



The Institute of
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IASB Update

IASB publishes IFRS for SMEs

The IASB has issued an International Financial Reporting Standard (IFRS) designed for use by small and medium-sized entities (SMEs), which are estimated to represent more than 95 per cent of all companies. The standard is a result of a five-year development process with extensive consultation of SMEs worldwide.

The IFRS for SMEs is a self-contained standard of about 230 pages tailored for the needs and capabilities of smaller businesses. Many of the principles in full IFRSs for recognising and measuring assets, liabilities, income and expenses have been simplified, topics not relevant to SMEs have been omitted, and the number of required disclosures has been significantly reduced. To further reduce the reporting burden for SMEs, revisions to the IFRS will be limited to once every three years.

Benefits

The IFRS for SMEs responds to strong international demand from both developed and emerging economies for a rigorous and common set of accounting standards for smaller and medium-sized businesses that is much simpler than full IFRSs. In particular, the IFRS for SMEs will:

- provide improved comparability for users of accounts
- enhance the overall confidence in the accounts of SMEs, and
- reduce the significant costs involved of maintaining standards on a national basis.

The IFRS for SMEs will also provide a platform for growing businesses that are preparing to enter public capital markets, where application of full IFRSs is required.

The IFRS for SMEs is separate from full IFRSs and is therefore available for any jurisdiction to adopt whether or not it has adopted the full IFRSs. It is also for each jurisdiction to determine which entities should use the standard. It is effective immediately on issue.

The complete IFRS for SMEs (together with the basis for conclusions, illustrative financial statements, and a presentation and disclosure checklist) can be downloaded from go.iasb.org/IFRSforSMEs.

IASB Clarifies the Accounting for Group Cash-settled Share-based Payment Transactions

The IASB has issued amendments to IFRS 2 Share-based Payment that clarify the accounting for group cash-settled share-based payment transactions.

The amendments respond to requests the IASB received to clarify how an individual subsidiary in a group should account for some share-based payment arrangements in its own financial statements. In these arrangements, the subsidiary receives goods or services from employees or suppliers but its parent or another entity in the group must pay those supplier

The IASB revised its initial proposals in the light of comments received. The amendments issued clarify:

- the scope of IFRS 2. An entity that receives goods or services in a share-based payment arrangement must account for those goods or services no matter which entity in the group settles the transaction, and no matter whether the transaction is settled in shares or cash.
- the interaction of IFRS 2 and other standards. The Board clarified that in IFRS 2 a 'group' has the same meaning as in IAS 27 *Consolidated and Separate Financial Statements*, that is, it includes only a parent and its subsidiaries.

The amendments to IFRS 2 also incorporate guidance previously included in IFRIC 8 Scope of IFRS 2 and IFRIC 11 IFRS 2—*Group and Treasury Share Transactions*. As a result, the IASB has withdrawn IFRIC 8 and IFRIC 11.

Discussion Paper - Credit Risk in Liability Measurement (Due Date for Comments: 1 September 2009)

The IASB has published for public comment a discussion paper on the role of credit risk in liability measurement. The paper is accompanied by a staff paper that describes the most common arguments for and against including credit risk in measuring liabilities.

Credit risk in liability measurement is often referred to as 'own credit risk'. Existing IFRSs require profit or loss resulting from changes in 'own credit' to be booked when debt is fair valued. From an accounting perspective there are good reasons for applying fair value measurement to both assets and liabilities. However, some see the outcome as counter-intuitive. Recent developments in the financial markets have led to increased concerns about gains that result from changes in the value of an entity's liabilities.

This discussion paper responds to this concern. The issue of 'own credit risk' has relevance to other IASB projects, in particular in the accounting for financial instruments, insurance, fair value measurement and provisions, contingent liabilities and contingent assets.

The discussion paper can be downloaded at: www.iasb.org

Exposure Draft - Management Commentary

(Due Date for Comments: 1 March 2010)

The IASB has published for public comment a proposed non-mandatory framework to help entities prepare and present a narrative report, often referred to as management commentary. Management commentary is an opportunity for management to outline how an entity's financial position, financial performance and cash flows relate to management's objectives and its strategies for achieving those objectives.

The information contained in management commentary is therefore of keen interest to investors and other users of financial statements. However, while management commentary type reporting is mandatory in many jurisdictions, some do not have guidance for this type of narrative report. Many preparers and users therefore indicated a need for the IASB to provide such guidance.

The proposals draw upon international best practice in the preparation and presentation of management commentary. The IASB believes that providing non-mandatory guidance will improve the consistency and the comparability of management commentary across jurisdictions.

The exposure draft can be downloaded at: www.iasb.org

Impairment of Financial Assets: Expected Cash Flow Approach

(Due Date for Comments: 1 September 2009)

The IASB has published a Request for Information on the feasibility of an expected loss model for the impairment of financial assets. Impairment is one of the issues that the IASB is addressing in the second phase of its comprehensive review of IAS 39 *Financial Instruments: Recognition and Measurement*

The Request seeks input on the practical issues that would arise, if an expected loss model was required. The input will assist the IASB in developing formal proposals that it plans to publish in an exposure draft in October 2009.

The current model in IAS 39 requires an entity to account for credit losses in financial assets only if an event (or a combination of events) has occurred that has a negative effect on future cash flows and that effect can be reliably estimated (this is known as the incurred loss model). A feature of that model is that an entity is not permitted to consider the effects of future expected losses. The financial crisis has highlighted this as an area of concern. Responding to the request of the G20 leaders and others the IASB is reviewing that approach and examining the expected loss model as an alternative.

The expected loss model requires an entity to make an ongoing assessment of expected credit losses, which may require earlier recognition of credit losses. This would better reflect the way that financial assets are priced and the way some companies manage their business.

The Request for Information can be downloaded: www.iasb.org

IFAC Update

IFAC Organizes G-20 Accountancy Summit

IFAC will continue to focus on how it can best contribute to strengthening the global financial system at a G-20 Accountancy Summit it is organizing in London on July 23 and 24. The goal of the summit is to gather input and discuss detailed positions that can form the basis of further IFAC submissions to the G-20 Working Groups as well as to contribute to the development of the institutes' own positions. It can be viewed at: www.ifac.org/financial-crisis/index.php

IPSASB Initiates Annual Improvements Program with Release of New Exposure Draft

To enhance the usability of International Public Sector Accounting Standards (IPSASs) and thus facilitate global convergence, the International Public Sector Accounting Standards Board (IPSASB) of the IFAC has launched an improvements project with the release of Exposure Draft (ED) 42, *Improvements to IPSASs*. This ED is the first of a proposed series of annual improvements to the IPSASs and is modeled on the successful annual improvements program developed by the IASB.

The proposed amendments in the ED are related primarily to the recognition, measurement, or disclosure requirements but do not represent substantive revisions to the content of existing standards. They reflect changes made by the IASB to related International Financial Reporting Standards.

Comments on ED 42 are requested by **September 30, 2009**. The ED may be downloaded at: www.ifac.org/Guidance/EXD-Outstanding.php

International Education Standards Board Seeks Comments on Proposed Strategy for 2010–2012

The International Accounting Education Standards Board (IAESB), a standard-setting board of the IFAC, is seeking comments from IFAC member bodies, regulators, accounting firms, employers, the academic community, and others on an exposure draft of its 2010-2012 strategy and work plan. Organizations and individuals with an interest in accounting education are invited to respond to the IAESB's proposals for its strategic direction, projects, and activities for the next three years.

The aim of the IAESB 2010-2012 strategy and work plan is to bring clarity to requirements that are needed to develop high-quality accounting education programs.

The IAESB's proposed strategy focuses on projects and activities aimed at developing International Education Standards (IESs), while providing adoption and implementation guidance to interested stakeholders in accounting education. This will assist IFAC's member bodies in increasing the capacity and capability of the global accountancy profession, contributing to strengthened public trust.

The IAESB proposes to undertake three high-priority activities, beginning in 2010. These are:

- Conducting a revision of the IESs, considering results of the IAESB's drafting conventions project and recent developments in the accountancy profession;
- Developing implementation guidance in areas of measurable implementation of the IESs, competency frameworks, and quality control measures for education providers; and
- Promoting greater awareness among academics, regulators, and others of the IAESB's pronouncements and its role in advancing international debate on emerging issues relating to development and assessment of professional accountants.

Comments on the exposure draft are requested by **October 5, 2009**. The exposure draft may be downloaded at: www.ifac.org/Guidance/EXD-Outstanding.php

International Ethics Standards Board for Accountants Releases New Code - Clarifies Requirements and Strengthens Independence

The International Ethics Standards Board for Accountants (IESBA) has issued a revised Code of Ethics for Professional Accountants (the Code), clarifying requirements for all professional accountants and significantly strengthening the independence requirements of auditors. The revised Code has been released following the consideration and approval by the Public Interest Oversight Board (PIOB) of due process and extensive public interest consultation.

The revised Code, which is effective on January 1, 2011, includes the following changes to strengthen independence requirements:

- Extending the independence requirements for audits of listed entities to all public interest entities;
- Requiring a cooling off period before certain members of the firm can join public interest audit clients in certain specified positions;
- Extending partner rotation requirements to all key audit partners;
- Strengthening some of the provisions related to the provision of non-assurance services to audit clients;
- Requiring a pre or post issuance review if total fees from a public interest audit client exceed 15% of the total fees of the firm for two consecutive years; and
- Prohibiting key audit partners from being evaluated on or compensated for selling non-assurance services to their audit clients.

The revised Code maintains the principles based approach supplemented by detailed requirements where necessary, resulting in a Code that is robust but also sufficiently flexible to address the wide ranging circumstances encountered by professional accountants.

The International Federation of Accountants' Statements of Membership Obligations have as a central objective, the convergence of a country's national code with the Code of Ethics for Professional Accountants. Further, the requirements specify that member bodies should not apply less stringent standards than those stated in the Code.

SECP Update

- SECP Circular No 20 – Requirements for approval of Merger of Open End Schemes
- SECP Circular No 21 – Deferment of application of IFRIC 4 “Determining Whether an Arrangement Contains a Lease” and IFRIC 12 “Service Concession Arrangements”
- SRO 447(I)/2009 – First Schedule of Companies Ordinance 1984 altered
- SRO 590(I)/2009 – Amendment to Listed Companies (Substantial Acquisition of Voting shares and Takeovers) Regulations 2008
- SECP Circular No 23 – Extension in period of Companies Regularisation Scheme until 31 July 2009

SBP Update

- SMEFD Circular Letter No 8 – Extension in Limit for Export Finance Scheme and Islamic Export Refinance Scheme – limits sanctioned by banks shall continue up to 31 August 2009
- SMEFD Circular No 9 – Long Term Financing Scheme (LTFF) – Extension in limit
- SMEFD Circular No 10 – Reduction in Export Performance Requirements under Part II of Export Finance Scheme for Hand Knotted Carpets
- SMEFD Circular No 11 – Modifications in Long Term Financing Facility for Plant & Machinery
- BSD Circular Letter no. 5 – the category of M/s Horwath Hussain Chaudhury & Company, Chartered Accountants has been upgraded from B to A in the list of panel of auditors of SBP.
- Announces auction target calendar for investment bonds
- BPRD Circular Letter no. 18 – Prudential Regulation M-1 obtaining computerized NIC from all the banks/DFIs customers/clients

FBR Update

- Amendment in the Customs Act, 1969 to change the CD% for a number of items
- FBR set to issue notices to insurance companies, banks and NBFIs for registration of FED at 16 per cent
- FBR issues changes in section 148, 153, 235, 236(A), 231(B) and Part IV of 2nd schedule of I. Tax Ordinance 2001 for withholding tax provisions through Finance Bill 2009 (Circular No 1(6)WHT/2009

ICAP News

ICAP & FBR link MoU for the Development of Tax Audit Framework

The Institute has signed a Memorandum of Understanding (MoU) with the FBR for the development and implementation of "Tax Audit Framework" for the conduct of tax audit by FBR through chartered accountants. This framework is aimed at laying down necessary requirements and providing guidance to the firms of Chartered Accountants and the officials of the FBR with regard to the scope of work, the reports to be issued by the tax auditors and other relevant matters for effective and efficient conduct of such audits. Currently the framework is for 'Company cases' only. MoU is effective from July 01, 2009.

Main objective of outsourcing the Tax audit through Chartered Accountants is to establish an objective and effective tax audit system that will create deterrence to mis-declarations in the tax returns filed by the tax payers. Such a system is expected to contribute in developing a culture of compliance with tax laws over time that will help in improving the tax collections as well as to improve the tax to GDP ratio.

The draft of Tax Audit Framework has already been circulated to members for their comments and is also available on ICAP website at: <http://www.icap.org.pk/web/links/0/taxation.php>
Comments may be sent to dtscomments@icap.org.pk

Technical Advisory Committee Opinion

Enquiry

Company A, an investment company, forms a subsidiary company B. To decide on functional currency of B, salient features of the entities are presented below:

1. B invested in another company namely C, a leading joint stock company.
2. The reason for incorporating B is to address some legal issues i.e. A cannot directly invest in C due to legal restrictions.
3. A is incorporated in country X and both B and C are incorporated in Country Z.
4. All the companies under discussion are using IFRS for preparation of their books and records.
5. The functional currencies of A and C are USD and Euro respectively.
6. B has no other activities except for holding investment in C.
7. B borrowed from a consortium of banks to finance acquisition of C. The debt is denominated in USD however lenders have relied on performance of C.
8. The dividend received by B are in Euro however these are converted and kept in USD short term deposits to be used for repayment of debt.

9. Major components of income statements of B are:
 - (a) Dividend income (in Euro)
 - (b) Interest expense (in USD)
 - (c) Gain/loss on fluctuation in exchange rates (due to USD debt and short-term deposits)
10. B have no active management and BOD are employees of A and all the decision are taken by A.

Based on above facts, I believe the currency of B should be the currency of A being treated as extension of activities of A i.e. those activities can be conducted by A directly.

Committee's View

We would like to draw your attention to the following paragraph of IAS 21 'The Effects of Changes in Foreign Exchange':

- 9 The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends cash. An entity considers the following factors in determining its functional currency:
 - (a) the currency:
 - (i) that mainly influences sales prices for goods and services (this will often be the currency in which sales prices for its goods and services are denominated and settled); and
 - (ii) of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services.
 - (b) the currency that mainly influences labour, material and other costs of providing goods or services (this will often be the currency in which such costs are denominated and settled).
- 10 The following factors may also provide evidence of an entity's functional currency:
 - (a) the currency in which funds from financing activities (ie issuing debt and equity instruments) are generated.
 - (b) the currency in which receipts from operating activities are usually retained.
- 11 The following additional factors are considered in determining the functional currency of a foreign operation, and whether its functional currency is the same as that of the reporting entity (the reporting entity, in this context, being the entity that has the foreign operation as its subsidiary, branch, associate or joint venture):
 - (a) whether the activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy.

An example of the former is when the foreign operation only sells goods imported from the reporting entity and remits the proceeds to it. An example of the latter is when the operation accumulates cash and other monetary items, incurs expenses, generates income and arranges borrowings, all substantially in its local currency. (underlining is ours)

- (b) whether transactions with the reporting entity are a high or a low proportion of the foreign operation's activities.
- (c) whether cash flows from the activities of the foreign operation directly affect the cash flows of the reporting entity and are readily available for remittance to it.
- (d) whether cash flows from the activities of the foreign operation are sufficient to service existing and normally expected debt obligations without funds being made available by the reporting entity.

12 When the above indicators are mixed and the functional currency is not obvious, management uses its judgment to determine the functional currency that most faithfully represents the economic effects of the underlying transactions, events and conditions. As part of this approach, management gives priority to the primary indicators in paragraph 9 before considering the indicators in paragraphs 10 and 11, which are designed to provide additional supporting evidence to determine an entity's functional currency.

In view of the above, currency of B should be the same as the currency of A as activities of the foreign operation are carried out as an extension of the reporting entity, rather than being carried out with a significant degree of autonomy.

Local News Brief

- Collection of Capital Value Tax has been withdrawn only on purchase value of shares of listed companies with effect from 1 July 2009 on the trade/transactions carried out on/after that date
- Bankruptcy Law to be introduced
- KSE issues reminder for Capital Adequacy Requirement Certificate as at 30 June 2009 should be submitted by 30 September 2009 (KSE/N-3773)
- Imposition of FED @ 16% in sales tax mode on services provided by stockbrokers. – KSE/ N 3722
- Amendment made in Petroleum Products (Petroleum Development Levy) Amendment Ordinance 2009
- Amendments made in KSE Regulations

World News Brief

- **Some Airlines would Face Big Liabilities under New Lease Accounting Rules**

New accounting rules aimed at bringing lease contracts onto balance sheets could result in millions of dollars in liabilities for airlines. Those that will be most impacted will be the weaker airlines who have no ability to borrow cash. It may highlight to the public the financial weakness of these businesses. The IASB is seeking feedback on the proposals and expects to issue a final standard by 2011.

- **U.S., Europe may take XBRL Beyond Corporate Financial Statements**

Financial regulators in the U.S. and Europe are looking into ways to take advantage of Extensible Business Reporting Language (XBRL) in applications that go far beyond the reporting of corporate financial statements. Soon XBRL data tagging may start showing up in proxy statements and documents relating to mortgage-backed securities. It can be viewed at: www.xbrl.us

- **EC Consults on Adoption of ISAs**

The European Commission (EC) has launched a public consultation to determine whether International Standards on Auditing (ISAs) should be adopted in the European Union (EU). In its consultation paper, the Commission commented on the International Auditing and Assurance Standard Board's (IAASB) governance and due process, stating that the "the current governance of the IAASB has matured to a stage where it may be justifiable to adopt ISAs in the European Union." A study undertaken by the University of Duisburg-Essen indicates that "an adoption of the ISAs in the EU would result in quantitative and qualitative benefits for companies, investors, and regulators, stemming from high quality and harmonized audits."

- **Banks still Lobbying against Off-Balance Sheet Changes**

The IASB is working quickly to produce some updated and clarified guidance on how to account for financial assets and liabilities. The financial meltdown renewed attention on this matter, as well as the use of special purpose entities to hold financial assets, a device that generally gets them off balance sheets. There is still disagreement on how big of a role off-balance sheet accounting played in starting the financial crisis, but banks appear to be against changes that would bring about greater disclosure of assets and liabilities.

- **Two CEBS Reports on European Bank Disclosures**

The Committee of European Banking Supervisors (CEBS) has published two reports assessing the following banks' disclosures:

- **Assessment of 2008 Annual Report Disclosures**

The analysis covers 23 large banks with cross-border activities. CEBS found 'a significant increase of disclosures compared to the previous analyses. At the same time CEBS identifies a number of areas within the CEBS good practices mostly in the context of accounting related disclosures, where disclosures could be further improved, including disclosures on

fair value measurement and related methodologies'. CEBS intends to develop a set of high-level disclosure principles to help banks prepare disclosures covering areas or activities that warrant particular attention or that are under stress.

- **Assessment of 2008 Pillar 3 Disclosures**

CEBS analysed the Pillar 3 disclosures provided by 25 banks relating to a bank's risk profile and capital adequacy. CEBS found that 'banks have notably enhanced the level of quantitative and qualitative information regarding credit risk and securitisation activities; however there are specific areas where further improvements could be made:

- ❖ the composition and characteristics of own funds
- ❖ the back testing information for credit risk and market risk
- ❖ the quantitative information on credit risk mitigations and counterparty credit risk the granularity of information on securitisations

- **Banks could Improve Accounting for Operating Cash Flow**

Companies could better understand the financial health of their commercial banks if the banks accounted for operating cash flow in a more consistent manner, according to a couple of professors. The researchers say a reliable comparison of banks cannot be done based on their recorded operating cash flows. CFO.com

- **Reporting on Corporate Governance in India Workshops, Global Corporate Governance Forum, Mumbai, July 22 and New Delhi, July 25, 2009**

In partnership with the National Institute for Securities Market and the Confederation of Indian Industry, the Forum is helping organize two media development workshops in Mumbai and Delhi respectively. The Thomson Reuters Foundation is collaborating with the Forum to provide technical and resource support for these events. The workshops aim to provide a theoretical underpinning of corporate governance blended with practical insights and inputs relevant to reporting on corporate governance in India. They will provide the participants with an overview of the current issues in corporate governance in India and globally, an understanding of specific reporting and writing techniques to enhance the investigative skills in the area of governance with the help of international experts, and an overall knowledge of the data and information sources to help in informed writing. More details about workshop agenda are available on website at: www.gcgf.org

