

# Financial Management and Governance Issues in Pakistan

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Prepared Under Regional Technical Assistance (RETA)  
5877: *Strengthening Financial Management and Governance in  
Selected Developing Member Countries.*

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## Foreword

This report describes financial management and governance arrangements in Pakistan, identifies deficiencies in those arrangements, and presents recommendations to address those deficiencies. For the purposes of this study, financial management and governance arrangements are narrowly defined as being accounting and auditing arrangements and practices.

The report was prepared for the Asian Development Bank (ADB) by Ted Godden, with overall guidance from Francis B. Narayan, Lead Financial Specialist. Research assistance was provided by Furqan Saleem, between May and June 2000 under Regional Technical Assistance (RETA) 5877 – *Strengthening Financial Management and Governance in Selected Developing Member Countries*. The contents of the draft report were discussed and debated with representatives from the Government, the private sector, and international organizations at a workshop that was held in Islamabad on 5-6 June 2000. The issues and recommendations were further discussed at an international conference at ADB headquarters in Manila on 16-18 October 2000.

This report should be read in conjunction with the Summary Report, which identifies and examines selected issues in relation to financial management and governance.<sup>1</sup>

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<sup>1</sup> Narayan, Francis B., Ted Godden, Barry Reid, and Maria Rosa P. 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.

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## Currency Equivalents

( as at 5 November 2000 )

Currency Unit – Pakistan rupee (PRe)

PRe 1.00 – \$0.01758

\$1.00 – PRe 56.88

The value of the Pakistan rupee is determined using a floating exchange rate.

## Abbreviations

ADB	Asian Development Bank
AGP	Auditor-General of Pakistan
ASOSAI	Asian Organization of Supreme Audit Institutions
AusAID	Australian Agency for International Development
CAPA	Confederation of Asian and Pacific Accountants
CPA	Certified Public Accountant
CPE	Continuing Professional Education
IAAS	International Accounting and Auditing Standards
IAS	International Accounting Standards
ICAP	Institute of Chartered Accountants of Pakistan
ICMA	Institute of Cost and Management Accountants
IFAC	International Federation of Accountants
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standard
MOF	Ministry of Finance
PAC	Public Accounts Committee
PAD	Pakistan Audit Department
PIFRA	Project for Improvement to Financial Reporting and Auditing
PIPFA	Pakistan Institute of Public Finance Accountants
PTCL	Pakistan Telecommunications Company Limited
RETA	Regional Technical Assistance
SAI	Supreme Audit Institution
SECP	Securities and Exchange Commission of Pakistan
SOE	State-owned Enterprise
TA	Technical Assistance
UNDP	United Nations Development Program

## Notes

- (i) The financial year of the Government, and most organizations, ends on 30 June.
- (ii) In this report, \$ refers to US dollars.

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# Executive Summary

## Background

Pakistan is an Islamic Republic and its capital is Islamabad. Its assets include a rich cultural heritage, abundant natural and human resources, a large and potentially more productive agricultural sector, and a strategic location for trade. Although Pakistan has been burdened by internal political instability and costly regional conflicts in its first 53 years of independence, it has still managed to achieve substantial economic growth.

While Pakistan's social welfare indicators have improved over the past two decades, progress remains slow and the challenges daunting. Only 40 percent of the population is literate, compared to the average literacy rate of 49 percent in South Asia and 53 percent in low-income countries worldwide.

The economy has been slowly recovering since the second half of 1999 because of improved agricultural performance. However, the balance of payments remains fragile and the long economic stagnation hampers the government's efforts to reduce rampant poverty. Medium-term economic prospects depend on political stability, structural reforms, and capital inflows.<sup>2</sup>

## Developments

Since Pakistan gained independence in 1947, the Republic has been under military rule for 50 percent of the time. The current government is headed by a military regime that came into power on 12 Oct 1999. The Constitution was promulgated in 1973 and includes articles covering the Annual Budget, Federal Consolidated Fund and the appointment and duties of the Auditor-General.

In 1951 the Institute of Cost and Management Accountants was formed and legally established in 1966. In 1961 the Institute of Chartered Accountants of Pakistan was legally established. In 1984 the Pakistan Institute of Public Finance Accountants of Pakistan was legally established under the Companies Act. The accounting profession in Pakistan is strong and accounting and auditing standards are well established and based on International Accounting Standards (IAS).

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<sup>2</sup> Asian Development Bank. 2000. *Asian Development Outlook 2000*. p. 143.

## **Accounting and Auditing in Pakistan**

The Government accounting system in Pakistan is governed by the Pakistan (Audit and Accounts) Order 1973 that requires submission by the Auditor-General of a General Financial Statement incorporating a summary based on the Consolidated Fund and the Public Accounts. The Auditor-General is responsible for both accounting and auditing in Pakistan, however a committee has been established to review this situation.

In the private sector, the Companies Ordinance 1984 requires that account books be kept and details the financial reporting requirements of listed companies and unlisted companies. The Act also contains details of audit requirements. Mandatory application of each International Accounting Standard (IAS) is also prescribed by issue of Special Regulatory Orders issued by the Securities and Exchange Commission.

The accounting basis of the public sector is cash and the private sector uses full accrual. The Auditor General is responsible for auditing and accounting and is a member of the International Organization of Supreme Audit Institutions (INTOSAI). All international big five accounting firms are represented and most have Pakistan citizens as their principals.

## **Professional Infrastructure**

Three accounting organizations exist in Pakistan. These organizations are established legally and they are all members of the International Federation of Accountants (IFAC).

The Institute of Chartered Accountants of Pakistan (ICAP) has 2,400 members and is governed by a Council, through the Standing Committee, and other Committees. Members must pass pre-entry proficiency tests and foundation examinations.

The Institute of Cost and Management Accountants of Pakistan (ICMA) has over 1,400 qualified members. It instigated an active training program four years ago, and there are now 23,000 registered students. A Council, through the Steering Committee, and other Committees, governs ICMA. Members must have a degree or equivalent, for entry.

The Pakistan Institute of Public Finance Accountants (PIPFA) has 1,450 members who are mainly public servants. The PIPFA was formed to produce a second tier of professionals. A Board of Governors, through the Standing Committee and other Committees, governs it. The

prerequisite entry is intermediate examination from a recognized education board, university or institution.

### **Accounting and Auditing Standards**

The ICAP plays the major role in setting accounting and auditing standards. ICAP publishes Exposure Drafts and receives members' comments. ICAP then recommends acceptance of IAS to Securities and Exchange Commission and, if in agreement, a Special Regulatory Order is issued under S 234 (3) of the Companies Ordinance and all listed companies must comply with this Order. Almost all International Standards have been adopted in full. Public Sector Accounting Standards have not yet been considered for adoption.

### **Education and Training**

There are 56 universities in Pakistan, the majority of which offer business and accounting degree courses. Public Sector training is mainly undertaken at the Audit and Accounts Training Institute in Lahore. Public Sector pre-service training is a requirement for all new entrants.

ICAP and PIPFA training is available at private colleges and ICMA training is available at the Institute's colleges. ICAP training is based on Pre-entry Proficiency Test, then two years Full-time Foundation Course, then four years training with Chartered Accountants, during which time two stages of the professional exams must be passed to become an associate member. ICMA training at its own colleges is based on passing Foundation and Professional exams and completing three years practical training before becoming a member. PIPFA training is in three stages – Foundation, Intermediate and Final. PIPFA courses are aimed at government accounting and students must complete two years practical training before becoming a member.

### **Government Budgeting and Accounting**

The Constitution contains articles covering the National Budget and National Government Accounts. The Government Accounts are in two parts – Consolidated Fund and Public Accounts. The annual accounts are designed to present all Government accounts on a common and comparable basis. A "Balance Sheet" is prepared; however, the figures do not contain totals of all assets. An Audit Certificate is issued.

Under the Project for Improvement to Financial Reporting and Auditing (PIFRA), the Consolidated Fund and Public Account are maintained. A Modified Cash System is introduced then full accrual is recommended. A Physical and Financial Assets Register is also recommended. Budgeting is compiled in order to be consistent with the Chart of Accounts. Spending ministries are responsible for their own budgets and the coordination of the Budget is the responsibility of the Ministry of Finance.

### **Donor Assistance**

The World Bank (\$28.8 million) sponsors the Project for Improvement to Financial Reporting and Auditing (PIFRA). The highlights are:

- studies commenced in early 1990s and the project commenced in 1997
- the Project has two parts – To improve public sector accounting systems and to provide the basis for enhancing public sector accountability
- the Project includes provision of consultancy assistance to design and implement a core accounting and reporting system for financial reports and budgets. Consultants are currently being sought for these activities
- various manuals and a Chart of Accounts have been distributed for comment, and
- PIFRA does not cover Private Sector Accounting Infrastructure, and Accounting and Auditing Standards.