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ROSC A&A
PAKISTAN

REPORT ON THE OBSERVANCE OF STANDARDS AND CODES, ACCOUNTING AND AUDITING

JANUARY 2017

CAPITAL MARKET PERFORMANCE

SMALL & MEDIUM ENTERPRISE DEVELOPMENT

STATE OWNED ENTERPRISE REFORMS

INCLUSIVENESS

WORLD BANK GROUP

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ABBREVIATIONS AND ACRONYMS

A&A	Accounting and Auditing
AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
ACCA	Association of Chartered Certified Accountants
AFC	Assessment of Fundamental Competence
AFRS	Accounting and Financial Reporting Standards
AGP	Auditor General of Pakistan
AOB	Audit Oversight Board
AOSSG	Asian-Oceanian Standard-Setters Group
CAF	Certificate in Accounting and Finance
CAPA	Confederation of Asia Pacific Accountants
CGA	Controller General of Accounts
CIMA	Chartered Institute of Management Accountants (United Kingdom)
CIPFA	Chartered Institute of Public Finance and Accountancy
CPA	Certified Public Accountant
CPD	Continuing Professional Development
CPS	Country Partnership Strategy
EMBI+	Emerging Market Bonds Index Plus
FDI	Foreign direct investment
FY	Financial Year
GDP	Gross Domestic Product
HEC	Higher Education Commission
IAASB	International Auditing and Assurance Standards Board
IAESB	International Accounting Education Standards Board
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
ICAEW	Institute of Chartered Accountants of England and Wales
ICAP	Institute of Chartered Accountants of Pakistan
ICMAP	Institute of Cost and Management Accountants of Pakistan
IES	IFAC Education Standards
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFIAR	International Forum of Independent Audit Regulator
IFRIC	IFRS Interpretations Committee
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
IPSAS	International Public Sector Accounting Standards
IPSASB	International Public Sector Accounting Standards Board
ISA	International Standard on Auditing
ISQC	International Standard on Quality Control
M&E	Monitoring and evaluation
MSA	Multi Subject Assessment
MSME	Micro, small and medium-size enterprise
PERN	Pakistan Education and Research Network
PFM	Public financial management
PIE	Public interest entity
PIPFA	Pakistan Institute of Public Finance Accountants
PSC	Public sector company
PSX	Pakistan Stock Exchange
QAB	Quality Assurance Board
QAD	Quality Assurance Department
QCR	Quality Control Review
RAET	Regulations for Accounting Education Tutor
ROSC	Report on the Observance of Standards and Codes
SAFA	South Asia Federation of Accountants
SBP	State Bank of Pakistan
SDG	Sustainable Development Goal
SECP	Securities and Exchange Commission of Pakistan
SME	Small and medium-size enterprise
SMO	Statement of Membership Obligation
SMP	Small and medium-size practices
SOE	State-owned enterprise
SRO	Statutory Regulatory Order
SSE	Small sized entity

PREFACE

Report on the Observance of Standards and Codes Accounting and Auditing (ROSC A&A) assess financial reporting and auditing practices in participating countries. These reports form part of a joint initiative implemented by the World Bank and the International Monetary Fund to review the quality of implementation of internationally recognized standards and principles in 12 key areas (the ROSC program) with a view to promoting financial and economic stability.

This report provides an assessment of financial reporting and auditing requirements and practices within the corporate sector in Pakistan and sets forth areas of consideration for improving the institutional environment for accounting and auditing[1]. The ROSC A&A used international benchmarks of good practice governing financial reporting and auditing in the assessment, including International Financial Reporting Standards and International Standards on Auditing. As an update to an earlier assessment that was published in 2005, this report was undertaken following a formal request from the Government of Pakistan.

[1] Not-for-profit companies and companies limited by guarantees are not in the scope of the ROSC A&A.

ACKNOWLEDGMENTS

The Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A) was conducted at the request of the Government of Pakistan. All findings reflect the period of the review from March 2016 to January 2017; some stated future events may have been achieved by publication date. The World Bank team was led by Akram El Shorbagi (Senior Financial Management Specialist) and Qurat ul Ain Hadi (Financial Management Specialist) and included Henri Fortin (Lead Financial Management Specialist, GGOFR, Washington); Abid Khan (Program Associate, Islamabad); and consultants Abdul Rahim Suriya, Naveed Saeed, and Jael Billy.

The review was conducted through a participatory process involving the World Bank Country Office Pakistan and various in-country stakeholders, including the Ministry of Finance, Securities and Exchange Commission of Pakistan, State Bank of Pakistan, Pakistan Stock Exchange, Institute of Chartered Accountants of Pakistan, Institute of Cost and Management Accountants of Pakistan, Auditor General of Pakistan, Institute of Business Administration, Association of Chartered Certified Accountants (United Kingdom), audit firms, academia, and other business communities. The ROSC A&A team would particularly like to thank the SECP self-assessment team members led by Ms. Khalida Habib, head of the Investor Education and International Relations Department, for carrying out a comprehensive self-assessment in advance of the World Bank team's visit to Pakistan. This greatly facilitated the timely completion of the study.

The team also gratefully acknowledges Illango Patchamuthu (Country Director for Pakistan) and Fily Sissoko (Practice Manager, Governance South Asia) for their guidance and support.

The report also benefited from the comments of peer reviewers: Alex Berg (Senior Financial Sector Specialist), Patrick Kabuya (Senior Financial Management Specialist), Sarwat Aftab (Senior Private Sector Specialist), Shabana Khawar (Principal Country Officer, IFC), Jiwanka B. Wickramasinghe (Senior Financial Management Specialist) and Adrian Lim (IFAC Analyst) and Darlene Nzorubara (Senior Technical Manager, Quality & Development, IFAC).

Taking serious steps for economic revival, the Government of Pakistan set up Vision 2025 to elevate the country from lower middle-income to upper middle-income status. With the recent stability in the macro-economic environment, GDP growth rate has reached 4.7 percent, the highest in eight years. To continue with the pace of reform, the Government sought the World Bank's assistance in conducting the Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A).

Adopting measures to strengthen the A&A environment will allow the Government to make significant progress in the reform agenda as outlined in Vision 2025. An earlier ROSC was conducted in 2005. Significant progress has been made in implementing ROSC 2005 recommendation which has contributed in economic revival. The ROSC A&A 2.0 assessment focuses on three pillars: (a) A&A standard analysis with reference to international benchmark; (b) institutional framework, including institutional capacity; and (c) monitoring and enforcement and analysis of A&A standards as designed and practiced.

The outcomes of the assessment directly contribute toward the Government's reform agenda to improve capital market performance, state-owned enterprise (SOE) governance, small and medium-sized enterprise (SME) sector development, and knowledge economy with inclusive and indigenous growth. The assessment is in line with the FY2015-19 Country Partnership Strategy, providing a framework for the World Bank Group and other donors to support Pakistan in its reform plan.

The key regulators responsible for the policy reforms are the Securities and Exchange Commission of Pakistan (SECP), Pakistan Stock Exchange (PSX), and State Bank of Pakistan (SBP), and Institute of Chartered Accountants of Pakistan (ICAP).

Measures to Increase Capital Market Performance

Capital market acts as a catalyst for transforming the economy. Vision 2025 aims to double market capitalization. The SECP and PSX have undertaken various structural and legal reforms to enhance investors' confidence such as strengthened corporate governance practices of the regulated entities. The Code of Corporate Governance is now embedded in the listing regulations, and more than 90 percent of listed companies disclose a statement of compliance which is annually reviewed by auditors. The ROSC A&A assessment identifies following areas to further improve capital market performance;

- ***Efforts toward establishing an independent Audit Oversight Board (AOB) will enhance investors' confidence and boost capital market.*** Protecting investors' interest promotes true capital formation. In July 2016, major reform based on ROSC 2005 recommendation was undertaken that resulted in the establishment of AOB regulations through amendments in the SECP Act, 1997. Earlier, the audit profession was self-regulated by ICAP. The ICAP has an established Quality Assurance Board (QAB) functioning since 2005. The QAB will now be supervised by AOB. This reform lends greater credibility to the quality assurance process and is in line with international good practice. However, considerable resources are required to build AOB capacity, which includes affiliation with the International Forum of Independent Audit Regulators (IFIAR).

- ***Full compliance with IASB-issued International Financial Reporting Standards (IFRS) will improve foreign direct investment (FDI)***. Vision 2025 aims to increase FDI by a factor of 15. Pakistan has adopted most, though not all IFRS. Significant effort has been made to achieve substantial alignment with IFRS through amendments in the Companies Bill 2017 and insurance rules.[2] However, some gaps exist in the banking and power sector, which constitutes 26 percent of total market capitalization. The power sector has a great potential to attract foreign investment through privatization / restructuring considering these companies largely operate as unlisted companies with a capital base of almost 25 percent equal to the current market capitalization[3]. Compliance with IFRS will reduce the investment cost for foreign investors because of the ease of comparability and enhanced disclosure of information.

Economic Turnaround in SOEs through Greater Transparency and Accountability

Improved governance and financial reporting and auditing practices in unlisted state-owned enterprises (SOEs) will improve performance and reduce fiscal drain on the Government's scarce resources. Majority of unlisted SOEs are burdening the national exchequer by incurring ongoing losses. Pakistan's Vision 2025 envisages turning loss-making institutions into profit-making entities for the good of the public sector. The ROSC A&A assessment identifies several key areas for improving economic turnaround in SOEs:

- **Compliance with the Code of Corporate Governance for Public Sector Companies will instill confidence among citizens and stakeholders.** Compliance with the Corporate Governance Rules, 2013, being relatively new for public sector companies, is gradually improving. Similar to regulated entities, auditors are required to annually review the statement of compliance for public sector companies. However, considerable efforts are still required by all key players, which includes board of directors and management of PSCs, regulators and auditors to improve the status of compliance particularly in the areas of accountability for public wealth, transparent internal and external reporting and use of appropriate accounting policies and procedures.

- ***Defined financial reporting framework for authorities will provide relevant information to the decision-makers.*** Most authorities defined as state-owned enterprises prepare their financial statements without following any defined financial reporting framework and thus are unable to provide relevant information to decision-makers. The ICAP, one of the country's professional accounting organization and principal standard-setter, should work in close collaboration with the Auditor General of Pakistan (AGP) for defining a financial reporting framework for such entities.

- ***Defined oversight mechanism in Ministry of Finance will ensure accountability in the use of public resources***. Oversight of A&A practices for federal and provincial authorities are not well defined. The reform actions might include setting up monitoring and enforcement teams in the Corporate Finance Wings of the Finance Division and Provincial Finance Departments, hiring of professional accountants, and developing risk-based review methodologies to monitor A&A practices and improve assessment of fiscal risk for federal and provincial authorities.

- ***The quality of financial information will improve with the enhanced transparency.*** The financial statements of SOEs are often not easily accessible and contain several audit qualifications. The quality of financial information will be improved with greater transparency such as availability of audited financial statements through public domains.

[2] Companies Ordinance 2016 was promulgated through Presidential Ordinance on Nov 11, 2016. However, the Senate turned it down and insisted the GoP to take the routine parliamentary approval process. The Companies Bill 2017 is now undergoing deliberations in the Senate, after due acceptance in the National Assembly.

[3] Total capital employed in power sector as mentioned in SOE performance report is approximately PKR 1.9 trillion (US $ 0.02 trillion).

SME Sector Development

The Government has targeted an increase in GDP, job creation, and export services through development of the SME sector. This can be achieved by providing a level playing field and a fair competitive environment. Following recommendations of the 2005 ROSC, SECP took measures in collaboration with ICAP and introduced local accounting and financial reporting standards (AFRS) for small-size companies in 2007 and IFRS for SMEs for medium-sized companies in 2015. This provided a structured template for providing simplified information that is most relevant to users of the financial statements of SMEs. The sector will be further facilitated with the adoption of the Companies Bill, 2017, and active involvement of professional accountants as business advisors to improve private sector development.

- ***Adoption of Companies Bill 2017 will improve quality of financial information for small size entities and encourage documentation of economy.*** The current audit requirement for small-size entities is stringent and imposes an undue burden on small-size entities. The requirement for financial statements to be audited by chartered accountants applies to companies with paid-up capital greater than PKR 3 million (US$ 28,639). Thus, 75 percent of the total registered companies are incurring a relatively high cost for mandatory audits performed by auditors not subject to professional standards[4]. As a result, audit quality is compromised. This deficiency will be removed by having introduced auditors' qualification in the Companies Bill, 2017.

  The Companies Bill 2017 also removes the audit requirement from the private companies with paid-up capital of less than PKR 1 million (US$ 9,546)[5]. These companies will be required to file annual unaudited accounts with SECP. The amendment would reduce the cost of compliance burden on smaller firms and serve as an enabler for documentation of the informal economy, which is more than 50 percent.

  This reform will be more effective when filing audited financial statements is also relaxed for the purposes of tax returns[6]. ICAP and ICMAP also consider providing a series of trainings to small and medium-sized practices focusing on how small audit and accountancy firms obtain the knowledge to be trusted business advisers for the SME sector and facilitate access to finance.

- ***The SME sector can benefit from a greater level of engagement with the SME Board at PSX to access potential investors for raising capital at lower cost.*** Due to the limited capacity of SMEs, this potential change agent is still unexplored. The capacity gap can be bridged with the active involvement of professional accountants with the SME sector.

Measures to Enhance Inclusive and Indigenous Growth

Develop a profession gender action plan to increase the number of female accountants in the country. Pakistan has one of the lowest representations of female accountants in the region at 9 percent, compared with 30 percent in Sri Lanka and 22 percent in India[7]. The percentage of female students enrolled in the accountancy profession is also quite low, ranging from 18 to 22 percent over the last three years. A major factor contributing to low female participation is the lack of an enabling work environment with day-care and pick-and-drop facilities. Increasing the participation of women in the labour force is a key aim of the Vision 2025 reform agenda.

Develop a national accounting curriculum and accreditation body in collaboration with the Higher Education Commission (HEC) to provide equal professional opportunity for all and career progression for the mid-tier accountants. The ICAP has recently revised its education policy to attract aspiring students by offering more exemptions to graduates of the top universities that offers international-level accounting and auditing curricula. However, this has also resulted in varying levels of exemptions for professional qualification due to lack of a national accounting curriculum. Further, the profession has a strong pipeline of partly qualified

[4] Total registered companies are 73,207, whereas total companies with the paid-up capital of PKR 3 million or less are 54,456.

[5] Two-third of total registered companies

[6] Rule 34 of the Income Tax Rules, 2002

[7] Pakistan's female representation includes chartered accountant, cost and management accountants, and ACCA accountants.

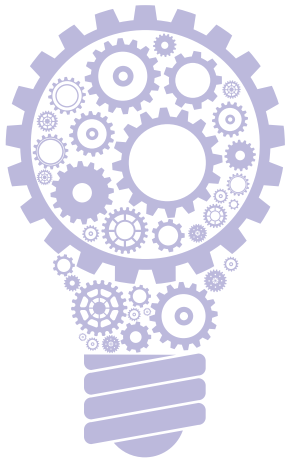
professional accountants. The ICAP has introduced a mid-tier certification for partly qualified professionals; however, because of lack of a national accreditation body, the Higher Education Commission has not provided equivalence to such certification.

Professionalize public financial management (PFM) by strengthening existing infrastructure. The ICAP and the Institute of Cost and Management Accountants of Pakistan (ICMAP) collaborated with AGP in 1993 to form the Pakistan Institute of Public Finance Accountants (PIPFA). The PIPFA produces a mid-tier accountant stream for the public and corporate sector. With the effort of ICAP, the Chartered Institute of Public Finance and Accountancy (CIPFA) and PIPFA signed a Memorandum of Understanding (MoU) in 2015 to promote high-quality PFM practices in Pakistan. Other avenues in training are being pursued under an MoU with ICAP, ICMAP, AGP, and CGA. However, a defined charter is required to put in place a business model for professionalizing PFM and to reap the full benefit of the existing infrastructure.

Measures to Improve Competitiveness through Knowledge Economy

Develop standard operating procedures and code of conduct to offer quality accounting shared services to the world. With a vibrant accounting profession, Pakistan holds great potential to serve as a competitive knowledge economy by offering shared services to the world. There are three professional accountancy organizations with IFAC membership in Pakistan. The local organizations, ICAP and ICMAP, are the full members of IFAC, the South Asia Federation of Accountants (SAFA) and the Confederation of Asia Pacific Accountants (CAPA). The other professional accountancy organization, PIPFA, is an IFAC associate member.

The international organizations ACCA and Chartered Institute of Management Accountants (CIMA) also have a strong presence in Pakistan. The profession's contribution to the skills sector in Pakistan is significant with, almost 31 percent of the national accounting professionals working abroad and being a source of foreign remittances. Pakistan has made good progress in accounting-outsourcing sector in the last two years. Local professional accountancy organizations are encouraged



to work jointly to develop a policy and code of conduct for providing quality services at the global level. Improving the knowledge economy index by promoting technology-based solutions is also a key pillar of Vision 2025.

Introduce third party assurance requirements on service organizations for improved performance and enhanced user satisfaction. There has been an increasing trend of outsourcing services in Pakistan particularly in the field of payroll processing, business process services, cloud computing, consulting, pension administrators, and others. This heightened operational risk is beyond the control of the user entity. To overcome this risk, IAASB has put forth International Standard on Assurance Engagement (ISAE) 3402, which prescribes an assurance methodology for service organization control to provide comfort over processes. An ISAE 3402 report, which constitutes an independent auditor opinion, is an effective method of communication that internal controls over systems and processes are suitably designed and are operating effectively within a well-controlled environment. Such formal communication has recently become an important success factor when differentiating between service organizations and demonstrating ability to achieve high-quality performance. The SECP and SBP may consider introducing third-party assurance requirements for service organizations providing outsourcing services. This will improve global and domestic market of the service organizations and provide enhanced user satisfaction.

Progress on ROSC 2005 Recommendations

The reform agenda is demand driven. Significant progress has been made in implementing the 2005 ROSC recommendations (Table A). The detailed status of 2005 policy recommendations is presented in section 3 of the report.

Table A. Summary of progress on ROSC 2005 recommendation

2005 Recommendation	***Key developments since 2005***
Develop simplified financial reporting requirements for SMEs	The IFRS for SMEs was adopted for medium-size, unlisted entities; and simplified national reporting standards (AFRS) were introduced for smaller entities.
Strengthen capacity of the professional accountancy organizations (ICAP and ICMAP)	ICAP has made progress toward full compliance with IFAC's SMOs. ICMAP has also strengthened its technical capabilities through greater cooperation with CIMA.
Take steps for improving academic and professional curriculum and education	ICMAP and ICAP have taken steps to improve the professional curriculum by aligning it with IES for professional accountants and CPD offering for existing members. ICAP has revised its education scheme and increased cooperation with leading universities in the country.
Introduce independent oversight of the auditing profession	SECP enacted AOB in July 2016. The remit of AOB includes oversight of quality assurance activities with respect to auditors of public interest companies.
Take steps for improving the capacity of regulators	The financial sector regulators, SECP and SBP, have increased staff with requisite competence and knowledge of financial reporting and auditing. In SECP, the number of professional accountants has almost tripled from 35 in 2005 to 93 in 2016.
Strengthen the monitoring and enforcement mechanism	SECP and SBP have strengthened the M&E process by developing methodologies and inspection manuals to review and enforce compliance with A&A requirements and produce more thorough and consistent reviews.

Key Areas for Consideration

The thematic areas for consideration for the 2017 ROSC A&A assessment are summarized in Table B. The detailed policy recommendations with responsible parties and timeframe for implementation are presented in section 4 of the report. The findings and policy reforms in the report will contribute to the development of the country action plan. The World Bank and other development partners can provide support to Pakistan as it addresses these issues.

Table B. ROSC 2017 key areas for consideration

	Institutional framework		
A&A standards	***Financial reporting framework***	***Institutional capacity and monitoring and enforcement arrangements***	***Observed reporting practices and perceptions***
• Develop road map to attain fully compliant status for IFRS • Cabinet approval of ISA 700R and 701[/a] • Introduce ISAE 3402 for service organizations	• Increase consultation with local industry to assess impact of IFRS before adoption. • Develop standard-setting committee in collaboration with AGP to support A&A practices and adoption of IPSAS in federal authorities and other public sector entities. • Adoption of Companies Bill 2017, to remove anomalies with the international best accounting practices and improve audit practices for SSEs	• Develop national accountancy accreditation body in collaboration with the HEC and establish uniform curriculum in accountancy for setting equivalence criteria and allowing exemptions etc. • Strengthen institutional arrangement for training public sector and mid-tier technicians in public and private sector. • Develop a professional gender action plan to facilitate equal economic participation by female professionals. • Professional accountancy organizations should support small and medium-size practices and build capacity to serve as trusted adviser for MSME sector. • Adoption of draft practice framework by ICAP to improve compliance with ISQC 1 and improve licensing process • ICAP, ICMAP and PIPFA should enhance the quality and relevance of the CPD program • ICMAP should align curriculum with IES and establish independent appeal body • Promote accounting outsourcing service and develop policy and code of conduct for the sector. • Provide support in building capacity of the Independent AOB and its affiliation with the IFIAR and enhance the capacity of the QAB at ICAP • Building monitoring and enforcement capacity of Economic Reform Unit and Corporate Finance Wings in Ministry of Finance and Finance Departments.	• Develop risk-based plan for improving A&A standards compliance in the SOE sector and • Improve timeliness of the preparation of financial statements and access to the financial statements of SOEs through public domain, such as websites etc. • Improve quality of audits for the SME sector that provides reasonable assurance to the lenders and users of the financial statements.

[/a]As per IFAC compliance, the status of ISA adoption is only considered adopted if it has legally adopted or incorporated the 2016 ISA into national requirements. The SECP has approved the audit report format in line with ISA 700R and 701 and submitted to the Cabinet for notification.

INTRODUCTION

1. Pakistan is a lower-middle-income country located at the crossroads of South Asia, Central Asia, China, and the Middle East, Pakistan is strategically positioned for trade and regional cooperation with its neighbours.

A. Country Background

2. Pakistan has reserves of natural resources such as coal, oil, natural gas, and minerals. However, challenges persist in leveraging these considerable resources into sustainable, inclusive economic growth and prosperity for its nearly 190 million citizens. The Government of Pakistan has set up Vision 2025 to elevate Pakistan from a lower-middle-income country to an upper-middle-income country. With the recent stability in the macroeconomic environment, GDP growth rate has reached 4.7 percent, the highest in 8 years.

3. **Pakistan's Vision 2025 will continue to focus on several priority areas as it moves toward upper-middle-income status.** Those areas include (a) meeting basic needs of people; (b) achieving sustained, indigenous, and inclusive growth to empower people particularly women; (c) encouraging responsible and accountable government and public sector; (d) improving human and social capital; (e) increasing private sector-led growth; (f) improving competitiveness through knowledge economy; and (g) modernizing infrastructure and strengthening regional connectivity.

B. Approach

4. The Government of Pakistan has taken steps for economic revival. To continue with the pace of reform, the Government has sought the World Bank's assistance for a repeat assessment with a second Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A). The previous ROSC A&A was conducted in 2005. This most recent ROSC A&A was conducted from March 2016 to January 2017. All findings reflect this period of the review; some stated future-designated events may have been achieved by publication date. The data and information used for the review were gathered from the revised ROSC A&A 2.0 diagnostic questionnaire completed by stakeholders and by reviewing professional accountancy-related documents. Other sources of data were collected through interviews with stakeholders from government, regulatory and accountancy bodies, accounting and auditing firms, banks, state-owned enterprises (SOEs), small and medium-size enterprises (SMEs), Commercial Audit Wings of the Auditor General of Pakistan (AGP), and academia. The review focused on assessing the institutional framework underpinning A&A practices in the regulated entities; private sectors, including SMEs; and SOEs of the country in comparison with international standards and good practice. The outcomes of the assessment directly contribute toward the Government reform agenda and provide means of achieving the targets set for the Sustainable Development Goals (SDGs) [Table 1].

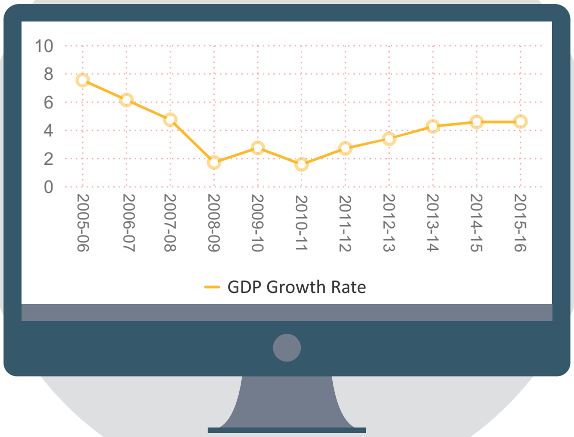
Table 1. Linkage of key proposed reforms with SDGs

Proposed reforms	SDGs
Improved A&A practices in SOEs	SDG 16: Build effective, accountable, and inclusive institutions at all levels
Developing entrepreneurial skills for small and medium-size practices (SMPs) and SMEs	SDG 9: Build resilient infrastructure, promote inclusive and sustainable industrialization, and foster innovation
Increase in GDP by improving capital market performance	
Improving knowledge economy	
Develop Gender Action Plan for profession	SDG 8: Promote sustained, inclusive, and sustainable economic growth; full and productive employment; and decent work for all
Develop national curriculum that provides equal opportunity to all students and strengthen public sector certification programs	SDG 4: Ensure inclusive and equitable quality education and promote lifelong learning

C. Economic Context

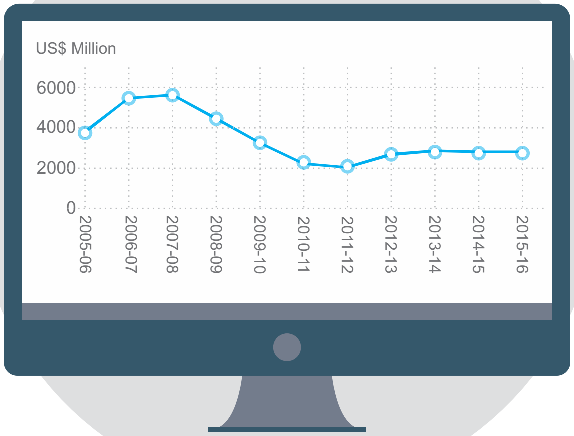
5. The GDP growth continues to increase but remains timid at 4.7 percent (FY2015/16), below the level required to accelerate job creation and significantly improve living standards. The GDP growth rate was at 8 percent in 2005; however, it was adversely affected by challenges ranging from the political and law-and-order environment in the country. The GDP growth in 2016 increased, albeit at a slower rate than the pre-financial crisis levels and below the South Asia regional average of 6.8 percent. The growth for FY2015/16 remains modest, increasing to 4.7 percent from 4.0 percent in the previous year, driven by large-scale manufacturing growth of 3.2 percent and services growth of over 5.7 percent (Figure 1).

Figure 1. GDP Growth



Source: World Bank website

Figure 2. FDI Inflows



Source: World Bank website

6. **Pakistan has made significant progress in reducing poverty over the last decade.** Based on the poverty line set in 2001, the percentage of people living below the poverty line decreased from 34.6 percent in FY2002 to less than 10 percent in FY2014. Moreover, these gains in income were shared with everyone; even the poorest 5 percent of the population saw real improvements. In April 2016, the Government announced a new national poverty line that sets a higher standard for well being, identifying 29.5 percent of the population as poor.[1] Economic growth, particularly private sector-led growth, is therefore critical if poverty reduction targets are to be met.

7. **The economy witnessed slim increase in foreign direct investment (FDI) in 2015–2016.** During FY2016, FDI inflows stood at US$2.8 billion against the outflow of US$860 million, compared with US$2.732 billion inflows and US$1.809 billion outflows in FY2015 (Figure 2). In absolute terms, the volume of FDI is low; the current surge in overall FDI is because of the low base from the previous year. However, improvement in corporate governance practices has started showing benefits to the economy. Pakistan's benchmark equity index, Karachi Stock Exchange-100, outperformed by 46 percent and turned out as Asia's best performing market in 2016. High-quality, reliable financial information such as that required by International Financial Reporting Standards (IFRS) and good practice signals to investors that Pakistan is an investment-friendly country and increases the attractiveness of the business climate for foreign investors.

8. **The level of private investment is relatively low.** Pakistan has one of the lowest investment-to-GDP ratios in the world. At 15.6 percent of GDP, the rate is less than half of the average for South Asia. Pakistan is currently ranked 144 out of 190 countries in the overall ease of Doing Business rankings. The implementation of the federal and provincial governments' joint action plan to improve the investment climate will be one important step toward reversing this long-term trend. Measures to improve the investment climate are underway, and there is evidence that some of these measures are starting to have a positive impact. During 2015-16, 6,200 new companies were registered, an increase of 24 percent with respect to the previous year. This has raised the total number of registered companies to 73,207.

D. Corporate and Financial Sector

9. The Securities and Exchange Commission of Pakistan (SECP) has a strong regulatory presence domestically and is actively engaged with international regulatory bodies. With the exception of banks and deposit-taking financial institutions, which are regulated by the State Bank of Pakistan (SBP), the SECP is the primary regulator for the nearly 70,000 registered companies in the country. The governance mechanisms, powers, and remit of SECP are prescribed in the Securities and Exchange Commission of Pakistan Act, 1997. The authority of the SECP with respect to corporate financial reporting is established in the

[1] World Bank. 2016. "Pakistan Development Update: Making Growth Matter."

Companies Ordinance, 1984, the principal legislation for companies. The SECP is a member of international standard-setting bodies such as the International Organization of Securities Commission (IOSCO) and the International Association of Insurance Supervisors.

10. **The Pakistan Stock Exchange (PSX) is gaining recognition from international investors as an emerging market.** The country's three stock exchanges recently completed a merger to form PSX. In December 2016, PSX sold 40 percent of its strategic shares to Chinese Consortium for PKR 8.96 billion (US $ 85.5 million) – a sale of strategic interest in the regional market. The PSX has five listing segments, including an SME Board targeted toward companies with paid-up capital from PKR 25 (US$ 0.24) to 200 (US$ 1.91) million. As of November 2016, there were 559 listed companies (less than 1 percent of registered companies) with a market capitalization of PKR 6.8 trillion (US$ 64.92 billion). Banks, insurance companies, and mutual funds comprise the principal institutional investors in the domestic market. The PSX was recently reclassified from a frontier market to emerging market status on a leading international benchmark index, effective May 2017. This recognition is expected to attract more foreign investors to PSX (Table 2).

Table 2. Pakistan Stock Exchange: Overview

	2013	2014	2015	2016
Total listed companies (Domestic)	557	560	572	559
Number of initial public offerings (IPOs)	3	5	8	5
Number of additional public offerings in the last three years	14	26	27	28
Trading volume for the previous four years (PKR Million)	49,570	51,514	54.045	52,231
Trading volume for the previous four years (US$ Million)	473.22	491.78	515.94	498.63

Note: Information provided by the SECP in response to the ROSC questionnaire on listed companies/

11. **The market's perception of country risk is improving.** Pakistan's Emerging Market Bonds Index Plus (EMBI+) risk spread has declined from its peak of 1,011 basis points (bps) in March 2013 to 369 bps in December 28, 2016. Moody's changed the outlook for its Caa1 sovereign credit rating from "stable" to "positive" in March 2015. Later, in June 2015, Moody's upgraded Pakistan's foreign currency bond rating to "B3" and assigned it a stable outlook. Moreover, Standard & Poor's raised Pakistan's credit rating outlook from "stable" to "positive" in May 2015 but affirmed its "B-" rating. Recently, in November 2016, Standard & Poor's revised Pakistan's long-term credit rating from "B-" to "B" because of improvement in the macroeconomic environment of the country.

Market confidence allowed Pakistan to raise US$2 billion in April 2014 through two dollar-denominated Eurobonds with bullet maturities and coupons of 5 years at 7.25 percent and 10 years at 8.25 percent, respectively, implying a spread of about 460–560 bps over U.S. Treasury. The Government issued a US$1 billion, five-year, international Sukuk in November 2014 at 6.75 percent. In September 2015, Pakistan once again tapped international capital markets and issued a 10-year Eurobond worth US$500 million at 8.25 percent. As international markets had significantly tightened, the pricing of the bonds was the same as a year earlier despite significant improvements in Pakistan's macroeconomic conditions. More recently, in October 2016, Pakistan successfully issued a five-year Sukuk worth US$1.0 billion at a historical low rate of 5.5 percent. Issued Sukuk are in alignment with the standards of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).

12. **The banking sector is growing, largely driven by rise in private sector advances and investments (mostly in government securities).** There are 35 banks in Pakistan, which together hold approximately PKR 14 trillion (US$ 133.65 billion) in assets; of these, 20 are commercial banks, 6 are Islamic banks, and 9 are owned by the state. The Government's domestic debt accounts for PKR 8.47 trillion (US$ 80.86 billion) or nearly 62 percent of net banking assets.[2] However, private sector credit is on the increase with a modest rise in lending to SMEs. Overall, nonperforming loans fell to 11.1 percent of the loan portfolio in 2016. Net nonperforming loans also continue to decline because of adequate provisioning, dropping to 2.2 percent in July 2016. Nonperforming loans for SMEs declined from 30.5 percent to 26.1 percent.

13. **The insurance sector, particularly life insurance, is a key area for growth**. The insurance market in Pakistan compared to its peers in the region is relatively underdeveloped. However, the market is steadily growing at an average of 6 percent in the last three years. There are 51 insurance companies, including 4 that are owned by the state. Net written premiums are approximately PKR 1.99 billion (US$ 18.99 million), over three-quarters of which are derived from the life insurance market.[3]

14. **The SOEs continue to play a significant role in the economy.** The SOEs are categorized under three broad categories: public sector companies (PSCs),[4] development finance institutions,[5] and federal/provincial authorities. The SECP ensures corporate compliances as per Companies Ordinance, 1984, and Rules of Business. Line ministries and Ministry of Finance regulate authorities whereas the development finance institutions are regulated by State Bank of Pakistan. An SOE report for 2013-14, published by the Ministry of Finance,[6] showed that SOEs constitute a considerable portion of the country's macro economy — employing 423,254 people, yielding a considerable 5.5 percent contribution in nontax revenue in the form of dividends, with a significant asset base worth PKR 9.633 trillion (US$ 91.96 billion) and a turnover of PKR 5.257 trillion (US$ 50.19 billion) contributing 20.7 percent to the country's GDP. Out of 175 public sector companies, 12 are listed on PSX. Listed SOEs contribute 34.4 percent and 38 percent to the total assets and total turnover of SOEs, respectively. The Government is an important source of finance for SOEs, having provided PKR 150 billion (US$ 1.43 billion) in loans, PKR 272 billion (US$ 2.6 billion) in subsidies, and PKR 134 billion (US$ 1.28 billion) in other forms of finance in FY2014. Federal authorities represent a large investment of public money, with 85 percent and 20 percent share in loans and guarantees to SOEs and sole recipient of grant to SOEs in 2013-14. However, such authorities are reporting on cash or accrual basis without any defined financial reporting framework, whereas a few have adopted IFRS. Good governance of SOEs is particularly crucial to the success of the reform agenda as a number of these enterprises operate in sectors that are key to economic growth and public service delivery such as energy and transport.

15. **The SMEs continue to face significant challenges in accessing finance.** Although SMEs comprise nearly 97 percent of registered companies in Pakistan, access to credit for SMEs remains a challenge and poses constraints on growth. One reason could be the low-capital base of SMEs that do not meet the requisite debt-to-equity ratio. Micro, small and medium-size enterprises (MSMEs) require further learning on the added value of financial reporting and assurance services to facilitate their access to finance. Credit provided to SMEs represented just 7 percent of the total bank lending to the private sector in 2014. While still relatively high compared with the overall loan portfolio, the level of nonperforming loans for SMEs is on the decline. Further, the small-size entity sector requires real support to increase its level of equity financing, which increases capital investments enabling more companies to operate as medium-sized companies that also generates employment. More professionals would need to engage with SMEs to provide technical support to access potential investors for raising capital at a lower cost through the SME Board at PSX.

[2] Pakistan Development Update November 2016.

[3] Information provided by the SECP in response to the ROSC questionnaire on the insurance sector.

[4] Public sector company means a company, whether public or private, which is directly or indirectly controlled, beneficially owned or not less than 50 percent of the voting securities or voting power of which are held by the Government or instrumentality or agency of the Government or a statutory body, or in respect of which the Government or any instrumentality or agency of the Government or a statutory body, has otherwise power to elect, nominate, or appoint majority of its directors and includes a public sector association not for profit, licensed under section 42 of the Ordinance.

[5] Development finance institutions provide a broad range of financial services in developing countries such as loans or guarantees to investors and entrepreneurs, equity participation in firms or investment funds, and financing for public infrastructure projects.

[6] Federal Footprint State-Owned Entities Performance Review Fy2013–14. The report is available at http://www.finance.gov.pk/publications/State_Owned_Entities_FY_2013_14.pdf

Table 3. Capital-based distribution of companies

Paid-up Capital	% of companies in each category
Paid-up capital up to PKR 100,000 (US$ 954)	38
Paid-up capital from PKR 100,001 to PKR 500,000 (US$ 955 to US$ 4,773)	15
Paid-up capital from PKR 500,001 to PKR 1,000,000 (US$ 4,774 to US$ 9,546)	11
Paid-up capital from PKR 1,000,001 to PKR 10,000,000 (US$ 9,547 to US$ 95,465)	25
Paid-up capital from PKR 10,000,001 to PKR 100,000,000 (US$ 95,466 to US$ 954,653)	8
Paid-up capital from PKR 100,000,001 to PKR 500,000,000 (US$ 954,653 to US$ 4,773,269)	2
Paid-up capital from PKR 500,000,001 to PKR 1,000,000,000 (US$ 4,773,270 to US$ 9,546,539)	0.38
Paid-up capital from PKR 1,000,000,001 to above (US$ 9,546,540 to above)	0.54
Total	**100**

Source: SECP report for 2015–2016.

E. Linkage of the Assessment to Pakistan's Development Agenda

16. The World Bank support through development policy credits over the last three years has complemented stakeholders in achieving many of the recommendations identified in ROSC 2005. Among those recommendations were amendments in the SECP Act and the Companies Bill, 2017. These amendments have strengthened the auditing and accounting standards for the corporate sector in Pakistan.

17. **The 2017 ROSC A&A update is relevant to the Government's reform agenda and Country Partnership Strategy (CPS) 2015-19.** The updated ROSC A&A exercise was undertaken following a formal request from the Economic Affairs Division at the joint request of SECP and ICAP. Adopting measures to further enhance the A&A environment will allow the Government to make significant progress in achieving the reform agenda outlined in Vision 2025 and contribute to improving GDP by capital market and private sector development, improving service delivery of public sector entities, developing knowledge economy, and building human capital through equitable opportunities. The outcome of the assessment directly relates to the strategic themes of the FY2015-19 CPS, which include private sector development, inclusion, and service delivery. The ROSC A&A provides a foundation for the World Bank Group and donors to support Pakistan in achieving its upper-middle-income country agenda.

II. ASSESSMENT

18. This section reports on A&A standards, institutional framework for corporate financial reporting, and observed reporting of practices and perceptions.

A. A&A Standards

19. This subsection will provide an analysis of financial reporting (accounting) standards and auditing standards.

Financial Reporting Standards Analysis

20. Accounting standards are critical business-related language tools for investors and other stakeholders. Pakistan is seeking to improve the business climate in order to attract FDI and mobilize finance in support of productive and job-creating activities. If adopted accounting standards for listed companies differ significantly from the increasingly adopted universal international benchmark, namely IFRS,[7] it could be difficult for foreign investors to understand the financial reports of domestic companies, thus potentially hampering investment and growth.

21. **Despite IFRS being adopted in Pakistan, full compliance has been hampered by a small number of exemptions and deferrals, mainly in the banking and power sector.** Table 4 summarizes the key areas of divergence between adopted accounting practices and IFRS. The IASB-issued standards that have effective dates in 2018 and 2019 — IFRS 9, *Financial Instruments*; IFRS 15, *Revenue from contracts with customers*; and IFRS 16, *Leases* — are under consideration for adoption in Pakistan.

22. **The SBP has deferred adoption of certain IFRS for banks under its regulatory purview.** The standards deferred include IAS 39, *Financial Instruments: Recognition and Measurement*; IFRS 7, *Financial Instruments: Disclosures*; and IAS 40, *Investment Property*. The rationale for the deferral with respect to financial instruments is because of differences between the valuation of investments and applicable disclosures prescribed by the corresponding IFRS and the preferred approach of SBP given the level of capitalization of domestic banks. The rationale for deferring the adoption of IAS 40 by banks, however, was less clear.

23. **A few requirements of the Companies Ordinance conflict with those of IFRS but are addressed in the Companies Bill, 2017.** The Companies Ordinance, 1984, prescribes A&A requirements for companies, some of which diverge from IFRS requirements. These include the accounting treatment for revaluing fixed assets or redeeming preference shares and the definition of subsidiaries and associates in joint arrangements. The amendments to the Companies Bill, 2017, address a majority of these areas of divergence.

Thus, the impact of these differences in company financial statements is expected to be limited in the future. Refer to Annex 1A and Annex 1B for a detailed description of the differences between the Companies Ordinance and IFRS and the amendments in the Companies Bill, 2017. These amendments were first introduced through Companies Ordinance, 2016, which was promulgated through Presidential Ordinance on November 11, 2016. However, the Senate turned it down and insisted that the Government take the routine parliamentary approval process. The Companies Bill, 2017, is now undergoing deliberations in the Senate after due acceptance in the National Assembly.

[7] IFRS are the standards issued by IASB, the standards issued by its predecessor IASC and adopted by IASB, and the interpretations issued or adopted by IFRIC.

Table 4. Key areas of divergence between adopted IFRS and IASB-issued IFRS		
Topic	**Relevant IFRS**	**Description of key differences**
		IFRS not adopted
First time adoption of IFRS	IFRS 1	IFRS 1 was not adopted because of deferrals of some IAS/IFRS. However, it is under consideration and is expected to be adopted in the short to medium term.
Presentation of financial statements	IAS 1	The financial statements for insurance companies diverge from the presentation requirements of IAS 1. However, insurance ordinance is undergoing revision, and the SEC Policy Board approved the Insurance Accounting Regulations, 2016 (Accounting Regulation) in January 2017. Under the Insurance Accounting Regulations, insurance companies are required to present financial statements in accordance with IAS 1, for periods commencing July 1, 2017, which is expected to eliminate these differences.
		IFRS adopted but exemption granted to specific sectors
Financial instruments	IAS 39 IFRS 7	IAS 39 and IFRS 7 have not been adopted for entities regulated by SBP. The requirements still apply to other companies that prepare financial statements according to IFRS, as notified in Pakistan. The 559 listed companies include 22 banking companies that are exempt from IAS 39 and IFRS 7 requirements.
Investment property	IAS 40	IAS 40 has not been adopted for entities regulated by the SBP. The 559 listed companies include 22 banking companies that are exempt from IAS 40 requirements.
Consolidated financial statements	IFRS 10	IFRS 10 does not apply to investments by companies in mutual funds established under a trust structure.
Share-based payments	IFRS 2	The SECP, through notification dated June 7, 2011, grants exemption from IFRS 2 share-based payment to certain SOEs, which are otherwise required to comply with IFRS 2 while accounting for the 'Benazir Employee Stock Option Scheme', dated August 14, 2009. However, the exemption is subject to compliance by these entities with the requirements of IFRS regarding effect of disclosure of such departure.
The effect of changes in foreign exchange rates	IAS 21, IFRIC 4 and IFRIC 12	Power sector companies have been allowed deviation from requirements of IAS 21 (in respect of capitalization of exchange differences), IFRIC 4 (determining whether an arrangement contains a lease), and IFRIC 12 (service concession arrangements). However, the same is in accordance with IAS 1, which allows departure from requirements of IFRS in exceptional circumstances. In compliance with IAS 1 and IAS 8, such companies are required to make complete disclosures, including the financial effect of the departure on each item in the financial statements that would have been reported in compliance with the requirement. The 559 listed companies include 19 listed companies that follow the modified requirements of IAS 21, IFRIC 4, and IFRIC 12.
		IFRS not applicable
Revenue recognition Leases Financial instruments	IFRS 15 IFRS 16 IFRS 9	This is applicable from 2018 and is in the process of adoption. This is applicable from 2019 and is under consideration for adoption. This is applicable from 2018 and is in the process of adoption.

Note: IFRIC = IFRS Interpretations Committee.

Auditing Standards Analysis

24. International Standards on Auditing (ISA) have been fully adopted in Pakistan with the exception of ISA 700R (revised), *Forming an Opinion and Reporting on Financial Statements*, and 701 (new), *Communicating Key Audit Matters in the Independent Auditor's Report*. The SECP has approved the audit report format in line with ISAs 700R and 701 and submitted to the Cabinet for notification. Pakistan has adopted ISA and other international standards and pronouncements issued by IAASB, including those related to quality control. The

IAASB recently revised the standards associated with the content and format of the auditor's report, particularly for listed companies. These standards were adopted by ICAP before December 2016; however, adoption requires revision in the format of the audit report, which is specified by SECP under statute. The SECP has approved the audit report format in line with ISAs 700R and 701 and submitted to the Cabinet for notification. The audit report format is in line with the revised standard and has been communicated by SECP for the period ending or closing January 1, 2017 onwards. The application date of such standards by IAASB was December 15, 2016. As per IFAC compliance program, the status of ISA adoption is only considered if it has legally adopted or incorporated the 2016 ISA into the national requirements. Therefore, compliance with the ISAs 700R and 701 will be considered only after Cabinet's notification. Given that the new auditor's report represents a significant change from the 'boilerplate' language in the traditional audit opinion and should increase transparency and understanding of key issues identified during the audit, adoption of these standards will increase the transparency and enhance investors' confidence on presentation of the financial statements.

BOX 01

IFRS adoption and FDI: Evidence from Nigerian quoted firms
(A study from Department of Accounting, Covenant University, Nigeria)

The result of the referenced study revealed a positive and statistical significance between IFRS and FDI in Nigeria. It showed that the company that fully adopts IFRS leads to a significant increase in FDI, as 1 percent increase in the IFRS causes 120.1 percent and 136.1 percent rise in FDI on Nigerian economy.

The study investigated the view of the preparers and users of the annual financial statements of the listed companies that adopted full IFRS. The results of the study were similar to earlier studies in this field such as **Beenish, Miller, and Yohn (2010)** that the IFRS adoption in the European Union significantly increases FDI. Similarly **Pius, Jane, and Raymond (2014)** also supported similar facts for adoption of the IFRS in Nigeria.

25 Full adoption of international standards without exceptions could be a means of attracting and mobilizing private investment. Internationally recognized standards such as IFRS and ISA bring increased credibility, comparability, transparency, and investor confidence (Box 1). Pakistan has adopted most, but not all, IFRS and has introduced IFRS for SMEs for medium-size, unlisted companies. Significant effort has been made to achieve alignment with IFRS. However, because of a few deferrals and deviation of local laws with applicable IFRS, full observance cannot be claimed. Pakistan should be able to improve its perception as an investment-friendly country by adoption of full, unmodified IFRS.

B. Institutional Framework for Corporate Financial Reporting and Auditing requirements

26. This subsection looks at the institutional framework for corporate financial reporting and auditing as it relates to (a) general financial reporting requirements, (b) listed companies, (c) banks, (d) insurance companies, (e) public sector companies, (f) the accountancy profession, (g) audit regulation, (h) professional education and training, (i) setting A&A standards, and (j) standard-setting process for other financial reporting standards.

General Financial Reporting and Auditing Requirements

27. General financial reporting and auditing requirements for the corporate sector are prescribed by law and are largely in line with international good practice. The Companies Ordinance, 1984, is the principal legislation that establishes general financial reporting requirements for companies in Pakistan. Corporate Governance Rules and sector-specific ordinances also apply to regulated entities such as listed companies and financial institutions. Table 5 summarizes the key legislation for corporate sector A&A requirements.

Notes:
[/a] This list is focused on A&A reporting requirements. Prudential reporting, listing regulations, taxation, and other similar corporate reporting requirements have therefore not been included.

[/b] Note that companies formed under sections 42 and 43 of the Companies Ordinance, 1984 as nonprofit entities, charities, or the equivalent which are included in the Fifth Schedule, are outside the scope of this review.
[/c] Refers to 'banking companies' as defined by the Banking Companies Ordinance, 1962.
[/d] Effective from December 31, 2016.
[/c] Refers to 'banking companies' as defined by the Banking Companies Ordinance, 1962.
[/d] Effective from December 31, 2016.

Table 5. Summary of principal statutory financial reporting requirements for the corporate sector/[a]		
Legislation	**Applicable Companies**	**Key Financial Reporting Requirements**
Companies Ordinance, 1984	Listed companies	**Fourth schedule** - Contents of financial statements for listed companies **SRO 633, 2014** – International financial reporting standards (IFRS) for listed companies
	Unlisted companies	**Fifth schedule** - Contents of financial statements for unlisted companies/[b] **SRO 929, 2015** – IFRS
Banking Companies Ordinance, 1962	Banks/[c]	**Second schedule** - Contents of financial statements for banks **SRO 633, 2014** – International financial reporting standards (IFRS) for listed companies
Insurance Companies Ordinance, 2000	Life and nonlife insurance companies	**Part VII, *Accounts and audit*** - Specific requirements for financial statements of life and nonlife companies
Code of Corporate Governance, 2012	Listed companies	**Section (xvi), *Corporate and financial reporting framework*** - Information to be included as annex to the directors' report in the financial statements
Code of Corporate Governance for Insurers, 2016/[d]	Insurance companies	**Section (xix), *Corporate and financial reporting framework*** - Information to be included as an annex to the directors' report in the financial statements
Public Sector Companies (Corporate Governance) Rules, 2013	Public sector companies	**Section 16 *Corporate and financial reporting framework***

28. **All companies are required to prepare an audited annual report with, at minimum, a balance sheet and profit and loss statement.**[8] Companies are classified as large, medium, or small based on minimum paid-up capital or turnover, or by sectors, as illustrated in Table 6. Companies are required to appoint an auditor to hold office at the annual general meeting of shareholders on an annual basis. Failure to comply with these requirements could result in a fine or even imprisonment for company directors.

29. **The audit threshold can pose an undue burden on small companies.** Nearly two-thirds of registered companies have paid-up capital of PKR 1 million (approximately US$9,540) or less. The requirement for financial statements to be audited by Chartered Accountants (CAs) applies to companies with paid-up capital greater than PKR 3million (US$ 28,639).[9] Thus, 75 percent of small companies have to bear relatively high costs for mandatory audits performed by auditors who may not be subject to ICAP's quality control and other professional standards such as ethical requirements. Such financial statements are not even required to be filed by

Note:
/[a] Unless stated otherwise, the definitions are as per the Companies Ordinance, 1984.
/[b] As notified by SECP in September 2015 in SRO 929.
/[c] Sections *External audit* and *Frequency of financial reporting (xix),* respectively, Corporate Governance Code, 2012.
/[d] Refer to the definitions of 'banking' and 'banking company' in the Banking Companies Ordinance, 1962.
/[e] Section 35, Banking Companies Ordinance, 1962.
/[f] Refer to the definitions of 'insurance' and 'insurer' in the Insurance Companies Ordinance, 2000.
/[g] Section *External audit* and *Frequency of financial reporting (xxi)* Corporate Governance Code for Insurers, 2015.

/[h] An extract from the definition in the PSC (Corporate Governance) Rules 2013.
/[i] Public sector companies as defined in SRO 929 and the only subset which is in scope for the ROSC A&A.
/[j] Section 23, *External Auditors*, Public Sector Companies Corporate Governance Rules, 2013.
/[k] Section 254, *Qualification and disqualification of auditors*, Companies Ordinance, 1984.
[8] Section 233, Annual accounts and balance sheet, Companies Ordinance, 1984.
[9] Section 254, Companies Ordinance, 1984.

SECP as the threshold for filing of accounts applies from paid-up capital of PKR 7.5 million (US$ 71,599) and above. It may be more cost-effective for non-audit assurance reviews of historical financial information, such as limited reviews, to be performed for such companies by professional accountants. The amendments in the Companies Bill, 2017, remove audit burden from the companies having paid-up capital of PKR 1 million (US$ 9,546) or less; however, such companies are required to file unaudited financial statements with SECP. Further, audit qualification of chartered accountant and members of the Institute of Cost and Management Accountants in Pakistan (ICMAP) is also proposed for auditors of the companies with paid-up capital of PKR 3 million (US$28,639) or less.

Table 6. Summary of A&A requirements in Pakistan by type of enterprise

	Legal definition	Accounting standards	Statutory audit requirements
Listed company/a	A company or other body whose securities are allowed to be traded on a stock exchange	IFRS as applicable in Pakistan	· Annual audit of financial statements by auditor with a satisfactory rating from ICAP's QCR program · Rotation of audit firm every 5 years for companies in the financial sector (e.g., banks, insurance companies) · Rotation of audit partner every 5 years for other companies · Limited scope review of half-yearly financial statements/c
Bank	Any company that transacts the business of banking in Pakistan/d	IFRS as applicable in Pakistan	· Annual audit of financial statements by a chartered accountant on panel of SBP-approved auditors/e · Limited scope review of half-yearly financial statements
Insurance company	Any company carrying out the business of insurance in Pakistan/f	IFRS as applicable in Pakistan	· Annual audit of financial statements by auditor with a satisfactory rating from ICAP's QCR program · Limited scope review of half-yearly financial statements/g
Public sector companies/b	A company, whether public or private, which is directly or indirectly controlled, beneficially owned by the Government, or not less than 50% voting power is held by the Government/h	IFRS as applicable in Pakistan/i	· Annual audit of financial statements by a CA with satisfactory QCR rating · Rotation of audit firm every five years for companies in the financial sector · Rotation of audit partner every five years for other companies/j
Large-size company	A non-listed company that has paid-up capital greater than PKR 200 million (US$ 1.91 million) or turnover greater than PKR 1 billion (US$ 9.54 million)	IFRS as applicable in Pakistan	· Annual audit of financial statements by a chartered accountant with satisfactory QCR rating
Medium-size company	A non-listed company that is not a public interest company, large-size or small-size company	IFRS for SMEs as applicable in Pakistan	· Annual audit of financial statements by a chartered accountant
Small-size company	Company having paid-up capital less than PKR 25 million (US 238,663) and turnover less than PKR 100 million (US$ 954,653) - (other than a nonlisted public company)	AFRS for small-size entities	· Annual audit of financial statements · Private companies with paid-up capital greater than PKR 3 million (US$ 28,639) require an audit by a chartered accountant/k

30. **The Companies Ordinance promotes transparency in financial reporting.** Private companies with paid-up capital over PKR 7.5 million (US$ 71,599) are required to file financial statements with the SECP Business Registry. Listed companies and financial institutions are required to make annual financial statements publicly available; financial statements for the larger unlisted companies are available from the Business Registry on payment of a small fee. However, some challenges remain in accessing the financial statements of unlisted SOEs. Effective compliance of Corporate Governance Rules for public sector companies will improve the timeliness of financial statements availability for public sector companies.

31. **The SECP monitors financial statements for compliance with applicable financial reporting requirements.** Responsibility for the review of audited financial statements of unlisted companies rests with SECP's Corporatization and Compliance Department. The Corporate Supervision Department reviews the financial statements of listed companies, and subsidiaries and associates of the listed companies. Initial reviews of financial statements of companies with paid-up capital of less than PKR 100 million (US$ 954,653) are performed by the corporate registrars who use comprehensive checklists to assist in detection of noncompliance.

32. **The Corporate Registrars' Office has adequate resources and suitably qualified staff to perform its monitoring duties.** Initial reviews of financial statements are performed by the corporate registrars who use comprehensive checklists to assist in the detection of noncompliance for SMEs. There are eight corporate registrars; four are professional accountants and four have extensive business expertise. Potential areas of noncompliance are forwarded to the Corporatization and Compliance Department for review and appropriate enforcement or other corrective action as required. The SECP has taken measures to expand its outreach through establishment of a Company Registration Office at Gilgit Baltistan, a capital market hub at Abbottabad, and facilitation counters at Sialkot and Gwadar.

33. **The SECP has proposed a number of changes to the statutory framework, which will significantly impact the financial reporting requirements for companies**. Amendments of the Companies Bill, 2017, include (a) an increase in the threshold for mandatory filing of financial statements and (b) significant increases in the penalties applicable to company directors for noncompliance with financial reporting requirements. Annex 1B summarizes the key proposed changes.

Listed Companies

34. **Financial reporting requirements for listed companies have been strengthened and are further aligned with international good practice.** The Code of Corporate Governance was enhanced in 2012 and now forms part of the listing regulations of the PSX. The PSX is an affiliate member of IOSCO. An IOSCO ordinary member, SECP has been a board member of IOSCO for the last three years. In addition to annual financial statements, listed companies are required to publish quarterly balance sheets and profit and loss statements.[10] Quarterly financial statements may be unaudited, but auditors are required to perform a limited scope review on the half-yearly statements. Listed companies are further required to include statements of compliance with IFRS applicable in Pakistan and with the code in the annual reports as an annexure to the directors' report.[11] Responsibility for compliance with these mandatory requirements rests with the chairman and board of directors and chief executive officer.

35. **Listed companies are required to have an audit committee**. The audit committee of a listed company should report to the board and must comprise a minimum of three non-executive directors and one independent director. At least one of the audit committee members must have significant expertise and experience in finance.[12] Stipulated in the Code of Corporate Governance, the duties and responsibilities of the audit committee include recommendations on the appointment and removal of external auditors, level of audit fees, and nonaudit services provided by the external auditor as well as review of financial statements before approval by the board of directors.

36. **Listed companies may only appoint audit firms with a satisfactory rating from ICAP's Quality Control Review (QCR) program, and auditor rotation is mandatory.** The Code of Corporate Governance for listed companies stipulates the criteria for the appointment of auditors.

[10] Section 245, Companies Ordinance, 1984.
[11] Corporate financial reporting framework section (xvi), Corporate Governance Code, 2012.
[12] Committees of the Board, Corporate Governance Code, 2012.

Only firms of auditors with a satisfactory rating from ICAP's QCR program, whose partners are in compliance with the Code of Ethics for Accountants as adopted in Pakistan, are eligible to be appointed as auditors of a listed company. Approximately 100 audit firms currently have an ICAP-issued satisfactory rating. As noted in Table, listed companies in the financial sector (e.g., banks, insurance companies) are required to rotate auditors every five years. Other listed companies must rotate, at least the audit engagement partner, every five years.

37. **As promoted by international good practice regarding ethics and independence, auditors of listed companies are restricted in the nonaudit services they may provide.** The PSX listing regulations provide a detailed list of services that auditors of listed companies are prohibited from providing to their clients. These include preparation of financial statements, actuarial services, and corporate finance services.

38. **The Corporate Supervision Department is adequately staffed to perform monitoring and enforcement of A&A requirements applicable to listed companies.** The Corporate Supervision Department has separate departments for reviewing the financial statements of companies and another for enforcement actions where necessary. The Department, which is led by an executive director with 19 years of experience as a professional accountant, comprises 27 staff with a mix of accountancy and commercial experience in a range of industries. Both on-site and off-site reviews are conducted. On average, each staff member of the M&E team in the Corporate Supervision Department reviews 40 listed and 100 unlisted companies on an annual basis. The SECP has undergone restructuring in 2017 and, as per recent arrangement, the examination of all unlisted companies except subsidiary and associate of listed companies will be done by the Corporatization and Compliance Department.

39. **The SECP applies comprehensive, risk-based review techniques and provides a summary of inspection findings and enforcement actions in its publicly available annual report.** The Corporate Supervision Department unit within the SECP has developed comprehensive, standardised checklists for reviewing the level of compliance of financial statements with applicable requirements. These requirements include the IFRS, the IFRS for SMEs, and ISAs as applicable in Pakistan as well as the Code of Corporate Governance for listed companies. Reviews are performed using risk-based criteria. The Corporate Supervision Department reviewed 928 financial statements in 2015 (1,116 in 2014 and 1,368 in 2013). There was a decrease in the number of statements reviewed as responsibility for the review of private companies with paid-up capital less than PKR 100 million (US$ 954,653) was transferred to Corporatization and Compliance Department. Summaries of the findings in respect of enforcement actions are included in the SECP's annual report which is publicly available.

Banks

40. Banks and other deposit-taking institutions are subject to high standards of financial reporting. In addition to the prudential requirements of the Banking Companies Ordinance and the general financial reporting requirements of the Companies Ordinance, listed banks and state-owned banks are also subject to Code of Corporate Governance for listed and public sector companies, respectively. The Banking Companies Ordinance takes precedence if there are conflicting requirements.

41. **Banks are only permitted to select auditors from a panel approved by the banking supervisor.** The SBP has established a framework for the audit of financial institutions within its regulatory purview and requires banks to select auditors from an approved panel. In addition to the statutory requirement of being a chartered accountant, an aspiring auditor of banks must have a 'satisfactory' rating from ICAP's QCR program. Auditors selected to the panel are further classified: Category-A auditors are eligible to audit all banks; Category-B auditors can audit banks with assets up to PKR 100 billion (US$ 954.65 million) or up to 160 branches; and Category-C auditors can audit banks with assets up to PKR 15 billion (US$ 143 million) and up to 30 branches. Audit firms are required to submit to SBP their applications for selection to the panel on an annual basis. As of January 2016, 15 audit firms were classified as Category A; 15 as Category B; and 13 as Category C.[13]

[13] Annex-A to BPRD Circular Letter No. 02 of 2016.

42. **The SBP performs on-site and off-site reviews of financial statements to determine compliance with applicable A&A requirements.** The SBP's Banking Inspection Department performs on-site examination and inspection of banks and other entities regulated by SBP. The Off-site Supervision and Enforcement Department reviews financial statements (quarterly, half-yearly, and annual statements) against the unaudited data reported by banks to the SBP.

43. **The SBP has adequate resources to perform comprehensive reviews of financial statements of regulated banks**. Reviews are conducted using comprehensive checklists to verify compliance of financial statements with minimum regulatory disclosure requirements, internal controls requirements, Code of Corporate Governance, and disclosures required by the auditors. On-site reviews focus on financial reporting requirements involving significant judgments (i.e., fair value, provisions, appropriations, and others). The staff involved in the monitoring and enforcement functions in the SBP are experienced professional accountants.

44. **While SBP communicates inspection findings with banks and their auditors, such findings are not included in the annual report, even at the summary level.** The SBP's inspection teams conduct thorough reviews that include meetings with the auditors of banks to discuss areas of concern (e.g., weaknesses of the banks' internal control systems, adequacy of provisions, and compliance with statutory and prudential requirements).[14] However, results of monitoring and enforcement activity are not included in SBP's annual report, even at the aggregate level, or publicly disclosed. Nonetheless, SBP discloses its major actions such as restructuring/dissolution of institutions in SBP reports.

Insurance Companies

45. **The insurance industry, though relatively small, is growing and subject to similarly high standards of financial reporting and good governance as listed companies and banks.** Financial reporting requirements for insurance companies are stipulated in the Insurance Companies Ordinance, 2000. These requirements include separate statements of premiums, claims, claims analysis, expenses, investment income, and exposures; instead of a balance sheet, a statement of assets and liabilities is required. Life insurance companies are required to provide financial statements on each statutory fund run by the company.

46. **Corporate Governance Rules specifically for insurance companies have been promulgated**. The Code of Corporate Governance for Insurers, 2016, are effective as of November 9, 2016. The Code establishes mandatory additional A&A requirements similar to those for listed companies such as the requirement to have an audit committee, mandatory auditor rotation, publication of quarterly unaudited statements, and half-yearly statements subject to a limited scope review by the auditors.

47. **Insurance companies are only permitted to select auditors from a panel approved by SECP, the insurance supervisor**. The Insurance Ordinance requires insurance companies to appoint an SECP-approved auditor and stipulates the responsibilities of the auditor. To be considered, an audit firm must have a minimum of two partners who are ICAP members and currently hold a 'satisfactory' rating from the QCR process. Firms are scored according to selection criteria such as size (number of qualified and partly qualified staff, including trainees); the last three QCR ratings from ICAP; affiliation with international network firms; audit experience of the firm with insurers during the preceding five years; and audit experience of the firm with listed companies in the last two years. Approximately 14 audit firms are on the approved auditor panel for insurers. Life insurance companies are further required to obtain an opinion from an appointed actuary on the valuation of the policyholder liability in the balance sheet.[15]

48. **The SECP Insurance Division performs on-site and off-site monitoring and enforcement of A&A requirements for insurance companies.** Financial statements of insurance companies are reviewed by SECP for compliance with the Companies Ordinance, Insurance Ordinance, SEC (Insurance) Rules, Federal Government Insurance Rules, and Code of Corporate Governance where applicable. The SECP Supervision Department also reviews quarterly regulatory returns, including solvency returns for life insurance companies and admissible assets. The review team comprises 24 members with

[14] BSD Circular Letter No. 10 of 2003 and Para 3.3 of Part-A BPRD Circular No. 7 of 2015.
[15] Section 52, Insurance Companies Ordinance, 2000.

requisite competence and knowledge of financial reporting and auditing. The Supervision Department has developed methodologies and manuals to review compliance on a more robust and consistent basis.

49. **Filing of annual statements is mandatory in compliance with Section 11 and 12 of the Insurance Companies Ordinance, 2000.** To enhance the monitoring of compliance with elementary licensing requirements on an annual basis, the Insurance Division has made it mandatory for the insurers (as of December 31, 2015) to submit a statement of compliance with Section 11 and 12 of the insurance ordinance duly signed by the chief executive/ principal officer and two directors of the insurer within five months of the close of the year. The statement is required to be filed along with the review report and certificate by the statutory auditor of the insurer.

Public Sector Companies

50. **Transparency and accountability in the financial reporting of public sector companies was significantly boosted by the introduction of PSC (Corporate Governance) Rules.** The PSC Rules were introduced in 2013 and have been a positive development in improving the quality of financial reporting of state-owned/-controlled commercial enterprises. Similar to the requirements for listed companies and financial institutions, public sector companies are now required to prepare quarterly balance sheets and profit and loss statements. The contents of the director's report to the shareholders of public sector companies include disclosure of subsidies or other forms of financial support from the government as well as a summary of key operating and financial data for the previous six years.

51. **Audit requirements for public sector companies are now of a similarly high standard as those of listed companies**. Public sector companies are required to have audit committees comprising a majority of non-executive directors who are financially literate. Public sector companies in the financial sector (e.g., banks, insurance companies) are required to rotate auditors every five years. Other public sector companies must at least rotate the audit engagement partner every five years. Auditors of public sector companies must provide a review report on the statement of the company's compliance with the Code of Corporate Governance.

52. **The monitoring and enforcement of compliance with applicable A&A requirements by public sector companies will improve with the recent restructuring in the Corporatization and Compliance Department.** The review of financial statements of public sector companies has recently been added to the mandate of the Corporatization and Compliance Department. The Department has undergone internal restructuring and is now being led by the Executive Director with 20 years of experience as a professional accountant. Professional accountants will perform the monitoring activities. It is expected that the increase in the reviewers' work force and strict compliance with the Code of Corporate Governance will improve A&A practices in the public sector companies.

53. **Monitoring of the compliance of the Code of Corporate Governance in public sector companies is performed by the Corporatization and Compliance Department.** The Code of Corporate Governance in public sector companies is a fairly new undertaking; however, a marked improvement is seen in filing of the statement of compliance in public sector companies. Sixty percent of the public sector companies filed the statement of compliance in 2016. The actual compliance of the Code of Corporate Governance in the public sector companies requires strengthening the governance, accounting, and auditing practices for effective utilization of resources. The A&A-related provisions of the Corporate Governance Rules showed that out of the total public sector companies registered with SECP, 58 percent are filing their accounts, 32 percent have formed independent audit committees, and 72 percent are holding regular annual general meeting.

The Accountancy Profession

54. **There are five professional accountancy organizations in Pakistan, with 22,000 professional members, including chartered accountants, ACCA accountants, and cost and management accountants.** As the principal professional accountancy organization, the Institute of Chartered Accountants of Pakistan (ICAP) has over 7,428 members in public practice, industry, and to a

[16] As of December 9, 2016.

lesser extent in the public sector.[16] The ICAP has almost 25 percent of professionals in public practice. Pakistan has a large number of small and medium-size accounting and auditing firms. There are 489 registered practicing firms in Pakistan, with 354 sole proprietors and 135 partnership firms. The chartered accountant designation is highly prized, and ICAP has close working relationship with s leading international professional accountancy organizations, the Institute of Chartered Accountants of England and Wales (ICAEW). The ICMAP membership is also held in high regard. Both professional accountancy organizations are members of the International Federation of Accountants (IFAC)[17] as well as the Confederation of Asia Pacific Accountants (CAPA), South Asia Federation of Accountants (SAFA), Asian-Oceanian Standard-Setters Group (AOSSG), and the AAOIFI. The two UK-based professional accounting bodies, ACCA and Chartered Institute of Management Accountants (CIMA),[18] have full IFAC membership and have branch offices in Pakistan. The ICAP and ICMAP also collaborated with the Auditor General of Pakistan in 1993 to form the Pakistan Institute of Public Finance Accountants (PIPFA), which is producing a mid-tier accountant stream for the public sector and corporate sector. The PIPFA is also an associate member of IFAC.

55. **The ICAP is run by a governing council that is responsible for discharging its statutory responsibilities**. Positions on the council are voluntary. The council comprises 15 elected members and 4 members nominated by the Government for a four-year term. The council elects the ICAP president for a one-year term.[19] The ICAP's responsibilities include issuing practicing licenses to statutory auditors and serving as the examining body for the chartered accountancy qualification.[20] The ICAP lacks sufficient staff to facilitate research activities and largely relies on its members for technical input on a voluntary basis.

56. **Members of ICAP and ICMAP are held to high standards of professional and ethical conduct, although these standards could be improved by greater alignment with international good practice**. The local code of ethics is based on the Code of Ethics for Professional Accountants of the International Ethics Standards Board for Accountants (IESBA). Members of ICAP and ICMAP are expected to complete 40 hours of continuing professional development (CPD) each year. Following an adopted input approach, ICAP members are required to (a) complete at least 120 hours or equivalent learning units of relevant professional development activity in each rolling three-year period, of which 60 hours or equivalent learning units should be verifiable; (b) complete at least 20 hours or equivalent learning units in each year; and (c) track and measure learning activities to meet the above requirements. The ICMAP has adopted the 2015 Code of Ethics with modifications. Professional accountancy organizations may also consider employing modern techniques such as webinars and e-learning assessments modules to increase members' participation in professional development activities.

57. **Members of ICMAP are primarily cost accountants.** Practicing members of ICMAP perform statutory audits of companies where paid-up capital is PKR 3 million (US$ 28,639) or less; however, only 64 ICMAP members are in public practice. The ICMAP has recently established its Quality Control Department; however, no quality assurance report has been published so far. The majority of ICMAP members work in industry. In addition, some ICMAP members provide cost audit services to companies falling within certain manufacturing industry sectors. The ICMAP revised its curriculum in 2012, which was then further reviewed in 2015, keeping in view the global changes in information and communication technology and following IFAC-issued International Education Standards.

58. **Professional accountancy organizations and regulators are promoting companies in adopting sustainability reporting and integrated reporting.** The profession is embracing new global trends for sustainability reporting and integrated reporting on a voluntary basis. The ICAP and ICMAP joint committee has taken the initiative to encourage sustainability reporting by introducing an award based on the criterion of the Global Reporting Initiative, an international standard on sustainability reporting by IFAC and the International Integrated Reporting Council. The SECP has also issued voluntary guidelines for Corporate Social Responsibility.

59. **The PIPFA was constituted in 1993 by ICAP, ICMAP, and the Auditor General of Pakistan to provide long-**

[17] Refer to Annex 2 for details of compliance with IFAC's membership obligations.
[18] Information for CIMA members was not obtained as it has recently started its operations in the country and most of the CIMA members are holding either of the certifications included in the total number of professionals.

[19] Section 12(2) of the Chartered Accountants Ordinance, 1961.
[20] Section 9 of the Chartered Accountants Ordinance, 1961.

term and enduring foundations for almost all public financial management (PFM) reforms. An associate IFAC member, PIPFA provides a mid-tier accounting stream for the profession. The PIPFA qualification is set as mandatory by the Auditor General of Pakistan for promotion in government audit and accounts department from the clerical tier to the operational tier. Also, its members are eligible for the position of company secretary in the public listed companies as per SECP criteria. It has 2,104 members, including associate and fellow members from the corporate sector as well as from the public sector. With ICAP efforts, the Chartered Institute of Public Finance and Accountancy (CIPFA) and PIPFA signed a memorandum of understanding in October 2015 to promote high-quality PFM practices in Pakistan. The reform initiated with the joint collaboration of private and public sector accountants and the firm commitment from the Government to create a unique stream of PFM professionals. However, it requires continuous commitments from the sponsoring agencies to evolve a well-designed professional qualification framework that is sufficiently robust yet flexible in its mode of delivery, and offers opportunities for the development of other training modalities to meet the inevitable progress in PFM needs.

60. **With a strong presence in Pakistan, ACCA has approximately 8,000 Pakistan national members, of which 23 percent are working in the public sector**. The ACCA qualification is well recognized in Pakistan; the Auditor General of Pakistan has included ACCA qualification in Basic Scale-16 and above for direct recruitment. The Ministry of Finance has also included ACCA qualification eligible for additional allowance for public sector employees.[21] Further, ACCA qualification is also included under Code of Corporate Governance, 2012, as one of the prescribed qualifications for a chief financial officer of a listed company. The Pakistan chapter of ACCA also established practicing firms in 2015 to facilitate its 32,000 students, which include 6,800 affiliates.[22] The ACCA members are subject to 40 hours of mandatory training in the relevant field. The ACCA Pakistan chapter is actively promoting export of accounting services and has entered into memorandum of understanding with various global companies for providing offshore accounting solutions.

61. **As is the case in many countries, the 'blue chip' end of the audit market is highly concentrated and dominated by audit firms affiliated with international networks**. The rest of the market is subject to intense competition among small and medium-size practices. According to ICAP, nearly two-thirds of listed and large private companies are audited by six firms that are part of an international network. Small and medium-size practices typically provide audit and tax services to small and medium-size enterprises. There is a high cost and resource effort associated with delivering quality audit services to these smaller enterprises, which have limited demands for audits other than the statutory requirement. It is therefore a competitive environment for new entrants and small and medium-size practices. IFAC SMP committees, IAASB, and various leading professional accountancy organizations around the world have issued guidance for small and medium practices.

62. **Pakistan has one of the lowest representations of female accountants in the region.** The percentage of female accountants is 9 percent,[23] compared with 30 percent in Sri Lanka and 22 percent in India. Out of a total of 7,135 chartered accountants in the country, only 500 are women. The percentage of female students enrolled in the accountancy profession is also quite low and has ranged from 18 percent to 22 percent over the last three years. A major factor contributing to low female participation is the lack of an enabling work environment such as day-care and pick-and-drop facilities at workplaces (Box 2). One of the measures adopted by the Big-4 international network firms and large corporations that seem to work well in increasing retention rates of female professional accountants has been the provision of day-care services for staff. Measures should be introduced to increase the participation of women in the accountancy profession.

BOX 02

Employing quality resources and reducing gender gap through unique working model

A QCR-rated all-women chartered accounting firm has been set up by a senior female ICAP member. This model provides opportunities for female accountants through flexible work hours and work-from-home arrangement and ensures quality services to the client.

[21] F.No. 1(2)imp/2016-333 dated July 1, 2016
[22] Passed all the exam but have not undergone training
[23] This includes chartered accountant, ICMAP accountants, and ACCA accountants.

63. **Pakistan has a competitive edge to be part of the high-end finance and accounting global outsourcing market, which is growing over 10 percent annually and forecasted to reach US$35 billion by 2017 (Box 3).** Pakistan has total of 22,000 professional accountants with national and international professional accountancy organizations. Currently 70,000 students are registered with the professional accountancy organizations. The average increase in students is 10 percent per annum. The profession's contribution to the skills sector in Pakistan is significant with almost 31 percent of national accounting professionals working abroad, also providing a source of foreign remittances. Pakistani accountants have demonstrated great acceptability in the international market due to hands-on knowledge of IFRS. Pakistan has an opportunity to develop knowledge economy and promote accounting shared services in international and local markets. An established telecom sector provides readiness of the infrastructure to establish an accounting outsourcing industry. Pakistan has made progress in this sector in the last two years. Professional accountancy organizations are encouraged to work jointly to develop policy and code of conduct to promote finance and accounting shared services in Pakistan in the international and local market and provide code of conduct for shared services and relevant talent, which is technically and ethically strong, commercially aware, and digitally enabled, with strong communication skills and proper service orientation (Refer Table 7).

BOX 03

Growing finance and accounting outsourcing trend in Pakistan

- International telecom operators have set up a shared services center (including finance and accounting) in Pakistan, which is serving their operations across the globe.
- ACCA (in 2015) assisted a U.K.-based finance and accounting services aggregator 'iplanaccounting'/Azure Premier (Pvt) Limited to partner with a Lahore-based professional accounting institute. Now they are serving over 1,300 clients with more than 70 resources in Lahore.
- Another U.K.-based SMP, 'adroitaccountax' accounting practice, set up its back office in Pakistan and in six months' time has expanded from less than 5 resources to over 30 resources based out of Pakistan.
- Arthur Lawrence Pakistan, a U.S.-based business process outsourcing, having a back-end office in Karachi, has witnessed an exponential growth in finance and accounting outsourcing, with a vision to expand their talent base from the current more than 50 professional accountants.
- 'Upwork.com' has several individuals and SMPs who have delivered over thousands of hours in the field of finance and accounting from Pakistan.
- The Big 4 are either establishing or have established their shared service practices for local and international clients out of Pakistan.

Table 7. Number of accounting professionals and students in various Professional accountancy organizations

Name of professional accountancy organization	Qualified professionals working in Pakistan	Qualified professionals working outside Pakistan	Number of students and partially qualified students
ICAP	5,878	1,550	20,000
ICMAP	6,428	1,000	15,000
ACCA	3,100[/a]	4,200	32,000
PIPFA		–	2,104[/b]
TOTAL	15,534	6,750	69,104

[/a] Excludes 118 members of ICAP holding dual certifications.
[/b] From IFAC Dashboard Report.

64. **A number of entities, including banks in Pakistan, have organisational/business structure where outsourced services organizations are used for operational purposes.** Service providers of all types — especially those servicing the financial institutions, hosting data centers, providing telecommunication services, arranging payroll-related services, managing logistic procedures — have a need to demonstrate to their customers and their customers' stakeholders that they provide complete, accurate, and secure transaction processing in a controlled environment. Further, the organizations that provide services effecting a company's financial statements necessitate a report on internal controls for the benefit of the company's management and their financial statements auditors. This report can eliminate or significantly reduce the requirement for the company's auditor to do additional testing of a service provider's control. An International Standards on Assurance Engagement (ISAE) 3402 report, which constitutes an independent auditor opinion, is an

effective method of communicating that internal controls over systems and processes are suitably designed and operating effectively within a well-controlled environment. Such formal communication has recently become an important success factor when differentiating between service organizations and demonstrating ability to achieve high-quality performance. Awareness of the use of such third party assurance under ISAE 3402 appears to be low in the country.

Audit Regulation

65. **The accountancy profession in Pakistan was largely self-regulated by ICAP until the recent establishment of the independent Audit Oversight Board (AOB).** The ICAP recently revised its QCR program. The SECP has made it mandatory for all audit firms conducting statutory audits of listed, large-size companies or other regulated companies to have a satisfactory QCR rating.[24] The QCR program follows the requirements of IFAC's Statement of Membership Obligation (SMO) 1, *Quality Assurance*, in terms of overall design, basis for selecting firms, and criteria for assessing compliance with the IAASB's ISQC 1. The program is based on a mixed approach, which combines elements of risk-based and cycle approaches with quality reviews of audit firms conducted every two-and-a-half years.[25] Any audit firm operating in Pakistan wanting to be 'QCR-rated' can participate in the program.

66. **The QCR program is placed under the oversight of the Quality Assurance Board (QAB).** Board members are appointed for a three-year term, renewable once. The QAB reviews results of the QCR and approves the rating assigned as a result of it (Table 8). The QCR framework requires that the majority of QAB members are ICAP members. Currently, 9 of the 11 board members are ICAP members. Out of 9 ICAP members, the QCR framework expressly requires only 2 members to be non-practitioners. The current composition of the Board is 4 SECP nominees, 1 nominee from both SBP and PSX and 5 ICAP nominees (3 practicing and 2 non-practicing).

67. **The quality assurance reviews carried out as part of the QCR program are a combination of (a) engagement audit reviews and (b) firm quality control system reviews, in line with international good practice.** The audit engagements reviewed are selected in such a manner that at least half of the audit partners are covered. Inspections are carried out using a checklist issued by the QAB predecessor, QCR Committee. On a regular basis, QCRs are charged with conducting the inspections. These individuals are part of the ICAP staff and as such are appointed and remunerated by it.

68. **The main competency requirements to become a QCR reviewer is ICAP membership and a minimum two-year post-qualification experience, which is relatively low given the importance of the QCR process and its potential complexity.** The QCR reviewers cannot have any involvement with an audit firm, but they are not subject to any 'cooling-off' requirement if they are former practitioners.

69. **The outcome of the QCR inspection depends on the result of the assessment of each review (engagement versus firm quality control) and may result in the removal of the audit firm from the list of QCR-approved firms.** For each audit firm review, a 'satisfactory' or 'unsatisfactory' rating is assigned to both engagement and the firm's QCR. If both reviews lead to an unsatisfactory conclusion, the firm is removed from the list-subject to appeal with QAB. When only one of the reviews is deemed unsatisfactory, the reviewed firm remains on the QCR-approved list but is required to undergo a review one year later instead of the normal two-and-a-half years (Table 8).

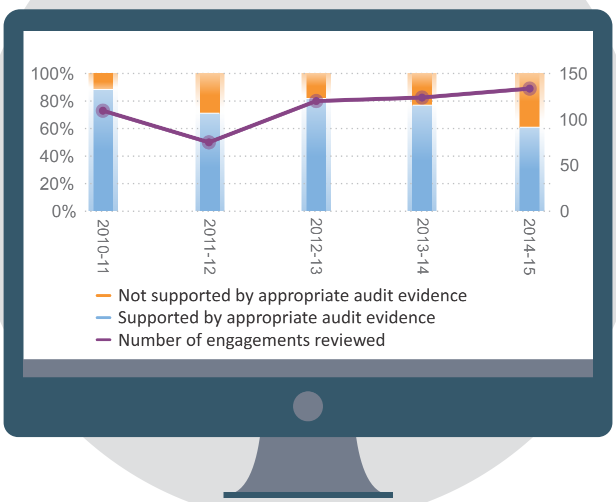
Table 8. Outcome of individual audit QCRs

Firm's Quality Control / Firm's Engagement	Satisfactory	Unsatisfactory
Satisfactory	No action (firm maintained on QCR-approved list)	One-year probation period and follow-up review
Unsatisfactory	One-year probation period and follow-up review	Removal from QCR-Approved list

[24] Insurance, corporate brokerage, and 'Modaraba' companies.
[25] ICAP Framework of QCR Program 2015. http://www.icap.org.pk/quality-assurance/qcr-framework-revised/.

70. **In 2015, QAB published a comprehensive report on QCR activities conducted during the FY2014-15, including a summary of the main deficiencies uncovered by the quality assurance reviews.** The report is published on the ICAP website.[26] The number of audit firms and individual engagements reviewed was 52 and 133, respectively, (compared to 62 and 123 during the previous year). The report includes a table summarizing the assessment of individual audit engagements reviewed over the last 5 years. It indicates that the proportion of engagements “not supported by appropriate audit evidence” was the highest in the more recent reviews, namely 39 percent versus 20 percent on average during the previous 4 years (see Figure 3), however, the report does not provide an explanation for such a sharp increase.

Figure 3. QCR: Assessment of Individual Audit Engagements Reviewed



71. **The creation of AOB with wide-ranging powers will aid Pakistan in meeting the level of standards of other jurisdictions around the world that have recently taken steps to strengthen the independence of auditors and the quality of audits.** The AOB was established through amendments in the SECP Act, 1997, which were prepared at the initiative of ICAP, SECP, and other regulators and stakeholders. The amendments in the SECP Act, 1997, were approved in the National Assembly and in the Senate in July 2016. According to the amendments obtained as part of this ROSC A&A, the AOB's roles would include (a) registering and de-registering audit firms, (b) overseeing QAB and the QCR system, (c) directing ICAP to make changes to the QCR system as AOB deems necessary, (d) ensuring auditing standards in Pakistan conform with ISA, and (e) conducting inspections and inquiries. The AOB have seven members appointed by the Government[27] on the recommendation of a Nominating Committee comprising high-level government officials, including Secretary to the Government's Finance Division, SBP Governor, ICAP President, and SECP Chairman).

72. **Although steps have been taken toward independent oversight, with the establishment of AOB, further development and a sustainable institutional framework are required.** The institutional capacity of AOB needs to be built, by ensuring adequate funding arrangements for AOB and QAB, affiliation with the International Forum of Independent Audit Regulator (IFIAR), and support in building the capacity of AOB and QAB. (Refer to Annex 6 for factors to be considered for the efficient functioning of the audit oversight).

73. **The ICAP is adopting a draft practice review framework that will run in parallel to the QCR program and will upgrade licensing procedures for non-QCR-rated firms.** This program aims to enhance the current licensing regime for all practicing members and compliance with ISQC 1. The scope of the practice review includes all firms operating in Pakistan providing audit, assurance, or related service assignments conducted under any legal or financing reporting framework, as applicable in Pakistan. The draft framework will ensure the compliance of SMO 1 across the board and will provide mechanism to review performance before renewing the practice license for non-QCR-rated firms. The framework is under active consideration of the ICAP Council and will improve the procedure for obtaining license by the auditors engaged in practice.

[26] http://www.icap.org.pk/quality-assurance/qcr-documents/qab-report/.
[27] The Government of Pakistan has announced the 7 AOB member on December 26, 2016, and the first AOB meeting was held on January 20, 2017.
[28] Refer to Annex 4 for IES compliance status.
[29] It includes subjects of Functional English, Business Combination, Quantitative Methods, and Introduction to Information Technology.
[30] It includes subjects of Introduction to Accounting, Economics and Finance, Business Law, Business Management and Behavioral Studies Application, Financial Accounting and Reporting, principles of Taxation, Cost and Management Accounting and audit and assurance.
[31] It includes subject of Advanced Accounting and Financial Reporting, Corporate Law, Business Management and Strategy, Business Finance Decisions, Advance Taxation and Audit, Assurance and Related Services.
[32] It includes Financial Reporting and Assurance and Strategic Management.
[33] Criteria is detailed in Bylaw 123 separately for students with 14 years of education, higher secondary school certificate or equivalent, and A level.
[34] As per ICAP Directive 1.2 of 2014, the approved regulations for accounting education tutors (RAETs) provide coaching facility for module AFC and CAF.
[35] National University of Science and Technology, University of Lahore, Sukkur Institute of Business Administration, Institute of Business Management, and University of Management and Technology.
[36] ICAP's directive 1.03 training regulations and guidelines 2015.

Professional Education and Training

74. **The ICAP has revised the syllabus for the chartered accountancy qualifications to further align with the International Education Standards for professional accountants**. The ICAP has restructured the chartered accountancy qualification by incorporating the latest developments in the curriculum.[28] This was done by adopting a learning outcomes-based approach and closely aligned the syllabus to that of ICAEW. Aspiring chartered accountant complete 21 papers spread over four levels: Assessment of Fundamental Competence (AFC),[29] Certificate in Accounting and Finance (CAF),[30] Certified Finance and Accounting Professional (CFAP),[31] and Multi Subject Assessment (MSA).[32] Each stage has stand-alone recognition. Ethics are also embedded in each discipline being taught and examined. The syllabus was reviewed by ICAEW at ICAP's request and was found to be in line with IFAC International Education Standards (IES).

75. **Acceptance to the chartered accountant qualification program is relatively straightforward and accessible to a wide range of aspiring professional accountants.** Students scoring a minimum of 50 percent marks in the higher secondary school certificate or completed A-levels or at least 45 percent marks in a university degree program are eligible for admission to the chartered accountant program. Students with 14 years of education from any degree-awarding institution recognized by the Higher Education Commission (HEC) are also eligible to claim exemptions from 4 AFC and 2 CAF papers after fulfilling the criteria specified.[33] However, the percentage of students who passed the final examination has been low. In the last three years, the passing rate ranges from 20 percent to 30 percent.

76. **The ICAP has revised its education scheme and increased the level of cooperation with leading universities and higher education providers in the country to better support aspiring members.** To attract the best students to the profession, ICAP has developed a policy for recognizing universities, in addition to approved registered private tutors.[34] This system works through prescribing the syllabus of the education providers along with a monitoring system. Under this scheme, specified degree-awarding institute status was given to two of the highest-ranking universities in Pakistan: Lahore University of Management Sciences and Sukkur Institute of Business Administration. Graduates of these universities are eligible to claim 13 exemptions from AFC and CAF levels. The ICAP has signed memoranda of understanding for mutual recognition with some universities[35] to create the arrangement for a Relevant Degree Awarding Institute (RDAs). Graduates with a minimum of 16 years of education from institutions other than the Specified Degree Awarding Institute or any local or foreign institution recognized by the Higher Education Commission are eligible to claim exemption from 8 papers (4 AFC and 4 CAF). The ICAP has mutual recognition arrangements in place with leading international professional accountancy organizations such as ICAEW, CIPFA, and CIMA, and Certified Public Accountants (Canada).

77. **Practical training is a prerequisite for ICAP membership.** The period of training varies with the mode of entry in the training organizations, which provides much needed flexibility and enhances the attractiveness of the profession. The practical training period for CAF-qualified students is 3½ years, 4 years for students entering directly for graduate programs or Relevant Degree Awarding Institute, and 3 years for students graduating from the Specified Degree Awarding Institute.[36] Further, to accommodate students who may increase with revision in the education policy, ICAP has

revised its training regulation and expended the horizon of training organizations by approving training in entities other than audit firms such as large corporate and regulatory organizations.

78. **The ICMAP has revised its syllabus to address the gaps with IES requirements.** The realignment of curriculum has enabled ICMAP in entering the memorandum of understanding for mutual recognition with CIMA and other institutes such as CPA Australia and CPA Ireland. The ICMAP has also approved new training scheme for its students. Under the new scheme, the students will be enabled to get practical training, including the entire cycle of accounting and finance. The ICMAP is taking steps to review their program against the latest IES requirements and address any identified gaps.

79. **The PIPFA is encouraged to take full member status for IFAC.** The PIPFA responsibilities include setting requirements for initial and continuing professional development and ethical requirements, and establishing an investigative and discipline system for mid-tier corporate and public finance accountants. The PIPFA is an IFAC associate member.[37] The reciprocal exemptions on PIPFA qualification available with the major accounting bodies, such as ICAP, ICMAP, ACCA, CIMA, and CIA, are only for corporate-stream students. Due to a recent MoU with CIPFA, some exemptions are now available for public sector accountants as well. The PIPFA provides training on IPSAS to employees of the Auditor General, Pakistan Military Accounts Department, Local Fund Audit, Treasury Departments of the Punjab Government, and Pakistan Railways Accounts Department. To keep members up to date on IPSAS, PIPFA monitors new and amended IPSASB pronouncements, and disseminates them to members through journals and CPD programs. In addition, PIPFA participates in the international standard-setting process by inviting members to review and respond to exposure drafts issued by IPSASB. The PIPFA is encouraged to participate in the international standard-setting process by reviewing and responding to IAESB-issued exposure drafts. The PIPFA is also considering IFAC guidance on the education training and development of accounting technicians.

80. T**he Association of Accounting Technicians has recently launched short qualification programs in Pakistan in collaboration with the renowned accountancy college. An IFAC member,** the Association of Accounting Technicians has recently entered into an MoU with one of the accountancy colleges and the registered tuition provider for chartered accountancy qualification. The short courses are particularly designed to help SMEs with understanding of budgeting for a business, managing cash flow to help keep a business healthy, and reading and understanding financial documents.

81. **The profession has a stream of partly qualified accountants who lack career progression.** In the absence of a proper accreditation body, the career progression for the partly qualified accountants poses a real challenge. The mid-tier accountants are well positioned to serve the growing market of SMEs. The Higher Education Commission of Pakistan in collaboration with the professional accounting institutions would be well served by a national accountancy accreditation body that could set equivalence criteria and allow exemptions based on specified criteria. This would serve the need of the SME sector and sets the career paths for partly qualified accountants.

Setting A&A Standards

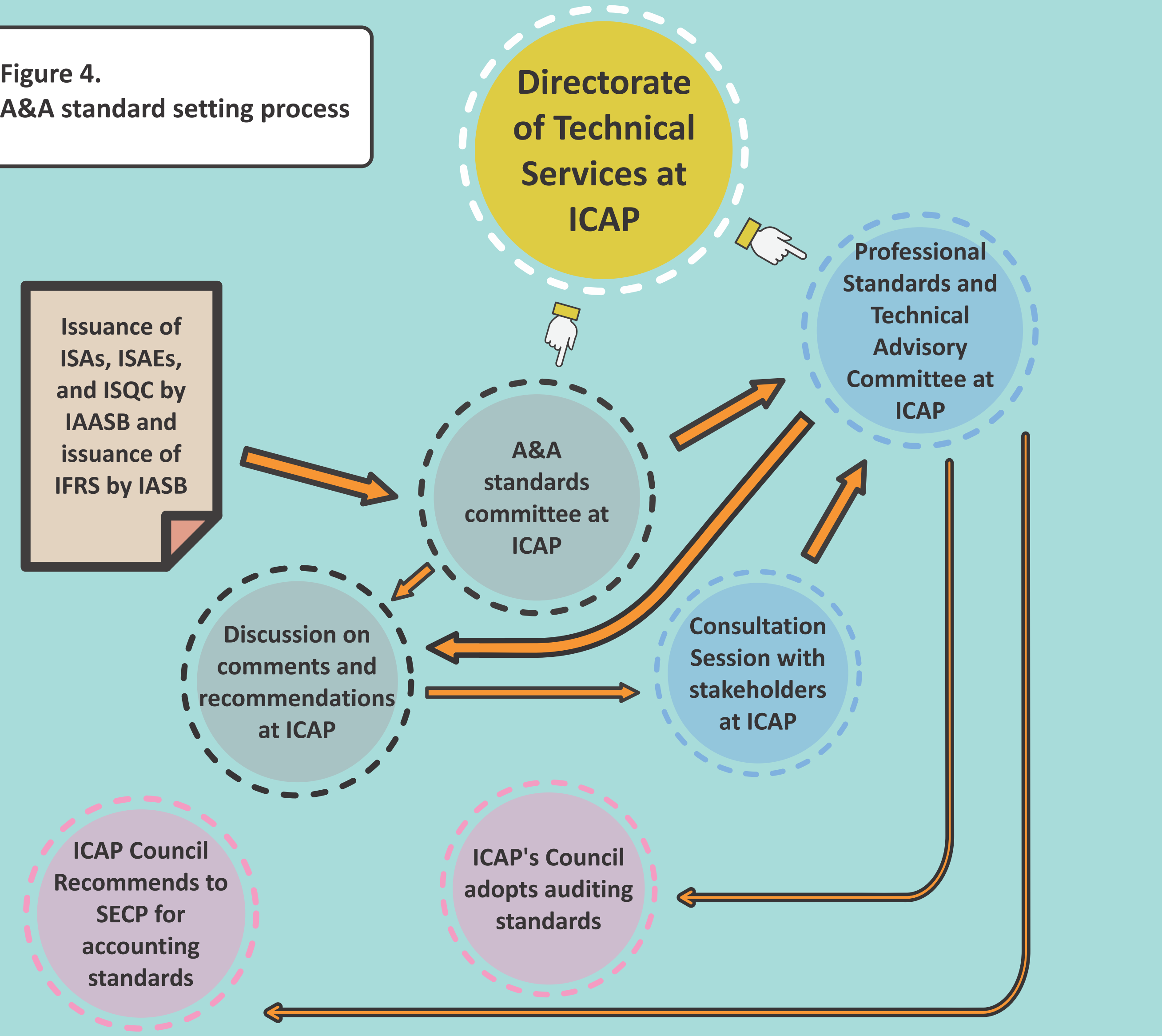
82. **Financial reporting standards applicable to the corporate sector are stipulated in SECP-issued statutory notifications as recommended by ICAP, whereas ICAP promulgates adoption of the ISA.** The SECP holds the statutory authority for promulgating accounting requirements in Pakistan. In practice, ICAP's A&A Standards Committees, under the supervision of the Professional Standards and Technical Advisory Committee recommend accounting standards based on full, unmodified IFRS to the SECP, whereas auditing standards are notified for adoption by the ICAP Council after due consultation. The mandate of the A&A Standards Committees includes providing comments and holding stakeholder consultations on exposure drafts circulated by IASB for IFRS and by IAASB for ISA. These comments and recommendations on the proposed standards are discussed at the Professional Standards and Technical Advisory Committee and approved by ICAP's Governing Council before submission to SECP for consideration (Figure 4). After discussion, ICAP's recommendations are accepted; however, the SECP has no legal obligation to act on these.

[37] Refer to SMO status in Annex 5.

Standard-setting Process for Other Financial Reporting Standards: AFRS for small-size entities and Islamic Financial Accounting Standards

83. **The ICAP has developed accounting and financial reporting standards (AFRS) for small-size entities and Islamic Financial Accounting Standards (IFAS) for Islamic banks/development finance institutions.** The Accounting Standards Committee develops the standards for interest free modes of investment and financing. The standards, so developed, are exposed to stakeholders; any comments received are duly considered; and the revised standards are presented to the Professional Standards and Technical Advisory Committee. The standards are then approved for adoption by the ICAP Governing Council and subsequently sent to SECP for notification.[38]

Figure 4.
A&A standard setting process



[38] SRO 929 of 2015.

84. **The national standard-setting process requires more transparency.** Public consultation on discussion papers and exposure drafts for national standards is not a statutory requirement; however, ICAP does undergo a consultation process with all stakeholders for the national standards. The consultation process may take four to six months. The comments received on the national standards are not shared publicly.

85. **The AFRS were introduced in 2007 and suggest a consistent and simple format for the presentation of the financial statements for small-size entities.** The objective of issuing standards for small-size entities is to outline the bare minimum provisions to report financial information by such an entity. The framework requires information about financial performance and financial position and at minimum includes statements of financial position, income statements, accounting policies, and explanatory notes.

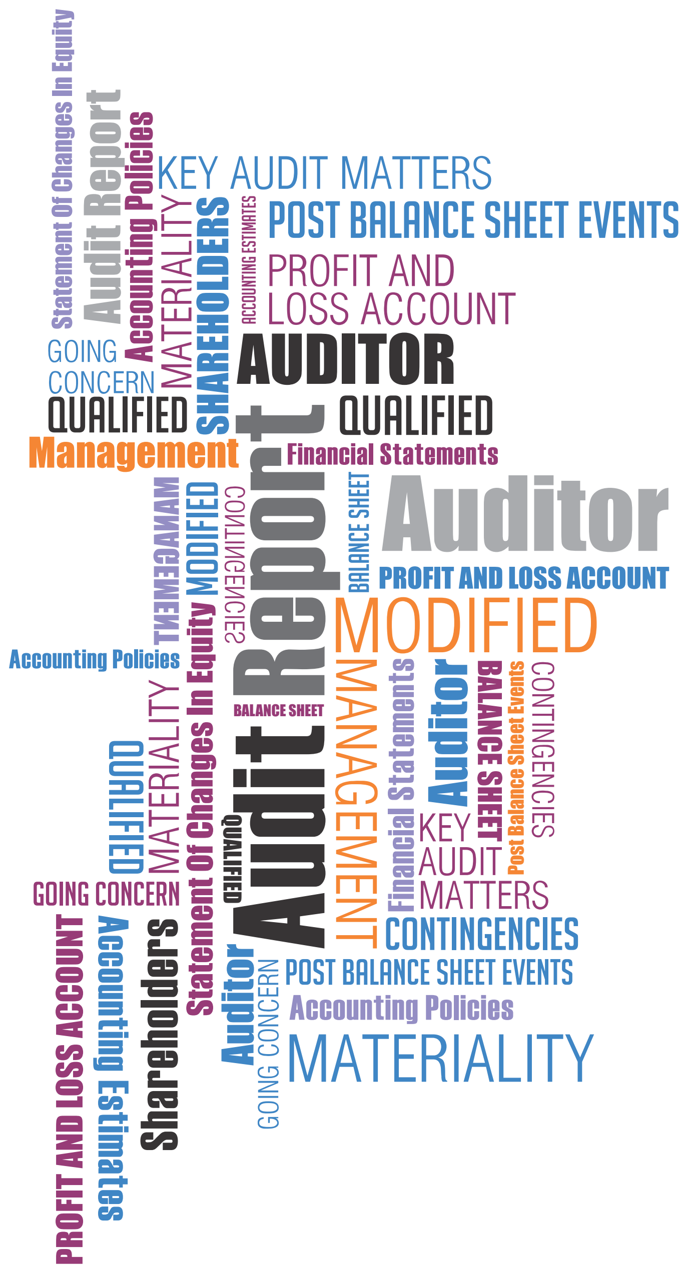
86. **Islamic Financial Accounting Standards have been developed by ICAP in line with AAOIFI Accounting Standards and tailored according to Pakistan's needs, thus enhancing consistency of presentation and promoting comparability with international market.** A summary of IFAS is as follows:

- **IFAS 1 for Murabaha** is mandatory for banks undertaking of Murabaha transactions effective from August 24, 2005.[39]
- **IFAS 2 for Ijara** is mandatory for Islamic banking institutions.[40]
- **IFAS 3 for profit and loss sharing on deposits** was to be implemented in June 2013 by SECP notification. However, SBP has not yet issued its regulatory instruction for implementation of this standard.[41]

[39] http://www.secp.gov.pk/ciculars/pdf/cir_2010/Cir_07.pdf.
[40] http;//www.secp.gov.pk/otification/pdf/2007/Notif_May22_IFAS2.pdf.
[41] SRO 584/2013.
[42] This represent listed SOE company in energy sector. The delay in the publishing of report was because of regulatory dispute with regulators on revenue recognition.
[43] Approved accounting standards as applicable in Pakistan, which comprise such IASB-issued IFRS as are notified under the Companies Ordinance, 1984—the provision of and directives issued under the Companies Ordinance, 1984. In case requirement differs, the provisions or directives of the Companies Ordinance, 1984 shall prevail. Hence, there may be deviations in the financial statements prepared based on approved accounting standards and provisions and directives of the Companies Ordinance, 1984, and the IFRS requirements.

C. Observed Reporting Practices and Perceptions

87. This subsection summarizes the ROSC teams review of financial statements and perceptions of the accounting and auditing practice in Pakistan.



[44] Includes 22 listed companies (9 manufacturing, 3 energy sector companies, 2 banks, insurance, leasing and service sector companies, and one brokerage house); 4 unlisted public interest companies and public companies; and 3 SOEs.
[45] Out of 50 selected financial statements, 10 relate to MSE where applicable reporting standards are the IFRS for SMEs. The application date of the IFRS for SMEs is the period beginning January 1, 2015. Thus, the availability of such financial statements is expected after September 30, 2016.

Financial Statements Review

88. A sample of 39 financial statements recently issued in the jurisdiction were reviewed by the ROSC team to determine whether the statements largely align with the expected presentation and disclosure requirements of the applicable financial reporting framework and have been prepared without significant errors or omissions. The sample comprised financial statements related to the year ending June 2015 with the exception of two audited statements for 2014, and one for 2012,[42] which were prepared under approved SECP-adopted accounting standards.[43] The sample includes the financial statements of 29 companies[44] prepared under IFRS as adopted in Pakistan and 10 prepared according to AFRS. An assessment of 11 statements prepared according to IFRS for SMEs[45] applicable in Pakistan was not possible as the first such statements prepared were not available until after June 30, 2016. The sample includes financial statements of manufacturing companies; banks and brokerage houses; and insurance, leasing, energy, and service sector companies.

89. **No significant deviations from the expected reporting framework were noted**. However, the inferences drawn from the review should be considered with a degree of caution given the limited sample size as well as the inherent limitations in attempting to gauge compliance without performing an independent audit. Generally, the disclosures in the reviewed audited financial statements seem to be in compliance with the applicable accounting standards notified by SECP.

90. **Review of the financial statement of public sector companies showed that financial statements did contain comprehensive disclosures; however, audited financial statements are not timely and auditor's report contains several matter with emphasis of opinion.** In some of the ROSC-reviewed financial statements, auditors' opinion raised doubt on the fair presentation of the company's financial statements. It is expected that as the principles of the Code of Corporate Governance for public sector companies are further embedded in practice, the board of directors will be empowered and will thus help to improve corporate compliance and enhance transparency and disclosure.

Perceptions of A&A Practices

91. **In addition to roundtable discussions with stakeholders such as industry associations, an online survey was circulated to gauge the perceptions of the quality of financial statements.** The inferences drawn from the survey served to corroborate some of the earlier observations from other assessments regarding the A&A environment. Typically, financial information reported by listed companies and financial institutions were perceived as high quality and useful for decision-making purposes and in lending decisions. The SOE and SME financial reporting was seen as relatively less credible and useful. The financial statements of unlisted SOEs in particular were considered less likely to provide a fair representation of the company's financial statements. Users faced challenges in accessing the financial statements of unlisted SOEs and smaller companies. The general perception regarding the quality of audit in small-sized entities was not satisfactory. The Bankers place low reliance on the financial statements of the SSEs. Bankers generally deploy their own teams in the field to obtain comfort over the financial statements assertions.

III. STATUS OF POLICY RECOMMENDATIONS OF ROSC A&A 2005

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Recommendation	Implementation status	Actions taken
A&A standards		
Develop simplified accounting and reporting requirements for the SMEs.	Yes	For unlisted small-size companies, separate local AFRS applied since 2007. IASB-issued IFRS for SMEs apply to unlisted medium-size companies since 2015–16.
Rationalize the Companies Ordinance to improve compliance culture, which includes application of IFRS for listed companies, non-listed companies filing requirements, eligibility criteria for the auditors of listed companies, establishing AOB, and granting authority to regulators for improving administrative sanctions.	Yes	SRO 929 of 2015 requires unlisted public interest companies and large-size company to apply IFRS as notified by SECP. Private companies with issued capital less than PKR 7.5 million (US$ 71,599) are exempt from filing audited annual financial statements with the Registrar of Companies. Private companies where issued capital is below PKR 3 million (US$ 28,639), there are no qualification/eligibility criteria for auditors. The Companies Bill 2017 has defined the qualification for auditors. The SECP in consultation with ICAP has established audit oversight through amendments in the SECP Act. The Companies Bill 2017 includes provisions to grant more authority to the regulators for imposing administrativesanctions.
Capacity to implement A&A requirements		
Improve the delivery of the continuing professional education.	Yes	PAOs are active in organizing quality training programs and workshops, as well as a 40-hour director-training program.
Take steps for improving academic and professional curriculum and education.	Yes	ICAP is working with many universities that have included IFRS, ISA, and professional ethics in their syllabus. These universities are engaging experienced chartered accountant to teach IFRS and ISA. IFRS and ISA are included in curricula and taught at universities where ICAP is offering mutual recognition. Teaching should focus on the practical implementation aspects of these standards using illustrations and cases. Ethical standards are embedded in different subjects covered in the syllabus. Ethics as a separate subject is not a recommended approach of IES. ICAP in 2013 revised and updated its education scheme to the latest international standards. The training regulations have also been updated, effective September 1, 2015, in line with the latest IES requirements. Revised RAET and training regulation for training organizations include appropriate monitoring controls. However, implementation has yet to commence. Monitoring of education providers. The performance of RAET, specified degree-awarding institute, and relevant degree-awarding institute is monitored by ICAP using key performance indicators. Education providers are required to prepare a self-evaluation report accompanied by a reasonable assurance report issued under the International Standards on Assurance Engagement by a practicing chartered accounting firm that carries satisfactory QCR rating. Hence, the quality of education delivery is kept under consistent check by ICAP. Previously, ICAP used to appoint its own inspectors.
Issue practical application guidance on IFRS and ISA.	Yes	Usually the implementation guidance issued by IFRS foundation for each IFRS is more than sufficient. In addition, ICAP has issued a disclosure checklist for the guidance of members. ICAP publicly issues technical opinions providing guidance on IFRS and ISA and guides its members and others. An IFRS guide, Gripping IFRS, has been made available to ICAP members. ICAP has arranged for PERN II knowledge base portal, provided by Higher Education Commission of Pakistan, which has a digital library consisting of leading international publications and research material from the top international universities. This material is instantly and remotely accessible to ICAP students and members on the Internet.

Recommendation	Implementation status	Actions taken
Introduce awareness programs for improving the degree of compliance with IFRS requirements.	Yes	ICAP and SECP are designing awareness programs highlighting the significance of compliance with A&A standards. These are aimed at shareholders, directors, and top officials from the corporate sector.
Strengthen capacity of ICMAP to function as a premier professional body of management accountants in the region.	Yes	ICMAP has revised its curricula, which now include comprehensive coverage of IFRS and IAS. Training on IFRS and IAS are also part of CPD. ICAMAP regularly organizes nationwide trainings, seminars, workshops, and conferences. ICMAP has also launched a specialized diploma in IAS/IFRS to equip members with the globally accepted reporting standards. ICMAP has established a cooperative linkage with CIMA to provide its members an accelerated entry gateway to CIMA qualification.
		Monitoring and enforcement
Strengthen the monitoring and enforcement mechanism.	Yes	SECP has strengthened monitoring and enforcement mechanisms and improved its capacity, both for listed and non-listed sectors. SECP has 93 professional accountants (35 in 2005) including 13 chartered accountants. SECP has developed and implemented monitoring manuals. The monitoring process covers review of accounts and other regulatory returns, inspections, investigations, adjudication, and prosecution. All annual and quarterly financial statements of listed companies are reviewed. In-depth analysis of the financials is conducted to ensure compliance with applicable statute and standards. Regulatory actions have been taken against noncompliant ompanies and their auditors. During the last 5 years, SECP has acted against 43 auditors for violations of disclosure requirements under s.260, s.255, and s.259 of the Companies Ordinance. Through these efforts, there has been greater monitoring and significant improvement in reporting standards.
Take steps for improving the capacity of regulators.	Yes	SBP and SECP have taken steps for improving capacity by hiring more professional accountants. SBP has hired 51 professional accountants. SECP trains staff on developments in accounting standards. Various trainings have been conducted for SECP staff in the past 5 years.
Introduce an arrangement for independent oversight of the auditing profession.	Yes	AOB was created in July 2016 by amendments in the SECP Act, 1997. However, effectiveness of the audit oversight needs to be strengthened
Strengthen capacity of ICAP.	Yes	Composition of ICAP Council is such that most members are in the profession; however, ICAP has made a conscious effort to balance the particpation of professional and private representation in QAB. Status of compliance with SMOs has been improved. ICAP has employed 29 chartered accountants (13 in 2005). Further, in the various committees of ICAP, over 100 most renowned chartered accountants are working around the year to achieve the assigned objectives. For the Investigation Committee, there are 3 full-time chartered accountants who conduct monitoring and enforcement. For the Quality Assurance Department, apart from 11 board members, there are 5 (4 in 2005) full-time chartered accountants, including the quality assurance director for dealing with periodic reviews of audit firms.

Recommendation	Implementation status	Actions taken
Audit practice review		
Upgrade the procedure for obtaining license by accountants and auditors engaged in public practice.	Partially	Periodic performance evaluation is covered under the QCR program whereby all QCR-rated firms and their partners' engagements are reviewed in 5-year intervals. Further, based on periodic reviews of engagements of the firms under the quality control framework, sanctions are imposed through withdrawal of QCR ratings that act as a significant catalyst on the practice license-holders to improve their quality control standards. For firms that are not QCR-rated, there is no mechanism to review performance before renewing their practice license. Regarding upgrade of the procedure for obtaining a practice license by ICAP members, a comprehensive framework for practice review is under consideration of the Governing Council. A draft of recommendations of the task force was publicly shared with members, with several consultative sessions with stakeholders held during the last year. Based on feedback, amendments in the framework are being internally debated. This includes reviews of individual partner engagements with implications for renewal of the practice license. The matter is under active consideration of the Council. Compliance with CPD requirements is governed by ICAP Directive 8.01. On noncompliance with CPD requirement at the end of each year and at the end of a 3-year rolling period, members are required to sign a declaration form of noncompliance with a firm commitment to make up the deficit within 180 days. On failure to comply with the requirements of this directive, CPD committee is required to refer the noncompliant cases to the Council for its consideration.
Investigation. Investigate valid complaints against auditors and audit firms and any irregularities identified from reviews of financial statements and audit practices.	Yes	ICAP discharges its role in assigning quality control ratings to professional firms through an exhaustive quality control framework that has been updated with latest enhancements, keeping in line with international developments through independent QAB members; carrying out investigative actions on professional misconduct of its members through a composition of independent personalities and ICAP Governing Council members;, and disseminating guidance on professional matters, including opinions on A&A matters. ICAP has amended its bylaw whereby independent members, who are not members of ICAP Governing Council, have been inducted in the Investigation Committee to bring more transparency in the investigation process. Further, a lawyer attends the meeting of the Investigation Committee to provide legal insight on the matters. To strengthen the investigation and discipline mechanism, ICAP is reviewing a comprehensive set of amendments in the Chartered Accountants Ordinance, 1961. The provision of Section 20 D of the Chartered Accountants Ordinance, 1961, requires the High Court to take a decision after the case is referred by the Governing Council for removal of a name from the register of members for a period exceeding 5 years or permanently, or in case the Council is of the view that the member should be held guilty of professional misconduct specified under the provision of Schedule II of the Chartered Accountants Ordinance, 1961. ICAP has proposed in the revised draft amendments in the Chartered Accountants Ordinance to remove the conditions of referring the case to the High Court to avoid unusual delays in the enforcement mechanism. However, AOB has enacted rigorous principles for review of auditors of public interest companies.
Disciplinary powers. Prescribe guidance to ensure adequate ethical standard and independence of auditors.	Yes	Under the Code of Ethics 2015 by ICAP, there is no restriction in providing audit services and tax advocacy for the same client; and even same partner can provide the audit and tax services to its client. As per revised Code of Ethics 2015, the cooling-off period must be met before a key audit partner or firm managing partner joins PIE audit clients as director, officer, or employee in an important position (i.e., mentioned in key highlights and also paragraphs 290.137 and 290.138 of the Code of Ethics 2015). The revised Code is in accordance with the latest IFAC Code and more stringent requirements under Chartered Accountants Ordinance, 1961. Cooling-off period must be met for partners and senior and other managers of an audit firm before they are allowed to join PIE clients with whom they have done audit work.

IV. KEY FINDINGS AND AREAS FOR CONSIDERATION

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1. The following findings and corresponding recommendations relate to further improvements that can be made to existing and generally successful regulatory initiatives undertaken largely by regulators and professional accounting organizations in the recent years; significant and commendable progress has been made in each area, but further improvements could help to attain good international standards and practices. The following table provides an outline for preparing the country action plan. The table identifies the responsible agencies for implementing the recommendations and the suggested timeframe (short term equals less than a year, medium term is 1-3 years, and long term is 3-5 years).

Findings	Recommendations	Responsible agency	Timeline
A&A standards assessment			
Pakistan is largely compliant with IFRS; however, full compliance cannot be claimed because of a small number of exemptions and deferrals.	A road map should be developed to attain fully compliant status for IFRS to enhance comparability, credibility, and investor's confidence. Internationally recognized standards such as IFRS bring increased credibility, comparability, and transparency at an international level, which foster investor confidence, increasing FDI but decreasing its cost.	SBP, ICAP, and SECP	Medium term
ISA have been fully adopted in Pakistan except for ISA 700R and 701. SECP has approved the audit report format in line with ISA 700R and 701 and submitted to the Cabinet for notification.	As per IFAC compliance program, the status of adoption of ISA is only considered adopted if it has legally adopted or incorporated the 2016 ISA into the national requirements. Therefore, SECP should seek Cabinet approval at the earliest to seek compliance status.	SECP, Cabinet	Short term
Trends of outsourcing services by service organizations are increasing without any required assurance model.	SECP and SBP may consider introducing ISAE 3402 requirement for service organizations. This will improve global and domestic market of the service organizations and provide enhanced user satisfaction.	SECP and SBP	Medium term
Institutional framework			
Financial Reporting Framework			
Increased consultation with local industry to assess the impact of IFRS before adoption.	Efforts are required to enhance consultation with local industry at the time of IFRS adoption to minimize the possibility of waivers/exemptions.	ICAP	Medium term
No formal arrangement exists between ICAP with AGP and CGA to support A&A practices and adoption of IPSAS in federal authorities and other public sector entities.	ICAP should include a range of stakeholders to systematically address the needs of private and public sector stakeholders in the standard-setting process. A standard-setting committee in collaboration with AGP and CGA will support A&A practices and adoption of IPSAS accrual in federal/provincial authorities and other public sector entities.	ICAP, CGA, and AGP	Medium term
As per statute, SECP notifies accounting standards for adoption. ICAP after due consultation recommends accounting standards for adoption to SECP. SECP is statutorily not bound to act on the recommendation of the recognized accounting body.	The documented process of adoption of IFRS may be officially prescribed.	ICAP	Medium term
Anomalies exist between the Companies Ordinance and international good practices and Banking Companies Ordinance with reference to contents of audit report and certain accounting treatments.	The draft Companies Bill, 2017, should be adopted to remove anomalies between the Companies Ordinance and international standards. (Refer to Annex 1A for differences in Companies Ordinance, 1984, and IFRS and suggested amendments.)	SECP, Senate	Short term

Findings	Recommendations	Responsible agency	Timeline
Undue audit compliance burden on small-size entities. MSME requires assistance to understand value added from financial reporting and assurance services.	The Companies Bill 2017 removes the audit requirement from the private companies with paid-up capital of less than PKR 1 million (US$ 9,546). However, this reform will be more effective when filing audited financial statements is also relaxed for the purposes of filing of tax returns. Small-size entities are encouraged to obtain business advice and other structured non-assurance/assurance services (that is, agreed upon procedures, compilations, limited reviews) that provide small business stakeholders with some confidence even where no audit opinion is provided and provide assurance to lenders for access to finance for small-size entities PAOs in collaboration with micro-finance institutions and micro-finance banks, other lending institutions, and industry associations should work to equip MSMEs with international good practice and improve the quality of financial information, which will enhance their growth potential and access to local and international credit markets.	FBR ICAP, ICMAP ICAP and ICMAP, trade associations, and micro-finance institutions	Medium term
Institutional Capacity including Monitoring and Enforcement Arrangements			
Pakistan lacks national accounting curriculum, which resulted in varying levels of exemptions for professional qualification. Further, average passing rate in profession is 25% with 10% increase in students every year. Therefore, the profession has a strong pipeline of partly qualified professional accountants. ICAP has recently introduced the mid-tier certification for partly qualified professional; however, because of lack of national curriculum, Higher Education Commission has not provided equivalence to such certification.	ICAP has introduced three-tiered certification leading to chartered accountancy, namely (a) CAF, (b) Professional Accounting Affiliate, and (c) Certified Accounting and Finance Professional. PAOs may consider creating a national accountancy accreditation body in collaboration with Higher Education Commission. This body may support prescribing a uniform curriculum of accountancy, setting equivalence criteria, allowing exemptions based on specified criteria, and promoting IFRS education across all universities in Pakistan. This will support career path for mid-tier accounting technicians.	HEC, ICAP, and ICMAP	Medium term
Existing arrangements for professionalizing PFM and mid-tier accounting technicians have weak institutional arrangements.	A defined charter is required to put in place a business model for professionalizing PFM and mid-tier accounting technicians in corporate and public sector and to reap full benefit of the existing infrastructure available in the form of PIPFA. PIPFA is strongly encouraged to attain full IFAC membership status. More formal arrangements are required to implement professional skill development program for public sector accountants. It is also suggested to take into account the approach adopted by other countries in the region for the professionalization of public sector accountants (e.g., Sri Lanka). PIPFA should also refer to IFAC guidance on education training and development of accounting technicians http://www.ifac.org/publications-resources/education-training-and-development-accounting-technicians	HEC, ICAP, ICMAP, AGP, and PIPFA	Medium term
Pakistan has the lowest representation of female accountants in the region.	PAOs may develop a Gender Action Plan to facilitate professional opportunities and equal economic participation by female accountants. Encouraging women to seek accountancy qualifications and provision of an enabling environment like day-care centers will allow female accountants to contribute to socioeconomic growth in a more effective way because of their education and knowledge of the environment. Financial assistance in setting up business will also enhance their participation.	ICAP and ICMAP	Medium term

Findings	Recommendations	Responsible agency	Timeline
The audit market is highly concentrated and dominated by audit firms affiliated with the international networks. Small and medium-size practitioners typically provide audit and tax services to SMEs. There is a high cost and resource effort associated with delivering quality audit services to SMEs, which have limited demands for audits other than the statutory requirement.	PAOs consider engaging in a process to educate their members about assurance and non-assurance offerings. Some aspects are less restrictive when dealing with small-size entities regarding non-audit services being provided to audit clients. PAOs may also consider providing series of training/workshops focusing on how small business auditors obtain the knowledge to be trusted business advisers as provided in many IFAC SMP committees, IAASB, and various leading PAOs around the world. http://www.ifac.org/publications-resources/guide-compilation-engagements http://www.ifac.org/publications-resources/guide-review-engagements http://www.ifac.org/publications-resources/guide-using-international-standards-auditing-audits-small-and-medium-sized-en Further, the technical and technological support to small and medium-size practice will assist in streamlining the internal quality control policies and procedures and improve the quality of the services provided.	ICAP and ICMAP	Medium term
The SME Board at the PSX is not fully functional and requires support to facilitate medium-sized companies to access potential investor for raising capital at lower cost. Due to the limited capacity of the SMEs, this potential change agent is still unexplored.	SME sector can be benefit from greater level of engagement with the SME Board at the PSX to access potential investor for raising capital at lower cost. The capacity gap can be bridged with the active involvement of professional accountants with the SME sector. Professional accountants can also serve as financial/transaction advisor in raising capital and other forms of business combination. SECP should also facilitate and work in collaboration with SME Board to increase capital market players.	Professional accounting firms, SME Board at PSX, SECP	Medium term
Up-grade the licensing procedure for non-QCR rated firms.	Adoption of draft practice review framework will provide mechanism to review performance before renewing the practice license for non-QCR rated firms.	ICAP	Medium term
Quality and relevance in CPD program of ICAP and ICMAP needs to improve constantly.	Engagement partners should be encouraged to share their training plans with ICAP, in order that CPD activities can be effectively planned to meet requirements of members in general, and engagement partners in particular. Also, CPD activities should be linked with learning outcomes. Consider use of technology to reduce CPD variable costs and improve access for members. Price CPD based on its value, offer a range of premium and standard CPD, and facilitate low-cost mechanisms where demanded by members. Integrate CPD and quality assurance system that will add perspective of QCR-based findings in the training and will reduce noncompliance. Members responsible for training are also mandated to be CPD compliant. ICAP can enhance the quality of service to its members by maintaining the database of the regulatory findings and aligning CPD activities accordingly.	ICAP, ICMAP and PIPFA	Medium term
ICMAP is not fully compliant with the IFAC SMOs.	ICMAP is encouraged to conduct gap analysis against the requirements of IES to report on compliance with full IES standards and address the gaps. Further, ICMAP should have separate appeal body to bring independence in the investigation process.	ICMAP	Medium term
Untapped potential for finance and accounting outsourcing services	PAOs are encouraged to work jointly to promote finance and accounting outsourcing services in Pakistan in international and local markets and develop policy and code of conduct for shared services.	ICAP, ICMAP	Medium term

IV. KEY FINDINGS AND AREAS FOR CONSIDERATION

Findings	Recommendations	Responsible agency	Timeline
Enhancing independence and quality of audit process. AOB lacks a business and training plan for its board members and senior management team. Further, ICAP also requires adequate staffing to effectively discharge its quality assurance function.	A sustainable structure is required for AOB, which includes affiliation with IFIAR. The capacity of AOB members also needs to be built for efficient and effective performance of their duties. Further, there is a need to enhance capacity of QAB by hiring sector specialist auditors to review the related audit file and increase the number of reviewers while also giving due attention to the revision of their terms of references.	AOB	Short term
The review of financial statements of unlisted public sector companies has recently been added to the mandate of SECP's Corporatization and Compliance Department. The Department also monitors the compliance of code of corporate governance for public sector companies.	SECP has recently undergone internal restructuring where more resources were transferred to Corporatization and Compliance Department for the purposes of review. In order for SECP to adequately discharge its mandate of monitoring A&A practices, continuous enforcement of the compliance of the Code of Corporate Governance is required.	SECP	Medium term
Lack of A&A monitoring arrangements in Economic Reform Unit in Ministry of Finance and Corporate Finance Wings in the Finance Departments.	PAOs and SECP should work with Finance Division and Finance Departments to build their capacity in monitoring A&A practices and improving assessment of fiscal risk for federal and provincial authorities. The reform actions could include setting up monitoring and enforcement teams in Economic Reform Unit and Corporate Finance Wings, hiring of professional accountants, and developing risk-based review methodologies.	ICAP ICMAP, SECP, and Economic Reform Unit in Ministry of Finance and Corporate Finance Wings in Finance Departments	Medium term
Observed reporting practices and perceptions			
A&A practices in unlisted SOEs (federal authorities and public entities) are too weak to apply international standards due to lack of capacity and inactive Board of Directors.	Develop risk-based plan for improving A&A compliance in SOE sector. Accessibility of audited financial statements of SOEs through websites should be encouraged. Plans should be devised for unlisted SOEs for (a) improved financial reporting for better and informed management decision-making and (b) greater transparency and accountability. PAOs in consultation with Ministry of Finance and SECP should include unlisted SOEs, including federal and provincial authorities in the directors' training program and conduct specific training to SOEs on reporting.	ICAP and ICMAP, SECP, and Economic Reform Unit in Ministry of Finance and Corporate Finance Wings in Finance Departments	Medium term
Less reliance of Bankers on the audited financial statements for small-size entities.	Introduction of audit qualification will improve the quality of audit. ICAP and ICMAP may consider providing support to small and medium-size practices for audit of small-size entities through technological support such as audit software and audit training and to encourage small and medium-size practices to apply ISQC 1 that enhances the quality processes at firm and engagement levels. Adoption of draft practice review framework will also enhance the quality of audit in SMPs. Further, ICAP and ICMAP should also hold regular meetings with the Pakistan Banking Council/Financial Institutions to improve quality of audit of SMEs and enhance Bankers reliance on the audited financial statements. This will also facilitate SMEs in access to finance.	ICAP and ICMAP and Pakistan Banking Council	Medium term

NOTES:

ANNEXES

ANNEX 1A:
COMPANIES ORDINANCE, 1984, COMPARED TO IFRS

Requirements of the Companies Ordinance, 1984	IFRS	Comments
Surplus on revaluation of fixed assets (Section 235): *Presentation:* Shown in the balance sheet after capital and reserves. *Accounting treatment:* The surplus on revaluation of fixed assets may be applied by the company in setting off or in diminution of any deficit arising from the revaluation surplus of any other fixed assets of the company.	**Requirements of IAS 16:** *Presentation:* If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognized in other comprehensive income and accumulated in equity under the heading of revaluation surplus. IAS 16 allows the decrease to be recognized in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that asset.	SECP has proposed revision in the draft Companies Bill, 2017, to align it with IAS 16. It is suggested that such specifications may be avoided in the Companies Ordinance to accommodate future development in financial reporting. The difference in the accounting treatment results in reduced equity if treated per local law as compared to international good practice.
Definition of Associates (Section 85): "Associated companies" and "associated undertakings" mean any two or more companies or undertakings, or a company and an undertaking, interconnected with each other in the following manner, namely: (a) If a person who is owner or a partner or director of a company or undertaking, or who, directly or indirectly, holds or controls shares carrying not less than 20% of voting power in such company or undertaking, is also owner or partner or director of another company or undertaking, or directly or indirectly, holds or controls shares carrying not less than 20% of voting power in that company or undertaking; or (b) I f the companies or undertakings are under common management or control or one is the subsidiary of another; or (c) I f the undertaking is a modaraba managed by the company; and a person who is the owner of or a partner or director.	**Requirement of IAS 28:** IAS 28 defines associate as "an entity over which the investor has significant influence."	The Companies Ordinance used the term companies and undertakings. However, nowhere does it define an undertaking. In legal definition the "associate" relationship is basically established through person(s) who is a director/shareholder in said companies and not through direct holding of an investor company. Draft Companies Bill, 2017, has aligned the definition of associate with IAS 28.
Definition of Subsidiary [Section 2(2)]: A company or a body corporate is subsidiary of another if: (a) That other company or body corporate directly or indirectly controls, beneficially owns, or holds more than 50% of its voting securities or otherwise has power to elect and appoint more than 50% of its directors; or (b) The first mentioned company or body corporate is a subsidiary of any company or body corporate, which is that other's subsidiary.	**Requirement of IFRS 10** IFRS 10 defines subsidiary as "an entity that is controlled by another entity."	The criterion of 50% holding shares is not applied in IFRS 10. It is recommended that the definition of "subsidiary" should be aligned with the definition in IFRS 10.

Requirements of the Companies Ordinance, 1984	IFRS	Comments
Definition of Related Party (Section 3): An entity that has the ability to control the company or exercise significant influence over the company in making financial and operating decisions or vice versa and includes the following: (a) Entities, which directly or indirectly through one or more intermediaries, control or are controlled by or are under common control with the reporting company, including holding companies, subsidiaries and fellow subsidiaries; (b) Associates, as defined in the IAS 28, *Accounting for Investments in Associates*; (c) Individuals owning, directly or indirectly, an interest in the voting power of the reporting company that gives them significant influence over the company, and close members of the family of any such individual; (d) Key management personnel (i.e., persons having authority and responsibility for planning, directing, and controlling the activities of the reporting company, including directors and officers of such company and close members of the families of such individuals); (e) Entities in which a substantial interest in the voting power is owned, directly or indirectly, by any person described in clause (c) or (d) or over which such person is able to exercise significant influence, including entities owned by directors or major shareholders of the reporting company and entities that have key management personnel in common with the reporting company; (f) Entities in which one or more of directors or members of the governing board are appointed by the reporting company or vice versa; (g) Where one or more of the directors or members of the governing board of the entity as well as the reporting company are appointed by the same person or persons; (h) Entities whose process of manufacture or business is wholly dependent on the use of know-how, patents, copyrights, trademarks, licenses, franchises, or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula, or process, of which the reporting company is the owner or in respect of which the company has exclusive rights or vice versa; (i) Where more than half of the raw materials and consumables required in the process of manufacture of an entity are supplied by the reporting company, or by persons specified by the company, or vice versa, and the prices and other conditions relating to the supply are influenced by the entity or the company; and (j) Where goods or articles manufactured or processed by an entity are sold or transferred to the reporting company or to persons specified by the company, or vice versa, and the prices and other conditions relating thereto are influenced by the entity or the company. *Explanation*: (a) In considering each possible related party relationship, attention should be directed to the substance of the relationship and not merely to the legal form. (b) For the purposes of this clause (i) "entity" means a partnership firm or a Hindu undivided family or an association of persons or a trust or a company; and (ii) "close members of the family of an individual" means persons who may be expected to influence, or be influenced by, that individual in their dealings with the reporting company.	**Requirement of IAS 24** A related party is a person or entity that is related to the entity that is preparing its financial statements (referred as "reporting entity"). (a) Person or close member of that person's family is related to a reporting entity if that person: (i) has control or joint control over the reporting entity; (ii) has significant influence over the reporting entity; or (iii) is a member of the key management personnel of the reporting entity or of a parent of the reporting entity. (b) An entity is related to a reporting entity if any of the following conditions applies: (i) Entity and reporting entity are members of same group (which means that each parent, subsidiary, and fellow subsidiary is related to the others); (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member); (iii) Both entities are joint ventures of the same third party; (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity; (v) Entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity. (vi) The entity is controlled or jointly controlled by a person identified in (a). (vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).	Proposed amendments in the draft Companies Bill, 2017, greatly align with the requirement of IAS 24 and define related party as; (a) Director or their relative; (b) Key managerial personnel or their relative; (c) Firm, in which a director, manager, or his/her relative is a partner; (d) Private company in which a director or manager is a member or director; (e) Public company in which a director or manager holds along with his relatives, any shares of its paid-up share capital. The requirements of IAS 24 are substantially aligned; however, more consultation is required to fully align the provisions of the Companies Ordinance with the requirements of IAS 24.

ANNEX 1B:
SUMMARY OF FINANCIAL REPORTING AMENDMENTS IN THE COMPANIES BILL, 2017

Provisions of the Companies Bill, 2017	Applicable companies	Proposed amendments
Contents of financial statements (s.225)	All companies	• SECP will have authority to change financial reporting requirements in the schedules that currently require action by the Federal Government.
Quarterly financial statements (s.237)	Listed companies	• Requirements of Companies Ordinance will be aligned with those of the Code of Corporate Governance for Listed Companies.
Directors' report (s.226 and s.227)	All companies	• Directors' report will be amplified to include descriptions of the principal activities and key risks facing the company. • Listed companies will also have to comment on future performance and the company's impact on the environment. • Concept of statement of compliance by directors is proposed.
Penalties for noncompliance (s.220)	All companies	• Increases in penalties for company directors for failure to comply with financial reporting requirements of the Companies Ordinance; the following penalties apply: o *Listed companies* — Imprisonment for up to two years and a fine of PKR 500,000 (US$ 4,773) and not more than PKR 5,000,000 (US$ 47,732) ; o *Unlisted companies* — Imprisonment of up to one year and a fine of up to PKR 100,000 (US$ 954).
Filing requirements for financial statements (s.223) and 233	Companies with paid-up capital greater than PKR 10 million	• Minimum threshold for filing financial statements has been raised to companies with paid-up capital greater than PKR10 million (US$ 95,465). • Listed companies are required to file statements within 30 days of the annual general meeting. • Unlisted companies are required to file financial statements within 15 days of the annual general meeting.
Classification of companies (s.224)	All companies	• Classifications for small-, medium-, and large-size companies as well as public interest companies are defined in the Companies Ordinance.

ANNEX 2:
ICAP ASSESSMENT OF CURRENT STATUS OF OBSERVANCE OF 7 IFAC SMOs

SMO	Degree of responsibility	Current status and challenges
SMO 1, *Quality Assurance*	Direct	*Complied.* ICAP has developed a self-assessment checklist to help firms assess and demonstrate their level of compliance with ISQC and provided mentoring programs to assist firms with implementation of ISQC 1. QAB also issued a revised ISQC 1 Implementation Guide with the dual objective of providing guidance and understanding ISQC 1 requirements as well as augmenting its acceptability and implementation within small and medium-size practices. It has developed a checklist for ISQC 1 compliance to be completed by the reviewer at time of visit of firm under the said standard. QCR program has been revised in July 2015 to make it more in line with the good practice approaches. Further adoption of Draft Practice Review Framework will provide assessment on compliance of ISQC 1. *Challenges.* An inclusion of a new section in the Chartered Accountants Ordinance, 1961, was recommended in 2009; however, no change in the legislation has been made to date. Under this section, a member of ICAP shall produce a document or disclose information to the Governing Council or a committee of the Council that may be required by the Council or such committee in pursuance of an investigation of a complaint against a member or in pursuance of proceedings for the purposes of a Quality Control Review.
SMO 2, *IES for Professional Accountants and other IAESB Guidance*	Direct	*Complied.* ICAP has revised its curriculum and syllabus to be compliant with IES. ICAP is in compliance with IES 2, 3, 4, 5, 6, and 7. IES 1 requires that POA should allow entrance only to those with a reasonable chance of successfully completing the professional accounting education program while not representing excessive barriers to entry. ICAP in addition to the university graduates also allows higher secondary school qualified candidates to take the chartered accountant exam. *Challenges.* ICAP is working on a proposal for changes and improvement in existing rules, regulations, and guidelines to bring them in line with IES 8. The revised IES 8, which is applicable from July 1, 2016, requires specific CPD requirements for engagement partners. Currently, following international practice, ICAP relies on the judgment of engagement partners to decide their specific CPD requirement.
SMO 3, *Standards and Codes by IAASB*	Shared with SECP and SBP	*Complied.*
SMO 4, *IESBA Code of Ethics for Professional Accountants*	Direct	*Complied.* ICAP Code of Ethics has been revised in light of 2014 IESBA Code of Ethics for Professional Accountants. The revised Code of Ethics is applicable from July 1, 2015. At prequalification level, students are tested on the Code of Ethics at both intermediate and final levels.

ANNEX 2:
ICAP ASSESSMENT OF CURRENT STATUS OF OBSERVANCE OF 7 IFAC SMOs

SMO	Degree of responsibility	Current status and challenges
SMO 5, *IPSAS and other IPSASB Guidance*	Indirect	*Partially Complied.* ICAP coordinates through the public sector committee with the Controller General and Auditor General Offices and other important stakeholders to organize meetings, seminars, and roundtables to raise awareness of IPSAS. ICAP has also organized two conferences to disseminate the importance of PFM. The conferences have given insight into the scale and complexities of PFM issues that often need to be addressed in developing countries and emerging economies. The enforcement of Public Sector Companies (Corporate Governance) Rules 2013 is an important step for improving governance and transparency of public sector companies ICAP has also included two public sector accounting standards in its syllabus to create awareness and interest of professional accountants in financial reporting of public sector. *Challenges.* ICAP is exploring ways to integrate with the Auditor General of Pakistan to provide technical support.
SMO 6, *Investigation and Discipline*	Direct	*Complied.* ICAP publishes news about the findings and decisions of the ICAP Governing Council on investigation cases from time to time in its publications. A manual containing decisions of the Council on investigation cases has been developed, which is being referenced during Council meetings and those of the Investigation Committee for guidance and consistency purposes. *Challenges.* To strengthen the Investigation and Discipline mechanism, the ICAP Governing Council is in the process of reviewing a comprehensive set of amendments in the Chartered Accountants Ordinance, 1961. A detailed exercise is being carried out in consultation with legal experts to holistically review the Chartered Accountants Ordinance. After following due process, including public consultation, the draft of amendments finalized by ICAP will be submitted to the Federal Government for approval, which may take time because of the legislative requirements. The revised provisions of the Chartered Accountants Ordinance will be available on the ICAP website and to ICAP members once they are finalized and approved by the relevant authorities after following due process.
SMO 7, *IFRS and other IASB-Issued Pronouncements*	Indirect	*Partially Complied.* As part of ICAP's strategy for full compliance of IFRS by banks and development finance institutions by January 2017, SBP should be persuaded to eliminate deviations in adoption of IAS/IFRS. ICAP should consider adoption of IFRS 9, *Financial Instruments,* by January 1, 2018, after due notification by SECP. *Challenges.* A joint road map for convergence to IFRS needs to be developed among ICAP, SECP, and SBP.

ANNEX 3:

ICMAP ASSESSMENT OF CURRENT STATUS OF OBSERVANCE OF 7 IFAC SMOs

SMO	Degree of responsibility	Current status and challenges
SMO 1, *Quality Assurance*	Direct	*Complied.* ICMAP has established QAB with the objective to enhance quality of services rendered by cost and management accountant firms. Purpose of QAB is to improve quality of financial, cost, and tax audits; to ensure transparency in financial accounts and management reporting; and to comply with relevant rules, regulations, and professional standards. ICMAP has taken the following measures to strength QAB: (a) ICMAP developed program essential for implementation of QCR. Program applies to all cost and management accountant firms holding valid Certificate of Practice. (b) ICMAP has also developed QCR Checklist essential for QCR implementation. (c) ICMAP established Quality Control Department to expedite decisions taken by QAB. The ICMAP Council has also approved hiring the services of reviewers to conduct quality audit of cost and management accounting firms.
SMO 2, *IES for Professional Accountants and other IAESB-issued Pronouncements*	Direct	*Partially Complied.* ICMAP offers Certificate in Accounting and Management, which involves the completion of a two-year course plus six months of supervised practical training. ICMAP also offers direct admission to the three-year CMA course. Students who have completed 14 years of education or attained a Master's degree in any subject are eligible. IFRS were incorporated to enhance local and global acceptability of qualified members. MoUs, Mutual Recognition Agreements, and Mutual Pathway Agreements were signed with other accounting bodies. Every member is required to complete 40 hours in one year or 120 hours every three years with a minimum of 20 hours per year. ICMAP has extended the required length of practical experience to three years to meet the requirements of IES 5 on practical experience requirements. ICMAP is encouraged to conduct a thorough review of its system against IES requirements to report on compliance with the full IES standards.
SMO 3, *Standards and Codes issued by IAASB*	None	ICMAP continues to support ongoing adoption and implementation of IAASB-issued pronouncements through both pre-qualification and post-qualification training provision.
SMO 4, *IESBA Code of Ethics*	Direct	*Complied.* ICMAP has adopted 2015 IESBA code of Ethics with modifications.
SMO 5, *IPSAS and other IPSAB-issued Pronouncements*	None	*Complied.* At ICMAP level, initiatives are being taken to promote the importance of IPSAS. For this purpose, ICMAP organized a conference on public sector accounting. The main objective of this conference was to improve the quality of public sector accounting, particularly in relation to disclosure, transparency, and corporate governance.
SMO 6, *Investigation and Discipline*	Direct	*Partially complied.* The ICMAP National Council has been empowered under Section 34 of the Cost and Management Accountants Act, 1966, to frame rules of professional and other conducts and to exercise disciplinary powers in relation thereto. In 2016, ICMAP completed a review of its investigation and discipline system and has incorporated many of requirements of SMO 6. It has noted that an appeals body does not exist that is separate from its disciplinary committee. ICMAP reports to IFAC that it has plans to address the identified gaps.
SMO 7, IFRS and other IASB-issued Pronouncements	None	ICMAP has launched a six-month diploma in IAS/IFRS to equip professionals with globally accepted reporting standards to enable them to avail such employment opportunities in the global and local corporate markets. As part of the strategy, ICMAP is fully cooperating with ICAP to promote ongoing convergence with IASB pronouncements.

ANNEX 4:
ICAP ASSESSMENT OF THE COMPLIANCE WITH IAESB STANDARDS

International Education Standards	Comments
IES 1	The minimum entry requirement equivalent to that for a university degree program, (i.e. higher secondary school certificate or A-Level qualification) is considered appropriate in view ICAP's own basic accounting education program that runs before an aspirant of chartered accountancy takes up Initial Professional Development. Further details on ICAP's streams are available at; http://www.icap.org.pk/become-ca/entry-routes/full-time-scheme/ http://www.icap.org.pk/become-ca/entry-routes/trainee-scheme/
IES 2	The competence areas of professional accounting education programs detailed in IES2 (financial accounting and reporting; management accounting and reporting; finance and financial management; taxation; audit and assurance; governance, risk management and internal control; business laws and regulations; information technology; business and organizational environment; economics, and business strategy and management) are incorporated throughout the curriculum of the chartered accountant program. For details visit the link: http://www.icap.org.pk/students/education-scheme-2013/
IES 3	The key professional skills highlighted in IES 3 (intellectual, interpersonal and communication, personal, and organizational skills that a professional accountant integrates with technical competence and professional values, ethics, and attitudes to demonstrate professional competence) are assessed by ICAP through various methods such as written examinations, practical training under supervision of a ICAP member and training through Registered Accounting Education Tutors.
IES 4	ICAP's education and training system ensures development of professional values and adherence to the code of ethics issued by ICAP.
IES 5	ICAP has mandatory practical training periods varying from 3, 3.5 to 4 years based on the qualification or years of education at commencement of training. The training is regulated under the Bylaws and Training Regulations issued by ICAP. ICAP provides a software-based training log, which is maintained by the students and monitored by ICAP member responsible for training. ICAP can review the progress on test basis.
IES 6	ICAP has revised its education scheme. The old modular system has been replaced with the new scheme of four levels that translates the role of the aspirants in terms of their expected achievement at the workplace.
IES 7	Details of CPD requirements for ICAP in compliance with IES 7 are provided in para 56
IES 8	IES requirements with regard to the professional competence that professional accountants performing the role of an engagement partner responsible for audit of financial statements is fulfilled through education program that contains relevant assessments and compulsory training in practice for at least two years. Maintenance of said competencies is currently the responsibility of the professional accountants through CPD activities relevant to the role of an engagement partner to audit professionals. ICAP is deliberating on prescribing specific and structured CPD requirements for all members in practice.

ANNEX 5:

PIPFA ASSESSMENT OF ASSESSMENT OF CURRENT STATUS OF OBSERVANCE OF 7 IFAC SMOs

SMO	Degree of responsibility	Current status and challenges
SMO 1, *Quality Assurance*	None	PIPFA evaluates ways to work with ICAP to support quality assurance reviews of auditors in Pakistan. To further develop its members' awareness of ethics and issues related to accounting and auditing, PIPFA conducts continuing professional development on ICAP's QCR framework, which incorporates ISQC 1. Other activities by PIPFA to keep members informed on quality control include the Technical Committee that updates members on developments by IFAC in regards to SMO 1, through technical update emails, the main website, and the PIPFA journal, in order to improve their quality of work.
SMO 2, *IES for Professional Accountants and other IAESB-issued Pronouncements*	Direct	*Partially Complied.* With direct responsibility to set initial and continuing professional development for its members, PIPFA introduced a new education scheme in June 2015, which incorporates IES requirements. The new education scheme addresses gaps that were previously identified such as incorporating ethics into the syllabus, increasing CPD hours, and increasing practical experience requirements. To support the learning of members, PIPFA has established a CPD framework, which includes running seminars on various topics related to public finance such as performance management, audit risk, and corporate governance. PIPFA plans to review its system against the revised IES, as it is introducing a new syllabus for its candidates. PIPFA is encouraged to participate in the international standard-setting process by reviewing and responding to exposure drafts issued by the IAESB.
SMO 3, *Standards and Codes issued by IAASB*	None	PIPFA has an ongoing process to monitor pronouncements by IAASB to keep members and students informed on relevant updates to the standards. In addition, PIPFA has a Technical Committee in place to conduct research on pronouncements by IAASB to incorporate in its syllabus and CPD content. PIPFA also participates in the international standard-setting process by reviewing and responding to IAASB exposure drafts.
SMO 4, *IESBA Code of Ethics*	Direct	*Complied.* With direct responsibility to set ethical requirements for its members, PIPFA has adopted the 2014 IESBA Code of Ethics and has a process in place to monitor pronouncements by IESBA to include updates in its initial and CPD content. Ethics is taught as a separate subject in the new syllabus for students. PIPFA also offers CPD courses on ethics, in which examples of case studies of conflicts and challenges are presented.
SMO 5, *IPSAS and other IPSASB-issued Pronouncements*	None	PIPFA is active in promoting full adoption of IPSAS by the Auditor General's Office, including having discussions on strategies to move to full adoption of IPSAS in Pakistan. Other activities with the Auditor General include discussions on disclosures in financial statements of public sector entities and working with the Auditor General to monitor public sector corporations in the country. PIPFA provides training on IPSAS to employees of the Auditor General, Pakistan Military Accounts Department, Local Fund Audit, Treasury Departments of the Punjab Government, and Pakistan Railways Accounts Department. To keep members up to date on IPSAS, PIPFA monitors new and amended IPSASB pronouncements and disseminates them to members via journals and CPD programs. In addition, PIPFA participates in the international standard-setting process by inviting members to review and respond to exposure drafts issued by IPSASB.
SMO 6, *Investigation and Discipline*	Direct	*Partially complied.* The PIPFA has investigation and discipline process in place for its members, and its disciplinary committee reports that it began reviewing this system in 2015, but a timeline has not been established as to when this review will conclude.
SMO 7, *IFRS and other IASB-issued pronouncements*	None	PIPFA also updates its educational syllabus to take into account new and amended standards issued by IASB. PIPFA also plans to consider introduction of short-term online and offline courses on IFRS for members.

ANNEX 6:
SIGNIFICANT FACTORS FOR EFFICIENT FUNCTIONING OF AUDIT OVERSIGHT

Key Areas	Status	Comments/Considerations
Organization's Location	Independent of regulators and Government	In line with IFIAR principles
Governance Structure	Majority of governing body is a non-practitioner. Comprised of lawyers, former audit professionals, and board members of PSX and SBP and retired government officials.	In line with IFIAR principles
Organizational Structure	Chief executive officer not hired; lacks organizational structure and basic infrastructure.	Develop business plan and training plan for Board members and management. Financial assistance is required to fund start-up and operational cost for initial years. To affiliate with IFIAR.
Sustainable Funding Model	Framework allows: • Government contribution; no commitment yet. • Raising revenues from registration of audit firms; low possibility as audit fee structure in Pakistan is the lowest in the region. • Fee/charges to PIEs; AOB does not intend to charge a fee to PIEs at the outset, consider charging a fee once it starts rendering its mandated services to these organizations. • Voluntary contributions from key stakeholders (ICAP, SECP, and SBP); SECP committed PKR 30 million (US$ 286,396). 50 percent is paid. • Grants and borrowings; none received so far.	Financial and technical assistance is required for sustainable funding model.
Regulators' Accounting and Auditing Capacity	Quality Assurance Department housed at ICAP and overseen by AOB lacks sector specialists and appropriate audit tools to review; Impact of QAB over the years is not encouraging. AOB currently required to hire reviewers	Hire reviewers and develop risk-based, sector-specific audit plans and methodologies. Equip with proper audit tools.

NOTES:

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PAKISTAN

REPORT ON THE OBSERVANCE OF
STANDARDS AND CODES,
ACCOUNTING AND AUDITING

JANUARY 2017

WORLD BANK GROUP