

ACCOUNTING PRACTICES IN MALAYSIA

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SINOPSIS

Kertas ini bertujuan memberi ulasan praktik perakaunan yang diamalkan di Malaysia berbanding dengan standard yang dibuat oleh International Accounting Standards Committee (IASC). Satu percubaan telah dibuat menganalisisan perbezaan praktik dari IAS dan sebab-sebabnya. Seterusnya kertas ini mencadangkan cara-cara untuk meminimumkan perbezaan pada masa depan.

SYNOPSIS

This paper comments on the significant accounting practices adopted in Malaysia against the Standards set by the International Accounting Standards Committee (IASC). An attempt is made to analyse any departure from the IAS and the reasons thereof, as well as to suggest means of minimizing the diversities in future.

INTRODUCTION

Financial statements are intended to provide information about the enterprise they relate to such interested parties as the shareholders, potential investors, creditors, employees, tax authority and other government agencies. The financial statements may not meet the needs of all these parties to the same extent. However, they should at least be capable of being understood by all such parties to mean the same thing. Unfortunately, this is often not the case. Because of the diversities in the accounting practices adopted, the same financial statements can be interpreted in different ways by different readers.

Consequently, the usefulness of financial statements in providing a basis for decision making becomes severely restricted. Worst of all, the diversities in accounting practices have been unscrupulously used as justification for financial statements which are misleading. The accounting profession and the regulatory authorities in several countries have expressed deep concern over the problems arising out of the diversities in the accounting practices adopted. Legislative guidelines have been proposed in some countries. In response, the accounting profession in several countries have issued guidelines for their members who are subject to disciplinary action for failure to observe the guidelines. Across national boundaries, the International Accounting Standards Committee (IASC) was set up in 1973, with the objective "to formulate and publish in the public interest, standards to be observed in the presentation of audited financial statements and to promote their worldwide acceptance and observance". The IASC has so far made 13 pronouncements on International Accounting Standards (IAS).

ACCOUNTING PRACTICES IN MALAYSIA – THE BACKGROUND

The accounting practices in Malaysia can trace their origin to the United Kingdom modified by local circumstances and subsequent developments. Several factors were responsible for this. The early corporate legislations in Malaysia were based on those in the United Kingdom. Companies were floated in United Kingdom to mobilise financial resources to invest in the rubber and tin mining industries in Malaysia. Published accounts of these compa-

nies were intended primarily for investors in the United Kingdom. For those early days, the accountants responsible for the financial management of these companies were either from the United Kingdom or Malaysians trained in the United Kingdom. Initially, the accounting practices in United Kingdom were adopted in toto. However, such accounting practices were modified and adapted to meet special local circumstances, thus allowing the emergence of some variations in the first place.

Very rapid economic development took place in Malaysia during the past two decades. Large industrial and commercial enterprises emerged under active encouragement of the Government with the view to diversify the economy which was then based on primary commodities. Corporate entities became accepted as the vehicles for mobilising investment capital with the development of the stock exchange in the country. Published accounts are now required for Malaysian investors in Malaysian companies.

Almost concurrently recent corporate legislations in Malaysia were modelled after those in Australia rather than those in the United Kingdom. Many of the Malaysian accountants received their accounting education and training in countries other than the United Kingdom. Accounting practices from outside the United Kingdom were also adopted in Malaysia modified by local circumstances. The formation of international accounting firms by practising accountants across national boundaries further facilitated the adoption of new accounting thoughts and practices from several sources outside Malaysia, thus further diversifying the accounting practices in the country.

The adoption of IAS by practising accountants has greatly reduced the diversities in accounting practices in the country, particularly in the case of published financial statements of companies quoted on the local stock exchange. Where IAS are not conformed, the departure is at least disclosed in the notes to the financial statements.

Nevertheless, diversities in accounting prac-

tices continue to exist. There are diversities between industries as well as between companies in the same industry. Selected examples of such diversities will now be commented upon.

DISCLOSURE OF ACCOUNTING POLICIES

Practically all published accounts of publicly quoted companies disclose the basic accounting policies adopted in drawing up the accounts. However, it is surprising that many different policies are being adopted even by companies in the same industry. One common disclosure is that the accounts are prepared under the historical cost convention but include revaluation of fixed assets where applicable. In respect of other items in the balance sheet and the profit and loss account, the policies or basis adopted are as varied as the items themselves.

Reference to IAS is not always made if IAS have been met, and this is generally assumed in the absence of anything to the contrary. Departure from IAS is disclosed, but justification is not generally offered for such departure. In other cases, departure from IAS was apparent in the accounts but was not mentioned. Therefore, the assumption that IAS have been met cannot always be made.

ASSETS — VALUATIONS AND CLASSIFICATIONS

Assets are valued at cost or revaluation and the basis is generally disclosed. In the absence of specific reference, cost is assumed to be the basis used. But there is a good deal of diversity in capitalization of cost e.g. certain items of cost are included in some cases but excluded in others. Revaluation of assets may be made by either directors or professional valuer, and is disclosed as such.

Assets are classified as fixed or current assets. Others are just shown in the balance sheets as assets outside the current and fixed assets sections. These are generally assumed to be non-current assets, e.g. long-term investment, interest in subsidiaries. Inter-company balances

are also shown either as current or non-current items.

The treatment of plantation cost by plantation companies are noteworthy. Some companies show the cost of plantation development together with the land, although freehold land and leasehold land are shown separately. Other companies show the plantation development cost separately from the land. The development cost is amortized. In some instances, the development cost is not amortized, but all replanting expenditures are charged to profit and loss as if incurred to maintain the value of the estate.

The treatment of replanting cess refunds is equally varied. Some companies credit them to expenditure while others credit them to profit and loss account. Some recognize the refund on accrual basis and show as receivable on the balance sheet. Others recognize them on the receipt basis.

INCOME RECOGNITION

Recognition of income is on the accrual basis, but this is not universal. In the case of housing development companies income is very often deferred to the time when the houses are handed over to the purchasers. In other cases, income from investment is taken into the profit & loss account on either the accrual basis or the receipt basis.

VALUATION OF INVENTORIES

Inventories of industrial concerns are valued at the lower of cost or net realizable value. In the past inventories of plantation and tin companies had always been stated at value hence or subsequently realized. Since the issue of IAS No. 2 most such companies now value inventories at the lower of cost or net realizable value. However, the capitalization of cost continues to be diversified. Some companies still state their inventories at value subsequently realized and admit that this is not in conformity with IAS No. 2 without justification.

CONSOLIDATED ACCOUNTS

Practically all published financial statements are presented in the consolidated basis where applicable. Departure from this practice is usually disclosed and justified. The equity method is now employed.

DEPRECIATION ACCOUNTING

Depreciation accounting is now generally adopted even though the basis may differ from company to company. Similarly, the rates applied for the same type of assets also vary.

As pointed out earlier, specific application of depreciation accounting among plantation companies is not uniform. However, among the industrial and commercial companies, depreciation accounting is adopted as the rule rather than exception.

DISCLOSURE IN FINANCIAL STATEMENTS

The presentation of the balance sheet and profit & loss accounts are now much abbreviated than before. But disclosure by way of notes to account provides very much more information than before. The details disclosed vary from company to company. Nevertheless, such additional disclosures generally meet with the requirements of the IAS.

PRICE LEVEL CHANGES

Like most countries Malaysia has also experienced an unprecedented rate of inflation in the past years. But procedures have not been adopted to reflect the price level changes in the financial statements. Thus the balance sheet very often does not reflect the true current value of the assets it carries, particularly fixed assets like land and buildings. To remedy this deficiency, periodic revaluation of fixed assets has been resorted to. However, such periodic revaluation of fixed assets is made on established principles, and very often at the discretion of the management. This revaluation of fixed assets becomes somewhat indiscriminate to the extent of being abu-

INCLUSION OF THE STATEMENT OF CHANGES IN FINANCIAL STATEMENTS

The inclusion of the Statement of Changes in Financial Position in published accounts is a recent development in Malaysia. Generally, all published accounts of publicly quoted companies would include this statement though it is not covered by the auditors' report and is not required under the Companies Act either. Such statements as they are prepared follow closely the format proposed in the IAS.

ACCOUNTING FOR CONSTRUCTION CONTRACTS

Both the percentage of completion method and the completed contract method are adopted by companies and the latter appears to be favoured, primarily for tax reason.

ACCOUNTING FOR TAXATION

The tax payable method was almost exclusively adopted up to a few years ago. The deferred method is gaining acceptance due largely to the pronouncement of IAS. The Malaysian income tax system is probably responsible for the lack of interest in either of the methods being adopted as the shareholders would eventually get back the taxes paid by way of dividend tax credit when dividends are distributed. The granting of accelerated capital allowance and the adoption of straight line basis for capital allowance will eliminate the timing difference involved in the deferred method. The calculation of P/E ratio by using the earning per share (E.P.S.) based on profit before tax is probably also based on the rationale of the income tax system.

FINANCIAL STATEMENTS OF UNQUOTED PUBLIC COMPANIES AND PRIVATE COMPANIES

The above comments are based on published accounts of publicly quoted companies, which are probably of more direct interest and concern to the investors and the public at large. Accounts of unquoted public companies are filed with the Registrar of Companies but are not available to the general public easily. Examination of the accounts of several unquoted public companies revealed the same diversities of

accounting practices adopted and that IAS are observed as in the case of publicly quoted companies.

The accounts of private companies are not easily available for examination. Having regard to the nature of things, it can be assured that the same degree of diversities in accounting practice would be evident but the observance of IAS would not be as stringent as in the case of public companies, both quoted and unquoted.

WHY THESE DIVERSITIES AND WHAT CAN BE DONE

Reference has already been made earlier to some of the factors responsible for the diversities of accounting practices in Malaysia. Another equally important reason is the absence of a unified accounting profession in the country. Whilst the Malaysian Association of Certified Public Accountants (MACPA) is the leading accounting body in the country, the body responsible for regulating the practice of accountancy rests with the Malaysian Institute of Accountants (M.I.A.) which is established by an act of Parliament, the Accountant's Act 1967. Those practising as Certified Public Accountants (CPAs) are regulated by the MACPA which is an associate member of the IASC responsible for issuing the IAS. Other accountants who are not members of the MACPA practise as "Public Accountants" under the M.I.A. The M.I.A. does not at present involve itself actively with professional standards and ethical conduct of its members.

If the diversities are to be reduced and uniformity is to be achieved, the unification of the accounting profession is essential. Besides this, the accounting profession must also involve itself in education, research, publication, in addition to enforcing compliance with IAS and ethical matters (education is the best way to sell an idea). In this regard, the existence of a unified profession is most vital. This would also be useful in speaking in a single voice in urging modifications to corporate laws and other government administrative measures affecting accounting practices and standards in the country.