

REPORT ON THE OBSERVANCE OF STANDARDS AND CODES (ROSC) MOZAMBIQUE

ACCOUNTING AND AUDITING

June 16 2008

Contents

Executive Summary

Preface

Abbreviations and Acronyms

I. Introduction

II. Institutional Framework

III. Accounting Standards as Designed and as Practiced

IV. Auditing Standards as Designed and as Practiced

V. Perception of the Quality of Financial Reporting

VI. Policy Recommendations

Appendix-1: Tentative Action Plan Matrix

Executive Summary

This report provides an assessment of the strengths and weaknesses of the existing financial reporting infrastructure that underpins financial accounting and auditing practices in Mozambique. The assessment focuses on six pillars of financial reporting infrastructure: statutory framework, professional education and training, accountancy profession, accounting standards, auditing standards, and monitoring and enforcement of the applicable standards. The main purpose of this assessment is to assist the development and implementation of a country action plan for strengthening institutional capacity with attendant effect on enhancing corporate financial reporting in Mozambique.

All the corporate entities in Mozambique, including investments with foreign participation, are affected by a serious shortage of qualified accountants and trained accounting technicians. Best estimates are that there are less than 50 fully qualified accountants working in Mozambique (mostly in the Maputo area), and that of these only 2 are citizens of Mozambique. Most of the corporate financial statements in the country are therefore prepared by *accounting technicians* whose level of skill and training is variable. At one extreme, a limited number of accounting technicians have completed training, which has not prepared them nearly at the level of a qualified accountant; and at another extreme, many technicians have no formal training. Most of the financial statement audits in the country are primarily carried out by representatives of the 6 international networks. The lack of senior-level local staff within those networks is of concern particularly as regulators lack any capacity to monitor the quality of financial reporting.

Based on significant inputs from in-country stakeholders, this ROSC makes recommendations for improving the statutory framework; building a strong professional accountancy body with the assistance of a reputed member of the International Federation of Accountants (IFAC); taking legally backed steps for mandating and disseminating International Financial Reporting Standards (IFRS) for public-interest entities and simplified financial reporting standards for small and medium enterprises; putting in place a sustainable arrangement for monitoring and enforcing application of IFRS and International Standards on Auditing (ISA); providing assistance to the small and medium practices to strengthen capacity to operate as modern audit firms; facilitating broader training programs on practical application of IFRS and ISA; and improving accountancy curriculum and teaching in higher educational institutions.

The recommendations contained in this ROSC offer the groundwork for preparing a country action plan aimed at building institutional capacity to promote high quality accounting and auditing practices in Mozambique.

PREFACE

Reports on Observance of Standards and Codes (ROSC) is a joint World Bank and International Monetary Fund (IMF) initiative that helps member countries strengthen their financial systems by adopting internationally recognized standards and codes. The overall goal of the ROSC program is promoting greater financial stability in national financial systems and thereby reducing the potential for disruptions in national, regional, and international financial markets; and laying essential foundations for sustained and higher rates of economic growth and the reduction of poverty and income inequality.

The ROSC involves preparation of reports in twelve key areas.¹ The ROSC Accounting and Auditing (ROSC A&A) review exercise evaluates a country's accounting and auditing standards and practices using as benchmarks the International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA). It also uses international good practices as reference points for assessing the strengths and weaknesses of the institutional underpinnings of the accounting and auditing regime of a country. The ROSC A&A focuses on the corporate financial reporting infrastructure that supports high-quality accounting and auditing practices in a country. Important pillars of the financial reporting infrastructure are statutory framework, accounting profession, accounting education and training, accounting standards, auditing standards, and monitoring and enforcement of applicable accounting and auditing requirements.

The ROSC A&A was carried out in Mozambique between November 2007 and February 2008 through a participatory process involving various stakeholders. The stakeholders include the Ministry of Finance, the Bank of Mozambique, the University of Eduardo Mondlane, the Office of the Inspector General of Finance, the Department of Taxes, leading audit firms, banks, insurance companies, state-owned enterprises, nongovernmental organizations, accountants, lawyers, and academics.

The Mozambique ROSC A&A was prepared by a World Bank team comprising M. Zubaidur Rahman, Program Manager (OPCFM); Jonathan Nyamukapa, Senior Financial Management Specialist, Task Leader (AFTFM); and Ludovic Kabran, Senior Operations Officer (AFTFM).

¹ The twelve ROSC areas are data transparency, fiscal transparency, monetary and financial policy transparency, banking supervision, securities, insurance, payment systems, anti-money laundering and combating financial terrorism, corporate governance, accounting, auditing, and insolvency and creditor rights.

ABBREVIATIONS AND ACRONYMS

| | |
|----------|---|
| ACCA | Association of Chartered Certified Accountants |
| AMAI | <i>Associação Moçambicana de Auditores. Internos</i> (Association of Internal Auditors in Mozambique) |
| GDP | Gross domestic product |
| IAS | International Accounting Standards (included in IFRS) |
| IASB | International Accounting Standards Board |
| IASC | International Accounting Standards Committee |
| IFAC | International Federation of Accountants |
| IFRS | International Financial Reporting Standards (including IAS) |
| IIA | Institute of Internal Auditors (United States) |
| IMF | International Monetary Fund |
| ISA | International Standards on Auditing |
| NGO | Nongovernmental organization |
| PGC | <i>Plano Geral de Contabilidade</i> (Standardized Chart of Accounts) |
| ROSC A&A | Report on the Observance and Standards of Codes, Accounting and Auditing |

I. INTRODUCTION AND BACKGROUND

1. This Report on Observance of Standards and Codes Accounting and Auditing (ROSC A&A) is a review of accounting and auditing practices and institutions underpinning the accounting and auditing environment in the Mozambique corporate sector. The review draws on international good practices and makes policy recommendations aimed at improving the quality of financial reporting in the country. An overview of the ROSC A&A and the detailed presentation of methodologies are available on the World Bank Group website.¹

2. Through the ongoing Mozambique Public Sector Reform Project, the Government of Mozambique has taken steps to develop a professional accountancy body known as the Order of Accountants in Mozambique. The Government has issued a decree to facilitate the establishment of the Order. In addition, the Government of Mozambique is using the World Bank-supported Financial Sector and Technical Assistance Project to facilitate introduction of International Financial Reporting Standards (IFRS) into corporate reporting with a structure and requirements for banking sector reporting in compliance with IFRS effective January 2008 and other corporate entities expected to follow IFRS compliance in 2009.

3. This ROSC complements existing efforts by producing a holistic evaluation of all necessary pillars required for a strong financial reporting infrastructure. The ROSC makes the necessary recommendations for ensuring a well-coordinated approach going forward. Mozambique needs to develop institutional capacity for supporting high-quality accounting and auditing practices in both private and public sectors as well as an effective arrangement for accountancy education and training.

4. The ROSC assessment focuses on the strengths and weaknesses of the prevailing accounting and auditing practices that influence the quality of corporate financial reporting. The ROSC uses IFRS² and International Standards on Auditing (ISA)³ as benchmarks and draws on international experience and good practice in the field of accounting and auditing regulation. The ROSC used a diagnostic template developed by the World Bank to facilitate data collection. The data was complemented by the findings of a due diligence exercise based on a series of meetings with key stakeholders conducted by World Bank staff. The intended audience includes national and international market participants who have an interest in the corporate financial reporting regime of Mozambique.

5. At its independence in 1975, Mozambique was one of the world's poorest countries. Economic mismanagement has been exacerbated by a brutal civil war from

¹ www.worldbank.org/ifa/rocs_aa.html

² IFRS are issued by the International Accounting Standards Board, an independent accounting standard-setter based in London, United Kingdom. In April 2001, the IASB announced that it would adopt all of the International Accounting Standards issued by the International Accounting Standards Committee. In this report, the term IFRS also refers to IAS.

³ ISA are issued by the International Auditing and Assurance Standards Board of the International Federation of Accountants.

1977-92. Starting in 1987, the Government of Mozambique embarked on a series of macroeconomic reforms designed to stabilize the economy. These steps, combined with donor assistance and political stability since the multi-party elections in 1994, have led to dramatic improvements in the country's growth rate. Now with a population of 20.9 million, Mozambique has seen its real GDP growth since 1993 averaging 8.1 percent while inflation has decreased from more than 50 percent in the mid-1990s to between 5 percent and 7 percent in the first semester of 2007.

6. Much of Mozambique's impressive growth rate can be attributed to foreign-financed projects and large aid inflows. The Mozal Aluminum Smelter and SASOL Natural Gas projects have played a major role in employment generation and increasing trade opportunities. Mozal in particular has significant downstream effects for the economy through the creation of supplier and service companies. Other major projects include the Moma Titanium Mine and Smelter south of Nacala, the Moatize Coal Fields, the Corridor Sands Titanium project in Gaza, and the oil refinery project on the Nampula coast. There are a total of 12 commercial banks in Mozambique, most owned by or linked with international financial institutions. The financial sector faces relatively high regulations by the Bank of Mozambique.

7. An additional spur to the economic growth has been the creation of spatial development corridors. The Maputo Development Corridor, a joint venture among the Governments of South Africa and Mozambique and private companies and banks has boosted the Port of Maputo and attracted more than US\$3 billion in investment. In 2006, the Investment Promotion Center issued 147 new investment authorizations representing about US\$848.3 million. These new investments are expected to create 19,372 new jobs.

8. The official language in Mozambique is Portuguese. Some foreign-owned companies prepare and present financial statements in both Portuguese and English languages to facilitate consolidation into the results of their English-reporting parent companies.

II. INSTITUTIONAL FRAMEWORK

9. The ROSC outlines legal principles applicable with regard to accounting, auditing, and financial reporting. Primarily an introduction to the issues, the ROSC is neither meant to be an exhaustive rendition of the law nor to give legal advice.

II.A Statutory framework

10. **Mozambique introduced a new Commercial Code in 2006 replacing business legislation dating from 1888.** According to the new Commercial Code of Mozambique, an incorporated company may take the form of a private limited liability company (*Sociedades Limitadas*) referred to as *Limitadas*, which may be formed by at least two members; or a public limited liability company (*Sociedades Anônimas*) referred to as *SA*, which requires at least 10 members and compliance with additional legal requirements. The vast majority of incorporated business enterprises in Mozambique are *Limitadas*. Although the new Commercial Code introduces some corporate governance rules and

strengthens the rights of minority shareholders, it does not include provisions in line with international good practice regarding accounting, auditing, and financial reporting by the corporate entities.

11. The provisions of Commercial Code regarding accounting and auditing lag behind international good practices. The Commercial Code makes reference to the books of account that a company must keep. The concepts of preparing and auditing financial statements are absent from the Code. The Code requires that companies keep books that record daily balances and inventories by using a standardized Chart of Accounts. There is no mention of accounting standards. Further, the Code does not make reference to auditing requirements, auditing standards, and qualification of statutory auditors. The statutory accounts of all business enterprises in Mozambique must be signed by an accounting technician (*Technico de Conta*) who is specifically authorized by the Ministry of Finance to sign such enterprise accounts. In addition, the accounting technician is required to prepare a supporting report on the applied accounting principles. Management representatives are also required to approve the financial statements.

12. Tax reporting requirements heavily influence corporate financial reporting. The Commercial Code states that companies are obliged to maintain organized accounting records under the terms of the Commercial Code and the Corporate Tax Law and requires that the records are organized in accordance with the *Plano Geral de Contabilidade* (standardized Chart of Accounts) referred to as PGC. However, the Code does not mention any penalties for PGC noncompliance. The Commercial Code states that companies must produce an annual return providing annual tax and accounting information and that this return must be submitted to the Tax Office. The accounting system in Mozambique is thus a codified system designed to be PGC compliant. The PGC in force was introduced by Decree No. 36/2006 on July 25, 2006. This replaced the old Chart of Accounts issued in 1984. The PGC dictates the categories of accounts, and all companies are obliged to comply with those categories. Article 108 of the Corporate Tax Law issued in 2006 specifies the accounting obligations of companies.

13. The Corporate Tax Law reaffirms the need for accounting records to be organized in accordance with the PGC. The Tax Law adds that all accounting entries must be supported by documentary evidence. The Tax Law states that the accounting records must be retained for 10 years and defines the dates and timing for the filing of annual accounting reports and tax returns with the tax authority. A revision of the Corporate Tax Law by Decree 34/07 on December 31, 2007, prescribes a penalty of 35 percent for any undocumented expenditure entered into the accounting records. Undocumented expenditure normally means invoices that do not comply with the terms of the Value Added Tax (VAT) Law. For tax purposes, depreciation is governed by a legislative requirement set in 1967 outlining the various depreciation rates to be adopted by companies. In spite of the fact that these depreciation rates are not based on the useful lives of assets, the companies are required to follow these rates for both tax reporting and general purpose financial reporting purposes. For general purpose financial reporting by corporate entities, the application of tax-oriented depreciation rates and other tax

accounting requirements contradict international good practice, including IFRS requirements.

14. **The Commercial Code requires that public limited liability companies (the SA) have a special body with supervisory and monitoring functions, called *conselho fiscal* or fiscal council.** The fiscal council is independent from management and the board of directors. It has broad powers and responsibilities, including supervising management and the board and issuing opinions on corporate transactions. The fiscal council is viewed as an important vehicle for protecting the interests of minority shareholders. However, its effectiveness largely depends on its members' knowledge of financial management and capability to proactively monitor the impacts of key decisions that benefit only the controlling shareholders. The fiscal council is required to ensure that the company's books of accounts are in order, verifying the accuracy of the annual accounts, and confirming the valuation criteria adopted in accounting and financial reporting. The fiscal council also has the responsibility of recommending to the shareholders the approval of the annual financial statements.

15. **Although the Commercial Code does not mention any requirement on preparation and presentation of audited financial statements, selected entities are required to have an annual audit.** An explanatory note issued by the Government after promulgation of the Law on Auditing in 1990, states that the Ministry of Finance would notify a company if it is required to have an annual audit. There is no mention of the criteria that the Ministry of Finance must follow for determining whether or not a company would need to have an audit. In accordance with requirements of other laws, generally all companies with foreign participation are required to prepare and present annual audited financial statements.

16. **There are legal requirements for auditing financial sector entities.** Issued in 2001, a legal requirement governing the audit of credit institutions and finance companies states that auditors of credit institutions and finance companies should have sufficient technical capacity, banking specialization, and specialized banking training for their staff. And audits should be performed in accordance with ISA. The credit institution and finance companies must apply to the Bank of Mozambique (the Central Bank) for approval of their external auditor within 30 days after the auditor has been selected. Up to now, the Bank of Mozambique has approved 5 auditing firms to conduct these audits. The legal requirement also outlines conflicts of interest between the auditor and the auditee, and specifies that an auditor (audit firm) should not audit the same credit institution or finance companies for more than 5 consecutive years.

17. The Credit Institutions and Financial Companies Law promulgated in 1999 requires banks to adopt a bank-specific Chart of Accounts. This Chart of Accounts requirement came by way of an *Adviso* (Notice) from the Governor of the Bank of Mozambique and forms part of the 1999 Credit Institutions and Financial Companies Law. Subsequently, the Bank of Mozambique issued *Adviso* No. 4/GBM/2007 in 2007 mandating the banking sector to prepare their financial statements in accordance with IFRS effective after December 31, 2007. In circumstances where the preparation of

financial statements in accordance with the Mozambican Banking Chart of Accounts leads to noncompliance with the applicable IFRS, it is unclear which requirement would prevail.⁴ The banks are required to submit their annual audited financial statements to the Bank of Mozambique by May 31 of each year. In addition the banks must file half-yearly unaudited financial statements with the Bank of Mozambique. The micro finance institutions are regulated by the Bank of Mozambique under its Decree No. 57/2004 to regulate micro-credit activities (replacing Decree No. 47/98); and are not required to prepare and present annual audited financial statements in compliance with the IFRS requirements.

18. The listing rules of the Mozambique Stock Exchange do not mandate the use of IFRS or any other financial reporting standards. The Mozambican Stock Exchange was set up in 1999 and is regulated by the Bank of Mozambique. The Exchange is predominately a bond market with 13 separate bonds issued from the government sector and the corporate sector. Only one company has shares listed on the Mozambique Stock Exchange.

19. The legal framework governing the insurance industry does not specify any requirement on financial reporting in compliance with IFRS or any other standards. Insurance companies are regulated under the Insurance Law (Law 3/03), and the Insurance Law Regulations are covered under Decree 41/2003. The Internal Regulations of the General Inspectorate of Insurance (*Inspecção Geral de Seguros*) are laid out in Ministerial Diploma 129/99. Mozambique has 5 major insurance companies whose operations are monitored by the General Inspectorate of Insurance.

II.B The Profession

20. The accounting profession in Mozambique is dominated by accounting technicians. It is estimated that more than 2,000 registered accounting technicians work throughout Mozambique. Accounting technicians provide bookkeeping services and signoff on the accuracy of information in financial accounting reports primarily to provide assurance to the taxation authorities. Most accounting technicians received formal training during the period before accounting was taught in academic programs in Mozambique's educational institutions. Therefore, the level of knowledge and skill among the accounting technicians varies widely. The Ministry of Finance maintains a list of approved accounting technicians. In order to be approved and registered as an accounting technician, an applicant must present the following to the Ministry of Finance:

- Academic certificate proving that the required level of education in accounting has been achieved (normally from the Commercial Polytechnic);
- Professional letter of reference from 2 practicing accounting technicians;

⁴ It is worth mentioning that the standardized Chart of Accounts can hardly be updated as frequently as new IFRS are issued and old IFRS requirements are amended.

- Criminal certificate stating that the applicant has not been convicted, at any time in his or her life, of a crime carrying a penalty of 2 or more years.

21. **The Ministry of Finance issues audit licenses to audit firms that the Ministry approves to perform audits.** Seven audit licenses have been issued to date; however, the information on audit licensees is not publicly available. Although 7 audit firms are known to have practicing licenses, 7 other firms advertise in the telephone directory (2007/8 Mozambique Yellow Pages) showing that they provide auditing and other various professional services in different parts of the country. Since the professional practice of external audit did not exist in the country prior to the beginning of 21st century, the local firms of accounting technicians could not demonstrate necessary practical experience to qualify for obtaining audit practice license from the Ministry of Finance. In order to facilitate transfer of practical knowledge of auditing into Mozambique, the Ministry of Finance has issued licenses only to those audit firms that are affiliated with international accounting firm networks. The Big-Four international networks are all represented in Mozambique, with offices in Maputo as well as other large cities. The Ministry of Finance licensed firms generally provide auditing services to the relatively large-size enterprises, banks and other financial institutions, NGOs, subsidiaries and branches of foreign companies, and enterprises with various other forms of foreign participation. Also, most of the international donor-funded projects are audited by these firms. Generally, the small and medium enterprises in all parts of the country often rely on professional auditing services provided by the firms that have weak capacity and do not hold audit practice license.

22. **Only two Mozambican nationals have a professional accountancy qualification awarded by an IFAC member body.** In addition, there are an estimated 25 foreigners working in Mozambique who have professional accountancy qualification awarded by the IFAC-affiliated professional accountancy bodies in various countries including India, Ireland, Portugal, South Africa, and the United Kingdom. These foreign qualified professional accountants work in audit firms, international organizations, and commerce and industry.

23. **There is no organized professional accountancy body in Mozambique.** Over the last 5 years, a Government-appointed committee has been working to establish a professional accountancy body to be known as the Order of Professional Accountants in Mozambique. This committee includes members of the accounting profession and representatives from the Ministry of Finance. The committee objective is to provide technical support in drafting statutes of the professional accountancy body. The enactment of draft statutes is expected to take place by mid-2008. The aim of the new professional accountancy body is to organize the accountancy profession under two sections: (a) certified public accountants and (b) accounting technicians. Arrangements will be put in place for launching a national professional qualification examination, support the professional development of qualified accountants in public practice, and apply for IFAC membership. Also, actions will be implemented focusing on certification and professional development of the accounting technicians. The certified accounting

technicians will be offered the opportunity to complete a conversion program of learning and examination in order to obtain the qualification of certified public accountants.

24. Mozambique does not have a quality assurance program for auditors. A quality assurance program reviews the auditors' work at both partner and firm levels and provides assurance that auditors perform their duties with integrity and in compliance with the applicable auditing standards and other requirements. The program also identifies weak areas in the auditing process that could require new training programs to improve the quality of audit. Establishing a country-level quality assurance program is an international good practice. ISQC 1, issued by the IAASB, requires audit firms to establish quality control policies and procedures necessary for reasonable assurance of conforming to professional standards in performing auditing services. This standard should be adopted as part of the adoption of the full set of ISAs. The national professional body should also sponsor training and related programs aimed at enhancing the quality of auditing services provided by audit practitioners in the country. To ensure that audit firms have effective quality control arrangements, a mechanism of independent review needs to be in place. Such reviews are more effective for monitoring and enforcement of applicable auditing and financial reporting requirements if and only if an independent oversight body conducts the review (e.g., audit practice reviews carried out by the Independent Regulatory Board for Auditors in South Africa). Such a review mechanism does not exist in Mozambique at the present time.

25. **Mozambique does not have a quality assurance program for auditors.** A quality assurance program reviews the auditors' work at both partner and firm levels and provides assurance that auditors perform their duties with integrity and in compliance with the applicable auditing standards and other requirements. The program also identifies weak areas in the auditing process that could require new training programs to improve the quality of audit. Establishing a country-level quality assurance program is an international good practice. The IFAC requires audit firms to establish quality control policies and procedures necessary for reasonable assurance of conforming to professional standards in performing auditing services. In this regard, the national professional accountancy body develops quality control standards and relevant guidance. The professional body also sponsors training and related programs aimed at enhancing the quality of auditing services provided by audit practitioners in the country. To ensure that audit firms have effective quality control arrangements, a mechanism of independent review needs to be in place. Such reviews are more effective for monitoring and enforcement of applicable auditing and financial reporting requirements if and only if an independent oversight body conducts the review (e.g., audit practice reviews carried out by the Independent Regulatory Board for Auditors in South Africa). Such a review mechanism does not exist in Mozambique at the present time.

26. **No legal requirement exists for auditors to have professional indemnity insurance.** Professional indemnity insurance assures auditors would meet liabilities in the event of valid claims against their professional conduct. Usually, the regulation will make it a condition for granting a license and for license renewal every year. At present, there is no requirement for auditors to have the insurance in order to get a practicing license. The importance of professional indemnity insurance would increase with the

increase in professional risk exposures of the practicing auditors. In this context, a new Anti-Corruption Law of Mozambique imposes penalties on auditors who do not disclose any indications of corrupt practices that come to their attention.

27. **The accountancy profession in Mozambique has not yet experienced any litigation on financial reporting.** As sophistication of the economy increases, the probability of such litigation also increases; hence the need for good financial reporting infrastructure as well as overall good corporate governance infrastructure.

28. **The Associação Moçambicana de Auditores. Internos (Association of Internal Auditors in Mozambique or AMAI) was founded in 2006.** The AMAI is affiliated with the Institute of Internal Auditors (IIA) based in the United States. The AMAI has approximately 300 members and is in the process of organizing training for members primarily using IIA training materials in Portuguese from Brazil.

II.C Professional Education and Training

29. **There is neither a local accountancy qualification nor practical-oriented training for professional trainee-accountants available in Mozambique.** Only 2 Mozambican nationals obtained professional accountancy qualification through the long-distance learning and accreditation program offered by the UK-based Association of Chartered Certified Accountants (ACCA). This long-distance program is very expensive for the citizens of Mozambique. Since there is no national institutional arrangement for a program of professional accountancy training and accreditation, Mozambique suffers from the scarcity of professionally qualified accountants (i.e., certified public accountants or chartered accountants). At present, there are approximately 30 Mozambican students studying for the ACCA qualification.

30. **Academic programs in accounting started only in the recent past.** The main state university, Eduardo Mondlane, began offering a four-year Degree in Accounting and Finance in 2004. The first students of that program are just about to graduate and be available for employment and further training. This very popular program has many applicants competing for limited space. The students must pass an entrance examination for admission into the program. Efforts are underway to start accounting programs in other universities. All higher education institutions suffer from a shortage of well-trained academic staff to teach accounting and auditing courses in line with international good practice. To complement the university's short-staffing of trained faculty, some accounting practitioners, employed in commerce and industry, work as part-time lecturers in evening classes. The scarcity of high-quality teaching materials on accounting and auditing in Portuguese constrains effective teaching in academic programs.

31. **The absence of a local professional accountancy body means that there is no locally designed and controlled practical training for accountants.** The training that is available at the audit firms for local audit staff is not formalized nor does it follow any organized sequence and structure. In addition, any available training is neither monitored

32. **There is no monitoring mechanism to ensure compliance with the IFAC-mandated requirements on continuing professional development.** There is no guarantee that even those *qualified* accountants in the marketplace are keeping up with new developments in internationally accepted accounting and auditing standards as well as codes of ethics for professional accountants. According to the IFAC International Education Standard for Professional Accountants No. 7, member bodies should require all professional accountants to develop and maintain competence relevant and appropriate to their work and professional responsibilities. The responsibility for developing and maintaining competence rests primarily with each professional accountant. When an input-based approach is used, a professional accountant should complete at least 120 hours or equivalent learning units of relevant professional development activity in each rolling three-year period, of which 60 hours or equivalent learning units should be verifiable. Continuing professional education should not be less than 20 hours during a year.

II.D Setting Accounting and Auditing Standards

33. **There are two sets of accounting requirements for the business enterprises in Mozambique.** These are (a) local accounting requirements, which are dictated by the PGC, issued by the Ministry of Finance; and (b) IFRS, issued by the International Accounting Standards Board (IASB).

34. **The *Plano Geral de Contabilidade (Standardized Chart of Accounts)* or PGC sets out the form of financial reporting to be used by the business enterprises.** The PGC outlines the accounting principles to be applied by a business enterprise and gives an overview on the accounting treatment of different items. Of course the PGC is not as detailed or as complex as IFRS. The IASB-issued standards, interpretations, and related discussion documents are covered in a few 1,000 pages whereas the PGC accounting requirements are covered in just 72 pages.

35. **Beginning with the annual financial reporting as of December 31, 2007, IFRS has been mandatory for presentation of financial statements of banking institutions.** The aim of the Government is to have the larger corporate entities reporting in compliance with IFRS starting with the financial year ending December 31, 2009. The IASB has been working on issuance of IFRS for the small and medium enterprise. It will be worth examining the feasibility of implementing these reporting requirements for the small and medium enterprise in Mozambique. Although the IFRS exposure draft for the small and medium enterprise is very brief compared to the full IFRS, small Mozambican

enterprises may find it extremely difficult and burdensome to apply these recommended accounting principles.

36. **The Government has taken steps for facilitating IFRS implementation in the whole corporate sector of the economy.** The Ministry of Finance has engaged a consulting firm under a World Bank-supported financial sector technical assistance project to craft a strategy for the introduction of IFRS in the country's corporate sector, as well as to assist with the implementation of the approved strategy and conduct training on IFRS for both accountants in Mozambique in general and government tax inspectors who will use IFRS financial statements.

37. **Auditing requirements are not defined in any Mozambican laws, rules, regulations, or standards.** No guidance exists as to which auditing standards are to be followed in Mozambique. Without such an institutional arrangement in the country for providing direction, auditors may have different interpretations with regard to the applicability of a particular ISA. The audit firms that operate in Mozambique claim that they adhere to the standards contained in the respective international network's audit practice manual. These audit practice manuals are said to comply with the ISA.

II.E Ensuring Compliance with Accounting and Auditing Standards

38. **No institutional arrangement exists to enforce PGC requirements for accounting and financial reporting.** No statutory body in Mozambique is tasked with enforcing compliance with the PGC accounting and financial reporting requirements. The accounting technicians who prepare the financial statements have primary responsibility to ensure compliance with PGC. In addition, in accordance with the Commercial Code, all SA companies must have a fiscal council that must verify the accuracy of the annual accounting reports. The fiscal council should report that the Annual Accounts and the Directors Report are accurate and complete. Due to low capacity with regard to financial management in both private and public sectors of the economy, members of the fiscal councils in many companies do not appear to have adequate financial knowledge and proper skills to perform this function satisfactorily.

39. **External auditors provide the last line of defense against noncompliance with accounting and financial reporting requirements.** When annual financial statements are audited, the audit report refers to accounting principles generally accepted in Mozambique (i.e., PGC). It is the auditor's duty to ensure that the financial statements have been prepared in conformity with these principles. Some larger foreign companies operating in Mozambique prepare their financial statements in accordance with IFRS in order to facilitate preparation of parent company consolidated financial statements in the countries of origin. These financial statements are subject to audit; the auditors are required to state in the audit opinion any deviations from IFRS, but there is no other independent authority monitoring and enforcing compliance with the IFRS requirements in these financial statements.

40. **The tax authority enforces compliance with tax rules rather than with accounting and financial reporting requirements.** It is within the scope of the tax authority to monitor and enforce financial reporting requirements. However, there is hardly any emphasis on compliance with the general purpose financial reporting requirements. The Commercial Code requires that the annual accounting reports be filed with the tax authority. The majority of private companies in Mozambique is not subject to an external audit and not obliged to have a fiscal council. Thus, for most companies, there is no third party examination of financial statements other than self-declaration about accuracy made by the accounting technicians who prepare these financial statements. The Government monitors the accuracy of reported profits exclusively through the mechanism of inspections by the tax authority. These inspectors have wide ranging powers and cover all aspects of accounting although their main objective is to maximize tax revenues. The inspections are discretionary and limited by the capacity and available skill of the officials of tax authority. The effect of this form of Government regulation on the majority of the private sector enterprises has created an impression that accounting records are maintained and financial statements are prepared only for tax purposes. The concept of general purpose financial reporting is not widely appreciated in the country.

41. **There is no mechanism with necessary capacity to provide assurance on the quality of work being performed by auditors.** The auditors belonging to an international network are subject to internal quality assurance reviews and are required by their global headquarters to apply international standards. Audit opinions on all annual accounts produced under IFRS or under local requirements in Mozambique normally state that the audit has been conducted in accordance with ISA, but there is no body that monitors or enforces this voluntary step.

III. ACCOUNTING STANDARDS AS DESIGNED AND AS PRACTICED

42. **The legal requirements on accounting and financial reporting are not consistent with IFRS.** As mentioned earlier, the accounting requirements set by the Commercial Code are primarily aimed at fulfilling the needs of tax reporting. Each account mentioned in the standardized Chart of Accounts, and each line item of balance sheet and income statement is assigned a specific account number. The hard structure of Mozambique's standardized Chart of Accounts or PGC constrains proper application of the IFRS reporting requirements. Inconsistencies arise from the fact that various IFRS that may be relevant in an enterprise are not covered by the PGC, for example, post balance sheet events (IAS 10), segment reporting (IAS 14), leases (IAS 17), employee benefits (IAS 19), related party transactions (IAS 24), and contingent liabilities (IAS 37). Some inconsistencies between PGC and IFRS requirements are presented in Table 1.

Table 1. Comparison of Selected IAS/IFRS and PGC Requirements

| <i>Concerned area</i> | <i>Accounting treatment PGC</i> | <i>Accounting treatment IAS / IFRS</i> | <i>IAS / IFRS</i> |
|-----------------------|-------------------------------------|--|-------------------|
|-----------------------|-------------------------------------|--|-------------------|

| <i>Concerned area</i> | <i>Accounting treatment PGC</i> | <i>Accounting treatment IAS / IFRS</i> | <i>IAS / IFRS</i> |
|---|---|---|----------------------------|
| Expenditure on research | Expenditure accounted as an intangible asset. | Expenditure recognized as an expense when incurred. | IAS 38 |
| Depreciation of development expenditure | Depreciation period up to 5 years. If greater period adopted, explanation is required. | Intangible asset depreciated over its useful life. | IAS 38 |
| Measurement of tangible assets | Occasional revaluations, legal or extraordinary, not considering the fair value amount. | Option between 1 of 2 models: - Cost model - Revaluation model | IAS 16 |
| Depreciation of tangible assets | Depreciation determined by tax based criteria. | Depreciation over the asset's useful life, based on depreciation method that reflects pattern of consumption of expected future economic benefits. | IAS 16 |
| Measurement of financial assets—subsidiaries and associates | Cost method. | Separate financial statements: - Cost method - Fair value concept applies to the available for sale financial asset. Consolidated financial statements: - Subsidiaries: combination of parents and subsidiaries financial statements line by line; - Associates: equity method; - Others: apply IAS 39. | IAS 27 IAS 28 IAS 39 |
| Measurement of financial instruments (for sale or to held) | Cost or market value whichever is lower. | Depending on the classification of the financial instrument, should be measured at cost, amortized cost or fair value. | IAS 39 |
| Government grants | Government grants not related to the operational activity recognized in equity. | Government grants shall be recognized as income over the periods necessary to match them with the related costs which they are intended to compensate, on a systematic basis. | IAS 20 SIC 10 |
| Accounts receivable / payable in foreign currency | Possibility to defer exchange differences related to noncurrent accounts receivable / payable, if there are expectations of reversal. | Exchange differences recognized in income statement. | IAS 21 |
| Inventories | Possibility to use the Last-In First-Out method. | The cost of inventories shall be assigned by using the First-In, First-Out or weighted average cost method. | IAS 2 |

| <i>Concerned area</i> | <i>Accounting treatment PGC</i> | <i>Accounting treatment IAS / IFRS</i> | <i>IAS / IFRS</i> |
|-------------------------|--|---|-------------------|
| Construction contracts | Option to choose between the stage of completion method or the completed contract method. | Contract revenue and contract costs associated with the construction contract recognized as revenue and expenses by reference to the stage of completion. When the outcome of a construction contract cannot be estimated reliably, revenue shall be recognized only to the extent of contract costs incurred that it is probable to be recoverable. | IAS 11 |
| Extraordinary items | Extraordinary item recognized if not related to the operational activity. | An entity shall not present any items of income and expense as extraordinary items. | IAS 1 |
| Prior period errors | Correction of material prior period errors on financial statements of the detection year. | Prior period errors corrected by retrospective restatement of the financial statements (current and prior year – comparative) if practicable. | IAS 8 |
| Disclosures and formats | The PGC does not have detailed disclosure requirements compared to the IFRS; also, the PGC provides formats for Balance Sheet and Income Statements and the requirements do not cover all the statements and explanatory notes required by IFRS. | <p>Detailed disclosure requirements of the IFRS are aimed at assisting decisionmaking by the stakeholders.</p> <p>According to IFRS requirements, a complete set of financial statements comprises:</p> <ul style="list-style-type: none"> (a) statement of financial position as at end of the period [Balance Sheet]; (b) statement of comprehensive income for the period [Income Statement]; (c) statement of changes in equity for the period; (d) statement of cash flows for the period; (e) notes, comprising a summary of significant accounting policies and other explanatory information; and (f) a statement of financial position as at beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, | IAS 1 |

| <i>Concerned area</i> | <i>Accounting treatment PGC</i> | <i>Accounting treatment IAS / IFRS</i> | <i>IAS / IFRS</i> |
|-----------------------------------|--|--|-------------------|
| | | or when it reclassifies items in its financial statements. | |
| Deferred Tax | Deferred tax is not considered in the PGC. | Deferred tax should be recognized in the financial statements. | IAS 12 |
| Cash Flows | No Cash flow statement required. | Cash flow statement required. | IAS 1 |
| Provision for Accounts Receivable | The PGC states that a provision should be made for the unrecoverable amount of receivables. The Tax Law states that the provision is limited to 1.5% of total receivables with a maximum total provision of 6% of receivables. | Receivables are treated as financial assets and if there is evidence that there is an impairment loss on receivables the carrying value of the asset should be reduced directly or through an allowance. | IAS 39 |

43. **The enterprises that prepare IFRS-based financial statements face practical implementation difficulties.** Discussions by the ROSC team with representatives of financial institutions, practicing accountants, and auditors revealed some IFRS implementation problems. Most of these problems arise from lack of adequate expertise among corporate accountants who find it difficult to prepare financial statements in accordance with IFRS. Moreover, the practicing accountants and auditors in many cases lack industry-specific knowledge with regard to application of relevant IFRS. Another major hurdle of implementing IFRS arises from the need to comply with some tax rule-oriented accounting requirements. There are instances where tax accounting requirements, including depreciation rates, contradict IFRS requirements. With regard to certain business transactions, many preparers of general purpose financial statements often depart from IFRS and follow tax rules as the method of accounting treatment. The companies sometimes manage their profits by using some accounting treatments allowed by tax rules in order to minimize taxation liabilities, an approach that is noncompliant with IFRS.

44. **Local companies' financial statements are generally in compliance with PGC; however, quality of financial reporting suffers due to weaknesses in the PGC accounting requirements.** The ROSC team reviewed 15 sets of financial statements, of which 12 are the PGC-based annual accounting reports, and 3 IFRS-based financial statements. The emphasis of PGC is more on completing the prescribed forms—balance sheet and income statement rather than presentation of a full set of financial statements. In the absence of a local accounting and reporting requirement on important matters that can involve material amounts and because the level of disclosure under PGC is less demanding than under IFRS, the financial information presented in a PGC-based annual

accounting report is prone to be incomplete, if not inaccurate in certain cases. Some IFRS-based financial statements reviewed by the ROSC team departed from IFRS requirements in the following examples:

- IAS 24 requires that companies disclose key management personnel compensation, split between short-term employee benefits, post-employment benefits, termination benefits, and share-based payments.
- IAS 1 requires that companies disclose the number of shares authorized and the number of shares issued and fully paid.
- IAS 1 requires that companies disclose the address of the registered office of the company or the principal place of business if different.
- Financial statements are required to make disclosures on accounting for operating and finance leases.
- IAS 38 requires that the statements disclose whether intangible assets are indefinite or finite and if the assets are finite, then the useful lives or the amortization rates should be disclosed.

IV. AUDITING STANDARDS AS DESIGNED AND AS PRACTICED

45. **Without local-based auditing standards, ISA are considered the de facto auditing requirements in Mozambique.** In practice, ISA application differs among different audit firms and different audit engagements. To assess actual auditing practices, the ROSC team interviewed practicing auditors, senior leaders of the auditing profession, and some regulators. It appeared that auditors associated with international accounting firm networks generally tend to follow internationally recognized auditing standards. Nevertheless, there were instances where some of these firms apparently had difficulties in complying with some auditing standards “in substance” mainly due to the fact that availability of properly trained audit staff with adequate knowledge of auditee’s business is often hard to find in Mozambique. In many cases the trainee auditors are entrusted with much more responsibilities than their counterparts in more mature audit markets of industrialized countries. Due to scarcity of well-trained senior audit practitioners, the trainees in many cases do not receive adequate level of supervision. The local audit firms, which do not have any relationship with international accounting firm network, carry out auditing activities in accordance with self-developed procedures that do not seem to be comparable with any internationally recognized auditing standards.

46. **The lack of practical training adversely affects quality of audit.** In conventional audit practices, the audit team is made up of a hierarchy of complimentary professional accountants. The lowest level is occupied by audit trainees, usually under a training contract. The trainees usually have a basic accounting qualification and undergo several years of on-the-job training as well as professional development and examination leading to certification as an IFAC-recognized professional accountant/auditor (i.e., chartered accountant or certified public accountant or similar professional designation). Other members on an average audit team would be the semi-qualified and part-trained

higher-level trainees and qualified seniors supervised by qualified managers and partners. This mix guarantees a certain level of output quality and performance consistency.

47. **In Mozambique, however, professional firms are under no obligation to employ audit trainees although all claim to do so.** While most staff of these audit firms have some measure of accounting, they do not undergo systematic training, coaching, and mentoring once hired. Training provided to accounting/audit staff relates primarily to the firms' audit methodology and practices and availability of other generalized training. Training is dependant upon availability of learning materials translated into Portuguese to benefit the majority non-English speaking staff. Some staff are independently pursuing the ACCA qualification. However, most large audit firms in Mozambique have on their teams one or two IFAC-recognized qualified accountants with a practicing certificate. As a result, about 50 percent of audit firms report that only about 50 percent of their audits are in accordance with ISA. The firms with more than 3 qualified professional accountants on the teams report 70 percent or higher adherence to ISA.⁵

48. **The staffing and qualification mix within the audit profession in Mozambique leaves room for improvement.** The quality of audit work, just from the structure of the audit practice, is unlikely to match that of accounting practices made up of the full compliment of trainee, partly qualified, and fully qualified accountants for each assignment. This is likely to be even more visible when the move to IFRS is made, as the proportion of persons with the right training to execute not only the accounting but also the review and checking for compliance is likely to remain low.

V. PERCEPTION OF THE QUALITY OF FINANCIAL REPORTING

49. **There is a lack of demand for high-quality corporate financial reporting.** There is a perception that the financial statements are prepared primarily for tax purposes. If the tax authority is happy with the annual financial statements, nobody questions whether or not high-quality accounting standards have been complied with. Many companies of various sizes are not subject to the financial statements audit. There is no tradition of financial analysis in the country, and no credit rating agencies. The banks do not place any reliance on corporate financial statements; generally the lenders manage credit risks through the use of collaterals. Also, personal relations and familiarity with the performance of a business entity are considered more important for business decisions than access to reliable financial information. With exception of a few large entities with foreign participation, companies in Mozambique are still largely family-owned and the business community generally sees limited interest in external financial reporting. In fact, many businesses are reluctant to provide transparent financial information, mostly for fear of tax consequences.

50. **There is a general perception that the financial statements audited by large firms meet higher standards of financial reporting.** Interviews and discussions with various stakeholders, including relevant regulators, revealed that a high degree of reliance

⁵ This data is based on information provided by all the seven licensed audit firms in the country.

is placed on the financial statements that are audited by the members of international accounting firm networks. Contrary to that position, some stakeholders viewed that audits, even by large audit firms, in most cases do not add value due to the fact that there is no pressure from the market to improve the quality of audit.

VI. POLICY RECOMMENDATIONS

51. The main objective of this ROSC review is to assist the Government and other stakeholders in strengthening the corporate sector's accounting, financial reporting, and auditing practices, as a means to facilitate the Government's goal of expediting economic development. Implementation of these recommendations will help in the following ways:

- Enhancing the investment climate and bolstering domestic and foreign direct investment in the private sector;
- Stimulating growth of the small and medium enterprises by facilitating their access to credit from the formal financial sector by shifting gradually from collateral-based lending decisions to lending decisions based on the financial performance of the prospective borrower;
- Supporting the development of the banking sector and mitigating the risk of crises due to loan collection problems and helping mobilize domestic savings; and
- Achieving greater financial transparency in the corporate sector, both state and private owned, thus allowing shareholders and other interested parties to assess corporate performance.

Without attempting to provide a detailed tactical design for reforms, this report provides principles-based policy recommendations to support the implementation of accounting reform and contribute to the enhancement of the quality of corporate financial reporting.

52. The policy recommendations in this section are mutually supportive requiring holistic, multi-disciplinary approaches for implementation. Implementation will require the cooperation of Government, regulators, academics, accounting and auditing profession, and other stakeholders. The Government, policymakers, and development partners should work together to secure the resources in order to achieve a strong financial reporting infrastructure in Mozambique. Due to the lack of qualified accountants presently in Mozambique, support from the development partners will be required to implement the following policy recommendations.

53. **Establish a multidisciplinary steering committee to coordinate the accountancy reform and development activities.** The steering committee should advise policymakers and regulators regarding implementation of the ROSC recommendations. Based on the successful experience of capacity-building activities in other countries, the ROSC team recommends that the steering committee develop a detailed country action plan that sets clearly sequenced key actions and allocates responsibilities for implementing the necessary reforms. The country action plan should

form the basis for capacity-building activities for strengthening the underpinnings of accounting and auditing practices in Mozambique.

54. **Update the legal framework of accounting and auditing.** The legal framework governing accounting, auditing, and financial reporting should be updated in line with recent international developments. Provisions of the Commercial Code and other relevant laws should (a) place greater emphasis on financial reporting, (b) provide legal backing for use of IFRS in the context of public-interest entities and simplified SME reporting standards issued by competent authorities,⁶ (c) establish some thresholds for financial statements audit and (d) outline an appropriate framework for monitoring and compliance. The updating of legal framework should underscore the overall principles and purposes of financial reporting, consistent with the IASB framework for presentation and preparation of financial statements. Detailed forms and requirements should be dealt with at the secondary-level regulations and/or standards pronounced by duly constituted bodies. Moreover, the legislation may simply refer to ISAs as issued by the International Auditing and Assurance Standards Board (IAASB) of IFAC, with the mandate to the national professional body for translation and issuance of the ISAs as national auditing standards.

55. **Consider enacting new corporate financial reporting legislation.** In order to improve the legal framework of corporate financial reporting, a Financial Reporting Act should be enacted with focus on all regulatory aspects of accounting and auditing. Provisions of the Commercial Code will need to be aligned with the requirements of the new Financial Reporting Act. Going forward, it will be easy to update accounting, auditing, and financial reporting requirements from time to time by simply amending the single Financial Reporting Act.

56. With regard to modernizing the legal framework on accounting and auditing, the following should be taken into account:

- Specify mandatory IFRS application in totality for all public interest entities in Mozambique. The public interest entities should be defined through an analysis of the business structure in Mozambique. Where the regulators (e.g., banking and insurance regulators) need additional information for prudential supervision purposes, this should come up by topping up IFRS.
- Develop an arrangement for issuance of simplified financial reporting requirements for small and medium enterprises. These thresholds should be provided by law.

⁶ Public interest entities are defined by the nature of their business, size, and number of employees; or by their corporate status by virtue of their range of stakeholders. Examples may include listed companies, banks and similar financial institutions, insurance companies, and large enterprises. To be considered a public interest entity, the large enterprises may be defined as individual enterprises and groups of enterprise that meet any two of the following three thresholds: (a) total number of employees exceeding [a number to be decided in consultation with the country stakeholders]; (b) total assets on the balance sheet exceeding [amount to be decided in consultation with stakeholders]; and (c) total turnover exceeding [amount to be decided in consultation with stakeholders].

- ISAs should be mandated for corporate sector audits. Audit procedures under ISAs can be scaled to large or small entities; therefore ISAs should be required for all audits. Experience in other jurisdictions, however, has shown that the smallest corporate sector entities may not need financial statements audit in accordance with international standards. The smallest entities, however, may need tax audit following the requirements set by the taxation authorities. The non-public interest entities below a certain threshold (revenues, assets and/or employees) may be exempted from audit. For the smallest entities that will not be subject to audit, consideration should be given to other forms of assurance, such as that described in International Standard on Assurance Engagements 3000 issued by the IAASB.
- Clearly mandate obligatory preparation of consolidated financial statements for group companies fulfilling the criteria of public interest entities.
- Provide legal backing to establish an arrangement for independent oversight of the auditing profession including audit practice review.
- Provide regulators with adequate authority to sanction appropriately against violations of applicable accounting and auditing standards and rules for ensuring effective monitoring and enforcing actions.
- Mandate appropriate requirements for filing of financial statements for all entities that are subject to annual statutory audit. Also, develop an arrangement for easy public access to the public interest entity's financial statements.
- Harmonize legislation on general purpose financial reporting by corporate entities with the tax framework. Guidance will need to be given on how to reconcile the accounting profit/loss with the taxable profit/loss. In absence of guidance, entities often intermingle tax reporting requirements and general purpose financial reporting requirements when preparing financial statements.

57. Establish systematic, institutionalized, monitoring and enforcement mechanisms to ensure compliance with accounting and auditing requirements. The quality of corporate financial statements cannot be ensured by only adopting internationally accepted standards. A country might formally mandate the application of IFRS and ISA; however, in practice there might be compliance gaps. To a large extent, quality depends on designing and implementing a proper monitoring and enforcement system. There are three parties directly involved in the process of ensuring compliance with the applicable standards, and each must be strengthened:

- ***Company directors*** with legal obligations to prepare the financial statements must employ capable accountants and ensure that the applicable standards are fully complied with.
- ***Audit service providers*** must possess adequate technical knowledge, put in place appropriate quality control arrangements, and discharge their professional responsibilities independently in order to provide assurance that financial statements comply with all applicable standards and portray “true and fair” view of enterprises’ conditions and results of the operations.

- Both *self-regulatory organization* (the professional accountancy body) and *statutory regulators* must ensure compliance with the standards and consistently take actions against violators. To ensure effective monitoring and enforcement, the regulators need adequate capacity, authority, and independence.

58. **Strengthen capacity of the proposed professional accountancy body—Order of Accountants in Mozambique—through a twinning arrangement for a period of 4 to 5 years.** The twinning arrangement should be developed with a reputable member of the IFAC that could provide assistance with advising on carrying out the preparatory work for launching the new institution; preparation of by-laws, policies and procedures, and other necessary documentation; development of strategic plan; guidance on operational activities; and other necessary assistance to this nascent institution to put in place arrangements for sustainable growth. The twinning partner could also help the national professional body to start its own professional accountancy qualification examination, professional learning and practical training arrangements, professional accreditation, audit practice certification, and related activities in line with international good practice. This will help the proposed Order of Accounts to start functioning as a modern professional accountancy body with the capability to also play an efficient and effective role in financial management education and training. Some specific areas of assistance by the twinning partner include:

- Prepare and implement a strategic plan for development of the accountancy profession in line with recent international developments;
- Design and implement strong governance and functioning arrangements for enhancing organizational effectiveness of the professional body;
- Strengthen professional standards by assisting to implement internationally comparable professional education, qualifying examination, and practical training arrangements;
- Put in place arrangements for enhancing continuing professional development of the practicing accountants and auditors;
- Develop the technical department capable of providing support for proper implementation of IFRS in public interest entities and simplified financial reporting standards in small and medium enterprises;
- Assist audit firms to build capacity for implementing ISA and improving the quality of audit; and
- Take necessary steps for full compliance with the IFAC membership obligations in facilitate full IFAC membership of the Order of Accounts.

59. **Designate the proposed professional accountancy body as the catalyst for strengthening accounting and auditing practices in both private and public sectors of the economy.** To bolster the role of professional accountants in Mozambique's economic development, the proposed national professional accountancy body should

produce and continuously develop qualified professionals with capability to provide services in all parts of the economy—private sector, governmental, and nongovernmental. In addition to working for professional development of the corporate accountants and auditors, the national professional body should take proactive measures for enhancing professional capabilities of the government accountants and auditors. In order to better serve the public sector of the economy, the professional body could have a public sector section with a separate membership stream and additional qualification requirements. An arrangement should be put in place to enable the existing government accountants and auditors to complete a learning program—both theoretical and practical—for obtaining professional (public sector section) membership. If all members of the professional accountancy body comply with requirements of continuing professional development, there would be qualitative changes in accounting and auditing practices of both private and public sectors of the economy.

60. Establish an audit oversight unit under the Ministry of Finance. An oversight unit should function under the direction of a council of advisors consisting of a small group of eminent persons in the country. The oversight will include monitoring and enforcement of auditing requirements, through audit practice review, investigation, and disciplinary actions. Given the dearth of experienced and professional accountants in Mozambique, it is important to operationalize an oversight arrangement with the involvement of specialists drawn from other audit regulators in the region and/or other regional and international organizations. The audit oversight unit should develop a partnership arrangement with the professional accountancy body in order to carry out monitoring and enforcement activities with efficiency and effectiveness. Expertise from the region can be drawn upon while gradually building Mozambique's capacity for undertaking independent oversight of auditors. Possibilities of regional joint efforts should be explored. Steps should be taken to plan and persuade other South African Development Community countries to establish a regional organization from where the expertise could be borrowed by Mozambique and other countries that have limited institutional capacity to carry out monitoring and enforcing activities.

61. Provide assistance to the small audit firms for capacity building to improve audit quality. There should be an initiative to develop a competitive audit market in Mozambique. Special attention should be given to assisting small audit firms to develop capacity for providing quality audit and assurance services, and also to take necessary steps for developing viable audit practices through merger or establishment of network arrangement. IFAC-issued guidelines and pronouncements for the small and medium audit practices should be disseminated through formal and informal training and related activities. Moreover, arrangements should be made for small audit firms to gain exposure to necessary technical knowledge for enabling them to comply with IFAC requirements on audit quality control, auditing standards, and professional ethics.

62. Issue practical application guidance on international accounting and auditing standards for both corporate and governmental entities. The professional accountancy body should take the lead to prepare and disseminate implementation guidance notes and related publications illustrating local cases, on IFRS, ISA, and

International Public Sector Accounting Standards (IPSAS). The implementation guidance should be prepared in consultation with relevant staff of IASB and IFAC. Arrangements should be made so that all international standards, interpretations, and other guidance are promptly available to the professional accountants and auditors, trainees, students, and academics in Mozambique.

63. **Enhance academic curriculum and training.** The accounting curriculum should include practical application of IFRS, and case studies to best prepare accountants (rather than bookkeepers) for careers in corporate Mozambique. A panel of experts should review and update the accounting curriculum in order to incorporate IFRS and ISA and practical-oriented teaching at the undergraduate university level. The ethical dimensions of business management, corporate finance, and accounting and auditing should be taught with case studies in undergraduate programs. Particular attention should be given for improving communication and critical thinking skills.


64. **Implement a training-of-trainers program for sustainable transition to IFRS.** A program should be designed and implemented giving special emphasis to preparing a core group of IFRS experts who would facilitate the development of a sustainable arrangement for implementation of current and future IFRS issued by the IASB. The core group of experts—*master trainers*—should make the commitment to (a) take active part in lecturing at the higher educational institutions and in continuing professional development programs to be organized by the new professional accountancy body and (b) writing and disseminating guidance notes on proper implementation of IFRS under local circumstances. Under the training-of-trainers program, international consultants should develop a collaboration arrangement with a leading public university and leaders of the accountancy profession in Mozambique. The program would require development for improving capacity of the higher educational institutions and the accountancy profession to bolster IFRS knowledge building in the country. The master trainers should also be helped to acquire necessary skills to handle issues relating to implementation of all current and future IFRS. The master trainers should be capable of developing a sustainable arrangement for development of IFRS learning materials in Portuguese to impart knowledge to the practicing and non-practicing accountants and auditors, university students, trainee accountants, and other interested parties.






65. **Enhance capacity of the banking regulator and ensure coordination of all regulators.** The Central Bank requires adequate staffing to handle and track the compliance of all financial institutions with financial reporting requirements. The Central Bank also needs to build its capacity and expertise to handle IFRS issues relating to financial institutions. Implementation of prudential regulations in financial institutions closely interacts with IFRS issues. Unless there is adequate understanding of IFRS issues by both the regulator and the banks and other financial institutions, difficulties will be experienced in reconciling IFRS and regulatory requirements. All financial sector regulators should closely co-ordinate with regard to financial reporting matters so that specialized expertise can be accessed when unavailable in some regulatory agencies.






66. **Introduce awareness programs for improving the degree of compliance with IFRS requirements.** The objective of the awareness programs should be to ensure that the enhanced financial reporting requirements are well understood and that there is capacity for the implementation of new requirements. Well-planned transition arrangements and appropriate timing for launching the awareness campaign would be essential. The professional accountancy body and other regulators should work jointly to design awareness programs highlighting the significance of compliance with accounting and auditing standards. Shareholders, directors, and top officials from the corporate sector should be briefed adequately on their responsibilities to ensure compliance with standards and enforcement process, including legal implications. Also, benefits of compliance with standards and best practices should be highlighted in such programs.

67. **Introduce audit engagement partner rotation, instead of audit firm rotation.** The Bank of Mozambique has mandated the rotation of Bank auditors (audit firms) at an interval of four years. The rotation of audit firms does not seem to be a feasible approach to enhancing audit quality in Mozambique. The country does not have adequate number of capable audit firms to provide high quality auditing and assurance services in the financial sector. It is worth noting that most of the developed economies have adopted the policy of audit engagement partner rotation instead of audit firm rotation. Australia, Canada, the UK and the US require rotation after five successive years. The European Union legislation requires rotation after seven years. Australia and the EU have adopted a two year time-out period before a ‘rotated’ auditor is allowed to resume involvement with the same audit client. Canada, the UK and the US have adopted a five year time-out period.

APPENDIX-1: TENTATIVE ACTION PLAN MATRIX

| MOZAMBIQUE ROSC ACCOUNTING AND AUDITING: TENTATIVE ACTION PLAN MATRIX | | | | | |
|---|-------------------|---------------------|---|-------------------------------|-----------------------------|
| Description of Action | Para No. | Responsibility | Timing of effective implementation | | |
| | | | Short-term (within 1 year) | Medium-term (2 to 4 years) | Long-term (4 to 6 years) |
| MODERNIZING STATUTORY FRAMEWORK | | | | | |
| 1. Strengthening legal framework for accounting, auditing, and corporate financial reporting focusing on: <ul style="list-style-type: none"> • Mandatory application of IFRS and ISA for the public interest entities (PIEs). • Simplified financial reporting requirements and defining thresholds for SMEs. • Updating provisions of Commercial Code and other relevant laws providing greater emphasis on financial reporting, legal backing for use of IFRS and ISA in the context of PIEs; and outlining appropriate framework for monitoring and compliance. • Enacting a new Financial Reporting Act and rationalising provisions with allied laws and regulations in order to improve accounting, auditing, and corporate financial reporting. • Independent audit oversight arrangement and mechanism for ensuring monitoring and enforcement. • Mandating obligatory preparation of consolidated financial statements for group companies. • Providing regulators with adequate authority to sanction appropriately against violations of applicable accounting and auditing standards and rules. • Mandating appropriate requirements for filing of financial statements for all entities that are subject to annual statutory audit and ensuring easy public access to the corporate financial reports. • Harmonizing general purpose financial reporting legislations with tax laws and issuing necessary guidance for reconciling accounting profits/loss with taxable profit/loss. | 53, 54, 55 and 56 | Ministry of Finance |  | | |

| TENTATIVE ACTION PLAN MATRIX (CONTINUED) | | | | | |
|--|----------|---|---|-------------------------------|-----------------------------|
| Description of Action | Para No. | Responsibility | Timing of effective implementation | | |
| | | | Short-term (within 1 year) | Medium-term (2 to 4 years) | Long-term (4 to 6 years) |
| DEVELOPING PROFESSIONAL ACCOUNTANCY BODY | | | | | |
| 2. Establishing twinning arrangement with a reputable member of IFAC for: <ul style="list-style-type: none">• Advising on preparatory work for launching a new professional body.• Preparation of by laws, policies, and procedures and other necessary documentations.• Development of strategic plan, and providing guidance on operational activities.• Assisting to start Mozambique’s own professional accountancy qualification, developing professional learning and practical training arrangements, and professional accreditation.• Supporting the new professional body in fulfilling IFAC’s membership obligations.• Assisting audit firms to build capacities for implementing ISAs and improving audit quality. | 58 | Ministry of Finance/ Professional Accountancy Body |  | | |
| 3. Develop the professional accountancy body as the catalyst for strengthening accounting and auditing practices in both private and public sectors through professional development programs particularly focusing on practical implementation issues of IFRS, IPSAS and ISA. | 59 | Professional Accountancy Body |  | | |
| 4. Providing assistance to the small and medium sized audit firms for capacity building to improve audit quality through imparting knowledge based on IFAC pronouncements. | 61 | Professional Accountancy Body |  | | |
| 5. Issuing practical application guidance on IFRS and ISA, with the support of regional and international organizations. | 62 | Professional Accountancy Body |  | | |
| 6. Introducing awareness programs for improving the degree of compliance with the applicable accounting and auditing standards. | 66 | Professional Accountancy Body |  | | |

| TENTATIVE ACTION PLAN MATRIX (CONTINUED) | | | | | |
|--|----------|-----------------------|---|-------------------------------|-----------------------------|
| Description of Action | Para No. | Responsibility | Timing of effective implementation | | |
| | | | Short-term (within 1 year) | Medium-term (2 to 4 years) | Long-term (4 to 6 years) |
| IMPROVING MONITORING AND ENFORCEMENT | | | | | |
| 1. Conduct systemic and institutionalized monitoring and enforcement in order to ensure compliance with the applicable accounting and auditing requirements. | 57 | Ministry of Finance |  | | |
| 2. Establish an audit oversight arrangement for conducting independent reviews of audit practices, investigations, and enforcing disciplinary actions. | 60 | Ministry of Finance |  | | |
| ACADEMIC AND PROFESSIONAL EDUCATION AND TRAINING | | | | | |
| 1. Improving accounting degree curriculum and teaching delivery focusing on practical implementation aspects of IFRS and ISA. | 63 | Ministry of Education |  | | |
| 2. Implement training of trainers program for smooth transition to IFRS by creating master trainers for furthering training at local level and writing implementation guidance using Mozambique-specific illustrations in corporate financial reporting and auditing. | 64 | Ministry of Finance |  | | |
| IMPROVE CAPACITY OF THE BANKING REGULATOR TO EFFECTIVELY DEAL WITH IFRS FINANCIAL REPORTING BY THE REGULATED ENTITIES | | | | | |
| Building the Bank of Mozambique’s technical and human resource capacities on practical IFRS related issues, and reconciling IFRS and prudential reporting requirements. In this regard, the relevant officials in Bank of Mozambique should be properly trained to monitor and enforce IFRS requirements in the general purpose financial statements prepared by the banks and other regulated entities. | 65 | Bank of Mozambique |  | | |