ASSESSMENT AND STRENGTHENING PROGRAM (ASP)
FOR
CIVIL SOCIETY ORGANIZATIONS (CSO)
AND
GOVERNMENT OF PAKISTAN

REVOLVING FUND ACCOUNTS
FOR
DEVELOPMENT PROJECTS IN PAKISTAN
Implementation Options and Way Forward

DRAFT REPORT ON RESEARCH STUDY

ASP-RSPN

Revolving Fund Accounts for Development Projects in Pakistan: Implementation Options and Way Forward

October 2011

Cooperative Agreement number:
391-A-00-11-01201-00

Implementing Partner:
Rural Support Programmes Network

Author(s):
Assessment and Strengthening Program – Rural Support Programmes Network (ASP-RSPN)

House # 70, Street 25, F-10/1, Islamabad, Pakistan.
Phone +92 51 2114311, Fax +92 51 2114314
Website www.asp.org.pk

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Acronyms and Abbreviations

ADB	Asian Development Bank
AG	Accountant General
AGPR	Accountant General Pakistan Revenues
CoA	Chart of Accounts issued by CGA
CGA	Controller General of Accounts
DAO	District Accounts Office
DG	Director General
EAD	Economic Affairs Division
FCAA	Foreign Currency Assignment Account
GoP	Government of Pakistan
IPSFRS	International Public Sector Financial Reporting Standards
LCAA	Local Currency Assignment Account
MoF	Ministry of Finance
NBP	National Bank of Pakistan
O.M.	Office Memorandum
PD	Project Director
PIFRA	Project for Improving Financial Reporting & Auditing
RFAs	Revolving Fund Accounts
SAE	Schedule of Authorized expenditure
SAP	System, Applications and Products in data processing
SBP	State Bank of Pakistan
USAID	United States Agency for International development
WB	World Bank

Contents.

Executive summary

As part of its endeavor to streamline policies and procedures for effective utilization of foreign aid, Assessment and Strengthening Program (ASP) undertook a diagnostic study through a consultative process to analyze the establishment and operationalization of Revolving Fund Accounts (RFAs) for donor funded projects in the public sector. The study identifies areas where improvements are needed to ensure robustness of the procedure for the RFAs . The approach here is not to reinvent the wheel, but to analyze the gaps and constraints in the present system and suggest measures for removing major bottlenecks in the system. In addition, the research also focused on control related issues in the system and how to mitigate those risks.

The main objectives of the study are mentioned as follows:

- To identify issues and bottlenecks in the establishment and operation of RFAs.
- To identify capacity issues in handling these accounts above project implementation level.
- To streamline the procedure for establishment and use of the RFAs.
- To recommend an updated procedure for adoption by CGA.

The ASP approach for the research study was based on a consultative process by engaging a wide array of stakeholders in a number of government organizations i.e., Ministries, Provincial Departments, offices of the Accountant and Auditor Generals etc. The methodology for the study entailed conventional and non-conventional methods of action research. The methodology comprised of review of literature, focus group discussions and interviews.

The current procedure for opening and operating of an RFA is being regulated through executive notifications issued by the Ministry of Finance (MoF) – the latest version of the notification was issued on January 17, 2012. The opening and operationlization of RFAs involves various agencies such as the Office of the Controller General of Accounts (CGA) and its establishment (Accountant General Pakistan Revenues, Provincial Accountant Generals, District Accounts Offices and Treasuries), National Bank of Pakistan, State Bank of Pakistan besides all donor agencies, including multilateral agencies such as World Bank, Asian Development Bank, United Nations as well as bilateral agencies.

The present procedure adequately provides details about the operation of the RFAs, however, in practical terms there are still gaps and bottlenecks which need to be addressed to have a robust and effective procedure.

The major issues, either procedural or managerial weaknesses, include: i. delays in opening of RFA, ii. un-timely accounting, iii. non-implementation of some instructions in the Revised Accounting Procedure 2011, iv. absence of a defined recognition criteria for debt and expenditure, v. lack of a criteria for recording the cost of debt, vi. restriction on onward disbursements, vii. delays in transfer of funds to Provincial Account, viii. shortcomings pertaining to asset management, loan amortization schedule, ix. contingent liabilities and long term commitments, x. absence of reporting on third party transactions, and xi. non-integration with the government accounting system.

The research analyzed the proposed solutions and recommended certain steps for removing the above mentioned constraints. Major recommendations made under this study include: i. establishment of a focal point/one window for opening and operating the RFAs, ii. improved reporting mechanism, iii. introducing internal controls and checks, iv. full and complete disclosure of third party transactions, v. improving HR management practices, vi. use of IT systems, vii. standardizing the accounting records, viii. incorporation of provisions in the accounting procedures for taking measures to reduce cost of debt, ix. provision for transfer of funds from RFAs, x. integration of RFAs of all the newly incepted projects with the SAP/R3[1] system in the CGA establishment and Ministry of Finance, and xi. provision for refunds to the project and reconciliation of receipts.

The summary is both comprehensive and compact. It is comprehensive inasmuch as it covers both policy and operational gaps known to bedevil the smooth functioning of RFA. It is compact in the sense that it focuses concretely on course corrections by suggesting improved processes and tools. ASP believes that addressing areas of concern highlighted by stakeholders, especially development partners, will go a long way in strengthening the national investment climate.

Finally, a notable feature of this study is the simultaneous development of a toolkit in the shape of a training manual based on recommended improvements.

[1] SAP stands for System, Applications and Products in data Processing. It is the name of a German Software company which provides Enterprise Resource Planning (ERP) software solutions to its client. CGA establishment is using SAP's R/3 version (R/3 stands for a Real time 3-tier architecture: Database, Application Server and Client)

1. Setting the context

1.1 Introduction

Recipients of donor funds for development projects need the money disbursed for expenditure on project activities and are required to produce financial statements and other financial and operational information in line with the fiduciary covenants stipulated in the loan/grant agreements. The Revolving Fund Accounts (RFAs)[2] are central to specialized nature of financial transactions in the donor funded projects. Smooth functioning of RFAs (Foreign Currency Assignment Account (FCAA)/Local Currency Assignment Account (LCAA)) is important for the purposes of spending donor funds in an effective, transparent and accountable manner so that the desired goals of socio-economic development of Pakistan are achieved.

Stakeholders have shown their concern on some aspects of the opening and operation of these accounts, There is, therefore, a dire need to study and address the problems and issues vis-à-vis RFAs faced by various stakeholders especially project managers, development partners and concerned government agencies. The emphasis here is to analyze the constraints in the present system and suggest measures for removing bottlenecks. The research also focuses on particular risk related issues in the system and suggests ways to mitigate those risks. While the focus of this study is the "Revised Accounting Procedure for Opening and Operation of RFAs (Foreign Currency Assignment Accounts)", which was issued on June 30, 2010 and then an amended version was issued on January 17, 2012, the research also takes into account other studies undertaken by other international agencies, past notifications regarding the revolving fund accounts and tracing how the system has evolved over a period of time. The research findings are followed by a set of recommendations for improving the present Procedure and includes a way forward for reforming it.

The subject has remained under discussion in a rich body of literature comprising of academic research papers, reports prepared by the development partners and Government of Pakistan, documents prepared internationally and research on public financial management system in Pakistan as well as studies conducted on overall governance reforms. One of the most recent and important effort was the formation of the working group on Financial Management (FM) & Procurement, Country Systems Strengthening and Harmonization. The Working Group was jointly led by the Government of Pakistan and World Bank and participated by development partners. The working group, though focused on the broader subject of creating harmonization in the government financial management system, dealt with the subject in detail.

The report prepared as product of discussions and deliberations by the working group and research carried out by the experts attached with the working group has given very substantive and practical recommendations. However, there is still a need that the practical issues surrounding RFAs are further analyzed in the context of the concerns pertaining to delays in development projects, reporting of

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[2] For the purposes of this study, wherever the word Revolving Fund Accounts (RFAs) is used it is referring to Foreign Currency Assignment Account (FCAA) and Local Currency Assignment Account (LCAA). Specific use of FCAA and LCAA has been used wherever necessary to further clarify their purpose.

finances in the country systems and reconciliation of the financial statements in different agencies in the Government and donors.

1.2 Objectives

Broader objectives of the research assignment were to conduct a mapping of the practical issues and problems on the ground and assess how much the concerns raised by stakeholders are posing real problems and how they affect the accounting, reporting and auditing processes. As logical corollary the research then looked into addressing these problems. This involved a critical review of the recent notifications for operationalization of RFAs. Detailed ToRs for the study are placed at Annex-A. The specific objectives of the research study were as follows:

- To identify issues and bottlenecks in the establishment and operation of RFAs including specific issues.
- To identify capacity issues in handling these accounts above project implementation level.
- To streamline the Procedure for establishment and use of the RFAs
- To recommend an updated Procedure for adoption by CGA.

1.3 Methodology

RFAs involves multiple and stakeholders and operate in complex financial management systems comprising of the Governments, banks and those of the development partners in-country and abroad. The study, therefore, applied conventional and non-conventional diagnostic techniques to identify the problems surrounding these accounts. This included as follows:

a. Literature Review

The available academic research on the subject was reviewed critically during the course of the study. Official reports and documentation of the government of Pakistan on the subject were also analyzed. The following documents were studied at length; however, the focus was mainly on matters pertaining to RFAs:

a. Technical Assistance on Financial Management and Procurement Systems and Procedures – Harmonization and Alignment (P110360). Final report on financial management system harmonization by South Asia Region Financial Management Unit. The World Bank (May 2010)

b. A Guide to Understanding the Budget in Pakistan: Prepared by USAID-Pakistan Legislative Strengthening Project. (June 2007)

c. Pakistan Public Sector Accounting and Auditing: A Comparison to International Standards. South Asia Region Financial Management Unit (May 2007)

d. Report on fund flow and expenditure tracking follow up study: National Health and Population Facility, Pakistan. (September 2006)

e. Accounting and Financial Management Manual for development projects in Pakistan. TA 4225-PAK: Strengthening of Financial Management Capacity of ADB PMUs in Pakistan (Revised January 2006)

f. Government Accounting: Recent Trends and Direction for India, the Chartered Accountant (January 2006)

g. Financial Management and Governance Issues in Pakistan: Prepared under Regional Technical Assistance (RETA): 5877 Strengthening Financial Management and Governance in selected Developing Member Countries including Pakistan. Asian Development Bank (October 2000)

A synopsis of the above documents is attached at Annex-B.

In addition notifications regarding Procedure pertaining to RFAs issued on the following dates were also reviewed. 3rd July, 1985, 25th November 2002, 15th April 2005, 24th September 2008, 30th June 2010, 27th July 2011

b. Focus Group Discussions

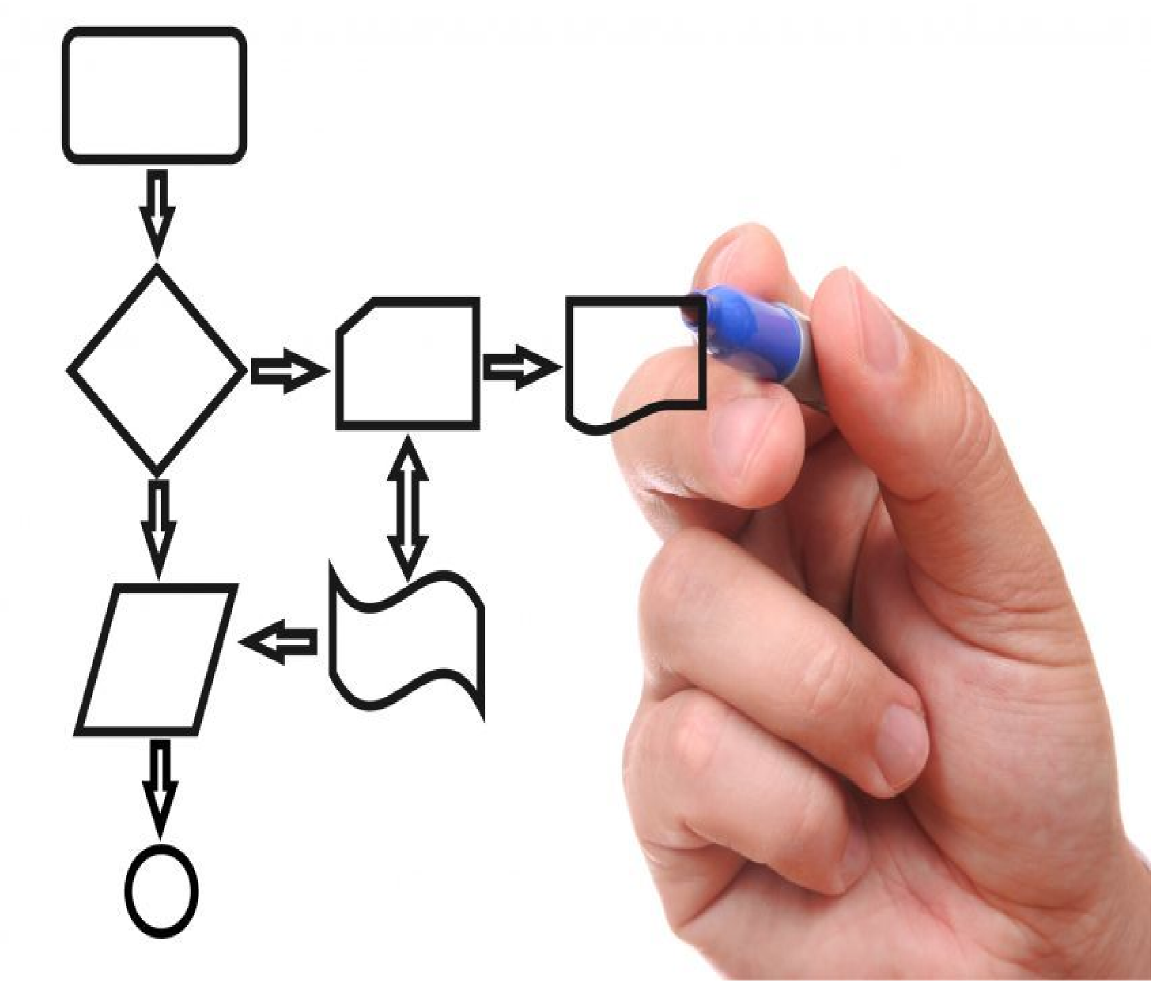
Focus group discussions were held with stakeholders including development partners (both bilateral and multilateral), Federal Government and four Provincial governments. The focus group discussion with Government organizations were organized in such a manner that representatives from cross section of the government departments relating to different areas were gathered in order to have productive discussions where the representative opinions were taken to cross check the information. For example, the focus group discussions would have representatives from: i) officers from the Provincial accountant general hailing from top, mid and lower management ii) Project Authorities i.e. Project Directors and their finance staff.

c. Semi Structured Interviews

In line with the nature of the research study, another diagnostic technique employed was to hold semi structured interviews with individuals in the stakeholder organizations and with relevant experts. These include interviews with officers of Controlling Ministries, Controller General of Accounts (CGA), Federal Accountant General of Pakistan Revenue(AGPR), Provincial Accountant Generals (P-AGs), Ministry of Finance (MoF), State Bank of Pakistan (SBP), National Bank of Pakistan (NBP), selected Project Directors (PDs) and their relevant staff/Project Finance Managers (PFM) using FCAAs/LCAAs.

All Findings and Recommendations have been placed in a matrix form at Annex – C of this document.

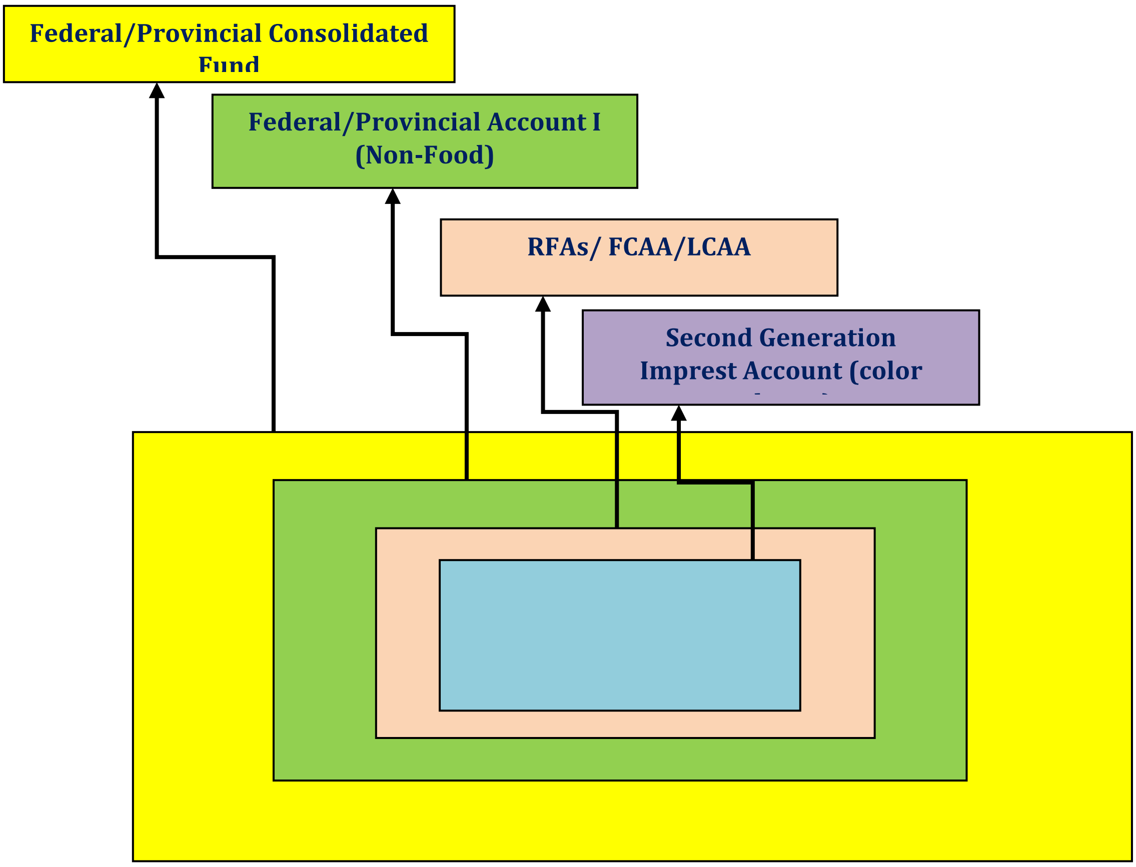
2. Current Procedure



A Revolving Fund Account (RFA) is a separate bank account opened in favor of a delegated authority for specified purposes. An Assignment Account may be drawn on by the delegated authority (usually the project director) located under a spending Division or Department without the requirement for certification and authorization by the AGPR/AG/District Account Office (DAO). Each Assignment Account is established at designated branches of the NBP in local currency. In cases where a project receives both GOP funding and foreign donor funding, separate Local Currency Assignment Accounts (LCAA) and Foreign Currency Assignment Account (FCAA) are maintained.

As far as donor funded projects are concerned, separate FCAA and LCAA is created for each loan/grant. All the RFAs (i.e. FCAAs and LCAAs) together constitute a single separate account called Child Account. The reason why it is called "Child Account" is due to the hierarchy of government accounts/funds. Since RFAs are a part of Federal Consolidated Fund and are recorded under Central Government Account No1 (Non-Food) held with the State Bank of Pakistan (SBP), therefore, all the RFAs bulked together are called Child Account under the Central/Provincial Government Accounts No. I (Non-Food). Below RFAs are Second Generation Imprest Accounts. SGIA can be referred to as a sub-RFA, which receives funds from the primary or First Generation Imprest Account to meet expenditures of a Provincial/regional unit within a project.

<u>Hierarchical setup of Assignment Accounts within Government Accounts</u>



2.2 Why RFAs?

Controller General of Accounts (CGA) is the prime public accounting body of Pakistan working under the Federal Ministry of Finance. With the exception of those organizations within the public sector, which have their own accounting set ups, offices under the control of CGA are providing pre-audit, payment and accounting functions/services for its clients i.e. all the executive agencies (other than self accounting entities) at Federal, Provincial and Local levels. Payments are made in the form of cheques against the budget approved by respective legislatures at Federal, Provincial and District levels. This approval is documented in the form of a Schedule called the Schedule of Authorized

Expenditure. The cheques are drawn in the name of State Bank of Pakistan or its agent i.e. National Bank of Pakistan. Details of how the budget is passed by the parliament are attached at **Annex-D**.

The fund flow mechanism in the development projects, however, is managed through the RFAs outside the ambit of CGA establishment to avoid the complexities and procedural delays in the public sector accounting systems. Logic for not running every transaction through the government system i.e. conducting pre-audits as a control exercise is to avoid rent seeking and delays. This also ensures that there is a continuous and unhindered flow of funds to the development projects, both GoP funding and donor funding, so that these projects are implemented effectively and within the given timelines for achieving development objectives.

2.3 Regulatory Framework

The current Procedure governing RFAs is linked to Article 79 of Constitution of Pakistan, and detailed notifications issued by MoF and Federal treasury rules.

The genesis of RFAs could be traced to a number of notifications issued by MoF from time to time. MoF being the supreme government agency for managing the finances of the federation has set up a regulatory framework which provides detail mechanisms and procedure for the establishment, operation, accounting, reporting and auditing in RFAs. The recent notification dated July 27, 2011 is currently in vogue which is followed by the stakeholders in conjunction with other rules and regulations of the Government of Pakistan and Provincial Governments. For example Federal Treasury Rules **168 to 170 B** are the relevant provisions relating to Letters of Credit, Assignments and other orders for payment. Moreover for the purposes of Internal Control arrangements **General Financial Rules - 13** and the **Internal Control Manual** issued by the Controller General are the reference documents for guidance of Project Management.

2.4 Account Opening

Planning process of the development projects and budget preparation starts with the development and approval of yearly development plans which is called Public Sector Development Program (PSDP) in case of Federal government and Annual Development Plan (ADP) in case of Provincial government. Both these plans are prepared and approved before the approval of respective annual budgets as these plans need to be part of the budgets.

After the approval of PSDP and ADP, Schedule of New Expenditure (SNE) for the respective project is furnished by the Controlling Ministry to the MoF/FD. Budget wing of MoF is the recipient of SNE and makes it part of the draft budget documents laid before the Legislature i.e. National Assembly and Provincial Assembly respectively for Federal and Provincial government as part of the budgetary process. This constitutes formal approval of the budget.

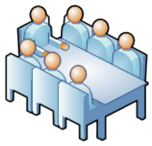
A formal loan/grant agreement needs to be signed by the Economic Affairs Division with the donor agency in case of the foreign funded projects.

Request by Project Management for administrative sanction is approved by the Principal Accounting Officer of the Controlling Ministry. Controlling Ministry's relevant section then requests the endorsement from Ministry of Finance. This endorsement request also has supporting documents such as PC-I, allocations in Pink Book, New Item Statement (Head wise allocations of expenditure) etc. Budget wing of Finance Ministry after review of documents forwards the same to Controller General of Accounts (CGA) for concurrence of opening LCAA. In addition, Controller General of Accounts (CGA) issues a specific Code of Classification in the Chart of Accounts (CoA) for identifying FCAA and LCAA. After concurrence by CGA, Budget wing of Ministry of Finance endorses the sanction letter (sent by Controlling Ministry) and returns the supporting documents to Controlling Ministry. The sanction letter with endorsement is then sent to AGPR with copies to Financial Advisor/Deputy Financial Advisor of Controlling Ministry, Budget wing of Ministry of Finance, Economic Affairs Division etc. AGPR’s relevant account section notes down the New Item Statement (Expenditure heads) on its register and also forwards an authority letter (AGPR’s Treasury Management section) to the National Bank of Pakistan (NBP) for opening LCAA. NBP opens the account after obtaining permission from State bank of Pakistan, (Exchange Policy Department), Karachi.

As far as the donor funding is concerned, the above process is followed, however, CGA office’s concurrence is not sought by the Ministry of Finance. Two separate cheque books are issued by AGPR/AG offices for operating the local and foreign currency Assignment Accounts.

Process for opening and operationalization of RFAs

A. PSDP/ADP reflecting Donor/GoP funding



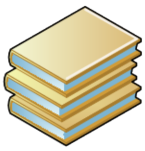
B. Approval of Budget by relevant Legislatures (Schedule of New Authorized Expenditure)

C. Administrative Sanction by Controlling Ministry
D. Concurrence by Controller General of Accounts
E. Endorsement by Ministry of Finance
F. Authority issued by AGPR to NBP

G. NBP opens Assignment Accounts for Foreign and Local currency components (Both A/cs are in Rupees)
H. Project Management uses two cheque books for drawing funds from Assignment Accounts

I. Project Management uses the two accounts as per the conditions prescribed in the loan/grant agreements
j. For each quarter, endorsement for spending the released amount is sought from FA/DFA of Controlling Ministry with regard to local currency Assignment Account

K. Project Management uses the Foreign Currency Assignment Account through withdrawal requests to donor agency while Local Currency Assignment Account is used through the budgetary channels of GoP



2.5 RFA in operation

I. Conversion of foreign currency

On receipt of funds from international agency, SBP advises the Chief Manager SBP-Banking Services Corporation (BSC) to credit Pak Rupee equivalent of Foreign Currency to the FCAA under appropriate Debt or grant Head. The SBP-BSC then authorizes NBP HQ to open FCAA in local currency and a copy is sent to all the relevant stakeholders including Project Director, donor, Planning & Development Division/Department, Economic Affairs Division and Finance Division/Department/AG/AGPR. Foreign currency received under the foreign loan/grant for FCAA is converted into rupees at the SBP Weighted Average Buying Rate of Exchange (WABRE) prevailing on the date of transfer of funds by the donors. This rupee account shows donor's share in the project. With this step, Project Management starts to draw funds from FCAA for the purposes mentioned in the loan/grant agreement.

II. NBP reimbursement

Once both the FCAA and LCAA are operational, project management starts to draw funds from these accounts through different cheque books issued by AGPR/AG offices. However, these payments/cheques are honored by NBP on behalf of SBP (NBP being an agent of SBP for the purposes of payment through FCAA/LCAA). NBP, therefore, is reimbursed by SBP against the payments made from FCAA/LCAA. NBP submits its claim to SBP-Baking Services Corporation (BSC) which is recording and reporting the transactions against individual FCAAs/LCAAs on daily basis. The reimbursement against payments is made to NBP within two working days. In the books of NBP, all the debits, credits and balance in Pak rupees are separately recorded for FCAA and LCAA.

III. Recording and reporting

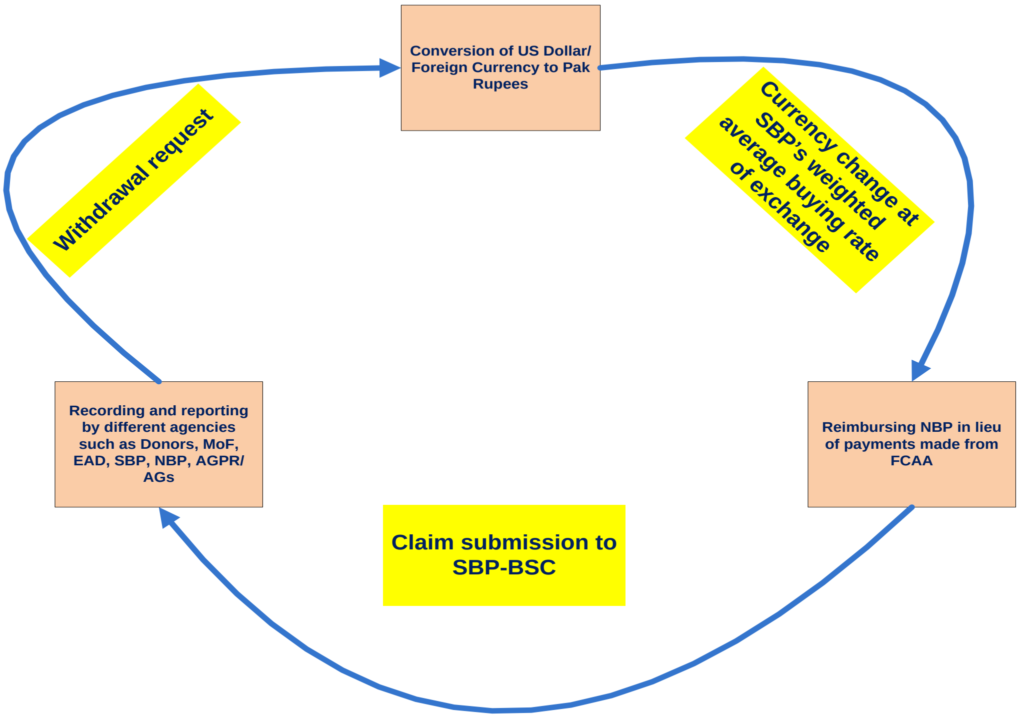
SBP reports balances of both FCAA and LCAA in the daily report of the consolidated balances of the Federal, Provincial Government Account along with other Government Balances of the Federal/Provincial Government (Finance Depts. AGs). The SBP-BSC after making the payment to NBP prepares a debit voucher of each payment for submission to Federal Treasury Office Karachi for accounting.

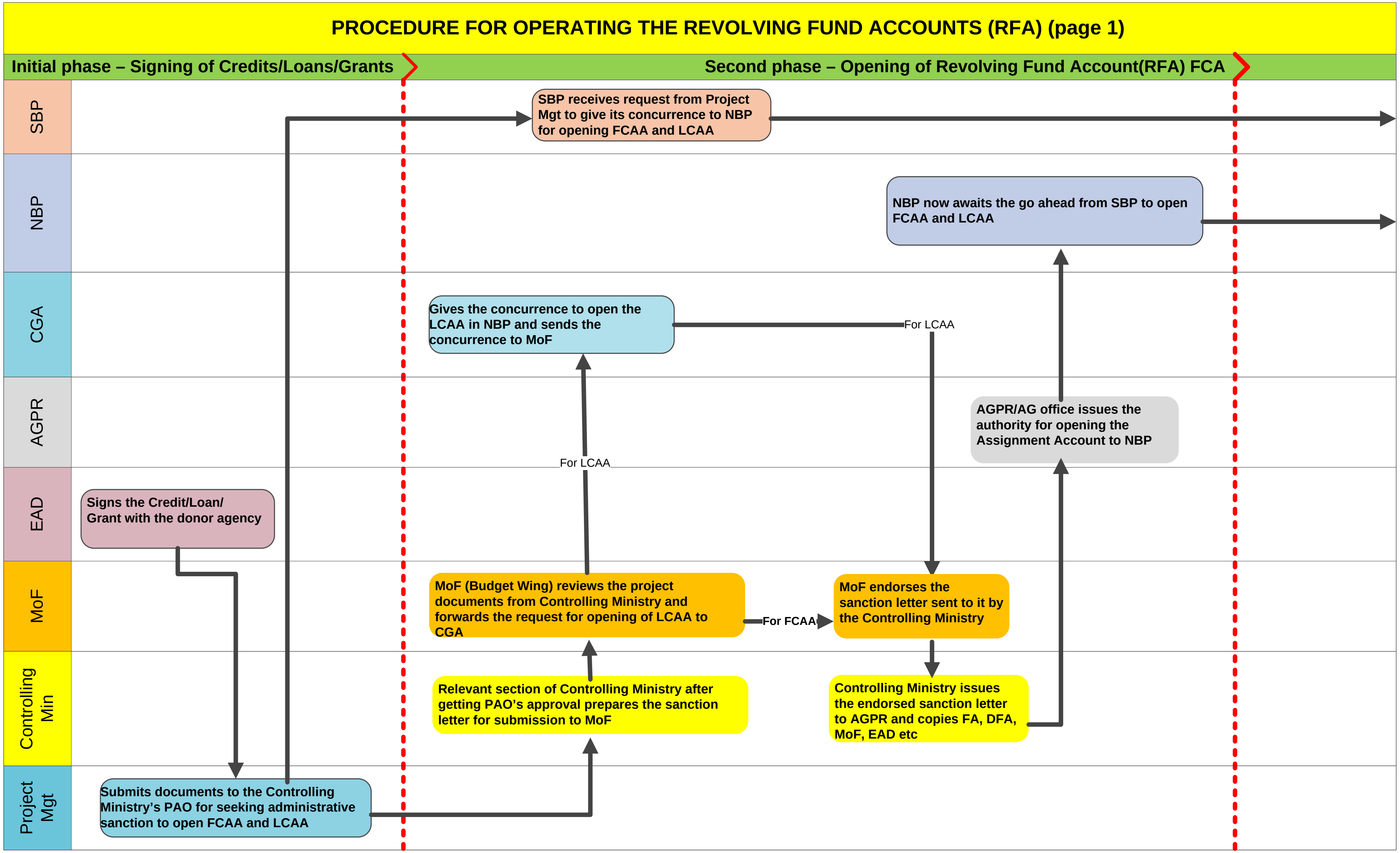
In case of FCAA, the first US Dollar/Foreign Currency receipt in the special account is received on the request of the project director. Generally, these funds are in the range of 10% of total funding or six months projected expenditure, whichever is lower. Respective donor agency then advises its banker to transfer the required amount of US Dollar/Foreign Currency to the State Bank of Pakistan. Funds are transferred in US Dollar/Foreign Currency from the State Bank of Pakistan to RFA in equivalent local currency opened with the National Bank of Pakistan. Similarly the Government transfers counterpart funds in the LCAA. The amounts for GoP funding released are in the range of 20% (quarter I), 20% (quarter II), 25% (quarter III) and 35% (quarter IV). Generally, government counterpart funds are used for operational purposes i.e. salaries, fuel and day to day running expenses of the project, while programmatic interventions/technical assistance costs are met from the foreign currency account.

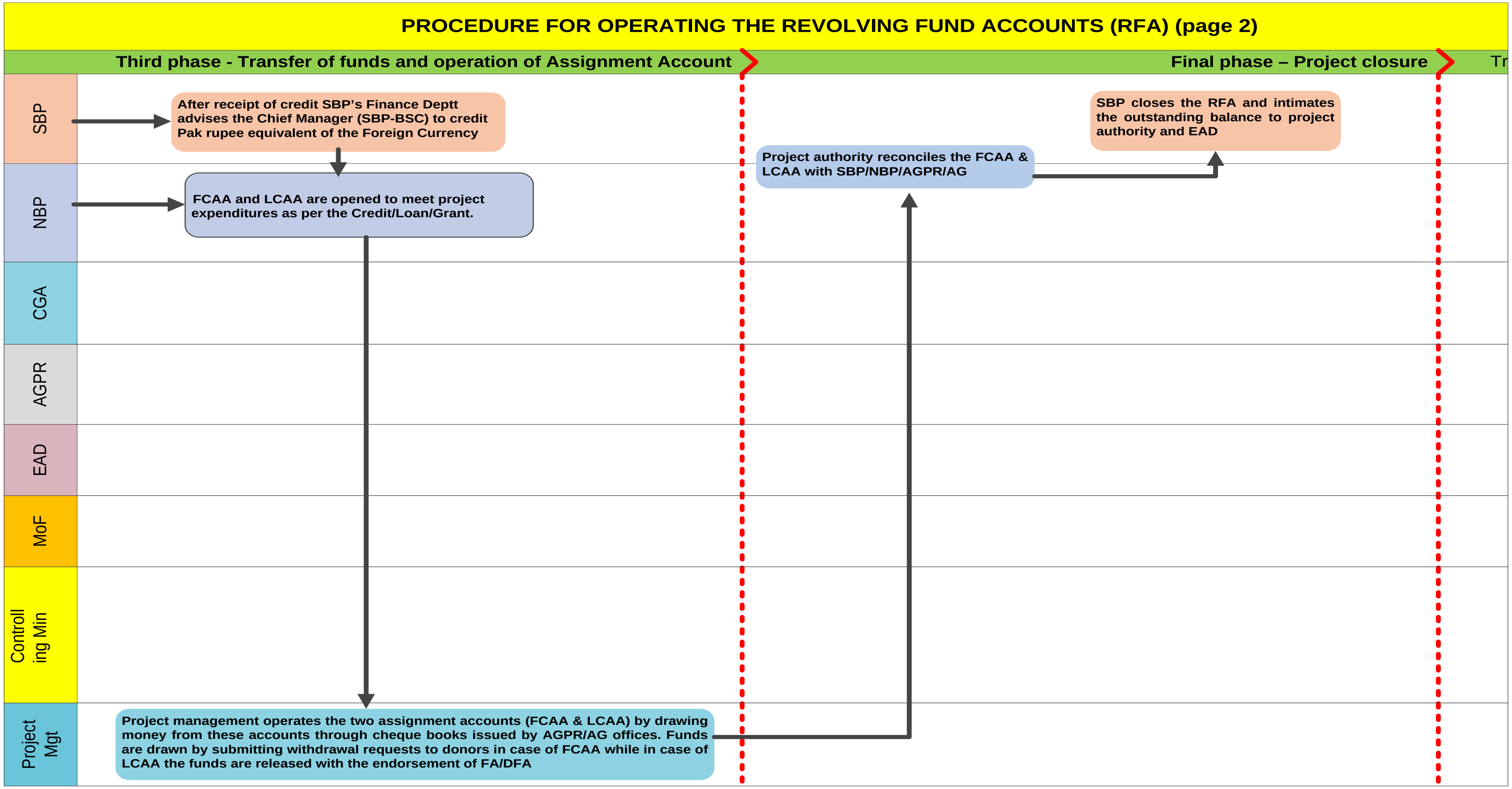
FCAA and LCAA are both lapsable, however, for FCAA the lapsed balance in one year is automatically protected through a budgetary allocation for next year i.e. the Project Authorities can have access to funds on 1st July of new financial year.

The steps related to operating of FCAA are shown in table below.

Summarized version of important steps in operating the FCAA




PROCEDURE FOR OPERATING THE REVOLVING FUND ACCOUNTS (RFA) (page 1)
Initial phase – Signing of Credits/Loans/Grants
Second phase – Opening of Revolving Fund Account(RFA) FCA
SBP
NBP
CGA
AGPR
EAD
MoF
Controlling Min
Project Mgt
SBP receives request from Project Mgt to give its concurrence to NBP for opening FCAA and LCAA
NBP now awaits the go ahead from SBP to open FCAA and LCAA
Gives the concurrence to open the LCAA in NBP and sends the concurrence to MoF
For LCAA
AGPR/AG office issues the authority for opening the Assignment Account to NBP
For LCAA
Signs the Credit/Loan/ Grant with the donor agency
MoF (Budget Wing) reviews the project documents from Controlling Ministry and forwards the request for opening of LCAA to CGA
For FCAA
MoF endorses the sanction letter sent to it by the Controlling Ministry
Relevant section of Controlling Ministry after getting PAO's approval prepares the sanction letter for submission to MoF
Controlling Ministry issues the endorsed sanction letter to AGPR and copies FA, DFA, MoF, EAD etc
Submits documents to the Controlling Ministry's PAO for seeking administrative sanction to open FCAA and LCAA


PROCEDURE FOR OPERATING THE REVOLVING FUND ACCOUNTS (RFA) (page 2)
Third phase - Transfer of funds and operation of Assignment Account
Final phase – Project closure
Tr
SBP
NBP
CGA
AGPR
EAD
MoF
Controll ing Min
Project Mgt
After receipt of credit SBP's Finance Deptt advises the Chief Manager (SBP-BSC) to credit Pak rupee equivalent of the Foreign Currency
FCAA and LCAA are opened to meet project expenditures as per the Credit/Loan/Grant.
Project management operates the two assignment accounts (FCAA & LCAA) by drawing money from these accounts through cheque books issued by AGPR/AG offices. Funds are drawn by submitting withdrawal requests to donors in case of FCAA while in case of LCAA the funds are released with the endorsement of FA/DFA
Project authority reconciles the FCAA & LCAA with SBP/NBP/AGPR/AG
SBP closes the RFA and intimates the outstanding balance to project authority and EAD

3 Findings

3.1 Findings

The mandate of the research study was to diagnose the problems in the opening and operation of the FCAA and LCAA. This included identification of the problems, analyzing them and suggesting viable and applicable solutions to these problems. By doing this, the main objective was to streamline the entire structure, procedures and processes for RFAs.

The succeeding portions of this chapter will present details on the findings of the study and solutions in order to facilitate all the stakeholders in securing a scenario where the development funds are disbursed and expended in an effective way and without hindrance coupled with ensuring a transparency and accountability.

The study revealed that the shortcomings and loopholes in the Procedure (latest notification issued by the Ministry of Finance) for RFAs and its operation are relating to different areas in the public sector financial management which range from opening of the account to the implementation and closing of the account. These issues and problems can be broadly categorized into two major types for the purpose of suitable interventions for improvements relating to policy making and amendment in the Procedure. These two categories are: i. Management weaknesses and ii. Procedural gaps.

The strategy is not to confuse management capacity issues with the omissions in the Procedure itself. Such issues have been segregated so that addressing them is treated separately except where any particular related action or step justifies inclusion in the Procedure. Secondly within the management issues change management has been taken as a separate issue important enough to warrant examination.

3.2 Management Weaknesses

Absence of standard operating procedures, delays in opening of FCAA/LCAA, Un-timely accounting, Non-implementation of Paras XVIII and XIX, Non-reporting by National Bank of Pakistan, Withdrawal applications not circulated, Transfer to other public accounts, Transfer/postings and ownership of the whole process and non-availability of project funds are some of the areas requiring attention by key stakeholders; primarily the MoF, CGA and Project Authorities. Some indicators lead to the conclusion that capacity issue/management weaknesses are the main factor in non-implementation of the Procedure in critical areas. Following management weaknesses were identified as a result of the research study.

a. Delays in opening of FCAA/LCAA

Account opening in some instances has taken as much as four months and even beyond defeating the very purpose of FCAA and LCAA. While primary reason for delays are capacity related at different levels within different stakeholders, lack of awareness and ownership of the process on the part of the relevant staff have also been highlighted as a major cause of delay. Controlling ministries have complained that there were serious capacity issues in the Project Management Units. Relevant documents are either not been submitted or submitted incompletely by Project Authorities. On the other hand Project Authorities state that even if the complete documents are submitted on time, the relevant section of the Controlling ministry takes weeks or even months in processing the case for approval of MoF. Delay in transfer of funds to the Provincial account as per Para X of the Revised Accounting Procedure 2011 was also noted as impediment in opening of RFAs. In addition, non inclusion of the project in the pink book which carries the printed version of the SNE also remains a constraint.

b. Un-timely accounting

Accounting offices are not receiving schedules regarding payment of expenditure as per procedure detailed in Para XIX of the Revised Accounting Procedure 2011 from Project Authorities. This prevents timely accounting because under NAM the expenditure is to be recognized upon issuance of cheques. The PDs are in fact, in most of the cases, not sending appropriate accounts under detailed object to the respective AGs. This is a serious weakness as project accounts must conform to the Project Accounting Module under New Accounting Model of Government of Pakistan and Provinces. This issue remained a common concern for agencies at Federal and Provincial levels.

In addition, Para XII of the Procedure discusses preparation of annual financial statements for project transactions including both receipts and expenditures. Only expenditure reporting has been covered, while no system has been prescribed to report and reconcile the receipts by Project Authorities. Moreover, mechanism for monthly financial statements has not been prescribed in the Procedure.

Since RFA is outside the accounting work flow being implemented by CGA through PIFRA, the above mentioned gaps are leading to inaccurate picture of the government accounts. The issue is further compounded by absence of data base in AGPR/AG offices on the projects operating under their jurisdiction.

c. Non implementation of Paras XVIII and XIX

At present procedure budgetary control checks can only be exercised by the Project Authorities or by AG offices, provided AGPR/AGs receive the schedules as per Para XIX of Revised Accounting Procedure 2011 which states as follows:

In order to record expenditure upon issuance of cheques, the concerned Project Authorities/Drawing and Disbursing Officer (DDO) are required to ensure following:

- **a.** Copy of the schedule in the format at Annex-A of the Revised Accounting Procedure 2011 is received by the concerned AGPR/AG office **on daily basis (or as the cheques are drawn depending on the volume).**
- b. Copy of the same schedule is also sent to the NBP by the DDO of the project when it is submitted to the AGPR/AG office.
- c. The Project Authority/DDO will also provide/submit a statement of account to AGPR/AG **on monthly basis**.

As per sample study, NBP and SBP do not apply these checks as is done by AG offices in case of locally funded Assignment Accounts. In addition, there are chances of fraud being committed due to non-submission of documentation to AGPR/AG.

In addition, checks have been given in Para XIII of the Revised Accounting Procedure 2011 against any fraudulent activity which states that:

After the internal agreements containing provision for the opening of Revolving Fund Accounts have been signed, the concerned Ministries/Divisions/Departments and the Project Implementing Agencies will arrange immediate opening of the Assignment Accounts at a branch of the NBP and special instructions for operation of the accounts, if any, shall be provided to all parties concerned. NBP, will however, open the account after obtaining necessary permission from Exchange Policy Department of SBP Karachi, and will provide a monthly statement of accounts to the Project Management by the end of the first week of the succeeding month. **It shall be mandatory for the NBP, in all cases, to mention clearly the name and account no. of the payee on the Monthly bank statement.** NBP shall send copy of the Bank statement on the 5th of the following month to SBP which shall be returned by SBP to NBP duly verified by 10th of the month. **Even "Nil" balance shall also be reported by NBP to SBP.**

Since NBP is acting as an agent of the SBP and SBP is also banking industry's regulator, therefore, the instructions issued to NBP under the Revised Accounting Procedure 2011would be through SBP. The Revised Accounting Procedure 2011 mentions that it will be mandatory to declare the name and account number of the payee from the Assignment Account. So far, however, SBP **has not issued these instructions to NBP.**

d. Non reporting by National Bank of Pakistan

National Bank of Pakistan does not supply bank statements on time as required under Para XIII of the Revised Accounting Procedure for Revolving Fund Accounts 2011 issued by MoF. Due to non submission of bank statements to AGPR, timely recording of transactions from the FCAA and LCAA is affected.

e. Withdrawal applications not circulated

Copies of withdrawal applications are not being sent in most of the cases to all the agencies indicated in Para XIV of the Procedure. Since withdrawal applications in original are only sent to the donor agencies, therefore, other important stakeholders such as AGPR/AG offices, EAD, SBP etc are not in picture about the amount of withdrawal requested by the Project Authorities from the donor agency.

f. Transfers/postings and ownership

Frequent turnover of key staff especially Project Directors/Coordinators, Finance Managers/Accounting specialists as key personnel dealing with Assignment Accounts and RFAs is a serious constraint that has surfaced during the interview process. This also goes for key staff in the MoF and NBP. The most effective projects are those having key positions occupied by one person for longer periods. In addition, some Project Authorities have complained of a non-facilitative approach by their Controlling Ministry and other relevant institutions. Project Authorities argue that they are doing their job as part of the overall government machinery but have little or no support from the institutions they are dealing with during the course of project implementation.

g. Non availability of project funds

Transfer of donor money to Provincial Government Account as required vide Para X of the Procedure is delayed leading to consequent delays in account opening at Provincial level. Lack of budget allocations is another reason for SBP not transferring the amount. This problem becomes more persistent when the counterpart funding by the government could not be provided due to financial crunch.

3.3 Procedural Gaps

a. Absence of reporting formats and SOPs

The present Procedure, except for mentioning the title of the columns of the annual financial statements (AFS), does not prescribe a detailed standardized expenditure recording/classification format of the AFS. The formats, principles and methods of project accounts have to conform to the requirements of both agencies: i.e. the donors and the AGP/CGA. Donor agencies generally require details under three heads: i. Receipts: donor share and GoP Share to be shown separately, ii. Payments showing operating activities e.g. (Operational and maintenance-GoP, technical assistance/consulting services and training & development and investing activities like civil works, equipment and vehicles and iii) Net increase or decrease in cash is shown and after adjustment with opening balances and foreign exchange gain or loss, year-end balance is shown.

b. Non reporting of Third Party Payments

Reporting of third party transactions (Payments made by donors directly to suppliers of goods or services to the project) to AGPR for incorporation in monthly civil account is not being done. It is important for the accounting procedure to clearly elaborate it. AGPR has adopted an ad hoc measure to take EAD figures for disbursements and subtract the ones recorded as expenditure to assume the balance as Third Party payments. In addition, Para XVI states:

"Direct payment" shall be noted as "third party transaction" for the purposes of reporting and an equivalent amount shall be entered as a "contra" receipt from the donor to ensure that the fiscal balances match the monetary balances of the project. The project finance manager shall be responsible for reporting third party transactions. The Project Authorities shall make sure that the detail of this payment has been communicated in written to EAD/Finance Division and respective AGPR/AG.

So far, no recognition criteria for debt and expenditure in context of third party transactions has been proposed with reference to date and rate of recording Pak rupee amounts in the national accounts. Institute for International Public Sector Accounting Standards (IPSAS) prescribe that there should be full disclosure of third party payments in the financial statements. The Performa attached with Revised Accounting Procedure 2011 is incapable of capturing such critical information.

c. Recording the cost of debt/ Foreign Exchange Loss and Gain

Para IV of the Revised Accounting Procedure 2011 states "The balance of RFAs for donor's share of financing shall be maintained in Pak rupees as well as in US Dollar/Foreign Currency but the funds available for utilization/expenditure to the Project Management would be the Pak Rupee balance.

Since the SBP converts the US Dollar/Foreign Currency from donor in equivalent rupee using exchange rate of the date on which the funds are received from the donor, the equivalent rupee amount becomes the fixed ceiling of Pak rupee funds available for use by the Project Authorities. In case of depreciation in the value of Pak rupees against the US Dollar/Foreign Currency, the Project Authorities and donors are faced with following problem:

a. **Once the Pak rupee ceiling is utilized by the Project Authorities, NBP will stop further payments from the RFA although the US Dollar/Foreign Currency balance will be available in the RFA.**

b. **Upon loan closure, it is mandatory for all Project Authorities to refund the unutilized US Dollar/Foreign Currency in their respective RFAs. However, since the RFAs do not have sufficient Pak rupee cover corresponding to the US Dollar/Foreign Currency balance, the Project Authorities in consultation with EAD/SBP/MoF are arranging for the "shortfall" in Pak rupees. This results in delays regarding loan account closing and it also means continued interest payment by GoP on the unutilized funds lying in RFAs.**

d. Transfer to other public accounts

The Procedure provides that cash payments or funds transfers from Assignment Accounts to any DDO-account or any other account for the sake of onwards disbursements shall be strictly prohibited. This instruction has been ignored in case of funds transferred for certain development works being executed by a government agency other than the project e.g.to DCOs for undertaking certain civil works.

Second generation RFAs are being operated by some projects in violation of Para III of the Procedure that allows only separate accounts for separate grants or loans. Some Projects have even transferred funds to private bank accounts.

e. Asset management, contingent liabilities and long term commitments

Asset management (including reporting as per international Accounting Standards) is one of the significant changes brought about by NAM. Development projects are the entities which create assets. Procedure to be adopted for depreciation/recording of assets has not been prescribed. For example, a draft Purchase Order Form or Asset Recording Form (Form 13B) could have been proposed under the Revised Accounting Procedure 2011. In addition, GAAP demands full disclosure of "Accounting methods", "Contingent liabilities" and "Long term commitments" under a contract. Most the contracts signed by development projects, using RFAs are single and multi year commitments. Effective fund, cash and debt management demands that such information should be available throughout the financial year to the decision makers. The Revised Accounting Procedure 2011 lacks the recording of commitments. The prevailing practice of budgeting, recording and reporting under one single head (A03970) is still in practice.

f. Integration with PIFRA's SAP/R3/R3 system

Revised Accounting Procedure 2011 has not considered the implications of automated systems handling reporting of transactions by Project Authorities. Thus, accounting offices have been showing lack of confidence in accepting direct automated online processing of schedules sent by Project Authorities to AGPR General Ledger System. Currently AGPR does not permit direct online transfer to its General Ledger (GL) under SAP/R3 system. The data sent by the projects online is 'parked' and entries are posted from there into the GL.

g. Refunds to project (Deposits)

Refunds to projects need a procedure for accounting. At present, any refunds made to project are deposited in the government treasury under receipt head and is not made part of the project's balances. This leads to non-reconciled balances in project's accounts.

h. Absence of reconciliation of receipts

The Procedure does not give detail steps for reconciliation of receipts. For example, the Procedure is silent about the format of the document/statement which would used for reporting of receipts amongst SBP/NBP/AGPR/AG/Project Management.

4 Recommendations

4.1 Recommendations

A number of major recommendations have emerged as a result of desk review and structured discussions/interviews with relevant stakeholders and practitioners. These recommendations are aimed to overcome the identified gaps and weaknesses in the existing system. The recommendations have been broadly categorized as those: i. regarding management issues, and ii. regarding procedural issues.

4.1.1 Recommendations regarding management weaknesses

a. One window operation

A central point where representatives from MoF, AGPR and NBP together address the concern of Project Management can be an option to resolve the issue of delays in account opening. This central point can be opened in the SBP.

In addition, a checklist can be added to the process and added to the file so that time taken can be documented for each stakeholder in process.

b. Reporting

A new statement of account prepared by the CGA to be submitted by Project Authorities on monthly basis. This statement should then be uploaded on CGA or AGPR/AG office websites. In addition, all the relevant information pertaining to project accounting including examples of filled forms/statements must be available on the website.

Project database can be populated online by respective AGs and AGPR. This database will be reconciled with EAD, and the project authorities can view the information online. Any corrections to be made will be undertaken by the project management which will be a one-time activity.

c. Internal controls and checks

The Revised Accounting Procedure should include specific stipulations for the project management to improve its internal control environment. In this regard, amendments to GFR-13 and a new version of Internal Control Manual prepared by CGA should be circulated for Project Management's consumption.

The option of post payment external budgetary check by AGPR/AG offices is also there, however, in order to obviate any misuse of such a check, timelines should be inserted in the procedure of post payment check. This timeline should start from the date the monthly statement is submitted and any observation must be communicated to Project Authorities within a stipulated time period.

The value of an effective internal audit is underestimated in development projects. Till date, the internal audit function could not be completely operationalised due to lack of specific rules for project's internal audit function by CGA. This research recommends that the drafting of rules should be the long term goal. However, for short the term, it is proposed that Internal Auditors be appointed in selected projects on pilot basis. The TORs of these auditors may be customized to meet the needs of donor projects who are the main stakeholders on this issue. A starting point in this direction could be improving the TORs developed for Chief Finance and Accounts Officers in Federal Government and adopting them for projects.

d. Full and complete disclosure

International Public Accounting Standards (IPSAS) prescribe full disclosure of "Third party transactions" in the financial statements. The performa attached with Revised Accounting Procedure 2011 needs to be amended. EAD/SBP/NBP/donors must agree on criteria for recording of third party transactions to capture third party transactions as well as rate of recording Pak rupee amounts in national accounts on the same basis i.e. weighted average buying rate of exchange. The idea is to have uniformity in the recording of transactions.

e. Project Management

Project Management is a specialized function within the public sector. The first disbursement shall be linked to the appointment of key staff as is being done in some projects. The ministries and Provincial departments shall therefore have robust ToRs for these positions and selection shall be conducted through a competitive process among a panel of officers from the government. In order to ensure sanctity of tenure PD and the key staff shall not be transferred until the donor has agreed to do so.

f. Availability of project funds

With the establishment of one window operation unit and a certificate with timelines is an option which may show improvements in availability of project funds to Federal as well as Provincial projects. The timelines should be function specific rather than based on yearly cycle of release of funds. For example, time to process the documents at Controlling Ministry may be five weeks rather than in-line with budgetary schedule.

g. Website for uploading scanned images of withdrawal applications

One window operation unit having a fully functional website should be the forum to resolve this issue. Scanned images of withdrawal applications (in original not photocopies) having a group email address will save time and also keep all the stakeholders informed about the circulation of withdrawal applications.

4.1.2 Recommendations regarding Procedural weaknesses

a. Accounting record to be prescribed by CGA

The CGA needs to prescribe a standard set of accounting record which is available at the one window operation unit. This set of record will conform to Project Accounting Module of Accounting Policies and Procedure Manual of CGA and will also be uploaded on the website of one window operation unit.

b. Third party transactions

A format for this purpose is proposed regarding Schedule for recording expenditure against third party payments. It is given below:

1	**Demand No.**	
2	**Fund Code.**	
3	**Loan No.**	
4	**Name of Financier (ADB/World Bank etc)**	
5	**Sub-Detailed Function**	
6	**Project Name**	
7	**Name of Ministry/Division**	
8	**Name of Executing Agency**	
9	**DDO Code**	
10	**Project Code (If allotted)**	
11	**Vendor Name, Bank Account No.**	
12	**Withdrawal Application No.**	
13	**Withdrawal Application Date**	
14	**Date of Transaction**	
15	**Currency of Loan**	

16	**Currency of Disbursement**	
17	**Amount in US $**	
18	**Amount in Pak Rupees**	
19	**Country of Vendor (payees)**	
20	**Country of Disbursement**	
21	**Reference of SBP (if local vendor)**	
22	**Name and signature of Project Director**	

PAYMENTS				**DEDUCTIONS**		
S. No.	**Loan category/ Component code**	**Object Code**	**Amount in Pak Rupees**	**Loan Category/ Component Code**	**Object Code**	**Amount in Pak Rupees**

c. Reduced cost of debt

It is suggested that the Revised Accounting Procedure 2011 be amended so that US Dollar/Foreign Currency amounts available in the respective FCAAs are taken into account. This would ease the burden of cost of debt for the GoP since the interest accrued on unutilized amount would be reduced.

The Revised Accounting Procedure 2011has set out a process for close/short close of project and refunding the amounts as per prescribed timelines. However, the responsibility of observing these timelines should be given to the one window operation unit proposed in this report.

d. Transfer of funds from RFAs

As has been stated in the findings, that Para XV of the Procedure prohibits further transfers from the Assignment Accounts to DDO-account or any other account. However, this restriction also prohibits transfer to Second Generation RFAs.

Following provision, therefore, may be added to Para XV of the Revised Accounting Procedure 2011:

This restriction is for the transfer of unspent cash from government account to private or individual's accounts even in the name of government officers. This is not applicable in case(s) where the Second

Generation RFAs are Assignment Accounts of the Federal/Provincial/District governments or a Personal Ledger Account of a Government department Executing Agency.

This provision will also clarify the issues mentioned in Para III which allows only separate accounts for separate grants or loans.

e. Disbursement to provinces

Timelines should be included in the Revised Accounting Procedure 2011 whereby once the RFA is opened at the Provincial level, the donor funds are remitted to the Provincial Account within a stipulated time period. The times lines are to be agreed amongst all the relevant stakeholders. By having timelines inserted in the Procedure, both the Project Management as well as the Approving Authorities would be able to plan their steps in a much more organized manner.

f. Asset management

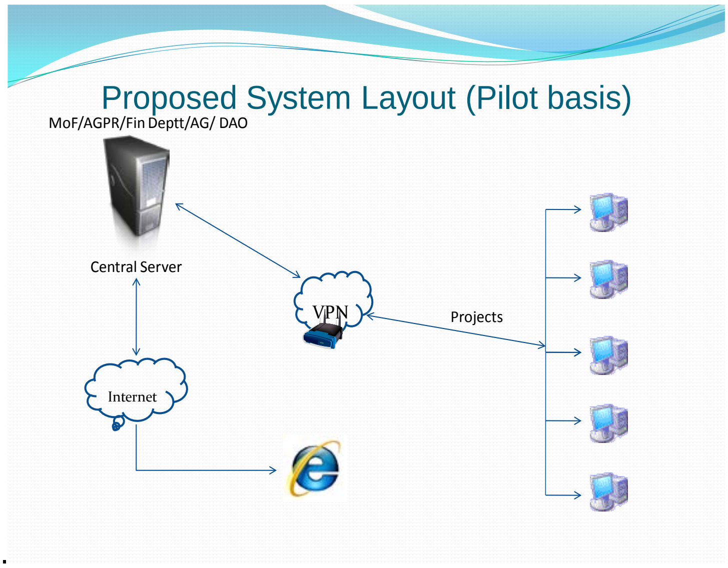
Purchase order form, Asset Recording Form (13B) should be available at the central point or one window for all Project Directors. A handbook of such forms filled with examples can help the Project Authorities to submit the information to AGPR/AGs. In addition, such forms can be uploaded on the website in Excel formats and then be submitted in soft formats to the AGPR/AGs.

The prevailing practice of budgeting, recording and reporting under one object head (A03970) must be discontinued.

A check box form for Project Authorities which includes internal controls should also be available at the central point.

g. Integration with SAP/R3/R3

This research recommends that terminals be provided to all the new projects. There are various options for this. However, for piloting the accounting process and linking it with SAP/R3 system, after the data is retrieved through internet in MoF/Finance Department/AGPR/AG, the budget should be uploaded on the project terminals and then it should follow normal procedures adopted for accounting in the AGPR/AG offices. For the ongoing projects, Planning Commission and the EAD, in consultation with MOF, AGP, and Provincial governments, shall prepare a phased-strategy to integrate these projects with SAP/R3 system.



h. Refunds to project (Deposits)

It is recommended that refunds and receipts on account of project operations shall not be credited to the RFA but deposited through a Challan in Government Account. Under the Government Account a separate account head for Project Refunds and Receipts will be created within the Chart of Account (CoA). Each project will be given a sub classification under the Project Refunds and Receipts for identification of amount deposited. Copy of Challan will be sent to AGPR/AG, respective Controlling Ministry for appropriation of refunds into the project account.

i. Reconciliation of receipts

Agencies involved in recording of receipts are the SBP/ NBP and AGPR/AG. The Procedure should spell out the basic steps starting with AGPR/AGs matching with the figures of SBP. Management Reporting System of SBP should ensure project-wise information including Project ID, Loan/Grant/ Amount received in USD and Pak. Rupee equivalent. Under paragraph III of the Procedure, the balances of the RFAs will be reported in SBP Finance Department Karachi and a daily report of the consolidated balances of the Federal/Provincial Government Account along with other balances has to go to the Federal/Provincial Government (Finance Division/Finance Department/respective A.Gs). The report should serve as a receipt reconciliation document. SBP and AGPR/AGs can hold a monthly reconciliation meeting for the purpose.

4.2 Proposed amendments

Following amendments (in bold) are proposed in the Revised Accounting Procedure dated January 17, 2012

(I) For a foreign donor-assisted project, a Revolving Fund Account (RFA) in respect of donor financing under loan/credit/grant shall be established at a branch of the National Bank of Pakistan (NBP), separately from the account to be established for the government's share of project financing (counterpart funds) if any required. Such accounts shall be in the nature of Assignment Accounts. **Not more than one account can be opened for a particular loan or grant by a single project. However if a loan or grant covers more than one project each project can have a separate Assignment Account.**

(II) The NBP shall be the designated bank for handling all transactions of Revolving Fund Accounts. The foreign currency amounts received under a foreign credit/ loan/ grant for RFAs shall be translated/ converted into Pak Rupees at the State Bank of Pakistan's (SBP) Weighted Average Buying Rate of exchange prevailing on the date of transfer of funds by the donors. The payments out of RFAs by way of reimbursement to NBP would be translated notionally at the aforesaid SBP rate of exchange prevailing on the date of payments from the RFAs. The RFAs at NBP branches shall show debits, credits and balance in PAK Rupees along with the US Dollar/Foreign Currency equivalent. However, for the utilization/ expenditure, the funds available to the Project Management would be PAK Rupees while the equivalent US Dollar/Foreign Currency debit/ credit and balance amounts shall be used by the Project Management for reporting to, reimbursement/ disbursement from and reconciliation with the donors. **Any differential which is resulted due to depreciation in value of rupee against the US Dollar/Foreign Currency and which further results in unspent US Dollar/Foreign Currency balances in the RFAs then the procedure followed will be as per Para IV.**

(III) Separate Revolving Fund Accounts shall be established by the Project Management at the NBP for each of the Loans/Credits/Grants, and each Revolving Fund Account will be designated a special Sub-Fund Identification Number upon establishment of the account. These individual sub-accounts will together constitute a single but separate account (Child Account) under Central Government Account No.1 (Non-Food) held presently with the SBP. Under no circumstances shall separate accounts in different NBP branches be opened for the same grant or Loan. The transactions against individual Assignment Accounts will be recorded and reported along with the other Government balances by the respective office of SBP Banking Services Corporation (SBP-BSC) to SBP Karachi (Finance Department-Government Accounts Division) on daily basis. The reimbursement of payments made by the NBP shall be claimed by NBP from SBP-BSC respective office on daily basis. **Since SBP-BSC**

branches are available in fifteen (15) cities only (including Karachi, Lahore, Islamabad, Peshawar, Rawalpindi, Quetta, Hyderabad, Faisalabad, Multan, North Nazimabad (Karachi), Muzaffarabad, Sukkur, Bahawalpur, Gujranwala, Sialkot, Dera Ismail Khan) therefore, for NBP branches which are not present in the above-mentioned cities, three days will be allowed for these NBP branches to submit their claims to SBP-BSC. The State Bank of Pakistan will ensure the reimbursement to NBP within two working days. For those braches where SBP branches are not available these two working days will be in addition to three working days given to respective NBP branch for submission of its claim to SBP. Exemption for submission by an addition of three days for those branches of NBP where SBP is not located will be given by SBP. The balances of the RFAs will be reported in SBP Finance Department Karachi's daily report of the consolidated balances of the Federal/Provincial Government Account along with other Government balances to the Federal/Provincial Government (Finance Division/ Finance Department/Respective AGs). The CGA will issue a Code Classification in the Chart of Account for RFAs. The code for Assignment Accounts for the Government counterpart funding is already allotted/available i.e. G01191. The SBP BSC respective office after making re-imbursement to NBP shall prepare a separate Debit (payment) Voucher for each payment out of RFAs for onward submission to FTO Karachi. The Federal Treasury Officer Karachi shall pass the following journal entry:

Debit: G01-Cheque Clearing Account – Foreign Aid Assignment Account.

Credit: F01-Central Government Account-I – (Non-Food).

The balance of Revolving Fund Accounts for donor's share of financing shall be maintained in Pak Rupees as well as in the **US Dollar/Foreign Currency** but the funds available for utilization/ expenditure to the Project Management would be the Pak Rupee balance. This account shall also be lapsable. The lapsed balance in one year will be protected through the budgetary allocation in the next year. **In case of depreciation in the value of Pak rupees against US Dollar/Foreign Currency, the balance available in terms of US Dollar/Foreign Currency will be converted into Pak Rupees at the State Bank of Pakistan's (SBP) Weighted Average Buying Rate of exchange prevailing on the date of transfer of funds. Project after concurrence of donor and Economic Affairs Division will utilize the funds available due to the depreciation of Pak rupee against US Dollar/Foreign Currency.**

(IV) If the funds from donors are received in currencies other than US Dollar, these shall be credited in respective Revolving Fund Accounts with Foreign Currency equivalent at the prevailing rate of exchange.

(V) Deleted

(VI) On receipt of the credit advice in respect of a disbursement of foreign currency funds to the project from donors that must be routed through the SBP Karachi, the SBP's Finance Department will advise the Chief Manager (SBP-BSC) Karachi, to credit Pak Rupee equivalent of the **Foreign Currency** to the Assignment Account (sub account of Central Account-I) under the appropriate Debt or Grant head. The Chief Manager will, in turn, and at maximum by the next business day, authorize amount in Pak Rupee credit into the relevant Revolving Fund Account of the project.

In the books of FTO/AGPR:
Debit: F01-Central Government Account-I (Non Food)
Credit: E03301-Permanent Debt (Foreign) – Direct
or Credit: C036-Foreign Grants (under relevant detailed head).

(VII) The (SBP-BSC) Karachi will immediately report the receipt in the Pak Rupee and the equivalent foreign currency to NBP HQ with a copy to respective NBP branch, the relevant Project Director, Planning & Development Division/Department (as the case may be), Economic Affairs Division and Finance Division/Department and AGPR/AG. No Accounting Entry shall be made in the books of DAO/AG/AGPR at this stage.

IX) On intimation of receipt of funds from SBP BSC Karachi, the respective branch of NBP will record it in the Revolving Fund (Performa) Account both in Pak Rupee and **US Dollar/Foreign Currency/Foreign Currency** equivalent under intimation to SBP Karachi, local office of SBP-BSC, relevant Project Director and NBP head office.

(VIII) In case of receipts on account of projects under the control of Provincial Governments, or Local Governments, Financial and Non-Financial Institutions under the administrative control of the Provincial Governments no additional permission shall be required from Federal Ministry of Finance only intimation shall be given. The SBP will simultaneously transfer the funds for credit to the concerned Provincial Government Account. The Provincial Finance Department shall ensure that the Budget allocations are available in the Provincial Schedule of Authorized Expenditure. SBP shall immediately inform the Provincial Authorities if such an action has not been taken to avoid delay in further processing. The following Journal Entries will be passed:

In the Books of Federal Government:

a. In the books of AGPR:
(i) On receipt of funds from donor:
Debit: F01-Central Government Account-I (Non-Food)

Credit: E03301-Permanent Debt (Foreign) - Direct **or**

Credit: C036-Foreign Grants

(ii) On transfer of funds to Provincial Government:

Debit: Demand No. & Function - A08-Loans and Advances to Provinces (under the relevant detailed head of account) **or**

Debit: A052- Grants Domestic (under the relevant detailed head of account)

Credit: F01-Central Government Account-I (Non-Food)

2. In the Books of Provincial Government AG:

Debit: F01-Provincial Government Account-I (Non-Food) Credit: E03302 Permanent Debt (Foreign) - received from Federal Government or Credit: C036-Foreign Grants.

3. On issue of payment/cheque following entry shall be made (Govt. Department only):

Debit: Demand No. & Function Code- A-Expenditures (under the relevant detailed head of account).

Credit: G01-Cheque Clearing Account – Foreign Aid Assignment Account.

(XI) All payments from the Revolving Fund Accounts shall be effected through NBP Cheques/Authorizations issued by at least two persons authorized to sign. The payments into the account in respect of donor funds shall be initiated through withdrawal applications signed by such persons as may be nominated by the Project Management with the approval of the administrative Ministry/Division/Department. Each Project Management shall submit, through its appropriate administrative Ministry/Division/ Department, its budget for the following year as required for all budgets that will be included in the 'Schedule of Authorized Expenditure' and such budgets shall be prepared and submitted with the information including Grant/Loan No. (Project ID), Project Name/Description, Fund Code, Cost Center, Sub-detailed Function, Detailed Object, consistent with the Government Chart of Accounts and within the Government's budget calendar. **A sample audit of the US Dollar/Foreign Currency rate applied on day to day transactions by NBP shall be conducted by the Project Authorities.**

(XII) Each project shall prepare its own annual financial statements comprising expenditure from Revolving Fund Account and Direct Payments (showing in three separate columns for RF Account, GoP Assignment Account and Third Party payments) and submit the same to donor/lender as well as to external audit as required under the loan/credit/grant agreements. The financial statements shall contain Heading of Receipts for both donor and local funding to be shown separately. Payments showing operating activities e.g. (Operational and maintenance-GoP, technical assistance/consulting services and training & development and investing activities e.g. civil works, equipment and vehicles. Net increase or decrease in cash should be shown and after adjustment with opening balances and foreign exchange gain or loss, yearend balance of cash and cash equivalent should be shown. The donors' requirements shall also be met. Nevertheless, the project accounts, being sub-accounts of receipts and expenditures under the Consolidated Fund of the government(s) will be subject to certification as part of the consolidated government financial statements by the Auditor General of Pakistan.

(XIII) After the internal agreements containing provision for the opening of Revolving Fund Accounts have been signed, the concerned Ministries/Divisions/Departments and the project implementing agencies will arrange immediate opening of the Assignment Accounts at a branch of the NBP and special instructions for operation of the accounts, if any, shall be provided to all parties concerned. NBP will, however, open the account after obtaining necessary permission from Exchange Policy Department of SBP Karachi, and will provide a monthly statement of accounts to the Project Management by the end of first week of succeeding month. It shall be mandatory for NBP, in all cases, to mention clearly the name and account no. of the payee on the monthly bank statement. NBP shall send copy of the Bank Statement on 5th of the following month to SBP which shall be returned by SBP to NBP duly verified by 10th of the month. Even 'Nil' balance shall also be reported by NBP to SBP. **SBP shall within three weeks of the notification of this Procedure, issue instructions to NBP for implementation.**

(XIV) Withdrawal Applications will be prepared and submitted to donors by the Project Management, requesting the amount of initial deposits/subsequent funding to the Revolving Fund Account through the foreign currency account of SBP Karachi for further simultaneous credit to the Revolving Fund Account (a named sub-account of the Central Account-I) at the concerned branch of NBP. The assigned identification number of the Revolving Fund Account will be indicated on the Withdrawal Applications. The person authorized to sign Withdrawal Applications and/or operate 'Revolving Fund Accounts' shall furnish copies of the Withdrawal Applications, simultaneously, to their respective Administrative Ministries/Divisions as well as to the Economic Affairs Division, NBP Head Office, Karachi, relevant branch of NBP, SBP Finance Department, Karachi and concerned AG/AGPR office.

(XV) The Finance Managers of the respective projects (or the persons so authorized) shall perform the role of DAO to the extent of authorization for payment within the available budgetary limits. He will also be responsible for the reconciliation through the donors, and financial reporting. All payments, except for an authorized petty-cash to be notified in writing by the Project Director to the relevant NBP branch, shall be made directly to the recipients through crossed-cheques. **Details of name and account no. of the payee on the monthly bank statement shall be provided by NBP to AGPR/AG office**. Cash payments or funds transfers from Assignment Accounts to any DDO-Account or any other account for the sake of onwards disbursements shall be strictly prohibited. **It is clarified that this restriction is for the transfer of unspent cash from government account to private or individual's accounts even in the names of the government officers. This is not applicable in case(s) where the Second Generation RFAs are Assignment Accounts of the**

Federal/Provincial/District government(s) or a Personal Ledger Account of a Government department (Executing Agency). The following entries will be made at the time of issue of payment/ cheque out of each Assignment Account:

Debit: Demand No. & Function Code - A-Expenditures (under the relevant detailed head of Account)

Credit: G01-Cheque Clearing Account- Foreign Aid Assignment Account (for separate Assignment Accounts).

(XIV) The 'direct payment' shall be noted as a 'third party transaction' for the purposes of reporting and an equivalent amount shall be entered as a 'contra' receipt from the donor to ensure that the fiscal balances match the monetary balances of the project. The project Finance Manager shall be responsible for reporting of third party payments. The Project Authorities shall make sure that the detail of this payment has been communicated in writing to EAD/Finance Division and respective AG/AGPR immediately on receipt of information from donors. **Recognition criteria for debt and expenditure with reference to date and rate of recording of Pak rupee amounts in national accounts agreed by MoF/CGA/SBP is in accordance with International Public Sector Accounting Standards (IPSAS)**. The following entry at time of submission of Withdrawal Application shall be passed:

Debit: Demand No. & Function Code - A-Expenditures (under the relevant detailed head of account)

Credit: E03301-Foreign Debt or C036-Foreign Grants (as the case may be).

(XVII) The consultancy charges payable by the donors shall be paid after verification of services rendered by the consultant, by the concerned Project Director/ Ministry/ Division or by the Provincial Governments. However, in case of foreign training prior approval of concerned Ministry/Division will be required.

(XVIII) In case there is balance available in US Dollar/Foreign Currency at the close or short-close of the project which is required to be refunded to the donor, the following procedure shall be adopted for refund of unspent balance:

i. The project authority shall reconcile the account with SBP/NBP at the close of the project to work out the exact amount of unspent balance, within two weeks of the close of a project.

ii. The project authority shall utilize the unspent US Dollar/Foreign Currency balance due to exchange rate differential for project activities. The period extended will be a no-cost extension for the project and no extra budgetary allocation will be made for extended period.

iii. The project authority shall after utilizing the unspent balance close the Revolving Fund Account (RFA) within two weeks of utilizing the unspent balance.

iv. The SBP shall close the RFA and shall intimate the project authority, NBP and

Economic Affairs Division (EAD). The SBP shall intimate the reconciled/exact amount of outstanding balance to project authority and EAD within two weeks of the close of a project.

v. After receipt of intimation from SBP as at (iii) EAD will reconcile unspent balance with concerned donors within one week's time. The Finance Division shall provide necessary funds in the block allocation of EAD in the Demand "Repayment of Foreign Debt" for refund of loan through normal budgetary process and all refunds in respect of foreign loans shall be charged to this Demand. In case of refund of foreign grants, the concerned Ministry/Division/Department shall arrange/provide the budget provision in its respective Demand. The concerned Ministry/Division/Department shall intimate the Head of Account and Demand Number to SBP for accounting/booking of refund.

vi. After receipt of necessary documentation, the EAD shall ensure that the authorization/repayment instructions to SBP are issued within 10 working days.

vii. The SBP shall refund outstanding balance to respective donor within 07 days after receipt of complete documentation.

XIX) In order to record expenditure upon issue of cheques, the concerned Project Authority/ DDO shall ensure that the copy of the schedule in the format at Annex-A is received to the concerned AGPR/AG Office on daily basis (or as the cheques are drawn depending on the volume). The copy of the schedule will also be sent to the NBP by the DDO. The Project Authority/DDO shall also provide/submit a statement of account to AGPR/AG on monthly basis. **AGPR/respective AGs shall be proactive in ensuring that the schedules are received without fail from the Project Authorities and in case of persistent default inform the Controlling Ministry and donors. In case of payments made out of authorized petty cash, Project Authority/DDO shall submit a statement of payments made out of petty cash to AGPR/AG on monthly basis. In order to reduce risk of errors regarding double bookings, cancelled and in lieu cheques, Project Authority/DDO will submit monthly statement of NBP to the AGPR/AGs which will clearly show the name and account no. of payee on the monthly bank statement.**

(XX) The controlling Ministries/Divisions shall reconcile expenditure on account of Foreign Aid with AGPR and EAD on monthly basis. The controlling departments of the Provincial Governments will similarly reconcile the expenditure on foreign aided projects with the AG/Provincial Finance Department. In case of non-reconciliation by 15^{th} of the following month, AGPR/Provincial A.Gs to advise the donor through the EAD not to entertain the next withdrawal request until the accounts are reconciled as per the donor's "Financial Management Guidelines".

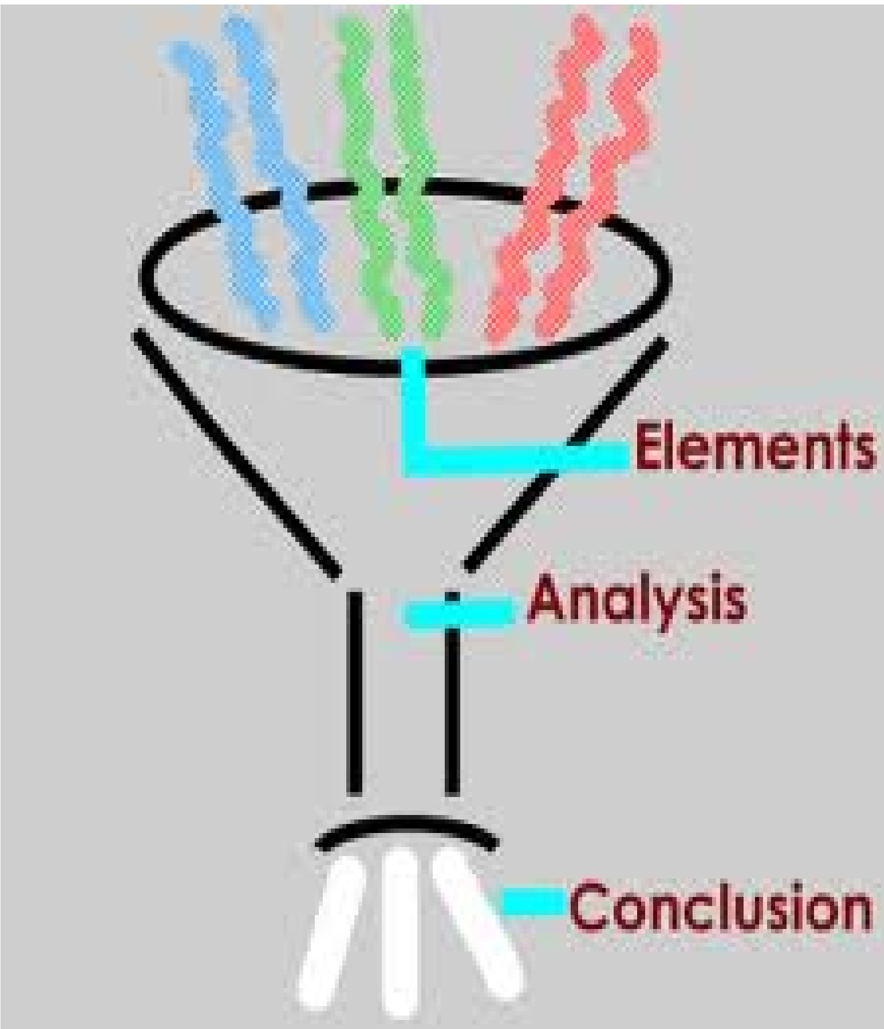
(XXI) **All projects shall ensure that their accounting function is integrated with SAP/R3 systems of the AGPR/AGs to avail the benefits of online transfer of schedules and other information. Software should enable reporting as required for projects under the New Accounting Model (NAM) Appropriate validation checks like digital signatures etc. should be instituted.**

(XXII) **Refunds and receipts on account of project operations shall not be credited to the RFA but deposited through a *Challan* in Government Account. Under the Government Account a separate account head for Project Refunds and Receipts will be created within the Chart of Account (CoA). Each project will be given a sub classification under the Project Refunds and Receipts for identification of amount deposited. Copy of Challan will be sent to AGPR/AG, respective Controlling Ministry for appropriation of refunds into the project account.**

(XXIII) **The CGA shall, with the approval of Auditor-General prescribe a standard set of accounting record to be maintained by all projects to conform to Project Accounting Module of Accounting Policies and Procedure Manual of CGA.**

(XXIV) **The CGA shall, circulate separate guidelines for appointment of Internal Auditors in all donor funded projects. The administrative reporting line for internal auditor would be the Principal Accounting Officer of the Controlling Ministry/Division, while functional reporting of Internal Audit function would be to the respective Public Accounts Committee. In addition, CGA will circulate an Internal Audit manual specifically for development projects in line/updated with the international standards/requirements.**

5 Conclusions



5.1 The Way Forward

Based on the above recommendations, following conclusions/future options are being suggested. These options are not exhaustive by any standards and present only the major steps in the process.

a. As a first step the Notification needs to revised as given here which enables the government to incorporate the recommendations suggested.

b. The Notification shall provide for the establishment of one window operation and subsequently establish the same in the State Bank of Pakistan Islamabad office (the option of opening it somewhere else can be discussed with the relevant stakeholders).

c. The ToRs of this unit will be drafted after discussion amongst the stakeholders; however, the main purpose of opening this unit will be to facilitate opening and operationalising of RFAs.

d. As suggested in the recommendation, each project must be provided with a computer terminal that is linked to the server in AGPR/AGs/DAOs. Budgets will be uploaded into the system wherever the project's management unit is located. A sub-account of the consolidated fund will then be established for each of the 20 development projects, representing the project's designated account. Whenever a payment is made through the system by the project, it will be charged against the sub-account of respective consolidated fund of the government.

e. Subsequent to the revised notification a revised Accounting Procedure shall be circulated to all donor funded project authorities funded (draft has been placed in the recommendations section of this report. However, further improvements/value additions will be required to be made to the notification after the integration of project accounting system with the SAP/R3 server in AGPR/AG/DAOs). A timeline can be decided amongst the donors and relevant government institutions for transition of all the projects to the new system.

f. CGA office will prepare a separate Internal Audit Manual taking into account the provisions of GFR-13. As has been recommended, 20 officers having background in Project Management and internal auditing will be seconded to these projects for implementing CGA's new Internal Audit Manual developed for donor funded projects. By adding value to overall system, Project Management and the executive agencies will appreciate the role played by internal auditors in improving the system. The internal auditors will report to project's steering committee. Within steering committee a separate committee on audit would be constituted for taking up the presentations/reports submitted by the internal auditor.

g. In order to ensure the implementation of the recommendations suggested in the revised notification, a training manual and a toolkit have been developed. The training manual addressed a long outstanding demand from key stakeholders for capacity building and has been developed as a part of the capacity building effort to train those who are involved in the opening and operation of RFAs. This manual will be used to train other PMUs. The toolkit prepared is a step by step guide to open and operationalize the RFAs.

ANNEXES

ANNEX-A

Detailed ToRs for the research

Short Description of Research Topic:

An *Assignment Account* is a separate bank account, more specifically an authorization, opened in favor of a delegated authority, to which funds are released for a specified purpose. Under 2002 rules, as amended in 2010, this account is a government bank account with the National Bank of Pakistan to provide independent drawing facility for nominated projects and other activities, within the prescribed limits.

An Assignment Account may be drawn on by the delegated authority without the requirement for certification and authorization by District Account Office (DAO)/ Auditor General (AG)/ Accountant General Pakistan Revenues (AGPR). This account is established both for local and donor funded projects. There are two types of Assignment Accounts

1. Assignment Accounts used by Schedule of Authorized Expenditure (SAE)
2. Assignment Accounts (also known as special Imprest Accounts) that are used for development projects.

The Assignment Account, typically established separately for each development project, is created with the approval of Ministry of Finance (MoF) in consultation with Controller General of Accounts (CGA) for situations where prompt payment is a necessary requirement of the entity. These accounts are included in the overall cash balance of the Government for the purposes of financial reporting and bank reconciliation.

The *Assignment Account* being established at Project Director level is called first generation Assignment Account and an Assignment Account established at project implementation level i.e. at district level is called second generation Assignment Account. Assignment Account provides a mechanism for a flow of funds that is meant to be effective and efficient.

Research Objectives:

- To streamline the procedure for establishment and use of the Assignment Account.
- To identify issues and bottlenecks in the establishment and maintenance of Assignment Account including specific issues indicated at annex-I.
- To identify capacity issues in handling Assignment Accounts above project implementation level.
- To recommend an updated procedure for Assignment Account for adoption by CGA.

Research outputs

- A policy paper providing detailed current procedures and bottlenecks on the establishment and use of Assignment Account
- Develop a model revised notification of Assignment Account.

- Develop user friendly manual/toolkit for establishment and opertaionlization of the Assignment Account.
- Develop a training manual containing training modules for users.

Proposed research methodology:

- Collection of relevant government notifications / amendments with regards to the subject research.
- Review of the available literature on the subject especially the best and successful practices.
- Face-to-face structured/semi structured interviews with relevant stakeholders such as CGA/AG/AGPR, Ministry of Finance (MoF), Project to Improve Financial Reporting and Auditing (PIFRA) and relevant Project Directors and Director Finance of the projects using Assignment Account.
- Focus group discussions with relevant stakeholders.

Timelines

SN	Tasks	End Date
4.1.2.1	Development of concept paper	June 17
4.1.2.2	Approval of research scope and concept paper by USAID	June 19
4.1.2.3	Finalization of the research scope	June 23
4.1.2.4	Engaging consultant to carry out research	June 27
4.1.2.5	Submission of report and research deliverables	August15
4.1.2.6	Review of report and findings in research committee and approval of USAID	August 20
4.1.2.7	Development of policy recommendations and sharing with USAID for approval	August 27
4.1.2.8	Conducting advocacy workshop for policy implementation	Sept10
4.1.2.9	Sharing of research results	Sept20

ANNEX-B

LITERATURE REVIEW

The literature review comprised mainly of desk reviews and following up through stakeholder consultation. Relevant government notifications/amendments with regard to subject research were collected for this exercise. The research also reviewed available literature on the subject and work done by other agencies in this area (including inter alia World Bank, Asian Development Bank, ICAP). Face to face structure with a standard questionnaire circulated and semi-structured interviews were held with relevant stakeholders such as officers of the AGPR/AGs, CGA and project managers. Finally focused group discussions with relevant stakeholders were arranged and way forward on how to improve the present procedure was discussed.

Although, some bilateral donors do transfer their project funds directly into Commercial Bank Accounts, funds of multilateral donors like the World Bank and ADB are channeled through the State Bank of Pakistan to the nominated commercial bank (NBP) and in effect, are accounted as part of the consolidated fund in the first instance and disbursed in total by the SBP. These funds are regarded as disbursed by the SBP from the consolidated fund as soon as these are transferred to the nominated NBP Account. The funds, however, may remain lying at the NBP and hence not accounted as part of the GoP's cash balance. This has the effect of undermining government's cash management system ***(Final report on financial management system harmonization, May 2010)***.

The situation is further worsened when CGA recognizes such receipts into the consolidated fund but makes no accounting entries under the government's chart of accounts in respect of expenditures made by the projects. Technically therefore, the expenditures reported by the CGA remain understated as no donor-funded project expenditures are captured in their system. This creates a necessity for an improved arrangement whereby all donors funded project receipts and expenditures are transacted and reported along with the governments' own expenses. The justification advanced for circumventing government systems in the process of implementing donor funded projects ranges from slow processing of payment transactions due to some high redundancy in processing steps employed to high rent-seeking potential. ***(Final report on financial management system harmonization, May 2010)***. It is in this backdrop that the study recommends integrating the project accounting with the SAP/R3 system at the Federal/Provincial levels.

Similar views have been expressed in a manual developed for development projects in Pakistan by Asian Development Bank ***(Accounting and Financial Management Manual for development projects in Pakistan, January 2006)***. The manual states that comparability will be achieved if accounting information produced by Project Management is measured and reported in a consistent manner. In this way, it can be compared and contrasted. Similarly, it will help the prefectures and central governments to aggregate data and formulate judgments on a broader range with consistency. Consistency means that the Project Management employs the same accounting treatment for similar events, from one accounting period to another as is done at Federal/Provincial levels.

All transactions in foreign currency are converted in Pak rupees using SBP weighted average buying rate of exchange prevailing on the date of transactions. Cash balances in bank accounts and liabilities in foreign currencies are translated at the rate of exchange prevalent on the balance sheet date. Exchange differences are dealt with using the Income and Expenditure Account. Foreign currency transaction of the Income and Expenditure Account items and Fixed Assets are converted using actual exchange rate on the date of drawdown (i.e. the date on which transfer of funds take place). All local expenditures paid out of the loan account or grant account in rupee is reconverted to foreign currency at the actual exchange rate at which the drawdown was converted on transfer from the external accounts to local accounts. Where expenditure has been met from more than one drawdown, the conversion of the expenditure from local currency to foreign currency is based on first-in-first-out ***(Accounting and Financial Management Manual for development projects in Pakistan, January 2006)***.

All expenditures incurred under development projects included under the Schedule of Authorized Expenditure must be recorded in the Government Accounting system, regardless of the source of funding. Direct funding arrangements between donors and project managers must still be recorded and reported to the Government, if the expenditure is included in the Schedule of Authorized Expenditure. If budget provision does not exist in the Schedule of Authorized Expenditure, the Supplementary Budget in such cases may be obtained from Ministry of Finance / Finance Department (under Technical Supplementary Grant) so that both receipts and expenditures should appear in the Government Accounts ***(Accounting and Financial Management Manual for development projects in Pakistan, January 2006)***.

To conclude, there is broad agreement that an integration of project accounting with SAP/R3 system at Federal/Provincial level can improve governance by providing real-time financial information that financial and other managers can use to administer programs effectively, formulate budgets, and manage resources. Sound integration, coupled with the centralized accounting procedures, will not only help Pakistan gain effective control over its finances, but also enhance transparency and accountability, reducing political discretion and acting as a deterrent to corruption and fraud.

Obstacles should not be underestimated. The road to successful integration is paved with difficulties, such as resistance from the bureaucracies involved; lack of decision-making from the top; weak human capital; corruption and fraud. Moreover, integration would be complicated, expensive, and difficult to manage and maintain. Experience shows that only few of the systems were likely to be sustained after donor support ceased.

Obstacles notwithstanding, the task is still feasible. The technology exists in Pakistan and donor agencies can play a very important role in helping the decision-makers choose the most adaptable and appropriate tool for their environments. The choice of a step-by-step or phased approach offers the best chances for successful implementation as a project can be carefully monitored and reviewed regularly. Given the cost of such exercises, it is important to aim first for piloting the system, which once functioning effectively, can then be extended to other projects. Indeed, the simple demonstration effect of effective integration will generate the necessary demand for more comprehensive systems.

Above all, integration will require patience. The full project life cycle—from definition of objectives, to system specifications, to system procurement, configuration, testing, and rollout—will take time. The time horizon may go beyond the attention span of Donors, which is why it is advisable to divide integration of project accounting with SAP/R3 into clearly defined stages with clear objectives and milestones. As each stage is completed, stakeholders should carefully assess project progress and ensure that the system under development still meets the needs of the government, and that government commitment is still there. The ultimate goal should be to put in place sound systems that are well understood and embraced by counterparts and in the end will be self-sustaining.

ANNEX-C

ISSUE	FINDINGS	RECOMMENDATIONS
MANAGEMENT RELATED		
Delays in opening of FCAA/LCAA	Account opening in some instances takes as much as four months and even beyond defeating the very purpose of FCAA and LCAA. While primary reason for delays are capacity related at different levels within different stakeholders, lack of awareness and ownership of the process on the part of the relevant staff have also been highlighted as a major cause of delay.	**Focal point/One window operation** A central point where representatives from MoF, AGPR and NBP together address the concern of Project Management can be an option to resolve the issue of delays in account opening. This central point can be opened in the SBP. In addition, a checklist can be added to the process wherein the required document for opening of the Account are mentioned without which the controlling Ministry/Department shall not start processing the case and added to the file so that time taken can be documented for each

		stakeholder in process.
Un-timely accounting	Accounting offices are not receiving schedules regarding payment of expenditure as per procedure detailed in Para XIX of the Revised Accounting Procedure 2011 from Project Authorities.	A new statement of account prepared by the CGA to be submitted by Project Authorities on monthly basis. This statement should then be uploaded on CGA or AGPR/AG office websites. In addition, all the relevant information pertaining to project accounting including specimens of filled forms/statements must be available on the website. Project database can be populated online by respective AGs and AGPR. This database will be reconciled with EAD, and the project authorities can view the information online.

		Any corrections to be made will be undertaken by the project management which will be a one-time activity.
Non implementation of some instructions in the Revised Accounting Procedure 2011	At present procedure budgetary control checks can only be exercised by the Project Authorities or by AG offices, provided AGPR/AGs receive the schedules as per Para XIX of Revised Accounting Procedure 2011. As per sample study, NBP and SBP do not apply these checks as is done by AG offices in case of locally funded Assignment Accounts. In addition, checks have been given in Para XIII of the Revised Accounting Procedure 2011 against any fraudulent activity.	**Internal controls and checks** The Revised Accounting Procedure should include specific stipulations for the project management to improve its internal control environment. In this regard, amendments to GFR-13 and a new version of Internal Control Manual prepared by CGA should be circulated for Project Management's consumption. The option of post payment external budgetary check by AGPR/AG offices is also there, however, in order to obviate any misuse of such a check, timelines should be inserted in the procedure of post payment check. This timeline should start from the date the monthly statement is submitted and any observation must be communicated to Project Authorities within a stipulated time

		period. It is proposed that Internal Auditors be appointed in selected projects on pilot basis. The TORs of these auditors may be customized to meet the needs of donor projects as well.
Non reporting by National Bank of Pakistan	National Bank of Pakistan does not supply bank statements on time as required under Para XIII of the Revised Accounting Procedure for Revolving Fund Accounts 2011. Due to non submission of bank statements to AGPR, timely recording of transactions from the FCAA and LCAA is affected.	**Full and complete disclosure** International Public Accounting Standards (IPSAS) prescribe full disclosure of "Third party transactions" in the financial statements. The performa attached with Revised Accounting Procedure 2011 needs to be amended. EAD/SBP/NBP/donors must agree on criteria for recording of third party transactions to capture third party transactions as well as rate of recording Pak rupee amounts in national accounts on the same basis i.e. weighted average buying rate of exchange to have uniformity in the

		recording of transactions.
Withdrawal applications not circulated	Copies of withdrawal applications are not being sent in most of the cases to all the agencies indicated in Para XIV of the Procedure..	**Website for uploading scanned images of withdrawal applications** One window operation unit having a fully functional website should be the forum to resolve this issue. Scanned images of withdrawal applications (in original not photocopies) having a group email address will save time and also keep all the stakeholders informed about the circulation of withdrawal applications.
Transfers/postings and ownership	Frequent turnover of key staff especially Project Directors/Coordinators, Finance Managers/Accounting specialists as key personnel dealing with Assignment Accounts and RFAs is a serious constraint.	Project management is a specialized function within the public sector. The first disbursement shall be linked to the appointment of key staff as is being done in some projects. The ministries and provincial departments shall therefore have robust ToRs for these positions and selection shall be conducted through a competitive process among a panel of officers from the government. In order to ensure sanctity of tenure PD and the key staff shall not be transferred until the donor has agreed to do

		so.
Non availability of project funds	Transfer of Donor money to provincial government account as required vide Para X of the Procedure is delayed leading to consequent delays in account opening at provincial level. Lack of budget allocations is another reason for SBP not transferring the amount. This problem becomes more persistent when the counterpart funding by the government could not be provided due to financial crunch.	**One window unit and timelines for availability of funds to Project Management** With the establishment of one window operation unit is an option which may show improvements in availability of project funds to Federal as well as provincial projects. The timelines should be function specific rather than based on yearly cycle of release of funds. For example, time to process the documents at controlling ministry may be five weeks rather than in-line with budgetary schedule.
PROCEDURE RELATED		
Absence of reporting formats and SOPs	The present Procedure, except for mentioning the title of the columns of the annual financial statements (AFS), does not prescribe a detailed standardized	**Accounting record duly prescribed by CGA** The CGA needs to prescribe a standard set of accounting record. This set of record will conform to Project Accounting Module of

	expenditure recording/classification format of the AFS. The formats, principles and methods of project accounts have to conform to the requirements of both agencies: i.e. the Donors and the AGP/CGA.	Accounting Policies and Procedure Manual of CGA and will also be uploaded on the website of one window operation unit.
Non reporting of Third Party Payments	Reporting of third party transactions (Payments made by Donors directly to suppliers of goods or services to the project) to AGPR for incorporation in monthly civil account is not being done. The profarma attached with Revised Accounting Procedure 2011 is incapable of capturing such critical information.	**Third party transactions** A format for this purpose is proposed regarding Schedule for recording expenditure against third party payments. This format is part of the report and is placed at the end of this matrix.
Recording the cost of debt/ Foreign Exchange Loss and Gain	Para IV of the Revised Accounting Procedure 2011 states "The balance of RFAs for Donor's share of financing shall be maintained in Pak rupees as well as in	**Reduced cost of debt** The Revised Accounting Procedure 2011 be amended so that US Dollar/Foreign Currency amounts available in the respective FCAAs

	US Dollar/Foreign Currency but the funds available for utilization/expenditure to the Project Management would be the Pak Rupee balance. In case of depreciation in the value of Pak rupees against the US Dollar/Foreign Currency, the project authorities and donors are faced with following problem: **a. Once the Pak rupee ceiling is utilized by the Project Authorities, NBP will stop further payments from the RFA although the US Dollar/Foreign Currency balance will be available in the RFA.** **b. Upon loan closure, it is mandatory for**	are taken into account. This would ease the burden of cost of debt for the GoP since the interest accrued on unutilized amount would be reduced. The Revised Accounting Procedure 2011has set out a process for close/short close of project and refunding the amounts as per prescribed timelines.

	all Project Authorities to refund the unutilized US Dollar/Foreign Currency in their respective RFAs. However, since the RFAs do not have sufficient Pak rupee cover corresponding to the US Dollar/Foreign Currency balance, the Project Authorities in consultation with EAD/SBP/MoF are arranging for the "shortfall" in Pak rupees. This results in delays regarding loan account closing and it also means continued interest payment by GoP on the unutilized funds lying in RFAs.	
Transfer to other public accounts	The Procedure provides that cash payments or funds transfers from Assignment Accounts to any DDO-account or any other account for the sake of onwards disbursements shall be strictly prohibited.	**Amendment in Para XV** As has been stated in the findings, that Para XV of the Procedure prohibits further transfers from the Assignment Accounts to DDO-account or any other account. However, this restriction also prohibits

	This instruction has been ignored in case of funds transferred for certain development works being executed by a government agency other than the project e.g.to DCOs for undertaking certain civil works. Second generation RFAs are being operated by some projects in violation of Para III of the Procedure that allows only separate accounts for separate grants or loans. Some Projects have even transferred funds to private bank accounts.	transfer to Second Generation RFAs. Following provision, therefore, may be added to Para XV of the Revised Accounting Procedure 2011: "This restriction is for the transfer of unspent cash from government account to private or individual's accounts even in the name of government officers. This is not applicable in case(s) where the Second Generation RFAs are Assignment Accounts of the Federal/Provincial/District governments or a Personal Ledger Account of a Government department Executing agency."
Asset management, contingent	Asset management (including reporting as per international Accounting Standards) is	**Asset management** Purchase order form, Asset Recording Form (13B) should be available at the central point

liabilities and long term commitments	one of the significant changes brought about by NAM. Development projects are the entities which create assets. Procedure to be adopted for depreciation/recording of assets has not been prescribed.	or one window for all Project Directors. A handbook of such forms filled with examples can help the Project Authorities to submit the information to AGPR/AGs. In addition, such forms can be uploaded on the website in Excel formats and then be submitted in soft formats to the AGPR/AGs.
Integration with PIFRA's SAP/R3/R3 system	Revised Accounting Procedure 2011 has not considered the implications of automated systems handling reporting of transactions by Project Authorities. Thus, accounting offices have been showing lack of confidence in accepting direct automated online processing of schedules sent by Project Authorities to AGPR General Ledger System. Currently AGPR does not permit direct online transfer to its General Ledger (GL) under SAP/R3 system. The data sent by the projects online is 'parked' and entries are posted from there into the GL.	**Integration with SAP/R3/R3 on pilot basis** This research recommends that terminals be provided to selected projects on pilot basis. There are various options for this. However, for piloting the accounting process and linking it with SAP/R3 system, after the data is retrieved through internet in MoF/Finance Department/AGPR/AG, the budget should be uploaded on the project terminals and then it should follow normal procedures adopted for accounting in the AGPR/AG offices.

Refunds to project (Deposits)	Refunds to projects need a procedure for accounting.	**Refunds to project (Deposits)** It is recommended that refunds and receipts on account of project operations shall not be credited to the RFA but deposited through a Challan in Government Account. Under the Government Account a separate account head for Project Refunds and Receipts will be created within the Chart of Account (CoA). Each project will be given a sub classification under the Project Refunds and Receipts for identification of amount deposited. Copy of Challan will be sent to AGPR/AG, respective Controlling Ministry for appropriation of refunds into the project account.
Absence of reconciliation of receipts	The Procedure does not give detail steps for reconciliation of receipts.	**Reconciliation of receipts** The Procedure should spell out the basic steps starting with AGPR/AGs matching with the figures of SBP. Management Reporting System of SBP should ensure project-wise information including Project ID,

		Loan/Grant/ Amount received in USD and Pak. Rupee equivalent. Under paragraph III of the Procedure, the balances of the RFAs will be reported in SBP Finance Department Karachi and a daily report of the consolidated balances of the Federal/Provincial Government Account along with other balances has to go to the Federal/Provincial Government (Finance Division/Finance Department/respective A.Gs). The report should serve as a receipt reconciliation document. SBP and AGPR/AGs can hold a monthly reconciliation meeting for the purpose.

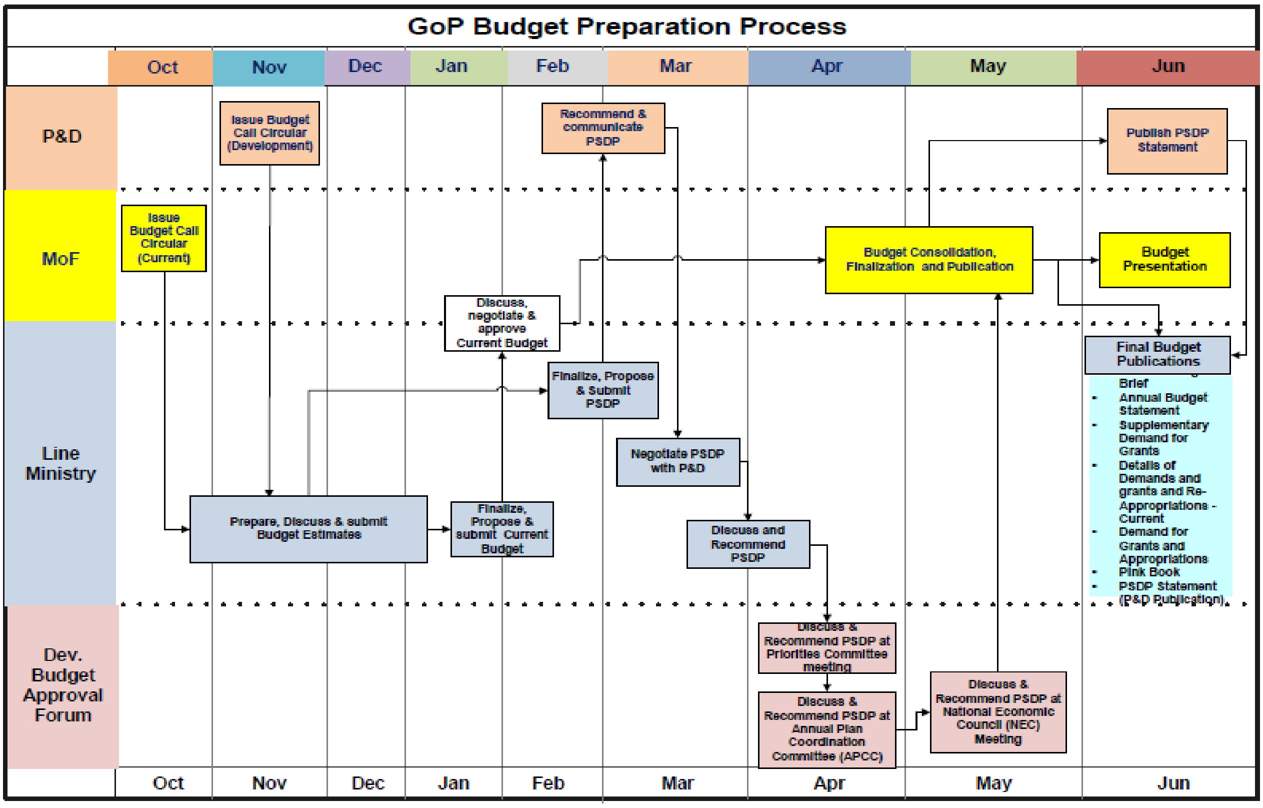
Format for third party transactions

1	**Demand No.**	
2	**Fund Code.**	
3	**Loan No.**	
4	**Name of Financier (ADB/World Bank etc)**	
5	**Sub-Detailed Function**	
6	**Project Name**	
7	**Name of Ministry/Division**	
8	**Name of Executing Agency**	
9	**DDO Code**	
10	**Project Code (If allotted)**	
11	**Vendor Name, Bank Account No.**	
12	**Withdrawal Application No.**	
13	**Withdrawal Application Date**	
14	**Date of Transaction**	
15	**Currency of Loan**	
16	**Currency of Disbursement**	
17	**Amount in US $**	
18	**Amount in Pak Rupees**	
19	**Country of Vendor (payees)**	

20	**Country of Disbursement**	
21	**Reference of SBP (if local vendor)**	
22	**Name and signature of Project Director**	

PAYMENTS	**DEDUCTIONS**					
S.No.	**Loan category/ Component code**	**Object code**	**Amount in Pak Rupees**	**Loan Category/ Component Code**	**Object Code**	**Amount in Pak Rupees**

Annex- D


GoP Budget Preparation Process
Oct
Nov
Dec
Jan
Feb
Mar
Apr
May
Jun
P&D
MoF
Line Ministry
Dev. Budget Approval Forum
Issue Budget Call Circular (Development)
Recommend & communicate PSDP
Publish PSDP Statement
Issue Budget Call Circular (Current)
Budget Consolidation, Finalization and Publication
Budget Presentation
Discuss, negotiate & approve Current Budget
Final Budget Publications
Brief
Annual Budget Statement
Supplementary Demand for Grants
Details of Demands and grants and Re-Appropriations - Current
Demand for Grants and Appropriations
Pink Book
PSDP Statement (P&D Publication)
Finalize, Propose & Submit PSDP
Negotiate PSDP with P&D
Prepare, Discuss & submit Budget Estimates
Finalize, Propose & submit Current Budget
Discuss and Recommend PSDP
Discuss & Recommend PSDP at Priorities Committee meeting
Discuss & Recommend PSDP at Annual Plan Coordination Committee (APCC)
Discuss & Recommend PSDP at National Economic Council (NEC) Meeting