MALAYSIAN INSTITUTE
OF ACCOUNTANTS

Driving Quality of Financial Reporting

Financial Statements Review 2020/2021 Annual Report

ABOUT THE MALAYSIAN INSTITUTE OF ACCOUNTANTS

Established under the Accountants Act 1967, Malaysian Institute of Accountants (MIA or the Institute) is the national accountancy body that regulates, develops, supports and enhances the integrity, status and interests of the profession in Malaysia. MIA accords the Chartered Accountant Malaysia or C.A. (M) designation to a professional in accountancy, business and finance with a recognised qualification and relevant work experience.

Working closely alongside businesses, MIA connects its membership to a wide range of information resources, events, professional development and networking opportunities. Presently, there are more than 36,500 members making their strides in businesses across all industries in Malaysia and around the world.

MIA's international outlook and connections are reflected in its membership of regional and international professional organisations such as the ASEAN Federation of Accountants (AFA), and the International Federation of Accountants (IFAC).

- PURPOSE -

To regulate and develop the accountancy profession to support economic growth and nation building

- VISION -

To be a globally recognised Professional Accountancy Organisation (PAO) in regulating and developing the profession for nation building

- VALUES -

Integrity, Mutual Trust & Respect, Professionalism, Accountability, Commitment, Teamwork, Sustainability

MIA's Functions

Section 6 of the Accountants Act 1967 (the Act) states that the functions of the Institute shall be:

- To determine the qualifications of persons for admission as members;
- To provide for the training and education by the Institute or any other body, of persons practising or intending to practice the profession of accountancy;
- To approve the MIA Qualifying Examination (QE) and to regulate and supervise the conduct of that Examination;
- To regulate the practice of the profession of accountancy in Malaysia;
- To promote, in the manner it thinks fit, the interest of the profession of accountancy in Malaysia;
- To render pecuniary or other assistance to members or their dependents as it thinks fit with a view to protecting or promoting the welfare of members; and
- Generally, to do such acts as it thinks fit for the purpose of achieving any of the aforesaid objectives

FOREWORD FROM THE CHAIRMAN FINANCIAL STATEMENTS REVIEW COMMITTEE

Financial statements are the core of a financial reporting system in providing relevant and reliable financial information to investors and other users. High quality financial statements hence play an important role in supporting a strong and confident capital market.

Over the years, financial reporting requirements have become increasingly complex and financial statements are now subject to much greater scrutiny by regulators. In addition, as the outbreak of the COVID-19 pandemic impacted businesses and the economy significantly and created uncertainty around business continuity, investors began demanding that companies provide greater transparency in financial reporting. As such, the focus has shifted from routine financial reporting to an emphasis on high quality financial reporting.

To ensure investors receive high quality, focused and reliable financial statements, each and every participant in the financial reporting ecosystem plays a distinctive role in the preparation of financial statements. All parties should collaborate and uphold professionalism to drive and elevate the quality and reliability of financial reporting.

Consistent application of accounting standards and disclosures will ensure that the financial statements remain transparent and comparable. The Financial Statements Review Committee (FSRC or the Committee) is entrusted with the responsibility to monitor the quality of financial statements for the purpose of determining compliance with statutory and other requirements, applicable approved accounting standards and approved auditing standards. In line with its function and role in the financial reporting ecosystem, the FSRC provides guidance to companies to meet the financial statements disclosure requirements as prescribed in the relevant standards. Through this report, the Committee continues to share the key review findings and financial reporting best practices which preparers should consider in the preparation of financial statements.

For the period under review, FSRC continued to focus on the application of new standards, particularly MFRS 16 Leases which became effective from 1 January 2019. Deficiencies were identified in terms of the clarity of disclosures, and the Committee suggests that more specific disclosures be required on those areas that involve judgement and estimates based on the event and circumstances of the entity. This would help users to understand the transactions undertaken by the entity and how the standards are applied. We also identified certain findings in other areas that continue to be a challenge in financial reporting practices. The Committee recommends that entities should include the appropriate level of qualitative disclosures to increase the transparency of financial information and better understanding of the activities undertaken by the entities.

FSRC will continue to discharge its role to monitor the compliance of financial statements and share financial reporting best practices to uphold the quality of financial reporting. As one of the surveillance functions, FSRC continues to support the Institute to regulate and develop the accountancy profession, which is in line with the Institute's distinctive vision for nation building.

IRVIN MENEZES
CHAIRMAN
FINANCIAL STATEMENTS REVIEW COMMITTEE

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A Key Observations from Review of Financial Statements

The Financial Statements Review Committee ("FSRC" or "the Committee") of the Institute was set up with the aim of upholding the quality of financial reporting of entities listed on Bursa Malaysia and public interest entities. The Committee reviews audited financial statements and audit reports that are prepared by or are the responsibility of members of MIA, for the purpose of determining compliance with statutory and other requirements, applicable approved accounting standards and approved auditing standards in Malaysia.

A Key Observations from Review of Financial Statements

To enhance quality of financial reporting, the FSRC communicates significant findings to members and highlights common deficiencies arising from the review of financial statements of public listed entities for the review period from July 2020 to June 2021. The financial statements under review are those with financial years ended ranging from December 2019 to December 2020.

The reviews identified the following significant findings on common disclosure omissions and deficiencies.

A. MFRS 16 *Leases*

MFRS 16 *Leases* ("MFRS 16") is applicable to companies with annual periods beginning on or after 1 January 2019. An entity is expected to present both qualitative and quantitative disclosures regarding their leasing activities within the notes to the financial statements.

For information, this report is focused on the disclosure requirements on a lessee's financial statements. MFRS 16 requires lessees to present all disclosures in a single note or separate section in its financial statements. However, a lessee need not duplicate information that is already presented elsewhere in the financial statements, provided that the information is incorporated by cross-reference in the single note or separate section about leases.

The objective of lessee disclosures is to enable financial statement users to assess the effect that leases have on a lessee's financial statements (e.g., the amount, timing and uncertainty of cash flows arising from leases).

Being the first year of review on MFRS 16 adoption, we noted that there is still room for improvement in terms of quality of lessee's disclosures in the financial statements.

Common issues identified during our review include the following:

Observation A1

Presentation of right of use ("ROU") assets not in accordance with MFRS 16 which requires a lessee to present ROU assets either in the statement of financial position as separate line item from other assets, or disclose in the notes of the underlying assets [MFRS 16.47(a)].

As noted in some of the disclosures, ROU assets were presented in two separate financial statements line items, i.e property, plant and equipment and ROU assets.

Separately, it was unclear from another disclosure whether any ROU assets were recognised in the financial statements.

FSRC's analysis and conclusion

MFRS 16.47(a) states that a lessee shall either present in the statement of financial position, or disclose in the notes, ROU assets separately from other assets.

If a lessee does not present ROU assets separately in the statement of financial position, the lessee shall:

(i) include ROU assets within the same line item as that within which the corresponding underlying assets would be presented if they were owned; and

(ii) disclose which line items in the statement of financial position include those ROU assets.

In any case, the FSRC is of the view that the selected application should be consistently applied.

Illustrative A1.1- Present ROU assets as separate line item

Statement of Financial Position as at 31 Dec 20X1

	Note	Group		Company	
		31.12.X1	31.12.X0	31.12.X1	31.12.X0
Assets		RM'000	RM'000	RM'000	RM'000
Property, plant and equipment		xxx	xxx	xxx	xxx
Right-of-use assets	A	xxx	xxx	xxx	xxx
Investment Properties		xxx	xxx	xxx	xxx
Investment in subsidiaries		xxx	xxx	xxx	xxx
Other Investments		xxx	xxx	xxx	xxx
At 31 Dec 20X1		xxx	xxx	xxx	xxx

Note A – Right-of-use Assets

Group	Note	Land	Buildings	Plant and equipment	Total
Cost		RM'000	RM'000	RM'000	RM'000
At 1 Jan 20X1		xxx	xxx	xxx	xxx
Addition		-	xxx	xxx	xxx
Disposal		(xxx)	(xxx)	(xxx)	(xxx)
Derecognition		-	-	(xxx)	(xxx)
At 31 Dec 20X1		xxx	xxx	xxx	xxx
Depreciation and Impairment					
At 1 Jan 20X1		xxx	xxx	xxx	xxx
Addition		-	xxx	xxx	xxx
Depreciation		(xxx)	(xxx)	(xxx)	(xxx)
Impairment loss		(xxx)	(xxx)	(xxx)	(xxx)
Reversal of impairment loss		xxx	xxx	xxx	xxx
Derecognition		-	-	(xxx)	(xxx)
At 31 Dec 20X1		xxx	xxx	xxx	xxx
Carrying amount 31 Dec 20X1		xxx	xxx	xxx	xxx

Illustrative A1.2– Present ROU assets within the same line item of the corresponding underlying assets

Note X – Investment Property*

The investment properties include properties that are held as right-of-use assets, as well as properties that are owned by the Group. The leases of investment properties contain an initial non-cancellable lease term of 5 to 10 years.

Group	Note	Owned property	Right-of-use assets	Total
		RM'000	RM'000	RM'000
At 1 Jan 20X1			xxx	xxx
Acquisition		xxx	xxx	xxx
Reclassification from property, plant and equipment		xxx	xxx	xxx
At 31 Dec 20X1		xxx	xxx	xxx

**For this illustrative, the ROU assets are presented within investment property.*

Observation A2

There was no disclosure of total cash outflow for leases [MFRS 16.53(g)].

Most did not disclose total cash outflow for leases in accordance with requirements of MFRS 16.53(g).

In some instances, it was noted that there were expenses relating to short-term and low value asset disclosed in the financial statements. However, only cashflows for payment of lease liabilities were disclosed in the Statements of Cash Flows ("SOCF"), instead of total cash outflow for leases.

FSRC's analysis and conclusion

The FSRC would like to reiterate that MFRS 16.53(g) states that a lessee shall disclose the total cash outflow for leases for the reporting period.

The above information can be presented in the notes or cross reference to where the disclosure is included, for example as a footnote to the SOCF.

Illustrative A2

Cash outflows for leases as a lessee*

	Note	Group		Company	
		20X1	20X0	20X1	20X0
		RM'000	RM'000	RM'000	RM'000
Included in net cash from operating activities:					
Payment relating to short-term leases		xxx	xxx	-	-
Payment relating to leases of low-value assets		xxx	xxx	-	-
Payment relating to variable lease payments not included in the measurement of lease liabilities		xxx	xxx	-	-
Interest paid in relation to lease liabilities		xxx	xxx	-	-
Included in net cash from financing activities					
Payment of lease liabilities		xxx	xxx	-	-
Total cash outflows for leases**		xxx	xxx	-	-

**The above illustrative can be presented in the notes or as a footnote to the Statements of cash flows*
***The above illustrative with itemised cashflows is best practice. Alternatively, entity may disclose total cash outflows without itemised cashflows.*

Observation A3

There were no disclosure of expenses relating to short-term leases and low-value assets accounted for by applying MFRS 16.6.

There were rental expenses disclosed but it was unclear whether these rental expenses relate to short-term leases and low-value assets.

FSRC's analysis and conclusion

The FSRC would like to reiterate that MFRS 16.53(c) and (d) requires a lessee to disclose the expense relating to short-term leases and low-value assets accounted for by applying MFRS 16.6.

Further MFRS 16.60 requires a lessee that accounts for short-term leases or leases of low-value assets applying paragraph 6 of MFRS 16 to disclose the fact. The disclosure can be made in the accounting policy for leases or the related notes on leases.

Illustrative A3.1 [MFRS16.53(c), (d) & (e)]

	Note	Group		Company	
		20X1	20X0	20X1	20X0
		RM'000	RM'000	RM'000	RM'000
Expenses/ (income) arising from leases:					
Expenses relating to short-term Leases		xxx	xxx	-	-
Expenses relating to leases of low-value assets		xxx	xxx	-	-
Expenses relating to variable lease payments not included in the measurement of lease liabilities		xxx	xxx	-	-

Illustrative A3.2 [MFRS16.60]

Significant Accounting Policy- Leases – recognition and initial measurement

The Group has elected not to recognise right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets. The Group recognises the lease payments associated with these leases as expenses on a straight-line basis over the lease term.

Observation A4

There was no information about leasing activities in accordance with MFRS 16.59.

FSRC's analysis and conclusion

The requirement of MFRS 16.59 relates to additional qualitative and quantitative information about leasing activities of lessee.

This additional information may include, but is not limited to, information that helps users of financial statements to assess the nature of the lessee's leasing activities, variable lease payments, exposure to lease extension options, residual value guarantees and lease commitments.

Companies can consider application guidance in paragraphs B48 to B52 in relation to the above. Further, companies shall, as far as practicable, present notes in a systematic manner [MFRS101.113] and cross-reference to the related notes.

Illustrative A4.1 [MFRS16.59(a)]

The Group leases land and buildings for its office and factories. The leases for office run for a period of 10 years, and leases of factories for three to five years. Some leases include an option to renew the lease for an additional period of the same duration after the end of contract term. Lease payments are increased every five years to reflect current market rentals.

Illustrative A4.2 [MFRS16.59(b)(i), B49]

Variable lease payments

The Group has lease contracts for machinery that contains variable payments based on the number of units to be manufactured. The fixed and variable payments for the year ended 31 December 20X1 were as follows:

Group	Fixed payments	Variable payments	Total payments
	RM'000	RM'000	RM'000
Leases with lease payments based on number of units manufactured	xxx	xxx	xxx
	xxx	xxx	xxx

5% increase in units produced for the relevant products would increase total lease payments by 1%.

Illustrative A4.3 [MFRS16.59(b)(ii), B50]

Extension and termination options

Extension and termination options are included in some of the leases of the Group to maximise operational flexibility in terms of managing the assets used in the Group's operations. The extension and termination options held are exercisable only by the Group and not by the respective lessor.

Group	Lease liabilities recognised	Potential future lease payments not included in lease liabilities	Historical rate of exercise of extension options
	RM'000	RM'000	
Buildings	xxx	xxx	xx%

Illustrative A4.4 [MFRS16.59(b)(iii), B51]

Residual value guarantee

To optimise lease costs during the contract period, the Group provides residual value guarantees in relation to some of the equipment leases.

The Group initially estimates and recognises amounts expected to be payable under residual value guarantees as part of the lease liability. The expected residual value at lease commencement is equal to or higher than the guaranteed amount, the Group does not expect to pay under the guarantees.

The Group monitors the use of these equipment and reassesses the estimated payable under the residual value guarantees at the reporting date. As a 31 Dec 20X1, the expected amount payable under the residual guarantees is RMxxx.

Illustrative A4.5 [MFRS16.59(b)(iv)]

Leases yet to commence

The Group has lease contracts that have not yet commenced as at the reporting date. The future lease payments for these non-cancellable lease contracts are RMxxx within one year, RMxxx within five years and RMxxx thereafter.

Illustrative A4.6 [MFRS16.59(c)]

Restriction or covenants imposed by lease

Some of the lease contract for office equipment restrict the Group to sublease the leased assets in the respective contracts.

Illustrative A4.7 [MFRS16.59(d), B52]

Sales and leaseback

The Group sold one of its factories and leased back for 10 years. The Group has an option to re-purchase the factory at the end of contract term. The sales and leaseback transaction enabled the Group to manage its capital efficiently.

Good Practice

Companies are encouraged to present additional information in relation to the lease for better understanding instead of just quantitative disclosures. Qualitative disclosures are useful for users of financial statements to assess the nature of leasing activities of the Companies. As a matter of best practice, the disclosures should be presented in a "centralised" note (alongside the related leases note) to assist in understandability. If the information is provided in separate section in the financial statements, proper cross-referencing to the note on leases is necessary for ease of reading and reference.

B. Impairment of non-financial assets

During our desktop review of selected financial statements, we often ask for additional information and/or seek clarification from companies in relation to the issue of impairment of non-financial assets. This is mainly due to disclosures in the financial statements are not sufficiently clear or because information disclosed as per requirement under MFRS 136 *Impairment of Assets* have not been provided, although there were impairment losses recognised in the financial statements.

However, it is worth to note that response furnished by certain companies has provided clarity on the concern surrounding the impairment of non-financial assets reflected and disclosed in the financial statements. In this case, the FSRC encourages companies to sufficiently disclose information as per requirement under MFRS 136 in the financial statements in order to promote clarity to users of financial statements.

Common issues identified during our review include the following:

Observation B1

There was no disclosure of events and circumstances that led to the recognition or reversal of the impairment loss [MFRS 136.130(a)].

Most did not disclose specific events and circumstances that triggers indication of impairment and results of impairment assessment.

FSRC's analysis and conclusion

In improving their disclosure, companies should give clear explanation of the triggering event(s) for impairment and nature of changes in circumstances that lead to the recognition or reversal of an impairment loss.

Illustrative B1

In 20X1, the Group recognised an impairment loss of RMxxx represents the write down of certain plant and machinery in the manufacturing segment to the recoverable amount, as a result of temporary closure of one of the product lines. Regulatory restrictions were imposed by the Government on the manufacture of certain products.

Observation B2

There was no disclosure on whether the recoverable amount of the impaired asset is its fair value less cost to sell or its value in use.

Those with material impairment loss did not disclose the recoverable amount of the asset(s) or CGU(s) affected.

FSRC's analysis and conclusion

MFRS 136.130(e) requires an entity to disclose the recoverable amount of the asset (cash-generating unit) and whether the recoverable amount of the asset (cash-generating unit) is its fair value less costs of disposal or its value in use.

In improving their disclosure, companies should disclose the basis (i.e. fair value less costs of disposal or value in use) and consider providing additional information to explain the circumstances giving rise to a change in the basis for measuring recoverable amount of the asset(s) or CGU(s).

Illustrative B2

In 20X1, the impairment loss of RMxxx represented the write-down of certain property, plant and equipment in the manufacturing segment to the recoverable amount as a result of technological obsolescence. The recoverable amount is determined based on the higher of fair value less costs of disposal or value in use.

The recoverable amount of RMxxx as at 31 December 20X1 was based on value in use and was determined at the level of the CGU. The CGU consists of the production plant of a subsidiary. In determining value in use for the CGU, the cash flows were discounted at a rate of 12.4% on a pre-tax basis.

Observation B3

There was no clear disclosure in the accounting policy of basis used to determine the recoverable amount of the impaired assets, i.e. whether it is higher of fair value less costs of disposal or value in use. It was disclosed that the fair value less cost to sell approach is using the net assets position attributable to ordinary shareholder at the end of the financial year.

From response upon enquiry, the company's recoverable amount of investment in subsidiaries were determined through the adjusted net assets and has been disclosed under the key source of estimation uncertainty in the determination of impairment loss.

FSRC's analysis and conclusion

The FSRC is of the view that net assets position does not reflect the fair value less costs of disposal or value in use in accordance with requirement of MFRS 136.

The disclosure of key source of estimation uncertainty explained the estimation of the value in use of the asset and not the disclosure of accounting policy/basis for the assessment for impairment of asset. Clear disclosure on the accounting policy, basis for the assessment for impairment of asset as well as the basis of determining the recoverable amount are required.

Illustrative B3

Significant Accounting Policies – Impairment of Non-financial Assets

At the end of each reporting period, the carrying amount of non-financial assets (except for inventories, contract assets, deferred tax assets) are reviewed to determine whether there is an indication of impairment. If any indication exists, the asset's recoverable amount is estimated.

For the impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use or cash-generating units. For the purpose of goodwill impairment testing, cash-generating units to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes.

Impairment loss is recognised if the carrying amount of the assets or cash-generating unit exceeds its estimated recoverable amount.

The recoverable amount of an assets or cash-generating unit is the higher of its value in use and its fair value less costs of disposal. In assessing the value in use, the estimated future cash flows are discounted to their present value using pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset or cash-generating unit.

Observation B4

There was no disclosure of discount rate(s) used in the current estimate and previous estimate (if any) of value in use. [MFRS 136.130(g)]

FSRC's analysis and conclusion

Companies need to consider elements that shall be reflected in the calculation of value in use [MFRS 136.30], which can be reflected either as adjustments to the future cash flows or as adjustments to the discount rate [MFRS 136.31].

Discount rate shall be a pre-tax rate that reflects the current market assessments of the time value of money and the risks specific to the assets [MFRS136.55].

When an asset-specific rate is not directly available from the market, an entity uses surrogates to estimate the discount rate. Appendix A of MFRS 136 provides additional guidance on estimating the discount rate in such circumstances [MFRS136.57].

Illustrative

Refer to Illustrative B2

Good Practice

Companies should improve on the clarity of disclosure on the basis for assessment of impairment loss for non-financial assets. Additional information, including the key input used in determining the discount rates, may be required to clearly demonstrate how the recoverable amount is derived (based on higher of fair value less cost of disposal and value in use).

C. Financial Instruments - Financial Guarantee Contract

A financial guarantee contract (FGC) is a contract that requires issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

FGC can be in various forms, for example, a guarantee, some types of letter of credit, a credit default contract or insurance contract. The accounting treatment does not depend on their legal form.

In this report, we look at the common disclosure omissions and deficiencies relating to FGCs that are accounted for in accordance with MFRS 9 *Financial Instruments.*

Observation C1

FGCs were disclosed as contingent liabilities. There are no other disclosures relating to FGC as required by MFRS 7 *Financial Instruments*: *Disclosures* were noted.

In another observation, FGC has been disclosed pursuant to requirements of MFRS 7 and as contingent liabilities pursuant to MFRS 137 *Provisions, Contingent Liabilities and Contingent Assets* at the same time.

FSRC's analysis and conclusion

The FSRC wishes to highlight that FGCs are within the scope of MFRS 9* and are not contingent liabilities. As such reference to disclosure on contingent liabilities should not be made.

Paragraph 2 of MFRS 137 clarifies that MFRS 137 does not apply to financial instruments (including guarantees) that are within the scope of MFRS 9. Hence, the disclosure of FGC as contingencies is not appropriate.

In addition, MFRS 7.31 states that an entity shall disclose information that enables users of its financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed at the end of the reporting period.

The disclosures required by MFRS 7.33 to 42 focus on the risks that arise from financial instruments and how they have been managed. These risks typically include, but are not limited to, credit risk, liquidity risk and market risk.

MFRS7.B11C(c) states that for issued financial guarantee contracts, an entity discloses the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

BC57 states that the International Accounting Standards Board ("IASB") decided to require disclosure of a maturity analysis for financial liabilities showing the remaining earliest contractual maturities (MFRS7.39(a) and MFRS7.B11–B16). Liquidity risk, ie the risk that the entity will encounter difficulty in meeting commitments associated with financial liabilities, arises because of the possibility (which may often be remote) that the entity could be required to pay its liabilities earlier than expected. The IASB decided to require disclosure based on the earliest contractual maturity date because this disclosure shows a worst-case scenario.

In this context, the maximum exposure to credit risk is the maximum amount the entity could have to pay if the guarantee is called on and the disclosure represents the maximum amount that is required to be settled in the event of the triggering event.

*[*Companies may elect to apply either MFRS 9 or MFRS 4 Insurance Contracts to such financial guarantee contracts. The issuer may make that election contract by contract, but the election for each contract is irrevocable [MFRS 9.2(i)(e)]. In either case, there should be clear and consistent application of the accounting policy, accompanied with the respective disclosure requirements covered by MFRS 7 Financial Instruments: Disclosures or MFRS 4 accordingly.]*

Observation C2

The maximum exposure of FGC under credit risk was disclosed [MFRS7.36a)]. However, under liquidity risk, maturity analysis of FGC was not disclosed because it was stated that no default has occurred as at the reporting date.

FSRC's analysis and conclusion

The FSRC wishes to highlight that entity is exposed to liquidity risk, notwithstanding the low or no risk of default.

MFRS 7.39(a) requires an entity to disclose a maturity analysis for non-derivative financial liabilities (including issued financial guarantee contracts) that shows the remaining contractual maturities. BC58C states that contractual maturities are essential for an understanding of the timing of cash flows associated with the liabilities. Therefore, this information is useful to users of financial statements.

Illustrative C
Disclosures on FGC

Accounting policy

Financial guarantee contract is a contract that requires issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Financial guarantee contracts are recognised initially as a liability at fair value, net of transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, they are measured at higher of:

- the amount of the loss allowance; and
- the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance to the principles of MFRS 15, Revenue from Contracts with Customers.

Credit risk

The maximum exposure to credit risk in relation to the financial corporate guarantees given amounts to RM7,000,000 (20X0: RM8,000,000) as at the end of the reporting period representing the outstanding* banking facilities of the subsidiaries as at the end of financial year.

Liquidity risk

	Carrying amount RM'000	Contractual cash flows RM'000	Under 1 year*** RM'000	1-2 years*** RM'000	3-5 years*** RM'000	More than 5 years*** RM'000
Trade payables	5,000	5,000	5,000	-	-	-
Other payables	2,000	2,000	2,000	-	-	-
Term loans	16,900	18,000	3,000	5,000	5,000	5,000
Bank overdraft	2,000	2,000	2,000	-	-	-
	25,900	27,000	12,000	5,000	5,000	5,000
Financial guarantee contracts**	NIL	7,000	7,000	-	-	-

* *This is for illustrative purposes as the maximum exposure is dependent on the contractual terms entered into between the issuer and the bank. The maximum exposure to credit risk is the maximum amount the entity could have to pay if the guarantee is called on, which may be significantly greater than the amount recognised as a liability [MFRS 7.B10(c)].*

** *The disclosure represents the maximum amount that is required to be settled in the event of <triggering event>.*

*** *The time band is for illustrative purposes. It is to be based on the earliest period to which the FGC can be called upon.*

Good Practice

If an issuer of FGC has previously asserted explicitly that it regards such contracts as insurance contracts the issuer may elect to apply either MFRS 9 or MFRS 4 *Insurance Contracts* to such FGC. Companies should have proper processes in monitoring of loan and borrowings for which FGC have been provided, and the application of either MFRS 9 or MFRS 4 to those FGCs. In either case, there should be clear and consistent application of the accounting policy, accompanied with the respective disclosure requirements covered by MFRS 7 *Financial Instruments: Disclosures* or MFRS 4 accordingly.

[The disclosures in the illustrative above are for illustration purpose only. The information disclosed in the financial statements should be based on the facts and circumstances surrounding the transaction and in accordance with the accounting policies adopted by the company]

B Common Findings

B Common Findings

The following common findings on non–compliances with the applicable accounting standards were compiled from the reviews of the financial statements conducted by the FSRC from July 2020 to June 2021.

Table A: Common findings of FSRC for the Review Period from July 2020 to June 2021

No.	Areas for improvement	FSRC's findings
1	**Tax expense/(income) and/or deferred tax**	Non-disclosure of deductible temporary differences, unutilised tax losses and unutilised tax credits of which no deferred assets are being recognised [MFRS 112.81(e)]. In addition, one should also be wary of the need to disclose the **expiry date** (if any) of the aforementioned items. The disclosures should also be made available for comparative period.
2	**Investment in subsidiaries, associates and joint ventures**	Non-disclosure of the **principal place of business** (and country of incorporation, if different) of those investees [MFRS 127.17(b)(ii), MFRS 101.138(a)]. Typically, most entities disclosed the country of incorporation and not the principal place of business. MFRS requires the disclosure of principal place of business. Country of incorporation shall be disclosed only if different from principal place of business.
3	**Fair value measurements**	Inadequate or non-disclosure of **valuation technique(s) and inputs used** in the fair value measurement, for recurring and non-recurring fair value measurements categorised within Level 2 and Level 3 of the fair value hierarchy [MFRS13.93(d)].
4	**Risk - sensitivity analysis - equity effect**	Non-disclosure of **effect of equity** affected by change in relevant risk variable for each type of market risk to which the entity is exposed at the end of the reporting period [MFRS7.40(a)].
5	**Cash and cash equivalents**	Classification of money market funds as cash and cash equivalents [MFRS107.6] [MFRS107.7]. Deposits with **maturities exceeding three months classified as cash and cash equivalents** [MFRS107.7]. Although the three-months presumption is not a "bright line", it is pertinent and relevant to take into account this three-months presumption in considering whether the fixed deposit is held for the purpose of meeting short-term cash needs or for investment purposes. The longer the fixed deposits' original maturity period, the more likely the deposits are held for investment purposes.
6	**Contract assets/liabilities**	(i) Contract assets/liabilities are not financial assets/liabilities within the scope of MFRS 9 Financial Instruments [MFSR9.2.1(j)]. (ii) No explanation on how the **timing of satisfaction of** entity's **performance obligations** [MFRS15.119(a)] relates to the typical timing of payment [MFRS15.119(b)] and the effect that those factors have on the contract asset and the contract liability balances. The explanation provided may use qualitative information [MFRS15.117].
7	**Investment in associate or joint venture**	Non-disclosure of **nature of the entity's relationship** with material joint arrangement or associate [MFRS12.21(a)(ii)].

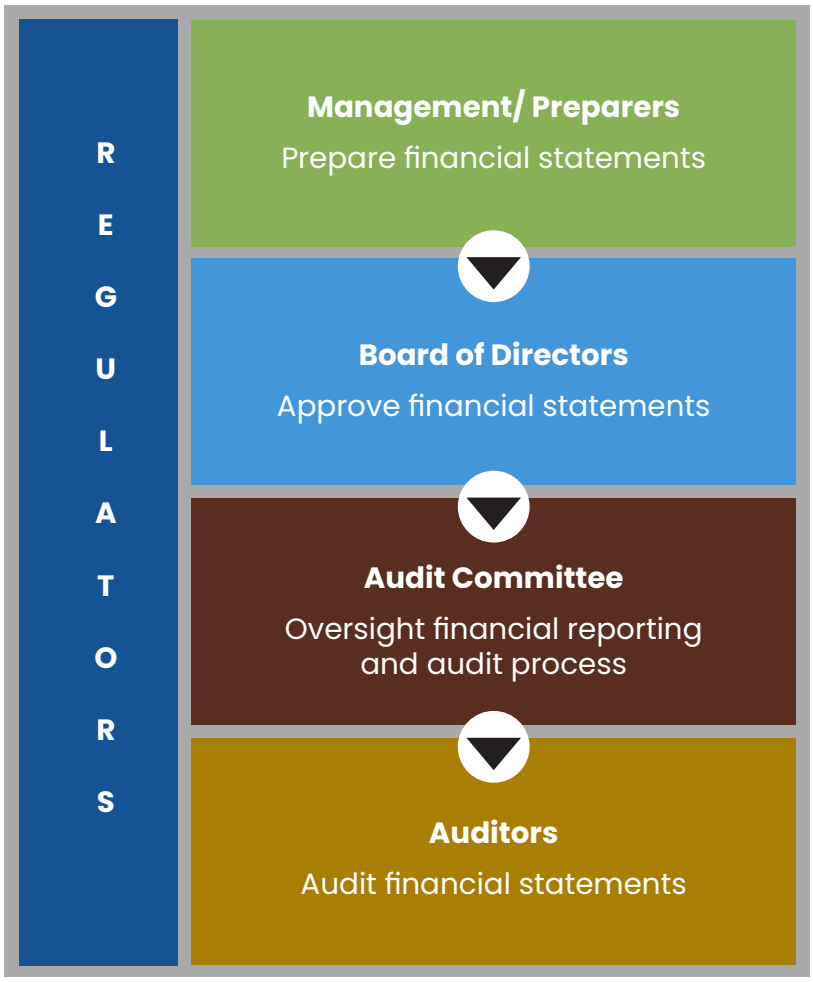
C Quality Financial Reporting and Responsibilities

C Quality Financial Reporting and Responsibilities

High quality financial statements disclosures are essential to investors to make sound investment decisions. Over the years, financial reporting requirements are increasingly complex which evolved with the ever-changing accounting and economic landscape. It is challenging for some companies to comply with the disclosure requirements and providing users with financial information that is meaningful and understandable. Hence, all participants in the financial reporting ecosystem, the preparers, management, board of directors, audit committee and auditors need to keep abreast with the latest development in the accounting profession as each participant has a role in driving the quality of financial reporting and to ensure high quality, relevant and timely financial information is provided to users.

Who does what?

"Who is responsible for the financial statements?" – a frequently asked question. It is always debatable whether the responsibility lies with the directors or the management. In fact, all participants play a key role in producing the desired high quality financial statements as illustrates below:



Management and Directors' duties over financial reporting

The management and directors are primarily responsible for a company's financial reporting. The management, often referred as the preparers of financial statements, is responsible for adopting appropriate accounting policies, maintaining effective internal control over financial reporting and certifying the accuracy of the financial statements.

The directors' responsibility on financial reporting arises from the duty of care to the company they are engaged with. Not all directors are expected to be accounting experts, however, they do have a responsibility overseeing the quality of financial reporting. The directors need to engage and seek explanation on the accounting policies adopted by the management, and have a key role in approving the assumptions, key areas of judgement and estimation applied by the entity in preparing the financial statements.

Ultimately, the directors are required to issue an opinion on whether the financial statements give a true and fair view of the financial position of the entity in accordance with applicable approved accounting standards and Companies Act 2016.

Management and Directors prepare financial statements; Audit Committee oversight role over the integrity of financial statements

Audit committees are appointed by the board of directors and required to act independently, to ensure that the interest of shareholders is protected in relation to financial reporting. Effective audit committee oversight on financial reporting process is essential for healthy and strong corporate governance.

The audit committee is responsible for overseeing and monitoring the financial reporting process, which includes monitoring the integrity of financial statements by reviewing the financial statements prepared by management and the significant judgements and estimates contained therein. To oversee the financial reporting process successfully, the audit committee should work with management, internal auditors and independent auditors.

Users/preparer's expectations on auditors

Whilst the responsibility of preparing financial statements lies with the management and directors, the auditors provide an independent opinion on the financial statements, which is a value-added assurance to investors. High quality audits serve to protect public interest and foster public trust in the capital markets.

The auditor has a responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements of a company as a whole are free of material misstatements. Auditors have to form an opinion as to whether the financial statements give a true and fair view of the company's affairs; and in accordance with the applicable approved accounting standards.

There is a common misconception that auditors are responsible for the preparation of financial statements of a company. The auditor may provide guidance to preparers in terms of the disclosure requirements in accordance with the applicable approved accounting standards and based on information provided by the management. However, management and directors should not rely on the auditor in the preparation of financial statements. Doing so will undermine the objective of an independent audit. The auditor's responsibility is confined to the expression of audit opinion on the financial statements.

Role of the Regulators

Regulators play an important role in the financial reporting ecosystem. They oversee the quality of financial reporting by undertaking inspections to ensure the consistency of information reported and enforce compliance with relevant statutory requirements. This in turn ensure that the information exchanged between investors and organisations is transparent and sound. It is apparent that regulators have an impact on the quality of financial reporting.

Companies Act Requirements

The FSRC wishes to reiterate that the responsibility for the preparation of financial statements lies with the company's management and Board of Directors. Companies Act, 2016 spells out the responsibilities of the relevant participants involved in the preparation of financial statements of an organisation.

COMPANIES ACT 2016	
Duty of care	**Duties and responsibilities of directors** **Section 213(2)** A director of a company shall exercise reasonable care, skill and diligence with: (a) the knowledge, skill and experience which may reasonably be expected of a director having the same responsibility; and (b) any additional knowledge, skill and experience which the director in fact has.
Keeping accounting records	**Accounts to be kept** **Section 245(1)** The directors and managers of a company shall: (a) cause to be kept the accounting and other records to sufficiently explain the transactions and financial position of the company and enable true and fair profit and loss accounts and balance sheets and any documents required to be attached thereto to be prepared; and (b) cause the accounting and other records to be kept in a manner as to enable the accounting and other records to be conveniently and properly audited.
Preparation of financial statements	**Directors shall prepare financial statements** **Section 248(1)** The directors of every company shall prepare financial statements: (a) within eighteen months from the date of its incorporation; and (b) subsequently, within six months of its financial year end.

Compliance with approved accounting standards

Financial statements in accordance with approved accounting standards

Section 244(2)

The directors of a company shall ensure that the financial statements of the company and, if the company is a holding company for which consolidated financial statements are required, the consolidated financial statements of the company are made out in accordance with the applicable approved accounting standards and shall:

(a) in the case of a public company, be circulated to its members and laid before the company at its annual general meeting; or

(b) in the case of private company, be circulated to its members or laid before the company at a meeting of members.

Financial Statements to be approved by the Board

Approval of financial statements

Section 251(1)

Financial statements shall be:

(a) approved by the Board; and

(b) accompanied with a statutory declaration by a director or where the director is not primarily responsible for the financial management of the company, by the person responsible in setting forth his opinion as to the correctness or otherwise of the financial statements and where applicable, the consolidated financial statements.

Section 251(2)

The directors shall make a statement in accordance with the resolution of the Board stating whether in their opinion the financial statements or where applicable the consolidated financial statements is or are drawn up, in accordance with the applicable accounting standards, to give a true and fair view of the financial position and financial performance of the company and of the group.

Audit of financial statements

Section 248(2)

The financial statements referred to in subsection (1) shall be duly audited before the financial statements are sent to every member under section 257 or, in the case of a public company, sent to every member under section 257 and laid before an annual general meeting under section 340.

Duties of auditors

Power and duties of auditors

Section 266(1)

Every auditor of a company shall report to the members on the financial statements and on the company's accounting and other records relating to those financial statements are prepared shall also report to the members on the consolidated financial statements, and the report shall be:

(a) in the case of a public company, laid before the company at its annual general meeting; or

(b) in the case of a private company-
   (i) Circulate to its members; or
   (ii) Laid before the company at a meeting of members.

Section 266(2)

An auditor shall, in a report under this section, state-

(a) Whether the financial statements/consolidated financial statements are in his opinion properly drawn up-
   (i) So as to give a true and fair view of the matters to be dealt with in the financial statement/consolidated financial statements;
   (ii) In accordance with this Act so as to give a true and fair view of the company's affairs; and
   (iii) In accordance with the applicable approved accounting standards;

(b) If in his opinion the financial statements/consolidated financial statements, have not been drawn up in accordance with a particular applicable approved accounting standard-
   (i) Whether in his opinion the financial statements or consolidated financial statements would, if drawn up in accordance with that approved accounting standard, have given a true and fair view of the matters to be dealt with in the financial statements or consolidated financial statements;
   (ii) If in his opinion the financial statements or consolidated financial statements would not, if so drawn up, have given a true and fair view of those matters, his reasons for holding that opinion;
   (iii) If the directors have given the particulars of the quantified financial effect, his opinion concerning the particulars; and
   (iv) If neither subparagraph (ii) nor (iii) applies, the particulars of the quantified financial effect on the financial statements or consolidated financial statements of the failure to so draw up the same.

D Moving Forward

D Moving Forward

In a perfect world, investors would have full confidence in companies' financial reporting. However, this may not be the case in today's business world with ever-changing economic landscape coupled with uncertainties in business while the COVID-19 pandemic continues. In this unprecedented time, reliable financial information and transparency in financial reporting is vital to ensure continuing trust from investors.

Compliance with financial reporting standards should not be seen as a burden to the reporting entities. Instead, it is the fundamental principle for preparation of high-quality financial statements. Good financial reporting practices will assist relevant stakeholders to have better understanding of the entity's results, circumstances of the entity's operations and how the effects of the COVID-19 pandemic are mitigated by the entity's actions. In light of the current fluid environment, such information are particularly useful for relevant stakeholders to assess the entity's operations.

In this context, all participants in the financial reporting ecosystem should be guided by relevant financial reporting standards in line with their distinctive role and responsibility. The FSRC wishes to reiterate that the responsibility of preparation of financial statements lies with the management and board of directors of a company. With good corporate governance and oversight of financial reporting function, all participants in the financial reporting ecosystem, the preparers, management, board of directors, audit committee and auditors should work together and strive to uphold the quality of financial statements.

In this regard, the FSRC will continue to focus on its entrusted responsibility to monitor the quality of financial statements and sharing with members on good financial reporting practices through publication. The previous FSRC's publications can be accessed via the Institute's website (https://www.mia.org.my/v2/surveillance/fsr/findings.aspx). Members are also able to seek technical advice from the Institute's Professional Practices and Technical division by sending the technical enquiries via the Institute's Members Services Portal (https://member.mia.org.my/#/enquiry). The Institute offers wide range of professional development courses to support members' continuing learning (https://pd.mia.org.my/dashboard).

In monitoring the compliance of financial reporting, FSRC's actions arising from the review of financial statements is guided by its penalty tariff. Regulatory action is taken against members depend on the severity of the non-compliance(s) on the disclosures of financial statements. As one of the surveillance functions, FSRC continues to support the Institute's strategy objective on regulating and developing the audit profession in Malaysia, which in turn achieves the Institute's distinctive vision for nation building.

Appendix - About FSRC

Appendix - About FSRC

FINANCIAL STATEMENTS REVIEW COMMITTEE

Objective & Scope

The Financial Statements Review (FSR) function is one of the surveillance functions of the Institute. The primary objective of FSR is to monitor and regulate the practice and strengthen the credibility of the accountancy profession in Malaysia.

The Financial Statements Review Committee (FSRC or the Committee) of the Institute was set up with the aim of upholding the quality of financial reporting of public interest entities. The Committee reviews audited financial statements and auditors reports that are prepared by or are the responsibility of members of the Institute, for the purpose of determining compliance with applicable approved accounting standards and approved auditing standards in Malaysia and other statutory requirements.

The FSRC assess the quality of financial reporting through:

Random Reviews

Review financial statements of companies incorporated under the Companies Act, 2016 that are prepared by or within the responsibility of members of MIA. This includes public listed companies and public interest entities.

Hot Pursuit

Public Interest - Review financial statements of companies on matters of public interest which have been reported in the financial press and/or in the press releases issued by the regulators/other relevant parties. Issues may relate to financial reporting of companies or conduct of the auditors.

Referral - Review cases referred by other Regulators such as Bursa Malaysia, Securities Commission Malaysia, Audit Oversight Board or Suruhanjaya Syarikat Malaysia.

Enhance Quality of Financial Reporting

The FSRC seeks to enhance quality and promote excellence in financial reporting by sharing on good financial reporting practices based on common findings identified during the review process.

How FSRC conducts the reviews

Review process of FSRC

Desktop review

- Conducts desktop reviews of the selected financial statements.
- Focuses on compliance with approved accounting and auditing standards.

Enquiry letters

- Address enquiries to the person responsible for the financial management of the entity (Preparer) when a desktop review of financial statements indicates potential significant non-compliance with approved accounting standards.
- Consider appropriateness of audit opinion issued by auditor if significant issues are identified. Enquiries are made to the auditors where necessary.

Replies

- Preparer/auditor to provide explanation and justification to the enquiries within the stipulated deadline. All explanations are received in writing.
- Preparer/auditor to address all enquiries with consistent facts and explanation.
- Preparer/auditor to be clear and transparent in explaining the entity's circumstances and the substance of transactions.

FSRC's Deliberation

- Deliberates replies received.
- Focuses on compliance with applicable approved accounting standards, approved auditing standards and other statutory requirements, taking into consideration both quantitative and qualitative factors.
- Repeats enquiry process until a decision is reached on each review.

Closure

- Concludes the case based on the degree of non-compliance and determine the penalty tariff accordingly.

Regulatory Outcome on The Reviews Conducted

All reviews are deliberated by FRSC and instances of non-compliance to applicable approved accounting standards are assessed by taking into consideration both quantitative and qualitative factors. Where judgement is required in the application of accounting standards, preparer/ auditor need to demonstrate that they have made the judgement fairly.

In concluding the reviews, FSRC applies the following penalty tariff, depending on the severity and degree of non-compliances:

Penalty Tariff		
Category 1	**Category 2**	**Category 3**
• **Minimum Action -** house keeping issues which require tidying up financial statements	• **Warning Letter -** substantial numbers of non-compliance. The financial statements will be under surveillance for up to 2 consecutive years	• **Disciplinary Action -** major non-compliances. Members could be referred to Investigation Committee of the Institute and/or other regulatory bodies. The financial statements will be under surveillance for up to 4 consecutive years

Category 1 prescribes the minimum action. This category relates to housekeeping issues, which require tidying up of the financial statements. It requires members who are responsible for the preparation of the financial statements to take necessary action on the financial statements and members who are responsible for reporting on them to be informed of the action.

Category 2 applies when there are substantial numbers of non-compliances with disclosure requirements of the applicable approved accounting standards. It requires members who are responsible for the preparation of the financial statements or for reporting on the financial statements to take the necessary corrective action. Members will be given a warning letter and will be informed that the financial statements of the company could be put under surveillance for up to two (2) consecutive years.

Category 3 applies when there are major non-compliances with the requirements of the applicable approved accounting standards and auditing standards involving material reporting discrepancies and/or deficiencies, caused by the member's failure to discharge his/her professional responsibilities with diligence and due care and/or the company's/firm's weaknesses in the system of quality control.

Under category 3, action to be taken on members, who are responsible for the financial reporting and preparation of the financial statements, could include referring the member(s) to the Investigation Committee or Practice Review Committee of the Institute and/or other regulatory bodies for appropriate action or serving the members with warning letters or reprimands, or other appropriate measures. The financial statements of the company concerned could be put under surveillance for up to four (4) consecutive years.

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