

FOR INFORMATION ONLY

COMMON FINDINGS OF FINANCIAL STATEMENTS REVIEW COMMITTEE

Financial reporting provides useful information about the financial position of the company to users of financial statements and facilitates informed decision making. Financial statements should be of sufficient quality to meet the needs of investors.

The Financial Statement Review Committee (FSRC) is entrusted with the responsibility to monitor the quality of financial statements for the purpose of determining compliance with statutory and other requirements, approved accounting standards and approved auditing standards; and generally accepted accounting and auditing standards and practices.

The following common findings on non-compliances with applicable accounting standards and approved standards on auditing were compiled from the reviews of the financial statements conducted by the FSRC from July 2005 to June 2006. The financial statements of the public listed companies, non-listed companies and government-linked corporations were reviewed against the Malaysian Accounting Standards Board (MASB) standards issued up to 31 December 2005. Financial statements that are prepared for the financial periods beginning on or after 1 January 2006 will have to comply with either Financial Reporting Standards (FRS) or Private Entity Reporting Standards (PERS) issued by MASB.

COMMON FINDINGS	RELEVANT STANDARDS/STATUTES AND RECOMMENDED PRACTICES
<p>1. Reclassification of Comparative Figures</p> <ul style="list-style-type: none">• Reclassification of comparative figures was made, without disclosure of their reason and nature of the reclassifications.	<p>FRS 101₂₀₀₄ (MASB 1), Presentation of Financial Statements, paragraph 40 requires that when the presentation or classification of items in the financial statements is amended, comparative amounts should be reclassified, unless it is impractical to do so, to ensure comparability with the current period, and the nature, amount and reason for, any reclassification should be disclosed.</p>

<p>2. Lack of clarity on the presentation of the newer accounting policies</p> <ul style="list-style-type: none"> Deferred taxation - the policy adopted by the company on the recognition of deferred tax asset on deductible temporary differences, unused tax losses and unused tax credits were not clearly made. 	<p>FRS 112₂₀₀₄ (MASB 25), Income Taxes, requires that a deferred tax asset should be recognised for :</p> <p>Paragraph 26 - all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised, unless the deferred tax asset arises from :</p> <ul style="list-style-type: none"> Negative goodwill which is treated as deferred income ;or The initial recognition of an asset or liability in a transaction which is not a business combination; and at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss) <p>Paragraph 37 – the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised.</p>
<ul style="list-style-type: none"> Employee Benefits – Inadequate disclosure of the employee benefits information on: <ul style="list-style-type: none"> i) The recognition policy for short-term employee benefits ii) Defined contribution plan i.e. contribution to the statutory pension scheme iii) Defined contribution plan expense 	<p>FRS 119₂₀₀₄ (MASB 29), Employee Benefits, Paragraph 12, 45 and 47 provides the requirement for recognizing and measuring the respective employee benefits.</p> <p>Paragraph 12(a) & (b) requires an enterprise to recognise the expected cost of short-term employee benefits in the form of compensated absences under paragraph 11 as follows:</p> <ul style="list-style-type: none"> In the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and

	<ul style="list-style-type: none"> • In the case of non-accumulating compensated absences, when the absences occur. <p>Paragraph 45 requires that when an employee has rendered service to an enterprise during a period, the enterprise should recognise the contribution payable to a defined contribution plan in exchange for that service:</p> <ul style="list-style-type: none"> • as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the balance sheet date, an enterprise should recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and • as an expense, unless another MASB Standard requires or permits the inclusion of the contribution in the cost of an asset (see, for example, MASB 2, Inventories, and MASB 15, Property, Plant and Equipment). <p>Paragraph 47 requires an enterprise to disclose the amount recognised as an expense for defined contribution plans.</p>
<p>3. Inadequate disclosures about the company plans to address going concern issues</p> <ul style="list-style-type: none"> • The financial statements have not adequately describe the material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern. In addition, management's plans to deal 	<p>FRS 101₂₀₀₄ (MASB 1), Presentation of Financial Statements, Paragraph 23 requires the management, when it is aware, in making its assessment whether the entity's ability to continue as a going concern, is aware of material uncertainties relating to events or conditions that may cast significant doubt upon the entity's ability</p>

<p>with such events and conditions have not been adequately disclosed.</p> <p>Examples of events and conditions are net liability or net current liability position, negative operating cash flows and no indication of financial support by lenders</p>	<p>to continue as a going concern, those uncertainties should be disclosed</p>
<ul style="list-style-type: none"> The auditor's report does not make specific reference to the material uncertainties that may cast significant doubt about the entity's ability to continue as a going concern and failed to render the appropriate opinion on the financial statements 	<p>AI 570, Going Concern provides guidance on auditor's responsibility with respect to going concern assumption used in the preparation of the financial statements.</p> <p>Paragraph 9 highlights the auditor's responsibility to consider the appropriateness of management's use of the going concern assumption in the preparation of the financial statements, and consider whether there are material uncertainties about the entity's ability to continue as a going concern that need to be disclosed in the financial statements.</p> <p>Paragraph 26 states when events or conditions have been identified which may cast significant doubt on the entity's ability to continue as a going concern, the auditor should:</p> <ul style="list-style-type: none"> (a) review management's plans for future actions based on its going concern assessment; (b) gather sufficient appropriate audit evidence to confirm or dispel whether or not a material uncertainty exists through carrying out procedures considered necessary, including considering the effect of any plans of management and other mitigating factors; and (c) seek written representations from management regarding its plans for future action.

	<p>Paragraph 32 states if the use of the going concern assumption is appropriate but a material uncertainty exists, the auditor considers whether the financial statements:</p> <p>(a) adequately describe the principal events or conditions that give rise to the significant doubt on the entity's ability to continue in operation and management's plans to deal with these events or conditions.</p> <p>(b) state clearly that there is a material uncertainty related to events or conditions which may cast significant doubt on the entity's ability to continue as a going concern and, therefore, that it may be unable to realize its assets and discharge its liabilities in the normal course of business.</p> <p>Paragraph 34 states if adequate disclosure is not made in the financial statements, the auditor should express a qualified or adverse opinion. The report should include specific reference to the fact that there is a material uncertainty that may cast significant doubt about the entity's ability to continue as a going concern.</p>
<p>4. Inventories</p> <ul style="list-style-type: none"> Inventories were not segregated into cost and Net Realisable Value (NRV). 	<p>FRS 102₂₀₀₄ (MASB 2), Inventories, Paragraph 11 requires that inventories should be measured at the lower of cost and net realisable value.</p> <p>The financial statement should disclose the total carrying amount of inventories and the carrying amount in classifications appropriate to the enterprise (FRS 102.37(b)); and the carrying amount of inventories carried at net realisable value (FRS 102.37(c)).</p> <p>(Please note that under FRS 102, the requirement</p>

	to disclose separately those inventory held at cost and those held at NRV is removed)
<p>5. Disclosure of material Expenses</p> <ul style="list-style-type: none"> Expense items of material in amount were separately classified from other ordinary activities as exceptional items. These items were not disclosed as part of operating items (either by nature or function of expenses) in arriving at profit or loss from ordinary activities. 	<p>FRS 108₂₀₀₄ (MASB 3), Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies, Paragraph 12 explains that virtually all items of income and expense included in the determination of net profit or loss for the period arise in the course of the ordinary activities of the enterprise.</p> <p>Nevertheless, Paragraph 18 requires that when items of income and expense within the profit or loss from ordinary activities are of such size, nature and incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately.</p>
<ul style="list-style-type: none"> Entity that classify expenses by function did not provide adequate additional information on the nature of expenses 	<p>FRS 101₂₀₀₄ (MASB 1) requires enterprises classifying expenses by function should disclose additional information on the nature of expenses, including depreciation and amortisation expenses and staff costs.</p>
<p>6. Cash Flow Statements</p> <p>Classification by activity provides information that allows users to assess the impact of those activities on the financial position of the entity and the amount of its cash and cash equivalents.</p> <ul style="list-style-type: none"> Wrong classification was reported on cash flow items of operating, financing and investing activities (e.g. non-trade balances with inter-company included 	<p>FRS 107₂₀₀₄ (MASB 5), Cash Flow Statements requires the cash flow statement to report cash flow during the period classified by operating, investing and financing activities.</p>

<p>under operating activities)</p>	
<ul style="list-style-type: none"> • Inclusion of non-cash transactions in the cash flow statement <p>Many investing and financing activities do have a direct impact on current cash flows although they do affect the capital and asset structure of an enterprise. Several companies include the acquisition of assets by means of finance leases in the cash flow statement</p>	<p>FRS 107₂₀₀₄ (MASB 5), Cash Flow Statements, Paragraph 43 states that investing and financing transactions that do not require the use of cash and cash equivalents should be excluded from the cash flow statement.</p>
<p>7. The Effect of Changes in Foreign Exchange Rates</p> <ul style="list-style-type: none"> • No information whether foreign exchange gains/losses are realised or unrealised. 	<p>FRS 121₂₀₀₄ (MASB 6), The Effect of Changes in Foreign Exchange Rates, Paragraph 42(i) & (ii) requires an enterprise to disclose exchange differences included in the income in respect of:</p> <ul style="list-style-type: none"> • gain and losses realised in the period from currency transactions: and • unrealised gain and losses from the foreign exchange translation
<p>8. Lease</p> <ul style="list-style-type: none"> • Non-disclosure of reconciliation between total of minimum lease payments at the balance sheet date and their present value 	<p>FRS 117₂₀₀₄ (MASB 10) Leases, Paragraph 26(b) requires that the total of minimum lease payments and their present value should be presented as follows:</p> <ul style="list-style-type: none"> i) not later than 1 year; ii) later than 1 year and not later than 5 years; iii) later than 5 years
<p>9. Consolidated Financial Statements and Investments in Subsidiaries</p> <ul style="list-style-type: none"> • Application of acquisition method on 	<p>FRS 127₂₀₀₄ (MASB 11), Consolidated Financial</p>

<p>changes in stakes / composition of the group which are settled by other than cash consideration</p>	<p>Statements and Accounting for Investments in Subsidiaries, Paragraph 41 requires that all other changes in stakes and changes in composition of a group which do not meet the standards in paragraph 37 or paragraph 39 should be treated as equity transactions between the group and its majority and minority shareholders.</p> <p>Any difference between the group's share of net assets before and after the change, and any consideration received or paid, should be adjusted to or against group reserves.</p>
<p>10. Property, Plant and Equipment</p> <ul style="list-style-type: none"> Accounting policy do not clearly state the adjustment for impairment losses 	<p>FRS 116₂₀₀₄ (MASB 15), Property, Plant and Equipment, Paragraph 33 and 34 requires that an item of property, plant and equipment should be carried at its cost/valuation less any accumulated depreciation and any accumulated impairment losses.</p>
<ul style="list-style-type: none"> Non-disclosure of the company's policy on the adoption of the transitional provision of IAS 16 (Revised): Property, Plant and Equipment <p>FRS 116₂₀₀₄ (MASB 15) (which supersedes IAS 16) would require revaluations to be carried out at regular intervals</p>	<p>The transitional provision is available only on the first application of the MASB Approved Accounting Standard IAS 16 (Revised): Property, Plant and Equipment which is effective for periods ending on or after 1 September 1998. The transitional provision will remain in force until and unless the enterprise chooses to adopt a revaluation policy in place of a cost policy.</p>
<p>11. Segment Reporting</p> <ul style="list-style-type: none"> Non-disclosure or inadequate disclosure of accounting policy on segment reporting. Entities disclosed segmental information reporting but did not disclose the accounting policy for segment reporting. It is common that 	<p>FRS 114₂₀₀₄ (MASB 22), Segment Reporting, Paragraph 26 requires that policies relate specifically to segment reporting, such as identification of segments, method of pricing inter-segment transfers, and basis for allocating revenues and expenses to segments to be</p>

<p>method of pricing inter segment transfers is omitted.</p>	<p>disclosed. Paragraph 76 of the standard requires that the basis of pricing inter-segment transfers and any change therein shall be disclosed in the financial statements.</p>
<p>12. Financial Instruments - Fair Value Disclosures</p> <ul style="list-style-type: none"> • Non-disclosure of fair values of the financial guarantee (e.g. on banking and credit facilities of subsidiaries) • Non-disclosure of fair value of non-current financial assets/ liabilities • Non-disclosure of fair value of the amount due by/to subsidiary companies and associated companies due to a lack of fixed repayment terms and inability to estimate fair value without incurring costs • Non-disclosure of the method and assumptions used to estimate fair value. 	<p>FRS 132₂₀₀₄ (MASB 24), Financial Instruments: Disclosure and Presentation, paragraph 86 requires that, for each class of financial asset and financial liability, both recognised and unrecognised, an enterprise should disclosed information about fair value.</p> <p>When it is not practicable within constraints of timeliness or cost to determine the fair value of a financial asset or a financial liability with sufficient reliability, that fact should be disclosed together with information about the principal characteristics of the underlying financial instrument that are pertinent to its fair value.</p> <p>Paragraph 88 clarifies that the fair value of a financial asset or financial liability may be determined by one of several generally accepted methods.</p> <p>Disclosure of fair value information includes disclosure of the method adopted and any significant assumptions made in its application.</p> <p>It shall be noted that financial guarantees will have to be fair valued and recognised on the balance sheet when FRS 139 on Financial Instruments: Recognition and Measurement comes into effect and is applied to measure the financial guarantees.</p>

<p>13. Financial Instrument – Other disclosures</p> <ul style="list-style-type: none"> • Non-disclosure of significant concentration of credit risk 	<p>FRS 132₂₀₀₄ (MASB 24), Financial Instruments: Disclosure and Presentation, Paragraph 74(b) requires that for each class of financial asset, both recognised and unrecognised, an enterprise should disclose information about its exposure to credit risk including significant concentration of credit risk.</p>
<ul style="list-style-type: none"> • Non-disclosure of significant terms of receivables/payables 	<p>Paragraph 55(a) of FRS 132 requires an enterprise to disclose the information about the extent and nature of the financial instruments, including significant terms and conditions that may affect the amount, timing and certainty of future cash flows.</p>
<p>14. Disclosures on taxation</p> <ul style="list-style-type: none"> • Component of tax expense (income) items as required by the standard were not presented or disclosed. Certain components that are applicable to the company were not disclosed • Tax reconciliation was not clearly/ correctly presented. Items which were included in the reconciliation do not explain the relationship between the tax expense (income) and accounting profit 	<p>FRS 112₂₀₀₄ (MASB 25), Income Taxes, Paragraph 78 prescribe the components of tax expense (income).</p> <p>Paragraph 79(c) requires an enterprise to disclose separately the explanation of the relationship between tax expense (income) and accounting profit in either or both of the following forms:</p> <ul style="list-style-type: none"> • a numerical reconciliation between tax expense (income) and the product of accounting profit multiplied by the applicable tax rate(s), disclosing also the basis on which the applicable tax rate(s) is (are) computed; or • a numerical reconciliation between the average effective tax rate and the applicable tax rate, disclosing also the basis on which

<ul style="list-style-type: none"> • Inadequate disclosures on deferred tax assets and liabilities in respect of each type of temporary differences, unused tax losses and unused tax credits • Disclosure of the nature of the evidence supporting the recognition of deferred tax assets 	<p>the applicable tax rate is computed.</p> <p>Paragraph 79(f) requires an enterprise to disclose separately in respect of each type of temporary differences, unused tax losses and unused tax credits:</p> <ul style="list-style-type: none"> • the amount of the deferred tax assets and liabilities recognised in the balance sheet for each period presented; • the amount of the deferred tax income or expense recognised in the income statement, if this is not apparent from the changes in the amounts recognised in the balance sheet <p>Paragraph 80 requires an enterprise to disclose the amount of a deferred tax asset and the nature of the evidence supporting its recognition, when:</p> <ul style="list-style-type: none"> • the utilisation of the deferred tax asset is dependent on future taxable profits in excess of the profits arising from the reversal of existing taxable temporary differences; and • the enterprise has suffered a loss in either the current or preceding period in the tax jurisdiction to which the deferred tax asset relates
<p>15. Quality of financial statements</p> <p>Common errors found in the financial statements:</p> <ul style="list-style-type: none"> • Wrong cross-referencing from the financial statements to the notes to the financial statements • Pagination error made in the Directors' Statement and Auditor's Report • Typographical errors in the description of line items and figures 	

<ul style="list-style-type: none"> • Figures do not cast or tally to the related notes <p>Presentation errors provide misleading information to the user of financial statements. Errors are fundamental and the preparer of the financial statements need to practice extra care to safeguard the quality of the financial statements.</p> <p>The above findings indicated that some companies were not well organised in the final stages of the reporting process.</p>	
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Whilst the FSRC continues to inform and educate members on good presentation and disclosure practices, its actions will be guided by its penalty tariff that depends on the severity of non-compliances. Category 1 bears minimum action requiring 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 will be informed of the action; whilst Category 3 will carry the most severe action on members who are responsible for their preparation or for reporting on the financial statements including referring the said members to the Investigation Committee of MIA and/or other regulatory bodies for appropriate action by the investigative body.

The financial statements are the responsibility of the company's directors. However, it is in the best interest of the companies and capital market in general, that the directors and auditors, in line with their responsibilities improve the quality of the financial reporting – to give investors clear, comprehensive and credible information and to contribute to the overall integrity of the securities market.