Nov 2019

PICG ADVISORY UPDATE-29

Pakistan Institute of Corporate Governance

The Update

Corporate governance refers to the way in which corporations are directed, administered, and controlled. It is concerned with both the relationship between internal and external stakeholders as well as the governance processes designed to help a corporation achieve its goals. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies as well as striking a balance between both economic and social goals and between individual and communal goals.

Compliance with applicable laws and regulations is fundamental to good governance. PICG's Advisory Update, therefore, aims at keeping our members updated with regards to the latest local and international governance-related changes to regulations, practices and corporate reporting.

The Update consists of a Summary Table (with links to relevant information) followed by a Synopsis of the changes.

A. Summary Table

Pakistan

Sr #	By	Reference	Date	Topic / Update link
1.	**Regulations/ Rules issued**			
i	SECP	S.R.O.1416 (I)/2019	Nov 20, 2019	General Takaful Accounting Regulations, 2019
ii	SECP	S.R.O.1417 (I)/2019	Nov 19, 2019	Draft Modaraba Regulations, 2019
iii	SECP	S.R.O.1415 (I)/2019	Nov 19, 2019	Corporate Rehabilitation Regulations, 2019
iv	SECP	Press release	Nov 12, 2019	Growth Enterprise Market Listing Regulations
v	SECP	S.R.O.1352 (I)/2019	Nov 11, 2019	Panel of Provisional Managers and Official Liquidators Regulations, 2019
vi	SBP	BPRD Circular No. 05 of 2019	Nov 1, 2019	Regulations for Digital On-Boarding of Merchants
vii	SECP	S.R.O.1306 (I)/2019	Nov 1, 2019	Corporate Restructuring Companies Rules, 2019

2. **Others**				
i	PSX	Press release	Nov 29, 2019	PSX agreement with SZSE for acquisition of Trading & Surveillance System
ii	SECP	S.R.O.1480 (I)/2019 S.R.O 1332(I)/2019	Nov 27, 2019 Nov 7, 2019	IFRS 14 – Regulatory Deferral Account application IFRS 9 - Financial Instruments - Applicability
iii	SECP	Press release	Nov 6, 2019	Concept Note for New Broker Regime
iv	SECP	Press release	Nov 5, 2019	Startup Portal for Tech Innovation in Pakistan

International

Topic	Links
World Bank Group Report - comparing business regulation in 190 economies	Doing Business 2020
OECD's report analyzing major economic trends and prospects	OECD Economic Outlook
EY Global's insights and data on the future of corporate reporting	Corporate Reporting Survey 2019

Changing the culture and mindset within an organization can help drive a more transparent corporate reporting agenda

- **Peter Wollmert**
(EY Global and EY EMEIA Financial Accounting Advisory Leader)

B. Synopsis of changes

Pakistan

1. Regulations/ Rules issued

Various rules and regulations have been notified by the Securities and Exchange Commission of Pakistan(SECP) and the State Bank of Pakistan(SBP) to streamline procedures, improve the ease of doing business and improve governance structures of companies in Pakistan. Following is a summary of significant Regulations / Rules (both drafts issued for public comments and final versions) issued during the month of November 2019 as notifications, circulars, drafts, etc., which have been placed on their respective websites:

a. Final Regulations/ Rules issued

Sr. no	Name	Description
i	General Takaful Accounting Regulations, 2019.	Applicable to regulatory returns and the published financial statements of Operators, including segment analysis and audit reports. ("Operator" means a Takaful Operator or a Window Takaful Operator, authorized by the Commission under the Takaful Rules, 2012, to undertake general takaful business) The Operators are required to comply with the requirements the of International Financial Reporting Standards(IFRS) adopted by the Institute of Chartered Accountants of Pakistan and the Islamic Financial Accounting Standards(IFAS), as notified by the SECP subject to certain specific provisions. The provision of Rule 19 of the Insurance Rules, 2017 pertaining to accounting and reporting, along with Annexure – II of the regulations and the provisions of the Insurance Accounting Regulations, 2017 shall not be applicable on a Takaful Operator; whereas the same shall stand applicable on a Window Takaful Operator to the extent of its conventional insurance business (modified to the extent stated in regulation 6 pertaining to the application procedure as an insurer in respect of its Window Takaful Business). The regulations shall come into force for accounting periods commencing on or after January 1 st , 2020.
ii	Corporate Rehabilitation Regulations, 2019	Issued under Section 41 of the Corporate Rehabilitation Act, 2018 (CRA) to facilitate the revival of distressed companies. It covers procedures for maintenance of a Panel of Insolvency Experts, manner of determination of remuneration of Insolvency Experts, and Code of Conduct for Insolvency Experts, etc. The CRA enacted last year aimed at providing companies facing bankruptcy with a legislative scheme to restructure their debts in order to return to productivity. Under the CRA, a company as specified in section 6 or qualifying creditor as defined in section 2(1)(q) thereof may file a petition in the High Court for order of mediation. The Court, after notice and hearing, may pass an order for appointment of insolvency expert (s) from a panel, maintained by SECP, to act as mediator for acceptance of a plan for rehabilitation filed by the company or the

		qualifying creditor. Accordingly, as required by the CRA, SECP has notified the Regulations to provide application procedure and eligibility/ineligibility criteria for persons who can apply to SECP for enlistment of their names in the panel of insolvency expert(s) maintained under section 5(1) of the CRA. Moreover, the regulations in terms of section 5 (3) of CRA also prescribe the code of conduct for insolvency expert (s), that requires such experts to act with integrity, independence and professionalism. The regulations take effect from Nov 19, 2019.
iii	Panel of Provisional Managers and Official Liquidators Regulations, 2019	As per Section 315 of the Companies Act, 2017: *'..For the purpose of the winding up of companies by the Court, the* ***Commission shall maintain a panel of persons from whom the Court shall appoint a provisional manager or official liquidator of a company ordered to be wound up****. A person shall not be appointed as provisional manager or official liquidator of more than 3 companies at one point of time..'* Consequently, SECP shall maintain a register of provisional managers and official liquidators which shall be available on the website of the SECP for public view.The regulation in this regard, therefore, sets out: a) The eligibility criteria for the Panel which includes: • Educational and Professional Qualification • Experience and affiliation b) Factors resulting in ineligibility c) Application procedure to obtain a spot on the Panel Note: Those persons who have already been appointed by the Court as Provisional Managers and Official Liquidators prior to these regulations shall be exempt from the requirments mentioned therein for the particular case that they were appointed for. The regulations came into force on Nov 11, 2019.
iv	Regulations for Digital On-boarding of Merchants	SBP has issued these regulations for Banks/MFBs in order to aid the growth of digital payment acceptance points in the country. The regulations shall facilitate Banks/MFBs to on-board small retail merchants and enable them to accept their payments digitally, thus providing new payment options to the consumers and broadening the financial inclusion base in the country.("Merchant on-boarding" means: process by which Banks/MFBs can open accounts of merchants to accept payments via digital means) The objectives of these Regulations are: a) To outline minimum due diligence requirements for on-boarding merchants based on simplified due diligence process. b) To facilitate in on-boarding merchants at various financial services access points and channels. c) To promote digital collection of payments from the sale of goods and services.

		Scope and Applicability: a) Applicable on Banks/MFBs, which may on-board individuals and self employed merchants as per their institutional risk assessment framework. b) Banks/MFBs shall formulate a merchant on-boarding policy in line with these regulations and ensure it is duly approved by their Boards. c) The regulations are not applicable on existing onboarding processes of full-fledged merchants and Banks/MFBs shall onboard full-fledged merchants as per applicable laws and regulations.
v	Corporate Restructuring Companies Rules, 2019	The Rules, notified in terms of section 15 of the Corporate Restructuring Companies Act 2016 with the approval of the federal government, provides information on the institutional arrangements and legal processes for revival and rehabilitation of potentially viable companies with an aim to turnaround the sick industry in Pakistan. The Act, 2016, defines a 'Corporate Restructuring Company' as: A public limited company licensed by the SECP to carry out the business of: a) acquisition, management restructuring and resolution of nonperforming assets of financial institutions; and b) restructuring, reorganisation, revival and liquidation of commercially or financially distressed companies and their businesses. Companies must obtain licenses as corporate restructuring companies according to the procedures laid out in the Rules. Required forms, documents and renewal procedures have also been mentioned therein.

b. Draft Regulations/ Rules issued

Sr. no	Name	Description
1	Draft Modaraba Regulations, 2019	In order to regulate and monitor the Modaraba sector , the SECP has proposed a new regulatory framework requiring certain minimum conditions on Modarabas for providing finance to their customers, limits in capital market, financial indicators of the borrowers and requirements for carrying out certain types of transactions. The draft regulations are laid out as follows: Chapter I - Definitions & Applicability Chapter II - Prudential Regulations Chapter III - Resource Mobilization Chapter VI - Miscellaneous Further, as part of the assessment of fitness and propriety, the directors or chief executive of the modaraba company shall not: (i) be a director in any other modaraba company engaged in a similar business in Pakistan (Note: this condition does not apply to nominees of the Federal or Provincial Govts on the board of any modaraba company); (ii) be a director, chief executive, chief financial officer, chief internal auditor, research analyst or a trader (by whatever name or designation called) in a stock brokerage house or in any company or entity owned and controlled by a member of securities exchange; and

		(iii) be a member of securities exchange engaged in the business of brokerage or is a spouse of such member or in control of more than 20% shareholding, directly or indirectly through his close relatives. (Note: conditions given in point (ii) and (iii) above, shall not apply to modarabas which are not involved in the issuance of certificates of musharakah). In case of key executives, the modaraba company must ensure that no key executive shall head more than one functional area that may give rise to conflict of interest within the organization. (For example, the departments of audit and accounts shall not be headed by the same person) Further, a key executive shall not hold directorship in his or her personal capacity: (a) in a business concern which is also a client of the modaraba, and (b) in any other financial institution.

c. Growth Enterprise Market Listing Regulations

SECP has approved the Growth Enterprise Market Listing Regulations to facilitate Small and Medium Enterprises (SMEs), Green field projects, Not for Profit and other companies that are aspiring to raise funds through capital markets but cannot fulfill the cumbersome conditions for listing on the Main Board of the Pakistan Stock Exchange (PSX).

In this regard, SECP has advised the Pakistan Stock Exchange (PSX) to arrange publication of new regulations to replace PSX's existing regulations governing listing and trading of equity securities of SMEs. Hence, in addition to the main board of PSX, the Growth Enterprise Market (GEM) will be a second board at PSX for listing and trading of equity securities. However, the trading screen for both boards will be same.

The GEM board also allows green field project and non-profitable companies to raise funds. Moreover, the companies listed on GEM board may graduate to the main board subject to the fulfillment of prescribed criteria, however, reverse migration is not allowed. In order to create liquidity on the GEM board, the concept of 'eligible investor' has been introduced and minimum lot size has been linked with the main board of the PSX, which is currently 500 shares. Eligible investor includes all institutional investors and eligible individual investors registered with National Clearing Company of Pakistan Limited (NCCPL) that have financial strength or expertise.

The post listing requirements of GEM board are also relaxed as compared to the main board such as non-applicability of code of corporate governance, submission of half yearly progress report as compared to quarterly progress report.

2. Others

a. PSX agreement with SZSE for acquisition of Trading & Surveillance System

Pakistan Stock Exchange (PSX), approved the execution of a contract with the Shenzhen Stock Exchange (SZSE) for the acquisition of a state-of-the-art 'Trading and Surveillance' System, to bring PSX at par with other international stock exchanges. Expected benefits of the SZSE trading system are built-in risk management, market access, market data dissemination, market control, real-time trading system, disaster recovery & system operation, monitoring and management, Growth Enterprise Market (so far known as Small and Medium enterprise trading), Bonds/Term Finance Certificate trading, single stock option trading, index option trading and real time fault-tolerant system.

A further additional interface is 'China Connec't which would give PSX access to the other Exchanges that SZSE is connected to (i.e. Shanghai and Hong Kong etc) thus, opening up the Asian market to PSX and Pakistan for business opportunities. Additionally, the improved data quality is expected to enhance PSX data vending potential and capability immensely.

SZSE is the world's 3rd largest Exchange in terms of trading value and has assured PSX of its continuous technical support as a strategic partner post-installation of this system. Both PSX and SZSE reaffirmed their commitment to technological cooperation which is expected to be helpful in elevating the image and standing of PSX vis a vis other developed exchanges around the world.

b. Application of IFRS 14 'Regulatory Deferral Accounts' & IFRS 9 'Financial Instruments'

The SECP has notified that the International Financial Reporting Standard (IFRS) 14 – "Regulatory Deferral Accounts" and any further revisions issued by the International Accounting Standards Board (IASB) shall be followed for the preparation of financial statements for the annual reporting periods beginning on or after 1st July 2019 by all classes of companies that are required by the Companies Act, 2017 to follow IFRS, as notified by the SECP.

Further, in partial modification of S.R.O. 229 (I)/2019, dated 14th February, 2019, the SECP has extended the effective date for applicability of IFRS on Financial Instruments (IFRS 9) in place of International Accounting Standard (IAS) 39 (Financial Instruments: Recognition and Measurement) for *Non-Banking Finance Companies* as: reporting period/year ending on or after 30th June, 2020 with earlier application being permitted, due to difficulties being faced by companies in its implementation. The IASB had issued IFRS 9 to be effectice from January 1, 2018 onwards, however, due to the expected credit loss approach introduced by the standard, major changes are required in the way the financial institutions assess the impairments of financial instruments due to which extension was requested.

The banking industry had also been requesting SBP to defer implementation of IFRS 9, hence, keeping in view of the importance of the Standard, the SBP advised the banking industry to carry out a quantitative impact assessment of IFRS 9 on their financials along with the assessment of their readiness of its implementation. In view of the impact assessment and stakeholders' representation, SBP decided that the effective date of IFRS 9 implementation for banks/DFIs/MFBs shall be January 1, 2021. Meanwhile, they have been advised to ensure meticulous compliance of certain instructions issued by SBP pertaining to proforma statements of financial poisiton etc.

c. **Concept Note for New Broker Regime**

The SECP has proposed a new brokers regime for stock market brokers with financial resource requirements via a concept paper which is said to be aimed at strengthening the brokerage industry, enhancing commercial viability of brokers, improving regulatory compliance and ensuring robust growth of the capital market.

The new regime divides brokers into three categories:

i. small-sized brokers (trading only brokers),
ii. trading & clearing broker, and
iii. trading & self clearing brokers.

The concept of "trading only brokers" has been introduced by the SECP for expanding investor base and draws attention to the issues faced by brokers in the current regime. The concept paper then goes on to highlight existing international practices and proposes a new regime stating the expected advantages along with the regulatory changes that would be required thereagainst.

The objective of the proposal has been stated as follows:

i. To strengthen the clearing members and custody participants in line with international best practices and to reduce the risk of clearing and custody defaults.

ii. Segregation of trading, clearing & settlement and custody functions of the broker so that brokers and institutions having prescribed financial resource requirements are only allowed to perform clearing function and hold custody of securities on behalf of clients.

iii. To expand market outreach through introduction of concept of the 'trading broker' so as to encourage new participants to start brokerage business at lower preliminary and operational costs.

The SECP also stated that in order to restore investor confidence, it is imperative that brokers have a sound system of internal controls and stringent compliance arrangements to prevent any misuse of client assets. Further, it is also important that such brokers are financially sound and meet enhanced capital adequacy requirements to prevent over indulgence, have the ability to absorb adverse market trends and contain the risk of institutional failure which is often the root cause of malpractices associated with unauthorized dealing of client assets and results in negative consequences for investors.

d. **Startup Portal for Tech Innovation in Pakistan**

SECP has launched a 'Startup Portal' to encourage tech innovation in Pakistan. The portal features a list of startups, simplified user experience for registration, access to mentors and incubation centres, online guides and video tutorials for Startup companies. The portal is intended to be a gateway to information and collaboration hub, for the facilitation and uplifting of existing and future entrepreneurs to connect and excel.

SECP stated that it has instituted various reforms to develop a comprehensive and coherent industry policy to shape regulatory thinking and promote a conducive Fintech environment in Pakistan to help attract local and international innovators. The SECP is also: reviewing the Companies Act with an objective to facilitate Startups and provide a conducive environment to young innovative entrepreneurs; making amendments to Private Equity and Venture Capital Regulations; drafting Equity Crowdfunding Regulations; setting up facilitation desks at CROs and launching the first ever regulatory Sandbox in Pakistan. Pakistan is the world's 26th biggest consumer market and its Startup sector reflects this appetite.

International

a. Doing Business 2020 – World Bank Group

Doing Business 2020, is a World Bank Group flagship publication, and the 17th in a series of annual studies measuring the regulations that enhance business activity and those that constrain it. The *Doing Business* report presents quantitative indicators on business regulations and the protection of property rights that can be compared across 190 economies—from Afghanistan to Zimbabwe—and over time.

The report covers 12 areas of business regulation. Ten of these areas—starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts, and resolving insolvency—are included in the ease of doing business score and ease of doing business ranking. The report also measures regulation on employing workers and contracting with the government, which are not included in the ease of doing business score and ranking.

By documenting changes in regulation in 12 areas of business activity in 190 economies, the report analyzes regulation that encourages efficiency and supports freedom to do business. The data collected addresses three questions about the government:

i. When do governments change regulation with a view to developing their private sector?
ii. What are the characteristics of reformist governments?
iii. What are the effects of regulatory change on different aspects of economic or investment activity?

The answers give an insight into the development in each country. The main findings of the report are:

- A total of 294 regulatory reforms were implemented between May 2018 and May 2019 worldwide, and 115 economies made it easier to do business.
- The economies with the most notable improvement are Saudi Arabia, Jordan Togo, Bahrain, Tajikistan, **Pakistan,** Kuwait, China, India and Nigeria. With reforms acknowledged ***in 6 areas i.e. starting a business, dealing with construction permits, getting electricity, registering property, paying taxes and trading across borders, Pakistan is ranked a number one reformer in South Asia and scored 6th position among the top ten reformers globally***. Out of six reform areas acknowledged in the report, the biggest jump of 58 points were recorded in 'Starting a Business'. (Expansion of online one-stop-shop facility through SECP's eServices to different federal and provincial agencies has reduced number of procedures required to set up a business from 10 to 5. Now an entrepreneur can get registration with 6 agencies i.e. SECP, NTN from FBR and registration with EOBI, PESSI/SESSI and labor department and excise and taxation department of Punjab and Sindh by submitting a single online application through SECP eServices).
- Economies in Sub-Saharan Africa and Latin America and the Caribbean continue to lag in terms of reforms.
- There is a steady convergence between developing and developed economies, especially in the area of business incorporation. Further, those economies that score well on 'Doing Business' tend to benefit from higher levels of entrepreneurial activity and lower levels of corruption.
- While economic reasons are the main drivers of reform, the advancement of neighboring economies provides an additional impetus for regulatory change.
- Twenty-six economies became less business-friendly, introducing 31 regulatory changes that stifle efficiency and quality of regulation.

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b. OECD Economic Outlook[1]

The OECD Economic Outlook is the OECD's twice-yearly analysis of the major economic trends and prospects for the next two years. The Outlook puts forward a set of projections for output, employment, prices, fiscal and current account balances and it covers all OECD member countries as well as selected non-member countries.

The current report includes a general assessment, a series of focus notes on selected macroeconomic and structural issues, and a chapter summarising developments and providing projections for each individual country.

The report states:

i. **The global outlook is unstable**
World GDP growth fell to 2.9% this year – its lowest rate since the financial crisis – and is expected to remain stuck at 3% over the next two years.

ii. **Governments must cooperate and invest to prevent prolonged stagnation**
- Urgent co-ordinated political action is needed to restore confidence, boost inclusive growth and raise living standards.
- Global trade is stagnating and is dragging down economic activity in almost all major economies.
- Policy uncertainty is undermining investment and future jobs and incomes. Risks of even weaker growth remain high, including from an escalation of trade conflicts, geopolitical tensions, the possibility of a sharper-than-expected slowdown in China and climate change.

iii. **What can governments do?**
- Invest now in infrastructure, in a greener future. Take advantage of low interest rates to boost public spending in infrastructure, stimulate private investment, and support a greener environment.
- Rethink policies to address the challenges of digitalisation and ageing.
- Stop distorting trade. Trade conflicts are creating uncertainty for businesses and are dragging down investment. Reduce subsidies which are at the heart of trade conflicts.
- Make the tax system fairer. Agree on transparent and equitable international taxation for the digital economy by 2020.

c. EY Global Corporate Reporting Survey 2019

The EY Global Corporate Reporting Survey 2019 is the Financial Accounting Advisory Services (FAAS) sixth global corporate reporting survey, in which more than 1,000 chief financial officers (CFOs) and financial controllers of large organizations were surveyed to understand the challenges they face in corporate reporting.

The report states that the 'trust' issue is critical in an environment where corporate reporting is under the regulatory spotlight. In a number of major markets, there is an increasing public, political and media focus on reporting, with a call for more robust regulatory oversight. This increased focus has followed a number of high-profile corporate failures and has raised questions around the emphasis auditors place on the going concern of a business, and also the forward-looking nature of corporate reporting. However, to really push the transparency agenda, a wider shift in attitude is required. Because corporate reporting has traditionally focused on historical financial data, the mindsets of those who produce it are far more aligned with focused, backward-looking financial reporting. Therefore,

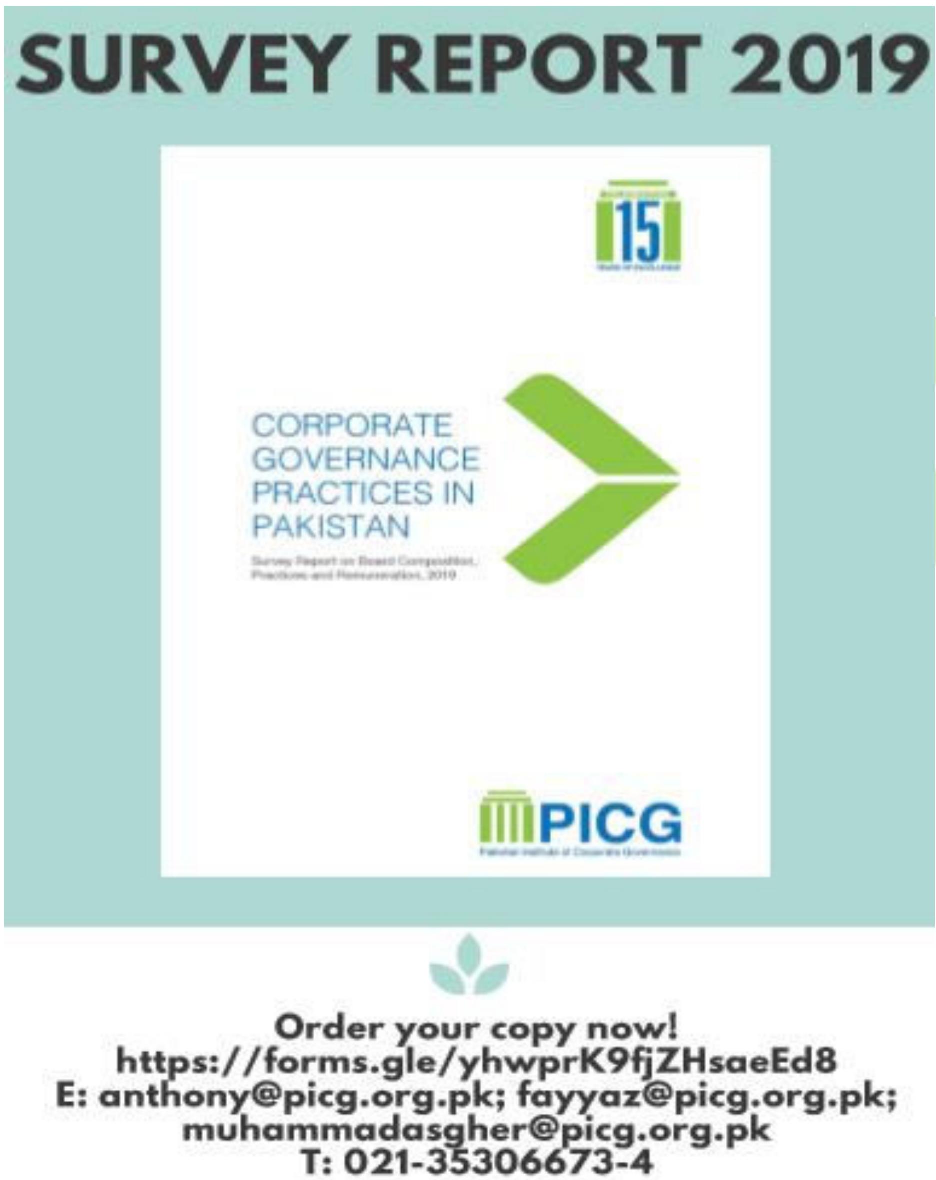
[1] OECD (2019), *OECD Economic Outlook, Volume 2019 Issue 2*, OECD Publishing, Paris, https://doi.org/10.1787/9b89401b-en.

transparent, forward-looking reporting – based on a wider balance between financial and nonfinancial information – requires changes not only to frameworks and practices but also to mindset and culture. In other words, a change of attitude is required if corporate reporting is to offer stakeholders open and transparent communication about value creation.

The abovementioned culture issue is the theme of this latest report. In earlier studies, finance leaders were focused on connected reporting, finance talent, finance operating model transformation, a rethink of traditional corporate governance models, and how to challenge the corporate reporting model by turning the huge volumes of data that organizations have at their disposal into a strategic reporting asset.

According to the study, organizations are now looking at their corporate reporting to genuinely engage with investors and other stakeholders. In other words, organisations are looking to a culture based on openness, authenticity and accountability. Hence, sorporate reporting can play an instrumental role in driving that culture — creating an environment where business and finance leaders are motivated to communicate and engage openly with core stakeholder groups.

The Pakistan Institute of Corporate Governance (PICG) has been the pioneer of Corporate Governance in Pakistan and while it continues to deliver highest standards of executive education, PICG over the years has also published quality research based papers, surveys and reports. In this regard, we are pleased to inform you that PICG's report on 'Corporate Governance Practices in Pakistan 2019', is now available. The report is based on a survey of Board Composition, Practices and Remuneration of over 130 companies in Pakistan and is an informative and comprehensive insight into the corporate sector of Pakistan.
You may place your orders for the survey via the link: https://lnkd.in/fNEB4jR



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