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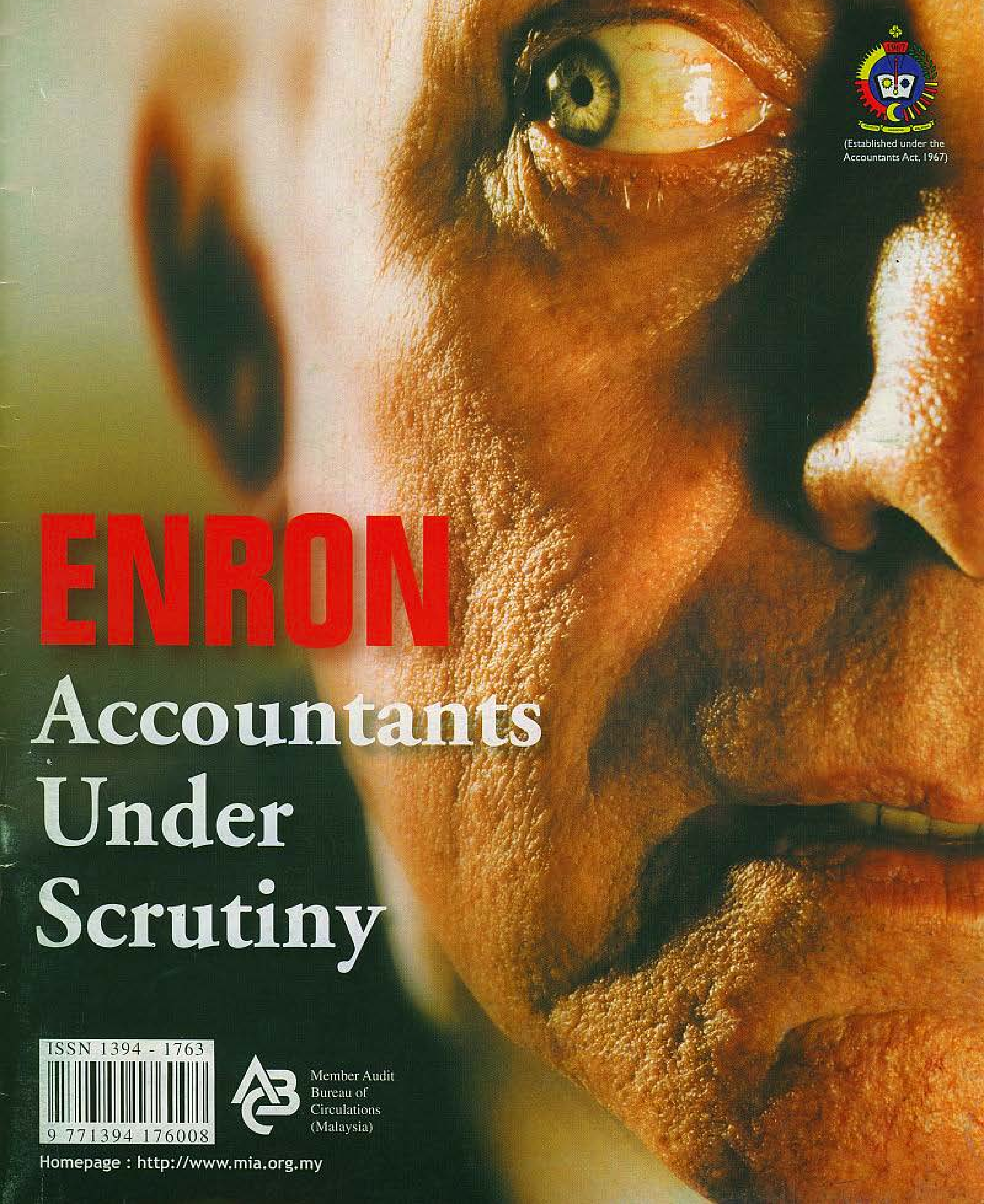
(Established under the Accountants Act, 1967)



ENRON

Accountants Under Scrutiny

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Malaysian Institute of Accountants
(Established under the Accountants Act, 1967)

The **Malaysian Institute of Accountants** is a statutory body set up under the Accountants Act, 1967 to regulate and develop the accountancy profession in Malaysia.

The functions of the Institute are, *inter alia* :

(a) To regulate the practice of the accountancy profession in Malaysia;

(b) To promote in any manner it thinks fit, the interests of the accountancy profession in Malaysia;

(c) To provide for the training and education by the Institute or any other body, of persons practising or intending to practise the profession;

(d) To determine the qualifications of persons for admission as members; and

(e) To approve, regulate and supervise the conduct of Qualifying examination.

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FROM THE EDITOR

Restoring Dignity

With the devastating explosion of energy trader Enron thanks to its questionable accounting practices, the public spotlight has been uncomfortably trained on the accounting profession.

Much of the blame accruing to Enron's failure has been laid squarely at the door of Enron's external auditors — no thanks to the very public issue of document shredding by a senior official at the Big Five firm servicing Enron. Unfortunately, the tarring of Arthur Andersen has resulted in guilt by association for the entire accounting profession. Since the Enron debacle, global capital markets in the US and Europe have punished companies suspected of practising opaque accounting methods.

But what must be stressed in the case of Enron and its brethren is that the accountancy profession is not at fault. Globally, accountancy standards and regulations are highly functional. Throughout the centuries, there have been minimal business failures involving creative accounting. Ergo, accounting standards and regulators have done their job in policing the majority of businesses.

Instead, cracks emerge in any enterprise where the people involved are greedy for lucre and willing to pursue the feathering of their nests at any cost. Ultimately, the dark side of human nature is the catalyst behind a crisis of this magnitude. Likewise, for Enron, the bottom-line was greed and lack of integrity among senior management, and the collusion of a few highly-paid external auditors in maintaining the myth of Enron's financial health. The Enron breakdown boiled down to people greedy for money.

No thanks to these few bad apples, the dignity of the accounting profession has suffered in the wake of Enron. Now that the sour milk has spilt, how can we accountants regain our cherished reputation as reliable, uncorrupted watchdogs safeguarding the interests of investors and shareholders?

The answer is simple. Accountability, discipline and a solid moral foundation are the bases for rebuilding public trust in the profession and ensuring the relevance of accountants in global business. Accountants must be accountable, disciplined and moral. As MIA President, Abdul Samad Hj. Alias puts it in this issue's cover story, "When they (accountants) prepare the accounts, they can put their hands on their hearts and say, 'I can stand by that'." In order to make such a statement sincerely, accountants must practise integrity, honesty, and transparency, and put the interests of company stakeholders, particularly minority shareholders, first.

At the same time, accountants must be policed more stringently. To enhance regulatory enforcement, the MIA is already moving in new strategic directions. We are working to ensure that MIA members in commerce, industry and public sector are subject to disciplinary procedures, so that we can control the actions of our members. Ultimately, the answer to safeguarding investors' confidence lies in the enforcement of existing guidelines and rules. The burden lies on regulators to ensure that regulatory enforcement and punitive measures deter the flourishing of greed and corruption á la Enron. AN

Editor

Letters to the Editor

A key element in the world of publishing is what readers have to say.
We want to hear from you on just about anything that appears in
each issue of *Akauntan Nasional*. Why not drop us a line now?

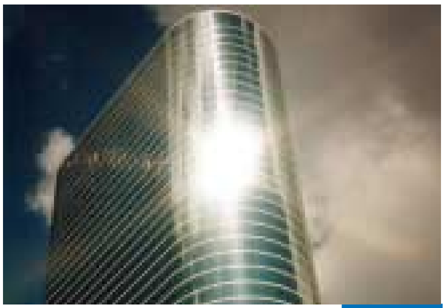
CONTRIBUTION OF ARTICLES

The *Akauntan Nasional* welcomes original and previously unpublished contributions which are of interest to accountants, executives and scholars. Manuscripts should cover domestic or international accounting developments. Lifestyle articles of interest to accountants are also welcomed.

Manuscripts should be submitted in English or Bahasa Malaysia and range from 2,500 to 5,000 words (double-spaced, typed pages). They should be submitted in hardcopy and diskette (3.5 inch) form in Microsoft Word or Lotus Wordpro. Manuscripts are subject to a review procedure and the Editor reserves the right to make amendments which may be appropriate prior to publication.

CONTENTS

Volume 15, Number 2 MARCH 2002



Debits, Credits and Discredits **Pg 6**

How to Score as the Ideal CFO? **Pg 24**

Taxation of Cyberspace Trading **Pg 44**

Pg 56 *Bangkok : Bargainers' Paradise*

Akauntan Nasional

The *Akauntan Nasional* is the official publication of the Malaysian Institute of Accountants (MIA) and is distributed to all members of the Institute. The views expressed in this journal are not necessarily those of the MIA or its Council. Contributions including letters to the Editor and comments on articles appearing in the journal are welcomed and should be sent to the Editor as addressed below.

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Malaysian Institute of Accountants
(Established under the Accountants Act, 1967)

VISION AND MISSION

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- To be a globally recognised and respected business partner committed to nation-building

MIA's Mission

- To develop, support and monitor quality and expertise consistent with global best practice in the accountancy profession for the interest of stakeholders

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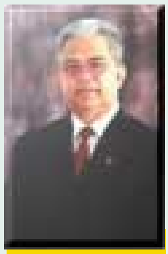
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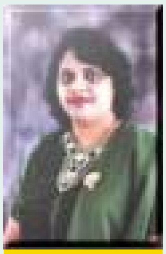
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ACCOUNTANTS SCrutinised!

By MIA Editorial Team

The collapse of Enron, the world's largest energy-trading company, has put the accounting profession under scrutiny. Far from being defensive however, the International Federation of Accountants (IFAC), representing the worldwide accountancy profession, readily accepts that the profession must contribute to reducing the occurrence of major failures such as Enron. IFAC represents more than 2.4 million accountants in public practice, education, government service, industry and commerce in 114 countries.

In a statement issued on February 12 this year, IFAC president, Aki Fujinuma, said IFAC would play its part in the drive for greater quality and consistency of accounting and auditing services. It is planning to form an international task force of investors, directors and auditors to make recommendations on the role and composition of audit committees and how they should report to shareholders.

The Malaysian Institute of Accountants (MIA), which is one of the 156 professional bodies under the IFAC umbrella is also decidedly frank about the Enron issue. Says MIA President, Abdul Samad, "There are no two ways about it. If the accountants want to be relevant, they have to be more diligent and more open about their assessment of management. They have to judge the credibility of the people involved with a high degree of scepticism." He adds that everyone involved in the reporting cycle has to be very honest, full of integrity, accountable and transparent. It is a tall order since it all lies in the whole fabric of human values. Adds Samad,"However, if you were an auditor in the situation of Enron, I think you'll be overwhelmed by management. Even here, if you are an honest auditor, I can bet my bottom dollar, you'll have that problem."

MIA Council member, Nik Mohd Hasyudeen Yusoff puts it thus, "Enron is more than an accounting issue. The auditors, regulators, and others must come together, realise the weight of their responsibilities and form a net so those events of untoward nature will not happen. Accounting standards alone will not be able to solely address the issues we have today." "Malaysian regulators are coming up with a more disciplined and organised financial reporting structure in order to ensure compliance and give more confidence to the public".

The Executive Director of the Malaysian Accounting Standards Board (MASB), Dr. Nordin Mohd Zain, adds, "we have to think beyond compliance by going back to the intent of these regulations. The overriding issue is what we are trying to achieve from these compliances — nothing but honest reporting so that people can make informed decisions about investments".

In his statement, IFAC's Fujinuma also stressed that ultimately the responsibility for the Enron affair cannot be laid at one door. He said, "The company and its management, the auditors, banks, analysts, regulators and standard setters are among those who will ultimately be challenged and some or all will be found wanting." He added that very significant issues would be addressed. These include the need for clear and unequivocal accounting and auditing standards of international application and based on principles, not detailed rules; recognition of the dangers that flow

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— Abdul Samad Hj Alias, MIA's President.

"Enron is more than an accounting issue. The auditors, regulators, and others must come together, realise the weight of their responsibilities and form a net so those events of untoward nature will not happen. Accounting standards alone will not be able to solely address the issues we have today."

Nik Mohd Hasyudeen Yusoff,
Council Member of MIA and the Executive
Chairman of Khairuddin, Hasyudeen & Razi.

from some of the new financial instruments that are now available; separation of powers between management and preparers; and honesty from management to the auditors.

Touching on corporate governance, Fujinuma also said honest communication involving management, preparers, auditors, non-executive directors and audit committees, is essential in order to ensure the highest standards of professionalism and integrity among those concerned in the management of enterprises and the preparation and presentation of financial information. Added Fujinuma, "The drive for the highest standards of corporate governance, designed to combat the natural desire of management to present the entity in its most favourable light to shareholders and potential investors requires a radical change in mindset, which sets the need for protection of investors and the public interest above commercial interests. By contrast, the responsibility for professional standards lies squarely within the profession."

The multi-faceted role of accountants in improving corporate governance is seen as a crucial link. Says MIA Vice-President, Albert Wong, "Maybe we should look at the role of accountants not just as auditors, but as part of management — how they can contribute towards better corporate governance. We in the profession look at ourselves in a more rounded manner, in the sense that audit is just one of our roles. There are other accountants in commerce and industry who actually play a role in management. The regulators, the Kuala Lumpur Stock Exchange and Securities Commission, have shifted the focus from auditors to accountants in management, and they have made it a requirement for audit committees to have accountants."

"Maybe we should look at the role of accountants not just as auditors, but as part of management — how they can contribute towards better corporate governance ..."

— MIA Vice-President, Albert Wong

Samad stresses that these accountants, should be just as accountable, as far as adhering to basic values such as independence, integrity and objectivity are concerned. He adds," In other words, when they prepare the accounts, they can put their hands on their hearts and say " I can stand by that." Indeed, this is also one of MIA's new strategic directions — to make sure MIA members in commerce, industry and the public sector are subject to disciplinary procedures, so that it can control its own members. To Samad, the answer to safeguarding investors' confidence lies in the enforcement of existing guidelines and rules. He says," What has happened in this country at present is a good indication. That's the sort of thing investors want to see. At least there is accountability. You don't go scot-free after an event of such magnitude." AN

Frequently Raised Questions

On whether auditors can be sued

Samad : Auditors have been sued in Malaysia before but these have not been reported by the media. The SC chairman, Datuk Ali Abdul Kadir, has said that auditors are liable to be sued by investors.

On suggestions that companies rotate their auditors every three years

Samad : It requires legislation and if that is legislated, all the Big Five would not be in business. The amount of investment in time and knowledge to understand the business and systems, clients, and what makes the business tick cannot be covered in three years. Moreover it is against the free market principles. If I am a major shareholder of a successful company, it is my money : I want somebody I can trust, not somebody that somebody asked me to go to bed with.

On the cosy relationship between auditor and client

Samad : There is nothing wrong with having a close relationship with a client *per se*. What is wrong is when you cannot exercise your independent judgment, when you let the close relationship colour your judgment. This is where as a professional, you have to have a healthy scepticism. You do not take your client's words as gospel. You check with corroborative evidence. If he were reporting 100 per cent more profits than a similar and as successful business in the same industry, wouldn't your suspicions be aroused? Wouldn't you want to raise the issue?

On actions by the MIA against members for irregularities

Samad : The accounting body has taken action against its members on alleged irregularities. I don't have statistics but a lot of people are involved in investigations. During the Deposit Taking Cooperative (DTC) crisis, a few members were disciplined and their names appeared in our journal. However, on reporting irregularities, what is there to protect the auditor from being counter-sued? Most times, some of these issues are highlighted in management letters to the management. It is within the purview of the audit committee to take action.

On public expectations

Nik : The public expects if there is something wrong with the company, the auditors need to inform them. This is wrong. After a particular event has arisen that requires management's attention, it has to be brought up with the management first. If they have corrected or subsequently correct it, it becomes a non-issue. What investors see at the end of it would be a clean report.

DEBITS, CREDITS and DISCREDITS

After ENRON, the accounting profession seems to have taken a turning point

By Ghazalie Abdullah

ENRON, the seventh largest corporation in the US worth US$80 billion at its height, has collapsed. Along with the colossal fall, came down the credibility of one of the most respected Big Five accounting firms. Soon, the credibility of the accounting profession followed. A recent *USA Today*-CNN Gallup Poll showed that slightly less than one third of people rate accountants high for honesty and ethical standards, down from two-fifths last year. Shocking as it may be, Ghazalie Abdullah from the public relations firm of Ghazalie Rafeah Ali & Associates Sdn Bhd, looks at public perception on the ENRON affair, the massive reporting in the media, its implication on the integrity of accounting practice and what is needed in damage control.

In the beginning way back in 1985, a company called Houston Natural Gas became Enteron — until told by some learned ones that the name suggested our innards, the intestines. Then, it became Enron and also turned into a politically well-connected player in the new deregulated market of energy trading. In the months that followed, Enron became part of the Internet revolution — the big borderless e-biz zone, and claimed to have become huge and profitable. The truth is that it was lying about both, and then the company failed. But how did Enron manage to hoodwink the world? That's what everybody is now trying to figure out. Public relations perception management, you might suggest. From all the mass reporting, here is what we know of the company's magic act thus far.

The catalyst was what you might call "accounting alchemy," says Paul Solman of WGBH-Boston — miraculously turning lead into gold, water into

"Enron is today the subject of congressional and criminal probes into manipulation of its accounts as well as corporate governance misdemeanours."

wine, losses into profits, making debts and bad investments, or anything they wanted to simply disappear. You know, the kind that Merlin the Wizard could wave with his magic wand. Or the kind our street medicine peddlers are known to do along Jalan Masjid India. Or to put it differently, Enron played the all-in-the-family fantasy finance game, manipulating hundreds of subsidiary companies with names out of '*Star Wars*', '*Jurassic Park*', and medieval Scotland.

By the early 90s, Enron made money with, for example, an oil partnership dubbed Jedi, after the '*Star Wars*' knights. One of its many subsidiaries, Raptor, which invested in Internet firms, was virtually minting money as its portfolio soared. And when Enron made a deal with Blockbuster Video to deliver movies on demand over the fibre optic cables it was installing across America, Enron seemed to be making all the right connections. How very clever. How very interesting.

Soon, Enron was America's seventh largest company in terms of revenues. But from the beginning, something was kind of over mesmerising. It turns out, Enron got so big, so soon, with some audacious sleight-of-hand accounting — call it "ledger domain." Enron recorded, as revenues, what on the stock market they simply refer to as volume. How could they have done that? Good advice, it was believed.

According to *Time* magazine, when Enron Chairman Kenneth Lay appears before the Senate Commerce Committee, Lay is expected to argue that he relied on the counsel of legal and financial experts who told him that there was nothing illicit or unethical about hiding billions of dollars of Enron's debt in off-balance sheet partnerships that ended up inflating the company's reported earnings.

It's hard to overstate the enormity of the impact of Enron's implosion. Enron is today the subject of congressional and criminal probes into manipulation of its accounts as well as corporate governance misdemeanours. The affair has all the sexy trimmings glaring at you, of the rich and famous scheming, cheating and profiting, one that's likely to draw a picture clear as digital photography, of sophisticated crony capitalism in the US.

"The biggest corporate collapse in US history is now dragging government, politicians, banks, accounting firms, other corporations, pension funds, investment analysts, the reputations of so-called business experts and millions of investors into an astounding vortex where they risk losing billions of dollars and some of the most trusted reputations in corporate America."

The White House and Congress have moved toward a historic court clash as congressional investigators filed their first-ever lawsuit for public records against the executive branch. The biggest corporate collapse in US history is now dragging government, politicians, banks, accounting firms, other corporations, pension funds, investment analysts, the reputations of so-called business experts and millions of investors into an astounding vortex where they risk losing billions of dollars and some of the most trusted reputations in corporate America.

Indeed, America, the world's most transparent market, has been scandalised and so has the good name of Arthur Andersen, the international venerable accounting firm that was widely reported to have destroyed documents and signed-off on Enron's doctored books.

Former lead auditor of Enron Corp David B. Duncan refused to answer questions during a recent US House of Representatives subcommittee hearing. A recent *Tonight Show* with Jay Leno depicted Andersen's chief as Satan taking the Fifth Amendment.

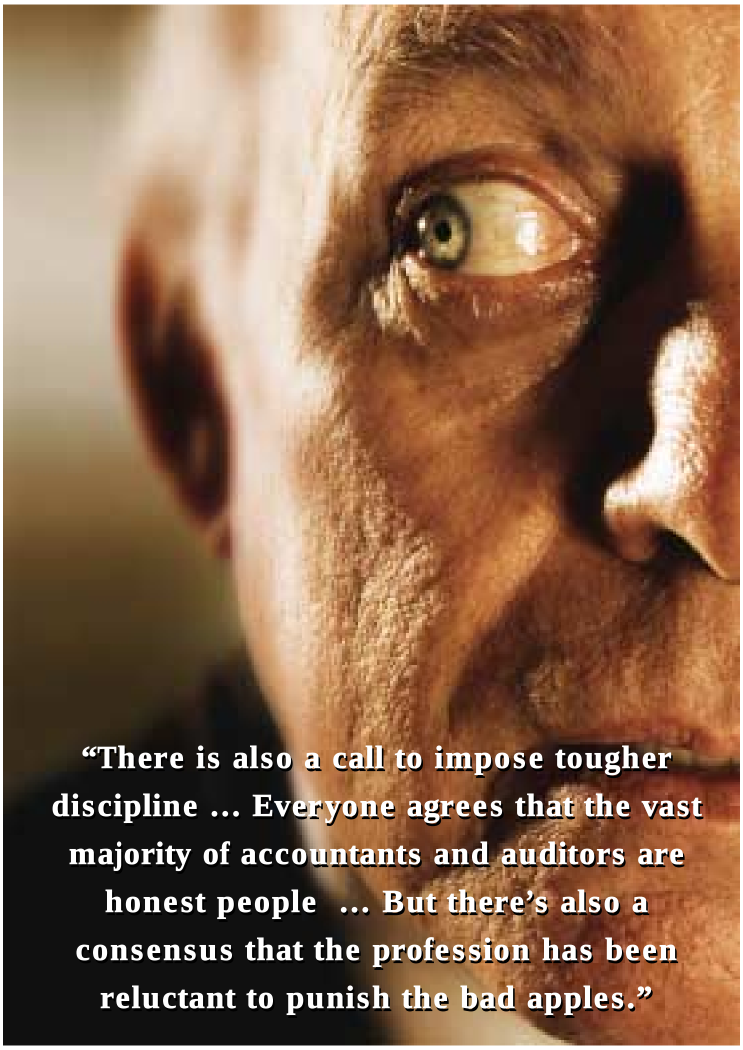
"I hope this Enron scandal doesn't turn kids off to an exciting career in accounting," Leno cracked. The taint of impropriety hanging over a profession long considered upright, if dull and arcane, is not amusing.

So how does all this impact the accounting profession and the professionals behind it? Quite a lot as events revealed. In a speech in San Diego, former comptroller general, Charles Bowsher mentioned that he had worked at Arthur Andersen from 1956 to 1981. The 125 people in the audience groaned. Bowsher was reported to be stunned.

"In the old days," he says sadly, "if you said you were with Arthur Andersen for 25 years, people were impressed."

It appears that the Enron case is not an isolated case. It is just the latest and most spectacular example of a company that collapsed. Arthur Andersen's role in the Enron case has hurt the profession's credibility and public trust in it, says a *USA Today* report.

Many would believe that this is crisis management for the accounting profession but in public relations reality, it is an issues management that is now at hand. When Enron collapsed, it was a colossal fall but not one that could not have been unexpected. Circles in the company, the industry and government saw the dangers ahead. Crisis management in public relations deals with those horrendous episodes that befall organisations suddenly whereas issues management deals with events that are possibilities and how a planned programme of PR action can be undertaken to mitigate or arrest the situation.



Given the evidence and the tons in publicity coverage, it would now seem for Arthur Andersen and the accounting profession to mitigate the impact through some form of damage control.

Building Back the Credibility

In America after the Enron debacle, the Big Five accounting firms are heading for a debate that is going to reshape the profession for decades to come. In a pre-emptive move, the Big Five have reversed ground and announced they would stop selling certain business advisory services to companies they audit so that their independence would not appear to be compromised.

The accountant's trade group AICPA has endorsed a proposed oversight body and is considering an advertising campaign to improve the profession's image. A concerted public relations effort by the profession to demonstrate the quality of integrity would be a much-needed boost.

There is also a call to impose tougher discipline. Integrity is after all, the epitome of the profession and third party policing should help. Everyone agrees that the vast majority of accountants and auditors are honest people trying to do the right thing for the right reasons. But there's also a consensus that the profession has been reluctant to punish the bad apples. Perhaps a watchdog dominated by respected public members and not accountants. The industry would need to be policed by a government body with handcuffs and subpoena power.

To add to credibility, it might be prudent for stock exchanges to determine the auditors of a listed company and that such appointments would see periodic rotations say once every five years.

Meanwhile, it is reported that Arthur Andersen will offer a presentation to Enron Corp's creditors, telling them how much the accounting firm can afford to pay to settle any litigation from the collapse of the energy trader, a plaintiff's lawyer told CNN/Money. Andersen plans to open its books to creditors and will present to them the amount the Chicago-based firm could cough out without going out of business, said Vincent Cappucci, of law firm Entwistle & Cappucci, which represents the New York City and Florida pension funds in a suit against Andersen.

Andersen, which acted as Enron's auditor before it was fired, may have to pay up to 40 per cent of a US$60 billion damage bill, in addition to claims from unsecured creditors, Cappucci said.

Settling the claims against Andersen may stop the departure of its clients. SunTrust Banks Inc. and Hard Rock Hotel and Casino in Las Vegas have already dropped Andersen as its auditor.

A spokesman for Andersen reiterated the firm's statement given. "Reaching out to the groups affected in this case is consistent with our commitment to address the issues raised by Enron's collapse in a straightforward and constructive manner," Andersen said.

It appears that Andersen is doing the right thing to right its image and that of the millions of accounting professionals. But it would be an uphill task as investigations unfold in the coming months. In public relations, where one dent normally requires ten other good things to repair the image, this would see the industry trying very hard to put the image correct. The malpractices in the Enron affair are just the tip of the iceberg, describe investigators. And as more beans spill out, the dents are expected to become wrecks.

But as Andersen puts it, "We think it is in the best interests of all parties to deal expeditiously and responsibly with what has occurred." AN

Note: Ghazalie Abdullah is Chairman and Chief Executive of Ghazalie Rafeah Ali & Associates Sdn Bhd, a public relations consultancy founded in May 1987. He was formerly a freelance television newscaster for TV3 and a broadcaster with RTM. His public relations clients include Edaran Otomobil Nasional Berhad, Tenaga Nasional Berhad and British American Tobacco Malaysia Berhad. He is also the Secretary of the International Assocaition of Business Communicators, Malaysia Chapter. While he serves on the editorial committee of *Akauntan Nasional*, Ghazalie is also the editor of the *eon&U* magazine. For more information, please visit www.jaring.my/grapr.

Statements from INTERNational accounting bodies

IFAC Comments on Enron and the Global Accountancy Profession's Commitment to the Public Interest

Aki Fujinuma, President of the International Federation of Accountants (IFAC) made a statement on 12 February 2002 which is available through the IFAC website

The International Federation of Accountants (IFAC), as the representative of the worldwide accountancy profession, readily accepts that the profession must contribute to reducing the occurrence of major failures such as Enron and will play its part in the drive for greater quality and consistency of accounting and auditing services. It will also take steps to encourage improved corporate governance. Toward that end, it is planning to form an international task force of investors, directors and auditors to make recommendations on the role and composition of audit committees and how they should report to shareholders.

The collapse of the Enron Corporation in the US has made it incumbent upon all accountancy organisations to assess what they can do to ensure the soundness of financial reporting worldwide and to encourage and support accountants in their efforts to protect the public interest. It will be many months, and even years, before all the reasons for the Enron collapse are made clear. However, action must be undertaken now to prevent future business failures that can so drastically impact the livelihood of so many people — from employees and their families to shareholders and creditors.

The US is already scrutinising the regulation of the accounting profession and the auditing standard-setting process. In addition, those investigating the Enron case must take a close look at corporate disclosure rules, the effectiveness of various securities laws, and the responsibilities and accountability of boards of directors and audit committees. A sound global financial architecture depends upon an independent accounting profession supported by the highest professional standards, an effective regulatory framework, and strong corporate governance.

> "It will be many months, and even years, before all the reasons for the Enron collapse are made clear. However, action must be undertaken now to prevent future business failures that can so drastically impact the livelihood of so many people — from employees and their families to shareholders and creditors".

Public Interest Initiatives

The Enron case clearly demonstrates the value of the traditional work of IFAC and its more recent public interest initiatives, which have been under development and/or review during the past two years. These include :

- The promulgation of International Standards of Auditing and the IFAC Code of Ethics, including its new rules on independence, and active support of the standards produced by the International Accounting Standards Board (IASs and IFRSs).
- The decision to strengthen the processes and transparency of the work of the International Auditing Practices Committee (IAPC). Effective in mid-2002, IAPC will be renamed the International Auditing and Assurance Standards Board (IAASB), membership will be expanded to include members independent of the profession, and meetings will be open to the public.
- The initiative of IFAC and the major firms in establishing the Forum of Firms (FoF), which is designed to improve the standard and consistency of audits of transnational entities around the world.
- The establishment of an independent review board to oversee the activities of IFAC and the FoF that affect the public interest.
- The implementation of the IFAC compliance regime, designed to ensure that na-

tional accountancy bodies that are members of IFAC meet the obligations of membership and, in particular, that they require compliance by their members with such standards.

- The International Forum on Accountancy Development (IFAD), established in 1999 by the World Bank and IFAC in order to improve corporate reporting and the alignment of national standards with global standards for accounting, auditing, corporate governance, and market regulation

The Need for Partnership

Achievement of the objectives of IFAC and of the initiatives referred to above requires a partnership of the profession, governments, regulators and other stakeholders. In particular, it necessitates :

- Recognition by governments, regulators and the profession, at the national level, of the need for high quality, common standards of global application, to ensure comparability of financial information around the world;
- Acceptance by governments and regulators of their responsibility to lead the campaign against corruption and inadequate financial management of public money; and
- The highest standards of professionalism and integrity among those concerned in the management of enterprises and the preparation and presentation of financial information. This demands honest communication between management and preparers, on the one hand, and auditors, on the other, with active, independent non-executive directors and strong and effective audit committees, or an equivalent mechanism, such as the two-tier board system, in countries where this option is deemed more appropriate.

It is important to stress the need for this partnership. IFAC and its member bodies can encourage governments, regulators and private enterprise to adopt this approach, but cannot compel them to do so. Similarly, the drive for the highest standards of corporate governance, designed to combat the natural desire of management to present the entity in its most favourable light to shareholders and potential investors, requires a radical change in mindset, which sets the need for protection of investors and the public interest above commercial interests. By contrast, the responsibility for professional standards lies squarely with the profession.

The Forum of Firms

The international accountancy profession's commitment to high professional standards is exemplified through the creation of the Forum of Firms.

Members of the FoF are committed to significant obligations in terms of compliance with IFAC's International Standards of Auditing and with the IFAC Code of Ethics. They will also be required to meet additional continuing educational and training requirements. The firms will also submit to additional quality assurance measures, details of which are currently being developed. These are designed to complement existing national monitoring and other quality assurance schemes that have been developed by national governments, regulators and accountancy bodies around the world.

> "At the end of the day, it is clear that responsibility for the Enron affair cannot be laid at one door. The company and its management, the auditors, banks, analysts, regulators and standard setters are among those who will ultimately be challenged and some or all will be found wanting."

These new quality assurance measures will be developed in cooperation with the member bodies of IFAC, to ensure their effective and cost-efficient delivery and to avoid duplication of effort and encroachment upon the jurisdiction of national entities.

IFAC will be concerned to ensure that the professional bodies are playing their part. Its compliance regime is designed to ensure that IFAC's member bodies around the world have, or develop, effective educational processes and admission procedures and that they encourage, or require, their members to undertake continuing professional education and training. Member bodies will be expected to have, or put in place, appropriate quality assurance regimes for their member firms and to have effective investigatory and disciplinary processes.

IFAC will also look to the participants in the International Forum on Accountancy Development (IFAD), which include representatives of regulators, international financial organisations (IFOs), and other international agencies and organisations to actively support this major public interest initiative.

Looking Toward Solutions

At the end of the day, it is clear that responsibility for the Enron affair cannot be laid at one door. The company and its management, the auditors, banks, analysts, regulators and standard setters are among those who will ultimately be challenged and some or all will be found wanting. Very significant issues will be addressed. These include the need for clear and unequivocal accounting and auditing standards of international application and based on principles, not detailed rules, recognition of the dangers that flow from some of the new financial instruments that are now available, separation of powers between management and preparers and honesty from management to the auditors. There may also be a need to bring forward the application of the new rules on independence in IFAC's recently updated Code of Ethics for Professional Accountants.

IFAC is committed to keeping these issues in the forefront of its 156 member organisations and to continually striving to conscientiously implement programmes that put the public interest first.

Enron Case: The potential impacts on the UK auditing & accounting profession

On 6 February 2002 Michael Groom, President of the ICAEW, gave a briefing to the ICAEW Council on Enron which has been made available on the ICAEW website

Here in the UK there has been considerable media interest in the story and a vast amount of speculation. Some of this reporting has been speculative and, at times, downright misleading.

We take justifiable pride in our reputation for integrity and excellence, and recognise the need to communicate this message as widely as possible to correct longstanding misperceptions in the market place.

The Institute has stepped up a programme of activity, which was already in hand in the planning stage, to explain more fully the role of auditors and the regulatory and ethical framework within which they operate here in the UK.

I am particularly indebted to Deputy President, Peter Wyman, who has been leading that long-term project and also, more particularly, for his very significant work on the short-term need to react to the Enron situation. Over the last few weeks, as you will have seen, he has spoken to just about every major newspaper and broadcaster here in the UK and beyond.

Peter has sought to explain why we believe that our Institute's ethical guidance, allied to the independent regulatory framework afforded by the Accountancy Foundation, is strong and effective.

As part of our push back on comments in the press, we have stressed, very strongly, the work, over a considerable number of years, of the ASB and APB, which, frankly, has made UK accounting standards world class. In addition we have emphasised the role the profession and particularly this Institute, has played in the development of corporate governance, where the UK has again led the world. As a result we are able to say quite categorically that the kind of off-balance sheet finance arrangements permitted under US GAAP would not have been permitted in this country.

We have, in plain English, explained how the UK framework approach, putting substance before form, differs from and is more effective than the US rules driven approach.

We have strongly restated our view that the issue of non-audit work, as long as our ethics code is adhered to, does not compromise independence.

> "Behind every headline case is a failure of corporate governance."

You will be aware of the leading role our Institute has played over recent years in the development of the Accountancy Foundation, reflecting our belief that accountability must be at the very heart of the profession.

We have noted that the recently announced proposals to reform the regulation of the accounting profession in the US broadly follow the system already put in place by the UK profession to provide effective monitoring of audit firms and independent oversight over standard setting, investigation of complaints and disciplinary tribunals.

I've just come back from a few days in New York and in both public and private meetings it was very very satisfying to find people saying quite openly, quite publicly, that the American corporate economy and the American profession need to look at what we have done in the UK.

Of course we must not be complacent. We are working with the Review Board on its work programme in this area and our Ethics Committee, in conjunction with other CCAB bodies, is liasing closely with the Ethics Standards Board at the Foundation. If any evidence emerges which suggests that changes are required in the UK, we will, of course, do whatever is necessary to maintain the highest possible standards.

Similarly, we will, of course, fully co-operate with any requirements from the announcement, this morning, of a review by the Treasury.

We have been working closely with the Audit and Assurance Faculty on this matter, particularly with the Faculty's new Chairman Andrew Ratcliffe, and the Faculty will continue to offer leadership in this area.

We live and work at a time when there is, quite rightly, increased public scrutiny of the professions. We owe a duty to our members and the wider community we serve to explain how we work and to demonstrate the fairness and effectiveness of the regulations and disciplinary processes that bind our members.

This is the message I shall be taking to the US next week when I meet with Harvey Pitt, Head of the Securities and Exchange Commission. Again, contrary to press speculation, that meeting was arranged late last summer and was delayed by the tragic events of September 11th. It is not a crisis meeting. That meeting continues the dialogue begun last year, very successfully, by Graham Ward. We requested this meeting, and I see this as a valuable opportunity to explain first hand how the UK regulatory regime works in practice.

In addition to wider audiences we will continue to press home a range of key messages we have been consistently delivering here and overseas as follows :

The vital and urgent need for all countries to engage with an open mind in the process of developing truly global, rather than country, accounting and auditing standards.

A similar need to move to principles rather than rules based approach to ethics, which has the full support of IFAC and the European Commission.

The need to move Corporate Governance to the very top of the agenda. Behind every headline case is a failure of corporate governance.

Let me repeat. We are not complacent.

But on the other hand the UK ways of doing things have much to commend them and that is gradually being recognised.

I welcome that. I will keep Council regularly updated on our activities in connection with this matter. AN

Enron: Learning the Lessons

The Enron debacle has exposed a multitude of corporate sins — deceit, cover-ups, betrayal and high-powered connections — besides bringing the accounting profession into disrepute. Can such a situation happen in Malaysia? Or has it already?

By Joanna Sze

Nothing shakes the stodgy world of finance and business like an explosive corporate scandal. And we've seen quite a few — Barings Bank in the UK, Daiwa Bank in Japan, Credit Lyonnais in France, Bre-X from Canada, the Savings and Loan crisis in the US … the list goes on.

But perhaps all these corporate undoings pale in comparison with the Enron Corp debacle that erupted in the US in December last year, a treacherous web of deceit, cover-ups, betrayal, greed and high connections *(see box article on Profile of a Scandal)*.

The impact of the downfall of the Houston-based energy giant, once the seventh biggest company in the US, cannot be adequately measured, but the tremors have travelled far and wide, across sectors and geographical borders.

"Undeniably, the Enron debacle, and for that matter any other financial collapse or fallout, has implications worldwide simply because of the increasingly globalised nature of business," says a Securities Commission (SC) spokesperson in an e-mail response to queries by *Malaysian Business*.

Can an Enron happen in Malaysia? Or has it happened? That's the million-dollar question. *Malaysian Business* spoke to local industry players, regulatory bodies and other parties on the still-simmering issue. Some, including two of the Big Five accounting firms, shied away from making direct comments.

SC Chairman, Datuk Ali Abdul Kadir has, according to Press reports, said an Enron-style scandal will not happen in Malaysia because the country's accounting standards are different from America's. Thus, special-purpose vehicles' accounts cannot be deconsolidated here as they were in Enron's case.

There are, of course, other differences : Malaysia does not have risky and complicated energy-derivatives trading; America's capital markets are also more advanced, with no safety net for investors; workers in Malaysia don't have to worry about losing their entire retirement fund — as was the case with Enron's employees who invested their savings in their company's stock — as they have compulsory savings with the Employees Provident Fund.

"The Malaysian Accounting Standards Board (MASB) is overseen by a financial reporting foundation," said Ali. "We sit on the financial reporting foundation to make sure that the work done meets our criteria. So we have more than two safety catches in place already."

Others, however, are not so sure. If adequate measures are not taken, they caution, Malaysia may soon boast a corporate

"Enron highlights the failure of the accounting profession, … If the profession doesn't wake up, people won't have confidence in it anymore."

Datuk Lee Hwa Beng, HB Lee & Co

failure of the Enron kind.

President of the Malaysian Institute of Accountants (MIA), Abdul Samad Alias, says smaller-scale Enrons have already happened here. "It happens all the time; the magnitude may not be as great but the social impact is still very big," he tells *Malaysian Business*.

The fact is, Malaysia does have some significant failures dotting its corporate landscape : BMF, the deposit-taking co-operatives, Sime Bank and several other listed companies. Their abuses included siphoning off of company funds, debt concealment and inflating of profit figures.

But there's no use crying over spilt milk. There are lessons to be learned and actions to be taken. Regulators and others players — owners, management, lenders, auditors, analysts — have hard questions to deal with.

The accounting profession, for one, is definitely not basking in the spotlight thrust upon it as a result of Enron. "Enron highlights the failure of the accounting profession," says accountant Datuk Lee Hwa Beng of HB Lee & Co. "If the profession doesn't wake up, people won't have confidence in it anymore."

Stephen Ong, technical director of Arthur Andersen, agrees. "The accounting profession is in crisis and something fundamental probably needs to be done."

In the case of Enron, its external auditors Andersen have come under fire for "forsaking their traditional role of outside sceptic for that of inside business partner", a 'betrayal' made more painful by Andersen's high profile and reputation. Among the criticisms : not highlighting, or possibly being party to, the fact that Enron had been overstating profits by some US$586 million since 1997 and hiding debt via off-balance sheet partnerships; shredding of documents and e-mail messages related to its audit of Enron; and possible clouding of auditing judgment arising from its multi-million-dollar consulting contract with Enron.

The backlash has led to calls for reform by observers, investors as well as accounting firms themselves to repair the damage done to the profession.

There have been strong calls to bar firms from providing consulting services to their audit clients. This has become a matter of urgency as in recent years, accounting firms have been making more from consulting services than from auditing. In Enron, for example, Andersen received US$27 million in consultancy fees in 2000, marginally more than the US$25 million it made in audit fees.

The MIA issued new regulations on 15 January, stating that if total fees arising from the non-audit services to the client represent 20 per cent or more of the member's individual revenue, or the firm's annual total fees, for two or more consecutive financial periods, then the auditor is no longer deemed independent.

In the wake of Enron, companies globally are also becoming more cautious about using consulting and audit services from the same firm.

The Big Five have begun detaching themselves from their consultancy arms since 2000. Ernst & Young was the first to divest its consultancy business, to Cap Gemini; KPMG US spun off its consulting arm on Nasdaq in February 2000; Andersen split from its IT-consulting arm Andersen Consulting, subsequently renamed Accenture, in 2000 but still maintains a consulting business.

PricewaterhouseCoopers and Deloitte Touche Tohmatsu have also announced their decision to spin off their consulting businesses. The latter had until now steadfastly

Anatomy of a Downfall

July 1985	:	Enron, an interstate natural gas pipeline company, is formed from a merger between Houston Natural Gas and InterNorth.
1989	:	It starts to make a name for itself when it begins innovative and revolutionary trading of natural gas and other commodities such as water, coal, fibre-optic capacity, newsprint and even weather derivatives. It also becomes the main broker in energy products, with sales of some US$101 billion a year.
2000	:	Its shares are worth US$85. Enron rises to number seven on the Fortune 500 and is constantly hailed as one of America's most admired companies.
16 Oct 2001	:	It reports a third-quarter loss of US$618 million and a US$1.2 billion reduction in shareholders' equity. The Security and Exchange Commission launches a formal investigation into the company.
8 Nov 2001	:	Enron discloses that it has overstated earnings by US$586 million since 1997.
2 Dec 2001	:	After a proposed buyout by rival Dynegy collapses, Enron files for bankruptcy protection. Its stock falls to below US$1 and is later suspended. Enron's 20,000 employees lose billions in their pension plans after they are barred by the company from selling their shares, while management have made millions from stock option profits. Enron's debts total US$15 billion.
9 Jan 2002	:	Criminal investigation into Enron is announced. Arthur Andersen, Enron's auditor, admits to destroying some Enron documents. Investigations are ongoing.

"We're watchdogs, not bloodhounds, … We're not there just to look for errors or fraud. In the course of our audit work, if something does crop up, we will report accordingly."

Raymond Liew of Raymond Liew & Associates

maintained its position that it could provide better service to clients by keeping its auditing and consulting businesses together.

"We believe the independence issue related to professional firms that provide auditing and consulting services to the same client is one of perception only," says Ahmad Mustapha Ghazali, managing partner of Deloitte KassimChan, Deloitte Touche Tohmatsu's local arm. "But this perception problem needs to be addressed."

Ernst & Young Executive Chairman Datuk Nordin Baharuddin agrees. "In the interest of public perception, regardless of whether the regulators will make it a rule to separate the two services, I think the Big Five are already moving towards that direction."

There have also been calls to limit the term of service of auditors for each client. "There should be a rotation of auditors every three to five years," says Lee of HB Lee & Co. Mandatory rotation, proponents say, would result in auditors being more careful as they know that within a few years, a competitor would be reviewing their work.

This is a suggestion the Big Five would not look too favourably upon. "This would never happen unless it's legislated," says Abdul Samad. "And if it's legislated, the Big Five would not be in business. The amount of investment in time and knowledge of a client, what makes the business tick, cannot be covered in three years."

Besides, he argues, mandatory rotation goes against the tenets of free market. "I want somebody I can trust, not somebody that somebody says I have to go to bed with."

In his piece '*How Accounting Can Get Back Its Good Name*', Jim Turley, Chairman of Ernst & Young International, suggests an alternative : a staggered rotation of all partners and staff on the engagement to provide a continuous flow of new eyes and objectivity, while maintaining the institutional knowledge that helps ensure audit quality.

But how then does one deal with the seemingly cozy relationship between auditors and their clients? "There's nothing wrong with being close to clients," says Abdul Samad. "What's wrong is when you cannot exercise your independent judgment, when you let the close relationship colour your judgment."

Investors also can play a part in holding auditors accountable.

"People don't file legal suits," says Lee. "If they did, many accounting firms would have closed down." There has reportedly been several suits against accounting firms in Malaysia, but these don't make the news often enough.

"Enron has brought about better awareness of the accounting profession," says Raymond Liew of Raymond Liew & Associates. "Auditors now are fearful of civil suits against them; it has become mandatory for them to purchase professional indemnity insurance, and premiums have been rising."

However, the public must understand the role of auditors. "We're watchdogs, not bloodhounds," says Liew. "We're not there just to look for errors or fraud. In the course of our audit work, if something does crop up, we will report accordingly."

Still, the profession could do more to better serve the investing public.

"Every accountant knows that companies have a choice of accounting methods that can change the numbers reported," says Ong of Andersen. "Every auditor knows that our existing auditors' reports are too uniformly bland. They only give a pass or fail report; they do not tell how good or bad the pass is and *vice versa*."

As Abdul Samad points out, "Everyone involved in the reporting cycle has a stewardship role to play; if accountants want to be relevant, they have to be more diligent and open."

"As our code says, integrity comes first," says Nik Mohd Hasyudeen Yusoff, execu-

Profile of a Scandal

Off-balance sheet accounts and other questionable accounting and business practices

The company hid its losses using a complicated web of subsidiaries, partnerships and special-purpose entities (SPE). According to regulations, outsiders need invest only three per cent of capital in an SPE for it to be independent and off the balance sheet.

Among others : the company issued stock options to employees instead of incurring remuneration expenses, boosted profits by booking income immediately on long-term contracts, and used aggressive tax avoidance strategy.

Cozy relationship with auditors

Arthur Andersen was paid US$52 million in fees in 2000, US$27 million of which was for consultancy work. In the mid-1990s, it even handled some of Enron's internal auditing work. Enron's in-house financial team was also dominated by former Andersen partners.

Friends in high places

The corporation and its executives have contributed almost US$5.8 million to political campaigns since 1989, US$424,000 of which went to US President George W. Bush's campaign and inauguration committee. Enron had a strong voice in forming energy legislation, including persuading the Commodity Futures Trading Commission to let it and other companies run largely unregulated energy-derivatives trading businesses.

Star-struck market observers and players

Those who questioned Enron's complicated financial reports were told they did not understand the firm's business. Analysts were still calling a buy on the Enron stock up till it filed for bankruptcy. In June 2001, Standard & Poor's noted that Enron's underperforming international assets were of growing concern, but quickly reaffirmed the company's credit rating after promises by Enron to sell the assets and address the issue.

What the Big FIVE Say About Enron

Datuk Nordin Baharuddin,
Executive Chairman, Ernst & Young

Undoubtedly, the eventual results of the Enron case are going to affect the auditing profession all over the world. The speed at which the Big 5 react to the current situation and how they do so will determine the future of the accounting profession in general. As for the corporate scene, the Enron case is definitely going to serve as a lesson to many for a long time to come.

Stephen Ong
Technical Director, Arthur Andersen

The Enron experience will have repercussions not only on the US but also across borders, including Malaysia. The accounting profession is in crisis and something fundamental probably needs to be done. Our existing financial accounting and financial reporting models are inadequate in serving the needs of investors and certainly can be improved.

Ahmad Mustapha Ghazali
Managing Partner, Deloitte KassimChan

We believe the independence issue related to professional firms that provide both auditing and consulting services to the same client is one of perception only. But this perception problem needs to be addressed. Most importantly, the market has moved - at least in the US and probably in a number of other countries. In these markets, we are finding an increasing number of clients declaring that they will not engage their audit firms to provide consulting services. We see this trend emerging in Malaysia in the future, in tandem with development in developed markets.

PricewaterhouseCoopers and KPMG

The two declined to comment.

tive chairman of Khairuddin, Hasyudeen & Razi. "At the end of the day, you are accountable to yourself as a professional whether you have fully discharged your duties as what society expects of you, without fear or favour."

In all fairness, the responsibility also extends to other industry watchdogs — analysts, rating agencies and bankers. Just as in Enron, these watchdogs have been criticised for looking the other way, for operating as a pack and avoiding negative calls.

For example, from 1994 to 1995, most local analysts had made a wrong call on Aokam Perdana Bhd. Similarly with Enron, analysts had been calling buys on its stock right up till the company's collapse. For research houses linked with investment bankers, there is also a potential conflict of interests as their calls could affect the investment-banking business.

"Opinions can be manipulated," says an analyst with a local stockbroking house. "If you want a totally honest opinion, you're not going to find it at a merchant bank-linked research house. It's unfortunate but it's true."

Analysts, as a whole, also have to deal with all sorts of pressure, he adds. "When the market is weak, most analysts try not to write anything bad. There are also the legal implications; research houses have had to come out with public apologies. If you write an unfavourable report, you'd have a harder time getting access to the company's information next time."

Usually, if analysts do not have anything good to say about a company, they keep quiet, that is, they try not to include it in their coverage. "We may choose to refrain from covering the stock for some time," says another analyst with a merchant bank-linked research house.

If that's not possible, analysts usually fall back on their stockpile of cushioning phrases such as 'neutral', 'there are uncertainties' and 'we're not convinced'. "At the end of the day, the analysts' reputation is at stake if they're willing to paint a rosy picture of a company and not identify potential risks," adds the analyst.

Of course, much of the blame and responsibility lies with individuals in positions of power within the company — the directors and management.

"Directors, CEOs, chief financial officers and financial executives must ensure that the company's financial statements meet not only the requirements of the authorities but also the needs of investors," says the SC spokesperson.

The Kuala Lumpur Stock Exchange has tightened regulations with its revamped listing requirements introduced last year, which include, among others, making directors directly liable for breaches of listing requirements, and the enhancement of corporate governance and disclosure.

Regulations, laws and guidelines are in place to ensure responsible financial reporting by listed companies. "Even prior to the fallout, there had been significant initiatives taken to promote corporate governance practices," says the SC spokesperson.

"The Enron fallout has called for changes particularly to financial reporting and corporate governance frameworks, and for improvements to regulation of the independent watchdog. We must be able to distill the lessons from such events and implement improvement measures, where necessary, to our frameworks."

What else remains to be done?

"What has been done in the past is to respond with more guidelines and laws," says Abdul Samad. "To me, this is not the answer. If it were, the Enron fiasco wouldn't have happened. To safeguard investors' confidence, there must be enforcement of existing guidelines."

Still, even the best guidelines and enforcement may not prevent another Enron, in Malaysia or elsewhere.

"How do you ensure the highest level of integrity of everyone involved in the process?" asks Abdul Samad. "It all lies in the whole fabric of human values."

"This is more than an accounting issue," says Dr Nordin Mohd Zain, Executive Director of the MASB. "Accounting standards alone will not be able to address the issues of today."

After the Enron excitement dies down and the issue becomes a page in history, will complacency and indifference set in?

A corporate lawyer has a sombre prediction. "Malaysians are very slow to learn from experience," he says. "People will just continue with their old ways. Accountants will continue to play multiple roles for corporate clients. No accountant will give up a business until and unless stopped by the law. To depend on their sense of good governance or 'client's-best-interest' judgment would be a farce." AN

Note : This article first appeared in the *Malaysian Business* Magazine, 1 March 2002. Reprinted with permission.

VOLUNTARY corporate social disclosureS (CSD) of Malaysian Public-Listed Companies

By Chan Jen Jing

Voluntary corporate social disclosures (CSD) provide the general public with information about the corporation's activities with respect to environmental, energy, product, human resource management (HRM) and community issues : issues which are becoming increasingly important to the community. CSD's are a means for companies to respond to society's social and environmental concerns about the impact of their economic activities on the well-being of society as a whole. They are possible avenues for a company to amend its wrongdoing or to enhance its image when positive contributions have been made. It acts like an information machine, which offers insights into the activities of firms and how they interact with the wider society in their pursuit of material wealth.

In this study, CSD is defined as the voluntary social and environmental reporting of information relating to an organisation's interaction with its physical and social environment, as disclosed in the corporate annual report. The amount of these disclosures, the form in which they are disclosed, and the themes of disclosures in corporate annual reports of the top 40 Malaysian companies, based on June 2000 market capitalisation, were examined. The forms of disclosures may be qualitative (or narrative) and/or quantitative (includes monetary and non-monetary).

The themes, such as environmental, energy, product, Human Resource Management (HRM) and community issues, represent subjects or ideas in the disclosures. Environmental and energy disclosures represent issues such as recycling of waste, water conservation, environmental programmes and general environmental concern and awareness. Product disclosures encompass issues of product development, and product safety. Disclosures of information on employee health, safety and training are examples of HRM disclosures. Examples of community disclosures are donations of cash, products, or employee services to support established community activities, events, organisations, education, and the arts.

Of the 40 Malaysian companies examined, 36 (90 per cent) companies had some CSD. Qualitative disclosures comprised 72.36 per cent of all the CSD disclosures. The HRM theme was the most frequent theme at almost 50 per cent of all disclosures, followed by community, environmental, product and energy. Table 1 summarises these disclosures.

International comparative studies previously carried out by Andrew, Gul, Guthrie and Teoh (1989), Williams (1999), and Williams and Ho (1999) provide a benchmark for changes in CSD practices of Malaysian companies over time. Table 2 summarises these studies. Andrew *et al.* (1989) examined CSD of Malaysian and Singaporean firms in their 1983 annual reports and found that CSD received little attention from most companies except the largest which were generally foreign owned. Williams (1999) examined CSD in 1995 annual reports, and Williams and Ho (1999) examined CSD in 1995 annual reports and websites. Andrew *et al.* (1989) found that out of a total of 119 annual reports of publicly-listed companies in Malaysia and Singapore, only 31 (26.05 per cent) of the sampled companies made some kind of CSD. Williams (1999) found that out of a total of 54 annual reports of publicly-listed companies in Malaysia, 40 (74.07 per cent) of the sampled companies reported at least one voluntary social and environmental issue. This recent study, where 90 per cent of companies had at least one voluntary disclosure, shows that Malaysian companies have improved their CSD practices over the 16-year period.

Andrew *et al.* (1989) found that qualitative disclosures predominated, being 74.57 per cent of total disclosures. Williams and Ho (1999) found that Malaysian companies had 85.30 per cent of total CSD in the form of qualitative disclosures. In this study,

TABLE 1 **Corporate Social Disclosures for Malaysian Companies**

	Mean No. of sentences of CSD per company	Total No. of sentences of CSD	Percentages of total CSD (%)
Panel A : *Amount of CSD*	28.230	1129	N/A
Panel B : *CSD Methods*			
Qualitative	20.430	817	72.36
Quantitative	7.800	312	27.64
Panel C : *CSD Themes*			
Environmental	3.750	150	13.29
Energy	0.275	11	0.97
Product	2.150	86	7.62
HRM	12.325	493	43.67
Community	9.725	389	34.46

TABLE 2 **STUDIES OF Corporate Social Disclosures By Malaysian Companies**

	Current Chan, 2000 (2000 data)	William and Ho 1999 (1995 data)	Williams 1999 (1995 data)	Andrew et al 1989 (1983 data)
Panel A :				
% Companies with CSD	90.00	N/A	74.07	26.05
Panel B : *CSD Methods (%)*				
Qualitative	72.36	85.30	N/A	74.57
Quantitative	27.64	14.70	N/A	25.43
Panel C : *CSD Themes (%)*				
Environmental	13.29	8.38	N/A	4.76
Energy	0.97	2.31	N/A	N/A
Product	7.62	14.74	N/A	14.29
HRM	43.67	26.01	N/A	71.43
Community	34.46	48.55	N/A	9.52

72.36 per cent of total disclosures were qualitative and 27.64 per cent quantitative. This shows that qualitative disclosures are still the preferred method of CSD in Malaysian companies.

The low proportion of quantitative disclosures is an indication that quantitative CSD practices are usually more difficult than qualitative disclosures. For example, it is difficult to quantify the amount of damage caused by pollution in either monetary or index terms compared to a simple qualitative disclosure that the company has polluted the river when some hazardous chemical was spilt. Even though qualitative disclosures are still the dominant type of disclosure, the percentage of total quantitative disclosures has increased. This could be attributed to the advancement in accounting and measurement practices which enable more firms to be able to quantify social and environmental information.

HRM disclosures are the dominant theme in this study, whereas Williams and Ho (1999) found community disclosures were the dominant theme. This may be attributed to a more powerful and articulate trade union in Malaysia than five years ago. For example, on 10 October 2000, the Malaysian Trade Union Commission (MTUC) picketed outside the Ministry of Human Resources to demand explanations for the long-standing court cases of workers who had been dismissed by their employers (Shari, 2000).

In Malaysian and Singaporean companies, Andrew *et al.* (1989, p. 373) found that the theme most commonly disclosed across the industry groupings was human resources, which represented 71 per cent of all social disclosures'. They suggested that the high level of disclosures in HRM was because companies in Malaysia and Singapore might have been concerned about the government's push to enhance the working conditions and living standards of the employees. Disclosure of employee welfare activities, for example, provision of housing, health clinics and other amenities would indicate the contribution by companies to this effort (Andrew et al., 1989,p.373).

The lower proportion of HRM disclosures found in this study (43.67 per cent) could possibly be attributed to the much higher living standards now found in Malaysia compared to 16 years ago. Increased living standards could mean concern for a wider range of issues including community and environmental issues. Hence, Malaysian companies have broadened their scope of disclosures to other areas such as community involvement and environmental issues in response to the changed concerns of its stakeholders.

In Malaysian companies 13.29 per cent of total CSD were environmental disclosures. In contrast, Williams and Ho (1999) reported that environmental disclosures were only 8.38 per cent of total CSD of Malaysian companies and in the study by Andrew *et al.* (1989) they were only 4.76 per cent of total disclosures. Malaysian companies have improved the quantity of their voluntary environmental disclosures.

This is reflective of the increase in the awareness of environmental issues in Malaysian society. The President of the Malaysian Nature Society, Datuk Salleh Mohd Nor wrote in *The Star* (4 June 2000, p. 27) : *"In Malaysia, not a week passes by without some news coverage on the environment and all the major newspapers in*

"In Malaysia, not a week passes by without some news coverage on the environment and all the major newspapers in the country make it their business to highlight bad environmental practices, such as poor rubbish disposal and other environmental issues".

Datuk Salleh Mohd Nor
President, Malaysian Nature Society

the country make it their business to highlight bad environmental practices, such as poor rubbish disposal and other environmental issues".

Moreover, Mohd Nor (2000) has stated that Malaysia has put in place excellent legislative devices to protect the environment. An example would be the Environmental Impact Assessment (EIA) legislation. The Environmental Quality (EIA) Order of 1987 made it compulsory for major development projects to have an EIA (Mohd Nor, 2000). However, the major difficulty has been the deficient coordination of environmental policies, strategies and programmes, especially in relation to the responsibilities of the federal, state and local authorities (Mohd Nor, 2000). The law enforcing agents seem to be unable to carry out their responsibilities effectively.

In spite of this, the increase in awareness of environmental issues may have been reflected in the increase in the amount of environmental disclosures in the annual report of Malaysian companies. It is suggested that mandatory CSD may be a means to further increase environmental disclosures in Malaysian companies.

For the energy theme, disclosures represent 0.97 per cent of the total CSD for a Malaysian company. Malaysian companies exhibit very low levels of energy disclosures. This is consistent with Williams and Ho (1999) where the energy theme was only 2.8 per cent of total CSD. It is possible that Malaysian companies do not see the energy theme as important, or it may be subsumed under the environmental theme, as some energy disclosures could also be identified as environmental. The action by companies to conserve energy, such as water and electricity, for example, could also contribute to the environmental well-being.

There are also firm specific factors which could impact on CSD practices of Malaysian companies. Analysis of the data in this study revealed that both company size and industry classification (the resource sector) did affect the amount of CSD. This is consistent with other studies.

Larger corporations tend to disclose more social and environmental information than smaller corporations. They pursue more activities, make a greater impact on society, and have more shareholders who might be interested in social programmes undertaken by the company. Their annual report provides an efficient means of communicating this information. As society is kept informed of the impact of the corporation's activities, society would continue to support the activities which it perceives to be socially acceptable. This communication legitimises corporations and provides them with a license to continue operating.

Industry classification can also affect the amount of CSD. Some companies are more politically visible because of their larger size as well as being in an environmentally sensitive sector, for example, petroleum, chemical and extractive industries. These companies are more likely to provide voluntary CSD in order to respond to government and public pressure. Some industries also face more stringent regulatory requirements and companies in such industries may find it necessary to provide voluntary social and environmental information to reassure existing and potential investors that all is well. This is also applicable to other stakeholder groups, for example, environmentalists and the government. This study found that companies in the resource and construction sectors had more CSD than those in other industries in the sample (namely manufacturing, finance and services). These findings are consistent with the contention that companies operating in more sensitive industries are more likely to voluntarily disclose information which they perceive would help them restore or enhance their corporate image.

Malaysian companies have improved their voluntary social and environmental disclosures since 1983. In spite of this, the level of CSD may not yet be adequate. The level of awareness of Malaysian consumers and investors has increased tremendously. In order for Malaysian companies to respond to this increased awareness and to succeed in the global economy, they have to be able to provide social and environmental information as well as conventional financial information. This is triple bottom-line reporting which has a focus on economic prosperity, environmental quality and social justice. It is tied to the concept of sustainable development which is the creation of long term value on an economically, environmentally and socially sustainable basis such that the needs of consumers and shareholders are met without destroying environmental and social capital. Triple bottom-line reporting allows stakeholders in companies to assess their performance in all of these areas. If stakeholders are more aware of the social and environmental impact of companies, would mandatory disclosure rules be necessary to increase social and environmental disclosures and improve the information available for decision-making? AN

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Determinants of corporate success and Failure: The Malaysian Case

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Introduction

A rash of business failures has marked the recent decline in the nation's economic performance. The ability to predict impending failures using common identifiable attributes can help formulate and implement pre-emptive measures to avoid or at least mitigate the adverse effects of such failures. This could evade the financial distress to all stakeholders, reduce the costs of failures and contribute to the business and financial environment stability. The total costs of failures is substantial and Altman (1984) showed that firms in developed economies incur bankruptcy costs in the range of 11-17 per cent of their value three years prior to bankruptcy.

There were 91 public-listed firms that were identified as failures in 2001 (Shanmugam and Sze, 2001). Firms are considered a failure when they apply to the court or relevant authorities for a restructuring or reorganisation scheme based on a scheme of arrangement pursuant to Section 176 of the Malaysian Companies Act 1965. Corporate failures have adverse spill over effects on the nation's economic growth and its business community. Failures jeopardise the performance of financial institutions and undermine the government's efforts to promote economic development. Therefore there is a dire need to evaluate the performance of listed firms on a continuous basis to identify and address the potential failures on a timely basis. To date, the most popular approach to assess business performance is the Altman Z-score model. The model was developed on the basis of data relating to US companies. Kharbanda and Stallworthy (1985) argued concerning the general applicability of this model in other countries. Argenti (1976) studied corporate failures in UK using Altman's (1968) model and translated some of the American accounting terms to the UK equivalent. The results are not conclusive and cannot be generalised to other countries due to different accounting standards and practices, market structure and legal provisions.

This paper briefly discusses the findings on identification of potential failures based on accounting and market information attributes. The findings provide important insights to policy-makers and financial institutions to guide them in formulating effective pre-emptive measures to mitigate corporate failures.

Data and Methodology

The study was conducted with data gathered from audited annual financial reports available at the Kuala Lumpur Stock Exchange's (KLSE) Library. Thirty-three failed firms were identified for the period of 1980 to 1996. A firm is considered a failure if it requests protection under Section 176 of the Companies Act 1965, or is approved to undertake a restructuring scheme to revive their financial condition by the KLSE, SC or relevant authorities and/or were put under receivership. Listed firms that qualify in any one or a combination of situations mentioned above are defined as failed firms. The paired sample design technique was employed in this study where each failed firm had a success match in the sample.

Findings

Forward stepwise multi-variate discriminant analysis was applied and the following determinants of corporate success and failure were observed : Total Liabilities to Total Assets, Asset Turnover, Inventory to Total Assets, Sales to Inventory, Market Value to Debts and Cash to Total Assets ratios[1]. Among the six variables, Total Liabilities to Total Assets discriminates the most and Cash to Total Assets discriminates the least.

The model developed in this study utilised both market and accounting infor-

[1] The models for identification of corporate success and failures are not provided in this paper but are available from the authors.

mation. The market-based model accurately classified 86.2 per cent of the firms compared to 88.1 per cent for the accounting based model. The models developed were tested for external validity on new samples of failed firms in the year 1998. The models can correctly classify failed firms up to four years before the event. However, these models could provide a guide to stakeholders to concentrate on firms in the 'grey area'[2]. Firms in the grey area should be scrutinised carefully due to their uncertain future. If the firms in the grey area are taken into consideration, the prediction models could accurately identify successful or failed firms up to five years before failure with only 17 per cent misclassification.

Finally, a strong relationship was observed among the variables identified in the models with cash flow, profit, working capital and net worth variables suggesting that the variables selected in the models are a good proxy for the commonly used variables by investors to predict financial health of firms[2].

Summary and Conclusions

Prediction models for business success and failure unique to the Malaysian business environment were successfully developed. Six ratios were identified as significant discriminants between failed and successful firms. The significant variables are Total Liabilities to Total Assets, Asset Turnover, Inventory to Total Assets, Sales to Inventory, Market Value to Debts, Cash to Total Assets ratios. The models developed can predict up to four years before failure occurs. However, the models managed to predict failures five years before the event when firms in the grey area were incorporated.

Practical Application of Failure Prediction Model

The significant variables mentioned above could guide policy-makers or users of the model to develop an early warning system to either evade or mitigate impending adverse effects of failures. For example, bankers or creditors could use these models to continuously assess the potential borrowers or credit applicants' credit risk and financial condition in making decisions to renew or extend the loan granted. Based on the prediction models developed in this study, financial institutions could develop their own unique model using their database to identify potential failures.

Managers could use these models in their financial planning. If failure can be predicted three to four years earlier, management could take remedial action such as a merger exercise or restructuring to avoid the potential failure costs.

Regulating agencies such as the Securities Commission and the Kuala Lumpur Stock Exchange might want to assess a firm's going-concern status, solvency and compliance of certain important requirements. This is important to pre-empt any systematic financial failures and bailouts using public funds.

Auditors could use these models to help them formulate a fair opinion of the overall financial condition and the status of the firm as a going concern. Unfortunately, in this study more than 60 per cent of the failed firms had an unqualified auditor report even one year before the actual failure.

Investors could use these models as early warning signals on financial conditions of firms in portfolio management decisions.

The Way Forward

Future research needs to address the issues on the predictability of failures of non-publicly traded firms. This research on failure prediction could be further enhanced through collaboration with the relevant agencies (Registrar of Companies, Bank Negara, KLSE and the Securities Commission). These agencies could provide the required information and benefit from the reported findings in making informed policy decisions.

Future research needs to focus on specific industries with reasonably large samples. Concentrating on specific industries (Brigham and Gapenski, 1994) could help develop more accurate failure prediction models. The difficulty is the data availability, particularly in obtaining the financial data for failed firms and to find a match sample of successful firms using a set criteria.

Finally, one interesting issue to explore is whether the restructuring initiatives undertaken in the market after the financial crisis can ensure the recovery of the failed firms in the future. Empirical evidence over time using the developed prediction models can provide stakeholders with answers to these research issues. AN

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[2] Grey area is the area where the characteristics of successful and failed firms overlap. The firms that fall into this category have the characteristics of both types of firms and need to be scrutinized closely by the interested party due to the possibility of either success or failure in the following period.

[3] In this study, variables that had negative value were excluded due to statistical requirement for normal distribution of the data. It is found that most of the data are non-normally distributed and need transformation procedures like log and square root transformation, which prevent potential variables with negative value from entering the analysis.

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How to score as the ideal cfo

By Sarah Perrin

It may be tough at the top, but finance directors (FD) and chief financial officers (CFO) need soft skills to be most effective. Becoming an ideal FD or CFO is all about clear communication, backed up by business onus and the ability to think strategically.

In the US, where many business trends first appear, CFOs are required to be all-round business people. Improved systems and outsourcing trends have removed much of the basic number-crunching from the finance function's role, says New-York based Gordon Grand, Managing Director and financial officers' practice leader for the global executive search firm, Russell Reynolds. "Companies are looking for the CFO to be a much stronger all-round executive," Grand stresses. "They expect them to get more involved with the businesses and to be more of a business partner to the CEO than a staff financial person."

Particularly in the current tougher economic climate, the CEO has to be the visionary, the company's strategic leader, but he needs the CFO to support him. When the analysts are grilling the senior management about what's going on in the company, the CEO is looking for the CFO to be the one who's been closely involved with the business on a day-to-day basis, so he can help the CEO get behind the numbers and say, "Here's what's really going on in this business." With all of our executive searches, when a CEO is talking about his needs, he says, "What I want first is a strong leader, a business executive who happens to also have good financial skills." To fulfil such a role effectively, many CFOs in the US are expected to have had some line management experience. They also need excellent communication skills and the ability to think strategically, Grand says.

> **"Companies are looking for the CFO to be a much stronger all-round executive, ... They expect them to get more involved with the businesses and to be more of a business partner to the CEO than a staff financial person."**
>
> *Gordon Grand, Managing Director of global executive search firm, Russell Reynolds.*

The picture is a similar one in continental Europe and the UK, says Jeremy Rickman, who heads up Russell Reynolds' financial officers practice in London. If CFOs in the US are effectively required to know even more about the business than the CEO, so it is in the UK too. Strategic and commercial ability is essential. "Many people today look for the CFO to get in front of the client early to help with negotiating the contract and make sure there are no mistakes coming through late in the process," says Rickman. "That leads FDs or CFOs to become more commercial. Rather than a CEO doing a deal and throwing it at the CFO and saying, "Sort it out", the CFO is sitting at the table with him doing the deal, and in some cases, doing the deal without the CEO."

Jeff Grout, a long-time recruitment specialist with Robert Half International, also believes that broader management and people skills hold the key to success for FDs. "The higher you go up the organisation, the less you use your technical knowledge," he says. "It's generally assumed that the FD is the number two to the managing director, and so that person has got to have the qualities of a deputy MD."

Finance directors clearly need to be willing to take on all areas of the business and express opinions on them, but venturing out of the finance function silo can be one of the most challenging aspects of becoming a FD for the first time. Stephen Schneider, Managing Director of CPS, a consultancy specialising in executive mentoring and boardroom development, says : "First-time FDs can find it hard to do what directors are obligated to do, which is to exercise judgment over a whole panoply of issues which a board has to tackle. They say, "I am just involved in the figures; don't expect me to get involved in Human Resource management or marketing."

However, FDs do have to get involved in wider, non-financial issues. They also need to set aside their managerial command and control skills and be prepared to debate issues with boardroom colleagues. "You have to master persuasion and advocacy to be an effective director," Schneider says. "Simply telling other board members what you believe the best course of action to be, and expecting them to go along with it, is not good enough. Fellow directors need to be persuaded of the wisdom of a move if they are to be fully committed to it."

In terms of particular experience required of FDs, the specifics may depend on the stage of development of the business. For example, unlisted companies with ambitions to join the stock market will want a FD with Initial Public Offering (IPO) experience. Many ambitious businesses will want a FD with past mergers and acquisitions involvement. Economic conditions also influence the qualities seen as 'ideal'. At the moment, finance-raising skills are particularly valued, Rickman says. "Experience in debt and equity finance-raising in the capital markets is particularly sought after in the market today because there is so much cash being held by venture capitalists and investors," he says. "Very little of it is getting out to companies. Clients looking to raise finance want someone who has done it before."

So what do those venture capitalists and investors look for in FDs, to persuade them to part with their cash? Patrick Groarke, a partner at Livingstone Guarantee, the UK's largest unquoted mergers and acquisitions boutique, stresses commercial ability over historical score-keeping. "FDs need to be able to understand the commercial rationale of things, rather than just producing numbers for the sake of it," he says. "In terms of private equity deals, FDs should probably have some financial modelling skills — being able to develop quite a sophisticated model looking ahead perhaps five years." Mergers and acquisitions exposure can also be helpful, Groarke says, and past experience dealing with investors and funders who have specific information requirements.

"Our requirements of FDs are simple," declares Ian Macdougall, a retail analyst at Williams de Broe. "We want someone with a good grasp of the numbers; we want them explained clearly to us. And one likes to feel the FD can relate his financial expertise to the broader commercial policies of the company and is part of that (commercial) process."

Macdougall also highlights the need for the FD to act as a strong counterbalance to the chief executive. "The worst situation is where you have a dominating chief executive and the finance director is nought but a scorer and appears to have no control and no ability to restrain," he says. "The FD can at times, in volatile markets for example, impose a useful constraint on over-ambitious plans. One doesn't want the FD to be a constant wet blanket, but he needs to be able to relate what's going-on on the commercial front to what the financial implications are or will be, according to his best assumptions."

"You have to master persuasion and advocacy to be an effective director, ... Simply telling other board members what you believe the best course of action to be, and expecting them to go along with it, is not good enough. Fellow directors need to be persuaded of the wisdom of a move if they are to be fully committed to it."

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Ian Macdougall, Retail Analyst, Williams de Broe

The specification of the ideal CFO or FD is a demanding one. Paper qualifications, including the type of accountancy qualification, are relatively unimportant once people reach the higher levels of business. It is what individuals have done with their qualification that really counts. For FDs technical ability is taken as given, a commercial outlook expected and communication ability — whether in persuading the board or handling investor relations — is essential. Those who have what it takes are in great demand, and so they should be. AN

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INTELLECTUAL CAPITAL & financial reporting in the Knowledge Economy

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The financial reporting model is still firmly rooted since its inception by Luca Pacioli 500 years ago. The emphasis of reporting in the industrial age concentrated on the physical existence of the assets of the entity. Hence physical inspection was of paramount importance then, which is one of the critical parts in most audit verification. Globalisation and liberalisation in the knowledge-based economy has reservations about this traditional reporting. There are hidden values, which cannot be found anywhere in these mandatory reports yet they are the value creation drive behind these companies. The hidden values here are the Intellectual Capital (IC). The components of IC are discussed and the importance of recognising it is looked into. The Western and industrialised nations have taken the lead in measuring and managing their IC. The pioneer in IC reporting was Skandia, the largest insurance and financial services company in Scandinavia. Skandia released its world first IC annual report in May 1995. IC will create bountiful opportunities in particular for the accountants in this k-economy if properly researched and developed.

Introduction

In a knowledge society, knowledge is the primary source for individuals and for the economy overall. Land, labour, and capital — the economist's traditional factors of production — do not disappear, but they become secondary. They can be obtained easily, provided there is specialised knowledge. At the same time, however specialised knowledge by itself produces nothing. It can become productive only when it is integrated into a task. (Peter Drucker, "Managing In A Time of Great Change", pp. 76)

The k-economy environment that we are in now is characterised by continuous innovation, the spread of digital and communications technology which is very different from yesteryears. One cannot deny the fact that the concepts used during the industrial age have become redundant, perhaps wasteful in the new economy. During the industrial age, organisations count on physical assets, and natural resources as their source of wealth. Likewise, in the k-economy, the force of globalisation has emerged so strongly that knowledge and communication have become the most critical assets in an organisation. Globalisation, computerisation and information developments have called for the urgent need to recognise intellectual capital.

Ever since A. Stewart published an article in the *Fortune* magazine in January 1991, on "Brainpower", and subsequently, in October 1994, "Your Company's Most Valuable Asset : Intellectual Capital" there has been an overwhelming response from corporate heads, researchers, regulators, academicians, accountants, and the list goes on. Books, articles, magazines and international conferences around the world are all talking about IC. They are all concerned that the value creating factors are not shown or disclosed anywhere in these audited reports.

The pioneer in revealing the hidden values in the traditional statement of accounts is Skandia. Skandia believes that their IC is at least as important as their financial capital in providing sustainable earnings.

Sveiby[17] (1998) highlighted that the high stock premiums in today's stock markets can be one of the indications of an emerging Knowledge-Economy. According to Sveiby, the parallel development of theories and practices in Sweden and in the US have now laid the ground for a first standard for accounting in the Knowledge-Economy, featuring three categories of intangible assets plus a fourth category, financial assets. Sveiby suggests that it is useful to measure intangible assets and that it is possible for managers to create shareholder value, without relying on the traditional indicators.

Based on research from Professor Baruch Lev[14] (1997), at Stern University, New York, on investment patterns in 1929 in the US, approximately 70 per cent went into tangible goods and some 30 per cent went into intangibles. By the 1990s, however the trend was reversed. In the US and Sweden, it was found that a major part of the investments go into intangibles such as Research and Development (R&D), education and competencies, IT software and the Internet. Professor Baruch Lev further commented that the average relationship between market-value and book-value in the late 1970s was one time, in the mid-1990s it had increased to an average of three times, and now it is more than six times the book value.

Sveiby (1998), in his "Intangible Asset Monitor", stated that a process that emphasises intangible assets as consisting of mainly human relationships and knowledge creation, is designed for organisations that are already experiencing the effects of the Knowledge-Economy. He further commented that the first to experience the Knowledge-Economy were the high-tech firms, the service companies and the professional services firms. Sveiby adds that the underlying principle of measuring intangible assets, intellectual capital, is that it must complement the accounting system with a new language for the dialogue of peers, not another system for controlling subordinates.

What Exactly is Intellectual Capital

My interest in this area began when I was looking for a topic for my Master's thesis. As I probed further I found that IC was going through a revolution stage. When I first mentioned that my topic for my research area was IC, the general response was the close link to Intellectual Property (IP). True enough, IP is part of IC, to a certain extent which is further explained below.

A. Stewart (1997) refers to intellectual capital in one sentence as intellectual material — knowledge, information, intellectual property, and experience — that can be put in to use to create wealth. It is collective brainpower. It's hard to identify and harder still to deploy effectively. But once you find it and exploit it, you win. Stewart classified intellectual capital under three components, human, structural and customer capital. Klein and Prusak defined intellectual capital as "Intellectual material that has been formalised, captured, and leveraged to produce a higher-valued asset"

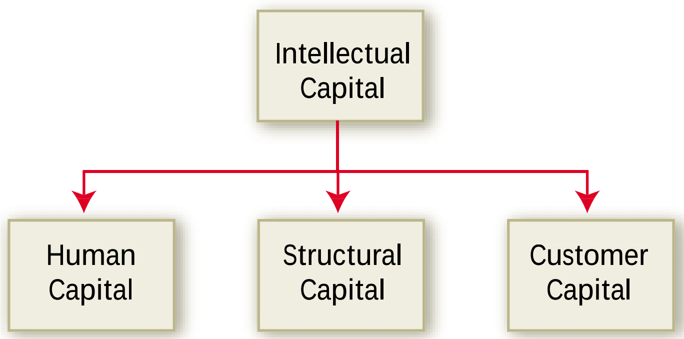
Brooking[5] classified intellectual components of an organisation into four — market assets, intellectual property assets, human-centred assets and infrastructure assets. Brooking stated that market assets are the potential an organisation has due to market-related intangibles. Examples given are various brands, customers and their loyalty, repeat business, backlog, distribution channels, various contracts and agreements such as licensing, franchises and so on. Brooking adds that market assets are important because they give a company a competitive advantage in the market place. The second component is intellectual property assets such as know-how, trade secrets, copyright, patent and various design rights. The intellectual property here represents the legal mechanism for protecting many corporate assets. The third component according to Brooking is human-centred assets. These assets are the collective expertise, creative and problem solving capability, leadership, and entrepreneurial and managerial skills embodied by the employees of the organisation. Brooking adds that unlike market intellectual and infrastructure assets, the company cannot own human-centred assets. The last component is the infrastructure assets such as the technologies, methodologies and processes, which enable the organisation to function. Examples given were corporate culture, methodologies for assessing risk, methods of managing a sales force, financial structure, databases of information on the market or customers, communication systems such as e-mail and teleconferencing systems. Brooking adds that infrastructure assets are important because they bring order, safety, correctness and quality to the organisation.

Edvinsson and Malone[9] in their Navigator reporting model categorised intellectual capital into five areas of focus — financial, customer, process, renewal and development and human. In the world of IC, the financials take on the new role of repository. The process may take hours or decades, but at some point in the future, all IC, if it is to have value, must convert to currency (or some, as yet undefined, substitute). According to Edvinsson and Malone, most companies today are geared towards "total customer service". The digital revolution has created new types of products and services and new types of customers. The consumer of 1997 expects to be able to personally define the product or service to match his needs. The process focus deals with the role of technology as a tool for supporting overall enterprise value creation. Electronic equipment, computers, semiconductors and telecommunications to name a few have allowed for greater organisational flexibility. The renewal and development focus touches on the future by establishing what things the company is doing now to best prepare itself to grasp future opportunities. They have identified customers, attractiveness of the market, products and services and strategic partners, infrastructure and employees as the potential areas of emphasis. Finally, the human focus, which Edvinsson and Malone regard as the most difficult part of the IC model because there is no simple way to measure what is in the heads and hearts of managers and employees.

"Intellectual capital … intellectual material — knowledge, information, intellectual property, and experience — that can be put in to use to create wealth."

FIGURE 1

Components of intellectual capital



Allee[2] defined intellectual capital as customer or external capital, human capital, and structural capital. Customer or external capital refers to alliances and relationships with customers, strategic partners, suppliers, investors and the communities. It also includes brand recognition and goodwill. Allee classified human capital as individual capabilities, knowledge, skills, experience and problem-solving abilities that reside in people in an organisation. Structural capital refers to systems and work processes that leverage competitiveness, including IT, communication technologies, images, concepts and models of how the business operates, databases, documents, patents, copyrights and other 'codified' knowledge.

The Danish Agency for Development of Trade and Industry (DATI)[18] (1997) draws distinction in intellectual capital as individual, structural and financial capital. Individual capital is the value of the competence, skills and knowledge in relation to the company possessed by individuals. Individual capital is related to the value of personal knowledge and commitment essential to companies aiming at flexibility and decentralisation. Individual capital is thus the part of the company's value, which goes home at closing time every day. Structural capital is the value of procedures, technologies, routines and systems left in the company when the employees have gone home. Structural capital is related to the value of the company's infrastructure and the kind of knowledge that is stored in manuals, method guides, product concepts, information systems, goodwill etc. DATI further explained that the interaction between individual capital and structural capital enables the company to produce financial capital, which will turn into equity capital in the ordinary accounts over time.

The Organisation for Economic Co-operation and Development[15] (OECD), (1999) defines intellectual capital as "the economic value of two categories of intangible assets of a company", that is, organisational and human capital. Organisational capital refers, for example, to proprietary software systems, distribution networks, and supply chains. OECD specifically draws the distinction that IC is a subset of intangibles rather than the same as the overall intangible asset base of a business.

Bontis[4], classified IC into three elements: human, structural and relational capital. Human capital refers to the individual-level knowledge that each employee possesses. Structural capital is the non-human assets or organisational capabilities used to meet market requirements. Bontis defined relational capital as being customer capital, the only one feature of the knowledge embedded in organisational relationships. Bontis has excluded intellectual property as it is a protected asset and has a legal definition as opposed to the other components of IC.

It can be summed up that all the authors have identified three elements of IC; human capital, structural capital and customer capital.

Adequacy of Traditional Financial Reporting

The most popular giant software company worth mentioning here is Microsoft. How much is the company's worth? It is evident that the tangible assets of Microsoft may be a few PCs but its real value lies in its knowledge of its workers, the software created and the continuous innovation carried out by Microsoft. It was further pointed out by Prof. G. Chacko that Microsoft's value (as of May 1995 it had a market capitalisation of about US$210 billion) lies in its widely used operating system by its customers. In summary, Microsoft's value lies in the intellectual capital such as the human capital, e.g. the employees' technical skills, creativity etc; structural capital being its database and software; and finally its customer.

The traditional reporting did not cater for these intangible assets such as knowledge of its workers, customers database, as these values did not fit in the bill of measurement and objectivity concepts in preparing the financial statements. This was highlighted in the survey conducted by PricewaterhouseCoopers, in which 28 per cent of the high-tech company leaders believe that their stock is undervalued because market analysts don't appreciate the value of the stuff that doesn't appear in. (*Accounting & Business*, October 2001)

Recently, a research carried out by Zulkarnain Muhamad *et. al.* (2001) found that half of the institutional investors perceived the annual audited financial statement as not credible. This is viewed very seriously and requires immediate attention from regulating agencies to identify and redress the factors perceived as contributing to the lack of credibility. This could perhaps be the start to the recognition of IC, which would supplement the current drive forward to disclosure-based reporting. This, in turn, fits in with the Code on Corporate Governance. This is especially so in Malaysia which has a relatively active but infantile capital market. Most of the Western and industrialised countries such as Australia, in Europe and Canada to name a few are actively looking into IC reporting. Malaysian companies should keep up with this movement in order to avoid being left behind by their foreign counterparts. It is timely and beneficial for Malaysian organisations to begin recognising and incorporating IC in their reporting.

The Financial Accounting Standards Board (FASB), UK has published a Special Report, Business and Financial Reporting, Challenges from the New Economy, reflecting debate over the information needs of New Economy companies and the sufficiency of Old Economy reporting. In the report it was urged that standard setters should focus their attention on :

- Examination of the conceptual and practical issues surrounding recognition of internally generated intangible assets and measurement of those assets;
- Expanded and systematic use of non-financial performance metrics; and
- Expanded use of forward-looking information.

Roger Adams, ACCA's Technical Director highlighted that intellectual capital is one of the areas that should be looked into.

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It is indeed very encouraging, as it appears that the direction towards recognition and measurement of IC is on the way.

The President of the Belgian Institute of Registered Auditors, Paul Behets, during his opening speech at a recent congress of the European Accounting Association, asked "Are Financial Statements an obsolete product?" His answer is "no". Financial Statements are an essential component of the financial reporting system that is necessary for the proper functioning of capital markets[3]. (Richard B. and Phillip W., 2000). I couldn't agree more with Behets, as the current traditional reporting has received many adverse comments of late. In order to improve the traditional reporting it should as a start be supplemented with more disclosures pertaining to the value creating factors of and for the organisation.

Eccles, R. G. *et. al.*[8] (2001) in their "The Value Reporting Revolution", quoted that the traditional corporate reporting model has failed those it ought to serve best. They

"During the financial crisis in 1997, the weaknesses in Malaysian companies were exposed resulting in several organisations going bankrupt or close to being so. Foreign investors' loss of confidence was partly due to lack of corporate governance ..."

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further commented that executives in most corporations feel their company's share prices are undervalued and investors feel frustrated because they are not getting the information they need. The inadequacy of the current traditional reporting issues are addressed and more emphasis on measurement of the wealth of companies in the k-economy are geared towards value-based information. Bob Herz[8] said more value-based information is needed in today's economy such as capital spending, research and development, brand value, market share, customer retention, intellectual capital and other intangible assets.

Asian Financial Crisis and Corporate Governance

Allow me to highlight the lessons we should learn to avoid history repeating itself. During the financial crisis in 1997, the weaknesses in Malaysian companies were exposed resulting in several organisations going bankrupt or close to being so. Foreign investors' loss of confidence was partly due to lack of corporate governance, according to YBhg Dato' Megat Najmuddin Khas[13], President of the Malaysian Institute of Corporate Governance. The Asian financial crisis in 1997-1998 served as a wake up call to the regulatory bodies to improve on reporting, and to compete globally and attract foreign investors. As such the Malaysian Code on Corporate Governance was issued in March 2000. This Code was designed to facilitate corporate self-regulation in the area of corporate governance and has since become effective for all listed companies in Malaysia with periods ended 30 June 2001. The Code established the principles and best practices of good governance and is consistent with international best practices in this area. As the saying goes, "once bitten twice shy", we should not wait until our foreign counterparts point out our shortcomings, as in the issue of lack of transparency, but should keep up with the changes.

Conclusion and Recommendations

Globalisation knows no boundaries, thus the areas on the need to recognise IC should be identified fast. The accountants, in particular should be more vigilant in keeping up with changes in the new environment. They need to be adaptive to the change of environment in view of the k-economy that we are in now. The Western and industrialised countries have been seriously measuring and managing their intellectual capital as it was felt that traditional financial statements failed to reflect a true picture of the value of the company. We, in Malaysia should not ignore the importance of IC. As IC measurement is still at its infancy stage, perhaps as a start organisations should start off by identifying the intangibles, which create value and concentrate on constructing indicators for the IC components. AN

Note : The writer wishes to acknowledge and thank all the respondents for their cooperation, especially Venu Thyagarajan of MMU, Cyberjaya for his supervision, suggestions and recommendations in her Master's Thesis on Intellectual Capital.

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The outsiders

Management Accountants Have Yet to Make an Impact on Non-Profit and Government Organisations.

By Regina Herzlinger

My past experience as a board member of nine large public companies and many small private ones has shown me, at first hand, the importance of managerial accountants in helping overseers to understand, evaluate and guide their organisations.

And yet managerial accountants are largely missing in action when it comes to non-profit and government organisations.

Their absence is unfortunate. Non-profit and government organisations require the assistance of management accountants even more than business organisations. Because they lack the innate oversight mechanisms of businesses, paying customers and owners, non-profits and governments need managerial accounting information to help them plan and evaluate their activities more intensely than businesses. Managerial accountants can play a critical effective oversight role.

After all, many of the clients of non-profit and government organisations are hardly in a position to press for accountability. Picture the homeless as the embodiment of the helplessness of non-profit and government clients. Like them, other clients are often poor and/or in a debilitated physical and emotional state. Nor can they increase accountability by taking their business elsewhere. They frequently do not pay the full cost of the services they receive and the organisation providing the services is typically a monopoly.

Although the ability of voters for government officials to hold managers accountable for their actions is somewhat akin to that of the owners of a publicly traded corporation, the voters have substantially lower power than shareholders. The feedback of owners of a public corporation can be as quick and specific as a stock trade, in response to specific management actions. But voters' feedback is limited by the calendar to election day and cannot be tied to any one specific action. (The growing popularity of referenda is attributable to the voters' desire to provide more specific feedback to the government).

All the oversight groups involved with

non-profit organisations acutely understand this accountability shortcoming.

Three-quarters of non-profit executives noted 'a problem of openness and accountability' in the non-profit sector and more than half predicted that 'public confidence in non-profits will continue to erode'. Non-profit board members and volunteers understand the problem too. All too many of them feel that their efforts do not yield commensurate results.

The importance of this problem becomes apparent in view of the high level of involvement overseers have with non-profit organisations. For example, virtually all US Fortune 500 CEOs serve on non-profit boards — 36 per cent of them serve on six boards. Nearly that percentage spend a whopping 10 or more hours a month on board service. And more than a sixth of the US population serve as volunteers in non-profits.

A primary reason for their discomfort is that non-profit organisations lack even the most primitive information about the results they achieve. Consider, for example, the estimable non-profit organisations that rehabilitate injured people. Their intent is surely noble. But their theory that every dollar produces corresponding social benefits had 'nothing to back that up' in the opinion of *The Chronicle of Philanthropy.* It took a major study to reveal that many of their trainees were not employable even after completing the programme.

Government organisations, too, suffer from the absence of accountability information produced through managerial accounting. As a result, the trust in governmental organisations has steadily eroded, from a high of 80 per cent in the halcyon days of the Kennedy presidency in the US to the low of 20 per cent 30 years later.

The lack of accountability surely contributes to the precipitous drop in voter turnout. In the US, only 33 per cent of eligible voters turned out for the 1998 Congressional elections, down from 59 per cent in 1960. Contrast this with the growth in the percentage of American households that own stocks from 19 per cent in 1983 to a staggering 48 per cent in 1999. Why the difference? Surely one reason is the absence of information in the governmental sector and the deluge of information in the financial one.

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difference in the performances of non-profit and government organisations?

It is impossible to provide a definitive answer because of general absence of accountability data; but two case studies indicate the possibilities. In New York State, the publication of data about the success of providers who performed open-heart surgery caused substantial decreases in death rates from the procedure and increases in the volume of the more successful providers. Similarly, in New York City, simple counts of crime cases and of the success of local police officials in solving them are generally credited as the leading causes of the sharp decreases in crime rates.

Why then, given the intense need for their services, are management accountants notable for their absence in non-profit and government organisations?

I believe one reason lies in the absence of a generally accepted framework for accountability in these organisations. While businesses use widely adopted frameworks such as economic value-added, the balanced scorecard, or the dashboard as instruments of accountability, non-profits and governments have none. Attempts to adapt business accountability mechanisms to the non-business sector are awkward at best because the purpose of non-profit and government organisations is so different from the business sector. For example, while economic value-added is an important tool for measuring the financial results of a business, it is virtually meaningless for organisations whose purpose is not to generate economic returns from the capital invested in them.

On the basis of the 35 years I have spent researching and working with non-profit and government organisations, I have developed the *Four by Four Report* to serve as such an accountability instrument. It addresses the four questions that are of particular importance to the four constituencies of non-profit and government organisations (see Table 1).

The answers to the questions present multiple dimensions with which to measure the organisation's success and to develop new courses of action.

The *four* constituencies each require different answers to these questions.

The *donors* want the organisation to achieve the purposes for which they gave funds, either as donors or taxpayers, in an effective and efficient way.

The *clients* want the best quality services, and as many of them as possible.

The *staff* members want to feel that their work is appreciated, rewarded and used in helpful ways.

And let us not forget about the other major constituency, *society.*

Society grants non-profit organisations a tax-exempt status and funds government organisations so that they can achieve socially important goals. The taxpayers that effectively subsidise these organisations have every right to inquire about the effects of their subsidy.

Most of the time, society lacks the voice, but when it is thwarted its voice becomes powerful indeed. Think about the front page of the *New York Times* or a *60 Minutes* story as the voice for society's concerns.

As shown in Table 2, they each want to know if the organisation has done the right thing for them.

TABLE 2

The Four by Four Report

Clients' Four by Four Report

1. Goals? Have we achieved client's goals in a manner that is effective, efficient, and appropriate to our resources?
2. Distributional equity? Are we fair to different generations and types or clients?
3. Match? Have we matched long-term clients' goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve our clients' goals?

Donor's Four by Four Report

1. Goals? Have we achieved donors goals in a manner that is effective, efficient and appropriate to their donated resources?
2. Distributional equity? Are we fair to different generations and types of donors?
3. Match? Have we matched long-term donor goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve the donors-goals?

Staff's Four by Four Report

1. Goals? Have we achieved staffs goals in a manner that is effective efficient. and appropriate to our resources?
2. Distributional equity? Are we fair to different generations and types of staff members?
3. Match? Have we matched long-term staff goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve the staffs goals?

Society's Four by Four Report

1. Goals? Have we achieved our goals in a manner that society considers effective, efficient, and appropriate for our resources?
2. Distributional equity? Are we fair to different generations and members of society?
3. Match? Have we matched society's long-term goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to meet society's goals?

The Four by Four Report

A government example of the four questions — social security.

To illustrate the accountability effect of the four questions in the *Four by Four Report* let us examine the case of the US government's social security programme. As shown in Table 3, the Social Security Administration fares poorly on all four questions.

TABLE 3

The Four Questions

A government example : social security

1. **Mission v Resources?**
   Poor, as shown by huge deficit.
2. **Equity?**
   Poor, current payers finance past generations and low-income current payers finance high-income past generations.
3. **Match?**
   Poor, long-term needs are financed by short-term payroll tax.
4. **Diversification?**
   Poor, taxes are sole source of funds and government securities sole investment.

To illustrate the accountability aspect of the four constituencies in the *Four by Four Report*, consider the case of a controversial 1999 exhibition by the Brooklyn Museum of Art of a collection owned by UK's Charles Saatchi.

The 'Sensation' exhibition caused a raging fire-storm. New York City's popular Mayor Rudolph (Rudy) Guiliani objected not only to the subject matter of the exhibition, which included a Madonna smeared with elephant dung but also to the secrecy surrounding contributions to defray the expenses of the exhibition. Guiliani contended that Saatchi planned to sell some of the art objects in his collection and was using the exhibition to inflate the value of his holdings. The Mayor cited a contribution by Sotheby's, a major art gallery affiliated with prior sales of Saatchi's art, as evidence of his thesis. He had every right to object because the Brooklyn Museum is a tax-supported organisation.

On the other hand, one purpose of a museum is to enhance people's visions of the world. Displaying cutting edge art is surely one way to achieve that purpose. As the director of New York's Metropolitan Museum of Art notes, "Our obligation is to broaden appetites … [We must] have the integrity and the independence to present things that are not obvious subjects for the public". Further, the museum argued that the Madonna picture was not offensive if it were viewed in the cultural context of the African artist who produced it. Dung is not an unknown material in that culture. As for the Saatchi and Sotheby contributions, they were legitimate ways to defray the substantial expenses of mounting a special exhibition. These costs are barely dented by the admission fees that are usually charged for these exhibitions. Notes the director of New York's SalomonlR Guggenheim Museum, "It's absolutely for sure that museums cannot survive on admission alone. If you were to look at our budgets and divide by the number of visitors, the average price would have to be around US$75."

But, just as the Brooklyn Museum was gaining ground in these defences, a new source of complaint arose from its professional curatorial employees. They groused publicly about interference by Saatchi in their display of his art objects. In retrospect, the public airing of their views was not surprising. Like other professionals, their loyalty was split between the mores of their profession and the institution for which they worked. In this case, their professional norms won out.

How could the *Four by Four Report* have helped this unfortunate situation?

To answer this question, consider the *Four by Four Report* in Table 4. Had it been available to the overseers, they could have contemplated the costs and benefits of the exhibition more clearly, including the apparently unanticipated negative response from the staff and from society, in the form of Mayor Guiliani. The *Four by Four Report* could also have served as a useful accountability mechanism to the public. After all, the complaints about the Saatchi and Sotheby donations fo-

TABLE 4

Responding to the Four Constituencies

Example : The Brooklyn Museum's Sensation Exhibition — the Saatchi Collection

Clients?

- Cutting-edge art, including a Virgin Mary portrait smeared with dung.

Donors?

- Charles Saatchi donated US$160,000 and was given considerable control over the exhibition.
- The art gallery Sotheby's contributed too, perhaps in anticipation of selling some of the works in the exhibition.

Staff?

- Their role diminished by donor. Employees 'fretted that Saatchi was taking over'.

Society?

- New York City Mayor withdrew government support.
- *New York Times* prints many unfavourable stories.
- Saatchi planned to sell some of his collection after the exhibition.

> "The public was surprised, during the 'Sensation' show … at how museums raise money from people who have commercial interests in the art being shown … Is disclosure the answer?"
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cused more on the secrecy of the donations than on their nature.

As *The New York Times* noted, "The public was surprised, during the 'Sensation' show … at how museums raise money from people who have commercial interests in the art being shown … Is disclosure the answer?"

The Four by Four Report

A Complete Example from Williams College

When Williams College announced in 1999 that its record endowment level, swollen to over a billion dollars by the buoyant US stock market, would enable it to maintain current prices for education in the forthcoming year, it expected plaudits. And, indeed, the move was hailed by some college administrators as bold, novel and appropriate.

But, to its surprise, the announcement was greeted with criticism too. Some complained that the funds should have been used to increase the diversity of students; to provide more financial aid; or to increase the programmes or faculty.

In the *Four by Four Report* terms, Williams was making an inter-generational transfer by using current gains in the endowment to benefit future students. But the move was viewed as inadequate. As one current student noted, "I don't think it's any act of generosity … to make the college more affordable, it's just a fact of the American boom. A more extraordinary announcement would have been that they're hiring more faculty, or they're giving a free ride to … students from Appalachia, or South Africa, or inner-city blacks … That's the School's challenge".

TABLE 5

The Four by Four Report

Williams College decision not to increase tuition

	Donors	Students	Faculty and Staff	Society
Missions v Resources	?	?	?	?
Equity?	?	Future Generation : OK Other students?	?	?
Match?	?	?	?	?
Sustainability?	?	?	?	?

As indicated by the many question marks in Table 5, a complete *Four by Four Report* would have enabled the college overseers to forecast these responses.

The Four Questions would have raised the issues of whether these funds should be used to change the resources devoted to programmes (question 1) and whether more long-term funds should be allotted to the long-term goals of faculty or financial aid expansion (question 2) or to diversify the student body (question 4). Similarly, the four constituencies' analogies would have revealed that donors, students, staff, and society may see more important uses for the money than freezing tuition and fees.

As a result, Williams College could have better anticipated the responses. For example, it could have used the increased endowment to benefit all four constituent groups in ways that responded to more than one need. And if it had determined that freezing educational fees was the best and only use for the endowment, a *Four by Four Report* would have better prepared the college to respond to its critics. Non-profit and government organisations must become more accountable to their constituents.

The Four by Four Report is a tool that managerial accountants can use to fulfil this important function. AN

Note : Regina Herzlinger is a CIMA visiting professor from Harvard Business School.
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And let us not forget about the other major constituency, *society.*

Society grants non-profit organisations a tax-exempt status and funds government organisations so that they can achieve socially important goals. The taxpayers that effectively subsidise these organisations have every right to inquire about the effects of their subsidy.

Most of the time, society lacks the voice, but when it is thwarted its voice becomes powerful indeed. Think about the front page of the *New York Times* or a *60 Minutes* story as the voice for society's concerns.

As shown in Table 2, they each want to know if the organisation has done the right thing for them.

TABLE 2

The Four by Four Report

Clients' Four by Four Report

1. Goals? Have we achieved client's goals in a manner that is effective, efficient, and appropriate to our resources?
2. Distributional equity? Are we fair to different generations and types or clients?
3. Match? Have we matched long-term clients' goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve our clients' goals?

Donor's Four by Four Report

1. Goals? Have we achieved donors goals in a manner that is effective, efficient and appropriate to their donated resources?
2. Distributional equity? Are we fair to different generations and types of donors?
3. Match? Have we matched long-term donor goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve the donors- goals?

Staff's Four by Four Report

1. Goals? Have we achieved staffs goals in a manner that is effective efficient. and appropriate to our resources?
2. Distributional equity? Are we fair to different generations and types of staff members?
3. Match? Have we matched long-term staff goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to achieve the staffs goals?

Society's Four by Four Report

1. Goals? Have we achieved our goals in a manner that society considers effective, efficient, and appropriate for our resources?
2. Distributional equity? Are we fair to different generations and members of society?
3. Match? Have we matched society's long-term goals with long-term resources?
4. Diversification? Do we use sufficiently diverse resources to meet society's goals?

The Four by Four Report

A government example of the four questions — social security.

To illustrate the accountability effect of the four questions in the *Four by Four Report* let us examine the case of the US government's social security programme. As shown in Table 3, the Social Security Administration fares poorly on all four questions.

To illustrate the accountability aspect of the four constituencies in the *Four by Four Report*, consider the case of a controversial 1999 exhibition by the Brooklyn Museum of Art of a collection owned by UK's Charles Saatchi.

The 'Sensation' exhibition caused a raging fire-storm. New York City's popular Mayor Rudolph (Rudy) Guiliani objected not only to the subject matter of the exhibition, which included a Madonna smeared with elephant dung but also to the secrecy surrounding contributions to defray the expenses of the exhibition. Guiliani contended that Saatchi planned to sell some of the art objects in his collection and was using the exhibition to inflate the value of his holdings. The Mayor cited a contribution by Sotheby's, a major art gallery affiliated with prior sales of Saatchi's art, as

TABLE 3

The Four Questions
A government example : social security

1. **Mission v Resources?**
   Poor, as shown by huge deficit.
2. **Equity?**
   Poor, current payers finance past generations and low-income current payers finance high-income past generations.
3. **Match?**
   Poor, long-term needs are financed by short-term payroll tax.
4. **Diversification?**
   Poor, taxes are sole source of funds and government securities sole investment.

TABLE 4

Responding to the Four Constituencies

Example : The Brooklyn Museum's Sensation Exhibition — the Saatchi Collection

Clients?

- Cutting-edge art, including a Virgin Mary portrait smeared with dung.

Donors?

- Charles Saatchi donated US$160,000 and was given considerable control over the exhibition.
- The art gallery Sotheby's contributed too, perhaps in anticipation of selling some of the works in the exhibition.

Staff?

- Their role diminished by donor. Employees 'fretted that Saatchi was taking over'.

Society?

- New York City Mayor withdrew government support.
- *New York Times* prints many unfavourable stories.
- Saatchi planned to sell some of his collection after the exhibition.

evidence of his thesis. He had every right to object because the Brooklyn Museum is a tax-supported organisation.

On the other hand, one purpose of a museum is to enhance people's visions of the world. Displaying cutting edge art is surely one way to achieve that purpose. As the director of New York's Metropolitan Museum of Art notes, "Our obligation is to broaden appetites … [We must] have the integrity and the independence to present things that are not obvious subjects for the public". Further, the museum argued that the Madonna picture was not offensive if it were viewed in the cultural context of the African artist who produced it. Dung is not an unknown material in that culture. As for the Saatchi and Sotheby contributions, they were legitimate ways to defray the substantial expenses of mounting a special exhibition. These costs are barely dented by the admission fees that are usually charged for these exhibitions. Notes the director of New York's SalomonlR Guggenheim Museum, "It's absolutely for sure that museums cannot survive on admission alone. If you were to look at our budgets and divide by the number of visitors, the average price would have to be around US$75."

But, just as the Brooklyn Museum was gaining ground in these defences, a new source of complaint arose from its professional curatorial employees. They groused publicly about interference by Saatchi in their display of his art objects. In retrospect, the public airing of their views was not surprising. Like other professionals, their loyalty was split between the mores of their profession and the institution for which they worked. In this case, their professional norms won out.

How could the *Four by Four Report* have helped this unfortunate situation?

To answer this question, consider the *Four by Four Report* in Table 4. Had it been available to the overseers, they could have contemplated the costs and benefits of the exhibition more clearly, including the apparently unanticipated negative response from the staff and from society, in the form of Mayor Guiliani. The *Four by Four Report* could also have served as a useful accountability mechanism to the public. After all, the complaints about the Saatchi and Sotheby donations fo-

> "The public was surprised, during the 'Sensation' show … at how museums raise money from people who have commercial interests in the art being shown … Is disclosure the answer?"
>
> *New York Times*

cused more on the secrecy of the donations than on their nature.

As *The New York Times* noted, "The public was surprised, during the 'Sensation' show … at how museums raise money from people who have commercial interests in the art being shown … Is disclosure the answer?"

The Four by Four Report

A Complete Example from Williams College

When Williams College announced in 1999 that its record endowment level, swollen to over a billion dollars by the buoyant US stock market, would enable it to maintain current prices for education in the forthcoming year, it expected plaudits. And, indeed, the move was hailed by some college administrators as bold, novel and appropriate.

But, to its surprise, the announcement was greeted with criticism too. Some complained that the funds should have been used to increase the diversity of students; to provide more financial aid; or to increase the programmes or faculty.

In the *Four by Four Report* terms, Williams was making an inter-generational transfer by using current gains in the endowment to benefit future students. But the move was viewed as inadequate. As one current student noted, "I don't think it's any act of generosity … to make the college more affordable, it's just a fact of the American boom. A more extraordinary announcement would have been that they're hiring more faculty, or they're giving a free ride to … students from Appalachia, or South Africa, or inner-city blacks … That's the School's challenge".

TABLE 5

The Four by Four Report

Williams College decision not to increase tuition

	Donors	Students	Faculty and Staff	Society
Missions v Resources	?	?	?	?
Equity?	?	Future Generation : OK Other students?	?	?
Match?	?	?	?	?
Sustainability?	?	?	?	?

As indicated by the many question marks in Table 5, a complete *Four by Four Report* would have enabled the college overseers to forecast these responses.

The Four Questions would have raised the issues of whether these funds should be used to change the resources devoted to programmes (question 1) and whether more long-term funds should be allotted to the long-term goals of faculty or financial aid expansion (question 2) or to diversify the student body (question 4). Similarly, the four constituencies' analogies would have revealed that donors, students, staff, and society may see more important uses for the money than freezing tuition and fees.

As a result, Williams College could have better anticipated the responses. For example, it could have used the increased endowment to benefit all four constituent groups in ways that responded to more than one need. And if it had determined that freezing educational fees was the best and only use for the endowment, a *Four by Four Report* would have better prepared the college to respond to its critics. Non-profit and government organisations must become more accountable to their constituents.

The Four by Four Report is a tool that managerial accountants can use to fulfil this important function. AN

Note : Regina Herzlinger is a CIMA visiting professor from Harvard Business School.
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SECuritisation

Concept and Application

By Wong Mun Fai & Wong Mun Ping

Securitisation is an innovative technique in raising finances for a company. Its primary objective is two-fold — convert dull assets into usable cash and clean up the balance sheet of a company.

By definition, securitisation refers to the parcelling and selling pools of eligible assets by the company owning the assets to a special purpose vehicle (SPV) company, which issues debt securities to finance the purchase of such assets. The SPV uses cash-flow from the assets to service the debt it created to purchase these assets. The debt securities are usually rated and tradable in the secondary market.

Overview of Securitisation

Three basic components are present in a securitisation transaction :

1. **The owner of the assets.**
This is the company that owns the assets. In other words, this is where the assets originate. As a result, the company owning the assets is also known as the 'originator'.
2. **The assets.**
The most commonly used assets in securitisation are receivables. Receivables can take many forms including mortgage loans, credit card balances, medium to long-term commercial rental income, and even utility bill receivables of independent power producers.
3. **The SPV that purchases the assets.**
The SPV is established to purchase assets from a company that owns these assets. The SPV can be owned by a totally different entity, or it can be owned (wholly or partly) by the company that owns the assets. Eligible assets are transferred to the SPV and become the underlying assets for the SPV to issue debt securities to fund the purchase of assets. The SPV is also known as the 'issuer'.

Reasons for Using Securitisation

The most common reason for using securitisation is that the company is able to convert its assets into cash. There are, however, other specific reasons for using securitisation :

1. **Alternative source of financing.**
Securitisation is another alternative in obtaining financing at (potentially) lower borrowing rates. It is especially useful when conventional financing is not permitted by market circumstances — in times of recession, financial institutions are unlikely to lend and in times of boom, financial institutions cannot keep up with the demand for financing.
2. **Improve return on capital.**
With securitisation, a company will be able to own assets with lower capital as the assets are funded by the issuance of debt securities (as a result of securitisation) that is in the book of the SPV. With less capital employed by the company, return on capital will improve significantly.
3. **Elimination of mismatch between borrowing and lending.**
Financial institutions accept deposits (borrowings by financial institutions) to give out loans (lending by financial institutions). Deposits are usually short-term with maturity of one year or less whereas mortgage loans are long-term with maturity of 25 years or more. In other words, the long-term lending is funded by short-term borrowings. With securitisation, mortgage loans are transferred to the SPV where debt securities with longer tenure, say five to 12 years, are issued. Therefore, securitisation plays its role in facilitating a more appropriate financing structure to the originator where lending is

more closely matched by long-dated borrowings.

4 **Off-balance sheet financing.**
The selling of eligible assets to an SPV not only converts assets into usable cash, it also effectively removes the assets (receivables) off its balance sheet. The balance sheet is left with cash that can be used for other purposes, such as business expansion or establishing new businesses.

5 **Value added through rating exercise.**
In most cases, the assets used in securitisation are rated by a rating agency. This will enhance the credit rating of the debt securities in the capital market and therefore lower pricing can be fixed by the SPV. If the SPV is owned (wholly or partly) by the company that originates those quality assets, a good rating on (the debt securities of) the SPV will more or less add value to the company. It is very likely that an originator with lower credit rating is able to issue debt securities with a higher credit rating. It is the creditworthiness of the underlying assets rather than the originator that is rated and marketed.

6 **Cheaper borrowing costs.**
Cheaper borrowing costs are made possible because securitised assets, with the help of credit enhancement, will have a credit rating that is above that of the originator. In addition, the debt securities are issued directly into the capital market, rather than through financial institutions. The above situations result in savings to the originator as the cost of the securitisation transaction will be lower than the lending spread incurred by the originator in order to achieve the required return on capital. These savings are ultimately passed on to new borrowers in the future.

7 **Diversify source\s of financing.**
Securitisation allows the originator to diversify its sources of funding so that it does not depend solely on financing from financial institutions.

Parties in Securitisation

Originator — Originator refers to the company that initially owns the assets (usually receivables) and has the intention of converting the assets into usable cash, and cleaning up the balance sheet so that there are no excessive receivables.

Issuer — Issuer refers to the SPV that is set up to purchase the assets from the originator. The issuer can be wholly or partly owned by the originator. It can also be a totally separate entity that is not owned by the originator at all. If the originator intends to convert its assets into cash and has no intention to engage in the financial service business, it will choose not to own the SPV. On the other hand, if the originator intends to convert assets into cash and engage in the financial service business, it may choose to own the SPV, either wholly or partly.

Lead Underwriter — The Lead Underwriter purchases the debt securities issued by the issuer and sells it to investors in the secondary market.

Trustee — The Trustee is usually appointed in most instances, at a fee, to safeguard the interest of investors who invest in the debt securities issued by the issuer. The trustee manages the bank account pertaining to the operation of the assets, and performs financial reporting to various parties in a securitisation.

Servicer — Servicer is a party that will continue to administer, at a fee, the day-to-day operations pertaining to the assets that have been sold to the issuer. This administration service is very likely to be outsourced to the originator for practical reasons. This is because the issuer has owned those assets and has the know-how in administering the operations of those assets. It is also necessary that the process of securitisation is transparent to borrowers by using the originator to continue servicing them so that there is no disruption to relationship with customers.

Back-up servicer — As a contingency plan, a back-up servicer is usually appointed, at a fee, to take over the administration function carried out by the servicer should disruption be experienced by the servicer. A back-up servicer usually has very similar infrastructure and know-how as that of the servicer in order that the activity can be taken over with minimum downtime.

Rating agency — A rating agency is usually appointed, at a fee, to rate the debt securities issued by the issuer. Technically speaking, it is the assets of the originator that are rated. This is the 'pass-through' effect where the cash flow and credit risks are passed through from the assets to the debt securities. For this reason, the debt securities issued by the issuer are also known as 'pass-through' securities. A (good) rating from the rating agency enhances the credit rating of the debt securities and the issuer can therefore fix a lower pricing in order to maximise return for the SPV. The rating agency also ensures that criteria governing the eligibility of assets are complied with at all times.

Eligible Assets Defined

As mentioned above, eligible assets securitised are mostly receivables. There are different types of receivables. In other words, securitised assets can be either existing receivables, or receivables that will arise in the future. While the former is known as Asset-Backed Securitisation, the latter is commonly known as Future Flows Securitisation.

In the US, where a substantial part of the total securitisation market is based on mortgage receivables, a distinction is made between Mortgage-Backed Securitisation and Asset-Backed Securitisation. Securities that are backed by receivables arising out of real estate are known as Mortgage-Backed Securities and all other securities are categorised as Asset-Backed Securities.

Characteristics of Eligible Assets

Assets that are eligible for securitisation have at least five characteristics.

The first characteristic of eligible assets is the ability to generate a series of future cash flows (future economic benefit) with contractual certainty. It is the future cash flow that is valued and utilised by the originator and the issuer to cooperate in obtaining upfront cash flow.

The second characteristic is the availability of collateral to the assets securitised to the issuer. This is prevalent in the case of mortgage loans, which provide an avenue to the issuer to recover outstanding arrears in defaulted mortgage loans from its disposal. However, other assets such as credit card balances and utility bill receivables do not provide such a security feature. The next best level of comfort that the issuer can have is the ability to suspend service when the accounts in arrears exceed the grace period stipulated in the service agreement. This will, to a certain extent, deter consumers from defaulting their accounts.

The third characteristic relates to the distribution of risk. The assets pool comprises a large portfolio of individual assets, where the poor performance of one asset is not likely to distort the overall performance of the pool. Nevertheless, the entire pool can be treated as a single asset.

The forth characteristic of eligible assets is their homogeneity. Homogeneous assets mean there is no wide variation in documentation, product type and origination methodology. Homogeneity is the key to pooling multiple assets as a pool for securitisation purposes.

The fifth characteristic is the absence of an executory contract. In order that the assets can be securitised, they must remain operational in the event that the originator ceases as a going concern. Clauses in the executory contract may impose obligations on the originator and make the securitisation not workable. For example, a real estate company that securitises its rental income receivables to an issuer and provides property maintenance to the issuer will make the securitisation not workable. This is because the winding up of the originator (real estate company) will render the property not being maintained as stipulated in the maintenance contract.

Criteria of Eligible Assets

Having possessed the necessary characteristics, assets must meet specific criteria set out by the originator and the rating agency. While both the originator and rating agency determine the criteria of eligible assets, the rating agency ensures the continued compliance of such criteria.

The criteria of eligible assets are different for each class of assets. Depending on the characteristics of the assets, these criteria are to ensure the continued 'performance' in generating cash-flow in its entire life.

Criteria applicable to residential mortgage loans may include the following :

1. The margin of financing must not exceed a pre-determined percentage in relation to value of assets;
2. The loan-to-valuation ratio must remain below a pre-determined percentage throughout the tenure of loans;
3. The loans must not be in arrears for more than a pre-determined period of time; and
4. The loans must be covered by valid mortgage insurance.

In-store credit card balances, on the other hand, may be given the following criteria :

1. The accounts must have existed for at least a fixed period of time;
2. The accounts must remain active following securitisation;
3. The accounts must not be in arrears for more than a pre-determined period of time; and
4. The accounts must be covered by a valid credit card payment insurance.

Transfer of Eligible Assets to SPV

Securitisation involves the transfer of receivables, not a borrowing on the security of the receivables, from the originator to the SPV. In legal terms, this is known as assignment of receivables, which signifies that the assignment of receivables is effectively a 'true sale', and not a financing against the security of the receivables. It is the 'true sale' of receivables by the originator to the SPV that provides 'bankruptcy remoteness' in securitisation, insulating the SPV from the originator. If the originator were to go bankrupt or get into financial difficulty, the rights of the investors on the assets held in trust by the SPV remain intact and the SPV continues to receive cash flow to service the debt securities.

Rating and Credit Enhancement

It is usually mandatory for the eligible assets to be rated before they are securitised. The rating agency will determine a credit rating based on the characteristics of a pool of underlying assets and its performance under the stress test, and structure of the SPV and the trust. Credit enhancement will be required by the rating agency in the event that the credit rating is not satisfactory in its own right. Credit enhancement can be provided by the originator or third parties and it takes many forms :

1. **Over-collaterisation**. This is done by providing security with value exceeding the face value of the debt securities. The disadvantage is that this will 'consume' assets that are otherwise available for securitisation in the future.
2. **Sub-ordination**. This is a structural credit enhancement where the debt securities are divided into senior securities and junior securities. The existence of junior securities enhances the credit rating of senior securities.
3. **Covenants by originators to replace bad assets**. This covenants effectively mean that the pool of assets will remain 'performing' at all times, and event of default is eliminated.
4. **Assets insurance**. It is common for the originator to take up insurance as a protection against the non-performance of assets that may eventually lead to foreclosure of the same. Asset insurance ensures that shortfall in the proceeds from disposal of assets is reimbursed by the insurer.
5. **Third party or parent company guarantee.** Third party guarantee can be in the form of bank guarantee or letter of credit. A guarantee from the parent company will also enhance credit rating of the assets.

Application of Securitisation in Different Industries

Securitisation has very wide applications across different industries. The most common application is in residential mortgage loans of financial institutions. However, its application is being extended to other areas, namely :

1. Motor vehicle hire purchase loans;
2. Equipment leases;
3. (In-store) Credit card balances;
4. Aircraft leases and revenues;

5 Utility bill receivables;

6 Government revenues; and

7 Future flows (receivables that are yet to be created).

Securitisation in Malaysia

Securitisation commenced operation in Malaysia in 1986 when the Government set up a mortgage financing body known as Cagamas Berhad (Cagamas) to promote the secondary mortgage market in Malaysia. Cagamas is by far the most important and active issuer of securitised instruments in Malaysia. It is the SPV between financial institutions (as primary mortgage lenders) and investors in private debt securities. As of December 2000, the amount of Cagamas debt securities issued and outstanding stood at RM21.48 billion. As of the same date, Cagamas had securitised 23.8 per cent of the outstanding housing loans of the financial institutions.

Other than Cagamas, it is understood that Pengurusan Danaharta Nasional Berhad (Danaharta) is keen in taking steps to securitise some of its rehabilitated and performing loans in late 2001. Danaharta believes that mortgage-backed securitisation will not only result in better recovery, but also assist in developing the Malaysian capital market in a wider and deeper dimension.

Danaharta comments that as at 31 December 2000, it had within its portfolio approximately RM5.45 billion of rehabilitated (and now performing) loans; of which approximately RM3.71 billion had been performing for more than 12 months (thereby indicating the robustness of their restructured cash flows). These performing loans valued at RM3.71 billion would be available for securitisation in tranches.

On 21 November 2001, Danaharta was reported to be selling RM310 million in mortgage-backed securities to generate cash and these will be secured by RM570 million of performing loans held by the national asset management company. According to Danaharta, it is undertaking the asset securitisation exercise instead of an outright sale of the loans because securitisation is a more efficient method of divestment as it overcomes the operational difficulties in selling or auctioning a large number of mortgage loan accounts and avoids the risk of 'cherry picking' by investors. The exercise is also helping the government in promoting securitisation and developing a viable market.

The said securitisation has the following credit enhancements :

1 The debt securities are over-collaterised, namely the RM310 million debt securities are backed by RM570 million worth of assets.

2 The debt securities are subordinated into senior notes and subordinate notes, where the senior notes are distributed through private placement, and the subordinate notes are fully taken up by Danaharta. The subordinate notes will not be traded in the securities market.

3 There will be a reserve account as credit protection to cover any shortfall in payment for the senior notes. The account will hold on-going funds equal to interest payment for the next one year.

4 Repayments on the subordinate notes will be made only after full settlement of the senior notes. This means that Danaharta will bear the losses from any default on the loan repayment.

As a result of credit enhancement, the senior notes have been rated AAA by Rating Agency Malaysia Berhad.

According to Danaharta, this marks the first of a series of securitisation in the next two years. Danaharta will monitor the success of this issue and plan accordingly for future issues. The whole series of securitisation is in line with Danaharta's plan to divest all performing loans and cease operation in the year 2005.

In short, the setting up of Danaharta has addressed the issues of non-performing loans by transforming them into performing loans. It has also created another active player in the market. Another important aspect is that the process of securitisation is also helping to develop the Malaysian capital market further.

In this context, securitisation is like a process of slicing a rotten apple. It is not the slicing that makes the rotten apple a good apple. It is the process of slicing away the rotten part of the apple that renders the sliced apple good. In other words, securitisation serves to re-package non-performing loans into performing loans again.

In order to facilitate the issuance of asset-backed debt securities in the Malaysian capital market, the Securities Commission has issued 'Guidelines on the Offerings of Asset-Backed Debt Securities' on 11 April 2001. The Guidelines serve to set out clear and transparent criteria in implementing securitisation transactions as required by the Commission pursuant to Section 32 of the Securities Commission Act 1993. The Commission has also issued '*Frequently Asked Questions — Guidelines on the Offerings of Asset-Backed Debt Securities*' on 12 September 2001 to provide additional information to some common questions on asset-backed debt securities.

With the active involvement of Cagamas and Danaharta in securitisation and the introduction of guidelines from the Commission, securitisation in Malaysia is fast gaining popularity in becoming an alternative financing technique. In addition, applications in areas other than mortgage-backed securitisation should be encouraged and explored, considering its outcome in promoting further development in the Malaysian capital market. AN

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Physicists love the word 'entropy'. It refers to the tendency every natural system has to move from a state of order to that of maximum chaos. Entropy explains why astronomers believe the universe appears to be heading toward a final 'heat death', countless billions of years from now. Entropy can also be used to rationalise why your clients' accounts sometimes refuse to balance; and why your teenager's bedroom might look like a concussion grenade just went off in it.

Not surprisingly, entropy also works in our financial lives. This regular feature represents Akauntan Nasional's (AN) serious bid to educate all Malaysians of the need for wise adherence to sensible financial planning principles and strategies. Each accountant is a centre of influence — in your office, to your colleagues and clients; and in your home, to your family. Money Tree is thus designed to help you learn and then teach — in steps — all that is important in crafting a life of financial abundance, bounty and contentment.

Why on Earth Does the Rule of 72 Work?

By Rajen Devadason

Virtually all human progress has resulted from responses to a rather special one-word ques tion : 'Why?'

Time and time again it has proved useful, profitable and illuminating. Why do I say that? For ready examples, just think about the long-run fruit of Alexander Graham Bell's, Henry Ford's, and Thomas Alva Edison's cerebral pursuits.

These giants of invention and industry must have asked, in one form or another : **Why** can't people talk over great distances? **Why** can't metal be forged and fashioned to allow us to travel far and wide over land? **Why** can't night be turned to permanent day, thus doubling each 24 hours' store of productive time?

Hard on the heels of their questions came their answers. And that's why we have the telephone, which is eminently useful; the entire automotive industry, which is immensely profitable; and the light bulb and its close cousins, all of which are outstandingly illuminating.

This simple word 'WHY', all by itself, suggests a thirst for knowledge that cannot be quenched. And so, in this column, we will rely upon 'WHY' to help us better understand an old, all-too-familiar friend.

Almost everyone who works in the financial sector has heard of the ubiquitous Rule of 72 and its tremendous predictive power to illustrate the snowballing effect of compound interest. Accountants, bankers and financial planners are especially adept at taking the number '72' and mentally dividing it by the absolute value of an interest rate (meaning 6 NOT 0.06 when considering six per cent, for instance).

We do so, to quickly work out the number of years compound interest needs to double our money.

A simple example will make things much clearer : **72 divided by 6 = 12**. So, by the Rule of 72, we know that if you have RM10,000 invested in an investment vehicle that compounds at a steady six per cent each year, it will take you 12 years to grow that money to RM20,000.

The same nifty rule can be utilised to figure out what inflation rate will halve your buying power in a set number of years. If you plan to retire in 18 years, you have more than a passing interest in knowing what inflation rate will result in RM1,000 today (in 2002) only being able to buy RM500 worth of goods and services in 2020. To do so, all you have to do is take 72 and divide it by 18. The answer is four, so the inflation rate we're looking for is four per cent per annum.

The Rule of 72 can also be of great help to debtoholics groping for some way of comprehending the rate their liabilities are ballooning. To illustrate that, consider this fictional scenario.

WENG YANG DECIDES ENOUGH IS ENOUGH!

Late one night, a depressed yet strangely hopeful Weng Yang entered his rented home. After telling Alice about Shankar's condition — stable but sprouting tubes through his nose, veins and elsewhere — Weng Yang explained the gist of a radical debt repayment plan Paul had painstakingly outlined to him.

Then, after changing his clothes, Weng Yang sat down with Alice at the kitchen table. Together they tabulated all the sums of money they owed various parties.

This is what they put down on paper, with the help of Weng Yang's dusty, trusty Casio calculator.

WENG YANG'S DEBT SUMMARY

NAME	BALANCE RM	INTEREST RATE RM	COMPOUNDING PERIOD RM	ANNUALISED INTEREST RATE %
Tan Ah Kow *(Alice's brother)*	10,000	0.0%	NONE	0.0%
Bill Chaang *(Chee Seng's uncle)*	5,000	10.0%	annual	10.0%
Donald Koo *(Chee Seng's cousin)*	6,000	1.0%	monthly	12.68%
Big Bank Visa	5,000	1.5% nominal monthly, actually 0.0493% daily	daily	19.71%
Big Bank OD	4,000	7.8%	annual	7.80%
Total	**30,000**			

Once they had totalled the various amounts, Alice sighed in frustration …

… Weng Yang said, "According to Paul, Albert Einstein was so impressed with the snowballing effects of compound interest that he called it the eighth wonder of the world!"

"Did Einstein really say that?" asked Alice incredulously.

"I guess. That's what Paul said, and I suppose he'd know! The point is that since our credit cards now charge 1.5 per cent a month — before September 1998 they charged two per cent a month — that works out to about 1.5 per cent divided by 30 or about 0.05 per cent a day. Actually, it is a little lower because what they do is take 1.5% x 12, which is 18 per cent, and divide that by the 365 days in a year."

"How much is that exactly?" asked Alice.

"Good question. I think Paul said it works out to 0.0493 per cent being charged per day. That then needs to be compounded each day. I'm not sure if I remember what Paul said correctly, but the calculation is quite simple."

"Show me."

Weng Yang nodded and began scribbling on a piece of paper, intermittently looking at his Casio and tapping its square, bouncy keys. When he was done, he slid the sheet of paper across to his wife.

ANNUALISED INTEREST RATE FOR BIG BANK VISA

(daily compounding)	= [(1+0.0493%)^365 – 1]
	= [1.000493^365 – 1]
	= 1.197098435 - 1
And rounding that to 4 decimal places :	= 1.1971 – 1 = 0.1971 = 19.71%

"…the point that I think Paul was trying to drive home to me was that if we succeed in lowering the effective interest rate on our RM1,000 in a regular bank savings account earning two per cent a year, RM3,000 in a fixed deposit account earning four per cent a year, and RM5,000 in a bond-based unit trust earning six per cent a year."

"If only…" muttered Alice wistfully.

"Don't worry, dear. Hopefully, we'll be high interest debt, then even if we only maintain the size of our current payments, we will make faster headway."

"I see, I see," said Alice, nodding vigorously.

"Paul mentioned something called the Rule of 72. He told me I should tell you about it."

"What is the Rule of 72?"

"Apparently, it is a simple way of figuring out how long it takes money to double."

"That would be good if we actually *had* some money to double."

Weng Yang frowned. He didn't like the sound of frustration creeping back into Alice's voice, but he doggedly went on with his explanation. "Unfortunately, the Rule of 72 also works well in calculating how long it takes a debt to double in size."

"Ouch!" Alice grimaced, and then said, "OK, you've convinced me. Tell me how it works."

"I'll start with two pleasant examples. Let's imagine we actually have some money saved and invested. I'll assume we have able to turn such pipedreams into reality soon. Now, let me ask you, if we didn't touch the money in those three different accounts, how long would it take for the money in each account to double?" asked Weng Yang.

"Let me see. You said that we imagine we have RM1,000 in a savings account earning two per cent. To double, we would need 100 per cent growth, so I would say it'll take 100 divided by 2, 50 years, to make the savings account money grow to RM2,000." Alice stopped waiting for Weng Yang to say something.

"Go on," he said encouragingly.

"I know that look. You're setting me up."

"Yes, I am. But go on, do your mental calculations first."

"OK. RM3,000 in an FD earning four per cent. I'd say it'd take 25 years to double to RM6,000. And as for the RM5,000 in the bond-based unit trust, what's 100 divided by 6?"

Weng Yang dutifully used the calculator and replied, "16 and two-thirds."

"Right, so it would take that RM5,000 16 years and 8 months to grow to RM10,000.

How did I do?"

"Stupendously and magnificently… wrong!"

Alice's eyes hardened. "What do you mean wrong?"

"You forgot to account for Einstein's 8th Wonder."

"Compound interest?"

"Precisely. That's where the Rule of 72 comes in. If you take 72 and divide it by any interest rate, just using the absolute number, it'll give you the number of years needed to double your money. Alternatively, it also works if you take 72 and divide it by the number of years you have in mind, to work out the required interest rate to double your money in that time."

"Let me see," said Alice, "if I take 72 and divide it by the savings account interest rate of two per cent, then 72 divided by 2, equals 36 years. It'll take 36 years to double our money?"

"Yes! Not 50," said Weng Yang. "And similarly RM3,000 earning four per cent a year will double to RM6,000 in, 72 divided by 4, 18 years. Not 25. And RM5,000 growing at six per cent a year will double to RM10,000 in just 12 years, not 16 years and 8 months. That's the power of compound interest!"

"Well, all that is well and good, but we don't have any investments or savings. What does all this have to do with us?" asked Alice.

"A lot. The Rule of 72 is non-partisan."

"What?"

"I mean it doesn't take sides. It doesn't care if a person is a net saver or a net debtor. The interest rate calculations still work the same way." Weng Yang stopped talking and slowly pushed the sheet of paper tabulating their debt situation across to Alice.

Comprehension quickly dawned on her face. "I see. If we owed money at 12 per cent or 24 per cent a year, the amount we would end up owing would double in six years or three years, respectively."

"Yes! If, of course, we didn't pay anything down on those loans."

"All that's very depressing, but I do understand what you mean by the power of compounding and the Rule of 72, but what exactly does it have to do with what we were talking about just now? In fact, what were we talking about exactly?"

"Remember, I said Paul thought it would be an excellent idea to hunt around for cheaper financing."

"I get it. If we swap an expensive 18% loan for a cheaper 9% loan, then instead of having the amount that we owe double every 4 years, it would take 8 years to double."

"Exactly right, if we don't pay a sen on either loan over those periods. Of course, even though most creditors expect timely payments, the advantage of servicing a cheaper loan over an expensive one is significant."

Note: Excerpted and edited for length from Chapter 4 of my new book, *Liberty! From Debt-Slave to Money Master*, published by I2Media Sdn Bhd and targeted for a late March 2002 release.

In a nutshell, the Rule of 72 has three different areas of application :

1. Doubling assets;
2. Halving buying power; and
3. Doubling outstanding debts.

But even if you already know how to use this useful rule, you may not be too sure WHY the Rule of 72 works.

So, if you're interested in finding out WHY it does, please keep reading.

(If, however, you're satisfied with just knowing how to use the Rule of 72, then you are welcome to stop right here and move on to another article.)

For those of you still with me, a clue to the intriguing issue of WHY is embedded in the following table.

TABLE 1

TIME NEEDED TO DOUBLE YOUR MONEY (To determine the value of X, where X% doubles an investment in X years)

Start Value (RM)	% of Investment (I)	Exact Number of Years (P) to double to:	End Value (RM)	I x P
1000	6.00	11.895	2000	71.37
1000	7.00	10.242	2000	71.69
1000	8.00	9.007	2000	72.06
1000	8.25	8.74380	2000.00	72.14
1000	**8.498245**	**8.498245**	**2000.00**	**72.22**
1000	8.50	8.49655	2000.00	72.22
1000	8.75	8.26340	2000.00	72.30
1000	9.00	8.045	2000	72.41
1000	10.00	7.270	2000	72.70

What might come as a surprise to some is that despite our extreme familiarity with its usage, the Rule of 72 DOES NOT work equally well for all interest rates.

Now, remember that the Rule of 72 can be described this way :

I = 72/P, therefore 72 = I x P

So, if the Rule of 72 were completely accurate for all interest rates, then for any combination of I and P *(where I = the APR, and P is the time period in years needed to double the value of the investment from I to 2I)* I x P = 72 exactly!

But that's not the way it is. If you look at Table 1, you'll see that the last column, marked I x P (for the interest rate of the investment (I) multiplied by the approximate number of years (or period, P) needed to double the value of that investment) only hovers around '72' for six per cent through to 10 per cent. And even within that range, instead of being exactly 72, I x P runs from 71.4 for I = 6 per cent to 72.7 for I = 10 per cent.

The further away we move from compounded annualised growth rates (or CAGRs) of six per cent to 10 per cent, the far less accurate the Rule of 72 becomes; look again at the last column of Table 1. For instance, if you want real accuracy, for I = 2 per cent, we should really use a so-called Rule of 70. Or for I = 20 per cent, we might use a Rule of 76.

Thankfully, that range of good fit running from six per cent to 10 per cent is where most long-term investment returns tend to fall. That makes the Rule of 72 immensely useful in day-to-day usage.

Unfortunately, that high level of utility has resulted in our using the Rule so mechanically that we often forget it is an approximation.

Let's return to our original quest. We want to find out WHY the Rule of 72 works at all! (To do so only requires a basic knowledge of algebra and the ability to tinker with numerical values in a simple spreadsheet.)

Going back to first principles necessitates our finding which annualised percentage rate or APR (X per cent) succeeds in generating a doubling of money in precisely X years.

To aid in this quest, we'll take a close look at Table 2, which focuses on I=6 per cent to I=10 per cent.

The highlighted line in Table 2 shows that an investment growing at 8.498245 per cent a year will double in 8.498245 years.

In terms of our earlier tagged 'X' value, we find that X = 8.498245 (to six decimal places).

(If you would like to double check this yourself, cobble together a similar spreadsheet and carry out the relevant calculations for 'Exact Number of Years to double your investment', P = 100 x I.)

And with that, our key question — **WHY the Rule of 72 works?** — is almost answered.

You see, the square of 8.49825 is 72.22 (to two decimal places). If we round that off to the nearest integer, we end up with our magical 72!

When we run the basic calculation of I x P on either side of 8.49825 per cent (meaning slightly less, 8.25 per cent say, or slightly more, 8.75 per cent say) we find that there is a predictable drift away from 72.22.

If I = 8.25 per cent, then the period needed to double an investment P is equal to 8.74380 years. Here I x P = 72.14, which is 0.08 LESS than 72.22.

If I = 8.75 per cent, then P = 8.26340 years. And I x P = 72.30, which is 0.08 MORE than 72.22.

As you can see from Table 1, in particular, when the I or APR is **less** than 8.498245 per cent, the Rule of 72 predicts a time to double your investment (or halve your money's buying power or double the value of your liability!) that is **too long.** For example, if I = 6 per cent, then the Rule of 72 predicts a doubling of value will take 12 years. But it only takes (71.4/6) years = 11.9 years.

And when the APR is **more** than 8.498245 per cent, the Rule of 72 predicts a time to double that is **too short.** Again, if this time I = 9 per cent, the Rule of 72 predicts a doubling in eight years. But it actually takes (72.4/9) years = 8.04 years.

But you must admit, 11.9 is pretty close to 12, and 8.04 is even closer to 8.

So, the next time a client asks you about the Rule of 72 — what it's for and what it can do — you will be able to add meat to your answer by explaining WHY it works. Here's what you can say :

"The reason the Rule of 72 (which should be called the Rule of 72.22, if we wanted to be pernickety about the whole thing!) works so well is because of the *very slow rate of drift* away from the 'central value' determined by money doubling in X years by compounding at X per cent a year."

You never know, perhaps like Bell, Ford and Edison, your ability to get to the crux of a compelling 'WHY' might one day lead you to a far better station in life. AN

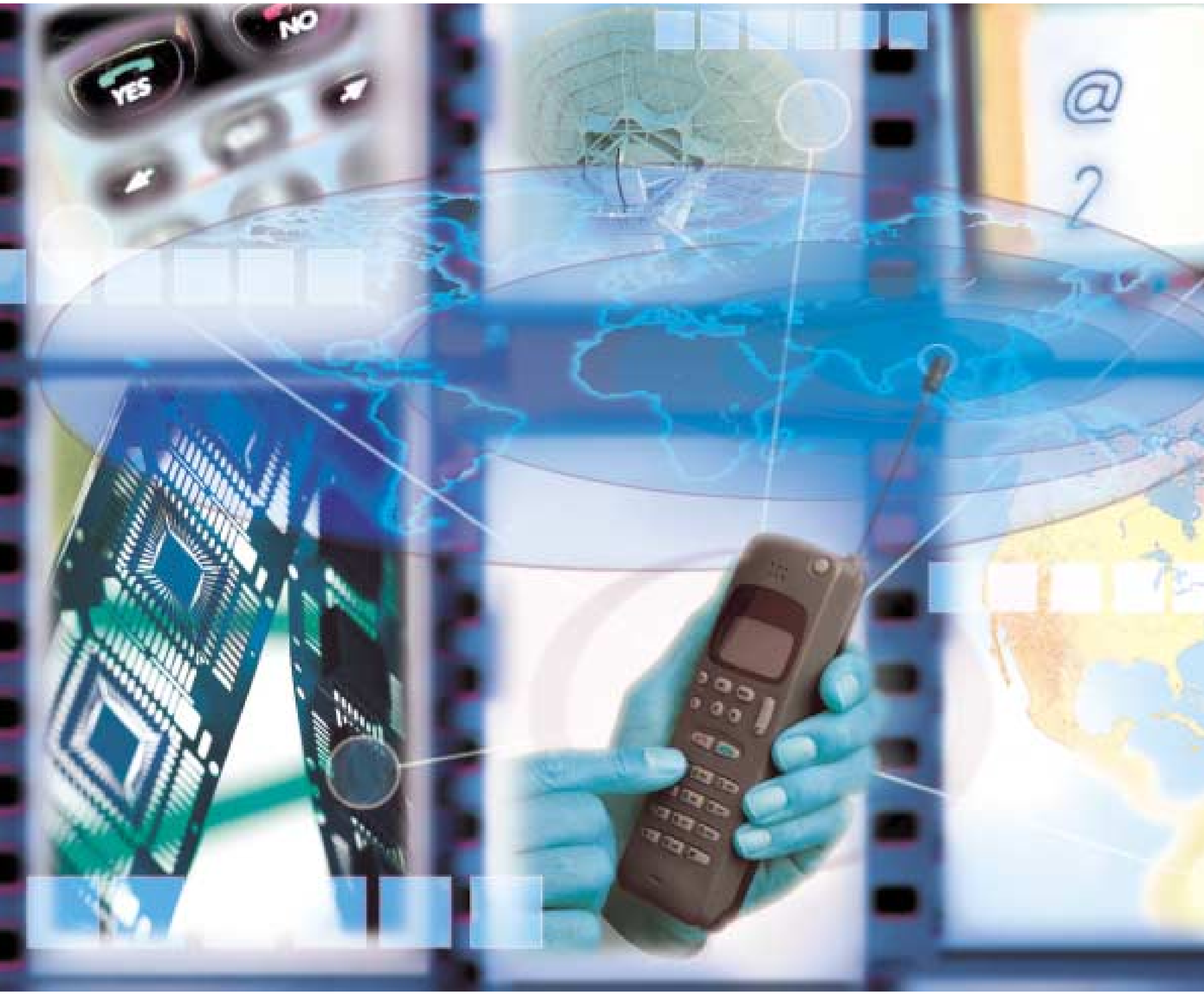
TABLE 2 TIME NEEDED TO DOUBLE YOUR MONEY

Start Value (RM)	% of Investment (I)	Exact Number of Years (P) to double to:	End Value (RM)	Approximate Number of Years	I x P
1000	2	35.000	2000	35	70.0
1000	4	17.670	2000	18	70.7
1000	**6**	11.895	2000	12	**71.4**
1000	**7**	10.242	2000	10	**71.7**
1000	**8**	9.007	2000	9	**72.1**
1000	**9**	8.045	2000	8	**72.4**
1000	**10**	7.270	2000	7	**72.7**
1000	12	6.115	2000	6	73.4
1000	14	5.290	2000	5	74.1
1000	16	4.670	2000	5	74.7
1000	18	4.187	2000	4	75.4
1000	20	3.802	2000	4	76.0
1000	30	2.642	2000	3	79.3
1000	40	2.060	2000	2	82.4

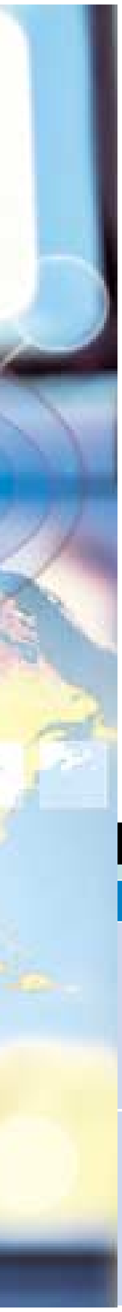
Taxation of cyberspace trading and its Impact on Malaysian Business

By Dr. Jeyapalan Kasipillai

Cyberspace trading has the potential of being one of the most outstanding innovations of the 21st Century, and Revenue authorities have a role to play in utilising this potential. 'Cyberspace' is the term used to describe the amorphous place where the Internet, the WorldWideWeb and other



instruments of communication technology, such as e-mail, operate. Advanced information technology has the ability to dismantle national borders and to alter the face of domestic and international trade. Consequently, on-line transactions pose some of the biggest problems to the government in their efforts to collect taxes. The problems arise as a business can now engage in cyberspace trade without having a physical presence : the virtual corporation concept is way beyond what was imagined during the formative stages of present day tax laws. Furthermore, cyberspace trading creates opportunities by removing barriers of time and space. The most common perceived benefit of cyberspace trade is that it provides for expanded geographical coverage. Enterprises are currently exploiting these advantages to rationalise their supply chains and register more direct relationship with their end users, providing better customer service, offering self-tailored products and a shorter time to market. Revenue authorities in various countries such as Australia, Singapore, the UK and the US are making efforts to ensure that tax laws do not lag too far behind the progress made in trade practices as well as new developments in electronic payment systems. The terms 'electronic commerce' and 'internet trade' are often used interchangeably with cyberspace trading.



Currently, the taxation principles that guide governments in relation to conventional commerce also guide them in relation to electronic commerce. This is also true in the case of Malaysia. However with the tremendous growth in Information and Communications Technology (ICT), it is uncertain as to whether existing taxation laws can be implemented effectively. While important issues remain unresolved and represent problems for the tax authorities, these uncertainties may also present opportunities for legitimate tax planning resulting in firms paying lower taxes in most or all the countries in which they operate.

Tax Structure

Economists generally split taxes into two broad classifications :

1 *Direct Tax*

This is a tax which is paid directly by those on whom it is levied. Examples of Malaysian taxes are income tax, real property gains tax, estate duty and stamp duty. In the past, other direct taxes that were imposed included estate duty and film hire duty.

2 *Indirect Tax*

This is a tax which is generally collected via some third party. An indirect tax is generally an addition to the price of a product or service and is collected by an intermediary who will then remit it to the tax authorities. Examples of indirect taxes are sales tax, service tax, excise duty, import and export duties and value added tax.

The Basis of Malaysian Taxation

The imposition of income tax in Malaysia depends as much on the establishment of sources and residence as on whether income has been derived, and if so, when and by whom. From an income tax compliance perspective, the question of who derives the income can be ascertained by tracing who owns the investment which generates the income. However, in cases involving transactions done electronically, ascertainment of who derives specific sales income will be problematic if a history of transactions is not kept. Furthermore, transactions may be made off-shore, making it difficult to enforce third-party information reporting.

The following section covers scope of charge, significance of residence status and classes of income.

1 Scope of Charge

The basis of taxation is the derived and remittance scope. Income of an individual is only assessed if it is derived in Malaysia or received in Malaysia from abroad. However, only income of a non-resident that is accrued in or derived from Malaysia is subject to tax. Foreign income received in Malaysia by resident companies are, however, excluded from the scope of taxation by virtue of the Income Tax (Exemption) (No 48) Order 1977. The exception to this rule is when a resident person carries on banking, insurance or air/sea transport operations. In such cases, the resident person carrying on such operations is assessable to tax on worldwide income even though the income is not received in Malaysia. A summary of the scope of charge to income tax applicable in Malaysia is presented in Table 1.

2 Significance of Residence Status

The residence status of an individual is determined under Section 7 of the Income Tax Act 1967 ("the 1TA"). In general, residence is determined by the number of days an individual is present in Malaysia, that is a quantitative test. This quantitative test determines whether an individual is :

TABLE 1

SCOPE OF CHARGE TO INCOME TAX

Scope of Charge	Territorial or Derived Basis	Derived and Remittance Basis	World Income Basis/Scope
Particulars **Basis of Chargeability**	Income accruing in or derived from Malaysia	Income accruing in or derived from Malaysia. or received in Malaysia from abroad	Income wherever arising from carrying on the business of sea and air transport, insurance and banking
Chargeable Person	Resident company (other than sea and air transport, insurance and banking company on that specific source of income) and non-resident person	Resident person (other than a company) of sea and air transport, insurance banking	Resident company carrying on the business

Regional Update

■ THAILAND

Thailand initially took a bold step to grant tax-free status to cyberspace trade transactions in order to encourage internet activity However, with Thailand's participation in the WTO. the government has repealed the tax-free status and commenced training its officials in cyberspace trade taxation with a view of prosecuting e-commerce tax evaders.

■ INDIA

In India there is little guidance on cyberspace trade from tax authorities. It has, however taken draconian tax measures on cyberspace trade transactions. As long as there is the 'availability of workstation software installed in an Indian-based office', there is a persuasive likelihood for profits arising from cyberspace trade to be subject to income tax.

■ JAPAN

In Japan, the National Tax Administration (NTA) has yet to provide guidance on e-commerce taxation due to inherent difficulties in identifying parties to an e-commerce transaction and enforcing the record keeping requirements for such transactions (Owaki and Tamazawa, 1999). The NTA is, however, planning to tax e-commerce transactions at the time of payment to credit card companies for goods and services. These rules are expected to be implemented in 2002.

■ REPUBLIC OF SOUTH KOREA

The South Korean government has todate not imposed any customs duty on goods delivered on line (Famulak *et al.* 1999). In attempting to address some of the emerging e-commerce issues, the National Tax Administration (NTA) of South Korea has introduced the Basic Act on Electronic Commerce and Signature Law (Jeong 1999).

■ AUSTRALIA

Australia tends to adhere to a residence-based taxation for e-commerce transactions. According to *Economist Intelligence E-Business* (2001) rankings, Australia ranks second only to the US as the country most conducive to Internet-based commerce. The proportion of medium-sized businesses in Australia with an enthusiastic internet site increased from 56 per cent in May 2000 to 67 per cent by May 2001 (Layton, 2001).

■ NEW ZEALAND AND THE UK

The New Zealand government has maintained the principle of tax neutrality/ and echoed the organisation for Economic Co-operation and Development's (OECD) call for a tax system that is both easy to comprehend and simple to manage. New Zealand adheres to a residence- based taxation for e-commerce transactions. The New Zealand Inland Revenue has issued guidelines for small businesses involved in cyberspace trade. The UK government has stressed that any taxation framework for e-commerce must not impose new taxes and must not impede the development of e-business.

■ HONG KONG

The Hong Kong Government in its 1999/ 2000 Budget indicated its intention to develop the island into a Cyber-city. In this regard, the Hong Kong Society of Accountants established a WebTrust Committee in 2000 to explore the development of WebTrust service. The service is to provide assurance of control and security in a website and the transactions and throughput related to the site. Such a move would provide more confidence in electronic transactions entered into.

■ SINGAPORE

The Inland Revenue Authorities of Singapore (IRAS) has come out with specific guidelines as to how Goods and Services Tax (GST) should be charged on electronic commerce transactions of physical goods as well as digitised goods and services. The GST is also known as Value Added Tax (VAT). GST is a tax on domestic consumption. It is charged on any supply of goods or services made in Singapore by a taxable person in the course or furtherance of any business carried on by a person. The present rate of GST is three per cent. All physical goods supplied over the Internet attract GST if the supplier is a GST registered person and the supply is made in Singapore. The principles guiding the charging of GST on e-commerce transactions is the same as that for traditional commerce. Therefore, as a GST-registered person, if one sells goods via the Internet and the goods are delivered locally, the person is making a standard-rated supply and GST is chargeable at three per cent. Malaysia does not have a VAT system in place.

■ exempted from remittances of income from abroad; and

■ entitled to personal reliefs.

Individual residents are granted personal reliefs and their income is taxed on a scale ranging from 0 to 29 per cent (0 to 28 per cent with effect from year of assessment 2002) depending on their marginal income. Non-residents normally do not benefit from any of the personal reliefs and are taxed on a fixed rate of 29 per cent (28 per cent with effect from year of assessment 2002) on their taxable income.

3 Classes of income

Income is categorised into various classes such as business, employment, interest, rent, discount, premium, pension, annuities, royalties and other gains. The classification however, does not exhaust all the possible sources of income since there is a catch-all category, (Section 4(f) of the ITA) which includes all the incomes not elsewhere classified. In the case of other income, it should be noted that income should have the characteristics of one or more of the specific classes of income in order for it to be considered as the catch-all category and subjected to tax.

Need For Flexibility in Tax Law

Some of the cardinal principles of taxation dictate that there should be certainty in the interpretation of the tax law, to ensure that the burden of tax is spread fairly and equitably among taxpayers and compliance costs should be as low as possible. More importantly, taxation systems should be flexible and dynamic so as to ensure they keep pace with technological and commercial developments. In cyberspace trade, enterprises encounter risk in the tax treatment of their methods employed to transact business. The risk element is partly due to the uncertainty in the application of the old principles to new technology. Simply put : the traditional tax structure was not designed to deal with new electronically-managed situations. For example, Malaysian tax laws like tax laws elsewhere were written much before the advent of e-commerce and do not address the unique issues raised by cyberspace trade.

The advent of cyberspace trading provides all businesses access to worldwide information. Using sophisticated information, businesses are given the opportunity to trade their products or services globally. Similarly, businesses engaged in cyberspace trading may be located anywhere in the world and their customers will be ignorant of, or indifferent to, their location. In this regard, the OECD Committee on Fiscal Affairs concluded that a website cannot, in itself, constitute a permanent establishment (Anon, 2000). However, if the enterprise carrying on business through a website has the server at its own disposal and operates the server on which the website is stored and used, the place where that server is located could constitute a permanent establishment of the enterprise

Nature of e-commerce

Cyberspace trade broadly encompasses two types of transactions :

1. sale of goods and services that are ordered electronically and delivered physically; and
2. sale of digital products that are ordered and delivered electronically.

The general consensus among revenue officials and tax professionals in most countries is that the existing tax structure can accommodate the former (see (1)) as it will meet compliance challenges in the normal course of business. There is a certain element of uncertainty in the latter (see(2)) as it could result in a potential loss of tax revenue to the government. This uncertainty has aroused a policy debate at both domestic and international levels.

Policy Debate

Several policy issues pertaining to taxation of income derived from cyberspace trade has been debated at tax forums and seminar gatherings at an international level. The core issues are outlined here. Cyberspace trade would make it difficult to identify the country or countries that claim to have the jurisdiction to tax such income. Cyberspace trade enables foreign firms to do business with a host country from any jurisdiction. This is because the server used by the foreign supplier to engage in international business can be located anywhere. Additionally, classifying income from transactions in digitised information is problematic as information now has no boundaries. As mentioned earlier, the taxation system in Malaysia and most other countries are traditionally based on the concept of source or residence. In a borderless world, business transactions are concluded without regard to physical or national frontiers. New challenges would arise in managing tax compliance due to a rise in transactions that leave little or no audit trail, particularly so, if it is done electronically. It would be difficult to trace the relevant parties to the communications and transactions made.

Concept of "Belonging to Singapore"

It is important to identify whether a business has a fixed establishment in Singapore so that the business would be considered as 'belonging' to Singapore for tax purposes. A business entity such as a company or a partnership is considered as 'belonging' to Singapore if the business establishment is in Singapore or it has a fixed establishment in Singapore. Situations may arise when a businessman may have more than one fixed establishment, that is, both in Singapore and elsewhere. In such a situation, a fixed establishment exists in the place where the services are most directly used or to be used. In the case of individuals, the person is treated as 'belonging' to Singapore if Singapore is his or her usual place of residence.

Touching on the thorny issue of digitised transactions involving electronic transmissions, the IRAS has provided some broad guidelines. If a businessman has a Singapore address in a membership database (indicating that he is a regular business client), a Singapore domain name or a Singapore IP address, these are indications that he has a business in Singapore.

However, the following may indicate that a business client belongs to a country outside Singapore :

- address of the business entity as shown in the host membership database is outside Singapore; and
- domain name or IP address indicates that the business is a foreign establishment; and
- the company gives a declaration, at the time of transaction, that the company is located, outside Singapore; and
- any other information indicating that the client as 'belonging' outside Singapore.

The Singapore government has also introduced a package of tax incentives, effective from year of assessment 1999, with a view of developing the island into a regional cyberspace trading hub. The new tax package is referred to as Approved Cyber Trader (ACT) Programme. A Singapore company that has been granted the ACT status will benefit from a low tax rate of 10 per cent for a period of five years. Furthermore, there will be total exemption or marginal withholding taxes on payments which qualify for the ACT programme.

Malaysia's Approach to Cyberspace Trade

The Inland Revenue Board (IRB) of Malaysia has not taken any concrete stand to tax income arising from cyberspace trade (e-commerce). It has taken a cautious move to adopt a common platform with other countries through participation in international forums such as OECD, APEC and WTO. The OECD Model Treaty provides a framework for determining general consensus relating to double taxation problems. The model serves as a framework that countries may use or modify to suit their needs in dealing with other countries. In the meantime, existing Malaysian taxation laws govern e-business transactions providing ample opportunities for cyberspace traders to minimise payment of tax.

In the 2002 Budget, the Malaysian Government proposed new incentives to promote the use of Information and Communications Technology (ICT) and accelerate the development of a knowledge-based economy. Patents, know-how, software, copyrights, trademarks and web-sites are a few examples of the expertise and other intellectual properties that serve to differentiate any enterprise in a competitive environment. The proposed incentives to encourage cyberspace trading are deliberated under the following sub-headings :

1. Tax incentives for Offshore Trading via websites;
2. Tax incentives for the Implementation of *Rosettanet*; and
3. Deduction on cost of developing websites.

Tax Incentives for Offshore Trading Via Websites

Currently, an offshore company registered under the Offshore Companies Act 1990 carrying on an offshore trading activity for the basis period for a year of assessment can make an election to either pay tax on its audited accounts at a concessionary rate of three per cent or pay tax of RM20,000 for a year of assessment.

It was proposed that income received by companies undertaking 'offshore trading', that is buying and selling of foreign goods to non-residents via websites in Malaysia be taxed at a concessionary rate of 10 per cent (instead of 28 per cent) for a period of five years. The proposed effective date is 20 October 2001. The company must have the approval of the Minister of Finance. 'Offshore trading' is defined as buying and selling of foreign goods to non-residents.

Income (after tax) that is distributed to shareholders would be further exempted from tax.

Tax Incentives for the Implementation of Rosettanet

The term 'Rosettanet' refers to the open Internet based common business messaging standard for the supply and management link-ups with global suppliers. The Income Tax Act (ITA) does not recognise capital expenditure for deduction purposes. The 2002 Budget has proposed that expenditure incurred on this system (Rosettanet) is to be considered a deductible item. Expenditures on equipment like computer and servers, salaries of full-time staff or employees seconded to Rosettanet Malaysia, sharing of software and programming as well as training of staff of local small and medium scale companies to use Rosettanet will now qualify for a deduction with effective from year of assessment 2002.

Deduction on Cost of Developing Websites

The cost of setting up a website is a capital item and hence not a deductible expense. At the same time, these expenses are not treated as qualifying capital expenditure under Scheme 3 ITA.

Since this expenditure is closely tied up to the tax incentive for trading via websites in Malaysia, the 2002 Budget has proposed that an annual deduction of 20 per cent be given for development costs of websites. Cost of developing a website includes cost of acquiring a domain name. The cost of maintaining a website is a revenue expenditure and hence deductible under Section 33 ITA. The principal objective of this incentive is to encourage the usage of ICT as well as encourage cyberspace trading in Malaysia. The government is also promoting a knowledge-based economy through the use of the electronic media. The amendment is effective from year of assessment 2002.

Recommendations

The Malaysian government too should formulate clear and simple rules for the taxation of electronic commerce so that businesses can anticipate, as far as possible, the tax consequences of the transactions they enter into. These rules should avoid incidence of double taxation. At the same time, the rules should be such that IRB should see to it that risks from increased evasion and avoidance are kept to a minimum. The principle objective should be such that the correct amount of tax is paid at the appropriate time and in the right country. In developing these rules, the guidelines need to be flexible to adapt to changes as more advances are made in the IT world.

The Ministry of Finance has to work closely with the IRB and the Royal Customs and Excise Department in the development of a Malaysian tax policy on electronic commerce. New legislation may be required on disclosure requirements to IRB such as furnishing e-mail and website addresses in the annual tax return as well as mandatory disclosure on gains from business transactions done electronically. It should also keep a close watch on the progress and strategies developed by neighbouring and other advanced countries before initiating its own tax policy on cyber trade suited to our own tax structure. The main challenge for the IRB is to develop an e-business taxation system that is equitable to the government and the business community without impeding the advancement of cyberspace trade. AN

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Food for Thought … and Action

This is a collection of tit-bits culled from here, there and everywhere which hopefully you will find not only interesting but also useful in your endeavour toward achieving a longer, healthier and more meaningful lifespan.

By Ooi Beng Choo
LL.B., (HONS), PROHIGHWAY HEALTHCARE

Probotics and Prebiotics

What's that? Sounds like some new scientific terms. They are in fact relatively new terms for certain foods and food ingredients that belong to a growing list of beneficial but not absolutely vital substances for your body known as functional foods or nutraceuticals.

Probiotics is the name given to describe the beneficial bacteria that aid in digestion and in maintaining urinary tract health. Your intestinal tract is home to over 400 types of bacteria — some good like the *Bifido* bacterium and *Lactobacillus* acidophilus, and some bad like the *E.coli*. Increasing the population of good bacteria helps inhibit the growth of harmful bacteria and thus lowers the toxin levels produced by the harmful bacteria. Good bacteria can be found in fermented milk products like yogurt and kefir and are also available in supplement form.

Prebiotics are non-digestible food ingredients such as fibre found in vegetables, fruits and whole grains, and fructooligosaccharide (FOS), a class of indigestible, slightly sweet carbohydrates found naturally in small quantities in garlic, onion, asparagus and artichokes. Prebiotics act as fodder for the good bacteria already present in your intestinal tract thus allowing the good bacteria to multiply. Prebiotics are also available in supplement form (capsule or powder) as well as in some nutritional products.

There is some scientific evidence in support of a wide range of health benefits of probiotics and prebiotics. Both pro and prebiotics boost the immune system, counteract toxic compounds in the body, lower blood cholesterol, regulate blood sugar, soothe irritable bowel syndrome, reduce food allergies, control the formation of damaging free radicals, improve the body's ability to produce and absorb several important vitamins and minerals, prevent traveller's diarrhoea, yeast infections and intestinal problems associated with taking antibiotic medications.

The list of benefits is daunting and some researchers believe that their benefits may be overrated. At any rate it is not a bad thing at all to include yogurt and fibre (in their natural form) in your diet. It is when you wish to take them in their supplement form (capsules or powders) that costs may be a prohibitive factor.

The Okinawan Diet

As more and more people opt for a purely or predominantly vegetarian diet partly because of the spread of the 'mad cow' disease and partly because of the movie '*Babe*', it is interesting to note that the Okinawans (Okinawa is one of the Ryukyu Islands south of Japan) probably enjoy the world's longest life and health expectancy. Since the start of the Okinawa Centenarian Study in 1976, over 600 centenarians have been investigated. Dr. Suzuki, the main investigator, found many of them to be youthful-looking, energetic, with remarkably low rates of heart disease and cancer.

Their diet by weight comprises 72 per cent vegetables, grains and fruits, 14 per cent soy and seaweed, 11 per cent fish and three per cent meat, poultry and eggs.

"The average Okinawan consumes a daily minimum of seven servings each of vegetables and grains and four servings of fruits".

The average Okinawan consumes a daily minimum of seven servings each of vegetables and grains and four servings of fruits. (5 to 10 servings of vegetables and fruits a day are recommended to provide the antioxidant vitamins and protective phytochemicals that can prevent or repair cell damage before it turns cancerous.)

The Okinawans have a preference for sweet potatoes, bean sprouts, onions and green peppers, eat their grains in various forms (bread, noodles, rice), many of them whole grains, but eat little dairy products.

Interestingly they share the same spiritual and religious values and their womenfolk are accorded a high status.

An Ode to Garlic

Culinary uses aside, garlic has been placed at the apex of the anti-cancer food pyramid. Experiments by scientists and ordinary people have shown that garlic helps prevent cancer and prevents certain cancers from growing larger. Garlic is useful as an antibacterial. It also helps to strengthen your immune system, lower high blood pressure and cholesterol and may even rectify the problems of impotence.

When raw garlic is cut or crushed a compound called diallyl-disulphide is formed. Recent research in the US shows that this compound can help shrink a tumour. A further compound, S-Allylcysteine, can stop cancer-causing agents from binding to human breast cells. You should therefore, allow the chopped garlic to rest for 10 to 15 minutes before cooking so as to allow these cancer-fighting compounds to develop.

What Would You Do Without Tomatoes!

Indeed without tomatoes how do you enjoy spaghetti or pasta or plain tomato soup, or for that matter, how do make tomato chutney, 'assam curry fish' and a string of other Asian and Western dishes.

Tomatoes are more than all that. Tomatoes are rich in lycopene (an antioxidant). According to Jean Carper, author of *Food, Your Miracle Medicine* (Harper Collins), lycopene contains P3, an anti-clotting factor that prevents and may even reverse heart disease. If your lycopene level is low you are three times more likely to suffer heart attacks or strokes. Research in US, Italy, Germany and Israel shows that lycopene can significantly inhibit several types of cancer — colon, lung, breast, prostate and endometrial cancers. Carper advises consuming at least five servings of tomatoes weekly, eaten raw, or cooked or processed with a little olive oil to help the body absorb the lycopene. Red peppers and red grapefruit also contain lycopene.

The Seven Wonders of Soya

Soya bean is the only plant food that contains all the essential amino acids your body needs. It is therefore a complete protein. Soya is cholesterol free and generally high in fibre. It provides you with many vitamins, minerals and phytochemicals (e.g. isoflavones) that work together for a healthier you.

1. Soy protein and isoflavones lower your LDL cholesterol (bad cholesterol) and reduce the risk of thrombosis (blood clotting). In turn, the risk of heart attacks and strokes is reduced.
2. Soy protein and isoflavones provide antioxidants, reduce plaque responsible for clogging up arteries, improve blood pressure and lower the risk of arteriosclerosis (hardening of the arteries), heart disease and hypertension (high blood pressure).
3. Basically soy protein and isoflavones protect your body from damage by free radicals, boost your immune system and promote healthy blood vessels.
4. Soy protein and soluble fibres help regulate glucose levels and kidney filtration, which help control diabetic conditions and kidney disease.
5. The soluble fibres in soya beans protect your body from a number of digestive-related cancers such as colon and rectal cancers. The isoflavones may protect you from many hormone-related cancers like breast, endometrial and prostate cancers.
6. Soy protein helps your body to better retain and absorb calcium in the bones. The isoflavones slow down bone loss and lessen bone fracture. This in turn helps prevent osteoporosis.
7. Soya isoflavones helps regulate estrogen when this hormone fluctuates or declines, thus helping to alleviate pre-menopausal symptoms and pre-menstrual syndrome.

Mushrooms for Longevity

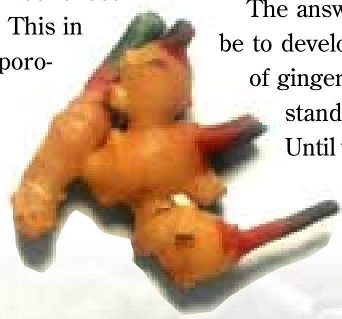
The Chinese and Japanese have for centuries been eating mushrooms to prevent illness and to cleanse the body. Studies show that mushrooms have special properties that can prolong life. The Shitake mushroom is a possible cancer-fighting agent and may reduce cholesterol. Button and abalone mushrooms are high in potassium and selenium.

Ginger Can Improve Osteoarthritis

Ginger contains a complex of 10 to 50 hydroxy-alkoxyphenyl compounds (HAPCs) that have anti-inflammatory properties. According to Dr. Lars Lindsmark, research director of Eurovita Holdings, clinical trials show that these compounds when refined can improve osteoarthritis symptoms.

The benefit of raw ginger in its alleviation of osteoporosis symptoms is not disputed but one needs to consume at least 100 grams of raw ginger a day to derive sufficient active ingredients. There is also the risk of gastro-intestinal problems. On the other hand, when ginger is boiled, the active ingredients are lost.

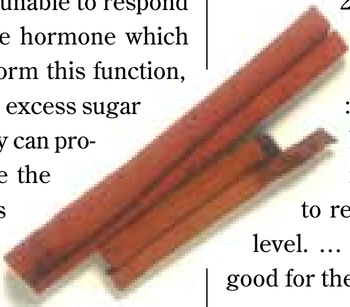
The answer to the problem would be to develop the active components of ginger into a refined drug with standardised dose and effect. Until then don't let this dampen your enjoyment of ginger in your favourite dishes.



"Soya bean is the only plant food that contains all the essential amino acids your body needs. It is therefore a complete protein".

Try Cinnamon for Type II Diabetes

Type II or adult-onset diabetes occurs when the cells in the body that deal with excess blood sugar are unable to respond to insulin. Insulin is the hormone which tells these cells to perform this function, namely, to transport the excess sugar into the cells so that they can produce energy or to store the excess sugar until it is needed.



Scientists in Maryland, US, have found an extract of cinnamon that can actually revitalise this function of the cells so that they become more responsive to insulin.

The scientists recommend taking 1⁄4 teaspoon of cinnamon powder a day. It can be added to your coffee, tea, oatmeal, and even orange juice. Cinnamon may also be effective against the E. coli bacterium which can cause food poisoning.

Spiritual Health

Spiritual health is as important as bodily health. It is the other side of the coin. Being in touch with your inner self, your innate qualities of peace and bliss, can lead you to a sense of self-worth and calmness which has a direct bearing on the well-being of your body.

In his article on health, "Resolve to quit bad habits" (*Sunday Star*, 30 December 2001), Rajen M. a pharmacist with a doctorate in Holistic Medicine wrote on this need : "Whether it is in nature, in halls of worship or on your meditation cushion, take time to relate to your soul on a deeper level. ... What is good for the soul is good for the body ..."

The Five Secrets of Centenarians

In essence, to achieve a longer, healthier and more meaningful life-span, you need to consider all facets that make you wholesome — your physical body and your spiritual being which also covers your attitude and outlook to life.

I shall end by quoting what Lynn Peters Adler, JD, recommends in "Centenarians : The Bonus Years" :

1. A love of life;
2. A positive, yet realistic attitude;
3. The courage and willingness to use modern medical interventions when needed;
4. A spiritual or religious belief; and
5. A remarkable ability to renegotiate life at every turn adjusting to and accepting the inevitable losses that come with longevity. AN

MORE TIPS FOR HEALTHY AGEING

1 Exercise daily. Also, put in at least one hour of vigorous exercise a week.

2 Try not to be underweight or overweight. Limit weight gain in adulthood to less than 11 pounds (5 kg). Evidence shows a link between endometrial and breast cancers with obesity.

3 Eat small, frequent meals that are rich in nutrients. Chew well. Take 5 to 8 servings of vegetables and fruits a day. Don't over eat, not even if it is 'good' food.

4 Once a month go on a juice fast for one day. By doing this you detoxify your system and restore hormonal balance.

5 Make nicotine your lifelong enemy. Even if you merely keep an unlit cigar between your lips to complete your manly image, you are still taking in nicotine!

6 Alcohol should be in moderation. It definitely increases your risk of cancers of the mouth, pharynx, larynx, liver and oesophagus.

7 Limit your salt intake and use herbs and spices instead to season your food.

8 Don't eat foods that are contaminated with fungal micro-organisms. They can increase your risk of liver cancer.

9 Eat a serving of spinach at least twice a week.

10 Avoid red meat. If you can't then eat less than three ounces of red meat a day.

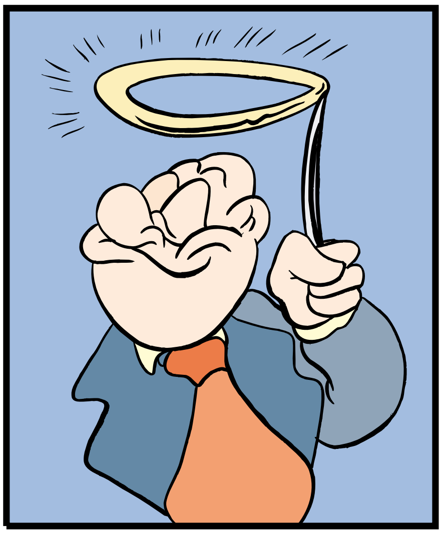
11 Go for margarine that is free of trans fat. Most margarine, french fries and many processed and fried foods are made with hydrogenated fats which is a top source of trans fat. Trans fat may increase your risk of breast cancer.

12 Commercial olive oil dressings are usually made with a mixture of oils. Why not make your own. Simply mix half olive oil with half balsamic vinegar.

13 Keep perishable foods in the fridge so as to preserve them.

14 Don't eat charred food as it contains potentially hazardous compounds. Smoked meat, 'satay' and grilled fish should be taken only occasionally. Steaming, poaching, braising, stewing, baking or roasting by low-temperature is a better way to cook meat.

Honesty is No Longer the Best Policy



By Sue Chuah

When we were growing up, one of the virtues extolled by our parents and schoolteachers was **Honesty**. In those days, lying was tantamount to committing the cardinal sin while being honest was praised and rewarded. (I remember a classmate was once redeemed of stealing my essay after admitting to the act and was even regarded as the 'victim' when I remained unforgiving). As children, we often got away with telling the truth despite causing red faces among adults during ill-timed moments.

Now that we are older and wiser, honesty seems to be out of fashion and on the brink of extinction. It is generally unsophisticated to be frank especially if you are socialising with the who's-who in town. Imagine the 'loss of face' if a CEO was to admit his non-membership of certain prestigious clubs or a socialite of the non-authenticity of her 'diamond' jewellery. Being outspoken is often frowned upon in the corporate world and may be misconstrued as being unprofessional bordering on insubordination. On the domestic front, the ideal daughter-in-law should be one who 'does not speak up' while abiding with the wishes of her elders including her husband. Today's youngsters find it 'uncool' to reveal their fears thus succumbing easily to vices and unhealthy activities.

Social acceptance, career advancement, filial piety and peer pressures are not the only causes leading to the dearth of directness. Official code of ethics dictates that the truth is taboo in the diplomatic circle while company staff handling confidential matters are sworn to secrecy. Pride also plays a part in preventing people from expressing their true thoughts for fear of rejection.

We often lie for noble reasons : parents do so to protect their children from the 'ugly truth'; spouses avoid hurting each other's feelings; suitors put on their best to win their ladies' affections. This list is infinite with the ends justifying the means in most cases, at least for the moment. Unfortunately, when the truth hits home in due course, the impact is often devastating for the parties involved especially when revealed at the wrong time. When that happens, disillusionment sets in after the initial indignation, which may lead to drastic consequences. Hence, we have divorces/ estrangements in marriages, broken friendships, rebellious offspring's, embittered employees, cynics and so on.

However, honesty is still quite alive among a few diehards like this writer. Despite decades of existence and sufficient profound experience culled from career, marriage and motherhood, I still cannot lie to save a life. Ironically, my city roots have not nurtured in me the ability to mince words, an art which even small town migrants excel in upon settling down in the concrete jungle. I am often amazed by my own steadfast bluntness and have difficulty checking the words before blurting them out.

For instance, whenever I received compliments on a dress or accessory I was wearing, my immediate response was to confess its humble origin (i.e. a hand-me-down, cheap offer, etc). Maybe it was modesty albeit not my strongest virtue but my frank confession soon turned off interest from the other party. A few years ago, when we were negotiating with contractors on some home renovations, I had my dear spouse squirming with embarrassment over my candid disclosure of our limited budget. We succeeded in getting a lower bill for the job. Although the materials and workmanship were not superior but the house is still standing.

My outspoken nature knows no bounds even when discussing a sacred subject like religion. This often resulted in outrage over my seeming blasphemy. In fact, my open stand on being a 'free thinker' never failed to shock many including school authorities who would lecture my bewildered children on the immorality of atheism and its grave (pardon the pun) consequences. Frankly, I prefer ostracism and will risk 'ineligibility for passport to Heaven' over hypocrisy (with guilt-ridden insomnia)! I am sure the 'Almighty' will understand that this 'lost sheep' is still seeking its 'shepherd'.

Notwithstanding the above confessions, this writer is not beyond redemption and is able to exercise tact when the necessity arises. The call of official duty and years of handling customer service have instilled in me an innate sense of discretion. Additionally, maturity plus a traumatic 'feud' with the in-laws (caused by my frankness) has made me realise the futility of forthrightness.

Of course, honesty still prevails under the right circumstances when I am with close friends and loved ones. This exclusive group of human beings who have suffered and stood by my honesty will continue to have the privilege of my utmost sincerity. As for the others, the truth is out there ... AN

How Healthy is Your Career?

By Peter D. Weddie

How healthy is your career? Are you building solid occupational strengths? Are you developing the level of competence and endurance you'll need for long-term success in your field of work? Or, is your career showing symptoms of being out of shape? Are you professionally flabby? Do you seem to be slowing and unable to get ahead as you once could?

As with physical fitness, many people don't know the answers to these basic questions about their worklife. They assume that all is okay because they aren't suffering from career cardiac arrest, or what most of us call unemployment.

But careers can be sick long before the pink slip arrives. There can be all kinds of hidden illnesses gnawing away inside a person's career, weeks, months even years before the symptoms visually manifest themselves. As with many physical diseases, you can't see these viruses early on, but they are very real, and they are terribly career-threatening.

Career fitness is a philosophy of working — a whole new approach to your worklife as much as it is a set of discrete activities for you to accomplish. It works best and you'll get more out of your effort if you have a sure sense of its full scope and purpose.

YOUR CAREER FITNESS

1 When was the last time you went back to school in your occupational-field?
a. This year.
b. Last year.
c. 2-4 years ago.
d. 5 or more years ago.

2 Do you have a mentor?
a. Yes.
b. No.

3 When was the last time you sat down and evaluated the course of your career and assessed its impact on the satisfaction and sense of accomplishment you get from your work?
a. Within the last 90 days.
b. Within the last six months.
c. Within the last year.
d. More than a year ago.
e. Never.

4 Are you weary or tired, despite a decent night's sleep, before you even get to work?
a. Yes.
b. No.

5 Have you identified the next job you'd like to have?
a. Yes.
b. No.

6 Are you in training or school right now to add to the knowledge, skills, and abilities you can use in your current job?
a. Yes.
b. No.

7 Do you mentor or counsel and assist another person in your field?
a. Yes.
b. No.

8 With whom will you compete to win your next job? *Choose only one.*
a. Your co-workers.
b. New employees from outside the organisation.
c. Your boss.
d. Yourself.

EVALUATION

9 Do you keep a resume in circulation all of the time, so that others are aware of your work credentials?
a. Yes.
b. No.

10 Do you know what your career objective is?
a. Yes.
b. No.

11 Do you work to earn a living and pursue a hobby or non-work activity for enjoyment?
a. Yes.
b. No.

12 Who oversees the course of your career and ensures that you get the training you need and the opportunities you deserve?
Choose only one
a. Your boss.
b. Your employer.
c. The Human Resource Department in your organisation.
d. Your mentor.
e. You.

13 Is your resume up-to-date and complete?
a. Yes.
b. No.

14 How flexible are you in your willingness to relocate?
a. Not willing to relocate.
b. Only to certain regions or states.
c. Only to certain cities.
d. Anywhere for the right job.
e. Anywhere anytime.

15 How much vacation time have you used in the last two years?
a. All of the days allotted by your employer.
b. Half of the days allotted.
c. None.
d. A day here, a day there.
e. More than the allotted time.

SCORING

Tally your Career Fitness score using the key on the right. (The"best" answer will give you 5 points.) Then compare your score to the Standards for Career Fitness presented at the end. The results will tell you what kind of shape your career is in and the contribution a Career Fitness programme can make to your on-going career health.

1.	a. 5	b. 3	c. 2	d. 0		
2.	a. 5	b. 0				
3.	a. 5	b. 4	c. 3	d. 1	e. 0	
4.	a. 0	b. 5				
5.	a. 5	b. 0				
6.	a. 5	b. 0				
7.	a. 5	b. 0				
8.	a. 0	b. 0	c. 0	d. 5		
9.	a. 5	b. 0				
10.	a. 5	b. 0				
11.	a. 0	b. 5				
12.	a. 0	b. 0	c. 0	d. 0	e. 0	f. 5
13.	a. 5	b. 5				
14.	a. 0	b. 3	c. 2	d. 5	e. 3	
15.	a. 5	b. 3	c. 0	d. 2	e. 2	

Your Score Evaluation and Recommended Career Fitness programme

75 : Your career is in great shape! Congratulations, you already have very healthy career habits. Use the Career Fitness programme to design and implement a systematic process that will continue and enhance your good habits and thereby sustain the vigour of your career over the long term.

42-74 : Your career is in moderately good health. You have developed some genuine strengths, but there are a number of gaps that need attention. Use the Career Fitness programme to acquire a comprehensive set of principles and a systematic process for strengthening your Career Fitness in the near-term and maintaining it over the long-term.

31-41 : Your career is suffering and needs immediate attention. You must focus on your career right away and strengthen it by practising more healthy career habits Use the Career Fitness programme to learn and practice the skills of good career management in the near term and to establish a systematic process for sustaining Career Fitness in the long term.

0-30 : Your career is dangerously out of shape. You must devote your full and immediate attention to the failing health of your career. Use the Career Fitness programme to help you regain strength in your occupational field and acquire the skills of successful career management in the near term and to implement a systematic process for maintaining both over the long term.

Admittedly, the above exam is not a scientific assessment of your career. However, it will give you a good sense of your general Career Fitness and tell you how ready you are to deal with the demanding new challenges in the world of work in the 1990s. No less important, this evaluation will also point you toward some common-sense, "real world" activities you can do right now to improve the satisfaction and success you derive from your career… today, tomorrow, for the rest of this century and beyond. That's the power and the opportunity of Career Fitness. AN

BANGKOK *Bargainers' Paradise*

By Anis Ramli

Be prepared to max out on the credit card when you make a trip to this gem in Thailand

Any visitor to Bangkok needs no introduction to one of the city's most favourite pastimes — shopping. Since the Baht floated in mid-1997, Bangkok became the alternative shopping haven for those otherwise familiar with the Singapore and Hong Kong scene.

Shopping in Bangkok is simply an adventure. There are street stalls, flea markets and sophisticated shops in air-conditioned malls that offer glorious goods you can bring home. While prices in the plazas are fixed, bargaining is almost expected when you hit the various markets as well as roadside shops. When prices can be slashed between 10-40 per cent off the asking price, even the most discerning shopper will be easily parted from the wallet for a great bargain.

While each part of Bangkok offers an exciting shopping experience, these picks are some of the best places the first-time visitor should hit, especially if you're strapped for time.

Chatuchak Weekend Market

Also called JJ's by the local Thais, this place is easily accessible via the Skytrain (last stop: Mo Chit). If you're in Bangkok for the weekend, never give this flea market a miss. It opens only on Saturdays and Sundays from 8 a.m. to 6 p.m., and once you've experienced its delectable albeit chaotic spread, you'll never want to shop anywhere again.

This is practically a bargain-hunters' paradise, where you can buy just about everything from clothing to potted plants, antiques to furniture, and pottery to ceramics. They even have a section on pets and exotic animals! And yes, bargaining is expected and highly recommended.

It's easy to get lost in the market because of its vast number of stalls. Most people use the clock tower in the middle of the market square as a landmark or a good meeting point in case they're lost. While all the stalls are covered, the corridors between them seem to stretch forever resembling a quaint labyrinth. The stalls may seem a bit haphazard at first, but there's actually an organisation to them. The best way to tackle the 'maze' and optimise your time here is to invest in Nancy Chandler's illustrated *Map of Bangkok*, where she has conveniently colour-coded the stalls according to their wares.

Patpong Night Market

Patpong is notorious for its other kind of evening entertainment. These days however, many tourists hit the area for a different kind of fanfare. The night market is held every day and ends at about midnight. This is the best place to shop for gifts and last-minute souvenirs especially if you're in Bangkok on a tight schedule and don't have time for most malls and markets.

There are stalls selling everything from clothing to accessories, with many offering branded rip-offs like the typical Rolexes and Armani sunglasses. Men's shirts are generally well-tailored and last a couple of washings, so too are the jeans and t-shirts. If you don't care for brands, shopping here can be both pleasant and fun. Leather goods tend to change according to season. For the fashion-conscious, you might want to know what's typically hot on the scene before hitting the stores, where you can easily get an imitation (that looks as good as the real thing) for a lot less.

Bordering the night market stalls are various retail shops that sell furniture, including household curios and collectibles. Don't be misled by their claims of 'antique' ware. Again, most items here are clever copies. Be sure to browse around for the real thing. A good dealer will be able to help identify the best buy and arrange shipping and insurance for the trip back home.

Mah Boon Khrong (MBK)

Strike up a conversation with any native Thai on the plane and they'll tell you to do this plaza at least once. Affectionately called MBK for short, this also happens to be the shopping mecca for Singaporeans and Malaysians alike. Tourists love to flock to this place for its endless array of small youth-oriented fashion shops as well as stalls selling some of the best imitation goods ever to be seen this side of Asia. One particular shop on the 2nd floor called Spice Girls sells excellent designer knock-offs bags that are so good, you can't even tell they're not real.

MBK recently underwent a renovation and now boasts of its own unique ambience with some 400 main outlets, more than 1,000 kiosks that offer a staggering variety of merchandise, plus a multiplex theatre with six screens and a 27-lane bowling alley on the seventh floor. If the small stalls aren't your thing, the Tokyu department store offers typical malls and goods at fixed prices. Skytrain : National Stadium

Pratunaam-Ratchadamri-Ploenchit

This is where you'll find the World Trade Centre that houses Isetan and Zen department stores, Gaysorn Plaza, and Pratunaam Market. This major shopping destination is in a bustling area that sells everything under the sun, from haute couture to domestic produce at bargain prices. Siam Square is another trendy hangout for young fashionable Thais. It's one of the oldest shopping malls in the city with shops presenting the newest trends and fashion items. If you can't go to Chatuchak, Gaysorn Plaza has got two floors dedicated to Thai crafts and goods. Prices are not as good as the weekend market's, but the range is pretty impressive.

Sukhumvit

The whole stretch has uncountable individual shops that cater to all tastes of the area's foreign community. Retail giants such as Emporium, Times Square, Robinson and Central Chidlom are all here, stocking some of the best in haute couture and ready-to-wear names in fashion, including local Thai designers. For the best of local brands, look out for Chaps (think Polo Ralph Lauren) that make excellent polo shirts and chinos; Greyhound makes contemporary and fashionable clothes, while Jaspal designs stylish clothes for both men and women.

WHAT TO BUY

Clothing

Thailand is one of the world's leading manufacturers of ready-to-wear clothing. There are fashion boutiques in almost every shopping mall, while cheaper clothing such as T-shirts and jeans are available at bargain prices from street vendors. Custom tailoring is also very affordable and tailors can produce or copy most styles in just a few days.

Gems

Bangkok is the coloured gemstone capital of the world. Rubies and sapphires are indigenous stones, but virtually all coloured gems, as well as diamonds, are available. Shoppers should exercise caution and buy from reputable dealers only. To explore the wholesale market, head to Mahesak Road, off Silom Road. Here you'll find reputable dealers that engage in the import/ export of coloured cut stones.

Antiques

Thai, Chinese and Burmese antiques can be found easily and make excellent buys. There is however an export ban on certain pieces, particularly Buddha images. Check to see if the pieces you're buying require an export license. Get a reputable dealer to advise you on restrictions and any necessary documentation.

Silk & Cotton

One of the kingdom's more famous handicrafts, silk is available in a range of colours, patterns and plys, and is sold by the meters. They are also available as ready-made clothing and souvenir items. The best-known outlet for Thai silk is undoubtedly Jim Thompson and Shinawatra, which incidentally belongs to the Thai Prime Minister. Thai cottons are also popular. You'll find the hilltribe cottons woven by the tribal people of the North make good souvenirs for both the home and family, often lavished with embroidery.

Ceramics

The distinctive sea-green celadons from the Sukothai area in traditional and contemporary styles are the best buys. They are made from padi silt and wood ash, and nowadays come in various colours. Bencharong is another popular item. This ornate ceramics were originally reserved for use by Thai royalty. They are often done in red, green, blue, yellow or white in intricate designs with gold used as an outline. AN

Malaysia's Bid for the 17th World Congress of Accountants 2006

IFAC President and CEO satisfied with Malaysia's capabilities and commitments.

Malaysia's fame as an international event organiser *par* excellence is indisputable. From the 16th Commonwealth Games in 1998, the Sepang F1 Challenge to the Langkawi International Maritime and Aerospace Exhibition (LIMA), and the Commonwealth Heads of Government Meeting (CHOGM), we have successfully hosted world class events that have earned us recognition as a nation that delivers what it promises, and then some.

It is with this knowledge that both the Malaysian Institute of Accountants (MIA) and the Malaysian Association of Certified Public Accountants (MACPA) put their best foot forward in jointly bidding for the World Congress of Accountants 2006, a premier event for accountants the world over, held once in every four to five years. This year, Hong Kong is playing host to the 16th World Congress of Accountants (WCOA).

With the theme, *'Knowledge-based Economy and the Accountant'* the event which is hosted by The Hong Kong Society of Accountants, will focus on issues ranging from opportunities offered by the knowledge-based economy to the direction the profession is moving in.

Quoting his welcoming message in the 16th WCOA's announcement brochure, Tsuguoki (Aki) Fujinuma, the President of the International Federation of Accountants (IFAC) says that the 2002 World Congress will provide accountants with the opportunity to hear from the profession's leadership, government officials, CEO's, academics, and regulators on how accountants can work together to provide services of consistently high quality in the public interest.

As Asia continues to look for solutions from accountants and others to address the challenges of its own changing knowledge-based economy, Aki together with the Chief Executive Officer of IFAC, Peter Johnston, were in Kuala Lumpur from 26 until 28 January, to gauge Malaysia's suitability as host nation in 2006.

The Institute together with MACPA went to great lengths to ensure a pleasant stay for both gentlemen and also prepared a comprehensive audio visual presentation and information booklet that was packed with a variety of information from Malaysia's excellent infrastructure to both the organisation's vast experience at hosting a multitude of immensely successful international and national conferences, conven-

One for the album ... (seated L-R): MIA Executive Director, Ho Foong Moi; MACPA Executive Director, Tan Shook Kheng; MIA and MACPA President, Abdul Samad Haji Alias; IFAC President, Tsuguoki (Aki) Fujinuma and IFAC CEO, Peter Johnston. (Standing L-R): Joyce Lim, Iszudin Mohd Amin, Andrew Leong, Chuah Soon Guan, Richard Teo and MIA Council Member, Manjeet Singh

Putting the facts together ... Chuah and Iszudin presenting Malaysia's commitments, track record and capabilities in organising the event in 2006

Digesting the fact ... Peter, Abdul Samad, Aki and Manjeet (not in pix), as well as both the ED from MIA and MACPA, focusing attentively to the comprehensive presentation tions and seminars.

Aki arrived at the Kuala Lumpur International Airport (KLIA) on the evening of 27 January 2002 and was whisked to one of Kuala Lumpur's leading restaurants to be treated to a sampling of Malaysian hospitality at its best. Here, he was joined by IFAC CEO Peter Johnston who had arrived a day earlier, and Ranel Wiresingha, President of the Confederation of Asian and Pacific Accountants (CAPA) who together with Peter had attended a CAPA meeting the previous day. Also present at the dinner was MIA's President Dr Abdul Samad Haji Alias, Council Members Manjeet Singh and Beh Tok Koay, Registrar Mohammad Abdullah and Executive Director Ho Foong Moi. Joining the dinner party from MACPA were its council members Sukanta Dutt, Dato' Abdul Halim Mohyiddin and Abdul Jabbar Abdul Majid who together with Executive Director Tan Shook Kheng and CAPA's Executive Director Leong Chew Poon joined our distinguished guests for a night of fine food and traditional entertainment that reflected the rich ethnic diversity of the various races which co-exist in Malaysia. The Kuda Kepang dance from Johor, the Dikir Barat from Kelantan, the Bamboo Dance from Sabah, a mix of Chinese and Indian dances and yet another Portuguese dance completed the representation of Malaysia as a unique country that is home to a multiracial society.

The dinner ended at 10.00 p.m. and both Aki and Peter, accompanied by Abdul Samad and several others were then driven to Genting Highlands where the audiovisual presentation was scheduled for the next morning. It being the eve of Thaipusam celebrations, they were caught in a massive traffic crawl when the driver mistakenly took the route heading towards Batu Caves, Gombak. Here, our guests bore witness to the colourful annual Thaipusam celebration that brings together Hindus from all over Malaysia, which is a fine example of the racial and religious tolerance practised in the country. After some time, the driver managed to find his way out by using a different route to Genting Highlands and reached it a little after 11.00pm.

Genting Highlands has been earmarked as a possible venue by virtue of the conference facilities at the 'Genting International

Borneo's delight ... The Bamboo Dancers from the 'Land Below The Wind' — Sabah

Malaysia Truly Asia ... the welcoming dinner hosted by MIA and MACPA Council Members for bothh Aki and Peter, depicting Malaysia's rich potpourri of culture and tradition. Seen in the picture with Aki and Abdul Samad is CAPA President, Ranel Wiresingha (standing 4th from left)

Convention Centre (GICC) and the accommodation at First World Hotel which will be capable of hosting the over 6,000 attendees expected at the Conference in 2006. (The First World Hotel is currently partially ready and is able to house 3,000 people. It is expected to operate at its full capacity in 2005). Apart from First World, there are several other excellent hotels nearby.

Both Aki and Peter were impressed with the visual presentation the next morning that highlighted Malaysia's excellent air, rail and road transportation; world class hotels; and the country's experience at hosting a variety of successful international events. The presentation was a joint effort between MIA, MACPA, Tourism Malaysia and the Multimedia University. Additional information was contained in a comprehensive information booklet given to our guests. We are confident we will give the other bidders, Singapore, Turkey, Lebanon, Czech Republic and Spain, a 'good fight'.

Later in the day, our guests were taken to the Putra World Trade Centre (PWTC) to have a look at the convention facilities there to give them an idea of the alternatives available. Both Aki and Peter were suitably impressed with what they saw and we are confident our bid will be given due consideration. Should Malaysia be given the honour to host an event of this magnitude, we are confident we will be able to undertake this task and do it well. We look forward to this privilege with great anticipation. AN

Chinese Visitors Call on MIA

A six-member delegation comprising of senior officials from China's Ministry of Finance recently called on the Malaysian Institute of Accountants (MIA) on a fact finding mission. The visitors were led by two staff from Deloitte KassimChan, which is the Malaysian member of the international professional services firm, Deloitte Touche Tohmatsu (DTT), whose member firm in China has been engaged by China's Finance Ministry to advise on accounting standards in that country.

From left : Manjeet Singh, Datuk Nur Jazlan, Albert and Liu Yuting together with the other delegates.

The Chinese party led by Liu Yuting, the Ministry's Deputy Director-General of the Accounting Regulatory Department was on the Malaysian leg of a study tour to gain an overview of other countries' accounting experience in standards setting, training, academia, professional accountancy bodies and the relationship between the various players who make up the accountancy profession.

At MIA, the visitors received a warm welcome from Vice-President Albert Wong Mun Sum, Council members Datuk Nur Jazlan Tan Sri Mohamed and Manjeet Singh Santokh Singh, MIA Executive Director Ho Foong Moi, its Head of Continuing Professional Education (CPE) Chuah Soon Guan and *Akauntan Nasional* Editor Iszudin Md Amin. After the formalities, Chuah proceeded with a PowerPoint presentation on MIA's 15 year experience in providing CPE programmes to its members. This was followed by another presentation on the Institute's history, its services to members, as well as its relationship with the various players in the accountancy profession and the current status of the Institute as a statutory body charged with duties to regulate the accountancy profession in the country.

A question and answer session ensued where the visitors took the opportunity to clear their doubts and gain valuable information from the Council members. Apart from MIA, the delegation also called on the Malaysian Association of Certified Public Accountants (MACPA) before proceeding to their next country in their mission tour. AN

Albert (left) presenting a memento to Liu

USM's Accounting Club 2002

Universiti Sains Malaysia's (USM) Accounting Club recently held its open ing ceremony on 17 January 2002. The ceremony was held at the School of Management and was attended by Prof. Daing Nasir Ibrahim the Dean of School of Management, representatives from MIA, MACPA, ACCA, CPA Australia and CIMA, as well as lecturers from the school of management, committee members of both the accounting club and management society, and accounting students. The move to start an accounting club was ?????? when the Bachelor of Accounting Degree was introduced during the 1999/2000 intake.

At the Opening Ceremony, Prof. Daing

One for the album ... Prof. Daing Nasir Ibrahim, Dean of USM's School of Management (seated centre) flanked by representatives from MIA, MACPA, ACCA, CIMA and CPA Australia together with fellow lecturers in the back row

Nasir in his speech, conveyed his gratitude to MIA for its support and assistance to USM in formulating the Accounting Degree curriculum. He also thanked the professional accountancy bodies for their participation in helping to develop the accounting programme.

Later, Prof. Daing Nasir together with the representatives from MIA, MACPA, ACCA, CIMA & CPA Australia cut a ribbon to symbolically mark the birth of USM's Accounting Club 2002. AN

Prof. Daing Nasir Ibrahim and representatives from MIA, MACPA, ACCA, CIMA and CPA Australia cutting the ribbon

NOTICE TO ALL MEMBERS
ERRATA

We wish to advise the following :

Page 100 Note 9 of the *Annual Report and Financial Statements 2001,* "Amount owing to suppliers" should be published as "Amount owing to sundry creditors".

"How to Lose Your Job as an Accountant"

In conjunction with Universiti Sains Malaysia's Management & Accounting week, Chan Choung Yau, President of MIA (Northern Branch) Toastmasters Club was invited to present a talk on 15 January 2002.

His unconventional choice of topic was "How To Lose Your Job As An Accountant". An excellent facilitator, Chan encouraged the students to list the various reasons for job loss as an accountant. Among the reasons given were closure, redundancy, dismissal, downgrading and others, all of which connoted negativity. The perfect reason as disclosed by Chan was PROMOTION, lose your job as an accountant and be promoted to say, Managing Director or Chief Executive Officer. Being an accountant, you will be in the ideal position to propel yourself on to the upper echelon of management. The topic was well thought of and highlighted the importance of a shift in paradigm thinking, the need to think out of the box.

Chan also shared some tips on the attributes of an accountant and how to get a promotion. The students actively participated in another session conducted by Chan to illustrate the importance of proper communication, both verbal and written.

Chan sharing a light moment with the audience before his presentation on "How To Lose Your Job As An Accountant"

Chan Yau with some of the USM students

The MIA (Northern Branch) Toastmasters Club welcomes all MIA members, accountancy graduates and students. It meets every 2nd and 4th Thursday at the MIA Penang office (located behind Citibank) from 8pm to 10pm the address is 1st Floor, Menara Penang Garden, 42A Jalan Sultan Ahmad Shah, 10050 Penang. Free admission for guests.

2002 MIA PENANG BRANCH COMMITTEE

Chairman
Steven Teh Eng Hin
Vice Chairman
Adelena Lestari Chong Ai Lin
Hon. Secretary
Yap Soon Hin
Hon. Secretary
Albert Yeoh Pit Shing
Committee members
Andy Chew Kah Hoe, Prof. Daing Nasir Ibrahim, Fan Kah Seong, Prof. Madya Dr. Hasnah Haron, Heah Theng Chye, Ho Swee Wang, Ooi Foo Kim, Richard Con Hock Chye, Prem Jitindar Singh, Tan Chooi Cheng. AN

CIMA

Bowling Fun

To celebrate the end of the November 2001 CIMA examinations, the CIMA Students Club organised a fun-filled Bowling Tournament for nearly 60 students at the Cheras Leisure Mall recently. The objectives of the Bowling Tournament were to engender teamwork and to promote closer relationships among students, members and staff of CIMA.

The participants were divided into 13 groups consisting of four students each. Emerging as the grand prize winner was the *Liverpool CFC-The Reds* team, followed by the *Sure Win* team which came in second. Not far behind in the scores was the *Keep Rolling* team which walked away with the third prize.

Steven Pragasam and Lee Pei Yeng won the Best Male and Female Bowler prizes. AN

Strike! ... We are the winners!

CIMA Members Get Together

CIMA organised its final Chartered Management Accountants Night for the year 2001 on 7 December at the Kuala Lumpur Golf & Country Club. Over 50 members and divisional staff attended the event.

Attendees were given an insightful presentation by B. K. Wong who shared his views on the current changes in the corporate world and why people, even those at the very top of their chosen profession, were making life changing decisions to leave their profession.

Following the presentation, Tuan Haji Muztaza bin Haji Mohamad (Immediate Past President of CIMA Malaysia Division), Lim Eng Seng (Institute Council Member for Area 16) and Yeo Tek Ling (CIMA/MIA Council member) took to the stage and sought member support for the MIA elections held on 29 December 2001. Those present had the chance to meet and mingle with newly admitted members of CIMA and at the same time share their knowledge and experience in their respective fields over a buffet dinner. AN

Strengthening Outreach in Melaka

To improve outreach to members in Melaka, the CIMA Melaka Informal Network was formed last December. Heading this network is Chairman, Tan Chee Wan FCMA, a Council member of CIMA Malaysia Division. He is assisted by Vice-Chairman, Eric Lee Choong Wai FCMA.

The appointment of the Informal Network committee members was held over dinner at the Renaissance Hotel in Melaka. The other committee members are James Lee Beng Tai ACMA (Treasurer), Sharon Wee Mui Ching ACMA (Secretary), Ng Kim Neo ACMA, Koh Lay Suat ACMA, Teh Kok Leong ACMA and Lee Lai Hock ACMA.

The Melaka Informal Network will serve the interests of CIMA members in Melaka through various activities and CPE programmes. AN

The Melaka Informal Network Committee ... Front Row (from left) : James Lee Beng Tai, Eric Lee Choong Wai, Tan Chee Wan and Sharon Wee Mui Ching. Back row (from left) : Lee Lai Hock, Ng Kim Neo, Koh Lay Suat and Teh Kok Leong

B.K. Wong (right) receiving a token of appreciation from Gurbakhish Singh

Doha Implementation Decision Explained

No area of WTO work received more attention or generated more controversy in the two years before the 4th Ministerial Conference in Doha, Qatar, than the issue of 'implementation' — developing countries' problems in implementing the WTO Agreements. Around 100 issues were raised. The decision, combined with paragraph 12 of the main Doha Declaration, provides a two-track solution :

- More than 40 items under 12 headings were settled at or before the Doha conference, for immediate delivery.
- The vast majority of the remaining items are immediately the subject of negotiations.

It covers the main areas :

- The main Doha Declaration and the resulting negotiations and other work; and
- The decision on implementation and resulting work.

The November 2001 declaration of the 4th Ministerial Conference in Doha, Qatar, provides the mandate for negotiations on a range of subjects and other work, including issues concerning the implementation of the present agreements. The negotiations include those on agriculture and services, which began in early 2000. A number of other issues have now been added. The declaration sets 1 January 2005 as the date for completing all but two of the negotiations. Negotiations on the Dispute Settlement register of geographical indications for wine and spirits will be resolved by the next Ministerial Conference in 2003. Progress is to be reviewed at the 5th Ministerial conference in 2003 (now to be held in Mexico) — the exact date has not been fixed yet.

The negotiations take place in the Trade Negotiations Committee and its subsidiaries. Other work under the work programme takes place in other WTO councils and committees.

Ministers also approved a linked decision on implementation-problems developing countries face in implementing the current WTO agreements. AN

New President and Vice-President for ICAI

At a meeting of the Council of the Institute of Chartered Accountants of India (ICAI) held in Delhi, Ashok Chandak of Nagpur and R. Bupathy of Chennai were elected as President and Vice-President respectively of the ICAI for the Year 2002-2003.

The ICAI established in 1949 has a membership of over 100,000 members spread all over the country and abroad. In addition about 200,000 students are pursuing the Chartered Accountancy course offered by the Institute. The ICAI functions through a network of five Regional offices and 96 Branches. The Examinations of the Institute are held every six months at about 157 centres spread over 78 cities across the country besides Kathmandu and Dubai.

ASHOK CHANDAK

A.K. Chandak, FCA, 48 years, a commerce graduate, became a member of the Institute of Chartered Accountants of India in the year 1978 and a Fellow Member in 1983.

He has been the Vice-President of ICAI for the year 2001-2002. He served the Institute as a member of the Central Council of ICAI since 1995. He has also served as a Vice-Chairman and as member of various Standing and Non-Standing Committees of the Institute. He has also been a member of the Western India Regional Council of the Institute from 1986-1994 and was the Vice-Chairman of the same during 1986 - 87. He was elected as a member of Nagpur Branch in 1979 and has served the branch in various official capacities up to 1985.

Chandak is the Chairman of the Committee on Education, Examination, Training & CPE of the South Asian Federation of Accountants (SAFA), which is an Apex body of SAARC. He is a member of the Working Group on SMPs constituted by the International Federation of Accountants (IFAC) and a permanent invitee on the Inter-Governmental Working Group of Experts on International Standards of Accounting & Reporting (ISAR) of UNCTAD.

He is also a member of the Central Direct Taxes Advisory Committee of CBDT; RBI Sub-Committee (Audit) of the Board for Financial Supervision; SEBI Primary Market Advisory Committee; SEBI Bhagwati Committee on Substantial Acquisition of Shares & Takeover Regulations; SEBI Committee on Par Value; Study Group of Dept. of Company Affairs to examine to operationalise the concept of corporate excellence on a substantial basis to sharpen India's Global Competitive edge and to further develop corporate culture in the country; Apex Committee to review/follow up the qualifications on the audit reports of the companies submitted by auditors; Working Group on Consolidated Accounting & other quantitative methods to facilitate consolidated supervision in banks constituted by RBI.

Chandak has been associated in various capacities with Trade Organisations like FICCI, Vidarbha Industries Association, NAG Vidarbha Chamber of Commerce, etc. He has also served several other professional organisations like All India Federation of Tax Practitioners, Sales Tax Practitioners Association of Maharashtra, Vidarbha Tax Practitioners Association and Sales Tax Bar Association. He has also authored books on Sales Tax, VAT and Service Tax and contributed several articles in professional Journals and Newspapers. He has also been a faculty in several National and International Seminars.

R. BUPATHY

R. Bupathy, 51 years, graduated in commerce from Vivekananda College Chennai and became a member of the Institute of Charted Accountants of India in 1976.

He has been a member of the Central Council of ICAI since 1995 and chaired a number of Non-Standing Committees of the Institute including the Board of Studies, Fiscal Laws Committee, Research Committee and has also served as Vice-Chairman of these Committees of the Institute. He has been twice Member of the Executive Committee and a member of the Disciplinary Committee for 2001-2002, the Standing Committees of the Institute. He has been member of several other important Non-Standing Committees of the Institute.

An academician, he has authored several publications and has been a faculty/ resource person in a number of national and international seminars. AN

TOP 100

ACCOUNTANCY FIRMS RANKING

PricewaterhouseCoopers handily held on to the first position in Public Accounting Report's 2001 Top 100 survey which reflects rankings of the top 100 public accounting firms, ranked by revenue. With net revenue of US$8.299 billion, PwC maintained a large margin over the second-ranked firm, Deloitte & Touche, which reported in with US$5.838 billion. The top 10 firms, according to the new ranking, are as follows :

- PricewaterhouseCoopers : US$8.299 billion
- Deloitte & Touche : US$5.838 billion
- KPMG : US$5.449 billion
- Ernst & Young : US$4.485 billion
- Andersen : US$3.6 billion
- BDO Seidman : US$420 million
- Grant Thornton : US$342 million
- BKD : US$198 million
- Crowe Chizek : US$185 million
- McGladrey & Pullen : US$167 million

Newcomers to this year's Top 100 list include :

- Katz, Sapper & Miller/Indianapolis, IN (not on last year's list because it was part of HRB Business Services)
- Rea & Assoc./New Philadelphia, OH
- Yeo & Yeo/Saginaw, MI
- Armanino McKenna/San Leandro, CA
- Ehrhardt Keefe Steiner & Hottman/ Denver, CO
- Vitale Caturano & Co./Boston, MA
- Knight Vale & Gregory/Seattle, WA
- Baker Newman & Noyes/Portland, ME AN

CAPA Strategic Review Task Force Meeting

17 JANUARY 2002 • THE PENINSULA, MANILA

The CAPA Strategic Review Task Force held its meeting in Manila, Philippines on 17 January 2002. It was chaired by Li Yong (China). The country representatives in attendance were as follows :

Australia	—	Joycelyn Morton
		Jim Dickson
Canada	—	Robin Harding
China	—	Li Shuang
		David Liu Weihua
Sri Lanka	—	Asite Talwatte
		(Absent with apologies)

Rahim (second from left) delivering his views and ideas on the strategic direction for CAPA

Li Yong (centre) chairing the meeting while Leong (CAPA Executive Director, sitting on the extreme right) looks on

Malaysia was represented by Abdul Rahim Hamid and Cik Sazalina Kamarudin. The meeting discussed CAPA's Strategic Directions. CAPA's Mission and Objectives were reviewed and it was established that they were in line with the International Federation of Accountant's (IFAC's). It was agreed that the current ones are still relevant (with some refinements). CAPA agreed to use available funds to achieve its objectives and improve services to members. One suggestion given was that CAPA create a data bank of reports that every member country submits e.g. demographics and current issues affecting the accountancy profession.

On CAPA's Structure and Meeting Schedule, it was agreed that there should be regular meetings to discuss current issues affecting the accountancy profession. It also identified two major aspects that members expect from CAPA; viz. the business of technical exchange of information and networking. In addition, invitations to IFAC to attend CAPA Excom meetings were encouraged in a move to promote cross-pollination and sharing of mutual interests between IFAC and CAPA.

The next meeting would be held in Japan in early April 2002 in conjunction with the Excom Meeting. AN

PwC to Hive Off Consultancy Arm

The need to separate the accounting and consultancy businesses has been made more urgent by the Enron debacle

The consultancy division of business services giant Pricewaterhouse-Coopers (PwC) is to uncouple from the general accountancy practice through a 'global and rapid initial public offer (IPO)'. The details of the plan — hastened by the Enron debacle — will be unveiled later this week.

The decision was announced by PwC Chief Executive, Sam DiPiazza, at a meeting of senior partners, though it has yet to be endorsed by the firm's main governance bodies. According to an internal communication obtained by AFX News, the divorce from the audit practice has been accelerated by the Enron collapse, though PwC played no part in the world's biggest financial scandal.

However, the debacle has highlighted possible conflicts of interest when audit and consultancy work is carried out for the same client. PwC's rival Andersen earned millions in consultancy fees from Enron as well as being its auditor.

PwC consulting last year generated revenues of US$6.7 billion and a flotation could value the business at US$5 billion to US$10 billion, analysts said.

A PwC spokesman confirmed : "We've been pursuing the options for the legal separation of the divisions for some time - a third-party transaction, strategic investment or an IPO." However, she refused to confirm that the spin-off would be unveiled this week. "We don't comment on rumour or speculation."

According to recent reports PwC set an internal deadline of 1 July for legal separation of its consultancy and audit arms. It has long wanted to separate the two increasingly disparate businesses and planned to sell the unit to computer giant Hewlett-Packard for as much as US$18 billion. AN

ICAA Visits MIA

Allen Blewitt paid a courtesy visit to the Institute recently. MIA President, Abdul Samad Hj. Alias was briefed about the various changes on the Chartered Accountants (CA) programme. He also touched very broadly on the reciprocal arrangement issues as well as the pressure for most countries to enter into Mutual Recognition Arrangements (MRA's). He agreed that much of the changes would be to go into branding the Australia's Chartered Accountants as part of "the heart of business, offering their skills to a range of organisations and providing solutions to a wide variety of business problems".

He also impressed upon the fact that the 'CA designation' is recognised worldwide as a mark of excellence, inspiring respect and confidence. Not only are CAs the elite of their profession, they maintain the highest professional and ethical standards. This means that CAs are justly proud of their title because it denotes the independence and objectivity that are the cornerstones of the profession.

One of the more interesting points he raised was the changes to the CA programme (previously known as the PY programme). In short the CA Programme equipped with several modules (from the CA Foundations to the Final Integrative) is designed to develop its candidate to be informed of the latest international, disciplinary and business knowledge and be forward thinking business advisors. All in all they can enter immediately after High School and finish with three years of supervisory experience (articleship). In total, it would take about six to seven years. One interesting point to note is their mode of delivery of the programme. It is highly technology driven and is made a lot more personalised and small with interactive discussions, both at the personal level as well at the internet level.

Allen Blewitt, Deputy CEO, ICAA

He indicated that they do recognise 21 companies or firms in Malaysia for the purpose of 'training' grounds for budding ICAA members.

On the developments relating to the negotiations at the WTO level, he also touched on the MRAs entered upon with the American Institute of Certified Public Accountants (AICPA) and the various stages of negotiations they had to go through before it finally materialised. AN

IAPC to Get New Name

The International Federation of Accountants' International Auditing Practices Committee is to be renamed by the middle of 2002. This was one of the recommendations that IFAC's board approved recently.

It is renamed International Auditing and Assurance Standards Board (IAASB) to reflect its role better. Its objectives are revised and membership has expanded from 14 to 18 and its technical resources increased.

MIA has submitted our nomination to be on the board of the IAASB.

Excerpts from IFAC Summary of significant changes

IAPC composition

The recommendations in the draft Report that garnered the most comment were those addressing the proposed IAPC membership structure.

Perhaps the most divergent views received were on the proposal to introduce non-auditor members. Many responses fully supported the recommendation, while others strongly disagreed or suggested other ways that non-auditors could be included in the standard-setting process at a more strategic level. We concur with the majority of respondents that the reasons for including non-auditors on IAPC are valid and, therefore, continue to recommend that there be three non-auditor members.

We were, however, persuaded by those who argued that our commitment to the principle of including non-auditors appeared suspect when we suggested in the draft Report that auditors could be appointed to these positions if non-auditors could not be identified. We agree that best efforts must be made to find appropriate non-auditors to serve on IAPC. We also accept that suggesting that others can fill these positions might not encourage the extra effort that might be needed to identify qualified non-auditors. For that reason, we have deleted any reference to substituting auditors for non-auditors in our final Report.

Other comments on membership related primarily to the adequacy of representation of various constituencies, in particular smaller audit firms and member bodies - both those with well-developed national standard-setting procedures and those who do not have national standard-setting functions. A number of responses made the point that it would be very difficult in practice for an individual to "wear two hats" - which might have been seen as a solution to achieve necessary balance within the fifteen member complement.

In our draft Report, we recommended increasing the size of IAPC by one. For the reasons discussed above, we propose increasing the number of members by a further three (thus increasing from IAPC's current 14 members to 18 in total), with ten, rather than seven, members nominated from member bodies. While recognising that this increases the number of people at the table, we believe such an increase is necessary to optimise representation. At the same time, we are continuing to limit to one the number of technical advisors with the right to the floor at meetings that each member can bring to meetings (recognising that, as we propose that IAPC meetings be public meetings in future, other representatives from member bodies or national standard-setters would be entitled to attend the meetings as observers).

In addition, we have clarified in the final Report our view that the principle of firm/country balance should not preclude selecting an individual from a firm or country that is already represented. For example, an individual from a particular country member body should not be precluded from serving as an IAPC member if the Transnational Auditors Committee has also nominated an individual from the same country, or vice versa. Both firm and member body perspectives are valuable to the standard-setting process and it would be unrealistic to expect one member to be able to reflect the perspectives of both. Within an eighteen member complement, however, the Nominating Committee should have sufficient flexibility to achieve appropriate firm/country balance without being unduly restricted if the "best persons" among the various nominations include more than one person from any particular firm or country.

We believe that increasing the number of member bodies represented on IAPC from seven to ten should address a number of the most significant concerns raised in the responses to the draft Report. To ensure appropriate representation from auditors of small entities and smaller firms of auditors, we would suggest that member bodies be encouraged to consider putting forward nominations that are either auditors of small entities or from smaller firms of auditors as possible candidates to achieve appropriate balance in IAPC's overall composition.

Proposed Change in IAPC's Objectives and Name

One suggestion raised in the responses that we believe warrants serious consideration is changing the name of IAPC. We are proposing that the name of IAPC be changed to the International Auditing and Assurance Standards Board (IAASB).

Changing "Committee" to "Board" would be a precedent within IFAC. However, we believe that such a change, together with a reference to "standards" rather than "practices", would convey an important message regarding real change being made in IAPC's stature — including raising the bar on the expected quality and acceptance of ISAS as the global standards for auditors to follow.

Adding "assurance" to IAPC's name gives appropriate recognition to IAPC's responsibility for standards not only for the audit of financial statements, but also for assurance engagements. Some responses believed that there was not adequate attention given to assurance engagements in the draft Report. We have also made corresponding changes to the proposed objectives for IAPC to provide greater acknowledgement of IAPC's responsibility for assurance engagements.

An important change we are proposing in the objectives is to remove the reference to "unquestionable" high quality in reference to the standards and guidance. Our reasons for doing so do not include a change in our intent — the international standards on auditing must be perceived to be high quality standards in order to be accepted by stakeholders worldwide as the appropriate benchmark for audit performance. In fact, we believe that our recommendations collectively raise the bar in that respect. Nevertheless, we were convinced by respondents that the phrase "unquestionable quality" might be subject to misinterpretation and, therefore, have deleted that phrase. On the other hand, we have elaborated further in our final Report on what we expect of "quality standards" by defining their characteristics. We are also encouraging IAPC to address the authority and hierarchy of its standards and statements, including the proper interpretation of black and grey lettering, to eliminate any ambiguities related thereto.

There were also quite strongly held views in the responses regarding the emphasis in the draft Report on IOSCO endorsement — some arguing that the "overemphasis" on governments and, in particular, regulators could be interpreted as giving them preference over (and greater influence than) other stakeholders, including the profession itself.

IOSCO endorsement is a strategic objective of IFAC and is also of high priority to IAPC. Given IOSCO's commitment to review the ISAS as the basis for its endorsement of them in future, this focus is justified but does not in any way diminish the importance of other stakeholders in IAPC's processes. Respondents pointed out that the EU is equally important at this time as it is also in the process of considering the role that the ISAS might play in Europe in the future. Other regulators may also have similar processes under way. Accordingly, we have made changes to the Report to give greater recognition to the EU and other stakeholders.

Role of National Standard Setters

There was virtually unanimous support for the need to have close working relationships, liaison and co-ordination with the national standard-setters. A number of responses pointed out, however, that if convergence is the goal, stronger ties than had been proposed in the draft Report are needed.

In part, the increase in the size of IAPC will allow more member bodies with well developed standard-setting processes to be members of IAPC at any point in time — something that a number of respondents argued was important. We have also strengthened the wording of this section of the final Report. The changes emphasise that the relationships with national standard-setters are important, not only to benefit from the work done by national standard-setters with advanced agendas and important resources, but also to put in place the relationships that will be vital to promote convergence through shared goals and aligned agendas.

Strengthened Consultative Process

A number of responses emphasised the vital importance of consultation and communication to IAPC going forward. This includes not only the Consultative Advisory Group meetings and IAPC's regular newsletters and other communications vehicles, but also a programme of face-to-face meetings and ongoing consultations to manage IAPC's relationships with regulators, national standard-setters, and other key stakeholders.

We had envisaged the importance of these functions in our draft Report in our recommendation to elevate the role of the Chair to substantially a full-time occupation in light of his or her increased role as public spokesperson for IFAC on IAPC matters. We continue to believe that the Chair position will need to be essentially full-time. We have further recognised the importance of the consultative process in our final Report by strengthening the recommendations on how communications might be improved.

In our draft Report, we also proposed introducing the position of Vice Chair to support the work of the Chair. While there was support for a Vice Chair role, responses expressed concern regarding the lack of transparency if the Vice Chair is selected by the Chair alone. We acknowledge these concerns and have amended our final recommendations. Since the Chair and Vice Chair will need to work closely together, we believe that the Chair's input on the selection of the Chair is vital, but accept that the Vice Chair appointment should go through normal approval processes. Thus, although we would expect the Nominating Committee would consult with the Chair, we agree that it should be the Nominating Committee that ultimately puts the nomination forward to the IFAC Board for approval. Furthermore, while we do not believe that the Vice Chair should necessarily be considered the designated successor of the Chair, we accept that such a possibility should not be disallowed.

Planning Sub-committee

Responses reflected unease regarding the proposed responsibilities for the Planning Sub-committee. There was concern expressed that the Planning Sub-committee would be essentially usurping responsibilities of IAPC itself — a concern that was heightened given the fact that meetings of the Planning Sub-committee would not be opened to the public.

In our final Report, we have clarified the responsibilities that we foresee for the Planning Sub-committee. We agree that IAPC should retain responsibility for interpretative guidance and for approving new projects that are added to its agenda. On the other hand, we can envisage the need for a strong planning function under the new regime and believe that the Planning Sub-committee's current role can be appropriately expanded to assist in that regard. The Planning Sub-committee can, for example, be responsible for preparing IAPC's long term plan and advise the Chair on establishing and managing priorities and on effectively dealing with agenda logistics and efficiencies.

Other Important Issues

Nominating Committee

A number of respondents commented on the key role that the Nominating Committee plays in the selection of IAPC, and other IFAC Committee, members. It is for this reason that we had emphasised in our draft Report that its work is crucial to the success of IAPC's goal of being seen to operate in the public interest, as well as to the successful implementation of our recommendations. It became apparent in the responses that a surprising number of stakeholders are not fully familiar with the Nominating Committee's membership, charter and operational activities. A number of responses specifically requested greater clarity on the Nominating Committee's terms of reference given the importance of the role that it currently plays and will be called upon to play in the future. Others, such as the World Bank, emphasised that proper public interest oversight of the Nominating Committee is essential.

The membership, organisation and processes of the Nominating Committee are beyond our terms of reference. However, we reiterate our view that they are critical to the successful implementation of our recommendations and IFAC's ability to demonstrate that IAPC operates in the public interest. For these reasons, we urge IFAC to address the concerns raised in the responses regarding the Nominating Committee's role and structure.

Public Sector Auditing

We have recommended adding a public sector representative as a "non-auditor" member (i.e. an individual that is not an auditor in public practice) because we believe that it would be useful for IAPC to have a public sector point of view in IAPC's deliberative process.

A number of responses, including the World Bank and the IFAC Public Sector Committee itself, suggested that IAPC should assume responsibility for setting auditing standards for the public sector as well as for the private sector.

The IFAC Public Sector Committee (IPSC) currently has responsibility for public sector auditing standards. In practice, this is achieved by providing a public sector perspective (PSP) on the applicability of the ISAs on the audit of financial statements of public sector entities. In our view, the process is working reasonably well.

Our terms of reference did not include consideration of the scope of IAPC's responsibilities in this regard and for that reason we have not addressed this issue in our final Report. IFAC may want, however, to revisit the respective responsibilities of IAPC and the IPSC in the future.

Timing of implementation

We are aware that there are a number of other important IFAC initiatives under way that will influence IAPC's activities in the future, including the creation of the new Public Oversight Board and the compliance activities of the Transnational Audit Committee. Indeed, a number of respondents commented on the importance of these initiatives to the overall strategy. These IFAC initiatives are key to the worldwide accountancy profession's self-regulatory regime and are important in creating the foundation necessary to support quality audits in future. As we emphasise in our final Report, quality auditing standards alone do not beget quality audits.

We understand, and appreciate the reasons why, these companion initiatives may take time to put into place. In our view, however, there are no reasons why the changes that we propose to IAPC's membership, organisation and processes need to be delayed pending further progress on these companion initiatives. In fact, we believe that there is a compelling need to move forward with them. IAPC is at an important threshold. With increased interest in the ISAs by not only member bodies, but also influential organisations including IOSCO and the EU, IAPC needs to be seen as continuously improving its processes so that stakeholders are confident that their support for the international auditing standard process is warranted. Delaying the necessary reforms to IAPC's membership, organisation and processes could delay IAPC obtaining the recognition it strives for. We encourage IFAC to implement our recommendations, including making necessary changes to IAPC's terms of reference (which might more appropriately be referred to as a "charter" if IAPC becomes a Board), as soon as practicable.

Given the extent of public interest in this review, we are of the view that our final Report should be disseminated publicly to ensure appropriate accountability to the many respondents to the draft Report. This could be achieved, for example, by posting our final Report and transmittal letter on IFAC's website. AN

73rd AFA Council Meeting

11-12 JANUARY 2002

The meeting was held at the Shangri La Hotel located on the banks of the Chao Phraya river. The plush setting in beautiful tropical gardens is easily accessible to central business and shopping hubs certainly made it a thought provoking meeting a successful one.

1. The 73rd AFA Council Meeting was held in Bangkok and was hosted by the Institute of Certified Accountants and Auditors of Thailand (ICAAT).
2. The meeting was attended by member countries from Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam. The Associate members in attendance were CPA Australia and Association of Chartered Certified Accountants. There were no representatives present from the Mongolian Institute of Certified Public Accountants and the Brunei Darussalam Institute of Certified Public Accountants.
3. MIA was represented by :

- Nik Mohd Hasyudeen Yusoff (representative)
- YM Raja Dato' Seri Abdul Aziz bin Raja Salim
- Ab Haron Gani (Accountant-General's Office)
- Sazalina Kamarudin (accompanying secretariat)
- Paitoon Taveebhol (ICAAT) chaired the meeting, being his first as the President of AFA. It was also unanimously resolved that Dr Wong from Vietnam be the Deputy President of AFA until 2003. The newly appointed Secretary General, Pichpajee Saichuae and Deputy Secretary General, Lee (both from Thailand) took office on 11 January 2002.

4. Khoo Ho Tong (Singapore) has taken over the post of the Treasurer, previously held by Roland Ma.
5. In respect of the Liberalisation of Trade in Services, it was decided that a Task Force comprising interested member bodies be set up to discuss issues re-

lating to liberalisation of trade in services (under ASEAN Framework Agreement in Services for Accountancy Services, CPC 862). The main objective would be "developing" a common stand among countries in the ASEAN region. The countries named to be part of the Task Force include Malaysia, Indonesia and Singapore. In view of the newly set-up Task Force, Malaysia also took the opportunity to brief the Council on the recent developments at the Coordinating Committee on Services held in Brunei on 9-10 January 2002.

Reports on the latest developments of the status of the Accountancy Profession from members were tabled and discussed. The main highlights are as follows :

The newly elected AFA President Paitoon Taveebhol, ICAAT (front row centre) and ICAAT's President Professor Kesaree Narondej (on Paitoon's right) with members of the 73rd AFA Council Meeting.

PRIMARY MEMBERS

i. The Brunei Darussalam Institute of Certified Public Accountants reported that it has formed a joint venture with a private education provider for the provision of accountancy and technician education in Brunei Darussalam for the year 2002.

ii. The Lao Institute of Certified Public Accountants reported that accounting and auditing firms have been authorised to perform according to the mandate of the accounting and the auditing services of the Lao PDR. There are about 12 companies being set up in Lao, including PWC and KPMG.

iii. The new President, Calito B. Fuentesfina reported for the Philippines Institute of Certified Public Accountants and mentioned that the Revised Accountancy Law is being reviewed by the Accountancy/Professional Regulation Commission for the submission to the Philippine Congress.

iv. The Institute of Certified Public Accountants of Singapore reported that it had organised a forum for members to deliberate on how Singapore's corporate legislation and regulatory regime could be improved to benefit the business community. The main issues discussed are as follows :

1. That the exempt private company structure may not be relevant
2. That exempt private companies should continue to appoint professionally qualified company secretaries; and
3. That the statutory audit requirement for all companies should remain although there may a case for dormant companies to be considered for exemption from audit. ICPAS also reported that the scheme of auto inclusion of dividends from private companies had been effected beginning 1 January 2002. This has enabled taxpayers to complete their tax returns efficiently without the need to report on Singapore dividends and forward supporting dividend vouchers.

v. The Institute of Certified Accountants and Auditors of Thailand's President, Professor Kesaree Narondej was present at the meeting. ICAAT also reported that the IAS is only applicable for large organisations, particularly listed company. In order to assist non-listed companies to be more flexible and have less complicated accounting standards, ICAAT issued the "Exception Rules of Accounting Standard for a Non-Listed Company" which consisted, inter alia, the Presentation of Financial Information by functions, Cash Flow Related etc.

vi. The Vietnam Accounting Associations reported that it had drafted and finalised 10 new accounting standards in the last two years. All have been submitted to the Ministry of Finance for comment and release.

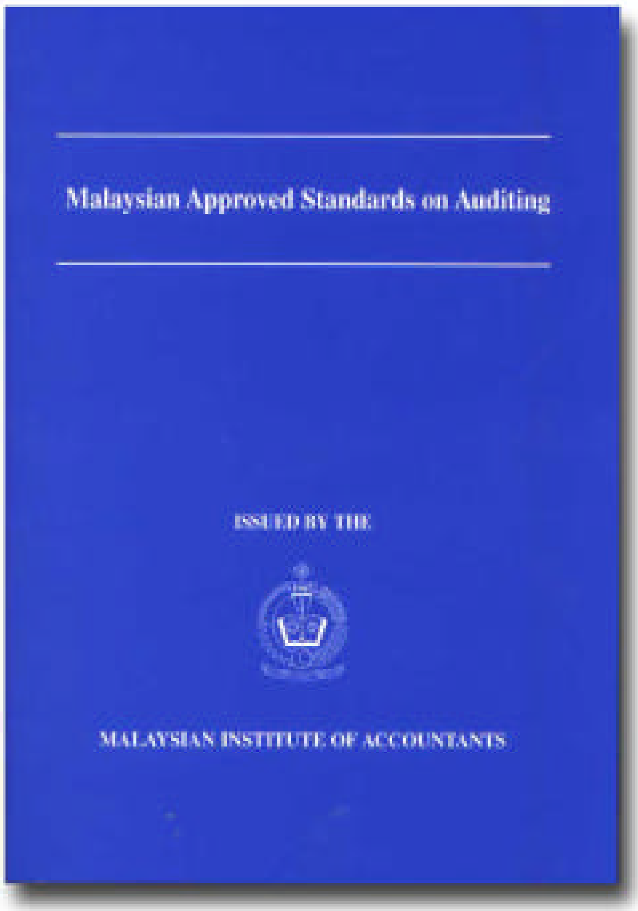
ASSOCIATE MEMBERS

vii. As the Associate member, CPA Australia reported that the New Privacy Amendment Act 2000 was passed and took effect on 21 December 2001. The Act regulates sole traders, consultants, body corporates, partnerships and various government businesses on how it uses, stores, discloses and disposes of personal information. Small businesses need to comply with several requirements to obtain exemptions. Businesses that fail to comply would be liable to pay compensation.

viii. The Association of Chartered Certified Accountants reported that at a recent survey most accountants rejected the move towards tax harmonisation of the European Union although they believed that it would take place regardless of the survey being carried out. In addition, ACCA also reported that it recently published a new guidebook on M-Commerce (Mobile Commerce) to understand the impact of mobile technology.

ix. The Mongolian Institute of CPA reported that in November 2001, the Parliament of Mongolia approved the amendments to the Law on Accounting of Mongolia. Currently, a draft law on auditing is under discussion among professional bodies in Mongolia. AN

Malaysian Approved Standards on Auditing (MASA)



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These standards should be read in conjunction with A — Preface to Approved Standards on Auditing, AI 100 — Preface to International Standards on Auditing and Related Services; AI 110 — Glossary of Terms and AI 120 — Framework of International Standards on Auditing.

These standards are mandatory for all members who assume responsibilities as independent auditors to observe in respect of the conduct of their audit under all reporting frameworks.

An update to the Malaysian Approved Standards on Auditing will include the following International Standards on Auditing issued by the International Auditing Practices Committee :

ISA 100	—	Assurance Engagements
ISA 260	—	Communications of Audit Matters with Those Charged with Governance
ISA 505	—	External Confirmations
ISA 570 (new)	—	Going Concern
IAPS 1010	—	The Consideration of Environmental Matters in the Audit of Financial Statements
		Glossary of Terms (revised)

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