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Greater scrutiny by auditors on the cards

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KUALA LUMPUR: The International Auditing and Assurance Standards Board (IAASB) is introducing a suite of new and amended auditing standards that will put Malaysian companies under greater auditor scrutiny for audit periods ending Dec 15, 2016 onwards. The new and amended standards include a revision of the auditor's report in the financial statements that will help enhance communication between auditors and investors.

This will be done through the inclusion of a section on "key audit matters" in the audit report which would refer to those matters that, in the auditors' judgement, are of most significance in the audit. The auditors will then be expected to explain how the key audit matters raised are addressed in the audit. The inclusion of the key audit matters will be compulsory for public listed companies.

According to PricewaterhouseCoopers Malaysia assurance leader Pauline Ho, the amendments will make the audit report more informative and insightful.

"[The inclusion of the key audit matters] provides an avenue for shareholders to understand the key areas discussed with the audit committee who represents the board of directors of an entity, and will also prompt companies to provide better disclosure around these key areas discussed to ensure that their perspective is shared clearly with the shareholders," she said in an email response to *The Edge Financial Daily*.

Chairman of the Malaysian Institute of Certified Public Accountants (MICPA) Accounting and Audit-



ing Standards Committee Sukanta Dutt said the amendments will be a game changer for auditor communications with investors.

"The auditors' report has mostly been boilerplate unless there has been a need to issue a qualified report or other form of modified report. The requirement for a key audit matters section will mean that public company auditors will need to communicate on matters of most significance to their audit of financial statements," he said in a March 27 statement by MICPA.

The new and revised auditor reporting standards are set to be effective for Malaysian audits of financial statements for periods ending on or after Dec 15, 2016.

Of late, reports have surfaced questioning the transparency of auditors in their conduct of audits, such as in the case of 1Malaysia Development Bhd (1MDB), in which its former auditors KPMG Malaysia were alleged by some to have failed

Ho says the amendments to auditing standards will make the audit report more informative and insightful.

to act with integrity in their audit of the debt-laden firm.

However, KPMG later defended their audit of 1MDB, stating that the conduct of their audit was in compliance with international standards for auditing.

On whether the amended audit report would enhance the transparency of the audit, Ho said new standards will allow auditors to demonstrate more visibly the value and relevance of the audit.

"[In the amended audit report], there is a new description of management's responsibility for assessing the entity's ability to pay its liabilities when due and to continue its operations without interruption known as the 'going concern' basis of accounting.

"The report also includes the auditors' views as to whether the use of the going concern basis is appropriate, as well as disclosing any matters relating to going concern that will enhance transparency in reporting," she said.

However, MICPA president Datuk Abdul Rauf Rashid said the implementation of the revised audit report will not be a straightforward process for auditors, listed companies, and the capital market as a whole.

"There are challenges, and potentially significant implications which will require careful consideration and planning by all parties

and stakeholders, including regulators, directors, financial statement preparers and auditors," he said in the MICPA's statement.

Ho opined that the implementation of the revised audit report will bring both challenges and opportunities for auditors, audit committees and managements of public listed entities.

"Some pressures to companies include the sharing of information which they feel is sensitive — an example would be a legal case involving them and positions taken by the company to support its case.

"Auditors, on the other hand, would have to ensure that key audit matters are articulated clearly so as to not give a wrong impression over a particular issue ... certainly, this will take more time and effort," she said.

Ho added that while shareholders may value the additional information, management or audit committee boards may not necessarily agree and feel that it is an added cost of compliance.

However, she said Malaysia has decided to adopt international standards for accounting and auditing, hence it should respond accordingly to the call for more insight, transparency and readability of auditor reporting, as per the IAASB's practice.

"We should similarly adopt the practice in Malaysia to better communicate the value of the audit," said Ho.

The new and amended auditing standards have been implemented in the United Kingdom where, Ho said from the experience there, investors are keen to hear from auditors the key areas of risk companies face.

AUDITOR REPORTING LANDSCAPE FACES A CHANGE

A suite of new and amended Auditing Standards is set to change the auditor reporting landscape for public listed companies. Introduced by the International Auditing and Assurance Standards Board (IAASB) after a six year process informed by academic research, public consultations and stakeholder outreach, the new requirements respond to calls for more informative and communicative audit reports in the public interest.

Among the most significant of the new requirements is for the inclusion in the auditor's report of a section on 'Key Audit Matters' ('KAMs'), i.e. those matters that, in the auditor's judgment, were of most significance in the audit. These could include areas of higher assessed risk of material misstatement in the financial statements, those requiring significant auditor and management judgement and estimation uncertainty, and the effect on the audit of significant events or transactions that occurred during the financial period. KAMs could further include areas in which the auditor encountered significant difficulty during the audit or with respect to obtaining sufficient appropriate audit evidence; circumstances that required significant modification of the auditor's planned audit approach; and the identification of a significant deficiency in internal control. The auditor would be expected to explain how the Key Audit Matters reported on were addressed in the audit.

Other requirements introduced include stating the respective responsibilities of management and the auditor for assessing going concern (i.e. the entity's ability to continue in business in the foreseeable future), and challenging the adequacy of disclosures when going concern is a "close call".

The auditor's report will also require the inclusion of an affirmative statement about the auditor's independence and fulfilment of relevant ethical responsibilities. Additionally, new requirements have been introduced for enhanced description of the auditor's responsibilities and key features of an audit, and the disclosure of the name of the audit engagement partner.

In its recent announcement of the new requirements, the IAASB, stated that enhanced auditor reporting is critical to influencing the value of the financial statement audit and to the continued relevance of the auditing profession. The IAASB intends for the new requirements to result in an auditor's report that increases confidence in the audit and the financial statements. In addition to increased transparency and enhanced informational value of the auditor's report, the IAASB believes that the changes will also enhance communications between investors and the auditor as well as between the auditor and those charged with governance, i.e. Boards and Audit Committees. The IAASB further believes that management and those charged with governance will direct increased attention to financial statement disclosures to which reference is made in the auditor's report. The renewed focus of the auditor on matters to be communicated is expected to also indirectly result in increased professional scepticism during the audit.

The IAASB is an independent standard-setting board established under the auspices of the International Federation of Accountants. The primary beneficiaries of the IAASB's work on auditor reporting are expected to be investors, analysts and other users of the auditor's report. The reporting of KAMs is expected also to assist users of financial statements in understanding the audited entity and to provide a basis to further engage with management and those charged with governance.

The Malaysian Institute of Certified Public Accountants (MICPA), in recognizing the importance of the new and revised Auditor Reporting standards and the urgency in preparing the business community and other stakeholders in Malaysia for the changes that they need to implement to comply with these new requirements, is leading and participating in a joint working group set up together with the Malaysian Institute of Accountants to address the implementation of, and transition to, the new standards.

Co-Chairman of the joint working group and Chairman of the MICPA's Accounting and Auditing Standards Committee, Sukanta Dutt says "the new requirements on Key Audit Matters would be a game-changer in auditor communications through the audit report on financial statements of public companies." Sukanta added that "whereas hitherto the auditor's report has mostly been boiler-plate unless there has been a need to issue a qualified report or other form of modified report, the requirement for a Key Audit Matters section will mean that public company auditors will need to communicate in the ordinary course regarding matters of most significance to their audit of the financial statements." He further said that "such commentary should enhance the understanding of audit and related reporting issues, of users of these financial statements."

MICPA President, Dato' Abdul Rauf Rashid, added that "implementation of the new and revised Auditor's Report will not be a straight-forward process to auditors, the listed companies and the capital market, as a whole. There are challenges and potentially significant implications which will require careful consideration and planning by all parties and stakeholders including regulators, directors, financial statement preparers and auditors."

The new and revised Auditor Reporting standards will be effective for audits of financial statements for periods ending on or after December 15, 2016.

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