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“The current global environment is full of opportunities, but it poses unique challenges. SMEs need to adopt innovative approaches.”

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INDIA

Big March for SME

Changing business environment

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In keeping with recent and ongoing changes in the business landscape, business is focusing on mobility rather than stability, and the service business has evolved accordingly. Globalization is the buzzword as geographic boundaries cease to exist. Business is competing for opportunities in an international arena. Because the world is connected in a single unit, any crisis in one part of the world has repercussions in other parts, too.

Small and medium-sized enterprises (SMEs) play an important role in the world economy and contribute substantially to income, output and employment. SMEs are the growth engine for the emerging world economy, accounting for 85% to 90% of business population, 55% of private-sector value addition and 77% of private-sector employment. The contribution of SMEs to economic fundamentals varies substantially across countries: from 16% of GDP in low-income countries (where the sector is typically large but informal) to 51% of GDP in high-income countries. The BIG question is: are they equipped to grow in a changing business landscape with more cross-border opportunities emerging than ever?

The recent global financial crisis created a particularly tough climate for SMEs, reducing demand for goods and services and tightening the resources available from banks and other financial institutions. They face a challenging business environment includ-

ing changes in business, leadership and approach.

SME challenges

Globalization is a market force and an economic reality. Though constrained by the global financial crisis and ongoing recession in some countries, SMEs want to take part in international growth once recovery is fully underway. The challenges they face are many.

- Assessing various business risks: A globalized business world involves various risk factors including finance, market, credit, liquidity and technological uncertainties to name a few. Furthermore, fluctuations in raw material prices, exchange rate fluctuations, currency risk, different accounting and control systems and inflation pressure add to the uncertainty of success. Assessing these risks and addressing them in business strategy is essential for International business.
- Access to markets: Apart from physical barriers, foreign-market regulations are another barrier for small businesses. Most SMEs have no clue about these markets.
- Sub-optimal scale of operation: The scale of operation of small businesses generally does not satisfy global demand. To increase production, more capital infusion will be needed and capital availability is a challenge.
- Technological obsolescence:

Staying abreast of international standards, production practices and technology is vital in maintaining production capability and requirements.

- Supply chain inefficiencies: Productivity is very much dependent on the supply chain, and inefficiencies will lead to decreased profit margins.
- Funding shortages: Availability of funds is important for planning expansion, working capital requirements and other expenses. SMEs are often denied funds for new projects and products.

Implication of the challenges

While the current global environment is full of opportunities, it poses unique challenges for entrepreneurs and small and medium-sized businesses. To cope with these challenges SMEs need to adopt innovative approaches. This may require them to step out of comfort zones with real ambition.

Entrepreneurs hesitate to take the road to innovation because of the associated risk. The risk aptitude of SMEs is usually low and they look at direct and immediate benefits. In consulting they also need to have a more immediate tangible outcome rather than directional advice for managing risks. Ready availability of finance can be an approach which will help them to take up challenging projects, but understanding the associated risks and mapping them is fundamental yet at times overlooked.



This has given rise to a knowledge-based economy, with knowledge being the most important resource and learning the most important process. Competitive advantage lies in the ability to generate new ideas and transform them into economic and social value. Access to physical resources by enterprises comes only after this. Competitiveness lies in the ability to use knowledge to improve performance, which leads to innovation. This is the driving force behind expanding global SMEs. The knowledge-based economy requires resources with the right skills. Building various functional skills including sales, marketing and communications is critical. Improvements in processes require innovative ideas. All these need the right leadership to take on the changing challenges. Choosing the right talent for

each of the different resources is very essential, and providing them with need-based training with changing trends in the market is equally important. Existence of a formal procedure and discipline is very important for an enterprise to function smoothly and even more critical for small and medium enterprises. Furthermore, there is a tendency for these procedures to change frequently. This makes it difficult for a third party or a newcomer to understand the existing business practices. Bringing in a process and functional approach is absolutely essential to establishing credibility when pitching to new clients.

Staying up to date with the latest technology is critical in the digitized world. Providing the systems with IT support is vital as they reduce redundancy and improve performance; with social media they can transform the concept of reach and communication to stakeholders. Leveraging the digitally connected world is a challenge as they require clear understanding and focus, and management might not understand the need to invest in this. SME management might require the use of information technology in day-to-day management and accordingly train employees to improve efficiency.

The Big March™

An approach which can prepare a business to understand the elements of next flight; there is no magic pill for growth, but simple elements like understanding the real value of their efforts, defining success in the business, the valuation of enterprise, sustainable elements can unleash their own growth path.

A deep understanding of business objectives or intent, well-defined resource strategy, efficient work systems to get things done, and talent that builds a growth ecosystem is the bedrock of BIG MARCH. **B**usiness Intent, **G**rowth through Systems, **M**arshalling Resources and **C**hannelizing talent.

A focused business intent will help develop a strong strategy with the required resources and create an ecosystem for the talent involved. Establishing a system and processes coupled with the right resource tapping will help SMEs reach their goals in the ever-evolving business landscape.

The workshop series around the 4 Pillars can help ECOVIS to position itself not as an accounting or law office but as a consulting powerhouse, helping clients to grow and work as partners of choice in a Financial, Legal, Accounting and Consulting space.

Tip

Read more about the opportunities for professional services online:

www.ecovis.com/en/category/global-newsletter/02-2015



“The objective of Broad Based Black Economic Empowerment is to correct inequalities stemming from apartheid. It has a real impact on business.”

Rossouw Pieterse CA (SA), ECOVIS ARB Auditors Inc., South Africa

SOUTH AFRICA

Why BBBEE is important for business

The legislation Broad Based Black Economic Empowerment (BBBEE) has an impact on business. It is intended to be temporary in scope.



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The objective of BBBEE is to correct inequalities that were placed on the population in the past through apartheid. Due to the lack of opportunities in terms of the education and skills development given to the previously disadvantaged groups the poverty gap has grown significantly and it is difficult to find a balance of economic participation. BBBEE is intended to stimulate the process of participation of previously disadvantaged groups in the economy to lead to increased economic growth.

When the new Constitution was adopted, a provision was made that government tenders must take black-owned entities into consideration.

The Preferential Procurement Policy Framework Act was then written and promulgated. This led to the implementation of Black Eco-

nomics Empowerment in 2003. The focus of the policy was to give ownership in companies to previously disadvantaged groups. The method was flawed and only a small group of people benefited. Following this, Broad Based Black Economic Empowerment was formed and implemented in 2007. BBBEE comprises a scorecard with 5 elements (May 1, 2015). Companies are awarded points for each of the 5 elements to establish a total score out of 109. Based on the score, you obtain a certain level. Level 1 is very compliant while level 8 is non-compliant. Unlike the previous legislation, the new codes focus on all requirements to uplift economic participation and include socio-economic development, supplier development, enterprise development, skills development, employment equity and management control.

You have to be BBBEE compliant to be able to do business in South Africa. One of the 5 elements of the BBBEE scorecard is preferential procurement and supplier development. This is the element that carries the most weight (nearly 40%). If you procure from other entities that are BBBEE compliant your BBBEE score increases. One can see the trickledown effect from suppliers to government down to their suppliers. Once again the goal is to try and achieve a level 4 as this gives you 100% contribution towards preferential procurement. To address differences among

different types of entities they are placed into 3 categories.

- The first is Exempt Micro Enterprises (EME). This represents entities with an annual revenue of less than R10 million. If you fall in this category you will be awarded as a Level 4 contributor.
- The second category is Qualifying Small Enterprises (QSE). This represents entities with an annual revenue of between R10 million and R50 million. In the new codes QSEs need to comply with all 5 elements and at this stage the advantages of a QSE is not clear (prior to May 1, 2015, they only needed to comply with 4 out of 7 codes).
- The third category is Generic Entities; it represents all entities with an annual revenue of more than R50 million. These entities need to comply with all the elements of the BBBEE scorecard.

It is very important to be aware of BBBEE when doing business in South Africa. It is a unique piece of legislation and very important for economic growth in the country. Businesses need to embrace BBBEE to become successful. Planning ahead is vitally important to obtain the required level.

Please contact Rossouw from ECOVIS ARB Auditors Inc. regarding any further details on BBBEE or to obtain more information on how we can assist you with BBBEE-related services.



“As a result of the 2015 Japanese Tax Reform, the consumption tax – similar to VAT or GST – now applies to cross-border digital services.”

Yoshiaki UNO, ECOVIS XAT Tax Corporation, Japan

JAPAN

Revision of the Japanese Consumption Tax

The 2015 Tax Reform Package was passed by the National Diet on March 31, 2015. The Tax Reform contains a new imposition of the Japanese consumption tax on cross-border digital services provided on or after October 1, 2015, by overseas service providers to customers in Japan. The Japan Consumption Tax is similar to VAT or GST in various other countries.

The key changes at a glance:

Scope of digital services

- Digital services subject to the new taxation include distribution of e-books, music, and advertising. Digital services also include cloud services and the licensing of copyrights by overseas license holders.
- International telephone communication services and services where the main transaction is the transfer of goods or tangible assets are excluded from these digital services.
- Under the revised law, the cross-border digital services are deemed to be provided in Japan where their customers are located.

How consumption taxes are collected from customers and delivered to the Japanese government

→ Provision of B-to-B digital services

Reverse charge mechanism for consumption tax will be implemented for B-to-B digital services, where parties in Japan receiving digital services from overseas service providers in connection with the parties' business have an obligation to pay and deliver to the Japanese government the consumption tax on digital services. For such parties in Japan, consumption tax paid on digital services can be counted as consumption tax eligible for consumption

tax credit when they file and pay consumption tax received from their customers on sales or services in Japan.

→ Provision of B-to-C digital services

All digital services provided by overseas service providers other than B-to-B digital services will be classified as B-to-C digital services. Digital services provided to both business parties and individual consumers will be classified as B-to-C digital services unless the services are definitely provided only to business parties because of the nature of the services or the service contract. Any B-to-C digital service provider will be obligated to pay consumption tax to the Japanese government. The registration system for overseas service providers will be implemented on or after July 1, 2015. For business parties in Japan, consumption tax paid to registered overseas provider for digital services can be counted as consumption tax eligible for a consumption tax credit.

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Other details

There are exceptions and further details which will be provided to overseas providers.



“Change to accounting framework used by SMEs in Malaysia effective financial year 2016 will require early and informed preparation.”

Eileen Lim, ECOVIS AHL, Malaysia

MALAYSIA

Transition to MPERS

Practical changes to be implemented as early as 2015.

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Small and Medium Enterprises (SMEs), touted as the backbone of the Malaysian economy due to the size of their contribution, have become the focus of hope to lead Malaysia to high-income nation status by 2020¹. By 2020, SMEs will be the key driver of growth, contributing 42% to the nation's gross domestic product, employing 63% of the country's workforce and making up 25% of Malaysian exports².

With plans ready to push SMEs to the economic forefront through the SME Masterplan 2012-2020, regulators' eyes are on the sophistication, relevance and sufficiency of the financial reporting practices of these entities to supply the needed information. The current Private Entities Reporting Standards (PERS), based on pre-2003 International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB), have not been updated since being issued between 1999 and 2004.

In February 2014, the Malaysian Accounting Standards Board (MASB) announced that all private entities shall apply the new accounting framework, the Malaysian Private Entities Reporting Standards (MPERS), in their financial statements beginning on or after January 1, 2016. The MPERS is the word-for-word version of the IFRS for SMEs issued by the IASB with the exception of the requirements on income tax and property development activities and a few terminological chang-

es. Alternatively, private entities may choose to apply the International Financial Reporting Standards (IFRS)-compliant Malaysian Financial Reporting Standards (MFRS). The latter requires more fair-value based reporting for assets and liabilities and robust financial statements disclosure.

Application of MPERS and MFRS is retrospective and requires early preparation so that financial information is available on the date of transition to the new framework or MFRS. The earliest date of transition is January 1, 2015.

Differences between PERS and MPERS are few. MPERS uses more cost-based models to measure assets and liabilities, and where fair value measurement is applicable it is only necessary if the fair value can be measured reliably without undue cost or effort, or it remains an option. In spite of this, preparation for transition to MPERS should begin as early as the date of transition to MPERS in several areas of accounting. This article discusses the pertinent areas.

Financial instruments

Entities on the PERS framework since inception are not exposed to the concept of financial instruments. MPERS introduces Section 11 Basic Financial Instruments and Section 12 Other Financial Instruments Issues (these are the specific fair value accounting standards not seen in PERS) to recognize, derecognize, measure and disclose financial assets and liabilities.

Section 11 Basic Financial Instruments: Examples of financial instruments are cash, demand and fixed deposits, receivables, payables, investments in preference shares and ordinary shares, bonds and similar debt instruments and commitments to receive a loan.

Financial assets and liabilities are recognized initially at transaction costs, except for financing transactions, where financial instruments are measured at present value of future payments discounted at market rate of interest for a similar debt instrument. Examples of financial instruments that are financing arrangements are long-term loans made to another entity, goods or services sold to customers beyond the normal interest-free credit period and loans received from a bank.

On the date of transition and on every subsequent reporting date, financial assets are measured at cost less impairment, except that investments in shares which are publicly traded or where their fair value can be determined reliably are measured at fair value through profit or loss.

Unless an entity adopts MPERS ahead of the mandatory effective date, the above financial instruments need not be recognized or remeasured at fair value before the financial year beginning on or after January 1, 2016.

Section 12 Other Financial Instruments: Derivative instruments (for example options, swaps, futures and forwards) are off-balance sheet items under PERS.

¹ *New Economic Model*

² *SME Masterplan 2012-2020, Role of SMEs in the Economy*



On the date of transition, entities must obtain market prices (which may be more conveniently available on or near the date of transition) to measure the derivative contracts at fair value through profit or loss and recognize the fair value difference between contract date and date of transition in profit or loss. Subsequently derivative contracts are measured at fair value through profit or loss at each reporting date.

Inventories

MPERS has disallowed the last in, first out (LIFO) method for determining inventory costs. The standard cost method, retail price method or most recent purchase price for measuring the cost of inventories is allowed if result approximates cost.

Entities applying the LIFO cost formula must recalculate inventory costs on the date of transition based on a permissible cost formula (for example first in, first out (FIFO) or weighted average). Doing this would go a long way to facilitate migration to a non-LIFO method of inventory costing in financial year 2016 (and eliminate substantially the pain of recalculating costs of inventory sold in the first year of adopting MPERS).

Entities must be prepared to assess potential impairment on inventory where the carrying amount is not fully recoverable at each reporting date, commencing on the date of transition.

Investment property

Under PERS, fair value changes on investment properties carried at revalued amounts are only recognized in revaluation reserve. Entities adopting MPERS can now measure investment properties at fair value through profit or loss if fair value can be determined reliably. Market value in property valuation report (at, or before date of transition) can be designated as deemed cost at the valuation date.

Share-based payments

Entities shall record the previously off-balance sheet share-based payments (in the form of shares or share options) to employees at fair value of services received on grant date or, if there are vesting conditions, during the vesting period. If fair value cannot be estimated reliably, the value of share-based payments can be measured by reference to fair value of equity instruments granted. Exemptions are available to first-

time adopters of the MPERS from the need to apply Section 26 Share-based Payment to equity instruments that were granted before the date of transition to MPERS, or to liabilities arising from share-based payments that were settled before the date of transition.

Conclusion

The transition period from PERS to MPERS can be less arduous if accountants are well prepared with technical know-how, migration plans and staff capacity. Starting early and working steadily (at a minimum on areas mentioned in this article) is a key to successful adoption of MPERS with minimal stress, time and costs.

The more robust financial reporting with adoption of MPERS will contribute to enhancing the quality, transparency and comparability of private entities globally and improve their accessibility to finance locally and globally. With the benefit of hindsight, accountants can take advantage of opportunities to unlock value in the entity through adoption of MPERS should the entity decide to go public.

ⁱ A private entity defined according to MPERS Section 1 is a private company incorporated under the Companies Act, 1965, that is not required to prepare or lodge its financial statements to the Securities Commission or the Central Bank of Malaysia and is not a subsidiary, associate or joint venture of an entity required to prepare or lodge its financial statements to the Securities Commission or the Central Bank of Malaysia.

ⁱⁱ Private entities prepare their first set of MPERS-compliant financial statements for financial year beginning on or after January 1, 2016. Comparative information for financial year 2015 shall be restated for comparability. An entity may present comparative information in respect of more than one comparable period. However, impact of changes to accounting policies arising from application of the MPERS must be shown on the date of transition to MPERS which is the beginning of the earliest comparative period presented i.e. the first day of the comparative period. Date of transition to MPERS for private entities of December 31 year-end is January 1, 2015.

Tip

To read more detailed information about biological assets and agricultural produce check out our homepage www.ecovis.com/en/category/global-newsletter/02-2015

ABOUT ECOVIS

Ecovis is a leading global consulting firm with its origins in Continental Europe. It has over 4,500 people operating in over 50 countries. Its consulting focus and core competencies lie in the areas of tax consultation, accounting, auditing and legal advice. The particular strength of Ecovis is the combination of personal advice at a local level with the general expertise of an international and interdisciplinary network of professionals. Every Ecovis office can rely on qualified specialists in the back offices as well as on the specific industrial or national know-how of all the Ecovis experts worldwide. This diversified expertise provides clients with effective support, especially in the fields of international transactions and investments – from preparation in the client's home country to support in the target country. In its consulting work Ecovis concentrates mainly on mid-sized firms. Both nationally and internationally, its one-stop-shop concept ensures all-round support in legal, fiscal, managerial and administrative issues.

The name Ecovis, a combination of the terms economy and vision, expresses both its international character and its focus on the future and growth.

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