



Implementation of IFRS & SME Standards Pakistan Experience

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Agenda

- ICAP's role in adoption of IFRS
- Effective enforcement of International Standards.
- Achieving success by working closely with regulators
- World Bank ROSC conclusion on IFRS adoption & enforcement
- Roadmap for achieving full compliance with IFRS
- SME Project- using SMEGA ISAR guidelines
- Way forward for financial reporting standards for SMEs

Role of the Institute of Chartered Accountants of Pakistan in Standard Setting & Enforcement

- Established under CA Ordinance, 1961.
- Statutory body responsible for Regulation of Accounting profession.
- Only members of the Institute can sign the audit reports of all companies except for very small ones.
- Governed by 16 member Council (12 elected members and 4 Govt nominees)-

Regulatory Framework

- S. 234 of Companies Ordinance 1984 requires mandatory compliance with the accounting standards that are notified by SECP.
- SECP notifies IASs on the recommendation of ICAP Council.
- Each IAS / IFRS is reviewed by two regional Accounting Standards Committees and a due process of exposure to the members and other stakeholders is carried out prior to recommending adoption.

Current status & Strategy for IFRS implementation

- All IASs, except IAS 41, and new IFRSs are enforced through Companies Ordinance.
- IAS-41 & IFRS 2, 3, 5 & 6 approved by ICAP council- in process of notification by SECP. After these notifications, IFRS 1, 4 and 7 will remain.
- Effectively, Pakistan is very close to full IFRS compliance, that are called approved accounting standards.
- ICAP has also adopted all ISAs since inception. Thus, auditors compliance with ISAs, being members of ICAP helps in enforcing compliance of IFRS.

Pakistan's approach to IAS / IFRS

- Pakistan has been adopting IASs, without modification since 1970s when IASC started issuing IASs.
- IFRSs part of the ICAP syllabus.
- Pakistani Accountants are well versed with IFRSs.
- Exporting IFRS experts through out the world.
- Pakistani qualified Accountants being recruited by big 4 in US, UK and other regions / getting same salary as UK qualified CAs.

Enforcement mechanisms

- **SECP Monitoring of listed company Fin Stats**
 - **Over 30 auditors of listed companies fined, mainly for disclosure lapses.**
- **ICAP has implemented a stringent disciplinary process: 16 members found guilty with varying penalties including removal from membership in a few cases.**

Quality Assurance Program

- **Mandatory Quality control Program being enforced through Quality Assurance Board.**
- **All firms required to undergo review of their working papers.**
- **Listed companies can only appoint audit firms that have satisfactory ratings from ICAP's QAB.**
- **Full time qualified reviewers used by QAB**
- **Reviews carried out under a framework of Quality Control to ensure whether or not work was conducted in accordance with ISAs (see website of icap)**
- **Two unsatisfactory reviews or indication of gross negligence results in referral to the investigation committee.**
- **Current QCR program largely based on review of selected audit engagements (ISA 220)**
- **General quality controls i.e., ISQC 1 is planned to be adopted in phases.**

Working together with the Regulators

- **Chairman SECP, Chairman CBR and two federal secretary level persons- members of ICAP council**
- **Joint Coordination committees with SECP & SBP which meet on quarterly basis.**
- **ICAP advice is sought on all issues relating to accounting & auditing standards**
- **On the advice of ICAP most of the inconsistencies in Corporate Laws with IFRSs already removed.**

World Bank -Report on Observance of Standards & Codes (ROSC)

- Many stakeholders commended regulators role during recent years for improving quality of financial reporting.
- A majority of the interviewed stakeholders praised the initiatives undertaken by SECP, SBP and ICAP geared towards improving the quality of financial reporting in Pakistan.
- Stakeholders viewed that mandatory application of IFRS, monitoring and enforcement of standards, and introduction of QCR were important steps towards establishing sound corporate financial reporting regime.

Road Map for complete IFRS compliance

- Council has approved a strategy that all IFRS to be adopted by December 31, 07 by all publicly accountable entities.
- Work closely with Regulators to achieve these objectives & to address implementation issues.
- Few remaining laws that may be inconsistent with IFRS are to be modified to enable full implementation.
- SME framework : already developed being enforced for fin.stats beginning July 06.
- Unreserved compliance for Fin-stats for Dec 31,07.

Approach to SME standards

- Like many other emerging markets, SMEs play a vital role in the country's economic development.
- Compared to 600 listed companies, the non listed companies nearly 50,000.
- Previously, ICAP had required use of IFRS for all companies. This approach was not cost effective.
- Relaxation from some complex standards- IAS-39, 19, 12 etc. was given approx two years ago.

Pakistan's SME Project

- Considering the dire & urgent need for a simplified accounting framework for SMEs, and slow pace of IASB project, ICAP set up a committee to develop accounting standards for SMEs.
- After detailed study, ICAP decided to adopt three Tier approach on the pattern of SMEGA guidelines issued by ISAR.

Pakistan's SME Standards

- **Basic concepts based on ISAR SMEGA guidelines – i.e., three tier structure.**
 - Tier I entities i.e., Public Interest Entities : Full IFRS that are adopted in Pakistan
 - Tier II, Medium Sized Entities : Based on SMEGA II updated for changes in IFRS from 2002 to 2005.
 - Tier III : Very small entities: Based on SMEGA III

Pakistan Standards

■ Three Tier Applicability Threshold:

- **Tier I: Entities that are publicly accountable**
 - listed entities, public utilities, unlisted banks & large size entities that meet any two of the three criteria:
 - Turnover over Rs. 1000m \$ 17M;
 - Employees over 750;
 - borrowings in excess of Rs. 500M \$ 8.5M
- **Tier II: Medium size Entities that are neither Tier 1 nor Tier II.**
- **Tier III: Small size entities, both of the following conditions must be met:**
 - Turnover less than Rs. 200 m (US \$ 3.5M.
 - Equity less than Rs. 20 m (US \$ 0.35m)

Accounting & Financial Reporting Standard for Medium Size Entities (MSEs)

■ Basic concept from ISAR- SMEGA II +

- Changes in IFRS since 2002
- Guidance on investments & IAS-19 included that were not included in SMEGA II.
- Concept similar to IASB project but several complex issues not expected to be encountered by SMEs such as derivatives, not covered.
- “Mandatory fallback” to full IFRS if the ME standard does not address an issue – but only on such issue.
- ICAP standard about 90 pages vs IASB draft of over 240 pages.
- The standard will be updated after the IASB SME standard has been issued.

Accounting & Financial Reporting Standard for Small Size Entities (SSEs)

- SSE standard is almost fully based on SMEGA III except for one difference:
 - SMEGA guidelines allow national regulators to allow preparation of financial statements on cash basis for a limited purpose. This option is not available in Pakistan's SSE standard.

Way forward.

- Separate accounting standards for SMEs, that comprise bulk of business enterprises in emerging markets is vital to meet the needs of users of such enterprises.
- Use of full IFRS for such entities is not cost effective.
- The IASB standard under development, of around 240 pages, not likely to meet fully the requirements of developing countries.
- IASB standard unlikely to be effective till 2008-09
- ISAR / SMEGA guidelines & Pakistan SME standards are more suited for developing countries.
- South Asian countries' SAFA forum has approved to adopt Pakistan's SME standards as SAFA guidelines that can be used by member countries to develop their own SME standards, keeping in view their country's requirements.

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Thank You.