

How it Impacts Audit Committee

7 April 2022







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Introduction

- What AOB does with Findings
- What Directors of PIEs should do with Findings



Common Findings and Observations

- Case study 1
- Case study 2



Annual Transparency Report

- AC's role
- Reporting requirements
- Background
- Contents of the Report
- AQIs



Introduction



What AOB does with Findings – AOB's Process





What AOB does with Findings – Before commencement



Risk-based selection approach

Use of data analytics to identify specific high risk areas

Significant accounting, auditing/other developments

Specific areas of industry or market concerns

Market capitalisation of PLC clients audited by audit firms

The AOB's risk assessment of registered and recognised audit firms



What AOB does with Findings – After completion





Conclusion of inspection

The AOB
issues Draft
Inspection
Report to
audit
firm on details
of findings

Written
responses
by audit
firm within
timeframes
prescribed by
the AOB

Analysis of audit firm's response and presentation of findings to the AOB Board The AOB Board's approval and decision

Issuance of
Final Inspection
Report to audit
firm

Remediation by audit firm within timeline agreed with the AOB

What AOB does with Findings – What is a Finding?



Firm reviews



Relates to compliance with the requirements of the International Standard on Quality Control 1 (ISQC 1)

Engagement reviews

- Relates to compliance with International Standards on Auditing (ISA)
- Individually critical deficiency, which may have an impact on the basis of audit opinion
- Pervasive issue where the impact cannot be easily quantified

Findings do not necessarily suggest that the affected PIE's financial statements contain a material accounting error or its controls in respect of financial reporting are weak

What AOB does with Findings – Actions that could be taken



IMPOSITION OF SPECIFIC REMEDIATION MEASURES

- Incorporate or revise the relevant audit procedures in their audits of the PIEs for the ensuing financial year
- Evaluate the impact of these audit procedures to the audited financial statements for the financial year inspected

2

REFERRALS

The related PIEs are

referred to the SC's Corporate Surveillance Department for further action to be taken on the PIEs, where relevant 3

SHARING OF FINDINGS WITH PIEs

 As provided under Section 31ZD(3) of the SCMA, the AOB may share its findings with PIEs relating to inspected audit engagements 4

ENFORCEMENT

- Inspection findings are referred to the AOB's Enforcement, Regulation and Quality Assurance (ERQ) Department for evaluation and review
- AOB may take enforcement actions against the audit firms and individual auditors

5

IMPOSITION OF ADDITIONAL REGISTRATION CONDITIONS AND INTERIM MEASURES

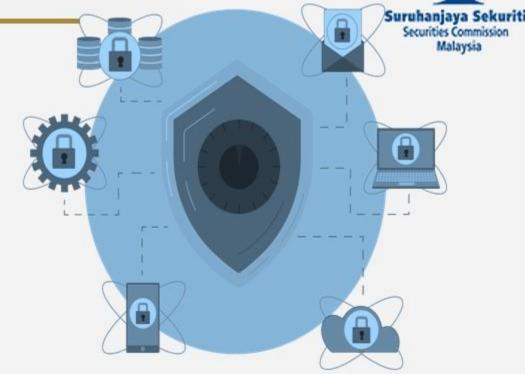
 Depending on the severity and pervasiveness of the findings, while enforcement proceedings are ongoing, additional registration conditions could be imposed on audit firms and individual auditors as interim measures to safeguard audit quality and to protect public interest.

What Directors of PIEs should do with Findings

Directors and Audit Committees have to be vigilant on an expanding range of issues and risks, including those relating to complexities of financial reporting caused by COVID-19

Continuous engagements with their auditors are essential to deal with these issues and to discuss the continuing impact of COVID-19, particularly at the earliest stage of the financial reporting & auditing process

In the area of Going Concern (GC) in particular, directors and Audit Committees must ensure that significant judgements made to reach that conclusion are sufficiently disclosed, as follows:





IFRS EDUCATIONAL MATERIAL

- Significant doubts about GC but <u>mitigating actions judged sufficient</u> to make GC appropriate, with <u>no Material Uncertainty Related to Going</u> <u>Concern (MUGC)</u>;
- Significant doubts about GC but <u>mitigating actions judged sufficient</u> to make GC appropriate. However, <u>MUGC remains after considering mitigating actions</u>.



Securities Commission Malaysia

Common Findings & Observations



Common findings & observations



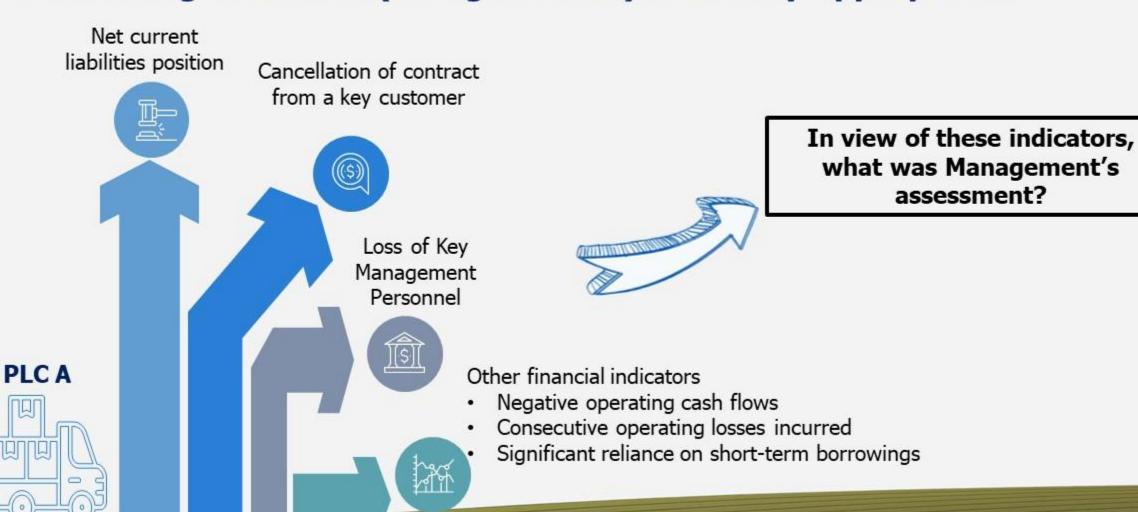
2020	2019
1 Audit Sampling	1 Audit Sampling
2 Accounting Estimates	2 Accounting Estimates
3 Revenue Recognition	3 Auditor's Report
4 Fraud Procedures	4 Fraud Procedures
5 Inventory Procedures	5 Group Audits

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Case Study 1



Accounting estimates (Going Concern): Are They Appropriate?



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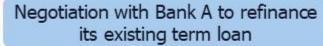
Case Study 1 (cont.)



Accounting estimates (Going Concern): Are They Appropriate?

Management's Assessment

Proposed issuance of redeemable convertible unsecured loan stocks (RCULS) subsequent to year end

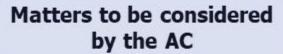


Utilisation of remaining unutilised Revolving Credit (RC) facility granted by Bank B

Financial support from its lenders and major shareholders

Potential candidates to replace the loss of Key Management Personnel will turnaround the PIE

New project in the pipeline for major subsidiary will improve the financial position of the PIE



Yet to be approved by the Board and released to be published as at the date of the auditor's report

No evidence to support management's representation on the status of negotiation

Unutilised RC insufficient to cover the PIE's net current liabilities

No letter of financial support obtained

Assessment performed based on qualitative factors which could not be corroborated

Cash flow projections were not prepared by the management to support the assumption



Common Observations

- Accepting management's representations without obtaining sufficient evidence to support such representations; and
- Insufficient assessment on adequacy of disclosures in the AFS in relation to material uncertainties surrounding the going concern assumption, and whether a modification to the audit opinion should be considered.
- Insufficient audit procedures performed to verify the reliability of the underlying data included in the cash flow projections; and
- Insufficient audit procedures performed to assess the reasonableness of assumptions used by the PIE management.







Case Study 1 (cont.)



What Should the AC Do?



Ensure sufficient challenge on PIE management's assumptions used in the cash flow projections



Ensure proper evaluation of the reasonableness of data source/ inputs used in the cash flow projections



Ensure assessment performed on the reliability of source documents provided by PIE management



Case study 2 - Background

Understanding fraud

What is fraud?

Intentional manipulation of financial statements to create a false appearance of corporate financial health

Why fraud takes place?



Suruhanjaya Sekuriti Securities Commission Malaysia

Common types of fraud

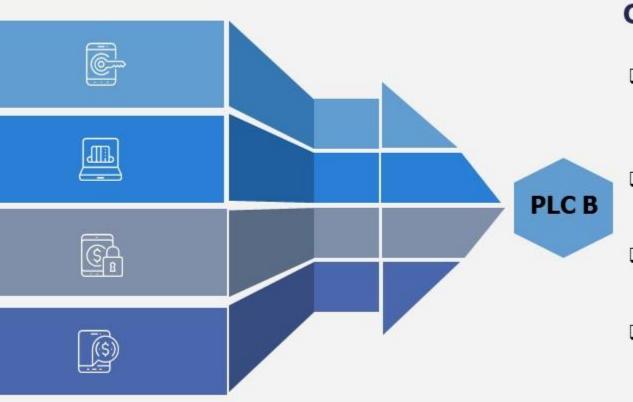
- Misappropriation of Assets
- Invoicing Fraud
- Expense Reimbursement



Case study 2

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How do we detect potential fraud?



Observations

- 10% of manual journal entries during the year were not approved as the Finance Manager responsible was not aware of the required approval process
- Documents to support the journal entries were not attached as the Finance Manager did not review the entries posted
- System access to journal posting was shared with individuals in the procurement department
- Dual signatories were not obtained on significant \$ payments made to vendors





What Should the AC Do?



Pay attention to internal control weaknesses in the financial statement close process



Ensure that relevant audit procedures such as management override of controls and journal entry testing have been adequately performed



Ensure constant and open communication with the auditors during the course of the audit





Annual Transparency Reporting



Annual Transparency Report – AC role





Establish criteria to guide decisions on the appointment and reappointment of the external auditor.



If the audit firm is not required to issue an Annual Transparency Report, the Audit Committee is encouraged to engage the audit firm on matters typically covered in an Annual Transparency Report

Annual Transparency Report – Reporting requirements



6 months after FYE 4 months after FYE 2021 2022 2019 2020 Deferred due to COVID-19 Required to publish their Revised implementation year · Initial implementation of The AOB introduced the ATR ATR on their websites within the ATR Required to share their ATR four months after the The first transparency

report is required to be issued by audit firms for fiscal year ending on or after 31 December 2019

- with the Audit Committees of their PIE audit clients
- The transparency report is required to be issued by audit firms for fiscal year ending on or after 31 December 2020.
- respective audit firm's fiscal year-end
- · A copy of the ATR is to be submitted to the AOB upon publication of the report on the firm's website

Annual Transparency Report - Background





Provide useful information for investors and audit committees to facilitate decision making on the appointment of auditors

Promote competitive behaviour among audit firms on audit quality Increase investor confidence in the role of the auditors as independent gatekeepers for reliable audited financial statements in Malaysia

- ➤ Audit firms with > 50 PIE audit clients
- The total market capitalization of above RM10 billion (PIE clients)

- PricewaterhouseCoopers PLT
- ➤ Ernst & Young
- ➤ KPMG PLT
- ➤ Deloitte PLT
- >BDO PLT
- ➤ Crowe Malaysia PLT
- ➤ Grant Thornton Malaysia
- ➤ Baker Tilly Monteiro Heng PLT

*As at 31 December 2020

Annual Transparency Report – Contents of the Report





Legal and governance structure

- Legal and ownership structure
- Governance and leadership structure
- Network and structural arrangements
- Disclosure on partners with substantial equity in the partnership
- Disclosure on family relationship between partners undertaking leadership role or holding substantial equity in the partnership with other partners of the audit firm



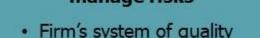
Measures taken by the audit firms to uphold audit quality and manage risks

- Firm's system of quality controls
- Accountability framework for partners
- Compliance monitoring
- Risk management process



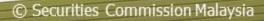
Information about the audit firm's AQI

- Comprises 15 minimum
 AQIs that must be
 included in the report
- Audit firms may disclose any other relevant AQIs monitored by the firm in addition to the above
- AQI statistics to cover a 3year period









Mandatory AQIs for Transparency Report





- ☐ Ratio of the average number of PIEs per partner
- ☐ Ratio of the average number of entities related to PIEs per partner
- ☐ Ratio of the average number of non-PIEs per partner
- ☐ Proportion of fee income derived from audit clients segregated into statutory audit, other assurance services and services provided by the non-audit practice
- ☐ Proportion of fee income between audit practice and non-audit practice

- ☐ Headcount of the audit personnel
- ☐ Headcount of audit personnel with professional qualifications
- ☐Turnover rate for audit personnel
- ■Average years of experience of audit partners and audit staff

- ☐Staff to partner ratio
- ☐Staff to manager ratio
 - ☐ Headcount of quality control functions

personnel

□ Hours of training

provided by the

firm to audit

Firm's

- Internal & monitoring
- ☐ Results of monitoring reviews that have been carried out by the firm or the firm's network
- ☐ Results of AOB inspections and compliance reviews by external bodies (e.g. MIA, professional bodies)

