AOB ALERT

TO AUDIT COMMITTEES AND AUDITORS MAR 2024

Suruhanjaya Sekuriti
Securities Commission
Malaysia

Impact of Climate-Related Risks on Financial Reporting of Public-Interest Entities

Why is this alert important to Audit Committees?

- To assist Audit Committees in engaging meaningful conversation with key stakeholders
- To provide updates on the AOB and its effort to promote audit quality

The Securities Commission Malaysia's (SC) Audit Oversight Board (AOB) closely monitors the impact of climate-related risks on financial reporting affecting public-interest entities (PIEs) that operate in the Malaysian capital market. Malaysia is committed to reducing greenhouse gas (GHG) emissions by 45% by 2030 and aspires to achieve net-zero as early as 2050. PIEs in Malaysia play an important role in transforming Malaysia into a low-carbon emissions country.

In June 2023, the International Sustainability Standards Board (ISSB) issued the International Financial Reporting Standard (IFRS) S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures. Subsequently, the IFRS Foundation republished an educational material, Effects of Climate-Related Matters on Financial Statements (IFRS Educational Material) to reiterate the comprehensive requirements of the IFRS Accounting Standards to report on the effects of material climate-related matters in the financial statements.

Directors and particularly Audit Committees should be aware that they are responsible for ensuring that PIEs' financial statements have considered and factored in the financial impact of climate-related risks and enhanced the connectivity between financial and non-financial information reported in the PIEs' annual reports and sustainability reports.

Auditors, as gatekeepers in the financial reporting ecosystem, are entrusted by investors to provide assurance on the information presented in audited financial statements. Auditors must challenge management's assessment of climate-related risks which are material to the financial statements.

The following are areas of focus, which directors and auditors respectively, should pay particular attention to when discharging their responsibilities:

DIRECTORS

To extensively discuss with management to gain an understanding whether there are processes in place to quantify the impact of the entity's climate-related risks in the audited financial statements;

To challenge management on the relevance and appropriateness of significant assumptions and judgements made by management in its cash flow projections used in financial reporting;

To ensure proper assessment and adequate disclosures are made by management in respect of any climate-related matters that create material uncertainties related to events or conditions that cast significant doubt upon a company's ability to continue as going concern;

To stand back and review if there is consistency in the information disclosed in sustainability reports and financial statements, including key assumptions and significant judgements.

AUDITORS

To take a step back and revisit procedures performed to obtain an understanding of the entity and its environment, particularly whether there is a revision to the entity's objectives and strategies to meet the environmental, social, and governance (ESG) requirements and any business risks arising from the revision;

To be mindful that in estimating the recoverable amount determined using value in use, MFRS 136 *Impairment of Assets* requires a company to consider the impact of climate change when performing the cash flow projections for an asset in its current condition;

In the event that the entity has revised its strategies, to be cautious and highly skeptical when scrutinising areas such as assessing potential indicators of asset impairment, provision, or contingent liability. For example, if a PIE has committed 'net-zero carbon emissions' in its business production process, the auditor to consider its impact when assessing indicators of assets impairment and provision;

To determine whether there are sufficient disclosures on assumptions and judgements about climate-related matters that could result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year;

In the event that climate-related matters create material uncertainties related to events or conditions that cast significant doubt upon a company's ability to continue as going concern, to assess if the uncertainties or management judgements have been sufficiently disclosed;

To take into account other information (Chairman's statement, Management Discussion and Analysis) included in annual reports and ensure that the financial and non-financial information disclosed are consistent with the key assumptions underlying the financial statements.

The above information is intended as a guidance for directors and auditors and are not exhaustive. Directors and auditors are advised to consider the areas of focus, taking into account the difference in the complexities of structures, industries, situations and operating environments in which the PIEs operate.

AUDIT OVERSIGHT BOARD
SECURITIES COMMISSION MALAYSIA