BY MAJELLA GOMES

Left to right: Philip Satish Rao, Tun Dato' Seri Zaki Tun Azmi, Datuk Azlan Abdul Karim, Dato' Mohammad Faiz Azmi and Wee Hock Kee

Conference delegates

SETTING THE TONE

AS KEY MEMBERS OF THOSE CHARGED WITH GOVERNANCE (TCWG), HOW CAN BOARD AUDIT COMMITTEES DISCHARGE THEIR OVERSIGHT PROPERLY AND SET THE RIGHT TONE FOR GOOD GOVERNANCE? DRILLING DOWN, HOW SHOULD BOARD AUDIT COMMITTEES MANAGE THE DISCLOSURE AND RESOLUTION OF KEY AUDIT MATTERS (KAMs) TO COMPLY WITH NEW REGULATIONS GOVERNING THE NEW AUDITOR'S REPORT?

"THE Audit Committee is probably any firm's most critical body but it faces the most challenges," said MIA President Dato' Mohammad Faiz Azmi, pulling no punches in his welcome address at the recent Audit Committee Conference 2016.

Since 1994, it has been mandatory for all listed companies to have Audit Committees. Perhaps one of the most pivotal duties of the Audit Committee is to set the right tone from the top to foster good corporate governance, enforce professional behaviour, shape core values and ultimately instil market confidence, remarked Ken Pushpanathan, Chairman, Audit Committee, Bursa Malaysia. Apart from possessing the prerequisite expertise and being fully conversant with processes and regulations, Board Audit Committees must be confident enough to challenge senior management's views, and hold them to account. "You don't need 'yes-men'; you need people who will question and challenge," Pushpanathan quipped.

CREATING THE RIGHT CULTURE

Tone from the top starts with a shared code of ethics. "You need to have shared values like company loyalty and professionalism," said Datuk Azlan Abdul Karim, CEO, Putrajaya Holdings. "Without the right values, you can't set the right tone."

Perhaps it is most important that an appropriate culture should permeate the organisation from the top down. "CFOs, CEOs and others in senior management need to have strong personal integrity in order to drive governance," Wee Hock Kee, Managing Partner, CG Board Asia Pacific commented.

Left to right: Abdul Rahim Abdul Hamid, Leong Wai Leng, David S. Berry, Seah Gek Choo and Lee Tuck Heng

THE AUDIT COMMITTEE IS PROBABLY ANY FIRM'S MOST CRITICAL BODY BUT IT FACES THE MOST CHALLENGES.

Dato' Mohammad Faiz Azmi
MIA President

Staff are an integral part to culture, and hence must be clear on the concept of good governance and ethics. Dato' Faiz said organisations must make expectations clear to staff when they are employed. To develop a healthy culture, Tun Dato' Seri Zaki Tun Azmi, Chairman, Astro Malaysia Holdings Bhd suggested rewarding employees well but stressed that punitive action for wrongdoing was important too. Firms should also conduct regular reality checks and chat with personnel in the lower ranks because "management may not admit they are having problems," asserted Dato' Faiz. "Information is inevitably filtered so you have to go down to the ground to get a real sense of what is happening," he added.

Remember that toxic cultures do not develop overnight; hence, lines of defence must be developed in parallel, over time, as a counter-measure. As one of the chief defences, "the AC should be independent and always aware of organisational culture," Wee advised. "Soft governance may be more effective as this is a highly sensitive area."

But fitting the right director to the right task is not easy. Directors' training is imperative; the more a director knows about the firm, the more effective he/she can be. At the same time, the longer the tenure, the less independent the director.

Training is especially critical because "Regulators want audit committees to do more," said David S. Berry, Deputy President, Malaysia Institute of Corporate Governance. "Bursa Malaysia is looking at financial reporting issues, significant and business judgement calls, and unusual transactions and events," in order to alleviate concerns relating to possible material misrepresentation and high levels of uncertainty.

GETTING CONVERSANT WITH KAMs

This is where Key Audit Matters (KAMs) come in as a mechanism to guide Audit Committees on how to identify red flags and resolve these in order to inspire better governance and market confidence. Since 16 December 2015, it has been mandatory that KAMs be shared in the Auditor's Report. This includes highlighting significant matters and judgements, and detailing how these were identified, addressed and resolved. Cautioning that KAMs should never make a first appearance in the audit report, Lee Tuck Heng, Chairman, Auditing & Assurance Standards Board (AASB), MIA said they should have already been reported and thoroughly discussed beforehand. "KAMs should be presented clearly in a format similar to the annual report," he said. "Almost 87% of annual reports received had statements but only about 20% had really insightful information."

Commenting on how to determine if additional disclosures on KAMs are required, Abdul Rahim Abdul Hamid, former MIA President and the Audit Committee Chairman of several listed companies said, "There is enough literature and technical assistance available. What is more challenging is having the 'heart' to deal with them. It's about directorial independence and whether one has an independent enough mind."

In tandem with the greater expectations placed on their shoulders, Board members seem to be demonstrating a growing sense of responsibility. Leong Wai Leng, GM & Head of Corporate Surveillance, Securities Commission remarked that Audit Committees were now taking it upon themselves to be more forthcoming when handling KAMs. "They're making sure they are protecting themselves, especially if they do not agree with management on particular issues," she said. "However, some walk away the moment things get uncertain. A more proactive stance is needed."

Perhaps Boards should consider bringing external help on Board to lighten their loads. Seah Gek Choo, Audit Partner, Deloitte Singapore, said, "There is nothing to stop the Audit Committee from getting more information or help to clarify a situation. Some have been proactive; they have actually referred to regulators when they encounter difficulties."

AUDIT COMMITTEES ARE THE FRONTLINE THAT KEEPS MANAGEMENT PROACTIVE ABOUT DOING WHAT IS RIGHT FOR SHAREHOLDERS. I ENCOURAGE EVERYONE TO TAKE AUDITORS' VIEWS VERY SERIOUSLY BECAUSE THEY'RE TELLING YOU WHAT YOUR RISKS ARE.

While he does recommend bringing in outside expertise, this is no substitute for your own learning, said Rahim. "You do need to understand in-depth the business of the company on whose Board you sit – only then can you make informed decisions." His personal practice is to meet the head of the organisation's Audit Committee privately to discuss matters, twice a year. "That way, you understand what the real problems are," he said.

ETIQUETTE WITH STAKEHOLDERS

While greater transparency is encouraged, it's still a personal call for directors when it comes to meeting with individual parties who have issues to discuss. "Any shareholder can ask questions at any time," Berry said. "But there are constraints; it should not be a secret meeting, for instance!" Abdul Rahim agreed, divulging that he has declined such meetings before as they were unethical.

Regarding what should be published in annual reports, it was generally felt that shareholders were being overwhelmed by the amount of information available, and could be distracted by unhelpful information. What should they look for? "At least read the KAMs," Seah advised. "They will give an idea of the Audit Committee's concerns and the auditor's views." "Audit Committees are the frontline that keeps management proactive about doing what is right for shareholders. I encourage everyone to take auditors' views very seriously because they're telling you what your risks are," concurred Leong.

BREACHES IN OVERSIGHT

Director's liabilities are an increasingly important area of focus as regulators tighten enforcement. As the regulating authority, Bursa can investigate breaches and take action, ie, suspend or de-list the company. It has fined directors before for breaches in reporting and inaccurate or misleading information.

Citing Transmile, Enron and Satyam as examples of how not to govern a business, Dato' Azmi Mohd Ali, Senior Partner, Azmi & Associates said that once a member of the Audit Committee is found guilty of breach, he will still be liable even if he has retired from the position, if the offence took place during his tenure. When the Audit Committee is found in breach of its duties, the company can make the rest of the board of directors liable as well. Remarking that many people do not understand the financial liabilities of directors, YM Raja Dato' Idris Raja Kamaruddin, Chairman, Kumpulan Perangsang Selangor said that personal liberty was at stake. "No directors' fees will ever be sufficient if you are slapped with a penalty by Bursa," he said. "You are governed by its regulations while you are a Board member – and beyond!" If there was any doubt, he advised seeking external advice. "Nobody can know everything," he said.

If terms of reference allow the use of external experts, do take advantage of this clause. Independent directors have the right to say "No", and can call for special or status audits if required. Four types of risk – strategic, operational, financial and regulatory – need to be considered by Audit Committees and directors, clarified Datuk Mohd Anwar Yahya, Advisor, PwC Malaysia. "Ensure the company has a risk framework in place, and always get a third party to evaluate this or give a professional opinion," he said.

To a question on the difference between Bursa and SC penalties, it was explained that while Bursa tended to impose penalties, fines or sanctions, SC brought action against fraudulent practices. SC penalties were heavier, and could extend to confiscating assets. What can be done when collective decisions are taken which individual directors may not agree with? The consensus was that the best recourse is to have your dissent documented in the minutes to protect yourself against possible punitive action. ■