key risk areas. The ERM Committee reviews risk issues at both the strategic business unit and Group levels. The areas of review cover risk policy matters, risk profiles and treatment plans as well as other Group risk initiatives.

Supporting the ERM Committee are sub-committees which look after their respective areas such as Health, Safety, Security and Environment (HSSE), Human Resource, Project Risk Management, Finance, Information Technology, Procurement and Critical Assets, amongst others. These sub-committees are headed by designated qualified persons and members are the domain experts from the strategic business units and the Group's corporate functions.

The organisation of the Group's risk governance structure is illustrated as follows:

Key Risk Management Initiative Highlights

The Group reviews its risk policies, profiles and plans annually. Emerging risk trends and issues are raised and discussed at risk meetings and external experts called in to share their knowledge and experience with management. These are some of the core activities set out in the Group's annual risk management workplan. Other initiatives carried out during the year included:

- Extension of the risk and governance assurance framework established in the previous year to the Group's overseas shipyards, with representatives from Group Risk Management and Internal Audit making field trips to Brazil and Indonesia to facilitate the process
- A calibrated Group-wide survey to evaluate the Group's risk culture. The respondents covered Sembcorp Marine directors as well as representative numbers of senior and middle management staff from all the strategic business units and overseas shipyards
- Internal controls awareness sessions by Group Risk Management and Group Internal Audit to educate employees on the fundamentals of corporate governance, internal controls, risk management and internal audit
- An anti-corruption training session was conducted by external consultants for the ERM Committee
- Development of formalised Group Risk Appetite statements

Key Risks and Mitigation Strategies

The Group's key risks were identified as part of an annual risk review exercise which factored in inputs from the strategic business units and overseas shipyards and also included development of the mitigation measures. These are set out in the following sections.

The year in review saw a familiar continuation of global trends and happenings – uncertain and fragile global economy, extreme weather events, political unrest and acts of terrorism. Closer to home, Singapore experienced its worst haze which affected outdoor operations. The tightening of foreign worker policy by the government led to a tighter labour supply situation. These are some of the factors that were considered in developing the Group's top risk profile.

Strategic Risks

Strategic risk considerations impact the Group's strategies and plans to grow its business and operations in Singapore and internationally. They typically encompass business environment, customers, markets, industries, competition, technology and new business initiatives (in terms of products and services of the oil & gas value chain). Discussions were held at both the ERM and BRC Committee meetings and risk factors were escalated to the Board of Directors at the annual strategic planning meeting.

External Environment Risks

Key risks in this category include commodity market volatilities; global trade and economy; stability of the global financial and banking systems; foreign exchange fluctuations; political risks; regulatory landscape; and natural disasters. Risks of such nature have far-reaching impacts which affect the Group and its customers, suppliers, vendors and other business partners.

Environmental scanning is an ongoing process by management which identifies potential and emerging risk exposures resulting from events and developments in the regions and markets which the Group operates in. These exposures are evaluated in terms of impact and likelihood and used for subsequent response planning. Recognising that external environment risks are inherently volatile, unpredictable and usually cannot be completely eliminated, the Group adopts the approach of mitigating them to as low as reasonably practicable with due consideration given to achieving appropriate risk/reward balances.

Project Management Risks

The Group's core business revolves around the projects in its order book. The Group has consistently demonstrated good project risk management through an established track record of safe and timely project deliveries, meeting budget, quality and environmental requirements. This applies across the entire project management process which starts from tendering, contract negotiation and upon award, the execution of engineering, procurement, construction, commissioning and delivery.

Third party risks in the form of non or poor performance of contractors, suppliers or vendors could affect the Group's ability to execute its projects as planned, thereby causing delays. This could happen when substitute manufacturers are limited, especially for specialised equipment. To this end, the Group has put in place, processes for selection of third parties with pre-defined criteria and constant monitoring and assessment which allow for early warning and timely actions.

The drillships for Sete Brasil had been progressing satisfactorily and the Group continues to proactively manage the risks in contract execution. The construction of the Estaleiro Jurong Aracruz shipyard in Brazil is progressing well and remains on track to commence initial operations in the second half of 2014.

The Project Risk Management Committee which is chaired by the President & CEO provides a platform for the strategic business units to report and discuss material project risk matters, including project schedules, costs, work variations, financial and contractual issues.

Human Resource Risks

The Group believes that employees are valuable assets that enable the achievement of its objectives and strategies. With the commencement of operations at the Sembmarine Integrated Yard @ Tuas in August 2013 and the Estaleiro Jurong Aracruz shipyard in Brazil in the second half of 2014, there is a high demand for additional human capital to run these operations, notwithstanding the advanced automation features and optimised facilities in these yards. Key risks identified include availability of skilled labour, staff turnover, management succession, work-life balance as well as compensation and benefits. Measures have been put in place to address the above-mentioned risks and others. The Group's human resource activities are discussed in detail in the Human Capital section of this report.

Financial Risks

The Group's international presence and worldwide clientele inevitably exposes it to the various financial risks arising from developments within the global financial market. Policies and procedures covering key areas – including treasury, foreign exchange, credit, accounting, inter-company transactions and others – have been established and implemented throughout the Group to mitigate the associated risks. These policies also set out approval limits for significant transactions and guidelines to minimise cost of capital, adverse effects of fluctuations in foreign currencies and interest rates on income as well as to ensure that sufficient funds are available to meet financial obligations and operational needs.

The Finance Committee, a sub-committee of the ERM Committee, looks into the areas of financial system integrity, regulatory reporting, accounting, risk management and compliance systems, including internal and external audit issues. Chaired by the Group Chief Financial Officer, the committee comprises key finance personnel from the strategic business units and the corporate functions of treasury, tax, internal audit and risk management.

The Group's financial risk management is discussed in detail in Note 36 to the financial statements.

Health, Safety, Security and Environment Risks

The Group emphasises and places great importance on providing a safe and healthy work environment for its customers, employees, contractors and the community. The Group Health, Safety, Security and Environment Committee, which comprises the key relevant representatives from all the shipyards is responsible for implementing the Group's four safety strategic thrusts which guides the Group's activities towards its vision of zero incidents. The committee also monitors and reports the Group's safety performance and other material related matters regularly to the ERM Committee and the BRC.

The Workplace Safety and Security section of this annual report provides more information on the principal activities carried out during the year.

Information Technology Risks

The Group Information Technology (IT) Committee, formed in 2012, is chaired by the Senior Vice President, Group Management Information Systems and comprises key IT personnel from the strategic business units.

The committee's mandate is to design and implement the Group's IT governance framework and strategies including IT risk management and controls. Key IT risk issues are escalated to the ERM Committee for discussion.

During the year, the committee reviewed and updated the Group IT risk profile, reviewed Group IT policies, infrastructure readiness for integration and process harmonisation, and developed security configuration baselines for network devices.

Critical Assets Risks

Certain assets are important enablers of shipyard operations. The Group Critical Assets Committee, a sub-committee of the ERM Committee, is tasked to raise standards in upkeeping critical assets employed in the Group and build capabilities for sound and safe operation of such assets. The major categories of assets identified by the committee are power and utilities; material handling equipment; docks and quays; workshops, and launching facilities.

During the year, the committee identified and documented applicable laws, rules, regulations and Codes of Practice for the Group's critical assets and began development of best practice manuals for each of the five categories of critical assets defined at the Group level.

The strategic business units have established policies and procedures for managing their critical assets which cover operations, performance measurement and tracking, maintenance, servicing and certification.

Fraud and Corruption Risks

The Group takes a zero tolerance stance against fraud and corruption which is articulated in the Group fraud risk management and anti-bribery policies. Acts of fraud or corruption committed by employees or parties that provide dishonest or unfair benefits to themselves or related parties to the detriment of the Group are strictly not tolerated. The perpetrators will face consequences, such as disciplinary warnings and termination of employment or other contractual relationships, and will be reported to the appropriate law enforcement or regulatory body.

During the year under review, there were zero confirmed incidents of corruption and corruption related termination/non-renewal/disciplinary cases, for both employees and business partners. Neither were there public legal cases regarding corruption brought against the Group or its employees.

In the Fraud Risk Management (FRM) framework, the Group had identified violation of anti-bribery and corruption laws such

as the United States Foreign Corrupt Practices Act (FCPA) and UK Bribery Act as a significant risk in the fraud risk assessment. To this end, the Group's FRM policy and requirements are communicated across its global operations to key business partners including customers, suppliers and contractors. The FRM policy and procedures are reviewed at least once every two years to maintain its relevance to the Group's business and operations. Management compliance to the FRM policy is audited by Group Internal Audit who provides an independent review of the effectiveness and adequacy of controls in place.

Augmenting these frameworks and the Group-wide whistle-blowing structure, Group Risk Management and Group Internal Audit continued to conduct a series of in-house training sessions to educate staff on risk governance and internal controls, including the corresponding Group policies. These trainings are also extended to employees in overseas yards. To date, over 75 per cent or more than 2,000 staff holding a supervisory or equivalent position and above had attended these sessions. An anti-corruption training session was conducted by external consultants for management staff in the ERM Committee in 2013.

An effective mitigation means utilised by the Group to combat fraud and corruption risks is through its whistle-blowing policy which provides an open channel to surface any potential wrongdoing and the mandate to subsequently evaluate and investigate independently every reported case based on its merits.

Investment Risks

Some of the ways in which the Group grows its business are through acquisition of business entities or operating assets, development of new capacities and expansion of its existing capabilities, facilities and activities. Investment activities, starting from the identification of targets to due diligence exercises (including risk assessment), are supported by a team of experienced managers and complemented by external professionals for specialised services. Business proposals are risk assessed and evaluated by senior management before deliberations by the Board of Directors.

Business Continuity Risks

To mitigate its business continuity risks, the Group has in place a Business Continuity Management (BCM) framework that complements its ERM framework.

The Group BCM Policy, previously based on the Singapore Standard for BCM (SS540), has been updated to incorporate elements of the ISO 22301 standard for BCM as well as to refine its existing crisis reporting procedures to ensure timely reporting and clarity of roles and responsibilities during a crisis.

The four base disaster scenarios identified for business continuity planning are major fire and explosion; prolonged power outages; infectious disease outbreaks; and major information technology disruptions or failures.

The internal controls awareness sessions for employees by Group Risk Management and Group Internal Audit also covered BCM where recent events were identified as case studies to share BCM learning points.

Other Group-wide Risk-based Activities

In addition to the aforesaid risk mitigation strategies, the Group has other risk management activities in place including Control Self Assessment and insurance programmes.

Control Self Assessment

The Group's Control Self Assessment (CSA) programme, which was established in 2008, is part of the overall Group Governance Assurance Framework. CSA processes are linked to identified controls for key risks to provide added assurance, complementing the external and internal audits.

Besides raising awareness among staff on risks and controls, the CSA programme also promotes ownership and accountability through identifying control owners for respective processes. Corrective actions taken for control lapses detected are tracked and reported to management till completion.

Appointed CSA managers in the business units work together with Group Risk Management and Group Internal Audit. Quarterly updates on the programme are also reported at the BRC and ERM Committee meetings.

All the Singapore strategic business units started their CSA implementation in 2008, adding new CSA processes each year to reach a total of 15 per unit in 2013. The programme has been extended to the overseas shipyards in 2013 and they will start with five processes for 2014.

Insurance

Insurance is used as a means of risk transfer where necessary or when it is mandated by legislation (eg. Work Injury Compensation Act) or contractual requirements. Another application is providing coverage for the Group against foreseeable events that may cause potential catastrophic financial losses. The approach taken by the Group is one that seeks to balance cost benefits with its risk appetite, risk management capabilities and self-insuring capacity.

Insurance is procured at the Group level, through pooling of the strategic business units' common insurance needs, hence achieving economies of scale. The insurance department works closely with insurance brokers to obtain optimal coverage for the Group at competitive prices.

During the year, the Group Insurance Committee reviewed the basis for sum insured for the Group's critical assets, integrated the strategic business units' public liability and motor fleet policies and consolidated the employees' benefit insurance program under a flexi-plan scheme.