MALAYSIAN INSTITUTE OF ACCOUNTANTS

The Enhanced Auditors' Report

Questions and Answers

May 2017

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The Enhanced Auditors' Report

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From 2017 onwards, users of audited financial statements for financial periods ended on or after 15 December 2016, will see an enhanced format of the independent auditors' reports that:

(a) Provides further clarity and insights into the audit of the financial statements of an entity; and

(b) Better describes what an audit is and what the auditors do.

The most significant change is the inclusion of a section on "Key audit matters" in the audit report of listed entities. Key audit matters (KAM) which were previously confined to communication between the auditors, management and those charged with governance (TCWG) will now have to be appropriately disclosed in the enhanced audit report. TCWG refers to the Board of Directors of an entity.

This publication aims to address some of the common questions relating to the enhanced auditors' report.

Introduction

1 What is an audit of financial statements?

An audit is an examination of the financial statements of an entity by a party independent of that entity. The purpose of an audit is to form a view on whether the information presented in the financial statements of an entity, taken as a whole, reflects fairly the financial performance for a period and the financial position at a given date.

At the end of the audit, the auditor issues an auditors' report giving an opinion on the financial statements drawn from work performed and outlining the key aspects of what the auditor has done.

2 What does an audit not do?

An audit does not guarantee that:

(a) All occurrences of fraud are identified or reported;

(b) All weaknesses in internal controls in an entity have been identified and resolved;

(c) An entity is solvent and able to continue its business indefinitely; and

(d) All financial figures are accurate.

This is because it will not be practical for an auditor to test every single transaction of the entity and judgement will need to be applied in auditing estimates and assumptions by the directors. Accordingly, audits can only provide reasonable assurance which is a high level of assurance but not a guarantee over the financial statements.

Enhanced Auditors' Report

3 What are the key changes in the enhanced auditors' report?

	APPLICABLE TO LISTED ENTITIES	APPLICABLE TO ALL ENTITIES
Restructuring of the audit report for readability – in particular, the **Opinion section** is required to be **presented first**, followed by the Basis for Opinion section	✓	✓
Communication of KAM	✓	**Optional**
Going concern (GC): • Description of the directors' and auditors' responsibilities for GC • Separate section on material uncertainty, where exists	✓	✓
Other information (OI): • Description of the directors' and auditors' responsibilities for OI • Status of the auditors' consideration of OI at the date of the auditors' report	✓ with additional reporting for listed entities	✓
Positive **statement about the auditors' independence** and fulfilment of other **ethical responsibilities**	✓	✓
Enhanced descriptions of the auditors' responsibilities and key features of an audit	✓ with additional descriptions for listed entities	✓

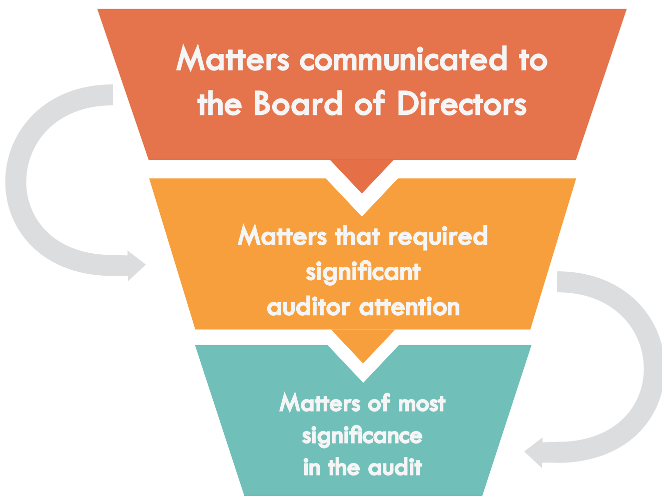
4 What are KAM?

KAM provide information to users of the financial statements on areas the auditor spent the most effort in the audit of the financial statements of the current period. Areas where the auditor spent the most effort are often difficult and complex areas in the financial statements and areas involving the use of significant judgement by the directors.

Understanding the critical areas the auditor focused on doing the audit should help users in understanding the financial statements better.

KAM are selected from matters communicated by the auditors to the Board of Directors. From these matters, the auditor selects those matters that required significant auditor attention in performing the audit. Finally, the auditor selects those matters of most significance in the audit.

The diagram below illustrates an overview of the decision making framework:



The description of each key audit matter will be tailored to the entity and will:

(a) Explain why the matter was considered to be one of most significance in the audit;
(b) Describe how the matter was addressed in the audit; and
(c) Provide a reference to where this matter was disclosed in the financial statements.

5

Is the auditor providing a separate opinion when communicating KAM?

The Opinion section sets out the auditors' opinion on the financial statements as a whole whereas the KAM section provides additional information on those matters that were of most significance in the audit of the financial statements. Accordingly, the auditor does not provide a separate opinion on KAM.

6

Are KAM audit qualifications?

As explained, KAM are matters that were most significant in the audit of an entity's financial statements. However, these matters should not be seen as there is something wrong with the financial statements or areas potentially giving rise to an audit qualification and are indicative of problems or weaknesses in the entity's internal control.

7

How should investors leverage on KAM to ask pertinent questions to directors and the auditors?

Investors should leverage on KAM in understanding the financial statements and to gain more insights into the entity. For example, if there is a key audit matter in respect of an acquisition of a business during the year:

(a) Possible questions to ask the directors include:
  1. What was the intention of the acquisition?
  2. On what basis was the purchase price accepted?

(b) Possible questions to ask the auditor include:
  1. How did the auditor obtain comfort that the valuation of intangible assets was appropriate?
  2. Was an external expert engaged for the valuation process?

8 What are directors' responsibilities in relation to KAM?

It is important to understand that the auditors do not take responsibility for the financial statements on which they form an opinion.

The responsibility for the financial statements remains with the directors of an entity. Accordingly, directors should communicate relevant information to users about the entity including providing adequate disclosures in accordance with the applicable financial reporting framework.

With KAM, the directors are expected to ensure that appropriate disclosures in the financial statements have been made and to comment, when appropriate, their assessment of the KAM.

9 Will the KAM be the same for entities operating in similar industries?

An audit is carried out on a risk based approach. Whilst entities may operate in similar industries, there still may be differences in controls and operating model and processes.

Accordingly, KAM for entities operating in similar industries may differ.

10 Are there circumstances when the auditor determine there are no KAM to report?

In certain limited circumstances, the auditor may determine that there are no KAM because there are no matters that required significant auditor attention. For example, a listed entity that has very limited operations may have no KAM in its audit report.

11

How will the auditors' report address going concern (GC)?

It is important to understand that the responsibility for assessing an entity's ability to continue as a GC remains with the directors of the entity.

The auditors' responsibilities are to determine the appropriateness of the directors' use of the GC basis of accounting and to determine if there are any GC issues that should be highlighted.

The auditors' communication on GC will depend on the facts and circumstances of the entity as follows:

<table>
<tr><th colspan="2">FACTS AND CIRCUMSTANCES</th><th>COMMUNICATION IN THE AUDITORS' REPORT</th></tr>
<tr><td colspan="2">The auditor concludes that the directors' use of the GC basis of accounting in the preparation of the financial statements is appropriate.</td><td>The auditor issues an unmodified audit opinion.</td></tr>
<tr><td colspan="2">The auditor concludes that the directors' use of the GC basis of accounting in the preparation of the financial statements is inappropriate.</td><td>The auditor issues an adverse audit opinion.</td></tr>
<tr><td rowspan="2">The auditor concludes that the directors' use of the GC basis of accounting in the preparation of the financial statements is appropriate.

However, a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a GC.</td><td>Disclosures by the directors in the financial statements are adequate.</td><td>The auditor issues an unmodified audit opinion.

In addition, a separate section with a heading "Material Uncertainty Related to Going Concern" is included in the auditors' report. This section will draw attention to the note in the financial statements that describes the material uncertainty.</td></tr>
<tr><td>Disclosures by the directors in the financial statements are inadequate or omitted.</td><td>The auditor issues as appropriate, a qualified or adverse opinion.</td></tr>
<tr><td colspan="2">Events or conditions were identified that may cast significant doubt on the entity's ability to continue as a GC but, after considering the directors plans to deal with these events or conditions, the directors and the auditor conclude that no material uncertainty exists (i.e., "close call" situations).</td><td>"Close calls" may be determined to be KAM and communicated in the audit report.</td></tr>
</table>

Chartered Accountants Malaysia and MIA

The Chartered Accountant Malaysia or "C.A.(M)" is a designation conferred by the Malaysian Institute of Accountants ("MIA") to a professional in accountancy, business and finance with a recognised accountancy qualification and relevant work experience. C.A.(M) are the industry captains, corporate leaders and decision makers that play significant roles in nation building.

MIA was established under the Accountants Act 1967 as the statutory accountancy body that regulates, develops, supports and enhances the integrity and status of the profession while upholding the public interest.

Working closely alongside strategic business partners and stakeholders, MIA connects its members to a wide range of continuous professional development programmes, updates and networking opportunities. Presently, there are over 33,000 members making their strides across all industries in Malaysia and around the world.

Vision

To be a globally recognised and renowned institute of accountants committed to nation building.

Mission

To develop, support and monitor quality and expertise consistent with global best practices of the accountancy profession in the interest of stakeholders.

Objectives

1. Develop and enhance the competency of accountancy professionals to meet market demand;
2. Advance and enhance the status (professionalism, competency, ethics) of members and the accountancy profession in Malaysia;
3. Support & regulate (furthering, drive, lead, ensure) the practice of the accountancy profession in Malaysia consistent with global standards and best practices;
4. Promote the accountancy profession as a profession of choice.; and
5. Well governed organisation with good Talent Management, Operational and Financial sustainability.

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