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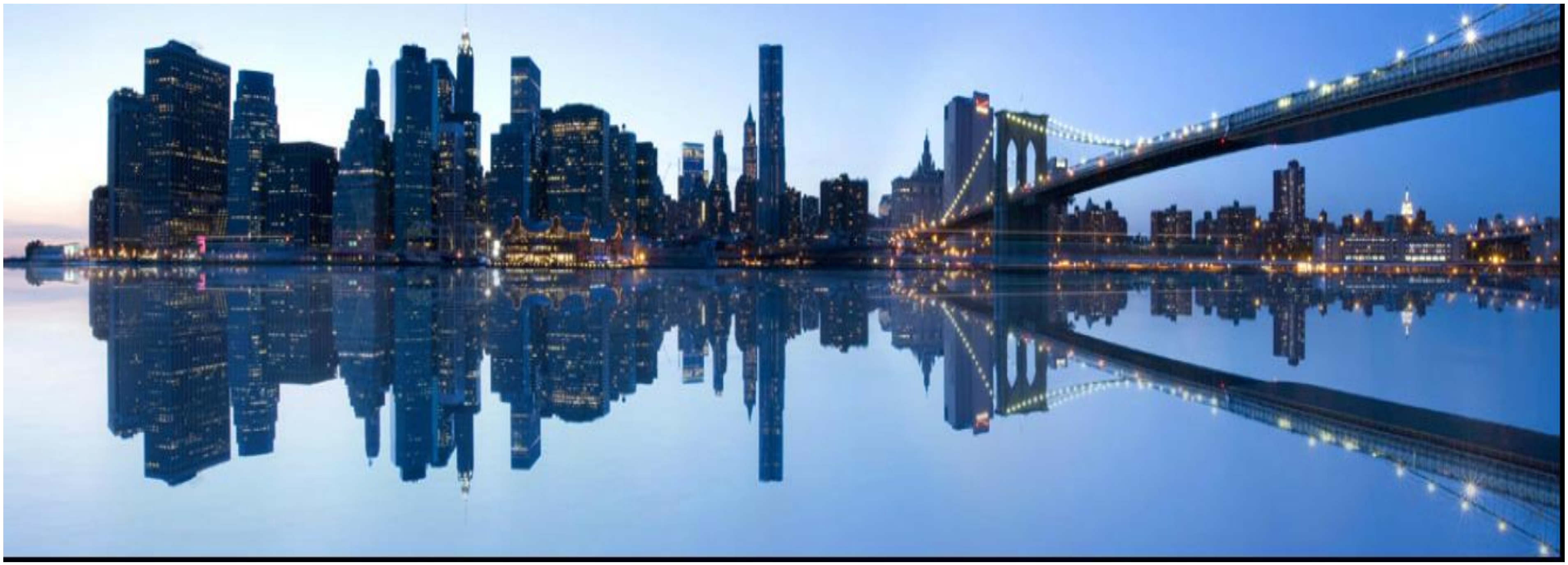

Financial Reporting under the Companies Act 2017

Your questions answered

Contents

Introduction

Pakistan has a differential financial reporting regime under which different financial reporting requirements are set according to the type of company, principally based on the level of public interest in the company.

The new financial reporting requirements of the Companies Act 2017 (the Companies Act) are now applicable, having direct impact on the companies preparing statutory financial statements for the periods ended after December 31, 2017.

In general, the new financial reporting frameworks, revised thresholds for classification of companies and new disclosure requirements will necessitate the reassessment of company's financial reporting, either by choice or out of necessity.

This publication "***Financial Reporting under the Companies Act 2017 - Your Questions Answered***" prepared by the Technical Services Department on the advice of Accounting Standards Board, addresses some of the common questions originating from the applicability of new financial reporting requirements of the Companies Act.

The objectives of this publication are to present an overview of the new financial reporting regime, provide clarifications on the financial reporting matters emanating from the application of the Companies Act and support members and other stakeholders in the preparation of financial statements in accordance with the relevant statutory financial reporting framework.

The publication covers different areas and aspects of financial reporting, primarily relating to the financial accounting and reporting changes brought in by the Companies Act and affecting different classes of companies.

The document is in a format that makes it easy to understand the new financial reporting requirements and identify the answers to common questions that a preparer of financial statements may have.

The document contains following sections:

What has changed - This section provides a snapshot of the different financial reporting frameworks and their applicability to different classes of companies. Further, this section also explains the significant changes brought in by the Companies Act in the financial reporting frameworks and categories of companies, in comparison with the repealed Companies Ordinance 1984.

Your questions answered - The questions and answers framed in this section address the accounting implications for companies that are preparing annual and quarterly financial statements that end on a date after December 31, 2017, and offer clarifications to the key changes and related accounting and reporting concepts.

IFRS update as at June 30, 2018 - The document also contains a list of all of the new IFRS (new standards, interpretations and amendments to the standards) distinguishing between those that are effective for the annual periods ended June 30, 2018 and subsequent periods.

Exemptions from the application of IFRS - The documents also contains the lists of the IFRS not yet adopted in Pakistan and the exemptions from the adopted IFRS, allowed by SECP or SBP to specific sectors / companies.

We hope that this publication would serve as a simple yet useful guide to assist members and other stakeholders formulate and execute their financial reporting plans achieve a smooth transition to the new financial reporting regime.

Farrukh Rehman
Chairman Accounting Standards Board

Sohail Malik
Director Technical Services

What has changed?

The underlying principle of the Pakistan statutory financial reporting system is to provide information to external users who have a need for company's financial statements but are unable to demand them. Before considering the technical accounting and reporting matters emanating from the applicability of Companies Act, a brief background to the financial accounting and reporting frameworks available to different classes of companies under the Companies Act is provided in this section.

What is the financial accounting and reporting framework in Pakistan?

The Companies Act outlines the financial reporting requirements for companies. Under the Companies Act the financial accounting and reporting framework is termed as "Accounting and Reporting Standards as applicable in Pakistan". Previously, the repealed Companies Ordinance 1984 termed the framework as "Approved Accounting Standards as applicable in Pakistan".

The Companies Act, consistent with the repealed Companies Ordinance 1984, sets out differential and proportionate financial accounting and reporting frameworks. Under this approach different classes of companies (based on the legal status, business activities, size etc.) are required to prepare statutory financial statements in accordance with different sets of financial reporting standards. This differential approach is being followed to meet the differing information needs of each class of company and users of its financial statements.

In general, the accounting and reporting standards as applicable in Pakistan comprise of the following, however, their applicability depends on the classification and nature of the activities of the companies:

Financial reporting standards	- International Financial Reporting Standards (IFRS) - International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs) - Revised Accounting and Reporting Standard for Small-sized Entities (AFRS for SSEs)
Provisions and requirements of the Companies Act	- Fourth schedule of the Companies Act - Fifth schedule of the Companies Act Other specific requirements of the Companies Act and related laws, regulations and rules
Specialized financial reporting standards	- Accounting Standard for Not for Profit Organizations (NPOs) - Islamic Financial Accounting Standards (IFAS)
Specialized financial reporting requirements	- Required under the law and related regulations applicable to specialized entities such as banks, DFIs, insurance companies and mordabas

A comparison of the financial reporting frameworks under the Companies Act 2017 and repealed Companies Ordinance 1984 is as under:

Companies Act 2017

- IFRS issued by IASB
- IFRS issued by the IASB and notified by SECP
- IFRS for SMEs issued by the IASB and notified by SECP
- AFRS for SSEs issued by ICAP and notified by SECP
- Accounting Standard for NPOs issued by ICAP and notified by SECP
- IFAS issued by ICAP and notified by SECP

Fourth schedule of Companies Act

Fifth schedule of Companies Act

Other provisions of laws and regulations applicable to specialized entities (such as banks, DFIs, insurance companies, microfinance banks)

Repealed Companies Ordinance 1984

- IFRS issued by the IASB and notified by SECP
- IFRS for SMEs issued by the IASB and notified by SECP
- AFRS for SSEs issued by ICAP and notified by SECP
- Accounting Standard for NPOs issued by ICAP and notified by SECP
- IFAS issued by ICAP and notified by SECP

Fourth schedule of Repealed Companies Ordinance 1984

Fifth schedule of Repealed Companies Ordinance 1984

Other provisions of laws and regulations applicable to specialized entities (such as banks, DFIs, insurance companies, microfinance banks)

The fourth and fifth schedules of the Companies Act set out disclosure requirements for the annual statutory financial statements. Under the Companies Act these disclosures have also been revised compared to the repealed Companies Ordinance 1984, resulting in: (a) elimination of the duplicative disclosures with the IFRS; and (b) incorporation of new disclosures.

Subsequent, to the enactment of Companies Act in May 2017, the third, fourth and fifth schedules to the Companies Act have been revised by SECP through S.R.O 1169 (1) / 2017 dated November 07, 2017. Accordingly, companies shall consider and comply with the revised schedules for the financial reporting purposes. The Institute has developed disclosure checklists of fourth and fifth schedules to assist in understanding and documenting the disclosure requirements during the preparation of financial statements. These disclosure checklists can be accessed at http://www.icap.net.pk/disclosure-checklists

With regard to the specialized companies (banks, insurance, DFIs) the regulatory laws and related rules and regulations applicable to these specialized companies specify the financial accounting, reporting and disclosure requirements. For example:

- The Insurance Ordinance 2000 establishes financial reporting requirements for insurance companies.
- The Banking Companies Ordinance 1962 outlines financial reporting requirements for banks and similar financial institutions.

What are the classes of companies for statutory financial reporting?

The Companies Act (through the newly inserted section 224 and related third schedule) classifies companies in various categorizes.

The third schedule outlines the qualitative (legal status, nature of business) and quantitative criterias (paid-up capital, revenue, number of employees) for the classification and sub-categorization of companies. Further, the third schedule also establishes applicable financial reporting framework for each category of the company.

The four classes and underlying sub-categories of companies, in accordance with the third schedule, are tabulated below:

Sub-categories of companies	Classes of companies			
	Public interest company	Large-sized company	Medium-sized company	Small-sized company
Listed company	✓			
Public sector company	✓			
Public utility company	✓			
Company holding assets in fiduciary capacity	✓			
Company having such number of members holding ordinary shares as may be notified	✓			
Company holding assets exceeding such value as may be notified	✓			
Public non-listed company		✓	✓	
Private company		✓	✓	✓
Foreign company		✓	✓	
Company licenced under sections 42 or 45 of the Companies Act		✓	✓	

What are the basis to determine the class and category of a company?

As mentioned above, the third schedule to the Companies Act prescribes the criteria / thresholds for the determination of class and sub-category of a company. The introduction of new sub-categories and revision of thresholds in the third schedule to the Companies Act, compared to the repealed Companies Ordinance 1984, can directly affect different companies, especially the foreign and small-sized companies. Resultantly, the financial reporting framework of companies may change under the Companies Act.

The following tables summarizes the class and category-wise criteria / thresholds of the third schedule:

Listed company
A company incorporated in Pakistan, having its securities (debt or shares) listed on the Pakistan Stock Exchange.

Large-sized company

Sub-category of company	Criteria / Threshold					Comments
	Paid-up capital		Turnover / Revenue		Number of employees	
Non-listed Public company **and** **Non-listed Private company**	Rs. 200 million or more	Or	Rs. 1 billion or more	Or	750 or more	Previously, the repealed Companies Ordinance 1984 prescribed two criterias for the determination of a large-sized company (i) paid-up capital (Rs. 200 million or more) or (ii) the turnover (Rs. 1 billion or more). The Companies Act has added criteria of number of employees.
Foreign company	_		Rs. 1 billion or more		_	The Companies Act now categorizes the foreign companies in the large-sized and medium-sized classes. This classification of foreign companies sets out differential financial reporting frameworks under the Companies Act. Previously, the repealed Companies Ordinance 1984 required all foreign companies to follow the financial reporting framework applicable to the large-sized companies, irrespective of their size.
Company licenced / registered under sections 42 or 45 of the Companies Act	_		Annual gross revenue (grant, income, subsidies, donations and other income) of Rs. 200 million or more		_	No change in the criteria, compared to the repealed Companies Ordinance 1984.

Medium-sized company

Sub-category of company	Criteria / Threshold: Paid-up capital		Criteria / Threshold: Turnover		Criteria / Threshold: Number of employees	Comments
Public non-listed company	Less than Rs. 200 million	Or	Less than Rs. 1 billion	Or	Less than 750	The Companies Act has introduced specific criteria for the determination of medium-sized companies. Previously, the repealed Companies Ordinance 1984 did not contain a specific criteria / threshold for the medium-sized companies; as these companies were classified, based on exception from the large-sized and small-sized companies.
Private company	More than Rs. 10 million and less than Rs. 200 million	Or	More than Rs. 100 million and less than Rs. 1 billion	Or	More than 250 and less than 750	Please see above comments
Foreign company	–		Less than Rs. 1 billion		–	The Companies Act now categorizes the foreign companies in large-sized and medium-sized classes. A foreign company having turnover less than Rs. 1 billion is classified as a medium-sized company.
Company licenced under sections 42 or 45 of the Companies Act	–		Annual gross revenue (grant, income, subsidies, donations and other income) less than Rs. 200 million		–	No change in the criteria, compared to the repealed Companies Ordinance 1984.

Small-sized company

Sub-category of company	Criteria / Threshold: Paid-up capital		Criteria / Threshold: Turnover		Criteria / Threshold: Number of employees	Comments
Private company	Up to Rs. 10 million	AND	Not exceeding Rs. 100 million	AND	Not more than 250	The Companies Act brought in two significant changes: - Addition of criteria of number of employees; and - Revision of the threshold of paid-up capital, as previously the repealed Companies Ordinance 1984 set the paid-up capital threshold up to Rs. 25 million.

Which accounting and reporting standards are applicable to a company?

Under the differential financial reporting regime of the Companies Act, the accounting and reporting standards applicable to the various categorize of companies are as under:

IFRS notfied by SECP + Fourth schedule	IFRS notfied by SECP + Fifth schdedule	IFRS notfied by SECP + Fifth schdedule + Accounting Stanadrd for NPOs	IFRS for SMEs + Fifth schdedule	IFRS for SMEs + Fifth schdedule + Accounting Stanadrd for NPOs	AFRS for SSEs + Fifth schdedule
Listed company	Public sector company	Large-sized Comapny licensed / registered under section42 or section 45	Medium-sized Public non-listed Company	Medium-sized Comapny licensed / registered under section42 or section 45	Small-sized Private comapny
	Public utility company		Medium-sized Private company		
	Company holding assets in fiducary capacty		Medium-sized Foreign comapny		
	Companies having specified number of shares or assets				
	Large-sized non-listed Public company				
	Large-sized Private company				
	Large-sized Foreign company				

IFRS issued by IASB	In accordance with the newly inserted provision of section 225 of the Companies Act, a company can now elect to prepare statutory financial statements in accordance with the IFRS issued by IASB. In such a case, company would be required to follow all the requirements of the IFRS and accordingly give an unreserved statement of compliance with IFRS in the financial statements. *Further, explanation on this topic is provided is the next section (Question 6 and 7).*

Your questions answered

1. What are the statutory annual financial reporting obligations?

The annual statutory financial reporting obligations relating to the preparation of annual financial statements are spread across various sections of the Companies Act. The following table summarizes the key statutory financial reporting requirements by company category, focusing on which companies have to prepare financial statements, whether an audit is required and whether the financial statements have to be filed with SECP and other stakeholders. Additionally, the necessary timelines for the preparation and submission of the financial statements are also mentioned.

Company and financial statements type	Preparation of financial statements	Audit of financial statements	Approval and authentication of financial statements	Notice of AGM and filing /submission	Adoption of financial statements in AGM	Filing / submission of financial statements
First financial statements (since the incorporation of the company)						
All companies	✓ All companies are required to prepare first statutory financial statements *Section 223 (1) & Section 225 (1)*	✓ All companies are required to get the first statutory financial statements audited, except, a private company having paid-up capital not exceeding Rs. 1 million and such a company is not a subsidiary of a public company *Section 223 (5)*	✓ Please see below requirements for different companies	✓ Twenty one days before the AGM date *Section 132 (3)* For the documents (related to the financial statements) to be sent along-with the notice please see below requirements for different companies	✓ Within sixteen months after the date of incorporation of company *Section 223 (3)*	✓ Please see below requirements for different companies

Company and financial statements type	Preparation of financial statements	Audit of financial statements	Approval and authentication of financial statements	Notice of AGM and filing /submission	Adoption of financial statements in AGM	Filing / submission of financial statements
Annual statutory financial statements						
Listed company	✓ Obligated to prepare annual statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule *Section 223 (1) &* *Section 225 (1)* However, specialized companies (such as banks, DFIs, insurance companies) shall consider the financial reporting framework provided in their relevant regulatory law *Section 225 (1)*	✓ Required to get the annual statutory financial statements audited *Section 223 (5)*	✓ Approval of the board of directors Authentication by chief executive officer, atleast one director and chief financial officer *Section 232 (1)* ** Specialized companies (such as banks, DFIs, insurance companies) shall consider the authentication requirements provided in their relevant regulatory law*	✓ Twenty one days before the AGM date *Section 132 (3)* Documents to be sent along-with the notice to members: - Audited financial statements - Auditor's report - Director's report - Chairman's review report *Section 223 (6)* Further, below filing and submissions: - By post: Three copies to Registrar, SECP and stock exchange - Electronically: One copy to SECP - Post on the company's website *Section 223 (7)* - E-service: One copy to registrar	✓ Within one hundred and twenty days following the close of company's financial year *Section 223 (2)*	✓ To the registrar, within thirty days from the date of AGM *Section 233(1)*
Foreign company	✓ The foreign company shall prepare the financial statements of its Pakistani business operations in accordance with the provisions applicable on the public company registered under the Act. *Regulation 13 of Foreign Companies Regulations, 2017*	✓ The financial statements of foreign company shall be audited in accordance with the provisions applicable on the public company registered under the Companies Act. *Regulation 13 of Foreign Companies Regulations, 2017*	✓	-	-	✓ With the registrar at a date which is earlier of: Forty five days of filing of the financial statements to the public authority of the country of origin; or One hundred and eighty days of the foreign company's balance sheet date. *Section 437 (2)* *Regulation 13 of Foreign Companies Regulations, 2017*

Company and financial statements type	Preparation of financial statements	Audit of financial statements	Approval and authentication of financial statements	Notice of AGM and filing /submission	Adoption of financial statements in AGM	Filing / submission of financial statements
- **Public sector company** - **Public utility company** - **Company holding assets in fiduciary capacity** - **Public un-listed company** - **Company licenced under sections 42 or 45 of Companies Act** - **Private company (other than below)**	✓ Obligated to prepare annual statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule *Section 223 (1) &* *Section 225 (1)* However, specialized companies (such as banks, DFIs, insurance companies) shall consider the financial reporting framework provided in their relevant regulatory law *Section 225 (1)*	✓ Required to get the annual statutory financial statements audited *Section 223 (5)*	✓ - Approval of the board of directors - Authentication by chief executive officer and atleast one director *Section 232 (1)*	✓ Twenty one days before the AGM date *Section 132 (3)* Documents to be sent along-with the notice: - Audited financial statements - Auditor's report - Director's report *Section 223 (6)*	✓ Within one hundred and twenty days following the close of company's financial year *Section 223 (2)*	✓ With the Registrar, within fifteen days from the date of AGM *Section 233(1)*
Private company (With paid-up capital exceeding Rs. 1 million but not exceeding Rs. 10 million)	✓ Obligated to prepare annual statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule *Section 223 (1)* *Section 225 (1)*	✓ Required to get the annual statutory financial statements audited *Section 223 (5)*	✓ - Approval of the board of directors - Authentication by chief executive officer, and atleast one director *Section 232 (1)*	✓ Twenty one days before the AGM date *Section 132 (3)*	✓ one hundred and twenty days following the close of company's financial year *Section 223 (2)*	✓ Filing of financial statements not required *Section 233(3)*

Company and financial statements type	Preparation of financial statements	Audit of financial statements	Approval and authentication of financial statements	Notice of AGM and filing /submission	Adoption of financial statements in AGM	Filing / submission of financial statements
Private company Having a paid-up capital not exceeding Rs. 1 million	✓ Obligated to prepare annual statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule *Section 223 (1)* *Section 225 (1)*	– Exempted from the mandatory statutory audit *Section 223 (5)*	✓ - Approval of the board of directors - Authentication by chief executive officer, and atleast one director - Affidavit of chief executive or a director of the company, affirming that the financial statements have been approved by the board of directors *Section 232 (1)*	✓ Twenty one days before the AGM date *Section 132 (3)*	✓ one hundred and twenty days following the close of company's financial year *Section 223 (2)*	✓ With the Registrar within thirty days from the date of AGM *Section 234 (1)*
Single member company (Separately, explained from the private companies, owing, to the differing financial reporting obligations)	✓ Obligated to prepare annual statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule *Section 223 (1) &* *Section 225 (1)*	✓ Audit mandatorily required if paid-up capital exceeds Rs. 1 million *Section 223 (9)*	✓ Signed by the director *Section 232 (2)*	– The requirement of holding AGM for adoption of financial statements is not applicable *Section 223 (9)*	– The requirement of presenting financial statements in AGM for their adoption is not applicable *Section 223 (9)*	If paid up capital: - *Exceeds Rs. 10 million*: Audited financial statements to be filed with Registrar - *Exceeds Rs. 1 million but does not exceed Rs. 10 million:* No requirement to file the financial statements with the registrar - *Does not exceed Rs. 1 million:* Authenticated financial statements (i.e. signed by director) to be filed.

2. Is there a statement of compliance for the financial statements prepared in accordance with the Companies Act?

The Companies Act through section 225 requires that the financial statements shall be prepared in accordance with the accounting and reporting standards specified in the third schedule.

The financial reporting standards (i.e. IFRS, IFRS for SMEs and AFRS for SSEs) which are part of the accounting and reporting standards, set out the requirement to disclose a statement of compliance in the financial statements.

Pursuant, to the enactment of the Companies Act and application of its financial reporting provisions, the statement of compliance shall reflect these legislative changes. Further, the statement of compliance shall outline the accounting and reporting standards as applicable in Pakistan, i.e. the financial reporting framework used by the company to prepare the statutory financial statements.

The Institute, vide Circular 4/2018 (dated March 26, 2018) has issued the statements of compliance for the financial statements prepared under the Companies Act, 2017.

The companies shall include the relevant statement of compliance in their statutory financial statements (annual and interim), prepared for the period/year ended after December 31, 2017 (e.g. period/year ended March 31, 2017, period/year ending June 30, 2018, December 31, 2018).

The statement of compliance can be accessed at:
http://www.icap.net.pk/wp-content/uploads/2018/04/Circular-No.4-of-2018-Statement-of-Compliance-for-the-Financial-Statements-prepared-under-the-Companies-Act2017.pdf

3. How a company identifies the applicable financial reporting framework?

The Companies Act under the third schedule has amended and added new-sub-categories of companies. In this context, following are the significant changes:

- Foreign companies have been sub-categorized in large-sized and medium-sized companies;
- The criteria and threshold of number of employees has been introduced in the large-sized public-unlisted companies; and
- The threshold for paid-up capital of small-sized company has been reduced from Rs. 25 million to Rs. 10 million.

The change in thresholds and sub-categorization criteria under the third schedule indicates that the financial reporting framework of some companies may change from the previously followed framework. Companies shall consider the criteria/s introduced under the Companies Act to determine their appropriate class and category and prepare financial statements in accordance with the applicable financial reporting framework.

The rule set by the third schedule for the determination of classification of a company for the financial reporting purposes is as under:

a. The classification shall be based on the previous year's audited financial statements; and
b. The classification will change when the company does not fall under the previous criteria for two consecutive years.

Generally, a company qualifies under a sub-category if it fulfils the conditions in that year. In any subsequent year a company must fulfil the criteria/conditions in that year and the year before. Resultantly, a company, which qualified under a classification in one year, and no longer meets the criteria in the next year, will still prepare the financial statements in that next year, in accordance with the prior year financial reporting framework.

Further, for the change in classification, the company shall evaluate criteria of two consecutive years (i.e. current year and immediately prior year).

However, companies affected by the introduction of the new criteria and thresholds of the Companies Act shall follow the new financial reporting framework without considering the above general principle of change in classification.

The following examples illustrate the above explanation:

Example 1:

	20x8	20x7	20x6
Revenue	Rs. 1,200 million	Rs. 850 million	Rs. 750 million

MAM is a private limited company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7 it was classified as a 'medium-sized' company, based on its 20x6 revenue of Rs. 750 million.

In the year 20x8, the company will continue to be sub-categorized as a 'medium-sized' company, as classification of a company is to be based on the previous years audited financial statements (In prior year i.e. 20x7, the revenue amounted to Rs. 850 million). Accordingly, company shall prepare financial statements of 20x8 in accordance with the financial reporting framework medium-sized applicable to medium-sized companies.

Example 2:

	20x8	20x7	20x6
Revenue	Rs. 1,200 million	Rs. 1,100 million	Rs. 750 million

MAM is a private limited company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7 it was classified as a 'medium-sized' company, based on its 20x6 revenue of Rs. 750 million.

In the year 20x8, the company shall be classified as a 'large-sized company', as it does not fall under the criteria of a medium-sized company for two consecutive years i.e. 20x8 and 20x7 (In both years revenue exceeds Rs. 1 billion threshold).

Example 3:

	20x8	20x7	20x6
Revenue of company	Rs. 900 million	Rs. 1,200 million	Rs. 1,400 million

MAM is a private limited company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7 it was classified as a 'large-sized' company, based on its 20x6 revenue of Rs. 1,400 million.

In the year 20x8, though the revenue of company is less than Rs. 1 billion, however, it shall continue to be classified as a 'large-sized company'. This is as per third schedule requirement that the classification is to be based on the previous year audited financial statements.

Example 4:

	20x8	20x7	20x6
Revenue of company	Rs. 900 million	Rs. 800 million	Rs. 800 million

AMY is a foreign company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7 it prepared financial statements in accordance with the IFRS notified by SECP and repealed Companies Ordinance 1984 (As required under S.R.0 929 of 2015).

In the year 20x8, the revenue of AMY is less than Rs. 1 billion. Further, in the prior year the revenue was also less than Rs. 1 billion. Therefore, in accordance with the third schedule, the foreign company is a 'medium-sized' company, and required to prepare statutory financial statements in accordance with the framework applicable to such companies.

The above change in the financial reporting framework is due to introduction of new sub-category for the foreign company and related financial reporting framework.

Example 5:

	20x8	20x7	20x6
Revenue of company	Rs. 900 million	Rs. 1,200 million	Rs. 800 million

AMY is a foreign company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7 it prepared financial statements in accordance with the IFRS notified by SECP and provisions of the repealed Companies Ordinance 1984 (As required under S.R.0 929 of 2015).

In the year 20x8, though the revenue of foreign company is less than Rs. 1 billion and it meets the criteria of a medium-sized company. However, in the prior year the revenue exceeded Rs. 1 billion. Therefore, in accordance with the third schedule, AMY is a 'large-sized' company, and required to prepare statutory financial statements in accordance with the framework applicable to such companies.

Example 6:

	20x8	20x7	20x6
Paid-up capital	Rs. 20 million	Rs. 20 million	Rs. 20 million
Revenue	Rs. 90 million	Rs. 80 million	Rs. 60 million
Number of employees	60 (Number)	60 (Number)	50 (Number)

SAM is private limited company, preparing its statutory financial statements for the year 20x8.

In the prior year, i.e. 20x7, it prepared financial statements in accordance the requirements of repealed Companies Ordinance 1984 (As required under S.R.0 929 of 2015). As per repealed Companies Ordinance 1984 it was categorized as a 'Small-sized' company (As its paid-up capital was less than Rs. 25 million and revenue was less than Rs, 100 million).

In the year 20x8, the classification of company will change due to introduction of new thresholds for the small-sized private companies. The company is not a small-sized company under the third schedule, as its paid-up capital exceeds the new set threshold of Rs. 10 million. The company is now a 'medium-sized' company, and required to prepare statutory financial statements in accordance with the framework applicable to such companies.

The above change in the financial reporting framework is due to introduction of new sub-category for the foreign company and related financial reporting framework.

4. How the exemption from the statutory audit and filing of financial statements determined?

The Companies Act provides relief from audit or filing of annual financial statements to following small-sized companies:

- **Exemption from filing of audited financial statements:** The Companies Act through section 233(3) exempts small-sized private companies, having paid-up capital exceeding Rs. 1 million but not exceeding Rs. 10 million, from the filing of audited financial statements with the registrar of companies. However, such companies are obligated to have their financial statements audited.

- **Exemption from the annual statutory audit: T**he Companies Act through section 234 exempts a small-sized private company having paid-up capital not exceeding Rs. 1 million and which is not a subsidiary of public company from the statutory audit requirement. However, the Companies Act requires these companies to mandatorily prepare and file the annual unaudited financial statements with the registrar.

  It is relevant to mention that though the company law has provided relief to the small-sized companies from the mandatory statutory audit requirement, however, in accordance with the income taxation law i.e. Income Tax Ordinance 2001, all companies are required to provide copy of audited financial statements alonhwith the return of total income.

The companies, which on the balance sheet date meet the above thresholds and requirements, are exempted from the mandatory audit and filing of the financial statements under the Companies Act.

5. What is a complete set of statutory financial statements under different financial reporting frameworks?

The Company's Act now contains a definition of the financial statements. The relevant clause 33 of section 2 is as reproduced as under:

"Financial statements in relation to a company, includes:

a) a statement of financial position as at the end of the period;
b) a statement of profit or loss and other comprehensive income or in the case of a company carrying on any activity not for profit, an income and expenditure statement for the period;
c) a statement of changes in equity for the period;
d) a statement of cash flows for the period;
e) notes, comprising a summary of significant accounting policies and other explanatory information;
f) comparative information in respect of the preceding period; and
g) any other statement as may be prescribed."

Further, section 225 in relation to the contents of the financial statements outlines that:

"The financial statements shall give a true and fair view of the state of affairs of the company, comply with the financial reporting standards notified by the Commission and shall be prepared in accordance with the requirements contained in the Third Schedule for different class or classes of companies."

The preparation of statutory financial statements requires that these shall be prepared in accordance with the applicable financial reporting standards (IFRS, IFRS for SMEs and AFRS for SSEs). The financial reporting standards in the following paragraphs specify the components of complete set of financial statements:

- **IFRS:** *IAS 1 Presentation of Financial Statements, paragraph 10*
- **IFRS for SMEs:** *Section 3, paragraph 3.17*
- **AFRS for SSEs:** *Section 1, paragraph 1.2*

The above definition of financial statements provided in the Companies Act read together with section 225 explains that the:

- **Preparation of financial statements in accordance with the framework:** The Companies Act in section 2(33) comprehensively lists down the components of financial statements that are relevant to the general-purpose financial statements of companies. In context of the preparation of financial statements, section 225 requires that these shall be prepared in accordance with the applicable financial reporting standards.

- **Minimum components of financial statements:** The applicable financial reporting standards (IFRS, IFRS for SSEs, AFRS for SSEs) set-out the minimum components necessary for the general-purpose financial statements. Therefore, the minimum components of financial statements prescribed under the relevant applicable accounting and financial reporting framework must be prepared in the statutory financial statements.

  In accordance with the IFRS and IFRs for SMEs, the complete set of financial statements include the same statements as defined in the Companies Act.

  The AFRS for SSEs that are applicable to the small-sized companies, in Section 1: *Presentation of Financial Statements,* outlines the minimum components of financial statements. Accordingly, the statutory financial statements of a small-sized company prepared in accordance with AFRS for SSEs shall mandatorily contain the following financial statement components specified under AFRs for SSEs.

  a) Statement of financial position
  b) Income statement; and
  c) Accounting policies and explanatory notes.

  However, the titles used for the above statements shall be as per the tiles of statements contained in the Companies Act section 2(33). Further, AFRS for SSEs allows companies to include other statements (such as statement of cash flows), in addition to the above three mandatory statements.

- **Single statement or two statement approach:** IFRS and IFRS for SMEs require that the statement of profit or loss and other comprehensive income for the period shall be included in the complete set of financial statements.

  In this regard IFRS (IAS I, paragraph 10 A) and IFRS for SMEs (Section 5, paragraph 5.2) provide an accounting policy choice between presenting total comprehensive income in a single statement or in two separate statements. Accordingly, the statutory financial statements of a company prepared in accordance with the IFRS notified by SECP or IFRS for SMEs, may follow:

  - Single statement approach: A single statement of profit or loss and other comprehensive income; or
  - Two statement approach: Separate statement of profit or loss and separate statement of comprehensive income.

- **Titles of financial statement/s:** The title of statements included in the complete set of financial statements, shall be the same as provided in the Companies Act section 2(33). For example, the title 'Statement of Financial Position' shall be used instead of previously used title 'Balance sheet'.

- **Income and Expenditure Statement:** The financial statements of a company licensed/ registered under section 42 and 45 of the Companies Act shall contain an income and expenditure statement in place of statement of profit or loss. Such company may follow the above explained single statement approach or two statement approach for the presentation of income and expenditure and comprehensive income for the period.

6. Can a company prepare the statutory financial statements by electing a higher financial reporting framework?

The repealed Companies Ordinance 1984 through S.R.0 929 of 2015 encouraged companies to prepare statutory financial statements in accordance with the higher financial reporting framework.

Under the Companies Act, a company is required to prepare statutory financial statements in accordance with the financial reporting framework prescribed in the third schedule. This prescribed framework can be termed a 'default financial reporting framework'. In general, the hierarchy of financial reporting standards in Pakistan is as follows:

- IFRS issued by IASB
- IFRS issued by IASB and notified by SECP
- IFRS for SMEs issued by IASB and notified by SECP
- AFRS for SSES issued by ICAP and notified by SECP

The specialized standards (e.g. IFAS) are applicable to the particular transactions / activities, and shall be followed accordingly.

Consistent to the above provisions of the repealed Companies Ordinance 1984, we believe that the companies shall be allowed to apply and prepare statutory financial statements in accordance with a higher financial reporting framework. Accordingly, the large-sized, medium-sized and small-sized companies can choose to apply higher financial reporting standards for the preparation of statutory financial statements. Below table summarizes the hierarchy of higher financial reporting framework for each class of company:

Class of company	Prescribed financial reporting standards	Higher financial reporting standards
Public interest and large-sized companies	IFRS issued by IASB and notified by SECP	- IFRS issued by IASB
Medium-sized company	IFRS for SMEs	- IFRS issued by IASB; or - IFRS notified by SECP
Small-sized company	AFRS for SSEs	- IFRS issued by IASB; - IFRS notified by SECP; or - IFRS for SMEs notified by SECP

The financial reporting standards (IFRS, IFRS for SMEs, AFRS for SSEs) being standalone standard/s are required to be complied in their entirety.

Under the company law, the board of directors are responsible for overseeing the financial reporting process and approval of statutory financial statements. Therefore, directors shall resolve to adopt a higher financial reporting framework. Further, companies shall apply the higher financial reporting standards on a consistent basis.

When deciding whether to apply the prescribed financial reporting standard under the third schedule, or a higher financial reporting standard, management should consider the needs of users of company's financial statements, ability to meet the enhanced reporting requirements, data and systems requirements and the corporate structures.

Note: The Institute's above views on the use of higher financial reporting framework have been shared with SECP and a clarification on the matter has been requested from SECP.

7. Can a company prepare statutory financial statements in accordance with IFRS issued by IASB?

The Companies Act has brought in a significant change in the financial reporting framework as companies can now prepare statutory financial statements in accordance with IFRS issued by IASB. The relevant section 225(4) is reproduced hereunder:

> *"Notwithstanding anything in this Act any company that intends to make unreserved compliance of IFRS issued by the IASB shall be permitted to do so."*
>
> *Explanation-The expression "IFRS" means International Financial Reporting Standards and the expression "IASB" means International Accounting Standards Board.*

Pursuant, to the above provision of the Companies Act, now company has a choice to prepare the statutory financial statements in accordance with the:

- IFRS issued by the IASB and notified by SECP; - IFRS for SMEs; or - AFRS for SSEs ** Whichever is applicable to the company*	Or	- IFRS issued by the IASB

When preparing the statutory financial statements in accordance with IFRS issued by IASB, the requirements of IFRS 1, First Time Adoption of International Reporting Standards and all other IASB effective standards and interpretations is required be complied with. In this regard the SECP granted exemptions from the application of the standard or interpretations will not be followed. Accordingly, company can ensure compliance with all IFRS requirements and make an unreserved statement of compliance with the IFRS issued by IASB in the statutory financial statements.

8. Is a company always required to comply with the disclosure requirements of fourth and fifth schedules?

The disclosure requirements of the fourth and fifth schedules of the Companies Act are in addition to the disclosure requirements of the financial reporting standards, including IFRS issued by IASB. The relevant clause of fourth schedule is reproduced hereunder:

> *"The disclosure requirements, as provided in this schedule, are applicable to the annual financial statements and are in addition to the disclosure requirements prescribed in International Financial Reporting Standards and shall be made in the notes to the accounts unless specifically required otherwise."*

The disclosure requirements of fourth and fifth schedules need to be made by companies regardless of the financial reporting standard applied. However, banks, DFIs, mutual funds and insurance companies are not required to comply with the disclosure requirements of fourth and fifth schedules.

A company preparing statutory financial statements in accordance with the IFRS issued by IASB (under section 225 (4)) is also required to consider and comply with the requirements and provisions of the Companies Act, including the disclosure requirements of fourth and fifth schedules.

Such a company shall:

- Comply with all the requirements of the IFRS and give an unreserved statement of compliance with IFRS in the statutory financial statements *(the statement of compliance with IFRS issued by IASB has been provided in ICAP Circular 4/2018, dated March 26, 2018);*
- Additionally, comply with the disclosure requirements of the fourth and fifth schedules (whichever is applicable to the company; and
- However, the disclosure requirements of the fourth and fifth schedules conflicting with the IFRS requirements shall not be followed. In case of conflict in the requirement/s of the Companies Act (including the fourth and fifth schedules) and the IFRS, apply the requirements of IFRS.

Conversely, if the framework for the preparation of statutory financial statements is IFRS Standards notified by SECP, company is required to comply with the requirements of IFRS (notified by SECP) and the Companies Act, including the disclosure requirements of the fourth and fifth schedules of the Companies Act. However, in this case the requirements of the Companies Act and fourth and fifth schedules will take precedence over IFRS requirements and shall be followed, accordingly.

9. What is the financial reporting framework for the banks and insurance companies?

The Companies Act stipulates the accounting and financial reporting framework for all companies. However, it also clarifies that the banks and insurance companies are required to follow the financial statements related requirements specified in the applicable regulatory laws. The relevant proviso of section 225, is reproduced hereunder:

> *"Provided further that, except to the extent, otherwise notified in the official Gazette by the Commission, this sub-section shall not apply to an insurance or banking company or to any other class of companies for which the requirements of financial statements are specified in the law regulating such class of companies."*

In this context:

- **The Banking Companies Ordinance 1962** sets-out the financial reporting requirements for the banks and DFIs. In terms of section 34 of the Banking Companies Ordinance, the banks are required to prepare statutory financial statements in the forms set out in the Second Schedule of the said Ordinance. In this regard, SBP through BPRD Circular 2 of 2018 has prescribed the revised format of financial statements for banks and DFIs.

- **The Insurance Ordinance 2000** establishes financial reporting requirements for insurance companies. In terms of section 46 of the Insurance Ordinance, the insurance companies are required to prepare the statutory financial statements in accordance with the format prescribed under the Schedule II of Insurance Rules 2017.

Accordingly, banks are required to prepare financial statements in accordance with the Banking Companies Ordinance 1962, related regulations, rules and SBP directives. Similarly, insurance companies are obligated to comply with the requirements of Insurance Ordinance 2000 and related regulations, rules and SECP directives.

These companies are not required to provide disclosures required in the fourth schedule. Further, due to applicability of specialized, banks and insurance companies cannot directly opt to prepare financial statements in accordance with the IFRS issued by IASB in terms of section 225(4) of the Companies Act.

10. What is the financial reporting framework for mutual funds?

Mutual fund industry is regulated by SECP, and the regulatory framework includes:

a) Part VIII of the repealed Companies Ordinance, 1984 (as this has not been repealed under the Companies Act, please see section 509) Non-Banking Finance Companies & Notified Entities Regulations, 2008

b) The Non-Banking Finance Companies (Establishment & Regulation) Rules, 2003

c) Circulars and Directives issued by the SECP under the provisions of the Companies Act.

Based on the above, the financial reporting framework applicable to the mutual funds includes:

- IFRS notified by SECP under the Companies Act;
- Provisions of and directives issued under the Companies Act along with part VIIIA of the repealed Companies Ordinance, 1984; and
- Non-Banking Finance Companies (Establishment and Regulations) Rules, 2003 (the NBFC Rules), Non-Banking Finance Companies and Notified Entities Regulations, 2008 (the NBFC Regulations) and requirements of the Trust Deed.

Where provisions of and directives issued under the Companies Act part VIIIA of the repealed Companies Ordinance, 1984, the NBFC Rules, the NBFC Regulations and requirements of the Trust Deed differ from the IFRS Standards, the provisions of and directives issued under the Companies Act, part VIIIA of the repealed Companies Ordinance, 1984, the NBFC Rules, the NBFC Regulations and requirements of the Trust Deed shall be followed.

In this regard, the disclosure requirements of fourth/ fifth schedule of the Companies Act do not apply to the mutual funds, as these entities are not considered 'company' under the Companies Act. Further, SECP through S.R.O 56 (1) / 2016 dated January 28, 2016 has exempted mutual funds from the consolidation requirements under the Companies Act (previously, repealed Companies Ordinance, 1984) and IFRS 10 in case of investment by companies in mutual funds established under trust structure.

11. What is the financial reporting framework for subsidiary of a listed company?

The Companies Act has prescribed differential and proportionate financial reporting framework for different classes and categories of companies. However, the third schedule has also clarified that the subsidiary of a listed company shall follow the requirements of the fourth schedule.

In this context clause (1) of fourth schedule stipulates that all listed companies and their subsidiaries shall follow the IFRS as are notified by SECP for the preparation of statutory financial statements.

Under the Companies Act, where a holding company prepares group accounts, its directors have to ensure that all subsidiaries in the same group apply a consistent accounting framework across entities. Therefore, subsidiary of a listed company, irrespective of its legal status, size and scale of operations is required to prepare the statutory financial statements in accordance with the financial reporting framework that is applicable to its listed holding company. The framework for the listed company as mentioned in the third schedule to be followed by a subsidiary company would be:

- IFRS notified by SECP; and
- Fourth schedule

Further, subsidiary of a listed company can also prepare statutory financial statements in accordance with IFRS notified by IASB, as allowed under section 225(4). However, companies need to consider that for the purpose of the consolidated financial statements the accounting policies of the subsidiary shall be aligned with those of holding company.

12. What is the implication of elimination of section 235 of repealed Companies Ordinance 1984 on the statutory financial statements prepared in accordance with IFRS and IFRS for SMEs?

The Companies Act has not retained the specific section relating to the surplus on revaluation of fixed assets i.e. section 235 of the repealed Companies Ordinance, 1984).

Previously, section 235 of the repealed Companies Ordinance, 1984 specified the accounting treatment and presentation of surplus on revaluation of fixed assets for the statutory reporting purposes. The said treatment differed from the accounting and presentation of revaluation surplus specified in IFRS (IAS 16 *Property, plant and equipment* and IFRS for SMEs (Section 17, *Property, plant and equipmen*t). However, companies were required to follow the requirements of section 235 for the statutory financial reporting purposes.

The elimination of the above-mentioned section 235 from the company law has removed the difference between the financial reporting standards i.e. IFRS and IFRS for SMEs, and the company law relating to the accounting treatment and presentation of surplus on revaluation of fixed assets. Accordingly, now companies shall comply with the following requirements of IAS 16 and IFRS for SMEs:

- Present surplus on revaluation of fixed assets under equity;
- Offset the deficit arising from revaluation of the particular asset; and
- Transfer the realized surplus directly to the retained earnings / unappropriated profit.

The applicability of above requirements of IAS 16 and IFRS for SMEs will result in the change in accounting policy of revaluation of surplus, for the first financial statements prepared after December 31, 2017.

13. What is the implication of elimination of section 235 of the repealed Companies Ordinance1984 on Revised AFRS for SSEs?

The Revised AFRS for SSEs has been prepared and issued by the Institute, and in 2015 SECP notified this standard for small-sized companies, under the repealed Companies Ordinance 1984.

In 2018, the Institute amended the AFRS for SSEs through Circular No. 7 of 2018. The objective of this amendment is to align the accounting treatment and presentation of revaluation surplus on property, plant and equipment prescribed under the Revised AFRS for SSEs with the Companies Act and other financial reporting standards. Prior to this amendment, the AFRS for SSEs specified the accounting treatment and presentation of surplus on revaluation fixed assets based on the section 235 of the repealed Companies Ordinance 1984. Therefore, the AFRS for SSEs prescribed accounting and presentation requirements of revaluation surplus was not in line with the other recognised financial reporting standards i.e. IFRS and IFRS for SMEs.

The amendments to Section 2 *Property, Plant and Equipment* of the Revised AFRS for SSEs have aligned the accounting treatment and presentation of revaluation surplus on property, plant and equipment with the accounting treatment and presentation of revaluation surplus provided in IAS 16 and IFRs for SMEs.

Consequent to the amendments to AFRS for SSEs, the company's accounting policy for revaluation surplus of property, plant and equipment shall be changed and the impact shall be accounted for and disclosed in accordance with the requirements of the Revised AFRS for SSEs.

The amendments to Revised AFRS for SSEs as issued through above-mentioned circular are applicable to the companies preparing financial statements under the Companies Act, for the period ended on or after June 30, 2018.

The above amendment to AFRS for SSEs can be accessed at:
http://www.icap.net.pk/wp-content/uploads/2018/07/Circular-No.7-of-2018-Amendments-to-Revised-AFRS-for-SSEs.pdf

14. How is the impact of change in accounting policy of revaluation surplus disclosed in the financial statements prepared in accordance with IFRS, IFRS for SMEs and Revised AFRS for SSEs?

Under the financial reporting frameworks, a presumption exists that an accounting policy once adopted shall not be changed in accounting for events and transactions of a similar type.

In accordance with IFRS (IAS 8) and IFRS for SMEs (section 10), the accounting policy shall be changed only in either of the following cases:

- The change is required by a newly issued or updated IFRS;
- The company can justify the use of an allowable alternative accounting principle will provide reliable and more relevant information

Further, in accordance with Revised AFRS for SSEs, section 19, the accounting policies must be applied consistently within the same accounts and from one financial year to the next. They shall be reviewed regularly to ensure that they remain the most appropriate to the entity's particular circumstances for the purpose of giving a true and fair view.

As explained above, the revaluation surplus shall be now accounted for and presented in accordance with accounting treatment prescribed in the financial reporting standard. The accounting treatment and presentation of revaluation surplus on property, plant and equipment and accounting and disclosure of change in accounting policy are prescribed in the following:

Financial reporting standard	Accounting treatment and presentation of revaluation surplus	Change in accounting policy
IFRS	IAS 16	IAS 8
IFRS for SMEs	Section 17	Section 10
Revised AFRS for SSEs	Section 2	Section 19

The above financial reporting standards prescribe same accounting treatment and presentation requirement for the surplus on revaluation of property, plant and equipment.

Further, with regard to change in accounting policy the above financial reporting standards outline the similar requirement of retrospective application of the accounting policy.

In consideration of same requirements for revaluation surplus and resultant change in accounting policy, the impact (if any) would be similar for all companies. Below the impact analysis based on IAS 16 is analyzed.

IAS 16 requirements differ from previously applied accounting treatment and presentation under the repealed Companies Ordinance 1984, therefore requiring a change in accounting policy.

In accordance with IFRS and IFRS for SMEs the impact of the change in policy of revaluation surplus in the annual financial statements prepared immediately after December 31, 2017 shall be reflected through retrospective application of the new accounting policy to all prior periods, unless it is impracticable to do so.

Under IFRS, the retrospective application means adjusting the opening balance of each affected component of equity for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented as if the new accounting policy had always been applied.

When an entity applies a new accounting policy retrospectively, it applies the new accounting policy to comparative information for prior periods as far back as is practicable.

However, IFRS also outline that if it is impracticable to determine either the period-specific effects or the cumulative effect of the change for one or more prior periods presented, the company shall apply the new accounting policy to the carrying amounts of assets and liabilities as at the beginning of the earliest period for which retrospective application is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of equity for that period.

Further, if it is impracticable to determine the cumulative effect, at the beginning of the current period, of applying a new accounting policy to all prior periods, the entity shall adjust the comparative information to apply the new accounting policy prospectively from the earliest date practicable

Below table explains the impact of differing requirements of IAS 16 and section 235 of repealed Companies Ordinance 1984:

IAS 16	Section 235 of repealed Companies Ordinance 1984	Impact on the financial Statements prepared under the Companies Act
Presentation: Revaluation surplus in the statement of financial position		
IAS 16 requires that if an asset's carrying amount increases due to revaluation, the increase shall be recognised in other comprehensive income and <u>accumulated in equity</u> under the heading of revaluation surplus. *(Underline is ours)*	Section 235 required that the increase in the value of revalued assets to be transferred to an account to be called "Surplus on revaluation of Fixed Assets Account" and shown in the balance sheet of the company <u>after Capital and Reserves</u>. *(Underline is ours)*	In accordance with IAS 16, the revaluation surplus is credited to other comprehensive income and accumulated in equity under the heading of revaluation surplus. Previously, section 235 required surplus on revaluation of fixed assets to be shown in the balance-sheet of the company after capital and reserves *(not as part of equity)*. **Impact** In consideration of the requirements of IAS 16 and specific disclosure requirement of fourth and fifth schedules of the Companies Act, the companies will have to change the presentation of revaluation surplus in the statement of financial position and statement of changes in equity. *(The fourth and fifth schedules to the Companies Act require that the revaluation surplus on property, plant and equipment shall be disclosed as a separate line item on the face of the statement of financial position)*

Accounting: Off-setting of a revaluation surplus

If an asset's carrying amount is increased as a result of a revaluation, the increase shall be recognised in profit or loss, or the decrease shall be recognised in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of the same asset. *(Underline is ours)*	Section 235 allowed that 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 of any other fixed asset of the company. *(Underline is ours)*	As stated above, IAS 16 requires revaluation surplus shall be credited to other comprehensive income. However, it allows offsetting of surplus only in respect of the same asset (where previously revaluation loss has been recognized). In such a case, the revaluation gain is first credited to the statement of profit or loss to the extent that the gain reverses a loss previously recognised in the statement of profit or loss related to the same asset. Under the provisions of the repealed Companies Ordinance, 1984, companies were allowed to apply the surplus on revaluation of fixed assets in setting-off or in diminution of any deficit arising from the revaluation of any other fixed assets of the company. **Impact** The companies impacted from the above change would be those that have utilized the revaluation surplus of an asset in adjusting the deficit arising from another asset. Such companies are required to account for the off-setting of revaluation surplus in accordance with IAS 16, and accordingly calculate the impact IAS 16 application by making retrospective adjustments to the affected items, in accordance with IAS 8.

Accounting: Realization of revaluation surplus on derecognition of an asset

AS 16 requires that the revaluation surplus included in equity in respect of an item of property, plant and equipment may be transferred directly to retained earnings when the asset is derecognized. This may involve transferring the whole of the surplus when the asset is retired or disposed of. *(Underline is ours)*	Under section 235 the revaluation surplus realized on disposal of the revalued assets, could be applied to set off or reduce any deficit or loss, whether past, current or future, or in any manner applied, adjusted or treated so as to add to the income, profit or surplus of the company, or utilized directly or indirectly by way of dividend or bonus. *(Underline is ours)*	Under IAS 16 the revaluation surplus included in equity is transferred directly to retained earnings/unappropriated profits when the surplus is realized (usually when the asset is de-recognised). Importantly, the transfer is made through reserves (in the statement of changes in equity), not through the profit and loss account. The section 235 allowed transfer of revaluation surplus elated to a disposed revalued asset to the profit or loss. **Impact** The above requirement of IAS 16 will impact companies which have in the prior years transferred the revaluation surplus related to the disposed revalued assets to the profit or loss. Such companies are required to retrospectively account for the impact by calculating and restating the directly impacted statements and items.

Accounting: Realization of revaluation surplus during the use of an asset		
In accordance with IAS 16, the revaluation surplus can also be transferred directly to retained earnings, as the company uses the asset. The amount transferred is the difference between depreciation based on the asset's revalued carrying amount and depreciation based on the asset's original cost (incremental depreciation) and net of deferred tax.	Section 235 also allowed charging of incremental depreciation related to the revalued assets against the surplus on revaluation.	IAS 16 allows the transfer of revaluation surplus included in equity to retained earnings/unappropriated profits when the surplus is used. In this context, an annual transfer from the asset revaluation surplus to retained earnings is made for the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on the asset's original cost. Importantly, this transfer is made through reserves (in the statement of changes in equity), not through the profit and loss account. The section 235 also allowed transfer of revaluation surplus related to the incremental depreciation of the asset. **Impact** The above requirement of IAS 16 will affect the companies that have transferred the revaluation surplus related to the incremental depreciation to the profit or loss, in the prior years. Such companies are required to retrospectively account for the impact by calculating and restating the directly impacted statements and items.

The accounting and presentation requirements of IFRS for SMEs and Revised AFRS for SSEs, related to the revaluation model of property, plant and equipment are same as IAS 16. Further, the requirements for the consistent application and change in accounting policy are also same to the IFRS requirements. Therefore, the above analysis also outlines the explanation and guidance on impact of change in accounting policy of revaluation surplus for the statutory financial statements prepared in accordance with the IFRS for SMEs.

Consequent to the change in accounting policy the company shall also consider the related implications such as:

- Presentation of third statement of financial position;
- Direct effects of retrospective application on financial statement items; and
- Labeling column headings in financial statements as 'Restated' when periods have been adjusted to reflect the retroactive application of the accounting policy

15. Is a third statement of financial position required for statutory annual financial statements, when there is a change in accounting policy or reclassification?

This third statement of financial position means that an additional statement of financial position is presented in the financial statements. The applicability of Companies Act may require change in accounting policy or reclassification of items in the statement of financial position. The following paragraphs discuss the impact of Companies Act on the policy and presentation of financial statements and the requirement of third statement of financial position with reference to the IFRS and other financial reporting standards.

Change in policy and reclassifications under the Companies Act

The application of Companies Act will impact the accounting and presentation of revaluation surplus, requiring change in policy from the previously followed accounting policy. Further, the presentation and disclosure requirements of fourth and fifth schedules may require the company to change the presentation and classification of previously reported items. The term 'reclassification' is considered as a change in the presentation or classification of items in the financial statements. On making such a change, comparative amounts are also reclassified unless this is impractical. The reclassification triggers a requirement for an additional statement of financial position even if this third statement is not affected.

In this context, the reclassifications and presentation changes may relate to the following items, as the fourth and fifth schedules require their presentation as separate line items on the face of the statement of financial position:

1. Revaluation surplus on property, plant and equipment;
2. Long term deposits and prepayments;
3. Unpaid dividend;
4. Unclaimed dividend; and
5. Cash and bank balances

IFRS

Under the IFRS (IAS 1 *Presentation of Financial Statements*) requires a third statement of financial position along with related notes if during the current period the company:

- Changes its accounting policy retrospectively;
- Makes a retrospective restatement in order to correct an error; or
- Reclassifies items in its financial statements.

This implies that all material adjustments to previously reported amounts and presentation give rise to the requirement for a third statement of financial position. This is also required in the year of initial adoption of a new accounting standard that requires retrospective application.

A company might make immaterial changes to its accounting policies, classifications etc. In principle, the immaterial changes do not give rise to a requirement for an additional statement of financial position. In this context the assessment of materiality depends on facts and circumstances and involve professional judgement.

IFRS for SMEs and AFRS for SSEs

The IFRS for SMEs and AFRS for SSES do not require third statement of financial position.

Impact on companies preparing financial statements in accordance with IFRS

In the first year ended after December 31, 2017, the company shall make the third statement of financial position when:

- Applying the changed accounting policy of revaluation surplus;
- The presentation requirements of fourth and fifth schedules reflect a material reclassification of previously reported items in the statement of financial position (such as unpaid dividend, unclaimed dividend and long-term deposits and prepayments);
- Applying a new IFRS

Other than disclosure of certain specific information (disclosure requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and notes related to the reclassification of corresponding figures), the other notes related to third statement of financial position are not required.

Impact on companies preparing financial statements in accordance with IFRS for SMEs or Revised AFRS for SSEs

As mentioned above the companies preparing financial statements in accordance with IFRS for SMEs or AFRS for SSEs, are not required to make a third statement of financial position.

16. Is a third statement of financial position required for statutory interim financial statements, when there is a change in accounting policy or reclassification?

In accordance with paragraph 20 of IAS 34, the interim financial reporting has a year-to-date approach and does not replicate the requirements of IAS 1 in terms of comparative information. Therefore, it is not necessary to provide a third statement of financial position as at the beginning of the earliest comparative period presented where a company has made a retrospective change in accounting policies and/or a retrospective reclassification.

17. What are the 'significant transactions and events' that require disclosure under the fourth and fifth schedules?

The Companies Act in fourth and fifth schedules has introduced a new requirement to disclose the significant events and transactions in the annual statutory financial statements.

What is the requirement?

The fourth and fifth schedules require that the statutory financial statements shall disclose a summary of the significant transactions and events that have affected the company's financial position and performance since the end of the last annual reporting period.

This new requirement applicable to all companies requires a summarized list and information of events and transactions that are significant to understand the changes in the financial position and performance of the company since the end of the last annual reporting period.

Objective of the disclosure of significant transactions and events

Company's financial position, financial performance and cash flows are impacted by the events and transactions. The effects of company's various activities, transactions and other events differ in frequency and magnitude, disclosing significant information regarding company's financial position and performance during the period would assist users in understanding the financial position and financial performance, and in making decisions and future projections.

The objective of disclosure of significant events and transactions in the financial statements is to furnish additional information, which will help users understand how, changes in the company's structure, scale and operations (if any) have impacted the financial position and performance.

The guidance on the significant events and transactions – available in the accounting literature

The Companies Act explains the term "significant accounting transaction' in section 424. This explanation is with reference to an inactive company. However, The Companies Act does not explanation of the significant event and transactions in relation to the active companies.

The Conceptual Framework indicates that the objective of financial statements is the provision of information that is useful to a wide range of users. However, the financial reporting standards (IFRS, IFRS for SMEs, AFRS for SSEs) in relation to the annual financial statements do not require a general disclosure of significant transactions and/or events in the financial statements. These standards set out specific disclosures related to the components and items of financial statements.

In relation to interim financial reporting, the IAS 34 *Interim Financial Reporting* (IAS 34) provides explanation and guidance on the significant events and transactions.

Due to absence of guidance / explanation regarding the significant events and transactions in the Companies Act and IFRS (other than IAS 34), analogy can be drawn from the guidance outlined in IAS 34 on the subject matter. The IAS 34 explains and lists down examples of significant events and transactions in context of interim financial reporting, and same can be used to develop an understanding and reference point to meet the above mentioned disclosure requirement of the Companies Act.

Significant events and transactions

The IFRS place particular emphasis on the need to take into account qualitative characteristics and the use of professional judgment when preparing the financial statements. Fundamentally, the assessment of significance of a transaction or event requiring disclosure in the financial statements depends on facts and circumstances and involves professional judgement.

The significant events and transactions are those items/ matters/ amounts that significantly impacted the company's financial position and performance during the year. The significant transactions and events may:

- Pertain to the ordinary course of the business or may relate to other than the ordinary activities.
- Relate be recurring items or unusual or infrequently occurring items.

The preparers of financial statements shall determine the significant events and transactions based on their assessment of quantative and qualitative factors and their relevance to the needs of users of financial statements.

Transactions which, according to their object and nature, characteristic and conditions are carried out in the ordinary course of business of the company and those which are free from any particular criticality in relation to their characteristic or the time of execution, are considered typical and usual. The unusual transactions and events are those that would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the company operates.

In determining, for the purposes of disclosure in the annual statutory financial statements, whether a transaction or event is significant, the company in general may consider some or all of the following factors:

- **Volume and frequency** - The size, number, and frequency of transactions / events, performed over a period, including whether the transactions, are increasing or decreasing over time and the rate of increase or decrease.
- **Nature -** The nature of the transactions /events, including the type, accounting and disclosure complexity, existence of related party and commercial purpose of the transactions.
- **Initiation to approval process -** Whether the transaction(s), is performed with the involvement or approval of management or only by clerical personnel; and whether the transaction(s), is part of a pattern of conduct or the result of a business development strategy.
- **Impact –** The impact of the transaction / event on the company's financial position and performance.

Disclosure in financial statements

Information disclosed in relation to the significant events and transactions shall update the relevant information presented in the last annual statutory financial statements, if it is relevant to understand current year's financial position and performance. Further, any new significant event / transaction occurring during the year shall also be included in the disclosure.

The significant events and transactions can be collectively disclosed in a separate note titled as 'Significant events and transactions'. On the other hand, each event or transaction can be individually disclosed under the disclosure of the relevant item in the financial statements, for example a significant transaction relating to property, plant and equipment can be disclosed in the related disclosure note of property, plant and equipment.

For events or transactions that are considered to be significant to an understanding of the statutory financial statements, an explanation of the transaction(s) and/or event(s) is required together with an update of the relevant information, which was included in most recent annual financial statements.

- Brief explanation of events and transactions along-with the monetary amounts involved (if any) that are significant to an understanding of the changes in financial position and performance of the company since the end of the last annual reporting period; and
- Any other element of the transaction(s) and/or event(s) necessary for an understanding of the financial statements, such as:
  - Background to and reasons for the transaction and/or event;
  - A description of the transaction and/ or event and its key terms; and
  - A description of the financial effects and key risks of the transaction and/or event (if any).

Examples of significant events and transactions

As explained above, the Companies Act does not provide an explanation of the significant events and transactions relating to the financial statements disclosures. Further, the IFRS also do not set out any requirement for disclosure of significant events and transactions in context of annual financial statements. In view of this, the analogy and examples of significant events and transactions as provided in IAS 34 can be used while preparing the annual statutory financial statements.

IAS 34 provides explanation on the significant events and transactions in context of interim financial statements. However, this explanation can be used/referred for the annual statutory financial reporting purposes. IAS 34 contains a non-exhaustive list of significant events and transactions. Based on this the events and transactions for which disclosures would be required, (if management determines that these are significant) in annual statutory financial statements may include:

- The write-down of inventories to net realizable value and the reversal of such a write-down;
- Recognition of a loss from the impairment of financial assets, property, plant and equipment, intangible assets, assets arising from contracts with customers, or other assets, and the reversal of such an impairment loss;
- The reversal of any provisions for the costs of restructuring;
- Acquisition and disposals of items of property, plant and equipment;
- Commitments for the purchase of property, plant and equipment;
- Changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, whether those assets or liabilities are recognised at fair value or amortised cost;
- Entering into or terminating financing arrangements
- Any loan default or breach of a loan agreement that has not been remedied on or before the end of the reporting period;

- Transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments;
- Change in classification of assets;
- Change in contingent assets or liabilities;
- Litigation settlements;
- Related party transactions;
- Change in accounting policies;
- Corrections of prior period errors;
- Application of a new IFRS; and
- Events after the reporting period.

It is relevant to mention that the above list is not exhaustive and the identification and disclosure of significant events and transactions should always be considered in context of the company specific materiality thresholds, nature of events, transactions and circumstances and financial statements users needs. Accordingly, the disclosure of a transaction or event may not be required in the financial statements due to the company specific materiality threshold or absence of a particular transaction or event. Conversely, there may be areas / items in addition to the above that are of significance, requiring disclosure as significant transaction or event in the financial statements.

18. What is the definition of 'related party' for the financial statements disclosures?

The Companies Act through newly inserted section 208 has established an extensive definition of the related party. This definition includes various types of relationships and positions as related parties, consequently making the definition more expanded compared to the definition provided in IAS 24 *Related Party Disclosures*. However, in accordance with the explanation provided in the fourth and fifth schedules to the Companies Act, the definition of related party as per IFRS i.e. IAS 24 *Related Party Disclosures* shall be followed for the financial statements disclosures.

IAS 24 requires disclosures about transactions and outstanding balances with an entity's related parties. The standard defines various classes of entities and people as related parties and sets out the disclosures required in respect of those parties, including the compensation of key management personnel.
All financial reporting standards contain the definition of related party, reference is as under:

- **IFRS:** *Related party defined in paragraph 9 of IAS 24*
- **IFRS for SMEs:** *Related party defined in paragraph 33.2 of section 33*
- **AFRS for SSEs:** *Related party defined in glossary of terms*

IAS 24 defines related party as follows:

> *"A related party is a person or entity that is related to the entity that is preparing its financial statements (in this Standard referred to as the 'reporting entity').*
>
> *a) A person or a 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. The entity and the reporting entity are members of the 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. The 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).

viii. The entity, or any member of a group of which it is a part provides key management personnel services to the reporting entity or to the parent of the reporting entity."

The other financial reporting standards i.e. IFRS for SMEs and AFRS for SSEs also contain definitions of the related party. Further section 33 and section 20 of IFRS for SMEs and AFRS for SSEs, respectively, set out the related party disclosures.

In addition to the above disclosure requirements of financial reporting standards, the fourth and fifth schedules require additional disclosures of related party transactions and outstanding balances.

In accordance with the explanation contained in the fourth and fifth schedules, company shall provide the related party disclosures required under the applicable framework (IFRS, IFRS for SMEs, AFRS for SSEs, additionally fourth and fifth schedules), based on the IAS 24 definition of related party. Therefore, the medium-sized and small-sized companies shall also make the disclosures specified in the relevant framework (IFRS for SMEs and AFRS for SSEs, in accordance with IAS 24 definition of related party.

The related party definition contained in IFRS and IFRS for SMEs are same, while the definition specified in AFRs for SSEs is substantially same to the definition provide IFRS/IFRS for SMEs, as only following relationship not provided in AFRS for SMEs:

"The entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity."

19. What is the definition of 'associated company' for the accounting and financial statements disclosure purposes?

In the Companies Act, a clarification has been provided in the section 225 (1) that for the financial accounting and reporting purposes, the definition of associate specified in the applicable financial reporting framework shall be considered.

The Companies Act defines associated companies and associated undertakings in section 2(4). This definition has been revised from the repealed Companies Ordinance 1984, as the companies related by virtue of relationship with the appointment of an independent director have been excluded. However, the revised definition of associated company contained in the Companies Act still differs from the financial reporting standards definition, exposing to the possibility of divergent accounting treatment of associated companies from IFRS requirements

In order to avoid divergence in accounting of associated companies from IFRS and global accounting practices, the above explained provision has been added in section 225. This will now ensure that the accounting treatment of associated companies in the financial statements is in accordance with the requirements of applicable financial reporting standard (i.e. IFRS, IFRS for SMEs, and AFRs for SSEs).

20. Is there any change in the IFRS for SMEs applicable to medium-sized companies?

The Companies Act has prescribed IFRS for SMEs to medium-sized companies; however, it has brought in a significant change in IFRS for SMEs by eliminating the requirement of capitalization of borrowing costs.

IASB issued the IFRS for SMEs in 2009. However, in Pakistan, IFRS for SMEs was recognised as a financial reporting framework under the repealed Companies Ordinance, 1984 in 2015.

In this context SECP, through SRO 929 of 2015 notified the IFRS for SMEs issued by IASB, with the following two exceptions:

Sr. #	SECP notified exceptions	Requirement of IFRS for SMEs issued by IASB (2009 version)
1	**Revaluation of property, plant and equipment** Allowed the revaluation model for property, plant and equipment in addition to the cost model	**Allowed cost model only** Required the measurement of property, plant and equipment using the cost model. Did not permit revaluation model.
2	**Capitalization of borrowing cost** Allowed capitalization of borrowing costs related to qualifying assets	**All borrowing costs charged to profit or loss** Required all borrowing costs to be charged to profit or loss. Therefore, did not allow capitalization of borrowing costs.

Subsequently, IASB after a comprehensive review of IFRS for SMEs issued the amended Standard in 2015. One of the significant amendment made by IASB was the inclusion of policy choice of cost model and revaluation model for the measurement of property, plant and equipment.

Owing, to the above amendments in the IFRS for SMEs issued by IASB, the only one exception of capitalization of borrowing cost existed in the repealed Companies Ordinance 1984 prescribed reporting framework and IFRS for SMEs.

However, the Companies Act has now removed this exception, as under third schedule it has prescribed IFRS for SMEs issued by IASB without any exception/amendment. Therefore, now there is no specific accounting treatment or exception to the requirements of IFRS for SMEs that has been specified in the Companies Act, and the change in the financial reporting framework of IFRS for SMEs is now aligned with the IASB issued IFRS for SMEs.

21. What is the impact of elimination of accounting treatment of capitalization of the borrowing costs on the financial statements prepared in accordance with IFRS for SMEs?

As explained above, Companies Act has deleted the accounting treatment of capitalization of borrowing costs. Previously, the Repealed Companies Ordinance 1984 (through S.R.O 929 of 2015) required capitalization of borrowing costs related to the qualifying assets for the companies preparing financial statements in accordance with IFRS for SMEs.

Consequent to this change in the Companies Act, companies preparing their financial statements in accordance with IFRS for SMEs shall now recognize all borrowing costs as an expense in the statement of profit or loss.

Further, companies having previously capitalised the borrowing costs, shall apply the new accounting policy of borrowing costs retrospectively.

Accounting of change in policy of borrowing costs

The companies are required to apply the new accounting policy of borrowing costs to comparative information for prior periods to the earliest date for which it is practicable, as if the new accounting policy had always been applied. This would be done by:

- Derecognizing previously capitalized borrowing cost (capitalized owing to the exception allowed by SECP under SRO 929 of 2015);
- Recognition of the related impact in the retained earnings, consequent to the change in accounting policy of the borrowing cost.

When it is impracticable to determine the individual-period effects of a change in accounting policy of borrowing costs on comparative information for one or more prior periods presented, the company shall apply the new accounting policy to the carrying amounts of assets and liabilities as at the beginning of the earliest period for which retrospective application is practicable, which may be the current period, and shall make a corresponding adjustment to the opening balance of each affected component of equity for that period.

(The explanation on the 'impracticability' in IFRS for SMEs is similar to the in the IAS 8, and discussed earlier in this document)

Disclosure of a change in accounting policy

The company shall disclose the following in relation to change in accounting policy of borrowing costs:

a) the nature of the change in accounting policy;

b) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment for each financial statement line item affected;

c) the amount of the adjustment relating to periods before those presented, to the extent practicable; and

d) an explanation if it is impracticable to determine the amounts to be disclosed in (b) or (c).

Financial statements of subsequent periods need not repeat these disclosures.

Further, third statement of financial position is not required under the IFRS for SMEs.

22. Is a statement of compliance under section 227 required for the June 2018 financial reporting?

The Companies Act through section 227 has introduced a new requirement of statement of compliance. This statement of compliance shall be attached with the financial statements. However, the scope of the statement of compliance and its contents are yet to be specified by SECP.

Accordingly, until the notification of the statement of compliance under section 227(4), the companies are not required to prepare and attach such statement with the financial statements.

23. Is every holding company required to prepare annual consolidated financial statements?

Under the Companies Act, every holding company is required to prepare consolidated financial statements, except for a private company if neither the said private company nor its subsidiary company (ies) have the paid up capital exceeding one million rupees.

Principles and basic characteristics for preparation and presentation of consolidated financial statements have been set out in IFRS 10 *Consolidated Financial Statements*.

IFRS 10 stipulates an exemption from the preparation of consolidated financial statements if the holding company meets all of the following conditions:

- The holding company is a subsidiary (wholly-owned or partially-owned) subsidiary of another entity. Owners forming non-controlling interest have been informed and have no objections to the holding company not presenting consolidated financial statements.
- Debt or equity instruments issued by the holding company are not traded in public market; nor did the company file the financial statements with a regulatory organisation for issuing instruments in the public market.
- Ultimate parent or any intermediate parent of the company produces consolidated financial statements prepared in accordance with IFRS that are available for public use.

Based on the above, the difference exists in the IFRS and Companies Act in relation to the exemption from the preparation of consolidated financial statements. With regard to the statutory financial statements the reporting obligations, the requirements and provisions of the Companies Act prevail over IFRS, therefore all holding companies (except those granted exemption/relaxation under Companies Act) shall prepare annual statutory consolidated financial statements.

The consolidated financial statements shall comply with the disclosure requirements of the relevant schedule and financial reporting standards notified by the Commission.

However, pursuant to section 225(4) the consolidated financial statements can be prepared in accordance with the IFRS Standards Issued by IASB.

Under the Companies Act, in case there are different financial year ends of the subsidiary and holding company, the interim financial statements of a subsidiary prepared for consolidation purposes are no longer required to be reviewed by the auditors of the subsidiary. The repealed Companies Ordinance 1984 required the auditors' review of interim financial statements of the subsidiary prepared in the above case.

24. What are financial reporting requirements for the quarterly financial statements under the Companies Act?

In accordance with section 237 of the Companies Act and provisions of CCG Regulations, the listed companies are required to prepared statutory interim (quarterly) financial statements.

The listed companies shall prepare these quarterly financial statements in accordance with the financial reporting standards notified by the SECP. The financial reporting standard related to the preparation and presentation of these quarterly financial statements is IAS 34 *Interim Financial Reporting*. Accordingly, listed companies shall prepare the quarterly financial statements in accordance with IAS 34 and other related provisions of the Companies Act.

In accordance with IAS 34, an entity that presents interim financial statements can choose to prepare them either in the format of a complete set of financial statements or in the format of a set of condensed financial statements.

For the purposes of the presentation of interim financial statements:

- the requirements of all paragraphs in IAS 1 apply to a complete set of financial statements; whereas
- In case of condensed financial statements only requirements of IAS 1 paragraphs 15 to 35 are applicable. These paragraphs cover the general features i.e. fair presentation and compliance with IFRS, Going concern, Accrual basis of accounting, Materiality and aggregation and Offsetting.

In this regard, the disclosure requirements fourth and fifth schedules are not applicable to the quarterly financial statements.

Further, in accordance with IAS 34 paragraph 10, companies are required to include at least each of the headings and subtotals that were included in their most recent annual financial statements. Additional line items also need to be included if their omission would make the condensed interim financial statements misleading.

IAS 34 prescribes reduced disclosure requirements, as it presumes that the reader of interim consolidated condensed financial will also have the latest annual financial statements available. It is therefore unnecessary that the notes in the interim consolidated condensed financial statements repeat information which is available in the most recent annual financial statements.

The Companies Act requires preparation of statutory annual consolidated financial statements under section 226. In accordance with IAS 34 paragraph 14, the quarterly financial statements shall be prepared on a consolidated basis if company's most recent annual financial statements were consolidated financial statements.

	Quarter 1		Quarter 2 (Half yearly)		Quarter 3	
	Separate	Consolidated	Separate	Consolidated	Separate	Consolidated
Preparation of financial statements	✓	✓	✓	✓	✓	✓
Review of financial statements by statutory auditor	-	-	✓	-	-	-
Endorsement of financial statements by chief executive officer and chief financial officer	✓	✓	✓	✓	✓	✓
Initialing of financial statements by statutory auditor	-	-	✓	-	-	-
Review of financial statements by audit committee	✓	✓	✓	✓	✓	✓
Approval of financial statements by the board of directors	✓	✓	✓	✓	✓	✓
Approval and authentication of financial statements by Director, Chief executive Officer and Chief Financial Officer (approval and authentication of financial statements of specialized companies banks, insurance companies etc., in accordance with relevant statutory law and regulations)	✓	✓	✓	✓	✓	✓
Submission / filing of financial statements	✓	✓	✓	✓	✓	✓

25. Can a holding company change its financial year to coincide with the financial year of its subsidiary?

In accordance with section 229 of the Companies Act, the board of directors of holding company shall ensure that, except there are good reasons against it, the financial year of holding company and each of its subsidiaries shall coincide.

Further, both the holding company and the subsidiary (ies) can change the financial year pursuant to SECP's approval. Previously, under the repealed Companies Ordinance 1984 only subsidiary was allowed to change its financial year to correspond with the holding company's financial year.

26. Is there any significant change in the IFRS that may affect future period financial statements?

Companies that prepare financial statements in accordance with IFRS are required to determine what disclosures are required under paragraph 30 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* about IFRS issued but not yet effective and not yet applied by the company.

IAS 8 requires that when an entity has not applied a new IFRS (Standard or Interpretation) that has been issued but is not yet effective, the entity shall disclose:

a) this fact; and

b) known or reasonably estimable information relevant to assessing the possible impact that application of the new Standard or Interpretation will have on the entity's financial statements in the period of initial application.

In this regard, the IFRS require companies to consider the following for disclosure:

- the title of the new Standard or Interpretation;
- the nature of the impending change or changes in accounting policy;
- the date by which application of the Standard or Interpretation is required;
- the date as at which it plans to apply the Standard or Interpretation initially; and
- either:
  - a discussion of the impact that initial application of the Standard or Interpretation is expected to have on the entity's financial statements; or
  - if that impact is not known or reasonably estimable, a statement to that effect.

During the period from July 01, 2017 to June 30, 2018, SECP has adopted following news IFRS:

New pronouncement	SECP notified Effective date	IASB Effective date
IFRS 9 *Financial Instruments*	July 1, 2018	Jan 1, 2018
IFRS 15 *Revenue from Contracts with Customers*	July 1, 2018	Jan 1, 2018
IFRS 16 *Leases*	Jan 1, 2019	Jan 1, 2019

Further, there are IFRICs, and many narrow scope amendments to the IFRS that would be effective in the next financial years. The next section of the document lists all these standards and interpretations along-with their effective dates.

As at June 30, 2018, these new requirements will apply to future financial statements and may significantly affect how and when revenue can be recognised, the values of financial instrument (including loan provisioning and hedge accounting), and assets and liabilities relating to leases.

It is important for the companies to plan for the new standards and inform investors and other financial statements users of the impact on reported results. Therefore, it is critical to determine the extent of any impact well in advance and accordingly put in place the implementation plans for these new standards.

Before the effective date of the IFRS, it should ensure that notes to the financial statements disclose the potential material impact on future financial position and results of new requirements for recognising revenue, for valuing financial instruments and accounting for leases.

27. Can a company early adopt an IFRS?

Under the Companies Act, SECP notifies the financial reporting standard (i.e. IFRS or IFRS for SMEs issued by IASB, AFRS for SSEs, and Accounting Standard for NPOs and IFAS issued by ICAP).

From the date of its adoption, the standard becomes part of the financial reporting framework under the Companies Act, obligating companies to evaluate and apply its requirements in the preparation of financial statements. The financial reporting standard becomes mandatorily applicable from the SECP notified effective date.

Each IASB issued standard, interpretation or amendment indicates the effective date and specifies when early adoption is permitted. The early adoption of a standard under the Companies Act is subject to SECP notification and specific permission of early adoption in the relevant standard.

The companies that prepare financial statements in accordance with the SECP notified financial reporting standard, and want to adopt a new IFRS accounting treatments at the earliest possible opportunity, can early adopt a SECP notified accounting standard. In this context, SECP has adopted following IFRS during the period from 01 July 2017 to May 31, 2018, which can be early adopted.

IFRS	SECP notified effective date Annual reporting periods beginning on or after	Early adoption permitted in IASB issued IFRS
IFRS 9 *Financial Instruments*	July 1, 2018	**Yes** - Mentioned in Chapter 7 of IFRS 9
IFRS 15 *Revenue from Contracts with Customers*	July 1, 2018	**Yes** - Mentioned in Appendix C of IFRS 15
IFRS 16 *Leases*	January 1, 2019	**Yes** - Mentioned in Appendix C of IFRS 16

However, companies cannot early adopt a standard or interpretation if:

- The relevant standard has not been notified by SECP; or
- The relevant standard or interpretation does not permit the early adoption.

It is advisable to the companies to carefully consider and evaluate the requirements of each IFRS and its potential impacts when making a decision whether early adoption is appropriate.

IFRS update as at June 30, 2018

IFRS adopted by SECP

After the enactment of the Companies Act on May 30, 2018, SECP has adopted following IFRS:

New pronouncement	SECP notified Effective date	IASB Effective date
IFRS 9 *Financial Instruments*	July 1, 2018	Jan 1, 2018
IFRS 15 *Revenue from Contracts with Customers*	July 1, 2018	Jan 1, 2018
IFRS 16 *Leases*	Jan 1, 2019	Jan 1, 2019

The tables below, set out the recent new pronouncements and whether they are optional or mandatory for the year ending June 30, 2018. Further, the applicability of these pronouncements to the interim financial statements for the period ending June 30, 2018 are also included.

Newly effective amendments to the IFRS

New pronouncement	IASB effective date	Year ending June 30, 2018	Half year ending June 30, 2018
Amendments to IAS 7: Disclosure Initiative	Jan 1, 2017	Mandatory	Mandatory
Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealized Losses	Jan 1, 2017	Mandatory	Mandatory
Amendments to IFRS 12: Annual Improvements to IFRS Standards 2014-2016 Cycle	Jan 1, 2017	Mandatory	Mandatory

New IFRS, IFRIC and amendments to the IFRS not yet effective but available for early adoption (with regard to June 30, 2018 year ends)

New pronouncement	IASB effective date	Year ending June 30, 2018	Half year ending June 30, 2018
Amendments to IFRS 2: Classification and Measurement of Share based Payment Transactions	Jan 1, 2018	Optional	Mandatory
Amendments to IFRS 4: Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts*	Jan 1, 2018	Optional	Optional *(As IFRS 9 is applicable from July 01, 2018)*
Amendments to IAS 40: Transfers of Investment Property	Jan 1, 2018	Optional	Mandatory
IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration*	Jan 1, 2018	Optional	Mandatory
Amendments to IFRS 1: Annual Improvements to IFRS Standards 2014-2016 Cycle	Jan 1, 2018	Optional	Mandatory
Amendments to IAS 28: Annual Improvements to IFRS Standards 2014-2016 Cycle	Jan 1, 2018	Optional	Mandatory

New pronouncement	SECP Effective date	IASB Effective date	Year ending June 30, 2018	Half year ending June 30, 2018
IFRS 9 *Financial Instruments*	July 1, 2018	Jan 1, 2018	Optional	Optional
IFRS 15 *Revenue from Contracts with Customers*	July 1, 2018	Jan 1, 2018	Optional	Optional

New pronouncement	SECP Effective date	IASB effective date	Year ending June 30, 2018	Half year ending June 30, 2018
IFRS 16 *Leases*	Jan 1, 2019	Jan 1, 2019	Optional	Optional
IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments*		Jan 1, 2019	Optional	Optional
Amendments to IFRS 9: Prepayment Features with Negative Compensation		Jan 1, 2019	Optional	Optional
Amendments to IAS 19: Plan Amendment, Curtailment or Settlement		Jan 1, 2019	Optional	Optional
Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures		Jan 1, 2019	Optional	Optional
Amendments to IFRS 3: Annual Improvements to IFRS Standards 2015-2017 Cycle		Jan 1, 2019	Optional	Optional
Amendments to IFRS 11: Annual Improvements to IFRS Standards 2015-2017 Cycle		Jan 1, 2019	Optional	Optional
Amendments to IAS 12: Annual Improvements to IFRS Standards 2015-2017 Cycle		Jan 1, 2019	Optional	Optional
Amendments to IAS 23: Annual Improvements to IFRS Standards 2015-2017 Cycle		Jan 1, 2019	Optional	Optional

New pronouncement	IASB effective date	Year ending June 30, 2018	Half year ending June 30, 2018
Conceptual Framework for Financial Reporting	Jan 1, 2020	Optional	Optional

IFRS issued not yet adopted by SECP

New pronouncement	SECP Effective date	IASB effective date	Year ending June 30, 2018	Half year ending June 30, 2018
IFRS 17 *Insurance Contracts*	Not yet notified by SECP	Jan 1, 2021	Not applicable	Not applicable

Exemptions from the application of IFRS

The exemption / waiver from the applicability of an IFRS is granted after its adoption by SECP.

The Companies Act empowers SECP and Banking Companies Ordinance 1962 empowers SBP to grant exemption/ waiver from the part or complete standard or IFRIC, in relation to the companies and banks, respectively.

Below table summarizes the status of not yet adopted IFRS and specific exemptions/ waivers:

IFRS issued and effective, however, not adopted by SECP	IFRIC Issued and effective, however, waiver granted	IFRS / IAS / IFAS Specific exemptions	IFRS / IAS / IFAS Specific exemptions
IFRS1 ***First-time Adoption of International Financial Reporting Standards*** (IASB efective date is 01 July 2009) **IFRS 1 requires an explicit and unreserved statement of compliance with IFRS,. This can only be achieved incase requirements of all IFRS are complied with.**	**IFRIC 4** ***Determining whether an Arrangement contains a Lease*** **Waiver granted by SECP to all companies through S.R.O 24(I)/2012 dated January 16, 2012**	**IFRS 7** **Eexemption by SECP to Banks and DFIs, through notification dated April 28, 2008**	**IFRS 2 Shared based payments** **Specific exemption granted by SECP to companies related to accounting of Benazir Employees' Stock Option Scheme (BESOS) , through S.R.O 587(I)/2011 dated June 7, 2011**
			IFRS 10 **Specific exemption by SECP to mutual funds, through S.R.O 56 (1) / 2016 dated January 28, 2016**
IFRS 14 ***Regulatory Deferral Accounts*** (IASB efective date is 01 January 2016) **IFRS 14 is an interim standard and applicable to first time adopter of IFRS. The final Standard is yet to be developed by IASB**	**IFRIC 12** ***Service Concession Arrangements*** **Waiver granted by SECP to all companies through S.R.O 24(I)/2012 dated January 16, 2012**	**IAS 40** SBP has deferred applicability to Banks and DFIs ((BSD Circular No. 10, dated August 26, 2002)	**IAS 21** **Specific exemption granted by SECP to power sector companies, through S.R.O 24(I)/2012 dated January 16, 2012**
			IFAS 3 SBP has deferred applicability to Islamic banking institutions (BPRD Circular No. 04 of 2015 dated February 25, 2015)

Notice to the readers

All reasonable care has been taken in the preparation of this publication, comprising the questions and suggested answers relating to the financial reporting under the Companies Act 2017. This publication is intended to provide only a general guidance on the topics covered and does not amend or override the Companies Act 2017, IFRS, IFRS for SMEs, AFRS for SSEs, other referred laws, regulations and standards, the text of which alone are authoritative. Further, it is not intended to be a substitute for reading the above mentioned /referred documents and other pronouncements, and a person should utilize his/her professional judgment, seek professional advice in consideration of the facts and circumstances involved in each particular case. The information presented in this publication should not be construed as legal, tax, accounting, or any other professional advice or service.

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