

audit oversight board
annual report

2014



Suruhanjaya Sekuriti
Securities Commission
Malaysia

Mission Statement



Fostering high quality
independent auditing
to promote confidence in the
quality and reliability
of audited financial
statements of public-interest
entities in Malaysia



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Executive Chairman's Message



EXECUTIVE CHAIRMAN'S MESSAGE



It is my pleasure to present the Audit Oversight Board's (AOB) Annual Report for the financial year ending 31 December 2014.

The AOB was involved in many fronts in pursuing its mission. Apart from its oversight activities, AOB has been gathering data and insights to better understand the state of play of the auditing industry. We were also involved in other efforts to strengthen the capacity of the accountancy profession, which ultimately influences audit quality.

Operating environment of the auditing industry

There is no significant change in the number of registered and recognised audit firms and individual auditors. The concentration of clients remained with the top 10 audit firms which collectively audit 957

public-interest entities (PIEs) covering 98.6% of the market capitalisation of public-listed companies (PLCs) in Malaysia.

We noted that the rate of increment of fees moderated significantly compared to the last two years while salary costs for auditors continued to be on the upward trend. Such observations are consistent with developments in other markets which raised questions on the value and relevance of audit to companies, their shareholders and other stakeholders.

While staff turnover appeared to normalise at the rate of 25%, the average turnover at the non-executive level remained high. This is still a concern as turnover at this level may indicate the lack of attractiveness of auditing as a career of choice among younger accountants, which could be detrimental over the long term.

Our concern on audit quality remains unabated

While we noted that audit firms have been enhancing their quality control systems, the outcomes of our audit inspections suggest that such efforts have not been able to improve audit quality broadly across the firms. The findings raised questions on the effectiveness of the firms' ability in ascertaining the actual root causes of the deficiencies identified by the AOB. It is important that the firms' internal monitoring processes are able to link these root causes to remedial measures which improve audit quality on a broad basis and remain sustainable.

The efforts to improve audit quality should go beyond process improvements and training. It should also include the overall strategy of competing in the market, alignment of incentive and business model of the firm as a whole. How the audit teams embrace and actualise professional ethics and values should also be the focal point. In this respect, the leadership of audit firms should set a clear tone for the rest to follow.

We are concerned that audit firms may have started to be complacent with the deficiencies and issues raised in our inspection reports and have not given the required attention to the effectiveness of their remediation plans as indicated earlier to AOB. Moving forward, we have decided that in order to uphold audit quality and standard as well as arrest this worrying development, AOB will publish the inspection report of firms in the public domain for failing to take relevant remedial measures.

Enforcing standards and expectations

The registration and recognition conditions have been the primary tool to set expectations on audit firms in fostering them to focus on audit quality. In 2014, the recognition conditions were tightened to ensure firms have adequate capacity, matched with the complexities and risks of their clients.

During the year, the AOB refused an application for recognition by a foreign audit firm due to its failure to comply with AOB's expectations as required in the registration conditions.

Auditors' independence remained our focus in 2014 as it is the foundation which influences auditors' opinion. In this respect, an action was taken against an audit firm which failed to comply with key audit partner rotation requirements, a critical measure to ensure independence.

“We view the implementation of the New and Revised Auditor Reporting Standards as a possible game-changer to enhance the quality of financial reporting in Malaysia. All stakeholders have to be involved to ensure smooth implementation of these standards.”

Collaboration and learning through international engagements

The AOB is committed to contribute towards and collaborate with our peers to continuously raise audit quality as well as uphold global standards of auditing. The collaboration among members of the ASEAN Audit Regulators Group (AARG) via regular discussions and knowledge-sharing to promote consistency of performance among audit oversight regulators has created an impact among the audit firms operating within this region.

We hosted the 8th Inspection Workshop of the International Forum of Independent Audit Regulators (IFIAR). This event held for the first time in the ASEAN region received strong support from over 100 delegates from 35 IFIAR member jurisdictions. It also provided our team members with opportunities to be directly involved and facilitate discussions.

The AOB continuously monitors global developments. During 2014, there was interest surrounding the European Union (EU) audit reform which mandates

the rotation of audit firms and restrictions in the provision of non-audit services to audit clients. There was also interest observed with regard to audit regulation in relation to China-related PIEs.

New audit reporting model – a game changer?

The International Auditing and Assurance Standards Board (IAASB) has issued the New and Revised Auditor Reporting Standards with an effective date of 15 December 2016. These standards would require auditors to incorporate Key Audit Matter disclosures in their reports. This would also lead toward reports which are more tailored to the circumstances of the clients rather than the existing format which contains mostly standard terms and boilerplates. We envisage that the information reported in the future would provide more insights of the risks surrounding a particular reporting entity and some of this information may have market impact.

We view the implementation of the New and Revised Auditor Reporting Standards as a possible game-changer to enhance the quality of financial reporting in Malaysia. All stakeholders have to be involved to ensure smooth implementation of these standards.

Staying focused

The acknowledgement we received from the Asian Corporate Governance Association (ACGA) in its *Corporate Governance (CG) Watch 2014 Report* is a testimony of how far AOB has matured from its humble beginning in 2010. Among others, the AOB was recognised as one of the better organised and transparent audit regulators in the region. This further strengthens our resolve to perform better in the future.

I wish to thank the AOB Board for their commitment and guidance over the year. I would also like to thank fellow regulators, professional accountancy bodies and other stakeholders for their ongoing support over these last five years.

Last but not least, to the AOB management team and staff, I would like to express my gratitude for their outstanding efforts. I look forward to reporting our continued progress in the year ahead.



Nik Mohd Hasyudeen Yusoff

Overview of the **AOB's Strategies**

The AOB aims to achieve the following desired outcomes:

- High quality financial reporting practices by PIEs
- Resourceful and high quality audit practices
- Independent and high quality audits
- High quality and reliable audited financial statements
- Enhanced confidence in audited financial statements

The AOB has adopted a strategic framework which links the service areas and activities of AOB to the desired outcomes which manifest the attainment of its mission. The strategic framework has four strategic themes, which are:

- Promote high quality audit practices
- Influence financial reporting ecosystem
- Leverage on stakeholders' support
- Support adoption and implementation of standards

Promote high quality audit practices

Our key oversight activities such as registration, inspection and inquiry are aimed at ensuring audit firms and individual auditors are committed to delivering high quality independent audits while achieving their business objectives. Towards this, the goals pursued under this theme are:

- Enforce registration policy that promotes quality and capacity
- Drive quality audit practices through inspection and remediation of auditors
- Set the tone for quality through enforcement actions.

Influence financial reporting ecosystem

High quality financial reporting would only be achieved if all the key components in the financial reporting ecosystem are effective in playing their respective roles. Understanding this, the AOB focuses on influencing other important stakeholders to ensure audit quality remains high on their business agenda. The goals pursued are:

- Increase collaboration among stakeholders in the financial reporting ecosystem
- Promote research and discourse on audit quality.

Leverage on stakeholders' support

The effectiveness of the AOB would be enhanced if it could leverage on efforts of other stakeholders who share the same interest in enhancing the quality of financial reporting of PIEs. This includes co-operating with international counterparts as auditing itself has become a global affair. The AOB aims to achieve the following goals:

- Enhance the co-ordination of activities with other authorities in Malaysia and abroad
- Participate in international activities to gain knowledge and experience and promote confidence in Malaysian audit quality
- Obtain higher financial support from stakeholders.

Support adoption and implementation of standards

Auditing and ethical standards provide the baselines for high quality independent auditing to be achieved. In this respect, the AOB pursues the following goals:

- Ensure no significant gaps
- Promote substance over form implementation
- Facilitate the implementation of standards among audit firms.



1

PART

Promote High Quality Audit Practices



REGISTRATION ACTIVITIES

INTRODUCTION

In strengthening the continuity of influencing the audit practices, the AOB has dynamically heightened its audit oversight activities through the registration, inspection and enforcement functions. The envisaged outcome is for audit firms to deliver consistent quality audits through continuous capacity building and effective quality framework.

In this pursuit, AOB consistently reiterates that audit firms are required to comply with the application of international auditing and quality control standards adopted by the accountancy profession in Malaysia. Firms intended to register with the AOB are expected to demonstrate their ability to comply with relevant quality control and auditing standards.

REGISTRATION OF AUDIT FIRMS AND INDIVIDUAL AUDITORS

Chart 1 tabulates the number of registered audit firms and individual auditors from the establishment of AOB to 31 December 2014. The number of

Chart 1

5-year registration statistics of registered audit firms and individual auditors



Source: AOB

registered audit firms has decreased since 2010 from 83 to 52. The number of registered individual auditors has remained stable for the past five years with minimal reduction shown in 2011 and 2012, followed by a slight increase from 2013.

Table 1

Registration of audit firms and individual auditors as at 31 December 2014

Profile of audit firms registered	No. of audit firms	No. of individual auditors	No. of PIEs audited	% of market capitalisation
Partnerships with 10 or more partners	8	181	940	95.52
Partnerships with 5–9 partners	6	30	75	0.54
Partnerships with 2–4 partners	35	90	123	3.93
Sole proprietors	3	3	6	0.01
TOTAL	52	304	1,144	100.00

The concentration of clients remained with the top 10 audit firms which collectively audited 957 PIEs covering 98.6% of the market capitalisation of PLCs in Malaysia.

For the year under review, the AOB did not reject any application for registration.

RECOGNITION OF FOREIGN AUDIT FIRMS AND INDIVIDUAL AUDITORS

As at 31 December 2014, the AOB recognised foreign individual auditors from five foreign audit firms who audited six foreign incorporated companies which are listed on Bursa Malaysia.

The AOB placed reliance on the oversight frameworks of the foreign auditors' home countries when considering their recognition.

Among the considerations were whether these audit firms were required to comply with international auditing and quality control standards and/or whether they were subjected to regular inspection by their home audit regulators. It is part of the recognition process for foreign auditors to disclose specific findings from the inspection carried out by their home audit regulators.

Any adverse findings from the inspection carried out by their home audit regulators will affect recognition in Malaysia.

“It is part of the recognition process for the foreign auditors to disclose specific findings from the inspection carried out by their home audit regulators.”

The recognition framework will be further refined to encourage capacity building of foreign auditors to enhance their quality control framework to deliver consistent quality audits.

During the year, the AOB refused an application for recognition of a foreign audit firm pursuant to the failure to comply with the requirements of Part IIIA or any written notices or guidelines made under the *Securities Commission Act 1993* (SCA).

REVIEW OF COMPLIANCE WITH PARTNER ROTATION AND EQCR REQUIREMENTS

The AOB continues to stress the importance of compliance with partner rotation and Engagement Quality Control Reviewer (EQCR) requirements

Table 2

Profile of the foreign audit firms recognised by the AOB

Jurisdiction	No. of audit firms		No. of individual auditors		No. of PIEs audited	
	2014	2013	2014	2013	2014	2013
Singapore	3	5	6	12	4	4
Hong Kong	1	1	2	2	1	1
United Kingdom (UK)	1	1	2	2	1	1
TOTAL	5	7	10	16	6	6

being fundamental in ensuring that independence of auditors and audit quality are maintained. As a result of continuous monitoring and engagement with the audit firms, there has been improvement in the trend of non-compliance with partner rotation requirement.

In 2014, despite previous warnings, AOB took action against an audit firm as a consequential failure to comply with the partner rotation requirement. The audit firm also did not comply with section

31N(1) of the SCA which requires audit firms to be registered with AOB when acting as auditor.

The AOB will continue to monitor the firms' appointment of EQCRs for the PIEs to ensure compliance with the standard which requires an EQCR to be an individual with sufficient and appropriate experience and authority to act as an audit engagement partner. The EQCR must be a registered partner with AOB.

Box 1 STATISTICS ON TOP 10 AUDIT FIRMS IN MALAYSIA

In 2014, the AOB introduced a structured approach in data gathering with the intention of providing trend analysis in order to have a deeper understanding of the profession, support capacity building and facilitate discussion on audit quality among relevant stakeholders. The trend analysis would bring forth key messages in promoting audit quality in a bigger spectrum to the audit firms serving Malaysia's PIEs. The AOB gathered statistics from the top 10 audit firms which collectively audited 957 PIEs covering 98.6% of the market capitalisation of PLCs in Malaysia.

Audit fees vs salary costs

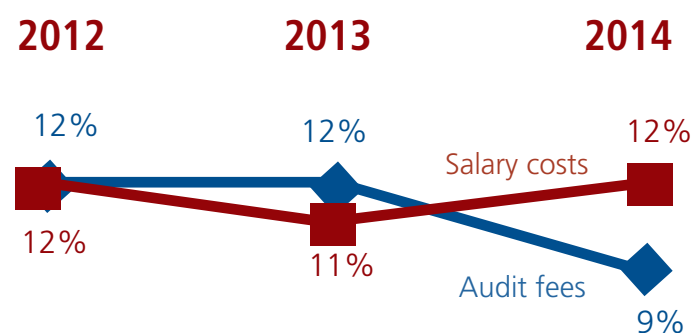
Chart 2 provides analysis on the correlation between the growth rates for the top 10 audit firms in Malaysia in terms of the statutory audit fees and salary costs. While the growth of audit fees has remained constant at 12.0% from 2012 to 2013, there was a reduction in 2014 in the growth rate at 9.0%. Comparatively, salary costs also remained constant for the past three years with a slight increase in 2014, in line with the increase in overall audit practice headcount by 6.6%.

The data supports the feedback that increase in salary costs is at a higher rate compared to the growth in audit fees. This continues to be one of the challenges for audit firms.

Training

In ensuring quality audit work, the AOB expects the firms' commitment and investment in the relevant infrastructure and training to support delivery of quality audit work.

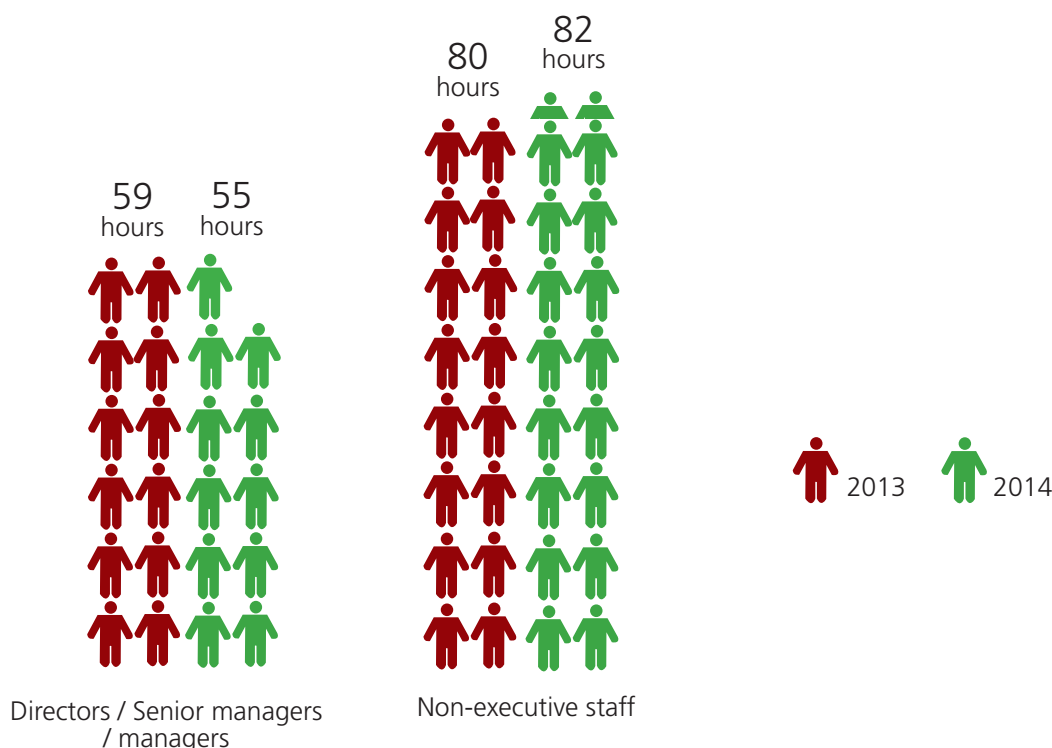
As required by the Malaysian Institute of Accountants (MIA), members must fulfil mandatory Continuing Professional Education (CPE) requirements of at least 120 CPE credit hours of relevant learning for every rolling three calendar year period. This is aligned with global standards and the International Federation of Accountants (IFAC), which averages to approximately 40 hours per calendar year basis. Based on the AOB's analysis, Chart 3 depicts that on average, staff of audit practice including partners and managerial levels spent more than MIA's mandatory CPE requirements on training.

*Chart 2***Growth rates in audit fees and salary costs**

Source: AOB Analysis – Top 10 audit firms in Malaysia

Chart 3

Average number of training hours spent

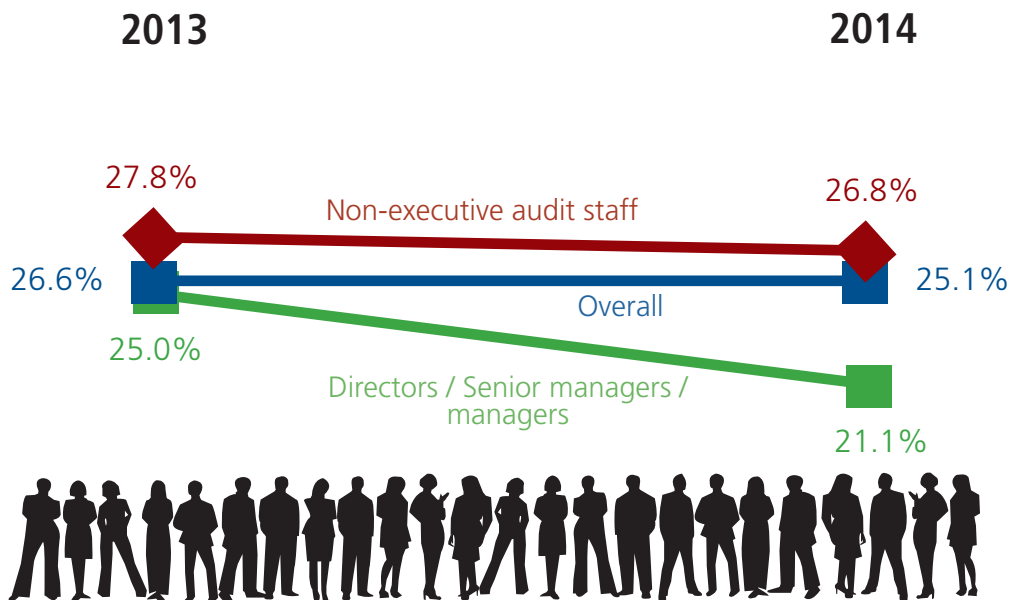


Source: AOB Analysis – Top 10 audit firms in Malaysia

While the AOB supports the firms' commitment in its investment in training, it is essential for audit firms to assess the effectiveness of such training. In delivering quality audit work, it is fundamental for audit firms to ensure the relevance, understanding technical and practical applications of the training.

Chart 4

Average audit staff turnover rate



Source: AOB Analysis – Top 10 audit firms in Malaysia

Human Resources: Talent Attrition

The AOB acknowledges the issue of lack of resources and talent retention as one of the main challenges faced in the audit practice. Chart 4 illustrates the average turnover rate for the top 10 audit firms in Malaysia, which show a reduction from 26.6% to 25.1%. Nevertheless, the average turnover from the non-executive remains the highest among top 10 audit firms.

Chart 5 shows the average ratios of audit staff to partner stood at 24:1 while non-executive audit staff to manager stood at 9:1 for top 10 audit firms in Malaysia for the year under review.

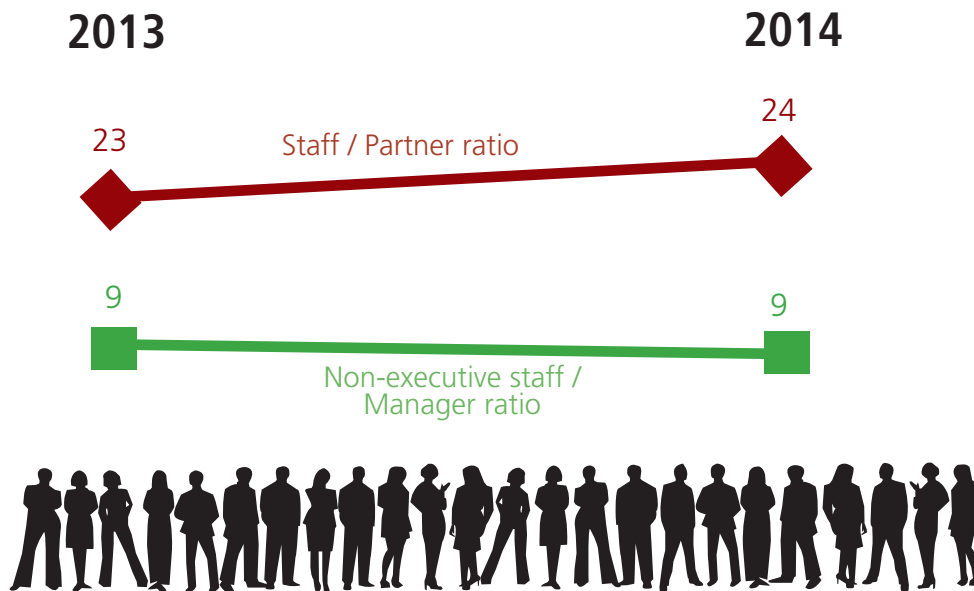
Human Resources: Experience

Chart 6 depicts that average years of experience for audit partners at 22 years while managers to directors level ranges between seven and 14 years. On the other hand, non-executive audit staff served an average of three years in the audit practice. The AOB detailed analysis revealed that six out of 10 audit firms fall within the range of average experience of 22 years for audit partners category.

It is important to have the right mix of skills and experience to ensure effectiveness of teams in carrying out an audit engagement.

Chart 5

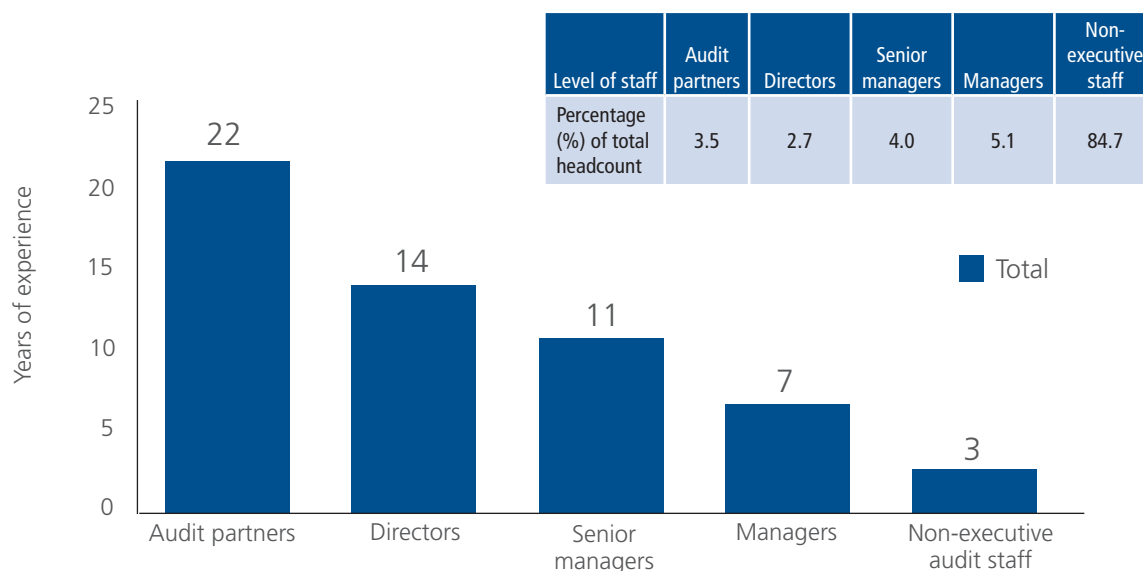
Audit staff to partner and non-executive audit staff to manager ratios



Source: AOB Analysis – Top 10 audit firms in Malaysia

Chart 6

Average years of experience for audit staff



Source: AOB Analysis – Top 10 audit firms in Malaysia

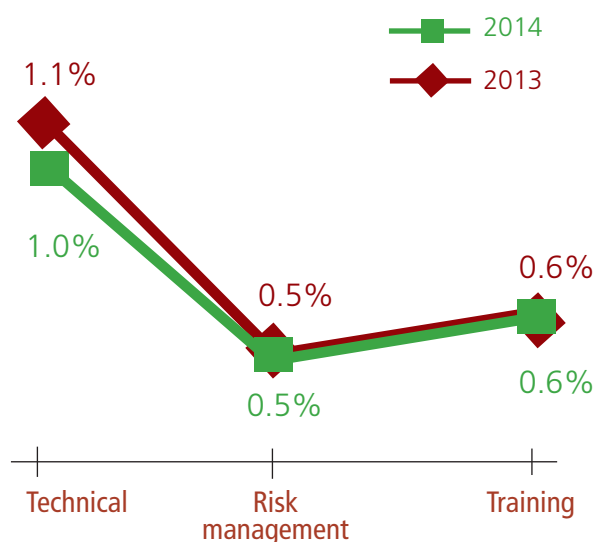
Monitoring and Quality Control

Audit firms are reminded to have a monitoring control framework in place to conform with the requirements of International Standard on Quality Control (ISQC) 1 *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements* and ensure its effectiveness.

Chart 7 illustrates the average ratio of quality control function over total headcount in audit practice of the top 10 audit firms. Resources at technical took up 1.1% of overall firms' headcount followed by training at 0.6%, a slight increase from last year. It is expected for all firms to place greater weightage on quality control function to support the delivery of audit quality work.

Chart 7

Average number of resources in quality control vs total headcount in audit practice



Source: AOB Analysis – Top 10 audit firms in Malaysia

Conclusion

Based on the three years analysis on the top 10 audit firms, salary costs continued to increase at a higher rate than the growth in the audit fees. The increase in salary costs is mainly due to the overall increase in headcount. Despite this increase, talent retention remains a challenge as there is no substantial improvement on the attrition rate based on the overall average turnover rate.

Further analysis on the training hours revealed that on average, staff of audit practice including partners and managerial levels spent more than MIA's mandatory CPE requirements on training. However, due to recurring findings observed in 2014 inspections, it is important for the audit firms to assess the effectiveness of training.

The concern over audit quality is further aggravated by the composition of audit personnel in the audit firm which is predominantly supported by employees with an average three years of experience. This was 85% of the overall headcount of top 10 audit firms. With the recurring deficiencies observed in 2014 inspection, an enhancement, includes a consideration to recalibrate resources in the monitoring and quality control function which would provide better support to deliver quality audit work.

INSPECTION ACTIVITIES

INTRODUCTION

Section 31V(1) of Part IIIA of the SCA mandates the AOB to conduct inspections of the auditors of PIEs to assess their degree of compliance with the relevant auditing and ethical standards as well as to assess the quality of audit reports prepared by them.

The inspections are followed by a report issued to the audit firm. The audit firm is required to identify root causes of the deficiencies highlighted in the inspection report and implement effective remedial action.

SUMMARY OF ACTIVITIES

The AOB conducts regular inspections annually of audit firms that have more than 10 partners and that audits more than 40 PIEs with a total market capitalisation of above RM15 billion (collectively referred to as 'the Major Audit Firms'). In 2014, six Major Audit Firms were identified in this category that collectively audited approximately 94% of the PIEs listed on the exchange, by market capitalisation.

Regular inspections of mid-tier audit firms and sole proprietors (collectively referred to as 'Other Audit Firms') are conducted on a pre-determined cycle which is risk-based. The AOB conducted regular inspections of four Other Audit Firms which included a re-inspection of one audit firm. In total, 10 audit firms collectively audited 957 PIEs covering 98.6% of market capitalisation of PLCs.



“ A firm review focuses on the review of an audit firm’s quality control systems and practices and the degree of compliance with the requirements of the ISQC 1.”

Regular inspections comprise firm and engagement level reviews. A firm review focuses on the review of an audit firm’s quality control systems and practices and the degree of compliance with the requirements of the ISQC 1. An engagement review aims to assess the degree of compliance with International Standards on Auditing (ISA) as well as compliance with the relevant ethical standards. For firms that have been inspected in the past, subsequent inspections of these firms would also include a follow-up review on the implementation of the firm’s remedial action plan.

Apart from regular inspections, the AOB continues to be actively involved with IFIAR and AARG to

Table 3

Inspection coverage

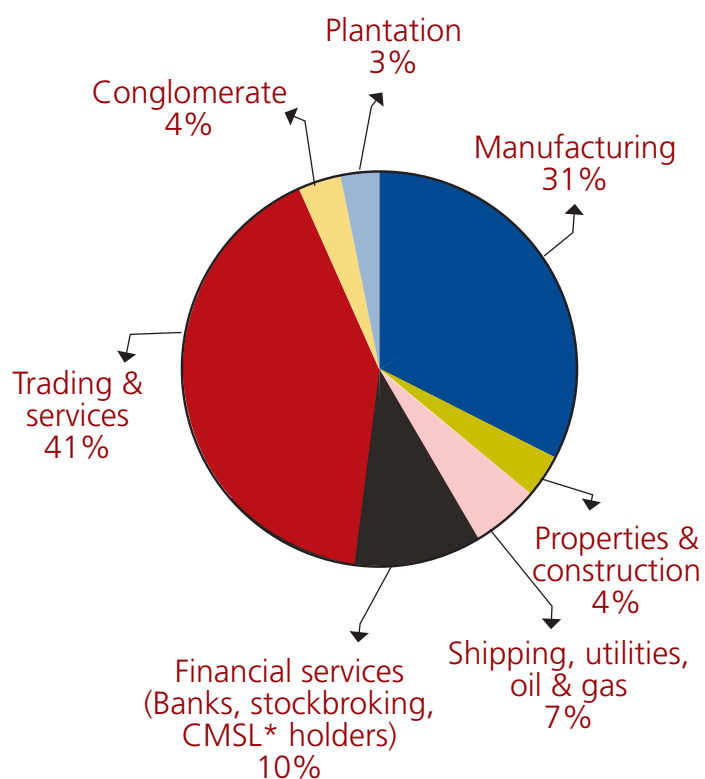
Profile of audit firms registered	Major Audit Firms		Other Audit Firms	
	2014	2013	2014	2013
No. of firms inspected	6	6	4	6*
No. of individual partners inspected	21	26	8	13*
No. of audit engagements inspected	21	25	8	13*

* includes one special inspection

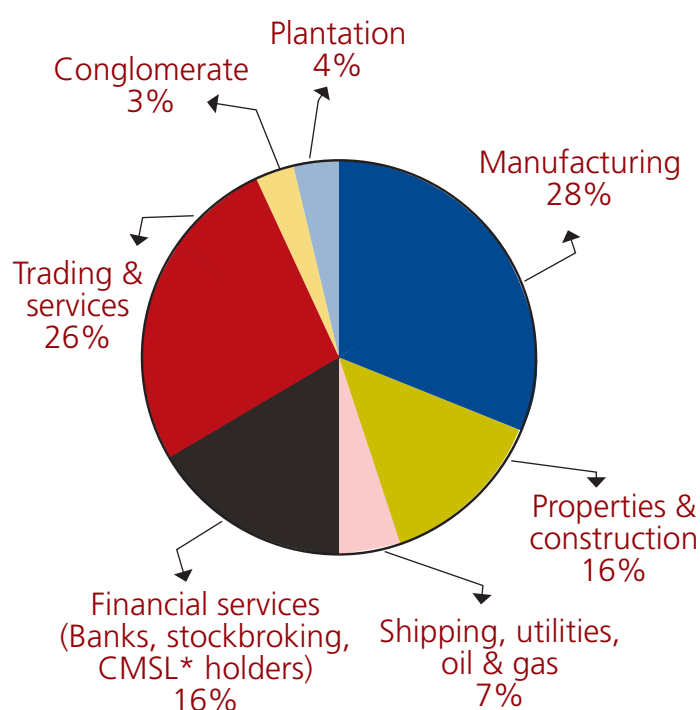
Chart 1

Analysis by sector of audit engagements

Engagement coverage by sector (2014)



Engagement coverage by sector (2010 to 2014)



* Capital Market Services Licence

AOB Local Engagements 2014



Dialogue session with the Top 10 Audit Firms on 29 September

In this dialogue, the AOB introduced a structured approach in data gathering which would facilitate analysis of industry trends as well as facilitate discussions about audit quality with the relevant stakeholders.



Sectorial dialogue session with the Other Audit Firms on 10 November

This dialogue served as an avenue for the AOB to provide regulatory updates as well as for two firms to share their experiences, key initiatives and best practices to deliver audit quality.

AOB International Engagements 2014



8th IFIAR Inspection Workshop from 10 to 12 March

Hosted by AOB in Kuala Lumpur, over 100 audit regulators from 35 jurisdictions attended this event to share technical skills, knowledge, practical experiences, relevant inspection findings and the identification of better practices in inspecting audit firms.



AARG meeting with the Big Four Firms from 15 to 16 May

During this meeting in Bangkok, Thailand, there was an exchange of information among AARG members (Malaysia, Thailand and Singapore) on the current and upcoming audit regulatory developments in their respective jurisdictions. The group also engaged with the Big Four Firms on topics relating to the monitoring processes, audit quality indicators used by the firms to measure improvements to audit quality and audit innovation.

keep abreast with latest regional developments as well as at international level. At the local level, the AOB continues to hold dialogues with both the Major Audit Firms and Other Audit Firms to promote key messages on audit quality as well as to obtain feedback on challenges faced by them.

OVERVIEW OF FINDINGS

The AOB noted incremental improvements where the number of recurring findings had reduced with respect to the engagement reviews involving re-inspected firms. However, consistency of

engagement performance among engagement partners remains a key challenge for most firms. AOB's review of engagement files revealed significant deficiencies. These deficiencies would impact the basis of audit opinion including any pervasive issue where the impact cannot be easily quantified. For three out of four of the Other Audit Firms inspected, there were gaps in respect of the firm's system of quality control policies and procedures.

Greater efforts are required to uphold audit quality. The AOB would like firms to be mindful of the following areas to drive audit quality (Table 4).

Table 4

Efforts to drive audit quality

Areas	AOB key messages
Tone at the top	<ul style="list-style-type: none"> • Remuneration of partners and staff should give due recognition to audit quality. • Establish and enforce a strong accountability framework to drive the right behaviour in partners to mitigate the risk of audit failure. The effectiveness of the firm's governance structure has to be assessed to capture the intended outcome. • Control over network branches to promote consistency of performance.
Talent recruitment, development and retention	<ul style="list-style-type: none"> • Continuously build capacity to ensure resource needs are met. • Invest in training to develop staff competency. • Be innovative and offer competitive remuneration to attract and retain the best talent commensurate with the work effort.
Technical competency in accounting and auditing	<ul style="list-style-type: none"> • Ensure partners and staff are kept abreast with latest changes in accounting and auditing standards. • Audit methodology should be reviewed and updated when there are changes to the relevant standards.
Acceptance of new audit client and engagement	<p>New audit client and engagement acceptance should give due consideration to:</p> <ul style="list-style-type: none"> • whether the firm has sufficient and competent resources; • client and audit risks; • firm's ability to comply with relevant ethical requirements; and • the ability to obtain the right fees.
Engagement performance	<ul style="list-style-type: none"> • Designed audit procedures should consider the appropriate nature, timing and extent that are based on and are responsive to the risk of material misstatement at the assertion level. • Ensure basis of sampling used is appropriate particularly when applying judgement to determine the number of samples for the testing. • Timely communication of pertinent and significant audit issues to the right level of audit client's management and those charged with governance. • Establish appropriate policies and procedures on consultation in respect of difficult and contentious matters. • Audit innovation to achieve audit efficiency should not be pursued at the expense of audit quality. • Portfolio management of PIEs should give due consideration to heightened risks particularly where the PIE is a regulated entity.
Internal monitoring system	<ul style="list-style-type: none"> • Monitoring procedures should be robust and rigorous. • Monitoring function should be adequately resourced with personnel who are technically sound and possess relevant experience. • Effectiveness of internal monitoring system should be assessed and fine-tuned.
Remedial action plan to address shortcomings in firm's system of quality controls	<ul style="list-style-type: none"> • Firm's remedial action plan should address actual root causes, implemented on a timely basis and monitored for its effectiveness.

Box 2 AUDIT INNOVATION

The climate change in the economic environment as well as the increasing trend in the growth of sophisticated and complex entities requires auditors to continuously review the current audit performance to ensure it remains relevant to address the specific risks associated with its clients' business environment. In addressing the challenges, the AOB recognises the practicality of audit innovation that is beneficial to the auditors in the following areas without compromising audit quality:

- Encourage improvements in efficiency, accuracy and reliability of the audit;
- Increase stakeholders' satisfaction; and
- Promote the application of best practices within the firm.

The following are examples of audit innovation observed by the AOB:

- Application of data analytics on multiple transaction line items to identify potential 'red flags' from the transactions entered by the PIEs;
- Use of various experts either internally or externally to support the audit conclusion reached;
- Establishment of a centralised team to assist audit teams with administrative matters such as following up of bank confirmations and debtor confirmations; and
- Greater use of audit tools and audit software to encourage real-time review by supervisors.

Where audit innovations involve a change in process and procedures, audit firms are constantly reminded to ensure proper communication and guidance to audit staff for better clarity on its application. Compliance with ISA and other relevant professional standards remains critical in meeting the intended objectives.

Notwithstanding, the key considerations with respect to the rationale on the changes of certain audit approach are crucial in providing clarity in their application. Some of the areas observed are as follows:

- Application of dual materiality;
- Encourage substantive audit testing which may cause a lack of understanding of controls surrounding a client's processes; and
- Reliance on audit procedures performed on balance sheet balances to address the key assertions for income statement items.

KEY OBSERVATIONS FROM FIRM LEVEL REVIEW OF MAJOR AUDIT FIRMS

Consistency of engagement performance and effectiveness of accountability framework

In general, the Major Audit Firms have to govern a larger pool of audit partners including those at branch offices and managing the behaviour of individual partners is made more challenging due to differences in individual character, values, priorities and risk appetites.

To drive the right behaviour and practices, Major Audit Firms have implemented a reward system based on the achievement of defined performance goals. Major Audit Firms have also introduced an accountability framework to hold engagement partners responsible for deficiencies relating to audit quality identified by external and internal reviews. The accountability framework introduces punitive measures that may be imposed on the audit partners. Some measures are financial penalties, removal from the audit engagements, imposition of additional training requirements and finally expulsion from the partnership.

The AOB is concerned about the increase in the number of inspected engagements with significant deficiencies in 2014 as compared to the prior year. For some Major Audit Firms, AOB observed that consistency of engagement performance among audit partners is still a concern including those at the branches. To ensure the quality and consistency of engagement performance among the partners in the Major Audit Firms, it is vital for such firms to reassess the effectiveness of their existing accountability framework to promote the right professional behaviour and practices among audit partners.

A strong and effective accountability framework is critical to foster the right behaviour and qualities in audit partners. For an accountability framework to be effective, firms should:

- Create the awareness on the types of punitive measures and circumstances that would trigger the imposition of such measures;
- Institute punitive measures that are sufficiently severe to serve as a strong deterrent; and
- Be consistent in the enforcement of the framework.

Rigour in the evaluation for the acceptance of new audit clients and audit engagements

Although the Major Audit Firms have established clear policies and procedures relating to the evaluation for the acceptance of new audit clients and audit engagements, the AOB observed numerous instances where the due process was not adhered to. Key observations are as follows:

- Instances where relevant approvals were not obtained in accordance with the firm's policies;
- Instances where the approvals for the acceptance of new audit clients and engagements were granted prior to completion of professional clearance checks and procedures to evaluate compliance with firm's independence policy; and
- Instances where the approvals for new client and engagement acceptance were untimely as they occurred after the 'consent to act' letters were issued to the PIEs or after the firm's appointment as auditor of the PIEs.

Audit firms are reminded to observe and apply appropriate client and engagement acceptance due process. Firms should be mindful that these processes are put in place as a key mechanism to protect the firms and assist them in identifying risks associated with prospective clients and engagements. The processes should not be taken lightly and viewed merely as an administrative burden.

Independence and ethics

The AOB noted instances where the MIA By-Laws (On Professional Ethics, Conduct and Practice) (MIA By-Laws) 5-year rotation requirement involving the EQCR was breached. In all cases, the affected Major Audit Firms detected the breaches prior to AOB inspection and a second EQCR was assigned by the firms to re-perform the work of the EQCR. Although this would mitigate the risk of familiarity threat, having two EQCRs is highly inefficient and would result in the firms incurring unnecessary time costs.

Compliance with the independence and ethical requirements reflects the auditor's ability to uphold integrity, objectivity and professional behaviour, which is fundamental in performing an audit. Audit firms are reminded to implement relevant measures to ensure that the partner rotation requirements are observed at all times.

Consultation process

At the Major Audit Firms, a consultative culture is encouraged which is supported by clear policies and an established framework for consultation. While consultation has taken place in some engagements that were inspected, AOB observed areas for improvement:

- Timing of consultation should be better managed. Consultations raised with the technical department should take place early during the audit rather than towards the end of the audit;
- More robust documentation should be maintained to support the firm's view on complex matters being consulted; and
- Adopted views or conclusions reached should be cohesive and consistent with the views of the audit profession.

Consultations on difficult or contentious matters are vital to mitigate the risk of an inappropriate audit opinion being rendered by the firm. Hence, it is critical for the consultation process to be properly conducted, approved in accordance with the firm's policies and robust documentation to be maintained within the audit engagement file.

Assembly of final engagement files

During the inspection of the Major Audit Firms, the AOB encountered instances where key audit documentation was not included in the final audit engagement files. Key audit documentation that is missing from the final assembled engagement files would pose a challenge for the audit engagement team to subsequently support the conclusions reached during the audit. In addition, the AOB noted that the network review involving one Major Audit Firm also identified that significant components of a PLC were not assembled in a timely manner.

Firms should reinforce the message on the importance of ensuring that all relevant audit documentation is completely assembled on a timely basis. Clear accountability should be established to promote tighter compliance with the firm's file assembly policies and procedures.

Effectiveness of firms' monitoring of system of quality control

In addition to annual cold reviews, some Major Audit Firms have also introduced hot reviews which are performed during the course of the audit engagement and prior to the issuance of the audit report. The hot reviews serve as a means for the firms to monitor the implementation of various improvement initiatives and allow upfront detection and remediation of shortcomings in the performance of audit.

Numerous significant deficiencies on the inspected engagements were observed. The AOB also noted instances of inconsistencies in the quality of engagement performance between the Malaysian head office of some Major Audit Firms and their branches across the country which may be attributed to insufficient supervision, monitoring and control of branches by the relevant head office.

Hence, Major Audit Firms need to ensure that their monitoring processes are rigorous and continuously evaluated for their effectiveness to ensure that audit quality is upheld throughout the firm.

For the engagement reviews to be effective, firms need to ensure that sufficient time and resources are allocated for this purpose. In addition, the reviewers should possess strong technical and industry knowledge.

KEY OBSERVATIONS FROM FIRM LEVEL REVIEW OF OTHER AUDIT FIRMS

Setting the right tone at the top

The AOB observed encouraging developments among the Other Audit Firms. For instance, the leadership of one small firm took the initiative to consult with firms that were previously inspected by the AOB to identify opportunities for improvement. In another firm that was previously inspected and was found to have major deficiencies, there was a change in the leadership. Dedicated resources with the support of the new managing partner were put in place to drive quality improvements.

Nevertheless, the tone at the top can further be improved in some Other Audit Firms. The AOB noted that while the majority of the firms inspected have implemented a process to evaluate the performance of partners, there is no clear and direct linkage between quality performance and partners' remuneration. Remuneration tended to be vastly business driven. Consequently, the performance appraisal process for partners may not provide sufficient incentives to foster quality oriented behaviour among the audit partners.

Firms should set the right tone at the top and demonstrate its seriousness to foster quality oriented culture by ensuring that the performance of high quality audits are given due recognition in performance evaluation, remuneration and promotion of partners and employees.

Client and engagement acceptance process

Some Other Audit Firms are cognisant of their competence and capabilities and hence, are not keen to increase their number of PIE clients. On the other hand, there are some firms that are aggressive in growing the number of PIE clients of whom are attained through mergers. The Other Audit Firms are reminded to apply sufficient rigour in their acceptance evaluation process and to be mindful of underlying audit risks or issues that may not be apparent on the surface. In deciding whether to accept a new audit client, due consideration should be given on the possible risks, capacity, competence, audit fee and the ability of the firm to comply with relevant ethical requirements.

Firms in their efforts to grow revenue should not secure business without giving due consideration to the actual costs and audit risks involved to carry out a quality audit.

Emphasis on training

The AOB noted that training on the recent changes to the accounting standards have not been carried out by some Other Audit Firms. Further, there are also firms that fail to monitor the attendance of their employees at training sessions. Consequently, there is a risk that employees who have not attended the relevant training are put on audit assignments before acquiring the necessary knowledge and skills set required to perform their audit engagements effectively, in accordance with professional standards.

Results of a joint survey titled 'Optimising Talent in Accounting Firms' conducted by the AOB and the Association of Chartered Certified Accountants (ACCA) in 2012 revealed that a steep learning curve is one of the key retention factors. Firms should recognise the important role of training not only to enhance the competency of its employees to deliver quality audits but also to serve as a firm's value proposition to retain them. Training sessions should encompass not only accounting and auditing but also soft skills.

Engagement performance

The AOB noted the following shortcomings in respect of the Other Audit Firms policies and procedures relating to the ISQC 1 element of engagement performance:

- **Firm audit methodology and audit work programme**
The AOB observed instances where an outdated audit manual, an outdated accounting standards disclosure checklist and a sampling worksheet were used for substantive testing thereby not meeting the requirements of ISA.
- **Consultation**
The AOB noted that some firms have a policy that requires consultation for 'any significant, difficult and contentious issue'. However, these firms have not provided definition or guidance as to what would constitute 'significant, difficult or contentious issue'. This raises the concern that audit teams may not be appropriately guided on matters that should be escalated for consultation. In another instance, the AOB observed that consultations are informal and not documented. This is not in compliance with the requirements of ISQC 1 and ISA which require that the nature of consultation, scope and conclusions reached are documented.

- **Assembly of final engagement files**

Some firms have not established procedures for the assembly of final audit engagement files within 60 days from the date of the audit report. Where policies and procedures have been established for file assembly, AOB observed instances of non-compliance where the audit engagements files were only assembled after 60 days from the date of the audit report.

- **Confidentiality of engagement documentation**

During inspection, the AOB observed that there was no established procedure for proper destruction of audit engagement files at the end of the retention period to safeguard confidentiality of engagement documentation. There was also an instance where the file storage room was shared with its other business entity which raised the concern of inappropriate access to audit engagement files by non-audit staff.

Firms should institute a process for the periodic review of their audit methodology to ensure that they remain current with the latest auditing and accounting standards. The consultation process should be enhanced and rigour of documentation should be emphasised to the audit team. In addition, firms should also ensure that audit engagement files are assembled in a timely manner and confidentiality of engagement documentation is safeguarded.

Monitoring quality control policies and procedures

The AOB continues to observe gaps in some of the Other Audit Firm's monitoring of their system of quality control as highlighted below:

- Firm and engagement level reviews were not performed although required by the firm's policies and procedures;
- Monitoring procedures were limited to review of engagements. There was no requirement within the firm's policy for firm level review to be performed to assess whether the firm's system of quality control is operating effectively; and
- AOB's review of an engagement that was subjected to a firm's own internal monitoring review indicated the lack of sufficient robustness and rigour.

Firms are reminded to ensure that its monitoring processes are appropriately designed and implemented effectively as they would be crucial in providing reasonable assurance that the firm's policies and procedures relating to the system of quality control are relevant, adequate, and operating effectively.

KEY OBSERVATIONS FROM ENGAGEMENT LEVEL REVIEW OF MAJOR AUDIT FIRMS AND OTHER AUDIT FIRMS

Inspection activities continue to be essential in fostering high quality independent audits of PIEs and promoting the integrity of the auditing profession. Although firms were committed to achieving audit quality, certain audit areas continue to be a challenge for both Major Audit Firms and Other Audit Firms.

Effectiveness of Engagement Quality Control Reviewer Process

The EQCR provides check and balance to the audit process through his or her independent and objective evaluation of key judgement areas and significant matters and assessment of whether related audit procedures and documentation support the conclusions reached. In this area, the AOB has concerns over the effectiveness of the engagement quality control review process in view of the deficiencies identified in the engagements for both Major Audit Firms and Other Audit Firms by AOB. This may be attributed to the EQCR lacking the relevant industry knowledge, insufficient time spent on the audit engagement as well as the lack of their involvement throughout the duration of the audit engagement.

The effectiveness of an engagement quality control review process is dependent on the competency of the reviewer, the timeliness and extent of his or her involvement in the audit engagement. Accordingly, EQCRs are reminded of their professional duty to apply appropriate professional scepticism and provide relevant challenge on the key areas of judgement and significant matters.

While engagement partners are primarily responsible for the performance of the audit engagement, this does not absolve an EQCR from being jointly accountable in the event of audit failure. Hence, firms are encouraged to establish an accountability framework for reviewers to ensure due care and diligence.

Common deficiencies for Major Audit Firms and Other Audit Firms

The following are the significant deficiencies observed for both Major Audit Firms and Other Audit Firms:

- Asset impairment;
- Audit of inventory; and
- Sampling

It is important to note that except for the audit of inventory, the other two deficiencies above have been highlighted by the AOB in prior years. The recurrence of issues raises the concern of the firms' efforts in addressing the root causes effectively and promptly.

Asset impairment

The common inspection findings observed are as follows:

- Indicators of impairment were not identified and addressed;
- Intangible assets with indefinite useful lives were not subjected to annual impairment assessment;
- Lack of verification and challenge of management's assumptions used in their cash flow projections; and
- Undue reliance of and lack of professional scepticism in management representations.

The AOB continued to observe findings in this area especially during the review of engagements with complex environments that carried higher risks of asset impairment. Examples of higher risk of asset impairment are loss making entities and entities with low asset turnover compared to industry average. The AOB had reiterated in the previous year's annual report of the need for auditors to critically evaluate the value-in-use cash flows prepared by management for the purpose of impairment testing. Firms should professionally challenge the key assumptions used such as forecasted sales volume, selling prices, cost and discount rates applied based on the prevailing economic climate rather than finding justifications to support management's assumptions. Auditors should stress test value-in-use computations, including performing adequate sensitivity analysis with levels of professional scepticism.

When reviewing the cash flow projections prepared by the audit clients, firms are reminded of the need to apply professional scepticism in questioning the reliability of evidence used as well as critically challenge the assumptions which support the impairment assessment. Where small 'headroom' exists to support the recoverable amount, the risk of material misstatement is heightened.

Audit of inventory

The AOB inspected a number of PIEs that were involved in manufacturing and trading activities. These PIEs would normally hold significant levels of inventories. The findings observed are as follows:

- Failure to address the existence and valuation of certain types of inventories;
- Inappropriate testing of costing model adopted by the PIEs;
- Insufficient evaluation of obsolescence and slow moving inventories;
- Variances between final inventory records and physical count samples not investigated; and
- Performing test of details based on reports not tested for reliability and accuracy.

The majority of the above findings were prevalent in Other Audit Firms as a result of insufficient rigour in planning and risk assessment procedures to understand and evaluate the appropriate level of evidence required for the intended audit procedures. For Major Audit Firms, there were shortfalls relating to the implementation and review of designed audit procedures particularly on valuation testing as well as inventory obsolescence. There were also instances where reliance was placed on costing reports provided by management without further verification.

Depending on the nature of the business entity, inventory may be a high risk account balance. The audit procedures on inventory should include the following:

- Understanding of business operations and market demand of the entities' products;
- Understanding of industry development and climate change of economics that affects the entities; and
- Understanding of the management process of identification of slow moving inventories including the nature of the inventories to assess for obsolescence.

Sampling

The findings observed from AOB's 2014 inspections are as follows:

- Inappropriate basis of sampling;
- Potential exceptions from test samples were not identified and properly evaluated;.
- Incorrect projection of potential misstatements; and
- Untested population

The AOB continues to observe the tendency of certain firms to select test samples based on a monetary threshold using the materiality set for the audit engagement. As the basis for selection was not representative of the population being tested, the results of such specific item testing cannot be used to project across the remaining untested population. Consequently, due to the lack of any other substantive testing or related test of controls performed, the appropriateness of the remaining untested population, could not be ascertained.

The AOB observed that in spite of the support of extensive methodologies providing relevant sampling guidance (including computerised sampling tools), there were still instances of lack of clarity with respect to the basis of sampling used, for example when determining the minimum or maximum number of samples for the testing.

Key considerations in sampling in accordance with ISA 530 *Audit Sampling*:

- Firms need to consider the characteristics of population from which the sample will be drawn;
- Sample items are selected in a way that each sampling unit has a chance of selection;
- Firms shall investigate the nature and cause of any deviations or misstatement identified and evaluate the possible effect on other areas of the audit; and
- For misstatements identified during the performance of test of details, firms shall project the misstatements found in the sample of population.

Common deficiencies for Major Audit Firms

For Major Audit Firms, the majority of AOB's engagement selection mainly involved PIEs that operate in complex and sophisticated environments such as banking, conglomerate and multiple construction contract activities. The following are the significant deficiencies observed for Major Audit Firms:

- Test of controls which has implication on revenue recognition;
- Reliability of information provided by management's experts; and
- Group audit.

Test of controls

The findings observed from AOB's 2014 inspections are as follows:

- Key assertions were not addressed in the testing performed;
- Samples selected were duplicated or not replaced when found to be inadequate, leading to insufficient samples tested to achieve the testing objective;

- Completeness of population for sample selection purposes was not addressed;
- Controls concluded as ineffective but was wrongly applied as effective when subsequently performing test of details; and
- Exceptions from test samples were not properly evaluated.

The AOB observed instances where the procedures designed for controls testing of key account balances were not representative of the actual performance or directly related to the assertions. For certain engagements, there were instances of duplicated samples or invalid samples that were not replaced. Consequently, the effective number of samples tested was insufficient to achieve the intended objective.

The AOB has concerns that certain firms placed high level of reliance on the PIE's group-wide control process resulting in a lack of substantive testing performed on certain material account balances or transactions where the assigned risk was low. The AOB reminds firms to comply with ISA 330 *The Auditor's Responses to Assessed Risks* requirements on substantive procedures where regardless of the assessed risks of material misstatement, auditors are obliged to design and perform substantive procedures for each material class of account balance, transactions, and disclosure.

Where the firms engaged its information technology auditors to perform review and testing on key IT related controls, effective co-ordination and communication between the financial and IT auditors is crucial to achieve the intended audit objectives.

Reliability of information provided by management's experts

The findings observed from AOB's 2014 inspections are as follows:

- No evaluation of the competence, capabilities and objectivity of the experts;
- Lack of understanding of the experts' work and the relevance of the methods used; and
- Insufficient evaluation of appropriateness and sufficiency of the experts' work.

The tendency to rely on the expert's work by auditors is normally dependent on the complexity of the entity's business. For instance, where reliance was placed on the work performed by a professional valuer, the AOB observed that certain Firms did not evaluate the competence, capabilities and objectivity of the expert. Further, there was lack of supporting evidence and clarity as well as ambiguity on the relevance of methods and assumptions applied by the expert to arrive at the valuation amount. As a result, there was no audit procedure performed to evaluate the appropriateness of the valuation amount given by the valuer. Firms need to consider whether they should engage and communicate with the valuer to obtain an understanding and comfort on the methods used by the professional valuer.

Based on ISA 500 *Audit Evidence*, where reliance is made using the work of the management's expert, the auditors are required to perform the following:

- Evaluate the competence, capabilities and objectivity of that expert;
- Obtain an understanding of the work of that expert; and
- Evaluate the appropriateness of that expert's work as audit evidence for the relevant assertion.

Group audit

The findings observed from AOB's 2014 inspections are as follows:

- Insufficient evaluation of the works performed by the component auditors including the tendency to rely on the works performed particularly when those component auditors were within the local Firm's own network;
- Consistency in the application of planned audit procedures by the component auditors;
- Lack of follow up on matters highlighted to the component auditors during the review of the component auditors' working papers; and
- Lack of follow up on reporting deliverables required by the group auditors.

The AOB has concerns on the effective co-ordination and communication between group and component auditors especially if the component auditors are not from the same network firms. In contrast, where the component auditors were from the same network, there was a tendency for the group auditors to merely rely on the works performed without further evaluation on the sufficiency of the works performed by the component auditors.

Key challenges:

- Auditing components residing in certain jurisdictions are increasingly more difficult as the relevant authorities are enforcing more stringent requirements that would restrict access to information of the entities; and
- Addressing the intervening period when auditing components with a different financial year-end may result in audit inefficiency as co-operation from the component auditors may not be forthcoming.

Common deficiencies for Other Audit Firms

For Other Audit Firms, significant deficiencies observed relates to the following audit areas:

- Revenue recognition;
- Presentation and disclosure; and
- Third party confirmation.

Revenue recognition

The findings observed from inspections are as follows:

- Insufficient evaluation of potential risk arising from revenue and purchases made from the same contract parties;
- Substantive analytical procedure not performed in accordance with ISA requirements; and
- Shortcomings in the performance of revenue cut-off procedures.

The AOB observed the lack of assessment performed to evaluate certain significant revenue and purchase transactions entered with the same contract parties where in substance it may contain a principal-agent relationship. For certain transactions that were evaluated in prior year audits, firms should ensure that the evaluation is properly carried-forward to form part of the current year audit working papers. Firms also should consider re-evaluating their assessment to determine the continued relevance of the conclusion reached in the past.

Applying substantive analytical review as the primary procedure that meets the requirements of ISA 520 *Analytical Procedures* remain an area of challenge. For Other Firms, the AOB continues to observe that the substantive analytical review was performed in the form of variance analysis which is limited to comparing the current year figures with the prior year.

ISA 240 The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements specifies that auditors need to evaluate the relevant type of revenue, revenue transactions or assertions that carried risk of material misstatements based on presumption that there are risks of fraud in revenue recognition. Where auditors conclude that risk of material misstatement due to fraud is not applicable, its conclusion should be properly supported and appropriately documented in the working papers.

Presentation and disclosure

Findings observed from inspections:

- Non-compliance with relevant Malaysian Financial Reporting Standard (MFRS) disclosure requirements; and
- Key presentation and disclosure items in the audited financial statements were not verified and evaluated, leading to incorrect presentation and disclosure.

There is a persistent issue with the lack of audit procedures performed to address the presentation and disclosure assertion of certain key account balances or class of transactions.

The following are areas of specific disclosures in the financial statement that were observed by AOB:

- Appropriateness of disclosure of information about major customers in accordance with MFRS 8 *Operating Segments*;
- Appropriateness of age classification analysis for financial assets that are either past due not impaired or individually impaired as at year end in accordance with MFRS 7 *Financial Instruments: Disclosures*;
- Appropriate offsetting of asset and liability in accordance with MFRS 101 *Presentation of Financial Statements* and MFRS 132 *Financial Instruments: Presentation*; and
- Appropriate disclosure of fair value for investment properties carried at cost model in accordance with MFRS 140 *Investment Property*.

Third-party confirmations

The findings observed from inspections are as follows:

- Lack of follow up action on third party audit confirmation responses;
- Reliance on photocopies, scanned and faxed copies of confirmation without further verification of its reliability; and
- Insufficient evaluation of potential misstatements identified based on the confirmation reply.

The AOB is extremely concerned on the findings surrounding third party confirmations especially how certain Firms manage and maintain its control over external confirmation requests. While there were alternative procedures performed in the absence of a confirmation, in most instances, such procedures did not necessarily address the intended objective of the assertions.

Key considerations to ensure effectiveness of the confirmation procedures:

- Early distribution of confirmation to third parties;
- Timely follow-up on outstanding confirmation response;
- Timely evaluation of potential discrepancies or unreconciled items from the confirmation replies; and
- Establish a structured documentation on circularisation and follow-up process for the confirmation request.

REMEDIATION

Overall progress

The AOB observed that the number of recurring findings on five out of seven re-inspected firms has reduced. This is a positive development that has culminated from the various efforts undertaken by these firms over the years.

Some of the larger firms continue to highlight partner workload as a root cause of the deficiencies identified by AOB during the inspection of the firm. Heavy partner workload stems from limited number of partners servicing a larger number of PIE clients and heavy concentration of PIEs with similar financial year ends. The consequential effect would be partners spending less time to review and supervise audit engagements. Efforts undertaken to address this includes promoting new audit partners and re-balancing of client portfolios among the partners to achieve a more equitable distribution of workload. Some firms are also withdrawing from clients that pose risks beyond the risk tolerance of the firm as well as low recovery audit engagements. To a lesser extent, some firms have been successful in convincing some of their PIE clients to change their year-end.

For smaller firms, there continues to be a need for the partners and employees to enhance their technical competence in accounting and auditing. Firms' efforts mainly relate to training and enhancements of

the audit methodology and monitoring framework. Firms should address the root causes of the deficiencies identified rather than just focus on the symptoms. In addition, Firms should continuously assess the effectiveness of the remedial plan and where relevant, enhance it appropriately in its efforts to minimise or eliminate recurring deficiencies. The AOB acknowledges numerous good practices by several audit firms that have leveraged on their internal monitoring process to track and measure the consistency of quality practices within their respective firms.

Recurring findings

It is encouraging to note the overall reduction in recurring findings during the inspection on engagement review for Major Audit Firms and one Other Audit Firm during the year. The recurring findings observed are as follows:

- Impairment assessment of assets/goodwill;
- Revenue cut-off procedures;
- Sampling and untested population;
- Application of substantive analytical procedures;
- Follow-up on confirmation procedures;
- Testing the reliability of system generated reports;
- Identification and evaluation of related parties and related-party transactions; and
- Untimely archival of key evidences in audit working papers.

While there were reductions in the number of recurring findings from the engagement reviews, the AOB still has concerns on the overall effectiveness of some firms remediation and monitoring process. Greater efforts on communication and effective training to relevant staff may address this area of weakness.

Moving forward, if Firms fail to take relevant remedial measures, AOB will publish the inspection report in the public domain.

Root causes

Over the years, the AOB observed the tendency of the firms to signify the lapses in documentation as the cause for the identified deficiencies to curtail the significance of the matters. The AOB re-emphasises the importance for the firms to take ownership of identifying actual root causes in order and acknowledging the root causes to develop a meaningful remediation plan. Consistency of performance among individual partners remains a challenge that the various firms' leadership need to address through effective governance policies and procedures.

AOB's analysis on root causes to audit deficiencies

The following are the main root causes that continue to be observed based on AOB's analysis on both Major Audit Firms and Other Audit Firms:

- Inadequate efforts by the firm's leadership to drive the messages on audit quality;
- Lack of timely involvement and insufficient supervision and direction by the engagement partners due to the heavy workload;
- Insufficient resources due to high attrition rate;
- Ineffective monitoring and communication process;
- Lack of understanding of the business and industries of the audit clients;
- Lack of technical competencies in both accounting and auditing;
- Lack of application of professional scepticism in applying professional judgement;
- Lack of technical support to safeguard audit quality, which includes consultation process and internal monitoring review; and
- Ineffective EQCR.

CONCLUSION

While the AOB continues to see the firms' ongoing efforts in improving audit quality, inspection findings still indicate that greater efforts are still required.

The AOB will continue to stress the significance of tone at the top to drive audit quality initiatives as well as promote consistency in engagement performance among audit partners. To promote the right partner attitude and behaviour, it is imperative for firms to enforce a strong and effective accountability framework.

Although there have been improvements in recurring deficiencies in Major Audit Firms, the sheer breadth and complexity of portfolio of PIEs continue to reveal lapses in judgement and planning. This may be due to assumptions made in identifying potential issues and managing the related audit risks. Consequently, the number of engagements with significant deficiencies in 2014 increased compared to the previous year.

Control over branch network and consistency of engagement performance remain an issue. Thus, effective portfolio management and distribution among the branches and engagement partners are some of the key factors to achieve the desired consistency level. In addition, firms need to ensure the training provided and planned for employees is effective and adequate to acquire the necessary knowledge and skill to perform the audit assignment effectively.

It is encouraging to note the increased number of formal consultations for the Major Audit Firms which is consistent with the continuous changes of accounting standards as well as the more sophisticated and complex business models of audit clients. Consultation helps to promote audit quality and improves the application of professional judgement. Thus, it is important for auditors to ensure the consultation process has considered sufficient evaluation of relevant facts and details to support the conclusion reached. On the other hand, where impact of changes of certain accounting standards or potential accounting issues are significant, firms should communicate such developments in a timely manner to the audit clients to manage any unnecessary delay in the performance of the audit that would result in audit inefficiencies and unintended consequences.

The AOB will continue to engage and communicate with the firms to identify methods and drivers to

improve audit quality. This includes audit innovations that would provide audit efficiency while maintaining audit quality.

For the Other Audit Firms, the speed of improvement needs to be accelerated. There are some firms that require significant improvement. AOB continues to remind the fundamental need for having the right training, infrastructure and technical competence to support audit quality. Continuous upgrade in technical knowledge and understanding the application, in view of rapid development in accounting standards is a must for all partners and professional staff. This is still lacking in majority of Other Audit Firms.

Due to the uncertainty of the economic environment, auditors at all times should maintain the appropriate level of professional scepticism during an audit. Auditors should heighten professional scepticism in certain areas that are susceptible to fraud and manipulation such as revenue, cash and bank balances. Auditors need to design the audit procedures considering the nature, timing and extent that are responsive to manage the associated risks. In this respect, the EQCR also has an important role to play to ensure that the audit engagement team has appropriately addressed all significant and high risk audit matters.

Moving forward there will be continuous interaction between AOB and the audit firms to discuss drivers of audit quality, and sharing of best practices, encourage positive changes in behaviour and promote culture in order to embrace audit quality.

“... auditors should heighten professional scepticism in certain areas that are susceptible to fraud and manipulation such as revenue, cash and bank balances.”

ENFORCEMENT ACTIVITIES

INTRODUCTION

Independent auditors play a critical role in enhancing the reliability of financial information by attesting as to whether the financial statements prepared by management fairly represent the financial position and past performance of PIEs in compliance with accepted accounting standards.

Effective oversight of independent auditors is important for the reliability and integrity of the financial reporting process. The rigour of the audit process as well as the quality and reliability of audited financial statements are crucial in the corporate governance framework.

There is no factor more integral to market confidence than effective enforcement. AOB has in place a robust enforcement mechanism with sufficient safeguards to ensure that fairness and justice prevails. From April 2010 until December 2013, a total of eight auditors were sanctioned for failure to comply with the recognised auditing standards in Malaysia i.e. ISA in the performance of their audit of the financial statements of PIEs and failure to comply with the ethical and professional standards of the MIA By-Laws. In 2014, action was taken against two auditors and one audit firm.

The principles of proportionality, efficiency and achieving the desired outcome continue to be essential to the strategic enforcement approach adopted by AOB. In determining the type of sanction

that is imposed on any contravention or breach, AOB takes into account the nature and seriousness of the offence, previous regulatory record and other aggravating or mitigating factors. Among the matters considered by AOB is the impact of the contravention on the integrity of the profession, the capital market as a whole and the impact of the breach on the confidence and reliability of audited financial statements of the PIE in question.

From an enforcement perspective, 2014 was an interesting year with AOB bringing significant action against an audit firm that was widely reported in the media. For the very first time AOB took action against an audit firm and prohibited it from accepting any PIE as a client for a period of 12 months. The audit firm was also imposed a monetary penalty of RM30,000. In the past, the sanctions exercised were confined to a reprimand and the highest monetary penalty imposed on an auditor was RM10,000.

Effective deterrence requires strong signalling to the profession and market that non-compliance to regulations and standards will not be tolerated. It is that clear signal that creates powerful incentives to bring about audit quality changes for market confidence.

AOB expects audit firms to adhere strictly to the laws and regulation and will not hesitate to take action against any registered individual or audit firm for non-compliance.

SANCTIONS IMPOSED IN 2014

The audit firm was sanctioned for failure to comply with regulations, guidelines and other applicable law that govern activities carried out by the audit firm and failure to comply with auditing and ethical standards in Malaysia. With respect to the ethical standards, the audit firm breached requirements in the MIA By-Laws which deals with independence,

more specifically the key audit engagement partner rotation requirement.

With respect to the sanction against the two individual auditors, the non-compliance with the ISA involved among others, failure by auditors to perform the procedures to obtain sufficient appropriate evidence to support the audit opinion. Details of the sanctions are in Table 5.

Table 5

Efforts to drive audit quality

No.	Nature of misconduct	Parties involved	Brief description of misconduct	Action taken	Date of action
1.	Breach AOB's registration condition imposed under section 31O(4) of the SCA.	Chan Kee Hwa Partner of Khoo Wong & Chan who was the engagement partner in the audit of a PIE for the financial year ended 31 March 2011.	Failure to comply with certain requirements of ISA in discharging professional duties in the performance of an audit of the PIE.	Reprimand	18 February 2014
2.	Breach AOB registration condition imposed under section 31O(4) of the SCA.	Lim Kok Beng Partner of Ong Boon Bah & Co, engagement partner in the audit of a PIE for the financial year ended 30 June 2011.	Failure to comply with certain requirements of the ISA in discharging professional duties in the performance of an audit of the PIE.	(i) Reprimand; (ii) Penalty of RM10,000.	
3.	Breach AOB registration condition imposed under section 31O(4) of the SCA.	Wong Weng Foo & Co	(i) Failure to comply with section 31N(1) of the SCA which requires audit firms to be registered with AOB when acting as auditor; and (ii) Failure to comply with the MIA By-Laws requirement which relates to independence of an auditor.	(i) Prohibit the Audit Firm from accepting any PIE as client for 12 months; and (ii) Monetary penalty of RM30,000.	30 May 2014

Note: On 5 June 2014, Wong Weng Foo & Co appealed to Securities Commission Malaysia (SC) against the decision made by AOB. On 26 June 2014, the SC rejected the appeal. The prohibition on the audit firm to accept any PIE as its client for a period of 12 months took effect from 30 June 2014.



PART 2

Influence the Financial Reporting Ecosystem and Leverage on Stakeholders' Support



INFLUENCE THE FINANCIAL REPORTING ECOSYSTEM AND LEVERAGE ON STAKEHOLDERS' SUPPORT

INTRODUCTION

The AOB recognises that high quality financial reporting by PIEs together with rigorous audit is a key differentiator in enhancing confidence in the market as well as attracting capital and potential investors to Malaysia. Understanding this, one of the AOB's strategic framework themes is to influence the financial reporting system.

The AOB conducts, participates and shares views in various stakeholder engagements to promote high quality financial reporting and audit practices. These engagement sessions on the local, regional and international front involve regulators, audit firms, accounting professionals, directors and academicians.

ASEAN AUDIT REGULATORS TACKLE REGIONAL AUDIT QUALITY ISSUES

The AARG's 4th annual meeting was held in Bangkok, Thailand from 15–16 May 2014. The group comprises Singapore's Accounting and Corporate Regulatory Authority (ACRA), AOB, and Thailand's Securities and Exchange Commission. The Accountant and Appraiser Supervisory Centre of the Ministry of Finance, Indonesia, participated for the first time as observers.

The meeting commenced with ACRA sharing the results of the Second IFIAR's Inspection Findings

Survey, followed by individual jurisdictions providing snapshots of their regulatory initiatives. The AOB shared updates on the strengthening of the accountancy profession in Malaysia, which is being done through the Committee to Strengthen the Accountancy Profession (CSAP).

From a global perspective, representatives from the Regulatory Working Group (RWG) of the Global Public Policy Committee (GPPC) discussed their projects on 'Future Role of Audit' which was undertaken by the Audit Panel.

During the Group Discussion session, AARG members discussed plans to improve financial reporting, audit quality in the region, potential areas of collaboration between regional firms and audit regulators as well as opportunities and challenges potentially faced with the implementation of the forthcoming expended auditors report.

The AARG meeting ended with engagements with individual leadership of the regional Big Four Audit Firms. Among the issues highlighted were, the review of audit quality issues identified from the audit firm's quality reviews, analysis of root causes of audit deficiencies as well as the firms' measurement on the effectiveness of remediation action plans. The dialogue also discussed indicators used to measure improvements to audit quality, audit innovation and productivity initiatives embarked by the Big Four Audit Firms.

Box 3 SUPPORTING IFIAR INITIATIVES

IFIAR Inspection Workshop

For the first time in the ASEAN region, Malaysia through AOB hosted the 8th Inspection Workshop of IFIAR. This event, which was held in Kuala Lumpur in March 2014, was attended by over 100 delegates from 35 IFIAR member jurisdictions.

The keynote address entitled 'The Challenging Road Towards Normalisation' was presented by Alex Ng, Chief Investment Officer, Asia Pacific, BNP Paribas Investment Partners Asia, who provided an overview of the current global macroeconomic situation and what the future might hold, along with current and emerging issues relevant to audit inspections.

Three plenary sessions focused on the following areas:

- 2nd IFIAR Survey on Inspection Observations;
- GPPC Working Group Agenda; and
- Risk-based Inspection Approach.

The workshop also provided IFIAR members from various jurisdictions the opportunity to exchange information and ideas on practical issues related to inspection techniques, observations and experiences through various breakout and elective sessions. These included:

- Inspection issues in specialised industries and bank audits;
- Inspections of small/medium-sized audit firms;
- Internal control testing and the use of IT specialists;
- Materiality of inspection findings and disciplinary actions;
- Follow-up of evaluation of firms' action plans;
- Requirements, experiences and views on the inspection documentation;
- Thematic inspections;
- Integration of corporate reporting inspections and audit quality inspections;
- The UK model for reporting to audit committees;
- Fees charged by auditors for non-audit services and potential regulatory risks; and
- Inspecting auditors' responsibility relating to fraud and anti-money laundering.

One of the breakout sessions was moderated by AOB. Two poster presentations were also introduced for the first time and provided insights in the following areas:

- European Audit Inspection Group (EAIG) database on inspection findings; and
- Audit quality measures.

The workshop was viewed as a good platform for independent audit regulators to meet and discuss inspections processes, learn and leverage from each other especially in areas that impact regulation of the audit profession.

IFIAR Regional Outreach Event

In conjunction with the workshop, IFIAR also held the Regional Outreach Event on 12 March 2014. This inaugural event was attended by officials from the following jurisdictions:

- Public Accountants Oversight Committee (PAOC), Ministry of Finance, Brunei;
- Securities Issuance Supervision, Securities and Exchange Commission of Cambodia, Cambodia;
- Financial Reporting Council, Hong Kong;
- Financial Inspection Department, Ministry of Finance, Lao People's Democratic Republic; and
- Independence Audit Division of Accounting Department, Ministry of Finance, Lao People's Democratic Republic.

The objective of the IFIAR Regional Outreach Event is to initiate and cultivate an exchange of information with regulators who have yet to become IFIAR members and in the process of developing an audit oversight system.

As an introduction, Janine van Diggelen, IFIAR Vice-Chair, covered details on structure, goals and current projects, working groups of IFIAR, membership requirements and IFIAR core principles.

The AOB together with the Netherlands Authority for the Financial Markets (AFM) and ACRA, Singapore shared perspectives on how various audit oversight systems are structured and developed.

IFIAR Plenary Meeting

The AOB, an IFIAR member since September 2010 together with the other members met in Washington DC, US at the 14th IFIAR Plenary Meeting in April 2014 to share insights and discuss key issues of interest. The meeting was hosted by the Public Company Accounting Oversight Board (PCAOB).

Topics discussed included:

- Whether the evolving economic and business model of audit firms presents a risk to audit quality, which was addressed with the chief executive officers of six global network audit firms;
- How the audit can better serve investors and audit committee members;
- Audit quality indicators;
- How to identify key systemic risks, and address them in dynamic audit regulation; and
- What is the importance of audit regulation to capital markets, addressed in a keynote speech delivered by Paul Volcker, former United States of America (US) Federal Reserve Chairman, and the origins of the *Sarbanes-Oxley Act of 2002*, addressed in a keynote speech delivered by former US Senator Paul Sarbanes.

IFIAR also announced the results of its second survey of members' inspection findings. The results reflected continued deficiencies in key areas of audit, and expressed concern about the implications of the findings for audit quality. IFIAR is determined to enhance co-operation among members with the goal of improving audit quality.

IFIAR 2014 Survey

AOB took part in this global survey carried out by the IFIAR of Inspection Results for Audit Firms. The purpose of this survey was to collect information regarding the structure of each IFIAR member's inspection programme as well as specific information on inspection findings.

Apart from that, AOB has also participated in the IFIAR Enforcement Working Group survey. The objective of this survey was to develop an understanding of members' enforcement regimes, enforcement and investigation issues, methodology and techniques.

The survey was the first global survey concerning IFIAR members' enforcement regime and the summary of the findings will be presented in the IFIAR Plenary meeting in April 2015.

ENGAGING LEADERSHIP OF AUDIT FIRMS

In 2014, there were several dialogues with the leadership of the local audit firms as part of efforts to support quality audit work.

Areas of discussion included regulatory updates, emerging issues such as restriction on China – related audit due to potential new regulations and issues of conflicts of interest arising from provision of non-audit services.

There was also dialogue on the introduction of annual data gathering and statistics analysis, emerging issues on readiness to implement the New Auditor's Report standards and impact of key audit exposure drafts. For the first time during the dialogue session, selected audit firms shared best practices which promotes audit quality.

“... more efforts are required especially from audit firms to engage with their clients in sharing some of the key developments of audit regulations including exposure drafts to minimise the impact of application when those exposure drafts become effective.”

From the AOB's engagement with the audit firms, it is envisaged that more efforts are required especially from audit firms to engage with their clients in sharing some of the key developments of audit regulations including exposure drafts to minimise the impact of application when those exposure drafts become effective.

COLLABORATING WITH REGULATORS

There have been continuous efforts by AOB in its collaboration with other regulators, particularly Bank Negara Malaysia (BNM), Companies Commission of Malaysia (CCM) and Bursa Malaysia. The collaboration entails discussion on policy matters and ways to enhance financial reporting practices.

There were shared efforts with Bursa Malaysia to promote high quality financial reporting practices which include the role of directors and audit committees. The initiatives for collaboration between the AOB and other regulators is an effort to reduce differences in regulators' approaches, minimise duplication of effort towards effective regulation and increase effectiveness of regulatory activities in supervising the financial reporting and auditing.

PROMOTING HIGH QUALITY FINANCIAL REPORTING PRACTICES

The AOB was involved in various external events and engagement to share views and thoughts.

The AOB participated in the following events which included:

- ➡ Ethics Standards Board (ESB) Outreach Programme organised by MIA
- ➡ Integrated Reporting Forum jointly organised by SC, ACCA and International Integrated Reporting Council (IIRC)

- ➡ Corporate Fraud Conference organised by the Institute of Internal Auditors Malaysia (IIAM)
- ➡ Talk on 'The 100 Drivers for Change against the Backdrop of the Digital Revolution' organised by ACCA Malaysia and AOB
- ➡ CCM National Conference
- ➡ KPMG ASPAC Quality & Risk Management Conference
- ➡ PricewaterhouseCoopers Malaysia launch of the report titled 'The State of Integrated Reporting in Malaysia'
- ➡ SC Industry Dialogue with professional bodies
- ➡ Talk by the Asian Institute of Finance (AIF) under the AIF Distinguished Speaker Series 2014 on the topic, 'Towards a Sustainable Financial System'
- ➡ Audit World 2014 Conference themed 'Evolving in Practice' jointly organised by MIA and The Malaysian Institute of Certified Public Accountants (MICPA)
- ➡ MIA-CPA Australia Forum
- ➡ Annual ASEAN Corporate Governance Summit organised by the Federation of Public Listed Companies Bhd (FPLC) and Malaysian Institute of Corporate Governance (MICG)
- ➡ Roundtable on Integrated Reporting and Assurance organised by SC and ACCA Malaysia
- ➡ MIA International Accountants Conference
- ➡ ESB Outreach Programme organised by MIA
- ➡ Seminar on Enhancing Auditors' Professionalism to Improve Audit Quality organised by National Audit Department
- ➡ MICPA 55th Anniversary Commemorative Lecture

STRENGTHENING THE ACCOUNTANCY PROFESSION

The CSAP, a multi-agency panel formed by the Ministry of Finance, released a consultative document in December 2014 inviting public feedback on the proposed recommendations to enhance the accountancy profession in Malaysia.

CSAP is aligned to the government's transformation agenda in enhancing the competitiveness of the country.

The recommendations are to enhance the contribution of the accountancy profession in nation building, ensure the economy is supplied with the requisite number of professional accountants and reset the governance of the accountancy profession to ensure its effectiveness. The consultative document is exposed for public comment until 31 January 2015.

A Financial Reporting Quality Task Force comprising representatives from SC, MIA, MICPA and academia was also set up to embark on ways to identify and promulgate measures to improve the quality of financial reporting and auditing of PIEs.



PART 3

Performance Assessment and Effectiveness



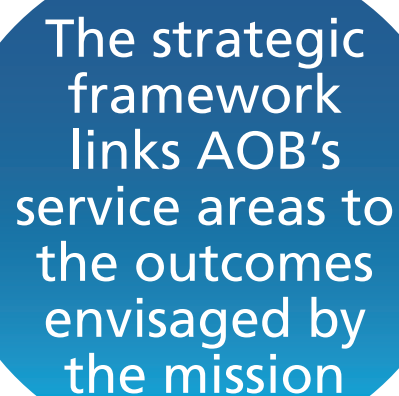
PERFORMANCE ASSESSMENT AND EFFECTIVENESS

INTRODUCTION

The AOB Board approved a new strategic framework which incorporated a three-year outlook of the market and regulatory landscape.

The strategic framework links AOB's service areas to the outcomes envisaged by the mission. While the core services such as registration and inspection are ongoing oversight activities, focus areas have been identified after considering the operating environment, developments in financial reporting and auditing, regulatory changes as well as global development in audit regulation. There will be continuous refinement to the following strategic outcomes:

- Confidence in audited financial statements;
- Audit opinion based on sufficient and appropriate evidence;
- Externalisation of professional values and ethics;
- Resourceful and capable audit practices; and
- High quality financial reporting practices by PIEs.



The strategic framework links AOB's service areas to the outcomes envisaged by the mission

At the beginning of each year, the AOB Board considers and approves the proposal from management on the annual operational plan including focus areas in the audit oversight function. Progress is reported to the AOB Board on a quarterly basis and mid-year performance review is also conducted.

Outcomes and progress achieved in the focus areas indicated that the AOB continued to achieve its regulatory mandate and mission in line with the overall aim of the strategic framework.

2014 PERFORMANCE REVIEW

AOB strategic outcomes	Activities	Performance assessment for 2014
Confidence in audited financial statements.	<ul style="list-style-type: none"> • Participation in public events to send key messages on audit quality to key stakeholders. • Contributed to the assessment by ACGA in collaboration with CLSA Asia-Pacific Markets. • Create awareness among key stakeholders and promote views on the importance of audit oversight in the capital market. 	<ul style="list-style-type: none"> • AOB participated in 15 local and international events. • In the CG Watch 2014 by ACGA, Malaysia was recognised for its strength in financial reporting and auditing standards, ranking equally first with another country in the category of accounting and auditing. • Auditors are more inclined to emphasise material issues in their audit report.
Audit opinion based on sufficient and appropriate evidence.	<ul style="list-style-type: none"> • There were 10 audit firms and 29 individual auditors inspected under the regular inspection conducted during the year. 	<ul style="list-style-type: none"> • There was no major audit failure reported during the year among the companies with large market capitalisation. • Auditors were more inclined to emphasise material issues in their audit report. • Enforcement action taken against two individual auditors and one audit firm for failure to comply with professional standards.
Externalisation of professional values and ethics.	<ul style="list-style-type: none"> • AOB continued to monitor audit rotation requirement which is a fundamental principle to ensure auditor independence. 	<ul style="list-style-type: none"> • Improvement observed in 2014, notwithstanding one audit firm being sanctioned for breaching the requirements of partner rotation and non-compliance of relevant regulations and guidelines. • Strengthened self-discipline among major firms.

AOB strategic outcomes	Activities	Performance assessment for 2014
<p>Resourceful and capable audit practices</p>	<ul style="list-style-type: none"> • Engagement with audit firms during the renewal of registration ensured audit firms have in place quality control framework. • Firms were required to identify root causes of the deficiencies identified by AOB during inspection and are at various stages of progress. • Firms were required to measure the effectiveness of remediation plans. • Supported the implementation of auditing standards. • Best practices driven via dialogues with audit firms to ensure continuous capacity building and right infrastructure, tone from the top and culture to support audit quality. 	<ul style="list-style-type: none"> • During the year, three auditors were subjected to specific remediation measures. • AOB refused the application of a foreign audit firm recognition pursuant to the failure to comply with the requirements of Part IIIA or any written notices or guidelines made under the SCA. • 14 remediation plans approved. • Involved in local standard setting board and provided comments in two exposure drafts to IFAC. • Held several dialogues with the leadership of the local audit firms.
<p>High quality financial reporting practices by PIEs</p>	<ul style="list-style-type: none"> • Participation in events to engage directors and members of audit committees as a reminder of their role in enhancing the quality of financial reporting. • Dialogues to support behavioural and cultural changes to promote consistency of quality practices. • Drive messages on investing in retaining talent and relevant infrastructure to support effective and high quality financial reporting functions. • Drive quality practices to build right behaviour and culture. • Establish the Financial Reporting Quality Task Force to identify and promulgate measures to improve the quality of financial reporting and auditing. 	<ul style="list-style-type: none"> • Participated in 17 events. • Recommendation in the CSAP report to address the issue of talent pool.

Box 4 RECOGNITION IN CG WATCH 2014 REPORT

The ACGA recently acknowledged AOB as one of the better organised and transparent audit regulators in the region in its CG Watch 2014 Report issued on 25 September 2014. In particular, Malaysia was recognised for its strength in financial reporting and auditing standards, ranking equally first with another country in the category of accounting and auditing.

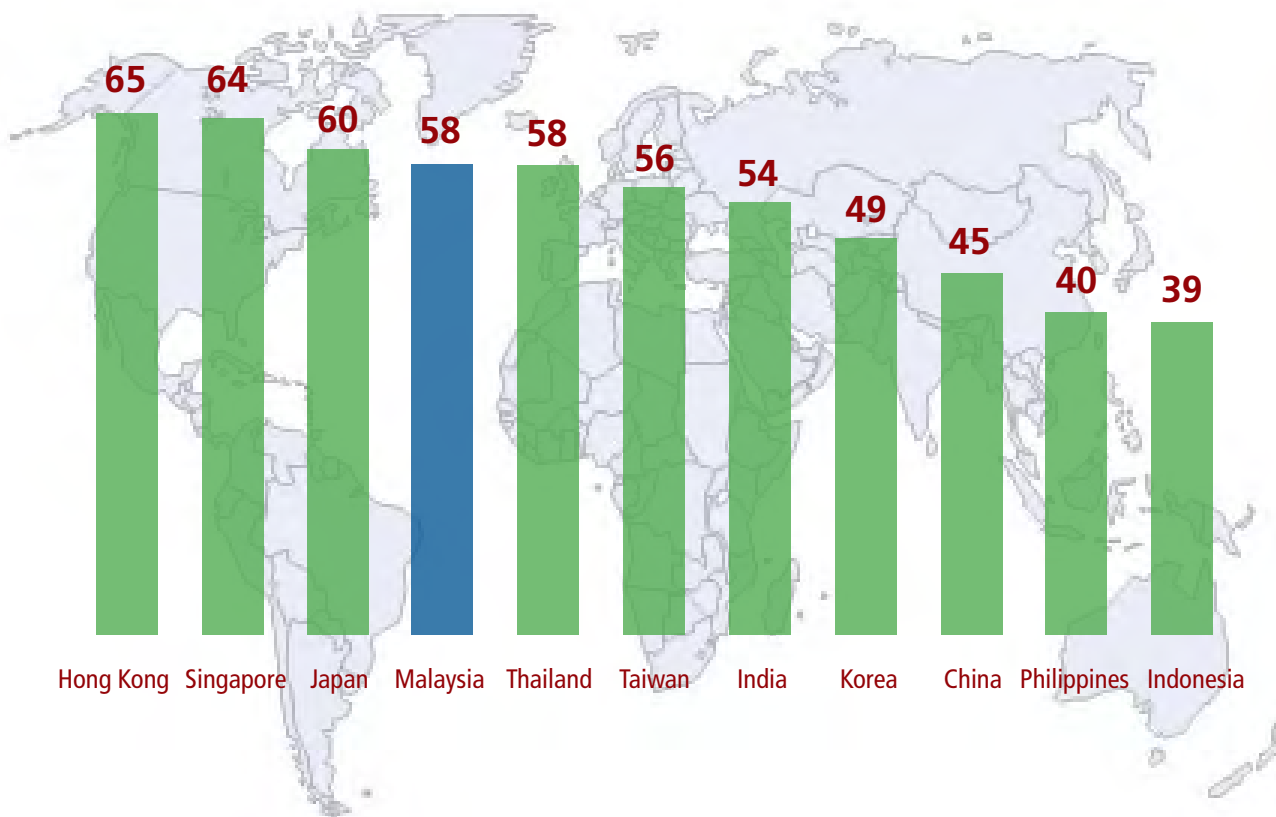
According to the report, Malaysia achieved an overall score of 58% in 2014, maintaining its rank of fourth in the region. The report also drew attention to the sustained and concerted efforts in driving governance reforms, resulting in Malaysia becoming the only market out of the Asia Pacific countries assessed that consistently improved its scores in each of the last four surveys.

The favourable acknowledgement of AOB's efforts has paved the way for enhanced confidence in audited financial statements of PIEs in Malaysia, which will be beneficial to audit firms registered with the AOB. It is further envisaged that Malaysia's strengthened regional standing will assist to bolster investor confidence while inspiring a stronger culture of corporate governance in the Malaysian capital market.

The CG Watch is a biennial report by ACGA in collaboration with CLSA Asia-Pacific Markets, an ACGA member and founding sponsor. The report ranks 11 Asian markets on macro CG quality and 944 companies on their internal governance systems. The CG Watch 2014 was conducted from February to August by a team of research analysts, experts and consultants.



CG Watch Market Scores 2014



Source: 'CG Watch 2014 – Market Rankings' presentation by Jamie Allen, Secretary-General, ACGA



PART 4

Support Adoption and Implementation of Standards



SUPPORT ADOPTION AND IMPLEMENTATION OF STANDARDS

INTRODUCTION

The AOB is committed to contribute towards and collaborate with peers and stakeholders of the financial reporting ecosystem to continuously raise audit quality as well as uphold global standards of auditing.

DEVELOPMENT AND IMPLEMENTATION OF STANDARDS AND REGULATIONS

The AOB's continued participation as an observer in meetings held by the Auditing and Assurance

Standards Board (AASB) and ESB of the MIA provided opportunities for AOB to share its views on matters of concern in addition to its submissions to various standard-setting and regulatory bodies.

Auditing and assurance

During 2014, the key activities of the AASB included the issuance of the *Illustrative Engagement Letter and Report of Factual Findings for an Agreed-upon Procedures Engagement in relation to Requirements of the Money Services Business Act 2011*.

Box 5 THE AUDITOR REPORTING PROJECT

The AOB had, in its annual report in 2013, followed the progress of the Auditor Reporting Project undertaken by the IAASB. The project was initiated in response to multiple calls from various stakeholders for more relevant information to be provided based on the audit that is performed. In today's fast-paced global business environment with financial reporting requirements which are growing in complexity, the availability of such information is crucial to the decision making process.

The exposure draft *Reporting on Audited Financial Statements: Proposed New and Revised International Standards on Auditing* issued by the IAASB in July 2013 sought views particularly on the overall form and content of the auditor's report, anticipated benefits arising as a result of the proposals, and additional effort or costs that may be expected.

In September 2014, the IAASB approved the following which were issued on 15 January 2015 with an effective date of 15 December 2016:

- ISA 700 (Revised) *Forming an Opinion and Reporting on Financial Statements*
- ISA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*

- ISA 260 (Revised) *Communication with Those Charged with Governance*
- ISA 570 (Revised) *Going Concern*
- ISA 705 (Revised) *Modifications to the Opinion in the Independent Auditor's Report*
- ISA 706 (Revised) *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*
- Conforming amendments to other ISAs

The AOB continues to caution against the inclination towards boilerplate disclosures to ensure continued relevance of the impending enhancements, in particular, that of the newly introduced 'key audit matters' section, in order to achieve the desired impact on stakeholders. The AOB also re-emphasises the need for auditors to manage the information to be included in the auditor's report to ensure that the content remains at a reasonable volume without compromising the communicative value of those disclosures.

Diagram 1

Components of the New Auditor's Report



Source: IAASB New and Revised Auditor Reporting Standards and Related Conforming Amendments issued on 15 January 2015.

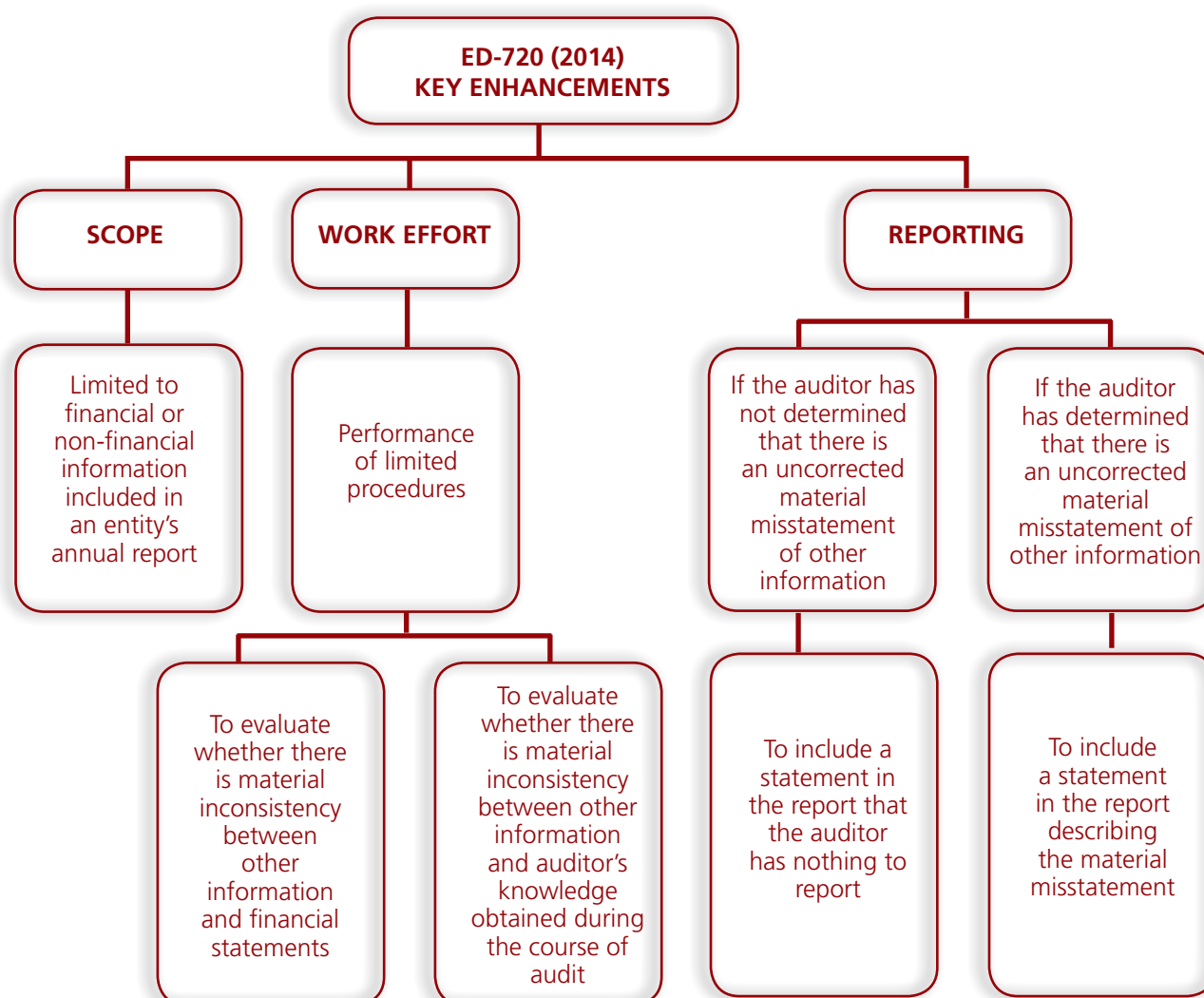
Responsibilities relating to other information

In March 2014, the IAASB issued the proposed ISA 720 (Revised) *The Auditor's Responsibilities Relating to Other Information* (ED-720 (2014)). This re-exposure follows the earlier proposed ISA 720 (Revised) *The Auditor's Responsibilities Relating*

to Other Information in Documents Containing or Accompanying Audited Financial Statements and the Auditor's Report Thereon (ED-720 (2012)) which had garnered overall support for the IAASB's intention to strengthen and clarify the auditor's responsibilities relating to other information, including clarification on the scope of documents covered and new reporting responsibilities.

Diagram 2

Key Enhancements in Proposed ISA 720 (Revised) The Auditor's Responsibilities Relating to Other Information



Source: IAASB exposure draft on proposed ISA 720 (Revised) *The Auditor's Responsibilities Relating to Other Information*

The ED-720 (2014) contains substantial changes to ED-720 (2012) to address the following significant concerns which were discerned to potentially undermine the benefits sought by the IAASB:

- That the proposals did not clearly articulate the auditor's objectives, scope of documents covered, and required work effort expected from the auditor; and
- That the proposals would not be workable in practice or would lead to divergent practices, both among auditors and between jurisdictions.

The AOB continues to support the IAASB's initiatives with regard to the auditor's responsibilities relating to other information and the proposed alignment of the effective date of the final standard to that of the Auditor Reporting Project. However, the decision for early application should only be made after gauging market readiness.

Addressing disclosures

Amid the whirlwind of evolutionary changes to financial reporting disclosure requirements over the past decade, fresh challenges arose for preparers and auditors alike in addressing new types of quantitative and non-quantitative information. An area of particular concern repeatedly raised by various stakeholders is that the resulting higher volume of note disclosures has, in some cases, increased the risk that useful or relevant information may be obscured.

To address these challenges, the IAASB issued an exposure draft on *Proposed Changes to the International Standards on Auditing – Addressing Disclosures in the Audit of Financial Statements*. The proposed amendments are anticipated to further support proper application of the ISAs requirements while clarifying the expectations of auditors when auditing financial statements disclosures.

Key proposed amendments in the exposure draft include:

- Enhanced definition of 'financial statements';
- Greater weightage given to considering potential misstatements arising from presentation and/or disclosures for the period under audit, as assertions relating to disclosures are to be considered in conjunction with the assertions about classes of transactions and events and account balances;
- Increased focus on auditing disclosure requirements, including increased emphasis on the need for early consideration of audit work needed relating to these disclosures;
- Greater attention drawn to information from systems and processes that are not part of the general ledger system, e.g. risk management system, valuation reports, etc; and
- Auditors to consider the possibility that management disclosures are intended to obscure information.

The IAASB has had active collaboration, co-operation, liaison and outreach with other interested stakeholders, including accounting standard setters, regulators, preparers and users, in cognisance that many of the issues around disclosures cannot be resolved alone. This is evidenced in the International Accounting Standards Board (IASB) exposure draft ED/2014/1 *Disclosure Initiative (Proposed amendments to IAS 1)* which highlighted similar concerns that useful information may become less visible and consequently less understandable.

The AOB strongly supports the IAASB's continuous involvement in the IASB Disclosure Initiative's *Materiality – assessment of existing guidance* project which is envisaged to improve the focus of disclosures in financial statements through increased emphasis on materiality and relevance. However, consistent application and understanding of 'materiality' should be encouraged without resorting to boilerplate financial statements disclosures. Also of importance is the careful consideration of the mechanics and practicability of all proposed

requirements while improving and streamlining understanding among stakeholders, imperative given the ongoing efforts of the IAASB with regard to the expanded auditor's report which introduces disclosure requirements such as 'Key Audit Matters'.

During 2014, the AOB noted that there was an increasing number of enhancements proposed which may increase the responsibilities of auditors. Recent developments in the accounting profession have placed increasing emphasis on materiality and relevance.

The AOB thus emphasises the importance of maintaining common understanding among stakeholders, in particular the management and / or those charged with governance, to ensure that there are basic prerequisites in place to facilitate the audit process.

Ethics

Key activities of the ESB in 2014 include the adoption and incorporation of the *Changes to the Definition of 'Those Charged with Governance'* in the MIA By-Laws. This is consistent with the change to the International Ethics Standards Board for Accountants (IESBA) Code of Ethics for Professional Accountants (the Code).

The AOB actively monitored IESBA developments during the year which were largely aimed at strengthening and enhancing independence provisions in the Code.

Non-assurance services

The IESBA issued an exposure draft on *Proposed Changes to Certain Provisions of the Code Addressing Non-Assurance Services for Audit Clients* in May 2014. The proposed amendments are intended to

clarify and strengthen the non-assurance services provisions and are in line with the public interest and existing requirements embedded in the Code for members of audit teams, firms and network firms to maintain independence both in mind and appearance of audit clients.

The proposed amendments to the Code include the following:

- Removal of the 'emergency exception' provisions related to bookkeeping and taxation services;
- Further guidance and clarification on what constitutes a management responsibility, including how the auditor can better satisfy itself that client management will make all judgements and decisions that are the responsibility of management, when the auditor provides non-assurance services to an audit client; and
- Enhanced guidance and clarification on the concept of 'routine and mechanical' services in relation to the preparation of accounting records and financial statements for non-PIE audit clients.

In Malaysia, paragraphs 290.172 and 290.185 of the MIA By-Laws prohibit a firm from providing bookkeeping and taxation services to an audit client that is a PIE, without any further consideration of whether the provision of such services are of a routine or mechanical nature. Hence, the proposed removal of the 'emergency exception' provisions would better align the requirements of the Code to that of the MIA By-Laws.

It should also be noted that auditor licensing requirements in Malaysia prohibit an auditor from directly or indirectly recording or maintaining accounting records for any company where the auditor or firm is the auditor of the company, except for accounting work related to the audit.

Long association of personnel

In response to stakeholders' growing concerns with regard to the appearance of independence and the need to ensure that threats created by the long association of audit firm personnel with an

audit client are appropriately addressed in all audit engagements, the IESBA also developed an exposure draft on *Proposed Change to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client*. The proposed key amendments are explored in Table 1.

Table 1

Proposed key amendments in the IESBA exposure draft on Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client

Proposed key amendments	Key considerations
<p>1. Strengthened general provisions that apply to all audits and assurance engagements with respect to the threats created by long association.</p>	<p>The proposed enhancements have allowed for greater clarity and understanding with regard to the identification and evaluation of familiarity and self-interest threats created by long association. However, the following should be noted:</p> <ul style="list-style-type: none"> • The safeguards listed are non-exhaustive. • The identification and evaluation of familiarity and self-interest threats potentially created by long association should always be performed objectively. • It is important to consider the nature of the roles undertaken by the respective individuals on the audit team, and whether these roles are potential threats to the independence in the audit engagement. <p>The AOB is mindful that in Malaysia, concerns giving rise to such threats are naturally addressed by the high staff attrition rate, which acts as a natural safeguard.</p>
<p>2. More stringent mandatory cooling-off period requirements for the engagement partner on the audit of an entity that is a PIE.¹</p> <p>An individual who has acted as the engagement partner at any time during the seven year time-on period shall not be a member of the engagement team or provide quality control for the audit engagement for five years.</p> <p>For any other key audit partner, the mandatory cooling-off period shall be for two years.</p>	<p>Key concerns:</p> <ul style="list-style-type: none"> • Certain jurisdictions may not have sufficient expertise to accommodate the extended cooling-off period, particularly in view of the proposed strengthened restrictions applicable during the aforementioned cooling-off period. • With the current fast-paced environment and frequent changes to standards and regulations, a longer cooling-off period of five years coupled with the strengthened restrictions may be counter-productive as the partner would not have the benefit of continuously keeping abreast with recent developments in the respective industry, thereby resulting in a loss of valuable expertise and experience. <p>The AOB recommended that the IESBA should further identify key success factors which can strongly support the proposed extended five-year cooling-off period.</p>

¹ Paragraph 290.151 of the MIA By-Laws imposes a more stringent requirement whereby the maximum time-on period is five years, in comparison to the seven years allowed in the Code.

On an overall basis, the AOB recommended that the IESBA should consider the potential additional costs of engaging audit partners and/or personnel with the relevant industry experience. This is in view that with the enhanced and strengthened restrictions, as well as existing limited expertise to provide technical consultations, certain jurisdictions may face challenges in meeting the immediate

resources needs of the respective firms, particularly where an expert view is required. Such firms would thus need to urgently look into alternatives such as engaging other firms within the network and/or otherwise to obtain the view of audit personnel with the relevant industry experience which may or may not be cross-jurisdictional in nature.

Proposed key amendments	Key considerations
<p>3. Strengthened restrictions on the type of activities that can be undertaken during the mandatory cooling-off period in relation to the following:</p> <ul style="list-style-type: none"> • Consultations with the engagement team or the client on technical or industry-specific issues, transactions or events affecting the audit engagement; • Responsibilities for leading or coordinating the firm's professional services to the audit client or overseeing the firm's relationship with the audit client; or • Any roles or activities with respect to the audit client, including the provision of non-assurance services, that would result in significant or frequent interaction with senior management or those charged with governance; or exerting direct influence on the outcome of the audit engagement. 	<p>Key concerns:</p> <ul style="list-style-type: none"> • Certain jurisdictions may not have sufficient expertise to take on the consultation role. This would be of particular concern say, in a situation where consultation is needed on an industry-specific issue and the only expert available is unable to provide the consultation due to the additional restrictions in place during the cooling-off period. • The introduction of the additional restrictions may inadvertently result in unintended consequences of increased application of the exemption provided under paragraph 290.155 of the MIA By-Laws (Paragraph 290.153 of the Code)², which may ultimately defeat the purpose of the introduction of the additional restrictions. <p>Since any consultation should always be made from an objective standpoint, AOB recommended instead that the Code allow for some form of judgement and require that safeguards be put in place to address the concerns raised. In any case, the AOB expects that the key audit partner would be fully responsible and accountable for the final decision made regardless of the results of the technical consultation, thus mitigating the risk of the former key audit partner directly influencing the outcome of the engagement.</p>
<p>4. Requirement to obtain concurrence of those charged with governance regarding the application of certain exceptions to rotation requirements.</p>	<p>The AOB is of the view that the decision to apply exceptions to rotation requirements should remain with the firm. However, for better transparency and client engagement, the firm should communicate the need for applying such exceptions to those charged with governance, supported by the necessary documentation in the audit working papers to justify the need for such application.</p>

² Paragraph 290.155 of the MIA By-Laws (paragraph 290.153 of the Code) allows an independent regulator in the relevant jurisdiction to provide an exemption from partner rotation, thereby allowing an individual to remain as a key audit partner for more than seven years, with specific alternative safeguards such as regular independent external review.

In view of the above, it may be advisable to be mindful that the introduction of the proposed amendments to the Code may well result in an overall increase in the cost of compliance and regulation on a global basis as an unintended consequence.

GLOBAL INITIATIVES IN REFORMING THE AUDIT MARKET AND PRACTICES

The AOB continues to promote audit quality of audit firms serving PIEs in Malaysia and monitors global developments relating to audit quality which have garnered particular international interest, as explored below.

Tracking these global regulatory developments assist in AOB's annual and ad-hoc dialogues with the auditors. For example, emerging issues pertaining to audit quality indicators and audit regulation in relation to China-related PIEs, further details on which can be found in Parts One and Two of this Annual Report.

European Union Audit Reform

The EU audit reform introduced a Directive amending the existing Statutory Audit Directive and a new Regulation on specific requirements regarding statutory audit of PIEs. The new legislation came into effect on 16 June 2014 and will be applicable in 2016.

To improve audit quality and restore investor confidence in financial information, the following key measures were introduced:

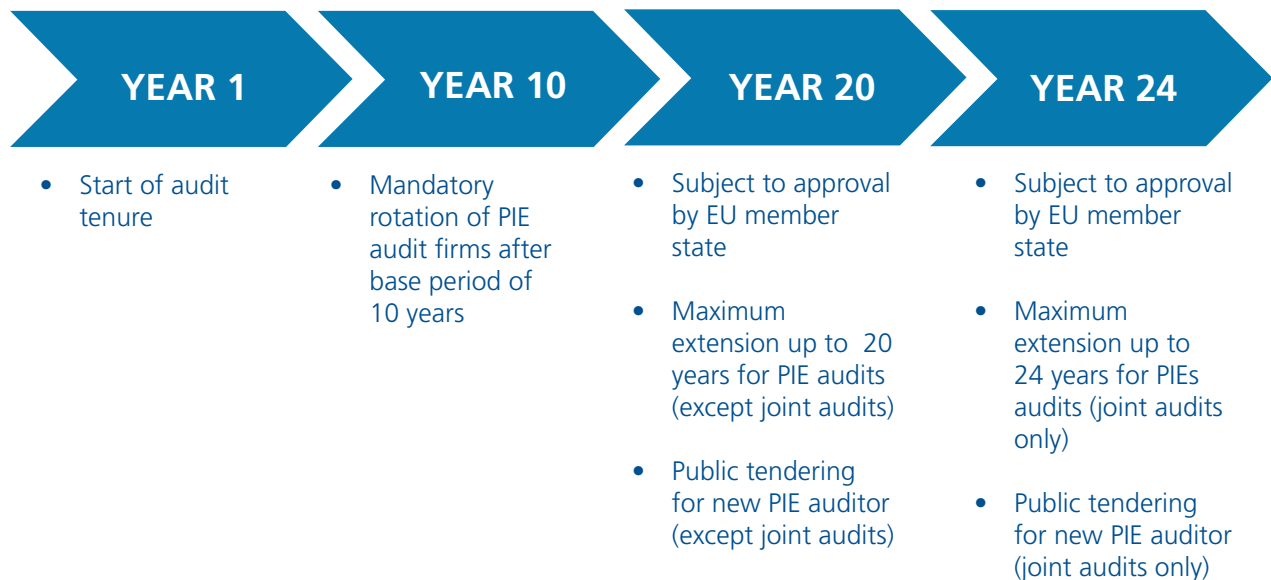
- The European Commission (EC) may adopt international auditing standards via delegated acts. Audit oversight will continue at national level, while co-operation and co-ordination will be carried out by the Committee of European Auditing Oversight Bodies (CEAOB), using the experience of the European Securities and Markets Authority (ESMA);

“ Fees generated from non-audit services rendered to a PIE audit client to be capped at 70% of the average fees paid for the last three consecutive years, calculated at the group level.”

- Enhanced information with the following requirements for PIE statutory auditors:
 - For investors, to report on key areas of risk of material misstatements of the annual or consolidated financial statements, as well as the extent of which the statutory audit was considered capable of detecting irregularities, including fraud; and
 - For the audit committee, to prepare an additional report providing further details on the outcome of the statutory audit, including the methodology used, possible significant deficiencies identified in the internal control system, and valuation methods applied.
- Mandatory rotation of PIE statutory auditors, as referred to in Diagram 3;
- Prohibition of audit firms from providing certain non-audit services to audited PIEs, in particular tax advice and services linked to the financial and investment strategy of the audited PIEs. However, EU member states may allow the provision of such services if they are immaterial, with no direct effect on the audited financial statements;
- Fees generated from non-audit services rendered to a PIE audit client to be capped at 70% of the average fees paid for the last

Diagram 3

EU mandatory rotation timeline for PIE statutory auditors



three consecutive years, calculated at the group level. Where total fees from a PIE audit client is found to exceed 15% of the total fees for the firm in the last three consecutive financial years, the audit committee should consider submitting the audit engagement for a quality control review. If this continues, the audit committee should also consider whether to retain the auditor, up to a maximum of two years; and

- Establishment of a 'European passport' in the form of a certificate attesting to the registration of the audit firm in its home member state. This will facilitate cross-border mobility of audit firms within the EU and strengthen the single market for audit.

EU member states will have some flexibility in terms of implementation, in that stricter requirements in

comparison to those in the new legislation may be imposed. However, the IFAC is deeply concerned that such flexibility could inadvertently lead to inconsistent implementation across all European jurisdictions. This may then result in the promotion of regulatory divergence and fragmentation not only within the EU, but also with other major jurisdictions, such as the US and Canada.

Further, the approved bipartisan bill in July 2013 amended the *Sarbanes-Oxley Act of 2002* to prohibit the PCAOB from requiring public companies to use specific auditors or requiring the use of different auditors on a rotation basis. The Center for Audit Quality (CAQ)³ cautioned that the implementation of the new requirements could affect companies and their auditors in the US. The CAQ hopes that the new requirements can be implemented with the greatest consistency possible across Europe with minimal extra-territorial impacts.

³ The CAQ is affiliated with the American Institute of Certified Public Accountants (AICPA).

Focus on audit quality

Audits are instrumental in fostering trust in the quality of reporting, which in turn supports global financial stability. This underscores the importance of continual improvement to audit quality and its undeniable relevance to all stakeholders in the financial reporting supply chain.

Prior to 2013, the IAASB embarked on the development of a framework that identifies factors contributing to audit quality at the engagement, audit firm and national levels. The IAASB Consultation Paper on *A Framework for Audit Quality* issued in January 2013, followed by its finalised counterpart, the non-authoritative document entitled *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality* on 18 February 2014, were a culmination of these efforts.

The Framework describes the key elements that create an environment of audit quality and demonstrates how, collectively, these factors have the potential to impact the nature and quality of financial reporting and, directly or indirectly, audit quality. These elements are also believed to be able to maximise the likelihood of quality audit being consistently performed.

The Framework is also cognisant that audit quality is best achieved in an environment supported by all participants of the financial reporting supply chain. The Framework thus aims to raise awareness of the mentioned key elements of audit quality and facilitate greater dialogue among key stakeholders who are encouraged to challenge themselves to do more to increase audit quality in their respective environments.

In April 2014, CAQ issued the *CAQ Approach to Audit Quality Indicators (AQI)* which highlighted that audit firms are required to establish a system of quality control that complies with regulatory and

legal requirements and that ensures audit reports issued by the firm are appropriate. The system of quality control is intended to address certain key elements, such as independence, integrity, objectivity, personnel management, engagement performance, communication and reporting, and monitoring.

AQIs are primarily quantitative in nature, supplemented by contextual qualitative narrative and dialogue between auditor and audit committee. It is envisaged that a set of potential AQIs may provide those overseeing the audit with additional perspective, information and transparency into the systems and processes that underlie the performance of an audit.

Discussions on the AQI are expected to occur annually with updates throughout the audit cycle, depending on the issuer's complexity and timing of the audit cycle. It should be noted that the identification and evaluation of AQIs is an evolutionary process requiring periodical assessment and refinement in order to meet the needs of the ever-changing business environment.

Audit regulation in relation to China-related PIEs

On 24 January 2014, the US Securities and Exchange Commission (SEC) banned the Chinese arms of the Big Four global accounting firms from working for US-listed companies for six months. These auditors had declined to share their working papers with the US SEC, citing that such an action would be in violation of Chinese secrecy laws. As of June 2014, the 6-month suspension was put 'on hold' pending appeal, the deadline of which was in December 2014.

On 19 May 2014, the Ministry of Finance China issued 10 proposed new rules on cross-border audit services⁴ by accounting firms. The proposed

⁴ Cross-border audit services refer to any audit engagement that is carried out for Chinese companies listed in overseas countries (including proposed listing).

new rules were aimed at clarifying the roles of mainland and international accounting firms, as well as enhancing the quality of auditing standards of mainland companies.

The proposed new rules include the following:

- Temporary licences issued to overseas accounting firms are not meant for carrying out audits of companies which are registered and listed overseas with operations in China. Hence, overseas accounting firms are not allowed to carry out any audit service or issue independent auditor reports for such companies;
- Where overseas regulatory listing requirements require a non-Chinese auditor to audit the financials of the aforementioned companies, the overseas accounting firm is required to co-operate with local Chinese accounting firms which hold a securities qualification or is ranked in the top 100 accounting firms in China based on the previous year's evaluation done by the Chinese Institute of Certified Public Accountants (CICPA). However, the audit opinion and responsibilities will

be expressed by the overseas accounting firm, with the auditor's report being legally unenforceable in China; and

- Chinese companies which are listed overseas and local Chinese accounting firms co-operating in the audit are required to strictly adhere to national secrecy laws.

Following these events, there were a number of legal cases in 2014 whereby audit firms were compelled by court to provide documents or audit working papers to regulators. In these cases, the court emphasised that it is not enough to assert that the documents may include state-sensitive information; the audit firm must show evidence that it is a real possibility that the accountants would be prosecuted in China should the information be shared with foreign authorities.

It should be further noted that the Ministry of Finance China had clarified that there is no blanket ban on audit documents relating to Chinese companies and state-owned enterprises from leaving the mainland, provided that these documents do not contain state secrets.



PART 5

Statement on Governance



STATEMENT ON GOVERNANCE

MEMBERS OF THE AUDIT OVERSIGHT BOARD

Goh Ching Yin

Datuk Nor Shamsiah
Mohd Yunus

Cheong Kee Fong

Chok Kwee Bee

Nik Mohd Hasyudeen
Yusoff

Dato' Gumuri
Hussain



NIK MOHD HASYUDEEN YUSOFF

Appointed 1 April 2010

Nik Mohd Hasyudeen Yusoff is the Executive Director of the SC responsible for the Market and Corporate Supervision as well as Executive Chairman of AOB.

He is presently a member of the Operational Review Panel of the Malaysian Anti-Corruption Commission, a member of the Financial Reporting Foundation and also serves on the Corporate Debt Restructuring Committee which was set up by BNM. Nik is an Adjunct Professor at the Faculty of Business and Accountancy, University of Malaya.

Nik was formerly President of MIA and also the former Vice-President of the ASEAN Federation of Accountants. He also served on the Malaysian Accounting Standards Board (MASB) and the Listing Committee of Bursa Malaysia.

He holds a Bachelor of Business from Curtin University of Technology, Australia and is a Fellow of CPA Australia.

GOH CHING YIN

Appointed 1 April 2010

Goh Ching Yin is the Executive Director for Market Development of the SC.

Helming the portfolio, Goh is responsible for strategy and risk, markets and products, economics and market analysis and data management. His team conceptualises and formulates capital market strategy, products, market mechanisms and the SC's business plan; providing policy analysis of key issues and input to the government on wider issues affecting the capital market and broader economy. The team also identifies and manages macro risks to the SC's regulatory objectives, and

provides oversight on initiatives to develop private equity, venture capital, derivatives and multi-lateral arrangements.

Prior to joining the SC in March 2007, Goh led a career in investment banking for 12 years. The earlier part of his career saw him holding various leadership and management positions in regional business development, strategic consultancy, corporate insolvencies and auditing. He holds a master's degree in Business Administration from the Cranfield School of Management, Cranfield University, UK.

DATO' GUMURI HUSSAIN

Appointed 1 January 2012

Dato' Gumuri Hussain is a Fellow of the Institute of Chartered Accountants in England and Wales as well as, member of MIA and MICPA. He is also a Commission member of the SC. He is the former Chairman of SME Bank and held that post from 2005 to 2013. He was also the Managing Director and Chief Executive Officer of Penerbangan Malaysia

Bhd from 2002 to 2004. Prior to this, he was a Senior Partner and Deputy Chairman of the Governance Board of PricewaterhouseCoopers Malaysia. He has served as the Non-Executive Director of Bank Industri & Teknologi Malaysia Bhd, Rangkaian Hotel Seri Malaysia Bhd, Malaysian Airline System Bhd and Sabah Bank Bhd.

DATUK NOR SHAMSIAH MOHD YUNUS

Appointed 1 April 2010

Datuk Nor Shamsiah Yunus is currently the Deputy Governor in BNM. She is responsible for the supervision division that supervises commercial banks (conventional and Islamic banks), investment banks, insurance companies (conventional and takaful) and development financial institutions. She also oversees the Strategic Human Capital Management, the corporate shared services function and the financial intelligence and enforcement functions. She sits as one of the members at the BNM Board of Directors. She is also a member of the Monetary Policy Committee, Financial Stability Policy Committee and Joint Policy Committee.

Datuk Nor Shamsiah represents BNM in a number of regional and international fora in the areas of banking supervision and anti-money laundering. She joined BNM in April 1987 and has extensive experience in the development of prudential regulation, legislation, policies and guidelines for the financial sector. She holds a Bachelor's Degree in Accountancy from the University of South Australia and is a Fellow of CPA Australia.

CHEONG KEE FONG

Appointed 1 April 2010

Cheong Kee Fong has been a Partner of Cheong Kee Fong & Co. since January 1990. He was the sole proprietor of Cheong Kee Fong & Co. from November 1988 to December 1989.

He was previously a member of the Corporate Law Reform Committee established by the CCM and a member of the Finance Committee on Corporate Governance Working Group II on Corporate Governance in Malaysia. Cheong was also a

member of the Financial Reporting Foundation from 1997–2001, CCM and its Audit Committee from 2002–2005.

Cheong obtained his LLB (honours) from the University of Singapore and his Master of Laws from Harvard Law School. He is an advocate and solicitor of the High Court of Malaya and Supreme Court, Singapore.

CHOK KWEE BEE

Appointed 1 April 2010

Chok Kwee Bee is the Managing Director of Teak Capital Sdn Bhd, a venture capital management company managing a technology fund under the Malaysia Venture Capital Management Bhd (MAVCAP) Outsource Partner Programme.

Prior to that Kwee Bee was with Walden International, a Silicon Valley based venture capital firm, overseeing the operations and investments of Walden International and BI Walden in Malaysia. Before becoming a venture capitalist, Kwee Bee was the Head of Corporate Finance at AmlInvestment Bank.

Kwee Bee is currently a member of the Malaysian Venture Capital Development Council (MVCDC). She also sits on the board of Hong Leong Bank Bhd and several portfolio companies. She was previously a member of the SC Capital Market Advisory Council, member of the Exchange Committee of Labuan International Financial Exchange and also a past Chairman of the Malaysian Venture Capital and Private Equity Association (MVCA).

MEETING ATTENDANCE

In 2014, the AOB held eight Board meetings. The attendance by the Board members is stated below:

Board member	Number of meetings attended
Nik Mohd Hasyudeen Yusoff	8
Goh Ching Yin	7
Dato' Gumuri Hussain	8
Datuk Nor Shamsiah Mohd Yunos	3
Cheong Kee Fong	7
Chok Kwee Bee	8
Dato' Naim Daruwish (retired 16 September 2014)	1

MEETING PROCEDURES

Due notice is given on issues to be discussed with the distribution of agenda and papers for consideration at Board meetings. These meetings provide a forum for balanced deliberation of issues and transparent decision making.

A full set of minutes of all Board meetings is kept properly by the Secretary of the Board.

REGISTRATION COMMITTEE

Section 31EA of the SCA provides that the AOB may establish such committees as it considers necessary or expedient to assist in the performance of its responsibilities as specified under section 31E(1) of the SCA.

RESPONSIBILITIES OF THE BOARD

The Board is responsible in assisting the AOB in discharging its functions under the SCA. The responsibilities include:



1. Implement policies and programmes in ensuring an effective audit oversight system in Malaysia.



2. Register or recognise auditors of PIEs for the purposes of the SCA.



3. Direct MIA to establish or adopt, or by way of both, the auditing and ethical standards to be applied by auditors.



4. Conduct inspections and monitor programmes on auditors to assess the degree of compliance of auditing and ethical standards.



5. Conduct inquiries and impose appropriate sanctions against auditors who fail to comply with auditing and ethical standards.



6. Co-operate with relevant authorities in formulating and implementing strategies for enhancing standards of financial disclosures of PIEs.



7. Liaise and co-operate with oversight bodies outside Malaysia to enhance the standing of the auditing profession in Malaysia and internationally.



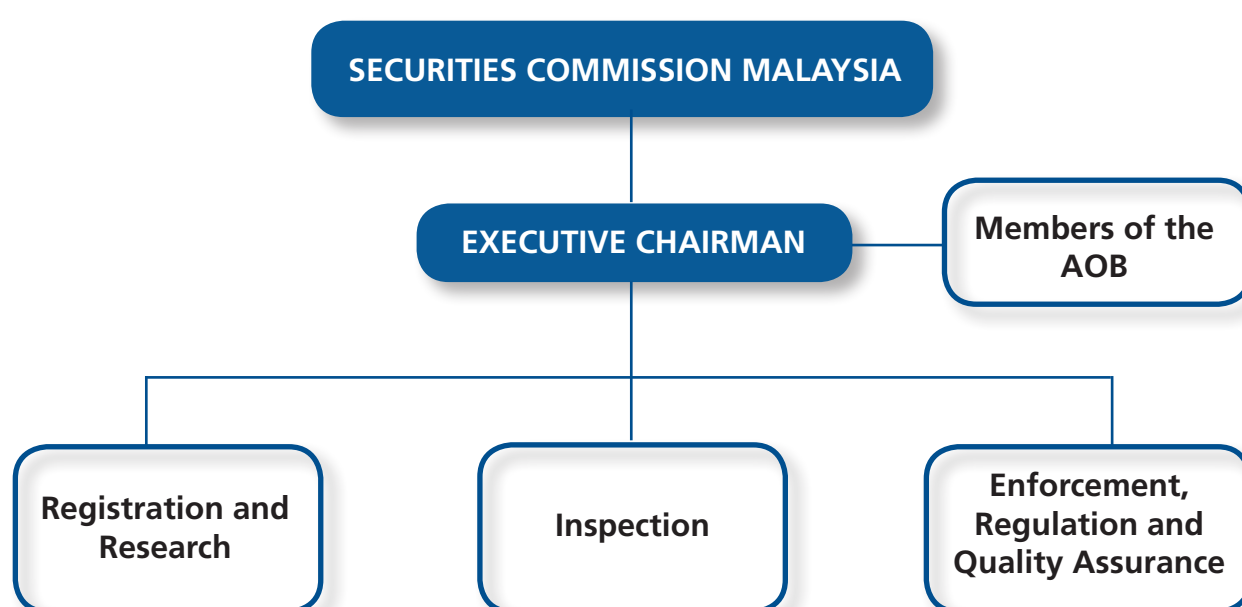
8. Perform such other duties or functions as the AOB determines necessary or appropriate to promote high professional standards of auditors and to improve the quality of audit services provided by auditors.

The Registration Committee was established in 2011 to determine matters regarding the approval of application for registration or recognition of auditors with the AOB. The Registration Committee recommends to the Board, wherein the Board deliberates and decides, for matters pertaining to revocation, suspension and non-approval.

The members of the Registration Committee are:

- Nik Mohd Hasyudeen Yusoff
- Goh Ching Yin

ORGANISATION STRUCTURE





PART 6

Financial Statements and Others



AUDIT OVERSIGHT BOARD

FINANCIAL STATEMENTS
FOR THE YEAR ENDED
31 DECEMBER 2014

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2014

	Note	2014 RM	2013 RM
Assets			
Current assets			
Other receivables	4	87,655	80,850
Cash and cash equivalents	5	1,118,651	828,350
Total assets		1,206,306	909,200
Reserves			
Funds from the Securities Commission Malaysia (SC)	6	12,500,000	9,000,000
Accumulated deficit	7	(11,379,980)	(8,120,800)
Total reserves		1,120,020	879,200
Current liabilities			
Other payables and accruals	8	86,286	30,000
Total liabilities		86,286	30,000
Total reserves and liabilities		1,206,306	909,200

The notes set out on pages 81 to 91 are an integral part of these financial statements.



Datuk Ranjit Ajit Singh
Chairman
Securities Commission Malaysia



Nik Mohd Hasyudeen Yusoff
Executive Chairman
Audit Oversight Board

Date: 29 January 2015

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2014

	Note	2014 RM	2013 RM
Income			
Registration fees		1,829,766	1,885,177
Finance income from fixed deposits	9	88,653	65,730
Other operating income		40,000	15,000
		<hr/>	<hr/>
		1,958,419	1,965,907
Operating expenditure			
Administrative expenses	10	(5,217,599)	(5,014,983)
		<hr/>	<hr/>
Deficit before tax		(3,259,180)	(3,049,076)
Tax expense	13	–	–
		<hr/>	<hr/>
Deficit for the year/Total comprehensive expense for the year		<hr/> <hr/> (3,259,180)	<hr/> <hr/> (3,049,076)

The notes set out on pages 81 to 91 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2014

	2014 RM	2013 RM
Cash flows from operating activities		
Deficit before tax	(3,259,180)	(3,049,076)
Adjustment for:		
Finance income	(88,653)	(65,730)
Operating deficit before changes in working capital	(3,347,833)	(3,114,806)
Change in other receivables	(6,805)	–
Change in other payables and accruals	56,286	(33,106)
Net cash used in operating activities	(3,298,352)	(3,147,912)
Cash flows from investing activities		
Finance income	88,653	65,730
Increase in restricted deposits	(40,000)	(15,000)
Net cash from investing activities	48,653	50,730
Cash flows from financing activity		
Funds received from the SC	3,500,000	3,000,000
Net cash from financing activity	3,500,000	3,000,000
Net increase/(decrease) in cash and cash equivalents	250,301	(97,182)
Cash and cash equivalents at 1 January	808,350	905,532
Cash and cash equivalents at 31 December	1,058,651	808,350
Cash and cash equivalents comprise:		
Cash and bank balances	118,651	328,350
Deposits placed with a licensed bank	1,000,000	500,000
	1,118,651	828,350
Less: Restricted deposits	(60,000)	(20,000)
	1,058,651	808,350

The notes set out on pages 81 to 91 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL

On 1 April 2010, the Securities Commission Malaysia (SC) established the Audit Oversight Board (AOB) under Section 31C of the *Securities Commission Act 1993* (SCA). The AOB was established for the purposes set out in Section 31B of the SCA, namely:

- a. to promote and develop an effective and robust audit oversight framework in Malaysia;
- b. to promote confidence in the quality and reliability of audited financial statements in Malaysia; and
- c. to regulate auditors of public interest entities.

To facilitate the abovementioned purposes, a fund known as the AOB Fund was established under section 31H of the SCA. The AOB Fund is administered by the SC. The SC provides administrative and accounting support to the AOB Fund and the accounts are kept separately from the accounts of the SC in accordance with Section 31L(5) of the SCA. The SC will continue to provide the necessary financial support to the AOB for the foreseeable future.

2. BASIS OF PREPARATION

(a) Statement of compliance

The financial statements of the AOB have been prepared in accordance with Malaysian Financial Reporting Standards (MFRSs) and International Financial Reporting Standards (IFRSs).

The following are accounting standards, amendments and interpretations that have been issued by the Malaysian Accounting Standards Board (MASB) but have not been adopted by the AOB.

MFRSs, Interpretations and amendments effective for annual periods beginning on or after 1 July 2014

- Amendments to MFRS 1, *First-time Adoption of Malaysian Financial Reporting Standards (Annual Improvements 2011–2013 Cycle)*
- Amendments to MFRS 2, *Share-based Payment (Annual Improvements 2010–2012 Cycle)*
- Amendments to MFRS 3, *Business Combinations (Annual Improvements 2010–2012 Cycle and 2011–2013 Cycle)*
- Amendments to MFRS 8, *Operating Segments (Annual Improvements 2010–2012 Cycle)*
- Amendments to MFRS 13, *Fair Value Measurement (Annual Improvements 2010–2012 Cycle and 2011–2013 Cycle)*
- Amendments to MFRS 116, *Property, Plant and Equipment (Annual Improvements 2010–2012 Cycle)*
- Amendments to MFRS 119, *Employee Benefits – Defined Benefit Plans: Employee Contributions*
- Amendments to MFRS 124, *Related Party Disclosures (Annual Improvements 2010–2012 Cycle)*
- Amendments to MFRS 138, *Intangible Assets (Annual Improvements 2010–2012 Cycle)*
- Amendments to MFRS 140, *Investment Property (Annual Improvements 2011–2013 Cycle)*

MFRSs, Interpretations and amendments effective for annual periods beginning on or after 1 January 2016

- Amendments to MFRS 5, *Non-current Assets Held for Sale and Discontinued Operations* (Annual Improvements 2012–2014 Cycle)
- Amendments to MFRS 7, *Financial Instruments: Disclosures* (Annual Improvements 2012–2014 Cycle)
- Amendments to MFRS 10, *Consolidated Financial Statements* and MFRS 128, *Investments in Associates and Joint Ventures – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*
- Amendments to MFRS 11, *Joint Arrangements – Accounting for Acquisitions of Interests in Joint Operations*
- MFRS 14, *Regulatory Deferral Accounts*
- Amendments to MFRS 116, *Property, Plant and Equipment* and MFRS 138, *Intangible Assets – Clarification of Acceptable Methods of Depreciation and Amortisation*
- Amendments to MFRS 116, *Property, Plant and Equipment* and MFRS 141, *Agriculture – Agriculture: Bearer Plants*
- Amendments to MFRS 119, *Employee Benefits* (Annual Improvements 2012–2014 Cycle)
- Amendments to MFRS 127, *Separate Financial Statements – Equity Method in Separate Financial Statements*
- Amendments to MFRS 134, *Interim Financial Reporting* (Annual Improvements 2012–2014 Cycle)
- Amendments to MFRS 101, *Presentation of Financial Statements: Disclosure Initiative*
- Amendments to MFRS 10, *Consolidated Financial Statements*, MFRS 12, *Disclosure of Interests in Other Entities* and MFRS 128, *Investments in Associates and Joint Ventures – Investment Entities: Applying the Consolidation Exception*

MFRSs, Interpretations and amendments effective for annual periods beginning on or after 1 January 2017

- MFRS 15, *Revenue from Contracts with Customers*

MFRSs, Interpretations and amendments effective for annual periods beginning on or after 1 January 2018

- MFRS 9, *Financial Instruments* (2014)

The AOB plans to apply the abovementioned standards, amendments and interpretations that are applicable and effective from the annual periods beginning on or after 1 July 2014, 1 January 2016, 1 January 2017 and 1 January 2018, respectively.

The initial application of the accounting standards, amendments or interpretations are not expected to have any material financial impacts to the current period and prior period financial statements of the AOB except as mentioned below:

MFRS 9, Financial Instruments

MFRS 9 replaces the guidance in MFRS 139, *Financial Instruments: Recognition and Measurement* on the classification and measurement of financial assets and financial liabilities, and on hedge accounting.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis other than as disclosed in Note 3.

(c) Functional and presentation currency

These financial statements are presented in ringgit Malaysia (RM), which is AOB's functional currency. All financial information is presented in RM.

(d) Use of estimates and judgements

The preparation of the financial statements in conformity with MFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

There are no significant areas of estimation uncertainty and critical judgements in applying accounting policies that have significant effect on the amounts recognised in the financial statements.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to the periods presented in these financial statements, and have been applied consistently by the AOB, unless otherwise stated.

(a) Financial instruments**(i) Initial recognition and measurement**

A financial asset or a financial liability is recognised in the statement of financial position when, and only when, the AOB becomes a party to the contractual provisions of the instrument.

A financial instrument is recognised initially, at its fair value plus, in the case of a financial instrument not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial instrument.

(ii) Financial instrument categories and subsequent measurement

The AOB categorises financial instruments as follows:

Financial assets

Loans and receivables

Loans and receivables category comprises other receivables and cash and cash equivalents.

Financial assets categorised as loans and receivables are subsequently measured at amortised cost using the effective interest method.

All financial assets are subject to review for impairment (see Note 3(c)).

Financial liabilities

All financial liabilities are subsequently measured at amortised cost using the effective interest method.

(iii) Derecognition

A financial asset or part of it is derecognised when, and only when the contractual rights to the cash flows from the financial asset expire or control of the asset is not retained or substantially all of the risks and rewards of ownership of the financial asset are transferred to another party. On derecognition of a financial asset, the difference between the carrying amount and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognised in equity is recognised in the profit or loss.

A financial liability or a part of it is derecognised when, and only when, the obligation specified in the contract is discharged, cancelled or expires. On derecognition of a financial liability, the difference between the carrying amount of the financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in profit or loss.

(b) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances and deposits with banks which have an insignificant risk of changes in fair value with original maturities of 3 months or less. For the purpose of the statement of cash flows, cash and cash equivalents are presented net of restricted deposits.

(c) Impairment

Financial assets

All financial assets are assessed at each reporting date whether there is any objective evidence of impairment as a result of one or more events having an impact on the estimated future cash flows of the asset. Losses expected as a result of future events, no matter how likely, are not recognised.

An impairment loss in respect of loans and receivables is recognised in profit or loss and is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account.

If, in a subsequent period, the fair value of the financial asset increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed, to the extent that the asset's carrying amount does not exceed what the carrying amount would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal is recognised in profit or loss.

(d) Income

Registration fees

Registration fees from the auditors of public interest entities are recognised in profit or loss when the payment is received.

Finance income

Finance income is recognised as it accrues using the effective interest method in profit or loss.

(e) Employee benefits

(i) Short-term employee benefits

Short-term employee benefit obligations in respect of salaries, annual bonuses, paid annual leave and sick leave are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid if the AOB has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) State plans

The AOBs contributions to statutory pension funds are charged to profit or loss in the financial year to which they relate. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

(f) Fair value measurement

Fair value of an asset or a liability is determined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The measurement assumes that the transaction to sell the asset or transfer the liability takes place either in the principal market or in the absence of a principal market, in the most advantageous market.

For non-financial asset, the fair value measurement takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

When measuring the fair value of an asset or a liability, the AOB uses observable market data as far as possible. Fair value are categorised into different levels in a fair value hierarchy based on the input used in the valuation technique as follows:

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that the AOB can access at the measurement date.

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: unobservable inputs for the asset or liability.

The AOB recognises transfers between levels of the fair value hierarchy as of the date of the event or change in circumstances that caused the transfers.

4. OTHER RECEIVABLES

	2014 RM	2013 RM
Deposits and prepayments	87,655	80,850

5. CASH AND CASH EQUIVALENTS

	2014 RM	2013 RM
Cash and bank balances	118,651	328,350
Deposits placed with a licensed bank	1,000,000	500,000
	<u>1,118,651</u>	<u>828,350</u>

Included in deposits placed with a licensed bank is RM60,000 (2013: RM20,000) restricted to be utilised for planning and implementing capacity building programmes in relation to the accounting and auditing profession.

The cash and cash equivalents are placed with a licensed bank which is under common control by the Government of Malaysia (a party that has an indirect influence on the AOB).

6. FUNDS FROM THE SECURITIES COMMISSION MALAYSIA

	2014 RM	2013 RM
Cash contribution:		
At the beginning of the year	9,000,000	6,000,000
Addition	3,500,000	3,000,000
	<u>12,500,000</u>	<u>9,000,000</u>
At the end of the year		

7. ACCUMULATED DEFICIT

	2014 RM	2013 RM
At the beginning of the year	(8,120,800)	(5,071,724)
Loss for the year	(3,259,180)	(3,049,076)
	<u>(11,379,980)</u>	<u>(8,120,800)</u>
At the end of the year		

8. OTHER PAYABLES AND ACCRUALS

	2014 RM	2013 RM
Amount due to the SC	65,086	—
Accruals	21,200	30,000
	<u>86,286</u>	<u>30,000</u>

The amount due to the SC is unsecured, interest free and repayable on demand.

9. FINANCE INCOME FROM FIXED DEPOSITS

	2014 RM	2013 RM
Interest income of financial assets that are not at fair value through profit or loss	88,653	65,730
	<u>88,653</u>	<u>65,730</u>

10. ADMINISTRATIVE EXPENSES

	2014 RM	2013 RM
The administrative expenses consist of:		
Auditors' remuneration	20,000	20,000
Honorarium payment	45,372	56,688
Non-executive members' allowance	81,000	87,000
Other miscellaneous charges	296,085	290,364
Rental of premises	328,350	311,286
Staff costs	4,446,792	4,249,645
	<u>5,217,599</u>	<u>5,014,983</u>

11. FINANCIAL INSTRUMENTS

11.1 Categories of financial instruments

The table below provides an analysis of financial instruments categorised as follows:

- (a) Loans and receivables (L&R); and
- (b) Financial liabilities measured at amortised cost (FL).

	Carrying amount RM	L&R RM	FL RM
2014			
Financial assets			
Other receivables, excluding prepayments	80,850	80,850	–
Cash and cash equivalents	1,118,651	1,118,651	–
	1,199,501	1,199,501	–
Financial liabilities			
Other payables and accruals	(86,286)	–	(86,286)
2013			
Financial assets			
Other receivables	80,850	80,850	–
Cash and cash equivalents	828,350	828,350	–
	909,200	909,200	–
Financial liabilities			
Other payables and accruals	(30,000)	–	(30,000)

11.2 Gains arising from financial instrument

	2014 RM	2013 RM
Gains on:		
Loan and receivables	88,653	65,730

11.3 Financial risk management objectives and policies

The AOB is primarily exposed to liquidity risk in the normal course of the AOB's operations. As the AOB is administered by the SC, the AOB is subject to the SC's financial risk management policies.

11.4 Credit risk

Credit risk is the risk of a financial loss to the AOB if a counterparty to a financial instrument fails to meet its contractual obligations.

The AOB is not exposed to any credit risk as the AOB does not have any trade debts.

11.5 Liquidity risk

Liquidity risk is the risk that the AOB will not be able to meet its financial obligations as they fall due.

The AOB, via the SC, monitors and maintains a level of cash and cash equivalents deemed adequate to finance the AOB's operations and to mitigate the effects of fluctuations in cash flows.

Maturity analysis

The table below summarises the maturity profile of the AOB's financial liabilities as at the end of the reporting period based on undiscounted contractual payments.

	Carrying amount RM	Contractual cash flow RM	Under 1 year RM
2014			
Financial liabilities			
Other payables and accruals	86,286	86,286	86,286
2013			
Financial liabilities			
Other payables and accruals	30,000	30,000	30,000

11.6 Market risk

Market risk is the risk that changes in market prices, such as interest rates that will affect the AOB's financial position or cash flows.

11.6.1 Interest rate risk

The interest rate profile of the AOB's significant interest-bearing financial instruments, based on carrying amounts as at the end of the reporting period was:

	2014 RM	2013 RM
Fixed rate instruments		
Financial assets	1,000,000	500,000

Interest rate risk sensitivity analysis

Fair value sensitivity analysis for fixed rate instruments

The AOB does not account for any fixed rate financial assets at fair value through profit or loss, and the AOB does not designate derivatives as hedging instruments under a fair value hedge accounting model. Therefore, a change in interest rates at the end of the reporting period would not affect profit or loss.

11.7 Fair values

In respect of cash and cash equivalents, other receivables, other payables and accruals, the carrying amounts approximate fair value due to the relatively short-term nature of these financial instruments.

12. FUND MANAGEMENT

The AOB's objective is to maintain adequate reserves to safeguard the AOB's ability to perform its duties and functions independently. The reserves are managed by the SC.

13. TAX EXPENSE

The SC was granted approval from the Minister of Finance to be exempted from taxation with effect from Year Assessment (YA) 2007 until YA 2014. Accordingly, the AOB is tax-exempted.

14. AUTHORISATION OF FINANCIAL STATEMENTS

The financial statements for the year ended 31 December 2014 were authorised by the SC for issuance and signed by the Chairman of the SC and Executive Chairman of AOB on 29 Januari 2015.

STATUTORY DECLARATION

I, **Vignaswaran A/L Kandiah**, the officer primarily responsible for the financial management of Audit Oversight Board, do solemnly and sincerely declare that the financial statements set out on pages 78 to 91 are, to the best of my knowledge and belief, correct and I make this solemn declaration conscientiously believing the same to be true, and by virtue of the provisions of the *Statutory Declarations Act, 1960*.

Subscribed and solemnly declared by the abovenamed in Kuala Lumpur on 29 January 2015.



.....
Vignaswaran A/L Kandiah

Before me:



38A, JALAN TUN MOHD FUAD 1
TAMAN TUN DR. ISMAIL
60000 KUALA LUMPUR

INDEPENDENT AUDITORS' REPORT TO THE AUDIT OVERSIGHT BOARD

REPORT ON THE FINANCIAL STATEMENTS

We have audited the financial statements of the Audit Oversight Board (AOB), which comprise the statement of financial position as at 31 December 2014, and the statements of profit or loss and other comprehensive income, and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages 78 to 91.

Commission Members' Responsibility for the Financial Statements

The Commission Members of the Securities Commission Malaysia (Commission) are responsible for the preparation of financial statements so as to give a true and fair view in accordance with Malaysian Financial Reporting Standards and International Financial Reporting Standards. The Commission Members are also responsible for such internal control as the Commission Members determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with approved standards on auditing in Malaysia. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Commission's preparation of the financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the AOB's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Commission Members, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the AOB as of 31 December 2014 and of its financial performance and cash flows for the year then ended in accordance with Malaysian Financial Reporting Standards and International Financial Reporting Standards.


OTHER MATTERS

This report is made solely to the Securities Commission Malaysia, as a body, and for no other purpose. We do not assume responsibility to any other person for the content of this report.



KPMG

Firm Number: AF 0758
Chartered Accountants



Loh Kam Hian

Approval Number: 2941/09/16(J)
Chartered Accountant

Petaling Jaya, Malaysia

Date: 29 January 2015

ACRONYMS AND ABBREVIATIONS

AARG	ASEAN Audit Regulators Group
AASB	Auditing and Assurance Standards Board
ACCA	Association of Chartered Certified Accountants
ACGA	Asian Corporate Governance Association
ACRA	Accounting and Corporate Regulatory Authority, Singapore
AFM	Netherlands Authority for the Financial Markets
AICPA	American Institute of Certified Public Accountants
AIF	Asian Institute of Finance
AOB	Audit Oversight Board
AQI	Audit Quality Indicator
ASEAN	Association of Southeast Asian Nations
BNM	Bank Negara Malaysia
CAQ	Center for Audit Quality
CCM	Companies Commission of Malaysia
CEAOB	Committee of European Auditing Oversight Bodies
CG	Corporate Governance
CICPA	Chinese Institute of Certified Public Accountants
CPA Australia	Certified Practising Accountants Australia
CPE	Continuing Professional Education
CSAP	Committee to Strengthen the Accountancy Profession
EAIG	European Audit Inspection Group
EC	European Commission
EQCR	Engagement Quality Control Reviewer
ESB	Ethics Standards Board
ESMA	European Securities and Markets Authority
EU	European Union
FPLC	Federation of Public Listed Companies Bhd
GPPC	Global Public Policy Committee
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
IIAM	Institute of Internal Auditors Malaysia
IIRC	International Integrated Reporting Council

ISA	International Standards on Auditing
ISQC	International Standards on Quality Control
MASB	Malaysian Accounting Standards Board
MAVCAP	Malaysia Venture Capital Management Bhd
MFRS	Malaysian Financial Reporting Standards
MIA	Malaysian Institute of Accountants
MIA By-Laws	MIA By-Laws (On Professional Ethics, Conduct and Practice)
MICG	Malaysian Institute of Corporate Governance
MICPA	The Malaysian Institute of Certified Public Accountants
MVCA	Malaysian Venture Capital and Private Equity Association
MVCDC	Malaysian Venture Capital Development Council
PAOC	Public Accountants Oversight Committee
PCAOB	Public Company Accounting Oversight Board
PIE	Public-interest entity
PLC	Public-listed company
RWG	Regulatory Working Group
SC	Securities Commission Malaysia
SCA	<i>Securities Commission Act 1993</i>
SEC	Securities and Exchange Commission
UK	United Kingdom
US	United States of America

DEFINITIONS

Auditor	An individual auditor or audit firm who is registered or recognised under section 31O of the SCA as an auditor of a PIE.
Big Four Audit Firms	Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers.
Major Audit Firms Audit	Firms with more than 10 partners and audit more than 40 PIEs with a total market capitalisation of above RM15 billion.
Other Audit Firms	Mid-tier audit firms and sole proprietors.
Public-interest entity (PIE)	Entity specified in Schedule 1 of the SCA: <ul style="list-style-type: none"> (a) a PLC or a corporation listed on the stock exchange; (b) a licensed institution licensed under the <i>Banking and Financial Institutions Act 1989</i>; (c) an insurance company licensed under the <i>Insurance Act 1996</i>; (d) a takaful operator registered under the <i>Takaful Act 1984</i>; (e) an Islamic bank licensed under the <i>Islamic Banking Act 1983</i>; (f) a developmental financial institution prescribed under the <i>Development Financial Institutions Act 2002</i>; (g) a holder of the Capital Markets Services Licence for the carrying on of the regulated activities of dealing in securities, dealing in derivatives or fund management; and (h) any other person as the Minister may, by order published in the <i>Gazette</i>, prescribe.

