

VII. Donor Assistance

This chapter describes donor coordination mechanisms and discusses donor activities in relation to financial management and governance arrangements. It is structured as follows:

- 1 – Overview
- 2 – Coordination Mechanisms
- 3 – Asian Development Bank (ADB)
- 4 – World Bank
- 5 – United Nations Development Programme (UNDP)
- 6 – Canada (CIDA)
- 7 – Japan
- 8 – United Kingdom (British Council)
- 9 – United States (USAID)

1. Overview

As of December 1999, there were 185 ongoing donor-assisted projects in the Philippines involving investment of \$12.2 billion. The consensus among donors is to promote more equitable sharing of the benefits of economic growth, reducing poverty at a faster pace, and enhancing the self-reliance and the service-delivery capacity of local governments.

Table 19: Overall External Assistance to the Philippines²⁰¹

External Source (US\$ million)	1994 – 1998 (annual average)		1999 Approvals	
	Loan/ Credit	TA	Loan/Credit	TA
Multilateral				
ADB	403.8	6.3	153.2	7.0
UN System	..	18.6	..	19.3
World Bank	257.3	..	339.4	..
Subtotal	661.3	24.9	492.6	26.3
Bilateral				
Australia	34.3	26.7	..	30.5
Canada	3.1	18.8	..	15.5
France	40.5	0.2
Germany	24.1	15.4	15.1	0.7
Italy	..	1.0
Japan	967.3	85.4	1,318.7	70.6
United Kingdom	15.9	..	16.2	..

²⁰¹ ADB. December 2000. *Country Assistance Plan (2001–2003): Philippines*. p. 30.

	1994 – 1998 (annual average)		1999 Approvals	
	United States	7.0	34.3	..
Subtotal	1,092.3	181.7	1,350.0	117.4
Total	1,753.6	206.6	1,842.6	143.7

2. Coordination Mechanisms

Annual Consultative Group meetings provide an opportunity for the Government and donors to discuss the Government's socioeconomic management to coordinate official development assistance. In addition to Consultative Group meetings and general coordination activities during programming and project processing, donors to the Philippines have been collaborating closely to improve the performance of the official development assistance portfolio, and in important strategic areas such as poverty reduction.

Efforts to improve project implementation have intensified in the past few years. In addition to undertaking a more thorough portfolio review exercise, a process of joint portfolio reviews with the World Bank and the Japan Bank for International Cooperation (JBIC) was initiated in 1999. Special emphasis is being placed on reducing underperforming projects, speeding up disbursement, and improving quality control at entry.

Government is also taking several important initiatives to improve portfolio performance. These include (i) improving coordination, supervision, and facilitation of implementation through strengthening the Presidential Committee on Flagship Programs and Projects; (ii) streamlining the procurement approval procedure; and (iii) strengthening legal and financial support for executing agencies to tackle right-of-way and land acquisition problems.²⁰²

3. Asian Development Bank (ADB)

The Philippines became an ADB member in 1966. As of 30 June 2000, 150 loans had been made to the Philippines totaling \$7,549 million. ADB has also provided technical assistance (TA) for 268 projects totaling \$113 million by 30 June 2000.²⁰³ As of 30 June 2000, audited project accounts and financial statements were due for 34 loans, of which 26 were in

²⁰² Asian Development Bank. December 2000. *Country Assistance Plan (2001–2003): Philippines*. p. 7.

²⁰³ Asian Development Bank. June 2000. *Loan and Private Sector Operations Approvals for the Period Ending 30 June 2000*.

compliance, 7 complied late by less than 6 months, and 1 did not comply (late by 6–12 months). The compliance level of the portfolio rose to 76.6 %, from 33.3 % during the first half of 1999 and from 77.1 % during the second half of 1999.²⁰⁴

Relevant Loan Projects

Loan 1858: Nonbank Financial Governance Program (\$75 million: 2001–2003)

This study provided input into this program's development, which is intended to support the development of stronger financial sector and institutions. Its key pillars are (i) strengthening the governance and enforcement capacity of the regulators, Bangko Sentral ng Pilipinas and SEC; (ii) introducing more transparency in the market; and (iii) encouraging equal enforcement of rules and regulations. Loan implementation is supported by TA 3773: *Strengthening Regulatory Market Governance*.

Loan 1363: Capital Market Development Program (\$150 million: 1995)

The project's objectives were to support financial and corporate governance reforms, particularly the development of capital market institutions with a view to enhancing transparency and predictability in the marketplace.

Relevant Technical Assistance

TA 31656-02: Strengthening Public Finance and Planning of LGUs-II (\$0.100 million: 2002)

This proposed TA is intended to assist the Government to conduct more detailed analysis of its budget processing and project-monitoring mechanism.

TA No. 3310: Capacity Building for Procurement (\$0.400 million: 2000)

This project strengthened institutions with procurement responsibilities.

TA No. 3245: Nonbank Financial Sector Development (\$2.0 million: 2000–2001)

Among other things, this TA has focused on reorganizing and strengthening the SEC.

²⁰⁴ Asian Development Bank. 2000 September. *Semi-Annual Report on Loan and Technical Assistance Portfolio Performance for the Period Ending 30 June 2000*. p. 70.

TA No. 3145: Strengthening Public Finance and Planning of Local Government Units (\$0.870 million: 1999–2000)

This TA focused on strengthening LGU budgeting and finance capabilities.

4. The World Bank

The World Bank's assistance is primarily for tax administration, financial market development, and supervision of financial institutions. In 1998, World Bank approved a Banking System Reform Project,²⁰⁵ which aims to strengthen banking sector regulation and supervision and develop a resolution framework for troubled banks. The release of the second tranche of this loan has been delayed due to the lack of agreement between the Government and the major shareholders on the pricing of government shares in Philippines National Bank (PNB). As a result, the Government has not been able to divest its PNB shares, which is a second tranche loan condition. Furthermore, a proposed loan for \$100 million to support public sector reforms was abandoned in 2000.

Public Sector Reform Loan (2001–; \$100–300 million)

In May 2001, the Government announced its intention to negotiate for a Public Sector Reform Loan to replace the Banking Sector Reform Loan (which lapsed due the Government's inability to comply with loan conditionalities).

Local Government Finance and Development Project (1999–2006; \$100 million)

The Local Government Finance and Development Project for the Philippines is assisting participating LGUs to expand and upgrade their basic infrastructure, services, and facilities and to strengthen their capacities in municipal governance, investment planning, revenue generation, and project development and implementation. It is also enhancing capabilities at the national level to provide technical support and long-term financing to local governments through the Municipal Development Fund (MDF). The project has four components. The LGU subprojects component expands, repairs, and improves basic infrastructure, social and environmental services and facilities. The second component provides LGU training and capacity building for (i) subproject development and implementation; (ii) municipal planning, finances, and management; (iii) improved training modules and delivery mechanisms; and (iv) piloting of new programs including distance learning; LGU twinning; and

²⁰⁵ World Bank. November 1998. *Banking System Reform*. Report No P7235-PH.

collaboration with local governments, nongovernment organizations, and the private sector. The third component supports LGU resource mobilization and monitoring the real property tax administration program; new initiatives to improve creditworthiness and revenue generation; and developing and implementing systems to improve monitoring of fiscal performance and local financial reporting and disclosure. The final component supports the MDF's reorganization and strengthening.

Banking System Reform Loan Project (1998–2001; \$300 million)

The Banking System Reform Project sought to support the strengthening of the banking system and enable it to better withstand current difficulties and future shocks. The focus of this program was to (i) improve on an ongoing basis the incentives for supervisors, bank owners, and the market to strengthen the framework for prudent banking; (ii) enhance the framework and the authorities' preparedness for early intervention and resolution of troubled banks; (iii) strengthen Philippine National Bank towards the standards maintained by the top tier banks in the country; and (iv) reduce the incentives for regulatory and tax arbitrage across financial institutions, and between the peso and foreign currencies.

However, the second and third loan tranches were never released and the loan lapsed in June 2001. This was due to the Government's inability to meet conditionalities, including (i) the full privatization and rehabilitation of the Philippine National Bank; and (ii) legislating an anti-money laundering bill.

5. United Nations Development Programme (UNDP)

The UNDP is supporting the following relevant projects:

Pipeline Project: Building the Capacity of the Department of Budget and Management to Oversee Public Sector Reform

The intention of this proposed project is to strengthen the role of the Department of Budget and Management (DBM) in the public reform process. Technical assistance shall be provided during the preparatory stage for a comprehensive needs assessment study.

Enhancing the Public Accountability Program of the Commission on Audit (2000–2002; \$950,000)

The Australian Agency for International Development (AusAID) is providing the majority of financing for this project, which aims to strengthen the COA. Three reports, which describe government

accounting and auditing, have been prepared under the project. These form the principal information source for Chapter VI – Government Budgeting and Accounting.

6. Canada (CIDA)

The Canadian International Development Agency (CIDA) is supporting two directly relevant projects:

Policy, Training and Technical Assistance Facility (PTTAF) Phase II (1999–2004)

CIDA is providing technical assistance and training to assist government departments and agencies to further develop their internal mechanisms and structure for increased efficiency in policy formulation, planning, implementation, monitoring and evaluation. These agencies include Philippine Deposit Insurance Corporation (PDIC), Bureau of the Treasury (BTr), BSP, SEC, Department of Health (DOH), Department of Education, Culture and Sports (DECS), Technical Education and Skills Development Authority (TESDA), DBM, and COA.

Local Government Support Project, Phase II - LGSP II (1999-2005)

This project aims to enhance the structures and mechanisms of local governments to increase their policy making and administrative capabilities in support of decentralization. It involves the provision of technical assistance, training and advisory services to LGUs.

7. Japan

Japan is the largest donor to the Philippines. It provides official development loans and untied loans through JBIC, and grants and technical assistance through the Japan International Cooperation Agency (JICA). Japan's country strategy for official development assistance emphasizes: (i) strengthening economic infrastructure, especially in power, transport and industry; (ii) poverty reduction and regional development through promoting rural development and improving basic social services; (iii) environmental conservation and disaster management; and (iv) human resource development. While Japan does not directly support financial management and governance activities, it provides indirect support through Japan-based education and training on financial management and public management.

8. United Kingdom (British Council)

While the British Council has not provided support for financial management and governance activities in the past, a forum on public accountability is planned for 2001.

9. United States (USAID)

The United States Agency for International Development (USAID) is implementing a large TA project²⁰⁶ to (i) develop the self-regulating organization (SRO) capacity of the PSE, (ii) assist in drafting rules for implementing the newly-enacted *Securities Regulation Code 2000*, (iii) review the corporate code, and (iv) facilitate company registration procedures within the SEC. Specific activities include, or have included, the following:

Securities and Exchange Commission (SEC) and Philippine Financial Markets (Ongoing \$750,000)

Assistance is being provided to the SEC to strengthen its regulatory framework and oversight of securities exchange in order to improve investor confidence, create a more transparent and stable market regulation, and increase domestic sources of investment financing. This activity also supports a series of advocacy activities aimed at supporting the successful passage of financial and banking policy reforms that will deepen and better regulate the financial markets.

Bangko Sentral ng Pilipinas (Ongoing \$879,000)

Assistance is being provided to BSP to strengthen its ability to effectively supervise and regulate banks (Part of AGILE).

Philippine Stock Exchange (Ongoing \$400,000)

Assistance is being provided to the Philippine Stock Exchange and its related institutions to strengthen governance and improve the image of the stock market as serving the interest of the investors (Part of AGILE).

Improving the Government Procurement System (Ongoing \$500,000)

This activity supports a government-wide effort to comprehensively reform the rules and procedures governing public procurement. The overall objective is to improve the efficiency, speed and transparency of the

²⁰⁶ Using a broad-based approach, the USAID project: *Accelerating Growth, Investment, and Liberalization with Equity (AGILE)* is providing approximately \$14 million in a comprehensive, multi-sector assistance package.

process, as well as to harmonize it with the procurement procedures of major sources of funds.

Strengthening Local Government Finance (Ongoing \$488,000)

Assistance is being provided to the Congressional Committee on Local Government and the DOF Undersecretary responsible for local government affairs in strengthening the financial structure of local government units and in legally enabling appropriate amendments to the Local Government Code (Part of AGILE).

Institutionalizing the Budget Dialogue Group (Ongoing \$312,600)

This activity supports the DBM in its efforts to increase the participatory nature of the national budgeting process (Part of AGILE).

Piloting a Budget Management Information System (Completed \$312,600)

The DBM is being assisted to develop a new budgeting management information system that will respond to the need for transparency and participation in the overall budgeting process (Part of AGILE).

Environmental Accounting Project

This project was funded by USAID through the United States–Asia Environmental Partnership Program. It focused on developing an environmental accounting course for accountants, engineers and managers from large, medium and small companies across the country. The courses included an introduction to the concepts of pollution prevention, clean technologies and environmental accounting, particularly the Total Cost Assessment approach of profitability analysis. It included a set of case studies based on Philippine industry experience. The courses were conducted in September 1999 after which a train-the-trainer course followed to ensure continued dissemination by PICPA.²⁰⁷ The Environmental Accounting project was implemented countrywide in 2000.

²⁰⁷ PICPA. March 1999. United States Representative Phyllis Khan Heads Visit to PICPA on EA Project. *Accounting Times*. Vol 51(2). p. 4.

VIII. Issues and Recommendations

This chapter presents the issues and recommendations that are associated with gaps or weaknesses in accounting and auditing arrangements. These issues and associated recommendations are consistent with those identified by the subsequent World Bank review of Philippine Corporate Sector Accounting and Auditing Practices, which is not surprising as the World Bank consultants were provided with the final draft of the Philippines DSAA report, before commencing their work.

The Philippines was less affected by the Asian financial crisis than some other countries in the region, largely due to better financial management arrangements. Moreover, accountancy is an elite and respected profession. However, the study revealed a range of issues that need attention if accountancy is to maintain its high status and if the Philippines is to successfully attract investment.

- In the case of **accounting and auditing standards and practices**, the study identifies deficiencies in the standards and in standard-setting arrangements. Several recommendations are made to enhance these arrangements so that the Philippines can have world-class accounting and auditing standards.
- The quality of **financial reporting** is undermined by a lack of compliance monitoring. To this end, the study recommends that financial disclosure monitoring be strengthened.
- Regarding **professional arrangements** the study identifies significant weaknesses in CPA licensure standards and quality assurance arrangements. The Philippines accountancy profession was once among the region's strongest. However, in the meantime, international standards and practices were continuously enhanced and neighboring countries developed their professions accordingly. The recommendations are intended to support the return of the Philippines accountancy profession to its former status.
- Standards of **accountancy education and training** might also be raised. To this end, recommendations are made to improve course quality and ensure that accountancy teachers keep up-to-date with international developments.

Some constraints can be addressed with minimal resources and effort. For instance, strengthening the profession by making PICPA membership compulsory for all CPAs. Others are more complex and will take

time, such as enhancing CPA licensure standards (examination, practical experience and continuing professional education).

The Philippines DSAA was undertaken before the other country studies in the 2001–02 DSAA series. The study recommendations were first discussed and debated with representatives from government, the private sector and international organizations at a workshop held at ADB's Manila Headquarters on 12–13 March 2001.

Some of the recommendations were the subject of intense debate. For instance, Philippine accountants could be licensed as CPAs—and could conduct audits—without ever having worked in accountancy. Some study participants disputed the need for a practical experience component in the CPA qualification. They contended that this requirement would be unworkable in the Philippine environment.

Moreover, some study participants disagreed with the study's general conclusion that Philippine financial disclosure and auditing practices were not consistent with international best practice:

“There have been instances of fraudulent reporting and audit failures in the US, United Kingdom, Singapore, Hong Kong and other supposedly best practice countries mentioned in the report. On the average, the Philippine accounting and auditing profession, at least those in the top tier, are comparable, if not better, than some of these countries.”²⁰⁸

Although these countries have had financial reporting and auditing failures—like those in the Philippines—there is a stark contrast in reactions. For instance, in response to recent US financial reporting scandals, stricter controls have been introduced; civil actions have been filed against the offending companies, their officers and their auditors; criminal charges have been laid against involved parties; and there has been intense scrutiny through the media and by the US Congress.

In contrast, following the Philippine scandals involving Engineering Equipment Incorporated (EEI) and Victorias Milling Company (Vicmico), neither PRC nor BOA investigated the auditors, the auditors were reportedly fined minimal amounts and these penalties were never reported in the media.

Whatever the case, the Philippines DSAA provided input into the development of the ADB-supported nonbank financial governance program.²⁰⁹ Some of the government-agreed policy conditions of that

²⁰⁸ Professional Regulation Commission (PRC). 11 March 2002. Comments on the ADB Study on Accounting and Auditing Issues in the Philippines. Letter.

²⁰⁹ ADB Loan 1858-PHI: *Nonbank Financial Governance Program*, for \$75 million, approved on 15 November 2001.

program reflect the study recommendations. Furthermore, ADB is providing technical assistance to strengthen the SEC's monitoring capacity in line with the study recommendations.

Significant efforts have already been made to implement the study recommendations. Each study recommendation—and the issues that it is intended to address—is set out below. The issues and recommendations are divided into two parts as follows.

- Part One: Where the matter referred to may be considered and, if any action is to be taken, this would be better achieved with external assistance.
- Part Two: Where the matter referred to may be considered and, if any action is to be taken, this may be achieved without the need for external assistance.

Part One. Where Donor Assistance Might be Appropriate

1. Advocate Changes to IASB Copyright and Pricing Policies

IASB promulgates IAS and associated guidance materials. The IASCF holds the copyright to these materials. Many developing countries, including the Philippines, are moving towards IAS. Investors, lenders, academics, practitioners and regulators should have access to the IAS and associated materials. However, IASCF's copyrighting and pricing policies effectively limit this access. In doing so, they appear to conflict with the IASB's constitutional objectives. It is recommended that ADB raise this issue with other multilateral and bilateral donor organizations, so that a joint approach may be made to the IASB and the international accountancy profession.

2. Directly Adopt International Accounting Standards

The ASC has recently begun basing IAS-based SFASs. However, (i) SFASs are not being issued as quickly as IASs, (ii) old SFASs are not always modified to reflect the impacts of new SFASs, (iii) IASs are not necessarily fully adopted as a whole, and (iv) a range of accounting policy choices continues to be available to financial statement preparers.

The direct adoption of IASs offers benefits through (i) reducing the costs and efforts associated with standard setting; (ii) improving the credibility of Philippine financial reporting; (iii) providing access to a greater range of training materials; (iv) making Philippine CPA skills more transferable on the international market; and (v) enabling

Philippine financial reporting standards to be current with international pronouncements and practices. Where an IAS does not address a certain country-specific arrangement, there is a case for promulgating a national accounting standard. For instance, Papua New Guinea uses IASs directly but has released a national accounting standard on Plantation accounting.²¹⁰ A Philippine case might possibly be argued for *Dacion en Pago* arrangements.²¹¹

To accommodate diverse international views, IASs offer a range of accounting policy choices. While the available choices have been significantly reduced since 1996, IASs are still criticized for being too flexible. For instance, IAS 2 *Inventories* allows for several valuation methods. Many countries who have adopted, or who are adopting, IASs limit the available choices to improve the consistency and comparability of financial reporting in their country. In many cases, accounting choices are limited to those allowed for taxation purposes.

It is **recommended** that (i) the Philippines adopt IASs directly and completely on 1 January 2004, and that existing SFASs be invalidated at that date; (ii) assistance be provided to prepare training and guidance materials on the differences between IAS and existing Philippines GAAP; and (iii) training programs for practitioners, academics, and regulators in this respect be supported. It is further **recommended** that amendments to IAS be (i) allowed only to remove multiple accounting policy choices, and (ii) effected through overlay regulations rather than a direct amendment to an IAS.

3. Alter Accounting Standard Setting Arrangements

The ASC's accounting standard-setting processes align with international practice, but its structure is heavily weighted in favor of financial statement preparers and auditors. This imbalance is arguably reflected in the wide range of accounting policy choices that SFASs allow. In comparison, the US FASB and IASB reflect users' interests alongside those of preparers. Furthermore, the imprimatur of the PRC, through BOA, is required before accounting standards have legal authority. The BOA, like the ASC, is balanced strongly in favor of the accountancy profession.

²¹⁰ Narayan, Francis B. and Ted Godden. 2000. *Financial Management and Governance Issues in Papua New Guinea*: ADB. p. 42.

²¹¹ See, for instance, Diga, Joselito. 1997. *Accounting in the Philippines*. Published in Baydoun, Nabil, Akira Nishimura and Roger Willet (eds). *Accounting in the Asia-Pacific Region*. Wiley. pp. 202–203.

The FASB and the IASB are, like the ASC, private sector organizations. The issue of whether accounting standard setting should be a government or private-sector function is a common one faced by many countries—it is influenced by a range of factors.^{212, 213} Assigning this role to a government agency can be counterproductive. Research has found that government regulation stifles the profession and that accounting standard setting can become a taxation policy instrument, thereby significantly reducing the value of financial statements to other users.²¹⁴ In the Philippines, the members of the ASC, and in particular the Chair, have devoted enormous amounts of voluntary time over the past 18 years to develop accounting standards. If the preceding recommendation on direct acceptance of IASs is implemented, the balance of the Council's membership re-weighted, and approval responsibility assigned away from the BOA, there seems no reason why the accounting standard setting process should not continue to remain in the private sector.

It is **recommended** that the *Revised Accountancy Law 1975* be amended to reflect the following improvements to accounting standard setting arrangements: (i) accord legal status to the ASC; (ii) prescribe the Council's composition and appointment processes—the composition should reflect a balance of constituency views; and (iii) define the ASC's role as being limited to reviewing IASs and identifying policy choice exclusions in IASs.

4. Strengthen Financial Disclosure Monitoring

There is evidence that financial statements do not comply with financial disclosure requirements. It is **recommended** that assistance be provided to the Office of the General Accountant (OGA) of the SEC to develop and implement (i) a strict monitoring regime over financial disclosures; and (ii) an automatic system of penalties for corporations who breach financial disclosure requirements and for auditing firms that do not qualify audit opinions where financial disclosure requirements are sub-standard.

²¹² Zeff, Stephen. 1987. Setting Accounting Standards: Some Lessons from the US Experience. *Accountant's Magazine*. December. p. 27.

²¹³ Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa Ortega. 2000. *Financial Management and Governance Issues in Selected Developing Member Countries: A Study of Cambodia, People's Republic of China, Mongolia, Pakistan, Papua New Guinea, Uzbekistan, and Viet Nam*. Asian Development Bank. pp. 25–26.

²¹⁴ Armstrong, Mikael and Katerina Hellström. April 1998. A Case Study of the Czech Republic. Stockholm School of Economics: Paper presented at 21st EAA Congress: Accounting in Times of Transition. Antwerp.

5. Directly Adopt IAASB Auditing Pronouncements

The ASPC promulgates SASPs, but is inactive. Consequently, SASPs have a narrow coverage and are behind IAASB pronouncements.

It is **recommended** that (i) the Philippines adopt ISAs, IAPs and all other IAASB pronouncements directly on 1 January 2004, and that existing SASPs be invalidated at that date; (ii) assistance be provided to prepare training and guidance materials on the differences between these pronouncements and SASPs; and (iii) training programs for practitioners, academics, and regulators in this respect be supported. It is further **recommended** that the *Revised Accountancy Law 1975* be amended to require that audits be conducted in accordance with the pronouncements of the IAASB.

6. Strengthen Compliance with Auditing Practices

It appears that Philippine auditing practices differ substantially from international and regional guidelines and norms in four areas: (i) auditor appointment and dismissal; (ii) auditor independence; (iii) audit reporting procedures; and (iv) exposure of auditors to liability. It is **recommended** that assistance be provided to develop and implement regulations covering the following areas: (i) auditor appointment and dismissal (e.g., appointments made by shareholders, automatic resignation at annual general meetings (AGM), and mandatory requirement for communications between incoming and outgoing auditors); (ii) auditor independence (e.g., restrictions on interests, restrictions on services, antilow-balling rules, mandatory rotation of audit firms or audit partners, mandatory disclosures of challenges to objectivity); (iii) audit reporting procedures (e.g., mandatory disclosure of fraud, illegal acts and internal control weaknesses in audit reports); and (iv) exposure of auditors to liability (e.g., remove legal liability caps). It is further **recommended** that assistance be provided to the Office of the General Auditor (OGA) of the SEC so that it can develop the capacity and procedures to ensure compliance with these requirements.

7. Amend the Accountancy Law so that Licensure Standards can be Raised

Qualifying as a CPA has four stages: academic, experience, examination and CPE. The Philippine CPA title meets international standards and regional norms on the first stage. It falls short on the others. There are three possible implications. First, the recently established IFAC Compliance Committee will be reviewing member body compliance with

IFAC guidelines and standards in the next few years. PICPA will have to explain deviations. The IFAC Compliance Committee is responsible for recommending actions to IFAC's Board and Council when member bodies fail to comply with guidelines and standards. Second, ISAR is embarking on a project to benchmark CPA qualifications from around the world. The "grade" given to a country CPA qualification will be based on compliance with international guidelines and practices. This grade will directly affect the international standing and transferability of CPA titles. Third, as a condition of membership, IFAC member bodies are required to comply with guidelines and standards. In this respect, IFAC has issued guidance on the procedures to be followed when agreeing on mutual recognition of qualifications. It appears that the Philippine WTO-GATS and Asia Pacific Economic Cooperation (APEC) negotiation strategy, in relation to accountancy services, is to conclude Mutual Recognition Agreements (MRAs). Under IFAC guidelines, member bodies must take education, examination and experience requirements into account when negotiating MRAs. As a significant exporter of accountancy services, the Philippines appears to be at a negotiating advantage. The legality of any MRAs that the Philippines concludes with other ASEAN countries might be open to challenge, from other APEC and WTO members, based on the quality of CPA licensure procedures.

The accountancy profession is attempting to raise standards—for instance, requiring mandatory CPE—but is hamstrung by the regulatory environment. A particular impediment is the uniform regulation approach applied through the PRC—which oversees 43 diverse professions. The story of CPE over the past decade has been one of endless legal proposals, reversals and court challenges. It is difficult to see how CPA licensure standards can be raised in the existing environment, without enabling legislative changes.

In order to create an environment that will enable CPA licensure standards to be raised, it is **recommended** that the *Revised Accountancy Law 1975* and other laws and regulations be amended to enable the introduction of (i) practical experience requirements for CPA licensure, (ii) a written component to the CPA licensure examination, and (iii) mandatory CPE as a condition of license renewal.

8. Address CPA Licensure Examination Issues

International guidelines recommend that a significant component of a CPA exam should be written, but the Philippine CPA licensure exami-

nation is entirely multiple choice. This approach was taken deliberately to minimize serious “leakage” problems in the examination process—it has been extremely effective in this sense. The tension between minimizing leakage and preparing high quality examinations is also reflected in the quality of examination questions. Examiners individually prepare one section each, but the other examiners do not review their efforts. The Microsoft certification approach provides a successful example of how technology can be employed to ensure that integrity is maintained while examinees are practically tested. This represents an updated approach to that used for the computerized CPA licensure examination. It is **recommended** that options for restructuring the CPA licensure examination be investigated with the objective of (i) introducing a written component into the examination; and (ii) implementing quality reviews over examination question setting.

9. Introduce an Experience Prerequisite for the CPA Title

The absence of a practical-experience prerequisite for CPA licensure does not accord with international standards or regional norms. Philippine accountants can be licensed as CPAs without ever having worked in accountancy. IFAC has published two documents to guide member bodies on how to meet the requirements of IEG 9.^{215, 216} The effective and fair implementation of these requirements in the Philippine environment poses some clear challenges; implementation and monitoring arrangements will need to be very carefully designed. It is **recommended** that specified practical experience be introduced as a prerequisite requirement for the CPA title.

10. Introduce Mandatory Continuing Professional Education

PICPA supports the introduction of mandatory CPE requirements—which international guidelines require. It is **recommended** that (i) mandatory CPE requirements be introduced through enabling legislative changes; and (ii) assistance be provided to design and implement appropriate procedures for monitoring CPE compliance.

²¹⁵ IFAC. Study I: An Advisory on Examination Administration Based on the Practices of Selected IFAC Member Bodies. New York: IFAC.

²¹⁶ IFAC. Discussion Paper on Work Experience. New York: IFAC.

11. Reassign Responsibilities for Monitoring and Investigating Certain Ethical Matters

BOA and PICPA are unwilling to investigate cases involving (i) gross negligence or incompetence, (ii) issuance of an accountant's certificate covering the examination of the client's accounts without observing the necessary auditing standards; or (iii) conduct discreditable to the accounting profession. This is perhaps because accounting firms have a strong representation in these bodies. In contrast, the SEC has shown willingness to investigate these types of ethical matters. Furthermore, the SEC is being restructured so that it can meet its responsibilities under the *Revised Securities Code 2000*. The restructure involves the creation of the OGA. This position was unfilled at February 2001.

It is **recommended** that responsibility for investigating cases involving; (i) gross negligence or incompetence, (ii) issuance of an accountant's certificate covering the examination of the client's accounts without observing the necessary auditing standards, or (iii) conduct discreditable to the accounting profession; be assigned to the Office of the General Accountant of the SEC. It is further **recommended** that assistance be provided to; (i) identify and draft the necessary legislative amendments to effect this reassignment; (ii) identify OGA requirements for implementing these responsibilities; and (iii) support the development of OGA capacity to meet these responsibilities.

12. Implement Quality Control and Assurance Arrangements

The accountancy profession places minimal emphasis on quality control assurance over professional practices—a recent limited initiative has been for the BOA to recognize accounting firms, based on their internal review processes. In contrast, IFAC recommends that member bodies, including PICPA, (i) adopt quality control standards and require individual accounting firms to implement these; (ii) develop and implement programs to review compliance with these standards; (iii) establish programs to review compliance with relevant professional standards for assurance engagements; and (iv) require accounting firms to make appropriate improvements in quality arrangements and procedures when these fail to meet standards. Neighboring countries have adopted robust programs of this nature.

It is **recommended** that assistance be provided for a project to improve professional supervision. The project would involve (i) studying the existing structures and processes of CPA firms; (ii) examining, and drawing useful lessons from international experience with regards to

supervisory regimes (including peer review regimes); (iii) designing a supervisory system for the Philippines that reflects local conditions and provides sufficient flexibility to deal with environmental changes; (iv) implementing the supervisory system and associated reporting systems; (v) reviewing and, where necessary, revising CPA legal responsibilities and associated disciplinary regulations; and (vi) improving the capacity of managers with supervisory responsibilities through training.

13. Introduce Provisional CPA Title

International practice is for CPA titles to be issued only after candidates have completely met academic, practical experience, and licensure examination requirements. In the period between meeting the academic requirements and receiving the full CPA license, accountants are accorded provisional status. They are not, however, allowed to sign audit reports or undertake certain other activities. It is **recommended** that PICPA and BOA establish a provisional CPA title for those who met academic requirements and are gaining prescribed practical experience.

14. Introduce Accounting Technician Membership Category

PICPA essentially has one individual membership category—that of the CPA. It has been estimated that the Philippines has a further 400,000 accountants. It is common international practice for professional bodies to have a range of membership categories with differing qualification criteria—particularly that of Accounting Technician. The establishment of at least one subsidiary membership category within PICPA would provide a transitional route for aspiring CPAs and professional representation for non-CPAs. It would also improve their societal status, and improve their knowledge and competence. Furthermore, this initiative would strengthen PICPA's membership and revenue base. It is **recommended** that PICPA and BOA consider establishing a professional membership category for accounting technicians.

15. Develop Annual Financial Management Scorecard

The establishment and systematic monitoring of financial management indicators would provide a impetus for raising standards. The BOA's initiative, of preparing examination result analyses and distributing these to under-performing academies, is an excellent example. It is **recommended** that assistance be provided to the OGA to (i) design a financial management scorecard; (ii) design and develop data-collection

methods to support the annual preparation of the scorecard; and (iii) prepare a scorecard for the 2001 calendar year.

16. Improve Monitoring of Accountancy Courses

There is a wide disparity in the quality of accountancy courses. Students from poorer families attend institutions with poor educational records in the hope that they will pass the CPA board examination. The BOA has initiated an excellent program to provide feedback to educational institutions on the quality of their courses. It is **recommended** that assistance be provided to the BOA to broaden its educational monitoring initiative.

17. Provide Continuing Training to Professors and Lecturers

There is a wide disparity in the quality of professors and lecturers. Anecdotal evidence contends that professors and lecturers, who teach accountancy courses to less-wealthy students, are not conversant with modern accounting and auditing practices. It is **recommended** that assistance be provided to design and implement a continuing education program for accounting lecturers and professors.

18. Define Accounting Information System Requirements

COA aims to increase the computerization of government accounting and auditing. Before further progress can be made, several policy issues must first be examined and a position agreed. Among others, these include (i) the accounting policy basis, (ii) consolidation policies and methodologies, (iii) the respective emphasis on financial and management accounting, (iv) the desirability of the Canadian practice of modified accrual accounting, and (v) the future of obligation and fund accounting. It is **recommended** that assistance be provided to COA to analyze these issues and develop agreed policies and plans to implement these policies.

Part Two. Where External Assistance is Not Required

19. Directly Adopt IFAC Pronouncements on Ethics

The BOA and PICPA *Code of Professional Ethics*, and procedures for dealing with potential ethical breaches, do not accord with international guidelines. Two examples follow. First, the Board and the Institute should have the authority to investigate potential ethical breaches, even when no complaint has been made. Second, the Board and the Institute should

publicize potential breaches and investigative actions as a matter of course, rather than as a matter of exception. It is **recommended** that the *Revised Accountancy Law 1975* be amended so that (i) the IFAC *Code of Professional Ethics* and other IFAC promulgations on ethical matters be accorded legal status; (ii) existing pronouncements and procedures on ethics be revoked; and (iii) the procedures of BOA and PICPA be amended to accord with IFAC promulgations.

20. Make PICPA Membership Compulsory for CPAs

Despite efforts to make it so, membership of the Accredited Professional Body—PICPA—is not compulsory—only about 20 % of CPAs are members. This limits quality control and educational efforts. It also undermines the financial position of the professional accountancy bodies. It is **recommended** that the Accountancy Law be amended to require membership of PICPA, a requirement for retaining the CPA title.

21. Minimize Compliance (Transaction) and VFM Auditing

Auditors spend the majority of their time on compliance auditing (checking transactions). Minimal time is spent on financial attest auditing as more effort is applied to value-for-money (VFM) audits. A proposed ADB TA will focus on strengthening financial attest auditing and VFM capacities. While this study strongly supports resources being redirected from compliance auditing to financial attest auditing, it cautions against similar redirection to VFM auditing, for three reasons. First, VFM audits are essentially policy evaluations but generally take place long after policies have been implemented. Strengthening the policy-making function, through policy evaluations, is more effective in this sense. Second, in contrast to a well-designed policy evaluation function, VFM audits are generally targeted on the basis of questionable criteria. A review of VFM reports from Supreme Audit Institutions (SAIs) around the world would reveal, in keeping with public choice theory, that issues are targeted for their media worthiness—not necessarily for their impact on significant public policy outcomes. Third, the skills required to conduct a policy evaluation or a VFM audit are generally not those of a CPA. This requires that organization capacity be established. Fourth, even if VFM audits do represent value for money, they inevitably divert resources away from financial attest auditing—a key tool in reducing graft and corruption. For instance, COA already devotes more resources to VFM auditing than it does to financial attest auditing. The SAIs of developed countries, which have a strong financial attest

auditing capacity, can afford to divert resources to VFM auditing. It is questionable whether the same is true of developing countries.

It is **recommended** that COA (i) continue to reduce the resources that are directed towards compliance (transaction) audits; (ii) continue to strengthen financial attest auditing capacity; and (iii) consider the appropriateness of directing scarce resources towards VFM auditing in the absence of a strong financial attest auditing capability.

22. Limit Proxy Voting in PICPA Meetings and Elections

Proxy voting is employed in PICPA elections. It has been contended that large accounting firms collect proxies and cast block votes. It is **recommended** that PICPA's Bylaws be amended to limit the number of proxy votes that individual members can exercise at meetings or during elections.

23. Exempt CPAs from Tax Agent Accreditation

In 1999, under the *National Internal Revenue Code*, the BIR required that tax agents be accredited. This requirement took legal effect from 1 January 2001, but has yet to be implemented in practice. It has been suggested that accreditation will encourage rent-seeking behavior. Moreover, as attorneys are exempt from accreditation, it has also been contended that this exemption should also apply to CPAs. It is **recommended** that the BIR treat CPAs in the same manner as attorneys for the purpose of tax agent accreditation.

24. Limit Accountancy Degree Courses to 4 Years

PICPA proposes that a 5-year accountancy curriculum be introduced. In contrast, the BOA recommends that a 4-year curriculum be continued and that focus be directed towards improving curriculum quality and teaching quality. This study supports the BOA's stand for two reasons. First, IFAC recommends a minimum 3-year curriculum—a longer education program will not necessarily address quality issues. Second, a 5-year curriculum will limit opportunities for less wealthy students. It is **recommended** that a 4-year course limit be placed upon accountancy degree courses.

25. Separate Accounting and Auditing Responsibilities

The Commission on Audit is exclusively responsible for promulgating accounting and auditing rules—per Article IX of the *Constitution 1987*. Their coexistence is inconsistent with the concept of auditor objectivity

and independence. Moves are already underway to address this issue—for instance, Senate Bill No 439 (2000) seeks to create a government accounting office under the DBM—this could be constitutionally troublesome unless carefully designed. However, a proposed ADB TA will examine COA’s structure and responsibilities with the intention of recommending a solution that is in keeping with the Constitution. This study supports efforts to separate government accounting and auditing responsibilities. But, it is **recommended** that initiatives to separate government accounting and auditing functions, be planned in full acknowledgement of Constitutional requirements.

26. Adopt International Public Sector Accounting Standards

There is no consistent set of accounting standards for budgeting and reporting. Major reporting differences result. COA is considering what accounting standards might be appropriate as it prepares for the introduction of accrual accounting. There are three sets of international standards available: (i) IMF Government Financial Statistics (GFS); (ii) UN System of National Accounts (SNA); and (iii) IPSAS. ADB, World Bank, IMF and UNDP have funded the development of IPSASs and are represented on the PSC. The International Organization of Supreme Audit Institutions (INTOSAI) is also represented on the PSC.

Most countries use the cash-based GFS and SNA standards. Furthermore—given that IPSASs are entirely grounded in IASs—a number of governments indirectly use them for preparing financial statements on the accrual accounting basis. While differences remain between GFS, SNA and IPSASs, significant progress has been made towards harmonization. As demonstrated by several governments, the IPSAS basis provides the necessary information to prepare GFS and SNA financial statements. Three advantages would accrue through the adoption of the IPSASs. First, government and private sector accounting practices would be the same. This would enable direct transferability of accounting skills between the two sectors. Second, training and guidance materials are available from governments that have already moved to an IPSAS-compatible accrual basis (e.g., Australia and New Zealand, among others). Third, as IPSASs are essentially IASs under another name, choices in computerized accounting systems are not limited to those with special functionality.

It is **recommended** that IPSASs be adopted if the Government moves to full accrual accounting.

IX. Country Action Plan

The Philippines was less affected by the Asian financial crisis than some other countries in the region, largely due to better financial management arrangements. Moreover, accountancy is an elite and respected profession. However, the study revealed a range of issues that need attention if accountancy is to maintain its high status and if the Philippines is to attract investment.

In contrast to the other country actions presented in this chapter, explanatory comments are included in the Philippine country action plan for two reasons. First, the study recommendations were initially discussed at the March 2001 Manila workshop. In the intervening period, efforts have already been made to implement the recommendations—the action plan describes these efforts. Second, Philippine study participants were less unified—when compared to other country participants—in agreeing on study issues and recommendations. Accordingly, the action plan describes discordant views.

Action	Priority	Donor Assistance?	Country Support	2002–2006
Directly adopt IAS in 2004 <ul style="list-style-type: none"> <i>The Philippines will complete direct IAS adoption by 2005.</i> 	High	✓	✓	■■■■■
Strengthen financial disclosure monitoring and impose strict penalties on erring corporations and auditors <ul style="list-style-type: none"> <i>ADB is providing TA to implement this recommendation.</i> 	High	✓	✓	■■■■■
Directly adopt IAASB pronouncements (International Standards on Auditing) in 2004 <ul style="list-style-type: none"> <i>The Philippines will complete direct adoption of IAASB pronouncements by 2005</i> 	High	✓	✓	■■■■■
Strengthen auditing practices and monitor compliance with auditing requirements	High	✓	✓	■■■■■

DIAGNOSTIC STUDY OF ACCOUNTING AND AUDITING PRACTICES IN THE PHILIPPINES

Action	Priority	Donor Assistance?	Country Support	2002–2006
<ul style="list-style-type: none"> Although one auditing firm strongly disagreed with this recommendation, other study participants were supportive. Moreover, Bangko Sentral ng Pilipinas has recently introduced 5-yearly mandatory rotation of bank auditors. 				
<p>Amend the Accountancy Law so that licensure standards can be raised</p> <ul style="list-style-type: none"> In keeping with the recommendation, the accountancy profession is preparing amendments to the Accountancy Law to support, among other things: (I) mandatory CPE; (ii) quality assurance improvements; and (iii) the introduction of practical experience requirements for auditors. 	High	✓	✓	██████
<p>Introduce practical experience prerequisite for the CPA title</p> <ul style="list-style-type: none"> The PRC is working to address this important international requirement. In particular, auditors are now required to have 3 years' practical experience before they may sign audit reports. 	High	✓	✓	████████
<p>Introduce mandatory CPE</p> <ul style="list-style-type: none"> The Philippines will introduce this international requirement through an amendment to the Accountancy Law. 	High	✓	✓	████████
<p>Reassign responsibility for investigating certain ethical matters from BOA and PICPA to the SEC</p> <ul style="list-style-type: none"> Although there was general agreement that BOA and PICPA had not effectively discharged their responsibilities in this area, there was no clear support for the recommendation on the basis that the SEC would also be ineffective. ADB is providing TA to SEC to strengthen its capacity in this area. 	High	✓	Mixed	██████
<p>Design and implement quality control and quality assurance arrangements over the profession</p> <ul style="list-style-type: none"> In keeping with the recommendation, amendments are being prepared to the Accountancy Law to strengthen quality assurance arrangements. 	High	✓	✓	████████

COUNTRY ACTION PLAN

Action	Priority	Donor Assistance?	Country Support	2002–2006
Introduce provisional CPA title <ul style="list-style-type: none"> Participants in the March 2001 Manila workshop supported this recommendation, as did all associated written comments. However, the PRC subsequently disagreed with the recommendation (March 2002). 	High	✓	✓	■■■■
Improve monitoring of accountancy courses <ul style="list-style-type: none"> In August 2001, the Commission on Higher Education approved a new accountancy curriculum. BOA would appreciate support to implement the new curriculum and associated monitoring arrangements. 	High	✓	✓	■■■■■
Provide continuing training to professors and lecturers <ul style="list-style-type: none"> ADB is supporting a regional response to this important issue.²¹⁷ 	High	✓	✓	■■■■■
Define accounting information system requirements <ul style="list-style-type: none"> COA has acted to define requirements. 	High	✓	✓	■■■
Directly adopt IFAC pronouncements on professional ethics <ul style="list-style-type: none"> BOA has prepared a revised code of ethics that is directly based on the IFAC code of ethics. 	High	✗	✓	■
Make PICPA membership compulsory for CPAs <ul style="list-style-type: none"> On the basis that this would probably delay congressional approval of the Accountancy Law amendments, PRC has not included this requirement in proposed Accountancy Law amendments, but intends to pursue this as a longer term objective. 	High	✗	✓	■■■
Minimize compliance (transaction) and value-for-money (VFM) audits	High	✗	Mixed	■■■■

²¹⁷ ADB TA No. 6028-REG: Small-Scale Technical Assistance for Upgrading Accounting Education (Training the Trainers), for \$100,000, approved on 11 April 2002.

COUNTRY ACTION PLAN

Action	Priority	Donor Assistance?	Country Support	2002–2006
<ul style="list-style-type: none"> With exception of current and former partners from a particular auditing firm, there was general agreement with this recommendation. However, as a nonstock corporation PICPA is required to allow proxy voting. Furthermore, it was suggested that the potential misuse of proxy votes could be addressed by limiting the number of proxies that can be assigned to an individual. For instance, the California Society of CPAs limits proxy assignments to 10. 				
<p>Exempt CPAs from BIR tax agent accreditation requirement</p> <ul style="list-style-type: none"> PRC/BOA subsequently met with the BIR Commissioner and officials to discuss this issue; a memorandum of agreement is being developed to give effect to this recommendation. 	Medium	✗	✓	■
<p>Limit accountancy degree courses to four years</p> <ul style="list-style-type: none"> This issue has since been resolved. In August 2001, the Commission on Higher Education approved a new accountancy curriculum. It requires a minimum of 177 units, which can be completed within 4 years. 	Medium	✗	✓	■■
<p>Carefully separate accounting and auditing responsibilities</p>	Medium	✗	✓	■■■
<p>Adopt International Public Sector Accounting Standards (IPSASs), if accrual accounting is implemented</p>	Medium	✗	✓	■■■
<p>Advocate changes to IASB copyright and pricing policies</p>	Low	✓	✓	■■■