

**NEWS PAPER CUTTING ON JUNE 2021  
THE STAR**

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# The essential role of an audit



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## Inside insights

THE powers and duties of an auditor are clearly defined under Section 266 of the Companies Act, 2016. Here, the law states that an auditor has a statutory duty to report to members with regards to the financial statements, company's accounting and other records related to those financial statements.

The auditor is also required to state in a report whether the financial statements presented give a true and fair view of the affairs of the company. An auditor is required to provide reasons if he or she is not satisfied with any matters related to the financial statements.

The function of an auditor is also clearly defined in the code of corporate governance, which came about mainly due to corporate failures, losses, scandals, economic turmoil as well as demand from stakeholders.

The origins of corporate governance itself can be traced back to the United States. The US Securities and Exchange Commission (SEC) led the early establishment of corporate governance among corporates when it required companies to have audit committees among listed companies.

In the 1980s, as the US stock market was rapidly developing and more and more US companies saw the emergence of institutional investors, the demand from these investors grew as they wanted to have

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more say on how these corporates were run with greater accountability and transparency.

The institutional demand grew louder in the 1990s but nothing materially changed until the Enron and WorldCom cases emerged in early 2000. These two corporate failures were the cornerstone of change when it came to corporate governance and the role of auditors.

### Fictitious accounting

In Enron's case, it was revealed that the board failed to perform its duty as fictitious accounting and earnings were reported. The board was more concerned on the value of their shareholding, and to maintain Enron's stock price, they effectively adopted strategies that were high risk and to ensure reported earnings can be managed to meet market expectations. Enron has since become a well-known example of wilful corporate fraud and corruption.

The scandal also brought into question the accounting practices and activities of many corporations in the United States and was a factor in the enactment of the Sarbanes-Oxley Act, 2002. The scandal also caused the dissolution of Arthur Andersen, one of the largest audit firms globally then.

In WorldCom's case, the company was caught using creative accounting in book-

ing "line costs" (interconnection expenses with other telecommunication companies) as capital expenditures on the balance sheet instead of expenses and inflating revenues with bogus accounting entries from "corporate unallocated revenue accounts".

In recent times, we have seen some large financial scandals too involving companies like Wirecard of Germany, Luckin of China, or even Hin Leong from Singapore. Historically, Malaysia too has its fair share of scandals that has brought shame and ridicule. We have seen in the past how scandals like the Pan-EI crisis of the 1980s or the case of Transmile's accounting scandal in early 2007 cause significant losses to investors.

In some of these cases, it is the management of the companies themselves who were involved but at the same time, the auditors too failed to detect early warning signs, until it was too late.

One does not need to go very far as even in the case of IMDB we had observed how auditors had performed their fiduciary duty as earlier appointed auditors could not complete their work, resulting in a change of auditors. When new auditors were brought in, despite vouching for the financial statements, they disowned their own opinions later on following the report from the Department of Justice (DoJ).

### The dynamics of the Serba saga

Over the past 10 days or so, the most talked about story in the financial market was that of Serba Dinamik. It all started on May 7, 2021, when the company announced to Bursa Malaysia that it was changing its financial year from a December year-end to a June 2021 year-end, or effectively an 18-month financial period from its last audited accounts of Dec 31, 2019, or the financial year 2019 (FY19).

The reason cited by Serba based on stock exchange filing was "continuing extension of the movement control order (MCO) in Malaysia and lockdowns in countries in which the group have hampered the ability to finalise the group's financial statements; expansion of groups operations in new countries further add to more time required to finalise financial statements; to facilitate better audit planning and allocation of resources to avoid the peak financial reporting period".

The market took little attention to this change in year-end by the company but there were some red flags from here itself. For example, the company announced its full-year unaudited financial results for FY20 on February 26, 2021. There was no mention about any change in the year-end then, and judging by the preceding year's FY2019 timeline, Serba, after announcing the year-end results in that year, had issued its annual report (AR) on May 29, 2020. In that AR, the auditors and directors had signed off the financial statements and the audit report on May 6, 2020.

Based on this, it does seem that the audit work carried out for FY20 by the auditors was well within the timeline set in previous years. It was only revealed to the market via Serba's response to the exchange and an online corporate and media presentation done last Saturday, May 29, 2021,

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## RM2.89bil in market cap has been wiped out due to uncertainty

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that the audit matters were raised by the auditors on May 3, 2021.

Interestingly, in the FY19 audit report, the auditors had highlighted three key audit matters then and they include:

- > Existence, accuracy and completeness of revenue recognition;

- > Completeness and existence of material on-site amounting to RM908mil; and

- > Valuation of trade receivables and contract assets valued at RM1,526mil.

In FY19, the auditors addressed these key audit matters via various methods and means to ensure the financial statements were accurately reflectively of the balances presented.

Hence, on May 25, 2021, to the surprise of the market, Serba announced that it was seeking suspension of trading of its shares as it was informed by its auditors "on some matters" on the statutory audit and at the same time the board announced that it is appointing an independent firm to commence a special independent review to assess the veracity and accuracy of the matters.

Serba shares remained suspended for the rest of last week, pending the release of further information.

On May 28, 2021, Serba announced that it has received a special notice from a non-independent, non-executive director

with a shareholding of 15.96% for the company to convene an EGM, to remove its current auditors and to appoint BDO PLT as new auditors of the company for the new financial year ending June 30, 2021.

On the same day, Serba also detailed out its response dated May 6, 2021, on the key audit matters that were raised by its auditors three days before that, as explained earlier. Serba claims that while it has responded to the matters that were raised by the auditors, the auditors themselves have not reverted to the company.

Last Saturday afternoon, in a rather unusual and rushed dissemination of information, Serba called for analysts/fund managers briefing as well as a separate media briefing on the chronology of events that has occurred.

Serba must be applauded for making the effort to come clean and to explain to investors and the media its side of the story for the matters that were raised by the auditors.

At the same time, we have also heard from Serba that the present auditors have reached out to independent directors of the company concerning the key audit matters. While it was not mentioned who these independent directors are, a quick check on the latest board of directors list suggests that Serba has nine board members, of which five are independent non-executive directors (INED), including

one senior INED.

The audit committee (AC) comprises four members, with the senior INED as chairman and two others being the INED. Only one of the AC members is a non-independent non-executive director.

Hence, since the present auditor has reached out to the INED, it can be concluded that at least three of them are AC members. Of the three INED AC members, two are members of the Malaysian Institute of Accountants (MIA) and one of them is a former partner of the present audit firm.

There is indeed no reason to doubt as to why the auditors have reached out to the INED and in particular, the INED who are AC members, as they do understand and can comprehend the issues that have been raised by the auditor.

In a late statement on Thursday, the INEDs too have expressed their concern on matters raised by the auditors and are taking steps to resolve the issues at hand, which include the appointment of an independent firm to assess the veracity and accuracy of the matters raised by the auditors, independently and objectively, without any element of interference from any party.

### The time to come clean is now

The market doesn't like uncertainty. At the time of writing, Serba's share price

was last seen at 83.5 sen as at Thursday's close, or 48.1% lower than its pre-suspension price of RM1.61. Some RM2.89bil in market capitalisation has been wiped out due to the uncertainty created by this impasse between the board and the auditor.

It has also wide repercussions for the company's bonds as rating agencies have downgraded the debt papers. Regulators have stepped in to investigate the matter. With the pressure coming from various stakeholders as well as concerns raised by several institutional investors, the special notice issued earlier has since been withdrawn.

Serba has taken measures to buy time by extending its accounting period to June 30 and this will allow the present auditors to complete the audit in time.

While time is of the essence, and investigations carried out by the regulators may take time, it is also important for the market to hear from the auditors themselves as to their side of the story, especially now that the special notice has been withdrawn.

After all, the issue at hand is related to audit matters and only they could put the record straight.

Pankaj C. Kumar is a long-time investment analyst. The views expressed here are his own.



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# Digitalisation to curb public sector corruption

Tengku Zafrul: It will reduce contact between parties

## TECHNOLOGY

By GANESHWARAN KANA  
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**PETALING JAYA:** The digitalisation of government services would serve to curb leakages, fraud and corruption within the public sector, according to Finance Minister Tengku Datuk Seri Zafrul Abdul Aziz.

He said that by moving the traditional government services online, it will reduce direct contact points between citizens and public officials, and hence minimise chances for corruption to occur.

In addition, the digitalisation efforts would also modernise public service delivery, enhance efficiency and expedite direct government assistance to ensure inclusiveness, accessibility, transparency and accountability.

"So far, direct aids have been done mostly on a cashless basis, where applications and payments for Bantuan Prihatin Rakyat and Geran Khas Prihatin are made electronically and online.

"In the near future, under MyDigital, the Finance Ministry will ensure payments for all government services by 2022 are made on a cashless basis.

"This will lead to higher transactional security, better coordination, enhanced communication on anti-corruption initiatives and greater ease of sharing information," Tengku Zafrul said.

He was speaking at the Malaysian Institute of Accountants (MIA) International Accountants Conference 2021 held virtually

***"In the near future, the Finance Ministry will ensure payments for all government services by 2022 are made on a cashless basis."***

Tengku Datuk Seri Zafrul Abdul Aziz

yesterday. In his remarks, Tengku Zafrul expressed his appreciation to MIA, among others, for its advocacy on sustainability and the environment, social and governance (ESG) principles.

Meanwhile, in a separate panel session that featured economists Mohd Afzanizam Abdul Rashid and Prof Jomo Kwame Sundaram, the topic of taxation in the post-pandemic world was discussed.

Jomo said the government should begin discussing greater tax reforms and the introduction of new taxes.

"Unfortunately, in countries like Malaysia, there has been very little public discussion about how to improve taxation.

"There are two major challenges, one is to have much greater tax collection.

"We have a huge problem there because we have many leakages and other problems with the system.

"There needs to be a unified tax system in Malaysia. Why do you have a customs authority that is completely unintegrated with the Inland Revenue authority?

"The other challenge is the progressiveness of the taxation system. We need a far more comprehensive, equitable and progressive

view in reforming the system," he said.

Jomo pointed out that there is a possibility for the government to generate additional revenue by imposing windfall and other capital gains taxes, although he said the tax proceeds "won't be very much".

Meanwhile, Mohd Afzanizam said the Covid-19 pandemic had accentuated the level of inequality in society, making it more difficult for the government to prescribe a new taxation system.

"Nevertheless, this crisis has opened up opportunities for the policy makers to rethink what are the best means to not just raise revenues, but also to redistribute wealth between the rich and the poor.

"Obviously, taxation is one of the mechanisms but the philanthropy economy such as donations or in the case of Islamic economy, *waqf* (endowment), is something that we need to look at more seriously at the moment," said Mohd Afzanizam.

Watch the video  
TheStarTV.com



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## 1MDB sues Riza Aziz, Hollywood studio for RM1bil

By NURBAITI HAMDAN  
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**KUALA LUMPUR:** Hollywood producer Riza Aziz Abdul Aziz has been sued by the 1Malaysia Development Bhd (1MDB) and its three subsidiaries for allegedly misappropriating US\$250mil (RM1.03bil) which was said to have been used for real estate purchases and financing movie productions.

According to a court document, Riza Aziz, who is also the stepson of former prime minister Datuk Seri Najib Razak, was named as the first defendant while a film company he co-founded, Red Granite Pictures Inc., was the second defendant.

Red Granite Capital Ltd, a related company, was named the third defendant and US-based law firm Shearman & Sterling was the fourth defendant.

The other three 1MDB subsidiaries which are the plaintiffs are 1MDB Energy Holdings Ltd, 1MDB

Energy Ltd and 1MDB Energy (Langat) Ltd.

The matter was brought up for case management before the Kuala Lumpur High Court yesterday.

According to the writ of summons, 1MDB claimed that Riza Aziz had received approximately US\$250mil in funds that were misappropriated from the sovereign wealth fund by its officers and their associates in 2011 and 2012.

It said that Riza Aziz, who controlled Red Granite Pictures and Red Granite Capital, "knew or ought to have known that those funds had been misappropriated".

It claimed that Riza Aziz and the two companies allegedly used the funds for their personal benefit and for the benefit of their associates, including for the purposes of financing movie productions and purchasing various real estate.

It also claimed that the fourth defendant Shearman & Sterling had allegedly permitted Riza Aziz and his associate, fugitive financier

Low Taek Jho (better known as Jho Low), to use the law firm's interest on lawyer accounts to launder substantial portion of the misappropriated funds.

1MDB wants, among others, a court declaration that Riza Aziz and the two companies are liable for the misappropriated funds and alternatively, a declaration that the plaintiffs are entitled to repayment of the said funds allegedly received by the three defendants on the basis of unjust enrichment as a consequence of the misappropriation.

The lawsuit is among 22 legal papers filed by 1MDB and its subsidiary SRC International Sdn Bhd against individuals, including 1MDB's former board of directors who allegedly defrauded the companies.

It was reported that the Finance Ministry confirmed that 1MDB and SRC filed a total of 22 civil suits to recover assets worth over RM96.6bil, including about

RM300mil against various local parties.

The ministry had said the writs, filed on May 7, comprised six by 1MDB and 16 by SRC.

The writs filed by 1MDB are against nine entities, including two foreign financial institutions, and 25 individuals, while those filed by SRC are against eight entities and 15 individuals for various wrongdoings.

The wrongdoings include breach of contractual, statutory, common law and fiduciary duties; breach of trust; fraud; conspiracy to defraud; fraudulent misrepresentation; fraudulent breach of duties and trust; abuse of power; breach of fiduciary duties in public office; and dishonest assistance in misappropriation of funds.

Red Granite Pictures is the studio behind the 2013 movie *The Wolf of Wall Street*, directed by Martin Scorsese and starring Leonardo DiCaprio, Jonah Hill, Margot Robbie and others.

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## Another bank employee held in kickback scandal

**KLANG:** Another man who was alleged to have a role in seeking bribes for over 110 bank loans amounting to RM18mil issued in the last two years has been arrested by the Malaysian Anti-Corruption Commission (MACC).

The 35-year-old bank employee is the latest suspect held by the MACC on Monday evening.

Six others were arrested last week for similar allegations.

A seven-day remand order was issued to the man by magistrate Parvin Hameedah Natchiar at the Shah Alam Magistrate's Court yesterday to enable MACC to question him further on the allegation of soliciting and receiving bribes from personal loan applicants between 2018 and 2020.

The man was detained after

MACC recorded his statement pertaining to the alleged bribes at their Selangor office on Monday.

The court also granted an additional four-day remand order to six other bank employees, aged between 36 and 45.

The extension was to enable MACC to question the suspects further.

All seven men, employed at several banks in the Klang Valley, were investigated for allegedly seeking inducements involving 110 loan transactions amounting to RM18mil.

These men were alleged to have asked for between 15% and 35% kickbacks from the principal amounts sought by the applicants who did not qualify to borrow money from the respective banks.



**Remand extended:** The suspects being escorted into the Shah Alam Magistrate's Court. — KK SHAM/The Star

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## Four remanded over alleged bribery linked to RM42mil tender project

By MAZWIN NIK ANIS  
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**PUTRAJAYA:** An assistant under-secretary of a ministry has been remanded for allegedly demanding bribes from a company involved in a supply tender worth RM42mil for an enforcement agency.

It is understood that the man, in his 40s, had demanded 5% from the

company that was awarded the four-year project to supply, process, print and post summonses issued by the enforcement agency from 2020 to 2023.

Also remanded were the contractor as well as two staff members of the company who allegedly paid the civil servant.

Sources said the man had set 5% to be paid to him based on the

progress payment received by the company from the government.

"Investigators are in the process of determining how much the man has received so far," said a source.

All four were arrested at 10pm on Tuesday at the Malaysian Anti-Corruption Commission (MACC) headquarters.

They were brought before Magistrate Shah Wira Abdul Halim,

who allowed MACC prosecutors to remand them for six days beginning yesterday.

The case is being investigated under Section 16(a)(A) of the MACC Act 2009.

In another case, a 43-year-old businessman has been remanded for five days for suspected involvement in money laundering.

He was arrested on Tuesday.

He is believed to have obtained money through the sale of a Ferrari worth nearly RM1mil that did not belong to him, to purchase a Lamborghini for himself that cost almost RM1.8mil.

The case is being investigated under Section 4 of the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001.