

A GUIDE TO UNDERSTANDING ANNUAL REPORTS: MALAYSIAN LISTED COMPANIES

July 2021

ABOUT CPA AUSTRALIA

CPA Australia is one of the largest professional accounting bodies in the world, with more than 168,000 members in over 100 countries and regions, including more than 10,500 members in Malaysia. CPA Australia has been operating in Malaysia since 1956 and opened our Malaysian office in 1994. Our core services include education, training, technical support and advocacy. CPA Australia provides thought leadership on local, national and international issues affecting the accounting profession and public interest. We engage with governments, regulators and industries to advocate policies that stimulate sustainable economic growth and have positive business and public outcomes.

Find out more at cpaaustralia.com.au

ABOUT THE MALAYSIAN INSTITUTE OF ACCOUNTANTS (MIA)

Established under the *Accountants Act 1967*, MIA 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.

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). For more information on MIA, visit www.mia.org.my

ISBN: 978-0-6487514-1-0

2021 Edition.
First published in 2014 by CPA Australia Ltd
Level 20, 28 Freshwater Place
Southbank VIC 3006 Australia

LEGAL NOTICE

The reproduction, adaptation, communication or sale of these materials ('the Materials') is strictly prohibited unless expressly permitted under Division 3 of the *Copyright Act 1968* (Cth). For permission to reproduce any part of these materials, please contact the CPA Australia Legal Business Unit – legal@cpaaustralia.com.au

COPYRIGHT NOTICE

© CPA Australia Ltd (ABN 64 008 392 452) ('CPA Australia'), 2021. All rights reserved.

DISCLAIMER: CPA Australia Ltd and the Malaysian Institute of Accountants do not warrant or make representations as to the accuracy, completeness, suitability or fitness for purpose of the Materials and accept no responsibility for any acts or omissions made in reliance of the Materials. These Materials have been produced for reference purposes only and are not intended, in part or full, to constitute legal or professional advice. To the extent permitted by the applicable laws in your jurisdiction, CPA Australia Ltd and the Malaysian Institute of Accountants, their employees, agents and consultants exclude all liability for any loss, damage, claim, proceeding and/or expense including but not limited to legal costs, indirect special or consequential loss or damage, arising from acts or omissions made in reliance of the Materials. Where any law prohibits the exclusion of such liability, CPA Australia Ltd and the Malaysian Institute of Accountants limits their liability to the resupply of the Materials.

TABLE OF CONTENTS

FOREWORD	4
WHAT IS AN ANNUAL REPORT?	5
WHAT IS A DIRECTORS' REPORT?	7
WHAT IS A CORPORATE GOVERNANCE STATEMENT AND REPORT?	8
WHAT IS A STATEMENT ON RISK MANAGEMENT AND INTERNAL CONTROL?	10
WHAT IS A SUSTAINABILITY STATEMENT?	11
WHAT IS A FINANCIAL REPORT?	12
WHAT IS THE INDEPENDENT AUDITOR'S REPORT?	13
WHAT DO THE FOUR PRIMARY FINANCIAL STATEMENTS SHOW?	15
WHY IS THE STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME DIFFERENT FROM THE STATEMENT OF CASH FLOWS?	16
WHY ARE FIGURES IN A FINANCIAL STATEMENT SUBJECT TO JUDGEMENT AND INTERPRETATION?	17
FEATURES OF THE FINANCIAL STATEMENTS	18
AN APPROACH TO READING FINANCIAL STATEMENTS	20
WHERE AND WHEN ARE THE FINANCIAL REPORTS PUBLISHED?	23
OPPORTUNITIES FOR SHAREHOLDERS	24
SAMPLE FINANCIAL STATEMENTS	25
GLOSSARY	31

FOREWORD

Capital markets, and the corporate entities within them, play a vital role in the growth and sustainability of developed and developing economies. For investors and other stakeholders, annual reports provide important information about the performance and governance of such corporate entities. This information influences share prices and market confidence, and facilitates resource allocation within and across economies.

The onset of the digital age has resulted in multiple information channels. Many of these are used by corporate entities to keep the market informed in real time. Despite the increase of information channels, the importance of conventional and well-established annual reporting remains undiminished.

The legal and regulatory frameworks, and professional rigour required to prepare and audit the information contained in annual reports is key to their credibility.

The frameworks for annual reporting continually evolve to reflect the increasing complexity of global business. The adoption of the Malaysian Financial Reporting Standards (MFRS), which mirror the International Financial Reporting Standards (IFRS; a 'universal language' for financial reporting), accommodates the diverse needs of different economies. Developments such as Integrated Reporting <IR> and the Task Force on Climate-related Financial Disclosures (TCFD) recommendations reflect demand for environmental, social and governance information in annual reports.

These factors mean that reading, interpreting and understanding annual reports need financial knowledge and expertise. *A Guide to Understanding Annual Reports: Malaysian Listed Companies* offers a roadmap of common content in annual reports. This will assist in deciphering the content and structure of annual reports to guide decision making.

This second edition has been updated to reflect the developments since the issuance of the 2014 Guide. These include non-financial reporting developments such as the Malaysian Code of Corporate Governance 2021 and <IR>; the *Companies Act 2016*; auditor reporting developments; as well as an enhanced guide on the approach to reading financial statements.



Merran Kelsall FCPA

President and Chairman
CPA Australia



Dr Veerinderjeet Singh

President
Malaysian Institute of Accountants

WHAT IS AN ANNUAL REPORT?

The annual report comprises information about a company and applicable entities it controlled during the **reporting period**. The annual report is a document through which companies communicate details of their activities, financial results and strategies, to shareholders and other stakeholders.

COMPONENTS OF AN ANNUAL REPORT

Information found in the annual report includes material required by statutory and regulatory requirements articulated in the *Companies Act 2016 (CA 2016)* and **Bursa Malaysia Securities Berhad** (Bursa Malaysia) **listing requirements**, including:

- the directors' report (see page 7)
- the corporate governance statement (see page 8)
- statement on risk management and internal control (see page 10)
- sustainability statement
- the financial report (see page 12)
- the auditor's report on the financial report (see page 13).

CURRENT AND FUTURE DEVELOPMENTS IN ANNUAL REPORTING

Sustainability reporting (variously described as non-financial information (NFI), corporate social responsibility (CSR) or environmental, social and governance (ESG) reporting), has emerged as an important part of communicating wider corporate performance. In helping engagement with non-shareholder stakeholders, there is growing awareness of the importance of climate-related risk disclosures to the business, providers of finance (both debt and equity) stakeholders, including governments and regulators, and society.

The key sustainability standard-setting and framework developments organisations are:

- the Carbon Disclosure Project (CDP)
- Climate Disclosure Standards Board (CDSB)
- Global Reporting Initiative (GRI)
- International Integrated Reporting Council (IIRC) and
- the Sustainability Accounting Standards Board (SASB).

In addition to these organisations' outputs, the development of sustainability reporting and the intended underlying behaviour of companies is influenced by the 17 United Nations' Sustainable Development Goals (SDGs) and the G20 Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).

The TCFD recommendations released in June 2017 provide a framework for consistent climate-related financial disclosures under the categories of Governance, Strategy, Risk Management and Metrics and Targets. These disclosures serve investors, lenders and the market generally in assessing and pricing climate-related risks and opportunities.

Bursa Malaysia Berhad in its second edition of the Sustainability Reporting Guide (“the Bursa Malaysia Guide”) provides guidance to companies on embedding sustainability in practices and reporting directed at driving deeper awareness of how business impacts the economy, environment and society.

The Bursa Malaysia Guide makes extensive reference to the SDGs, TCFD and the GRI standards, and also provides vital assistance for companies in preparing and issuing a Sustainability Statement to meet Listing Requirements.

The Bursa Malaysia Guide also makes mention of <IR> as a significant and valuable innovation in corporate reporting which report preparers can consider. An integrated report is intended as a concise communication about how a company’s strategy, performance, governance and prospects lead to value creation. An integrated report can improve the quality of information available to investors and promote greater transparency and accountability on the part of the company.¹ In addition, it helps businesses to think holistically about their strategy and plan, inform decisions and manage key risks to build investor and stakeholders’ confidence and improve their future performance.

<IR> provides significant information about an organisation’s strategy, governance, performance, and prospects in way that emphasises the commercial, social, and environmental context that it operates in. There are three fundamental concepts of the framework which are:

- the relationship between the organisation and the resources and relationships that underpin its success, described within the framework by reference to six capitals (financial, manufactured, intellectual, human, social and relationship, and natural)
- providing an explanation of the organisation’s business model
- value created, preserved or eroded for the organisation over time manifests itself in increases, decreases or transformations of the capitals caused by the organisation’s business activities and outputs.

In Malaysia, the **Malaysian Code of Corporate Governance 2021** (MCCG) encourages companies to adopt <IR> based on a globally recognised framework to promote greater internalisation of corporate governance culture. The framework refers to the <IR> framework developed by the IIRC that promulgates a more cohesive and efficient approach to corporate reporting that enhances accountability and stewardship of a broad base of capitals, addresses multiple stakeholders and tells the value creation story of an organisation.²

It is emphasised that the development of sustainability reporting is evolving at a rapid pace in both institutional governance and technical terms. These developments, briefly mentioned here, will increasingly impact on the understanding of the scope and content of annual reports.

Alignment between the five above mentioned standards setters and framework developers is underway directed at achieving comprehensive corporate reporting. These emphasise such matters as decision on an agreed set of sustainability topics, materiality, interoperability and the role of <IR> as a robust conceptual framework connecting financial reporting and sustainability disclosure standards.

These developments are accompanied by institutional consolidation including the proposed merger of the SASB and the IIRC, along with announcement from the IFRS Foundation of an intended greater role in driving consistency and comparability in sustainability reporting.

¹ Securities Commission Malaysia, 2017, Malaysian Code on Corporate Governance

² The Malaysian Institute of Accountants has been actively advocating the adoption of integrated reporting in Malaysia and participating in activities of the IIRC since 2015. MIA is also a certified IIRC trainer.

WHAT IS A DIRECTORS' REPORT?

The directors' report of a listed company has an important role in meeting the information needs of stakeholders. While a company's financial report provides useful information about financial position and performance, it will rarely provide all the information needed to ascertain the underlying reasons for a company's financial results. It will also provide little, if any, information about business strategies and prospects relevant to future financial performance.

The directors' report contains information that stakeholders would reasonably need to make an informed assessment of the company's performance and prospects. Such information can cover:

- the operations of the company reported on
- the financial results of that company
- the business strategies of that company and its financial prospects
- a statement of the company's principal activities and any significant changes in the nature of those activities
- details of matters since the end of the year that may significantly affect the company's future operations, results or state of affairs
- reference to likely developments in the company's operations and expected results of those operations
- details of the company's performance in relation to any particularly significant environmental regulation.

The directors' report identifies the names of the directors and officers of the company and discloses their benefits and interests in the company and its related operations.

The directors' report must also disclose other statutory information required by Section 253 of the *CA 2016*. For example, whether the directors are aware of any circumstances which have arisen that would render adherence to the existing method of valuation of **assets** or **liabilities** of the company misleading or inappropriate. The directors report must also disclose whether the directors are aware of any circumstances not otherwise dealt with in the directors' report or financial statements of the company which would render any amount stated in the financial statements misleading.

The directors' report must be approved by the Board and is signed on behalf of the Board by at least two directors.

WHAT IS A CORPORATE GOVERNANCE STATEMENT AND REPORT?

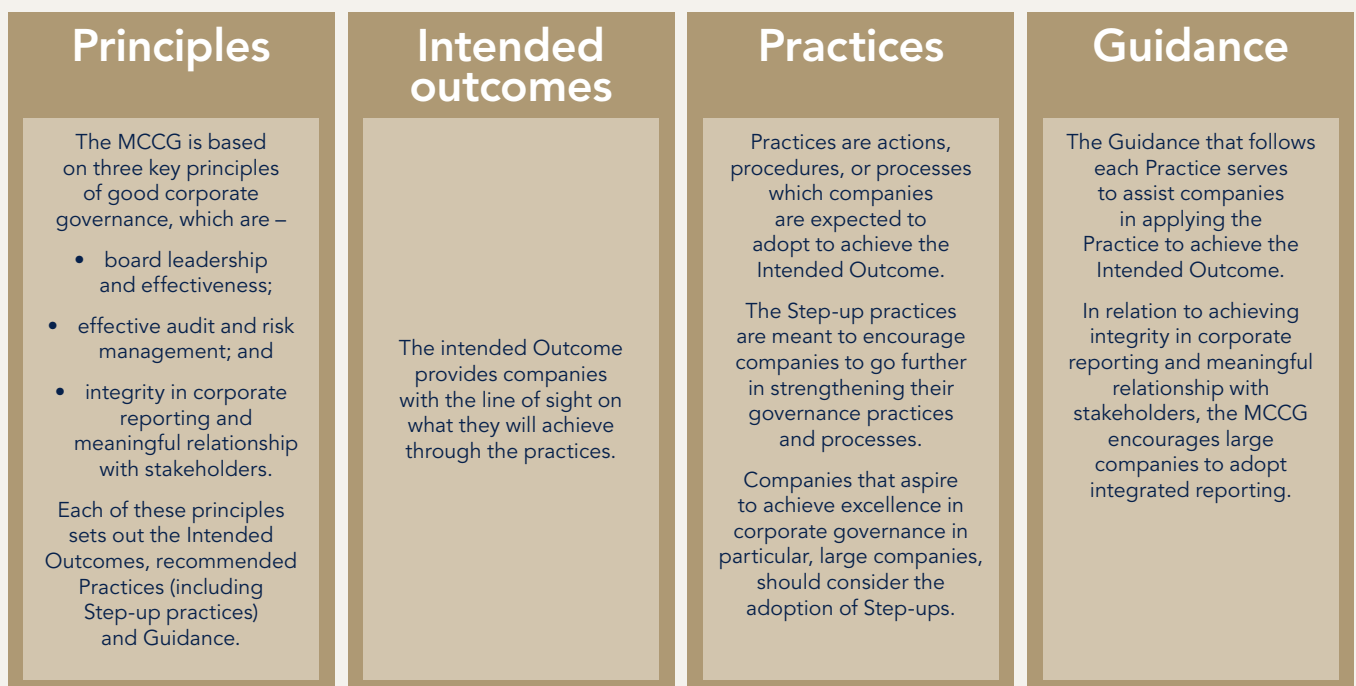
In Malaysia, the MCCG introduces best practices and guidance to improve board policies and processes including those related to director selection, nomination and appointment, strengthen board oversight and the integration of sustainability considerations in the strategy and operations of companies and encourage the adoption of the best practices, particularly those found to have relatively lower levels of adoption, as highlighted in the *Securities' Commission Corporate Governance Monitor* report.

The MCCG reflects global principles and internationally recognised practices of corporate governance which are above and beyond the minimum required by statute, regulations or those prescribed by Bursa Malaysia. The MCCG takes a systematic approach to promote greater internalisation of corporate governance culture.

The key features of the approach taken in the MCCG are shown below.



The MCCG has the following structure:



Paragraph 15.25 of the Bursa Malaysia Listing Requirements requires listed companies to make the following corporate governance disclosures:

- a. an overview by the Board of the application of the **Principles** set out in the Malaysian Code of Corporate Governance (MCCG) – included in its annual report, i.e. a Corporate Governance (CG) Overview Statement; and
- b. the application of each **Practice** set out in the MCCG during the financial year – disclosed in a prescribed format, i.e. a CG Report.

These disclosures should be made and published together with the annual report.

Listed companies must state in their annual report the designated website link or address where the CG Report may be downloaded.

A. CG Overview Statement

The CG Overview Statement provides a summary of the governance practices of listed companies during the financial year, and cover the following three principles:

- a. board leadership and effectiveness
- b. effective audit and risk management
- c. integrity in corporate reporting and meaningful relationship with stakeholders.

The CG Overview Statement should also include the key focus areas and future priorities in relation to the corporate governance practices of listed companies.

B. CG Report

A CG Report provides informative disclosure on the application of the MCCG practices by listed companies. Shareholders and potential investors need access to regular, reliable, comparable and integrated information for them to assess the stewardship of management, valuation of the company and the ownership structure. Thus, good corporate governance disclosure can, in the long run, help attract capital and maintain confidence in the capital market.³

In the report, listed companies must provide meaningful explanation on how it has applied each practice. Where there is a departure from a practice, the company must provide an explanation for the departure, and disclose the alternative practice it has adopted and how the alternative practice achieves the intended outcome.⁴

³ Malaysian Code of Corporate Governance 2021

⁴ *ibid*

WHAT IS A STATEMENT ON RISK MANAGEMENT AND INTERNAL CONTROL?

A listed issuer/corporation must include a statement about the state of internal control (Statement on Risk Management and Internal Control – SORMIC) in their annual report in accordance with paragraph 15.26(b) of the Bursa Malaysia listing requirements.

Readers may also wish to refer to Practice Note 9 (for issuers on the Main Market) and Guidance Note 11 (for issuers on the ACE Market) when seeking to better understand the content of the statement on risk management and internal control.

In preparing the SORMIC, a listed issuer/corporation is guided by the Statement on Risk Management and Internal Control: Guidelines for Directors of Listed Issuers (SRMICG). This was issued by the Task Force on Internal Control with the support and endorsement of the Bursa Malaysia. The SRMICG sets out internal control and risk management practices in place in the listed issuer/corporation which includes the following:

- Commentary on the adequacy and effectiveness of the risk management and internal control system;
- Affirmation that a review on the adequacy and effectiveness of the risk management and internal control system has been undertaken; and
- Assurance received from the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) whether the listed issuer's/corporation's risk management and internal control system is operating adequately and effectively in all material aspects based on the risk management and internal control system of the listed issuer/corporation.

In accordance with paragraph 15.23 of the Bursa Malaysia Listing Requirements, a listed issuer/corporation must ensure that the external auditors review the SORMIC and report the results of the review to the Board of Directors.⁵

⁵ The Malaysian Institute of Accountants issued Audit and Assurance Practice Guide 3 *Guidance for Auditors on Engagements to Report on the Statement on Risk Management and Internal Control included in the Annual Report* to provide guidance for auditors in the performance of a limited assurance engagement to report on the Statement on Risk Management and Internal Control included in the annual report.

WHAT IS A SUSTAINABILITY STATEMENT?

The Listing Requirements require listed companies to include a Sustainability Statement in the annual report. This is a narrative statement of how listed companies manage their material economic, environmental, and social risks and opportunities. The Sustainability Statement should contain information that is balanced, comparable and meaningful by referring to the Bursa Malaysia Guide.

The Sustainability Statement provides the following information:

- a. the governance structure in place to manage the economic, environmental, and social risks and opportunities (“sustainability matters”)
- b. the scope of the Sustainability Statement and basis for the scope
- c. material sustainability matters.

Sustainability matters are considered material if they:

- a. reflect the listed companies’ significant economic, environmental, and social impacts, or
- b. substantively influence the assessments and decisions of stakeholders.

Alternatively, listed companies may prepare their Sustainability Statement in accordance with the GRI Sustainability Reporting Guidelines.

WHAT IS A FINANCIAL REPORT?

The financial report provides people who are interested in a company – such as shareholders, lenders, analysts, employees and other stakeholders – with information about the financial performance and financial position of the company.

It is one means by which directors of the company advise shareholders on how the business has performed during the year. The financial report also provides information to shareholders on how the directors have discharged their responsibilities.

Financial reports consist of **four primary financial statements, the notes to the financial statements, the directors' statement and a statutory declaration.**

Four primary financial statements

Financial statements present information relevant to the current financial period and comparative figures for the previous year to illustrate how the financial performance and position of the company have changed.

The four primary financial statements are:

- the statement of profit or loss and other comprehensive income (sometimes referred to as a profit and loss statement)
- the statement of financial position (sometimes referred to as a balance sheet)
- the statement of changes in equity
- the statement of cash flows.

Notes to the financial statements

The notes to the financial statements explain the accounting policies used in its preparation and provide additional information about some data reported. Recently, there has been a movement towards the use of “streamlined financial reporting”, whereby the needs of investors and stakeholders are put first by providing them with the information they need in a format and language that is easier to understand, whilst continuing to comply with the underlying requirements.

The notes also provide financial information which is not contained in the primary financial statements, such as information about the uncertainties facing the company that meet the definition of **contingent liabilities**.

Later in this Guide we illustrate the possible form and content of the four financial statements and some notes by providing the partial financial report of a fictitious Malaysian listed iron ore mining company, ABC Berhad (page no. 25 to 28).

The directors' statement

The directors' statement is a statement from the directors that:

- the financial statements and the notes comply with accounting standards
- the financial statements and notes give a true and fair view.

Statutory Declaration

Under the CA 2016,⁶ a set of Financial Statements should be accompanied by a “statutory declaration” made by a director, or the person primarily responsible for the financial statements of the company, setting forth their opinion as to the correctness (or otherwise) of the financial statements.

⁶ Refer to Section 251(1)(b) of the *Companies Act 2016*

WHAT IS THE INDEPENDENT AUDITOR'S REPORT?

The independent auditor's report expresses an external auditor's opinion, and related information, on whether the financial statements in the annual report give a true and fair view of the company's financial position, financial performance and cash flows.

The *Companies Act 2016 (CA 2016)* requires a company's auditor to report to shareholders on the financial statements. In Malaysia, an approval from the Ministry of Finance is required for a person to be a company auditor. The auditor's report is addressed to the shareholders of the company, but it can also be referred to by other interested parties such as bankers.

The "opinion" section

The auditor's opinion is presented first and shall contain a clear expression of opinion unless the auditor is unable to do so. The auditor shall express an **unmodified** opinion when the auditor concludes that the financial statements give a true and fair view of the reported financial position of the company and of its financial performance and cash flows in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the *CA 2016* in Malaysia.

Other reporting responsibilities in addition to expressing an opinion on the financial statements arise mainly from statutory or regulatory requirements. For example, the auditor must express an opinion whether the accounting and other records and the registers required by the *CA 2016* have been properly kept by the company in accordance with the provisions of the Act.

The "basis for opinion" section

The auditor explains that the audit was performed in accordance with approved standards on auditing in Malaysia and International Standards on Auditing and confirms compliance with the By-Laws (on Professional Ethics, Conduct and Practice) of the Malaysian Institute of Accountants ("By-Laws") and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"). If the auditor's report has been modified, this section will also include an explanation of the reason(s) why the opinion has been modified.

The section on "Key Audit Matters"

For listed companies, the auditor's report includes a section on Key Audit Matters (KAM). KAM are those matters that, in the auditor's professional judgement, were of most significance in performing the audit. In simple terms, such matters will generally represent those that need greater audit attention. The number of KAMs the auditor identifies is not fixed and is therefore a matter of judgement. For each KAM identified, the auditor's report will include a description of the KAM and details of how the auditor addressed it. It is possible, although not particularly common, that the auditor might not identify any KAMs. In such cases the KAM section of the auditor's report must include a statement to that effect.

Other information section

Referring to the information included in the annual report that is not subject to the audit, this section highlights the fact that the opinion expressed in the auditor's report is only applicable to the financial statements and any other sections of the annual report that is subject to audit, and not applicable to other information included in the annual report. However, an auditor reads the other information in the annual report that is not subject to audit to ensure that such other information is not materially inconsistent with:

- the audited financial statements, and
- the auditor's knowledge obtained through conduct of the audit.

The auditor informs readers of the annual report that the accuracy of other information included in the annual report is the responsibility of the management of the company.

Modifications to the auditor's report

The auditor will issue a **modified opinion** when they conclude that the financial statements do not give a true and fair view, of the reported financial position of the company and of its financial performance and cash flows in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the *CA 2016* in Malaysia.

When the auditor modifies the opinion on the financial statements, the auditor includes a paragraph in the auditor's report that provides a description of the matter giving rise to the modification.

Limitations of the auditor's responsibilities

Whilst the auditor's report provides the reader with greater confidence in the information contained in the financial report, it does not guarantee the accuracy of the financial information, or the continued viability of the company. This is explained in the section on the auditor's responsibilities. The auditing framework is designed to enable auditors to make an assessment that is based on several factors, including materiality.

The CPA Australia publication *A Guide to Understanding Auditing and Assurance: Malaysian Listed Companies* explains the value and purpose of the auditor's report in plain language.

WHAT DO THE FOUR PRIMARY FINANCIAL STATEMENTS SHOW?

The primary purpose of financial statements is to aid current and prospective investors, lenders and other creditors in making economic decisions.

Financial statements also show the results of the management's stewardship of the resources entrusted to it. Other internal and external user groups such as employees, customers, financial analysts, tax authorities, government agencies and general public may also use financial statements to fulfil their information needs.

The statement of profit or loss and other comprehensive income provides an overall picture of company performance by reporting the income and **expenses** of the company during the **reporting period**.

The statement of financial position shows the monetary measure of all the resources controlled by a company and all the obligations falling due at a particular point in time (usually the end of the financial year), classified as current or non-current or in order of **liquidity**.

The statement of changes in equity reports all changes to equity during the financial period, including transactions with owners in their capacity as owners (E.g. Dividends paid).

The statement of cash flows shows the cash inflows and outflows for the financial period, split between operating, investing and financing activities.

The content of the four primary statements is supported by notes. The notes include items such as the accounting policies applied, further information on balances within the primary statements and other disclosures not directly related to the primary statements.

Financial statements of Malaysian listed entities are prepared in accordance with the Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the *CA 2016*.

WHY IS THE STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME DIFFERENT FROM THE STATEMENT OF CASH FLOWS?

Companies prepare their financial statements, except for the statement of cash flows, using the accrual basis of accounting. This means the financial effect of a transaction is recorded in the financial statements when the transaction occurs. This may be different from when the cash relating to the transaction is received or paid.

The statement of cash flows simply shows an inflow when cash is received (e.g. through the sale of goods/services, receipt of funds from borrowings, etc.) and an outflow when cash is paid (e.g. when purchasing an asset, paying for services, etc.).

For example, our fictitious mining company ABC Berhad may have entered into a contract to sell iron ore, and will recognise the sale proceeds as **revenue** when the customer has taken delivery of the ore, being the point at which it has satisfied its performance obligations under the contract.

However, payment is likely to be received at a later date, which may be after the end of the financial year. Thus, the sale will be included in the statement of profit or loss and other comprehensive income for the financial year and a receivable recognised in the statement of financial position. However, as no cash has changed hands, the proceeds will not be reflected in the statement of cash flows until the following financial year.

In addition, some transactions that are recognised in the statement of profit or loss and other comprehensive income are non-cash in nature. For example, items of property, plant/factory and equipment are subject to **depreciation**, which appears as an expense in the statement of profit or loss and other comprehensive income. However, depreciation represents an accounting entry only and does not result in an outflow of cash.

Therefore, depreciation expense appears in the statement of profit or loss and other comprehensive income and in the statement of cash flows.

WHY ARE FIGURES IN A FINANCIAL STATEMENT SUBJECT TO JUDGEMENT AND INTERPRETATION?

Financial statements portray the financial effects of what are often complex commercial transactions, and judgement may be required to determine how some transactions and events are to be represented. Accounting standards play an important part in ensuring that similar transactions are treated in a similar manner.

However, a principles-based approach to setting accounting standards means that explicit rules are not written to cover all situations. Therefore, professional judgement may be needed when interpreting and applying an accounting standard.

Returning to the ABC Berhad example, the amount shown as exploration expenditure in the statement of financial position is the cost that the company estimates will be recovered in future financial years. The application of accounting standards means the effect of the company's estimate is also seen in the statement of profit or loss and other comprehensive income as an impairment expense. Judgement is frequently required in determining those amounts and companies will often make use of an external valuation expert.

Companies are required to use judgement to decide how long an **asset** will remain useful and the resulting effect on **depreciation** of property, plant and equipment assets.

Clear and concise disclosure of the significant judgements and estimates made by companies in preparing the financial statements is paramount to assisting the readers to better understand the financial report. In many cases, it is often these matters which are commented on in the KAMs section of the auditor's report.

FEATURES OF THE FINANCIAL STATEMENTS

STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME

The financial performance report of ABC Berhad uses the single statement format of the statement of profit or loss and other comprehensive income, and starts with **revenue**.⁷

Note 3 in the statement of profit or loss and other comprehensive income identifies the types of revenue earned by ABC Berhad. Accounting standards require that finance costs and tax expense to be presented separately. The notes would contain further information on some items of expense.

For some expenses, the accounting standards allow the company to choose between presenting the information in the statement of profit or loss and other comprehensive income or in the notes to the financial statements.

STATEMENT OF FINANCIAL POSITION

The statement of financial position does not purport to be a valuation of the company, rather it is the outcome of applying accounting standards in measuring the **assets** and **liabilities** of the company. Therefore, it would be incorrect to conclude that the current monetary value of ABC Berhad is RM 266,358,000. (see the Statement of Financial Position on **page 26**).

Some of the assets of ABC Berhad are shown at a current valuation (such as trade and other receivables), while other assets, for example property, plant and equipment, are presented at their cost of purchase less **accumulated depreciation**. Notes 2(a) to (d) provide some further information about the approach taken by ABC Berhad in the preparation of the financial statements.

The accounting standards only allow the recognition of purchased **goodwill**, whereas the goodwill a company builds up during its years of operation is not recognised on the statement of financial position. For example, a company may generate goodwill in respect of areas such as its reputation, customer base, brand exposure, etc. but cannot recognise internally generated goodwill as an asset under accounting standards.

Although ABC Berhad is profitable and has operated for several years, its statement of financial position does not include goodwill as it has not purchased other businesses and prepared consolidated financial statements.

ABC Berhad classifies its assets and liabilities presented in the statement of financial position as **current** or **non-current**. The distinction is based on an assessment of the expected timing of recovering or settling the amounts. An item will be classified as "current" when its amount is expected to be recovered or settled no more than 12 months after the end of the reporting period, otherwise its classification is as "non-current".

Some companies may choose to classify their assets and liabilities only in order of liquidity and not separately presented as current or non-current. Others may use a combination of liquidity and current or non-current classifications.

The equity section of ABC Berhad's statement of financial position includes capital invested by shareholders and accumulated profits retained from previous years.

⁷ Some listed companies use the following two statements to present information about performance:

- a profit or loss statement
- a statement displaying components of other comprehensive income

Whatever the format used, the minimum information presented is specified by the accounting standard.

For companies that adopt accounting policies different from those used by ABC Berhad, the equity section might include:

- reserves that result from the accounting standards requirements for asset revaluations
- changes to the amount of financial assets at fair value through other comprehensive income
- effects of cash flow hedges
- foreign currency translations of subsidiaries' financial statements (the example does not include reserves).

Listed companies will sometimes control other companies, while ABC Berhad does not. In those situations, the financial statements of the parent show information for the consolidated group. The equity section of the statement of financial position would separately present equity attributed to the shareholders of the parent, and the non-controlling interest.

STATEMENT OF CHANGES IN EQUITY

The statement of changes in equity shows the overall change in equity during a period which represents:

- profit or loss and other comprehensive income during that period
- the changes resulting from transactions with owners acting in their capacity as owners.

In the current financial year, ABC Berhad activities with its owners are the issue of new shares at RM 336,000 and the payment of dividends of RM 35,912,000 (see the example Statement of Changes in Equity on **page 27**).

STATEMENT OF CASH FLOWS

The statement of cash flows shows movements of cash (cash on hand and demand deposits) and cash equivalents (short-term, highly liquid investments that are readily convertible to cash). It highlights the sources and uses of cash and cash equivalents, and analyses the areas of ABC Berhad activity as follows:

- operating activities
- investing activities
- financing activities.

The information in a statement of cash flows about cash and cash equivalents including their source can be used to assess the company's ability to meet its financial commitments and fund its activities. (see the example Statement of Cash Flows on **page 28**).

AN APPROACH TO READING FINANCIAL STATEMENTS

Financial statement reporting by listed companies is all about communicating monetary measures and supporting information to current and prospective investors, lenders and other creditors. Other stakeholders, including analysts and employees, may also be interested. Some parts of the statements may be of interest to all, while other parts will be of interest to particular groups.

Those readers planning to use the financial statements to make decisions need to be aware that a listed company's financial statements do not and cannot provide all the information they may need. Analysts' reports, the financial press, and the Bursa Malaysia website are other sources of information to assist decision making.

A final word of caution – financial statements are not designed to show the market value of the company, but they do provide information to assist shareholders, other providers of capital and other stakeholders in estimating that value.

Step 1	Understand the environment in which the company operates: to provide context when reading the financial statements.
Step 2	Read the auditor's report: to understand the auditor's opinion on the financial statements.
Step 3	Perform relevant vertical, horizontal and ratio analysis: to better understand its profitability, financial position and cash position.
Step 4	Read the accounting policies: to understand the accounting basis on which the financial statements are prepared.
Step 5	Read the notes to the financial statements: to further understand specific items in the financial statements.

STEP 1

The importance of preparation should not be underestimated when analysing the financial statements of a listed company. Increasing your knowledge about the environment in which the company operates in, plus its direction is a good and necessary start. For example, seeking information about local, national or global macro and micro economic conditions and the risk profile of the company's business(es).

Returning to our fictitious Malaysian listed iron ore mining company example, the current and prospective shareholders of ABC Berhad are likely to be interested in projected international demand for iron ore.

Most readers gain an overview of the company, an understanding of the business it's in and the risks the business is facing from reading other parts of the annual report. The statements from the chairman and the chief executive officer (CEO) that put the company's performance highlights into context against strategies and the directors' report are often important to read as well.

Readers should be mindful that statements from the chairman or CEO, except for the remuneration report section of the directors' report are not subject to audit in the same way as the financial report and the remuneration report. However, although the audit does not cover such other information contained in the annual report – beyond the financial report and remuneration report – the auditor must read the other information and report on whether it is materially inconsistent with the financial report, or knowledge gained through the audit, or appears to be materially misstated.

STEP 2

Read the auditor's report to see if the auditor's opinion has been modified or contains some other communication by the auditor. If so, read carefully why the auditor has issued a modified opinion or included another communication such as an **emphasis of matter** paragraph. Read the details of any KAM communicated by the auditor to gain an understanding of the areas of greatest audit effort.

STEP 3

Next, have a look to the statement of profit or loss and other comprehensive income and the statement of financial position to assess the size of the company and its profitability.

ABC Berhad generated **profit** after income tax for the current period of RM 40,674,000. But this figure means little unless we compare it to another time period or another similar company to give it context.

Horizontal or trend analysis can be used for intracompany comparative analysis. For example, you might decide to evaluate performance by using the comparative information in the ABC Berhad financial statements to benchmark the current year performance (profit after income tax RM 40,674,000 compared to the previous year figure of RM 26,705,000). Vertical analysis can be used for intracompany and intercompany comparative analysis.

A base amount is established and the monetary measure in the current period financial statement of ABC Berhad would be expressed as a percentage of this base amount.

For example, you might be interested in the relationship of cash and cash equivalents to total assets and how it compares to the previous year. For the current financial year, the relationship expressed as a percentage is 26.8 per cent (and the comparative financial year 25.6 per cent). Ratio analyses compares the relationships of financial statement information, and are worked out by dividing one monetary measure by another and can be used for intracompany and intercompany comparative analysis.

Fictitious Malaysian mining company ABC Berhad has current period **current assets** of RM 117,387,000 and RM 57,623,000 in **current liabilities**, which results in a current ratio of 2.04:1 (and a current ratio of 1.80:1 in the comparative year). You can use the outcomes from performing horizontal, vertical and ratio analysis to compare the results for the previous year, the industry sector or competitors.

Now consider the statement of cash flows and the information this provides on the company's cash and cash equivalents transactions and position.

The level of focus stakeholders place on the different primary statements will depend on the nature of the business. For example, in sectors where the asset base of the company is very important (such as banking, property, funds management, etc.) the statement of financial position may receive greater attention. However, in a company where **revenue, profit** or dividend payments are important to stakeholders, the statement of profit or loss and other comprehensive income may be considered more important.

STEP 4

Turn to the notes to the financial statements. For example, Note 2 to the financial statements of ABC Berhad states the basis of preparation for the financial statements is on an accrual basis and is based on historical costs which do not consider changing money values. Cost is based on the fair value of the consideration given in exchange for assets. Further, the accounting policies have been consistently applied, unless otherwise stated.

Read the accounting policies which are used for any items which have attracted your attention in the financial statements. Look for accounting policies which have changed during the year, the reasons for the change and the effect of the change on the financial statements. Companies are required to provide information on changes to accounting policies in the notes to the financial statements.

STEP 5

The remaining notes to the financial statements contain detailed financial information, including information on the areas in which the company operates, specific items of revenue and expense, and an explanation of the tax expense. Again, look for the notes which elaborate on any amounts which have come to your attention in the financial statements.

WHERE AND WHEN ARE THE FINANCIAL REPORTS PUBLISHED?

All listed companies publish their financial statements and reports on their website and through announcements via Bursa Malaysia website notifying shareholders of its action. Quarterly results are published no later than two months after the end of the immediate past quarter.

Unless a shareholder specifically requests not to receive the financial report, listed companies must prepare and send a copy of their financial report to all members at least 21 days before the Annual General Meeting (AGM) and within four months of the end of the financial year.

Listed companies are required to issue the annual audited financial statements, and lodge the same to the Bursa Malaysia within four months of the end of the financial year.

Based on para 2.19B from Main Market Listing Requirements, a listed issuer may send any document required to be sent under these Requirements to its securities holders ("Documents") by electronic means, if the following conditions are complied with:

- a. the constitution of the listed issuer:
 - i. provides for the use of electronic means to communicate with its securities holders;
 - ii. specifies the way the electronic means is to be used; and
 - iii. states that the contact details of a securities holder as provided to the Depository shall be deemed as the last known address provided by the securities holder to the listed issuer for purposes of communication with the securities holder;
- b. if the listed issuer publishes the Documents on its website, the listed issuer must separately and immediately notify the securities holders of the following in writing:
 - i. the publication of the Document on the website; and
 - ii. the designated website link or address where a copy of the Document may be downloaded;
- c. if the listed issuer sends the Documents or notification through electronic mail, there must be proof of electronic mail delivery;
- d. where a securities holder requests for a hard copy of the Document, the listed issuer must forward a hard copy of the Document to the securities holder as soon as reasonably practicable after the receipt of the request, free of charge; and
- e. where it relates to Documents required to be completed by securities holders for a rights issue or offer for sale, the listed issuer must send these Documents through electronic mail, in hard copy or in any other manner as the Exchange may prescribe from time to time.

To provide listed issuers with a sufficient grace period for compliance, the timeframe for issuance of the annual reports is within four months from the close of the financial year and dispensation, with the separate requirement for announcement of annual audited financial statements within four months from the close of the financial year (as the annual report issued within four months would already include the annual audited financial statements, directors' and auditors' report).

OPPORTUNITIES FOR SHAREHOLDERS

Shareholders are sent a notice of the AGM, which is an opportunity for shareholders to ask questions of the directors on any aspect of the company's operations and performance, of the annual accounts tabled at the AGM, and of the auditor about their report.

At the AGM, resolutions requiring shareholders' approval include, but are not limited to:

- reappointment of those directors subject to retirement and who have offered themselves for re-election
- directors' remuneration
- reappointment of auditors
- power to directors to allot shares or grant rights to subscribe for shares in the company.

SAMPLE FINANCIAL STATEMENTS

ABC Berhad is a fictitious Malaysian listed iron ore mining company with primary operations in Malaysia and secondary operations in Brazil. These sample financial statements of ABC Berhad show the way in which many listed companies present yearly financial statements. The figures are simplified to assist you in reading the statements. A selection of the notes to the financial statements is provided for illustrative purposes.

ABC BERHAD

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the year ended 30 June 20XC

	NOTE	20XC RM'000	20XB RM'000
Revenue	3	643,066	539,189
Raw materials and consumables	4	(123,142)	(98,342)
Depreciation		(29,367)	(44,461)
Employee benefits expense		(248,623)	(189,151)
Exploration expenses written off		(28,322)	(18,342)
Finance expenditure		(22,789)	(19,408)
Impairment of exploration expenditure	11	(114,251)	(121,000)
Other expenses	4	(18,492)	(10,174)
Profit before income tax expense		58,080	38,311
Income tax expense	5	(17,406)	(11,606)
Profit after income tax for the period	24	40,674	26,705
Other comprehensive income			
Items that may subsequently be reclassified to profit or loss			
Gain on translation of foreign operations		31	1,678
Other comprehensive income for the period, net of tax		31	1,678
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD ATTRIBUTABLE TO ABC BERHAD		40,705	28,383
Earnings per share for profit from comprehensive income		sen	sen
Basic earnings per share	27	20.62	15.19
Diluted earnings per share	27	20.62	15.19

The statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.

ABC BERHAD

STATEMENT OF FINANCIAL POSITION

As at 30 June 20XC

	NOTE	20XC RM'000	20XB RM'000
Current assets			
Inventories	6	5,641	7,131
Trade and other receivables	7	8,945	5,474
Cash and cash equivalents	8	102,801	98,879
TOTAL CURRENT ASSETS		117,387	111,484
Non-current assets			
Property, plant and equipment	9	69,693	63,163
Exploration assets	10	184,540	201,135
Deferred tax	11	11,353	10,345
TOTAL NON-CURRENT ASSETS		265,586	274,643
TOTAL ASSETS		382,973	386,127
Current liabilities			
Trade and other payables	13	29,054	4,689
Provisions	14	6,875	37,303
Income tax	15	11,266	4,268
Employee benefits	16	10,428	9,953
Borrowings	17	–	5,700
TOTAL CURRENT LIABILITIES		57,623	61,913
Non-current liabilities			
Provisions	18	22,911	8,326
Borrowings	19	18,374	37,476
Deferred tax	20	4,081	3,917
Employee benefits	21	13,626	13,266
TOTAL NON-CURRENT LIABILITIES		58,992	62,985
TOTAL LIABILITIES		116,615	124,898
Net assets		266,358	261,229
Equity			
Contributed Equity	22	223,610	223,274
Reserves	23	5,500	5,469
Retained profits	24	37,248	32,486
TOTAL EQUITY		266,358	261,229

The statement of financial position should be read in conjunction with the accompanying notes.

ABC BERHAD

STATEMENT OF CHANGES IN EQUITY

For the year ended 30 June 20XC

	CONTRIBUTED EQUITY	RESERVES	RETAINED PROFITS	TOTAL EQUITY
	RM'000	RM'000	RM'000	RM'000
Balance at 1 July 20XA	128,238	3,791	27,313	159,342
Profit after income tax for the period	–	–	26,705	26,705
Other comprehensive income for the period	–	1,678	–	1,678
Total comprehensive profit for the period	–	1,678	26,705	28,383
<i>Transactions with owners in their capacity as owners</i>				
Shares issued, net of costs	95,036	–	–	95,036
Dividends paid	–	–	(21,532)	(21,532)
Balance at 30 June 20XB	223,274	5,469	32,486	261,229
Balance at 1 July 20XB	223,274	5,469	32,486	261,229
Profit after income tax for the period	–	–	40,674	40,674
Other comprehensive income for the period	–	31	–	31
Total comprehensive profit for the period	–	31	40,674	40,705
<i>Transactions with owners in their capacity as owners</i>				
Shares issued, net of costs	336	–	–	336
Dividends paid	–	–	(35,912)	(35,912)
Balance at 30 June 20XC	223,610	5,500	37,248	266,358

ABC BERHAD

STATEMENT OF CASH FLOWS

For the year ended 30 June 20XC

	NOTE	20XC	20XB
		RM'000	RM'000
Cash flows from operating activities			
Receipts from customers		686,141	278,342
Payments to suppliers and employees		(292,348)	(215,474)
Interest received		24	9
<hr/>			
Net cash generated by operating activities	28	393,817	62,877
Cash flows from investing activities			
Proceeds from disposal of property, plant and equipment		10,321	879
Proceeds from disposal of exploration assets		632	2,783
Purchase of property, plant and equipment		(365,272)	(1,370)
Net cash used in investing activities		(354,319)	(2,292)
Cash flows from financing activities			
Proceeds from issue of shares		336	24,322
Dividends paid		(35,912)	(21,532)
Net cash (used in)/provided by financing activities		(35,576)	2,790
Net increase in cash and cash equivalents		3,922	67,959
Cash and cash equivalents at beginning of the financial year		98,879	(30,920)
Cash and cash equivalents at end the financial year	8	102,801	98,879

The statement of cash flows should be read in conjunction with the accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS (EXTRACT)

This is a sample of notes that you would expect to see in an annual report under notes to the financial statements.

NOTE 1: ADOPTION OF NEW AND REVISED ACCOUNTING STANDARDS

The principal accounting policies adopted in the preparation of the financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

New, revised or amended Malaysian Financial Reporting Standards (MFRS) and IC Interpretations adopted.

The company has adopted all the new, revised or amended MFRS and IC Interpretations issued by the MASB that are relevant to the operations and mandatory in the current **reporting period**.

Any new, revised or amended MFRS and IC Interpretations that are not yet mandatory have not been early adopted.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (EXTRACT)

a. Basis of preparation

The financial statements have been prepared on an accrual basis and are based on historical costs and do not consider changing money values. Cost is based on the fair value of the consideration given in exchange for assets. The accounting policies have been consistently applied, unless otherwise stated.

The financial statements are presented in Ringgit Malaysia (RM) and all values are rounded to the nearest thousand (RM '000) unless otherwise stated.

b. Statement of compliance

The financial statements are general purpose financial statements and have been prepared in accordance with MFRS, International Financial Reporting Standards (IFRS) and the requirements of the *Companies Act 2016* in Malaysia.

c. Critical accounting judgements, estimates and assumptions

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to **assets, liabilities, contingent liabilities, revenue and expenses**.

Management bases these assumptions on experience and on other factors such as expected future events it believes to be reasonable under the circumstances. The resulting accounting judgements and estimates will seldom equal the related actual results. The judgements, estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

d. Estimation of useful lives of assets

The company determines the estimated useful lives and related **depreciation** charges for its property, plant and equipment and deferred exploration expenditure. The useful lives could change significantly as a result of technical innovations or some other events. The depreciation charge will increase where the useful lives are less than previously estimated lives, or technically obsolete or non-strategic assets that have been abandoned or will be written off or written down.

NOTE 3: REVENUE

Revenue is recognised when or as control of the promised goods or services passes to the customer. In most instances, control passes when the goods are delivered to a destination specified by the customer. Revenue from the provision of services is recognised over time but does not represent a significant proportion of total revenue.

The amount of revenue recognised reflects the consideration to which the company expects to be entitled in exchange for the goods or services. Where the company has contracts with unfulfilled performance obligations at period end, it must disclose the transaction price allocated to these performance obligations.

	20XC	20XB
	RM'000	RM'000
Revenue from Contracts with Customers		
Sales of iron ore	629,249	536,661
Sales of other metal	12,492	1,868
	641,741	538,529
Other revenue		
Interest	1,325	660
	643,066	539,189

NOTE 8: CURRENT ASSETS – CASH AND CASH EQUIVALENTS

	20XC	20XB
	RM'000	RM'000
Cash on hand	95	103
Cash at bank	45,706	51,776
Cash on deposit	57,000	47,000
	102,801	98,879

GLOSSARY

Accumulated depreciation	The cumulative depreciation of an asset, from the date the asset is available for use to the date of the current financial year.
Accumulated profits	The amount of past years profits not paid in dividends. Sometimes referred to as retained profits. In contrast, losses from previous years not absorbed by past years profits are accumulated losses.
Asset revaluation	The application of an accounting policy choice, whereby the monetary measure of the asset is the amount for which it could be exchanged between knowledgeable, willing parties in an arms-length transaction.
Assets	Items of value which the company can trade or use in its business.
Bursa Malaysia Securities Berhad listing requirements	The rules governing the listing of securities and regulation of listed issuer on the Main Market and ACE Market in Malaysia.
Contingent liabilities	A potential liability dependent on uncertain future events which are beyond the control of the company.
Corporate social responsibility report	A report on how the company manages its business processes to produce an overall positive impact on society.
Current assets	Cash and cash equivalents and assets which are expected to be turned into cash in the next year.
Current liabilities	Amounts which the company is obliged to pay to others in the next year.
Depreciation	The systematic allocation of the cost of the asset over its useful life.
Emphasis of matter	A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial report that, in the auditor's judgement, is of such importance that it is fundamental to users' understanding of the financial report.
Employee benefits	Represent benefits offered to employees of the company and can include short-term (e.g. salaries and wages), long-term (e.g. long service leave), post-employment benefits (retirement benefits) and termination benefits.
Equity	Total assets less total liabilities; includes share capital, reserves and accumulated profits.
Expenses	The costs of deriving revenue.
Goodwill	An asset representing the future economic benefits arising from other assets acquired by a company when gaining control of one or more other businesses that are not individually identified and separately recognised.
Liabilities	Amounts which the company is obliged to pay to others.
Liquidity	The ease with which assets and liabilities may be converted into cash.
Listed company	A company which is publicly listed on a securities exchange.
Key management personnel	Persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that company.
Modified opinion	The auditor may issue a modified opinion, being a qualified opinion, an adverse opinion or a disclaimer of opinion.

Profit	Surplus of revenues and other income over expenses.
Reporting period	The period that the financial statements cover. This will typically be one year.
Reserves	Surpluses arising from (for example) revaluations of certain assets.
Revenue	Earnings arising in the ordinary activities of the company. Fees from the rendering of services are examples of revenue, as is revenue from the sale of goods.
Share option	A contract that gives the holder of the option the right, but not the obligation, to subscribe to the company's shares at a fixed or determinable price for a specified period.
Share-based payment arrangement	An arrangement between the company and another party (including an employee) that entitles the other party, on satisfying any conditions specific to the arrangement, to shares or share options of the company, or cash or other assets of the company that are based on the price of those shares or share options.
Sustainability report	A report that provides information about the company's performance towards the goal of sustainable development.
	* A glossary of key technical words used in this Guide has been provided to aid understanding. Bold font is used on the first appearance of the term.

