



The Institute of
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IASB Update

IASB issues Discussion Paper 'Leases - Preliminary Views' (Due date for Comments to IASB 17 July 2009)

This discussion paper presents the preliminary views of the US Financial Accounting Standards Board (FASB) and the IASB on significant components of an accounting model for lessees. It also includes a discussion of some of the issues that will need to be addressed in any new standard on lessor accounting. It is designed to gather information to assist the boards in developing a new standard on lease accounting.

The discussion paper *Leases: Preliminary Views* is a response to concerns raised by investors and other users of financial statements regarding the treatment of lease contracts under IFRSs and US generally accepted accounting principles (GAAP).

According to the World Leasing Yearbook 2009, total annual leasing volume in 2007 amounted to US\$760 billion; yet many of those lease contracts do not appear in an entity's statement of financial position (balance sheet). This is because IFRSs and US GAAP split leases into two categories—finance leases (capital leases under US GAAP) and operating leases and only the assets and liabilities arising from finance leases are recognised in the statement of financial position. For an operating lease the lessee simply recognises lease payments as an expense over the lease term.

The existing accounting model for leases has been criticised for failing to meet the needs of users of financial statements. In particular:

- (a) many users think that operating leases give rise to assets and liabilities that should be recognised in the financial statements of lessees. Consequently, users routinely adjust the recognized amounts in an attempt to recognise those assets and liabilities and reflect the effect of lease contracts in profit or loss. However, the information available to users in the notes to the financial statements is insufficient for them to make reliable adjustments to the recognised amounts.
- (b) the existence of two very different accounting models for leases (the finance lease model and the operating lease model) means that similar transactions can be accounted for very differently. This reduces comparability for users.
- (c) the existing standards provide opportunities to structure transactions so as to achieve a particular lease classification. If the lease is classified as an operating lease, the lessee obtains a source of unrecognised financing that can be difficult for users to understand.

In the discussion paper the IASB and the FASB discuss a possible new approach to lease accounting. The boards propose that lease accounting should be based on the principle that all leases give rise to liabilities for future rental payments and assets (the right to use the leased asset) that should be recognised in an entity's statement of financial position. This approach is aimed at ensuring that leases are accounted for consistently across sectors and industries.

The discussion paper 'Leases: Preliminary Views' can be downloaded from the IASB website. at www.iasb.org

Exposure Draft on 'Derecognition (Proposed Amendments to IAS 39 and IFRS 7)' (Due date for comments to IASB - 31 July 2009)

The IASB published for public comment an exposure draft of proposals to improve the derecognition requirements for financial instruments. Derecognition is when an entity removes a financial instrument from its financial statements. This occurs if the entity no longer controls a financial asset or no longer has an obligation to settle a financial liability.

The IASB is also proposing to enhance disclosure requirements, especially in situations where an entity continues to have an ongoing involvement in a financial asset that would be derecognised under the proposals. The additional disclosures would allow users to make a better assessment of the risks associated with such an asset.

The proposals are part of the IASB's comprehensive review of off balance sheet activities and follow the publication of proposals in December 2008 to strengthen and improve the requirements for identifying which entities a company controls, known as consolidation.

The use of special structures by reporting entities, particularly banks, to manage securitisations and other complex financial arrangements was highlighted as a matter of concern by the G20 leaders at their meeting in Washington, DC, in November 2008. The IASB's comprehensive review of off balance sheet risk is a response to that concern.

The IASB intends to hold public round tables to seek wider views on its derecognition and consolidation proposals and to broaden understanding of the interaction between the two projects. The IASB and the US Financial Accounting Standards Board (FASB) have already announced their intention that these will become joint projects once the FASB has completed short-term amendments to its existing standards.

The IASB invites comments on this exposure draft by *31 July 2009*. The exposure draft is available on www.iasb.org

Discussion Paper 'Preliminary Views on Revenue Recognition in Contracts with Customers' (Due date for comments to IASB - 19 June 2009)

The IASB and the US Financial Accounting Standards Board (FASB) initiated their joint project on revenue recognition primarily to clarify the principles for recognizing revenue. In US GAAP, revenue recognition guidance comprises more than a hundred standards many are industry specific and some can produce conflicting results for economically similar transactions. In IFRSs, the principles underlying the two main revenue recognition standards (IAS 18 *Revenue* and IAS 11 *Construction Contracts*) are inconsistent and vague, and can be difficult to apply beyond simple transactions. In particular, those standards provide limited guidance for transactions involving multiple components or multiple deliverables.

This discussion paper invites comments on the boards' preliminary views on a single, contract-based revenue recognition model. The boards are developing that model to improve financial reporting by providing clearer guidance on when an entity should recognise revenue, and by reducing the number of standards to which entities have to refer. As a result, the boards expect that entities will recognise revenue more consistently for similar contracts regardless of the industry in which an entity operates. That consistency should improve the comparability and understandability of revenue for users of financial statements.

The proposed model would apply to contracts with customers. A contract is an agreement between two or more parties that creates enforceable obligations. Such an agreement does not need to be in writing to be considered a contract. A customer is a party that has contracted with an entity to obtain an asset (such as a good or a service) that represents an output of the entity's ordinary activities.

The boards have not excluded any particular contracts with customers from the proposed model. However, because of the potentially broad scope of a standard on contracts with customers, they have considered whether the proposed model, and in particular its measurement approach, would provide decision-useful information for the following contracts:

- (a) financial instruments and some non-financial instrument contracts that otherwise would be in the scope of standards such as IAS 39 *Financial Instruments: Recognition and Measurement* and SFAS 133 *Accounting for Derivative Instruments and Hedging Activities*.
- (b) insurance contracts that are in the scope of IFRS 4 *Insurance Contracts* and SFAS 60 *Accounting and Reporting by Insurance Enterprises* (and other related US GAAP).
- (c) leasing contracts that are in the scope of IAS 17 *Leases* and SFAS 13 *Accounting for Leases* (and other related US GAAP). The boards have a joint project on their agenda for lease accounting.

IASB seeks comments on a proposed new standard on income tax accounting (Due date for comments - 31 July 2009)

The IASB published for public comment an exposure draft of a proposed new standard on the accounting for income tax. If adopted, the standard would replace the existing requirements in IAS 12 *Income Taxes*.

The proposed standard retains the basic approach to accounting for income tax, known as the temporary difference approach. The objective of that approach is to recognise now the future tax consequences of past events and transactions, rather than waiting until the tax is payable. Although the proposed standard retains the same principle, the IASB proposes to remove most of the exceptions in IAS 12, to simplify the accounting and strengthen the principle in the standard. In addition, the IASB proposes a changed structure for the standard that will make it easier to use.

The IASB expects to hold a webcast soon to introduce the proposals in the exposure draft and details will be announced on the website in due course. A flow chart and illustrative examples to illustrate the proposals in the exposure draft have been prepared and posted on the project page of the website.

The proposals are set out in the exposure draft *Income Tax* which is open for comment *until 31 July 2009*. The exposure draft is available on www.iasb.org

IASC Foundation issues IFRS Taxonomy 2009 and publishes for public comments its due process for XBRL activities (Due date for comments - 26 June 2009)

The International Accounting Standards Committee (IASC) Foundation issued the IFRS Taxonomy 2009 and published the *Due Process Handbook for XBRL Activities* for public comment.

The IFRS Taxonomy 2009 is a translation of IFRSs as of 1 January 2009 into XBRL (extensible Business Reporting Language). XBRL is an extensible, licence-free language used to communicate information between businesses. It allows companies, regulators, investors, analysts and other users of the IFRS Taxonomy 2009 to benefit from easier filing, improved access to and comparison of financial data.

The release of the IFRS Taxonomy 2009 follows the publication of the exposure draft in January 2009. Comments on the exposure draft were received from all over the world and from a wide variety of businesses and organisations. The comments focused on both technical and accounting details, and where appropriate have been reflected in the taxonomy.

The IASC Foundation also published a draft *Due Process Handbook for XBRL Activities* for public comment. The handbook sets out the IASC Foundation's XBRL mission, methodology and scope of work. It describes the mandatory procedures followed in developing the IFRS Taxonomy and in all other XBRL activities.

The IFRS Taxonomy 2009 and *Due Process Handbook for XBRL Activities* are freely available on the IASB website at <http://www.iasb.org/XBRL/XBRL.htm>

IASB and FASB announce further steps in response to global financial crisis

The IASB and the Financial Accounting Standards Board (FASB) announced further steps in response to the global financial crisis following their joint board meeting held in London on 23 and 24 March 2009.

The two boards have agreed to work jointly and expeditiously towards common standards that deal with off balance sheet activity and the accounting for financial instruments. They will also work towards analysing loan loss accounting within the financial instruments project.

These steps reaffirm a commitment to a joint approach to the financial crisis and to the overall goal of seeking convergence between IFRSs and US GAAP described by a Memorandum of Understanding (MoU) first published in 2006 and updated in 2008.

The boards will work together towards common standards by developing the IASB projects on consolidation and derecognition as joint projects once the FASB has completed its short-term amendments to its existing standards. Furthermore, the boards have agreed to issue proposals to replace their respective financial instruments standards with a common standard in a matter of months, not years. As part of this project the boards will examine loan loss accounting, including the incurred and expected loss models.

The boards will continue to draw on expertise provided by the **Financial Crisis Advisory Group (FCAG)**, a high level advisory body formed to guide the boards in their joint response to the financial crisis. Composition of the FCAG includes current and former investors, regulators, central bankers, finance ministers and others from industry and the public sector. The group has met on three occasions and will summarise their recommendations in a report which is expected to be published in the second quarter of 2009.

IASB responds to G20 recommendations, US GAAP guidance

The IASB responded to recent recommendations of the leaders of Group of Twenty (G20) countries regarding accounting standards and to recent decisions taken by the US Financial Accounting Standards Board (FASB). For the G20 recommendations, see <http://www.londonsummit.gov.uk/resources/en/PDF/annex-strengthening-fin-sysm>

Responding to the G20

The IASB is committed to taking action on each of the items recommended by the G20 by the end of 2009, the target date suggested by the G20, in order to ensure globally consistent and appropriate responses to the crisis.

In its recommendations, the G20 called for 'significant progress towards a single set of high quality global accounting standards.' To achieve this objective, the IASB is working intensively with the FASB, the Accounting Standards Board of Japan (ASBJ), and other national standard-setters. At their meeting on 24 March, the IASB and the FASB reaffirmed their commitment to a joint approach to the financial crisis and to the overall goal of seeking convergence between IFRSs and US GAAP.

Addressing Recent US GAAP Changes

On 2 April the FASB agreed to publish guidance in the form of FASB Staff Positions (FSPs) on fair value measurement and on impairments of debt securities. The IASB, which has worked closely with the FASB on convergence issues since 2001, understands the strong desire, voiced by many, for consistency between IFRSs and US GAAP on areas related to the financial crisis. EU Finance Ministers emphasised this point in a statement on 4 April. (See <http://www.eu2009.cz/en/news-and-documents/news/statement-by-the-informal-ecofin-15621/>.)

Initial reports regarding new or additional divergences between IFRSs and US GAAP being created by these FSPs appear to be overstated. A preliminary review of the FASB's decisions see <http://www.fasb.org/action/sbd040209.shtml> by IASB staff indicates that FASB's objectives and approach on the application of fair value when a market is not active appear to be broadly similar to those in IFRSs.

Once the FASB has finalised the FSP on fair value measurement, which they expect to do, the IASB staff will assess whether the FSP could lead to different results in practice.

The FASB also intends to publish an FSP modifying the recognition and presentation of other-than-temporary impairments of debt securities classified as 'available for sale' or 'held to maturity'. In requesting views on the FASB's proposals, the IASB noted that the concept of other-than-temporary impairments in US GAAP does not exist in IFRSs. Unlike US GAAP, IFRSs require an entity to recognise an impairment only if the entity has objective evidence to support an expectation of a default on contractual cash flows. In contrast, after the FSP, US GAAP will require an entity to recognise an impairment if it is possible that it will not collect all contracted cash flows or if it is more likely than not that the entity will dispose of the debt security before the entity can recover its cost basis.

More generally, IFRSs and US GAAP have multiple and different impairment models that relate to different financial asset types in different ways. The 'triggers' that initiate an impairment and the circumstances in which reversals of an impairment are allowed also differ. These factors mean that efforts to align IFRS and US GAAP impairment models could entail significant and complex change.

The IASB recognises the need for rapid consideration of these issues, which was anticipated by the shortened consultation period. Staff analysis, the comments solicited by the IASB's consultation, and input received from the Financial Crisis Advisory Group and the Standards Advisory Council will inform the IASB's decision at its 20-24 April meeting as to whether, in the light of FASB's actions, further guidance on the application of fair value in inactive markets and impairment of debt securities is needed.

At the same time, the IASB notes that the IASC Foundation Monitoring Board and the Trustees supported the IASB and the FASB's desire to prioritise the comprehensive project to produce a new standard rather than making further piecemeal adjustments. The comprehensive project is to undertake, on an accelerated basis, the replacement of existing financial instruments standards (IAS 39 *Financial Instruments: Recognition and Measurement*, in the case of the IASB) with a common and globally accepted standard that would address issues arising from the financial crisis in a comprehensive manner. The IASB plans to publish proposals within six months. This course of action is consistent with the call by the G20 'to reduce the complexity of accounting standards for financial instruments'.

IFAC Update

Exposure Draft 36 – Agriculture (Due date for comments 30 June 2009)

The International Public Sector Accounting Standards Board issued an exposure draft on the accounting treatment of and disclosures related to agricultural activity.

IAASB's Annual Report focuses on the Clarity Standards as a Foundation for Global Audit Quality

The International Auditing and Assurance Standards Board (IAASB), issued its 2008 annual report that highlights the culmination of the Clarity Project. With the completion of the Clarity Project, the IAASB has issued all its auditing standards in a form designed to enhance the understanding and implementation of them, as well as to facilitate translation. The annual report also details the IAASB's strategy and future direction as it continues to promote the adoption of International Standards on Auditing (ISAs) and develops new standards in response to extensive public consultation undertaken during 2007 and 2008 with key stakeholders.

In the report, former Chairman John Kellas describes the significance of the completion of the Clarity Project and outlines the IAASB strategy and work program. Covering the period from 2009-2011, the strategy and work program responds to significant developments in the environment in which audit and other assurance services are performed, and in which standards for such services are set.

Jim Sylph, Executive Director, Professional Standards, remarked:

"Now that the IAASB has completed the Clarity Project, there are a number of initiatives already underway that will grow in importance during 2009, such as the development of an alternative assurance standard for those entities that do not require an audit. In addition, new initiatives that are vital to the successful implementation of the clarified ISAs have been added to the IAASB's agenda, including the development of a process to assess the effectiveness of our standards."

Readers of the IAASB annual report are encouraged to visit the new Clarity Center on the IAASB website (<http://web.ifac.org/clarity-center/index>) for more information on the Clarity Project and the full suite of standards that will come into effect for audits of financial statements for periods beginning on or after December 15, 2009.

Exposure Draft - Explanatory Memorandum on IAESB Drafting Conventions (Due date for comments - May 29, 2009)

Both the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board for Accountants (IESBA) have recently developed drafting conventions to improve the clarity of their pronouncements. This memorandum provides background on, and an explanation of, the proposed International Accounting Education Standards Board (IAESB) Drafting Conventions, (the drafting conventions) was exposed for comment by the IAESB in March 2009.

SECP Update

- SRO 224(I)2009 issued for amendments to the Insurance Rules 2002
- Introduces amendments in the 6th Schedule to the Companies Ordinance, 1984 to facilitate the online submission of documents by companies to Company Registration Offices of the SECP. Fees for online services have been set at lower as compared to manual submission
- Circular No 9 of 2009 – electronic submission of periodic statements under the prudential regulations for modarabas. The SECP has decided to discontinue CFS Mk-II and Deliverable Futures products in the best interests of the capital markets in Pakistan. The effective date of the discontinuation is April 08, 2009
- The SECP in its continued efforts to enhance investors' confidence and facilitate the mutual funds industry has issued Circular No. 11 of 2009 wherein a number of measures have been introduced in line with the international best practices including phasing out of CFS MK-II and to ban licences for new financial institutions for at least 2 years.

SBP Update

- SMEFD Circular No 7 – Financing for plant, machinery and equipment to be used by the export oriented projects in Furniture and Pharmaceutical sectors for producing exportable goods shall also be eligible under the Long Term Financing Facility for Plant and Machinery
- BSD Circular No 6 – Sukuks issued by National Industrial Parks Management and Development Company are notified as approved security for the purpose of Statutory Liquidity Requirements
- SBP targets 350bn rupees in T-Bill auctions
- IBD Circular Letter No. 1 of 2009 – Format of Monthly Statement of Position (MSP) has been revised to be submitted by all Islamic banking Institutions with effect from April 2009.
- SMEFD Circular Letter 4 – Export Finance Scheme refinance facility available for export of bleached/unbleached cloth with export value of US\$2.50 or above.
- Circular debt to be settled with issuance of Rs 80 billion TFCs

FBR Update

- Further to Sales Tax General Order (STGO) No. 3, STGO 17 of 2009 issued regarding amendment in clause (viii) whereby “it should not be included in value for calculating withholding income tax” will be omitted.
- Sales Tax General Order 3 of 2009 issues relating to commercial importers
- FBR reviewing e-tax systems to avoid duplication

ICAP News

● ICAP Action Plans Published on IFAC Website

The Statements of Membership Obligations (SMOs) are issued by the IFAC Board and establish requirements for members and associates to promote, incorporate, and assist in implementing international standards issued by IFAC and the International Accounting Standards Board. The SMOs also establish requirements for quality assurance and investigation and discipline activities.

IFAC members and associates have to date participated in **three** parts of the compliance program that seeks to understand how the SMO requirements are being fulfilled.

- Part 1, Assessment of the Regulatory and Standard-Setting Framework
- Part 2, SMO Self-Assessment
- Part 3, Action Plans

The Part 3 process required two primary steps:

1. Organization’s review and agreement of proposed Policy Recommendations that had been prepared by the IFAC staff based on Part 2 submission.
2. After the Policy Recommendations had been agreed, organization then initiated the preparation of an Action Plan that more specifically sets out how the policy matters are to be addressed.

We are pleased to inform that the Institute’s Action Plans as part of the compliance program phase three have been published by IFAC and are now available on IFAC’s website. You may view the published plans at: <http://www.ifac.org/ComplianceAssessment/published.php>

- ICAP issues ‘Financial Statements Disclosure Checklist for Economically Significant Entities (ESEs)’. It may be downloaded from <http://www.icap.org.pk/web/links/0/disclosurechecklistguideline.php>

Local News Brief

- South Asian Federation of Exchanges (SAFE) in collaboration with Dow Jones Indexes Inc., New York has launched the first ever Dow Jones SAFE 100 Index comprising prominent companies listed on the major exchanges in the region
- New Petroleum Policy unveiled for 2009
- Government decided to replace the Cabinet Committee on Federal Reserve with a 20 member policy board
- Privatisation Commission Board – all permanent and contractual employees having a minimum of 5 years of service in the public sector enterprises are eligible for buying 12 percent shares of privatized entity on discount rates
- Swiss Business Council establishes office in Karachi
- Profit rate on savings scheme cut by 1.5%
- Petroleum exploration and production policy 2009 aimed at encouraging direct foreign investment, promoting local participation and offering 50 per cent of non skilled jobs to locals
- Central Bank of China has allowed Habib Bank trade/remittance settlements in Chinese currency (RMB)
- Cabinet approves revised Anti Money Laundering Bill

World News Brief

● **IFRIC 12 on service concessions endorsed for use in the EU**

The European Commission has endorsed IFRIC 12 Service Concession Arrangements for use in the European Union. In doing so, however, the mandatory effective date was changed from annual periods beginning on or after 1 January 2008 in IFRIC 12 to an entity's first financial year starting after 29 March 2009 in the EU-endorsed version, but with earlier adoption permitted. The endorsed version was published in the Official Journal of European Union - 26 March 2009.

● **FEE views on dynamic loan loss provisioning**

FEE(the Federation of European Accountants) has published a policy statement on dynamic loan loss provisioning for financial instruments. FEE's main messages are:

- If regulators allow entities to set up a dynamic provision for regulatory purposes, then part of non-distributable reserves in equity in the general purpose financial statements could be allocated as a buffer with proper note disclosures that the amount is determined in the prudential returns (by the regulatory rules);
- FEE is not supportive of any form of dynamic provisioning in general purpose financial statements affecting net assets or performance measures of the reporting entity;

- FEE encourages the IASB to provide further educative guidance and explanation as to how to conservatively apply IAS 39 for incurred losses since the incurred loss model is not equally applied by users in various territories;
- Any more fundamental change of general purpose financial reporting should be subject to in depth discussions and consultation, and the full due process would need to be followed;
- Any changes to financial reporting should be made at a global level to IFRSs to support comparability and maintain a level playing field.

The policy statement on dynamic loan loss provisioning for financial instrument can be download from www.iasplus.com/europe/0903/feeprovisioning.pdf

- China's Central Bank proposed replacing the US Dollar as the international reserve currency with a new global system controlled by the IMF
- A poll of 150 audit committee members who attended KPMG's recent Audit Committee Issues Conference found that 89% had made changes affecting their oversight boards as a result of the economic downturn. The poll also found relatively low satisfaction levels that those committees were expressing enough skepticism about management practices. For related information and resources, visit the AICPA's Audit Committee Effectiveness Center. WebCPA (3/24)
- Gulf states extend single currency deadline
- Dubai launched an exchange traded fund backed by physical gold
- Many small businesses on the verge of shutting down. After months of struggling to survive credit crunch and a recession, many small businesses, a crucial source of employment in the U.S., are close to giving up and closing their doors, business experts say. "We're getting close to the breaking point," said George Cloutier, head of American Management Services
- In the midst of an increase in the number of going-concern qualms stamped on company financials, standard-setters are working on changing how managers and auditors determine whether a business will stay viable in the foreseeable future.