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KUALA LUMPUR: The inclusion of the Key Audit Matters (KAMs) paragraph, which is a commentary on matters that were of most significance during the audit of a Malaysian public listed company (PLC), will give investors more clarity, say industry experts.

Malaysian Institute of Accountants (MIA) chief executive officer Dr Nurmazilah Mahzan said the inclusion of the KAMs will make it easier for investors to navigate their way around PLCs’ annual reports.

“There is so much information in annual reports, so when investors and other users of financial statements look at the KAMs, they know what were the key areas of [audit] focus.

“It also shows there was a robust discussion between auditors as well as the management and directors in certain areas,” she told The Edge Financial Daily in a recent interview.

In 2015, the International Auditing and Assurance Standards Board, which is the international body for setting auditing standards, approved a suite of auditing reporting standards, which resulted in an enhanced auditors’ report, which the KAMs now form part of.

These standards are to be observed for audits of financial statements for financial periods ending on or after Dec 15, 2016. In the same year, the MIA issued the same set of auditing standards that fully adopted their international equivalents, with the same effective date.

MIA Auditing and Assurance Standards Board chairman Lee Tuck Heng said it is important for stakeholders to note that the KAMs are not “new conclusions” or “new opinions” given by auditors.

“Auditors are still opining on one thing — which is the true and fair view of financial statements — and that hasn’t changed. On the KAMs, auditors are not concluding or giving mini opinions on financial statements.

“The mindset that there is something wrong, and that is why auditors are highlighting these [in the] KAMs, has to be changed. [Users of financial statements] need to understand that there are some matters that are inherent,” he said.

As example, he cited that for goodwill recognised, there is a need to carry out an impairment review every year as goodwill tends to be a substantive amount and is material, hence it tends to make it into the KAMs, making it a focus every year.

And even if auditors issue a modified audit or a qualified audit opinion, they will still need to disclose the KAMs, he added.

“However, if auditors issue a disclaimer [of] opinion, or in other words do not issue an opinion on financial statements, the standard says that you do not need to disclose [the] KAMs. The rationale behind that is by putting the KAMs [when a disclaimer opinion is issued], it gives financial statements more credibility than they deserve,” he said.

At present, there are 17 Practice Note 17 (PN17) companies and four Guidance Note 3 (GN3) companies listed on Bursa Malaysia. Many of these companies have ended up in predicaments due to accounting-related and going concern issues.

Nurmazilah said the KAMs could also give early warnings of the possibility of PN17 or GN3 status being triggered.

“[The] KAMs could give an indicator to users of what are the areas and possible reasons for triggering [PN17 or GN3 status]. In the past, [some] investors were probably not aware of what was happening, and suddenly found the company they had invested in was now a PN17 [company] and could not regularise its condition.

“With the inclusion of [the] KAMs, investors now have at least an idea of what were the [risk areas] for the company. But [on] whether the inclusion of [the] KAMs can reduce the number of PN17 or GN3 companies on Bursa Malaysia, I think the issues that have led these companies to their predicaments are much wider than just financial reporting issues. It also pertains to their business model and industry climate,” she said.

Part of an enhanced audit report also includes a separate section for a “material uncertainty related to going concern”, if any such uncertainty exists in a company.

Previously, such reporting would have been under the heading entitled “Emphasis of Matter”.

“There is now a separate header on a material uncertainty related to going concern in an audit report, and not just embedded somewhere in the annual report. So, this is a clear red flag [which stakeholders need to take heed of],” said Lee.

Minority Shareholders Watchdog Group (MSWG) general manager Lya Rahman said among the matters the MSWG would like to see included as part of the KAMs are those that pertain to a high risk of loss.

“[These include] potential concentration risk in a few large customers, liquidity risk or sensitivity analysis arising from changes in interest rates and foreign exchange rates, as well as high impairment losses and irrecoverability of receivables.

“They (auditors) can elaborate on the implications and impact, although such matters could have been stated briefly in the notes of financial statements,” she said in an emailed response to The Edge Financial Daily.

She added that companies should welcome and embrace the new and enhanced audit reports, as they will be useful to investors and readers, and facilitate them in making better and more informed investment decisions.

Companies that have already incorporated an enhanced audit report in their annual report for the financial year ended Dec 31, 2016 include Pharmaniaga Bhd, Malayan Banking Bhd, Public Bank Bhd, Boustead Holdings Bhd and all real estate investment trusts listed on Bursa.

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